

J SAINSBURY'S PLC AND ASDA GROUP LIMITED – RESPONSE TO CMA'S ISSUES STATEMENT

1. Introduction

- 1.1. [CONFIDENTIAL] to respond to the CMA's Issues Statement (dated 16 October 2016) in relation to the proposed combination of J Sainsbury PLC ("JS") and ASDA Group Limited ("ASDA", and together with JS, the "Parties") (the "Proposed Merger").
- 1.2. [CONFIDENTIAL]¹ [CONFIDENTIAL] (a) the Proposed Merger will create the largest grocery retailer in the UK, ahead of Tesco and (b) together the Parties and Tesco will benefit from a duopoly with estimated segment shares of 80% of the major multiple segment, 60% of the total grocery segment and 70% of the on-line grocery segment.² This will have significant negative implications and raise material competition issues at all levels of the supply and distribution chain, which ultimately will be will be **extremely detrimental for consumer welfare**.
- 1.3. The damaging effects of the Proposed Merger will be long-lasting and unlikely to be counter-balanced by any market developments (such as expansion of existing actors or new entry) or regulatory frameworks (such as GSCOP or existing competition law legislation). Unlike previous retail mergers, the Proposed Merger will cause a fundamental change to the structure of the grocery sector, to the detriment of consumers.
- 1.4. [CONFIDENTIAL]

2. Competitive constraint on one-stop shops

- 2.1. [CONFIDENTIAL] CMA's observation that the competitive constraint faced by grocery stores is asymmetric, i.e., one-stop stores are directly constrained only by other one-stop stores ("**Major Multiples**"). It is important not to overstate the importance of discounters (e.g., Aldi and Lidl) and online only players (e.g., Amazon).

Discounters:

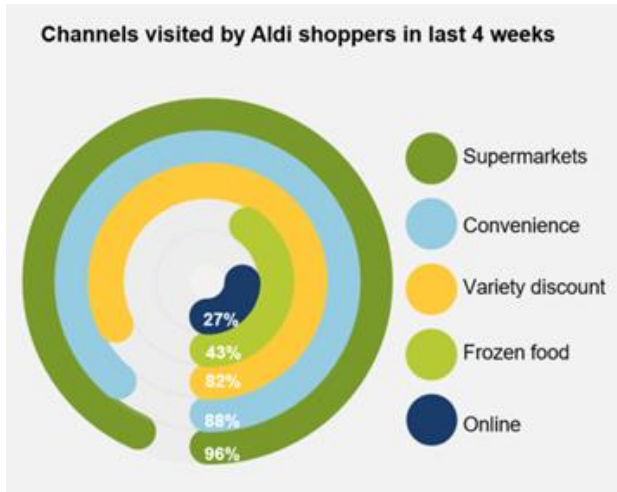
- 2.2. Discounters are **not** directly comparable to Major Multiples (Tesco, JS, ASDA, Morrisons and Waitrose) from a consumer-perspective owing to a critical factor – **lack of assortment and product choice**.
- 2.3. A discounter (e.g., Aldi, Lidl) typically stocks a maximum of 3000 SKUs compared to 33,000 SKUs at a Major Multiple³. As a result, discounters are mostly used as a complement to the Major Multiples, and the vast majority of consumers who shop at discounters also shop at Major Multiples. (The statement is also true for consumers who shop at convenience shops.) Concretely put, **96% of Aldi shoppers also visit a Major Multiple supermarket**, and the figures are similar for Lidl⁴.

¹ [CONFIDENTIAL].

² [CONFIDENTIAL] (re-attached as **Annex 1**).

