Supermarkets

Fixing Australia's supermarkets: how to drive competition without wielding a hammer

Short of breaking up Coles and Woolworths, retail experts call for regulation of wholesale supply deals and help for new entrants to access sites

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The Albanese government has ruled out breaking up Australia's dominant supermarkets after likening such a measure to the old Soviet Union's command and control economy.

While the government's position will disappoint some of Coles and Woolworths' fiercer critics, meaningful reform doesn't necessarily require a hammer, according to industry and supply chain experts.

Supplier access

Last year in New Zealand, a scandal known as "Weet-Bixgate" erupted. It referred to a decision by Sanitarium to cut supplies of its well-known breakfast cereal to The Warehouse, which competes with the country's two dominant supermarkets, Foodstuffs and Woolworths-owned Countdown.

The decision, which Sanitarium blamed on supply constraints, caught the attention of the country's commerce commission and raised questions over why the food company prioritised supplies to the majors.

The Warehouse had been significantly undercutting its bigger rivals on the price of Weet-Bix leading up to the decision.

"It's a really good example of the challenges of trying to get scale in this market," The Warehouse's chief product officer, Tania Benyon, told Guardian Australia.

"We can generally access products but not necessarily at a competitive price. And that's really the crux of our issue because we need access to fair pricing in order to be able to grow.

"There's a structural unfairness."

The issue, which Benyon said would also affect non-duopoly grocers in Australia, shows strong reforms could be required to ensure wholesale deals are not stifling competition in the grocery sector.

Wholesale supply arrangements would need to be consistent with what would typically be negotiated in a competitive market.

Amid a public uproar, Sanitarium promptly reinstated supplies to The Warehouse “albeit with a price increase”, according to Benyon.

A Sanitarium spokesperson said: “We are not in a position to comment in relation to the New Zealand market.”

Products such as Weet-Bix are seen as staple foods for many Australian households, making them prized items for supermarkets given their availability can influence where a person shops.

While many stores sell smaller Weet-Bix packages, the big two supermarket chains dominate the supply and sale of the larger 1.2kg value packs, which they sell at identical prices.

The Sanitarium spokesperson said the company was committed to making Weet-Bix, and larger value packs, available across a broad spectrum of Australian retailers.

Property squeeze

Large German retailer Kaufland invested several hundred million dollars in Australia before abruptly cancelling its plans in early 2020 due to difficulties setting up.

The decision robbed Australia of a new and formidable entrant that could have put pressure on Coles and Woolworths.

Kaufland built up a property portfolio of sites in Adelaide, Melbourne and south-east Queensland as it planned for its opening, although Australia’s most populous city, Sydney, was notably absent.

Jeremy Prestoe, head of NSW asset management services at real estate agency Knight Frank, said it was very difficult for a new entrant to compete with incumbents when it comes to land access.

“You’ve got to first find distribution sites, which is a challenge, followed very quickly by having well-placed supermarket space. Being able to find thousands of square metres for parking is virtually impossible in metropolitan Sydney, Melbourne and Brisbane,” said Prestoe.

“The only way that they could contemplate an opportunity in Australia would be an acquisition or a merger or a significant joint venture with a major investor who is prepared to wait 10 years to make any money.”

It has taken Aldi more than two decades to build a 10% market share after opening its first Australian store in 2001, although the property market has tightened considerably during that period.

The task of generating more competition is made all the more difficult by the large market share of the majors.

Metcash, which operates IGA, said in its parliamentary submission that in the 1980s the combined market share of the two biggest supermarkets was less than 40%, compared with their current share of about 70%.

Prestoe said there might need to be a coordinated effort from government agencies to help non-duopoly supermarkets access sites, otherwise Coles and Woolworths can use their dominance to shut others out.

“The majors could take a ‘loss leader’ to keep the others out, which is what happens when you have a duopoly. They can take a site and settle for making money there in 15 years’ time because they don’t want the other guy there.”

Proactive approach

The major supermarkets are subject to a Senate inquiry, which will hold its first public hearing on Thursday, and a 12-month probe by the competition regulator.

There is also a review of a voluntary code of conduct, designed to govern how the food retailers deal with suppliers, amid concerns they are too scared of retribution to complain.

A Woolworths spokesperson said the market, found by the competition regulator to be “workably competitive” in 2008, is now much more so.

“Being price competitive is critical in trying to win our customers’ shopping basket and the vast majority of consumers will shop across different retailers, so being competitive is key to attracting customers to shop with us,” the spokesperson said.

Coles has consistently defended its business and pricing practices and has described competition as “fierce”.

“We are focused on keeping the price of food and groceries low for our customers, while paying our hardworking farmers and producers fairly,” a spokesperson said.

Farming groups have accused the big supermarkets of using their power to distort the market, leading to elevated prices for shoppers and low prices for producers.

An ACTU-led inquiry recommended that a competition and prices commission be created to investigate potential cases of price-gouging, with the results publicised.

Sanjoy Paul, an associate professor in the UTS Business School who works on supply chain risk and resilience, said there needed to be proactive, rather than reactive, investigations.

“There is a scope for proactive investigations, because complaints are not reported regularly,” said Paul.

“We need to talk to suppliers to get the real stories of competition behaviour in Australia.”