³ The Grocer 2018, IGD.com 2018

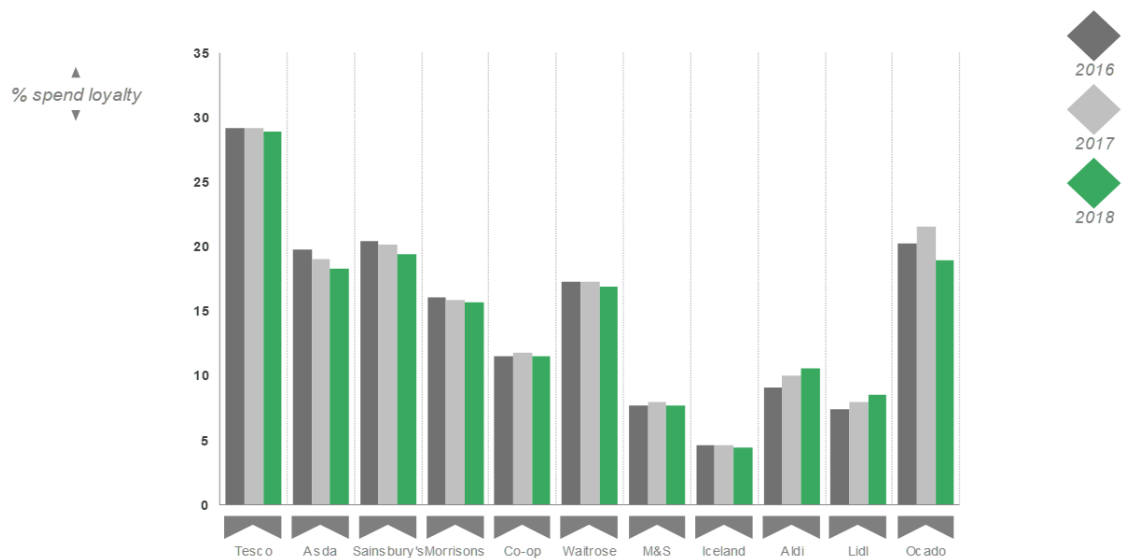
⁴ *Id.*



2.4. A significant proportion of total grocery spend is dedicated to the Major Multiples. The chart below shows a relatively low share of wallet for Aldi and Lidl indicating that these stores only account for a small proportion of total shopper spend.

Retailer FMCG loyalty

Share of grocery wallet (spend in retailer as a proportion of market spend)



RST (Grocery). KWP 2018 03. 52 w/e 25 Mar 18. 1 year panel

- 2.5. Total product assortment and choice drives the majority of consumer spend. Accordingly, it is largely **irrelevant** whether, (a) there are discounters in the same geographic area as a Major Multiple, and (b) discounters plan to expand their geographic presence or even assortment. Discounters will unlikely ever offer the same assortment and choice as a Major Multiple. There is no reason to believe that discounters will alter significantly their business model, which is hinged on a limited product range. Consumers will generally continue to use discounters as a complement.
- 2.6. Given that consumers do **not** generally use discounters for their one-stop shop, **discounters will not exert any direct meaningful competitive constraint on the Parties**. Only other Major Multiples will, to the extent possible given the degree of market concentration (see Section 3 below), be able to constrain the Parties.

Online players:

- 2.7. Online grocery shopping accounts for less than 5% of the total grocery sales. Segment shares of the Major Multiples in physical stores are more or less replicated in the online grocery segment (with the exception of Ocado)⁵. As the CMA notes, JS and ASDA are the “*second and third largest suppliers of online delivered groceries in the UK (after Tesco)*. Other grocery suppliers who offer a delivered groceries service tend to have a more **limited geographic coverage** or a **smaller range of products** offered for delivery” (emphasis added).
- 2.8. The Parties claim that the competitive landscape has changed significantly in recent years with the growth of online shopping including Amazon. However, the online grocery segment only accounts for an estimated 5% of total UK grocery. Amazon only accounts for less than 1% of all online grocery shopping, and an even smaller proportion of total grocery. In line with the CMA’s observation, Tesco, ASDA and JS each deliver to over 90% of UK postcodes, whereas other Major Multiples and Ocado have significantly limited coverage. Amazon’s coverage is even more limited as it does not supply fresh groceries outside of a very narrow geographic area. In this context, it is interesting that JS CFO stated that JS, “*compete [...] heavily with Amazon, particularly in general merchandise, and not so much in food in the UK*”⁶ (emphasis added).
- 2.9. If the CMA were to consider only online grocery retailers that deliver to consumers in the majority of geographic areas, this is likely be limited to the Parties and Tesco. Put differently, JS and ASDA are much closer competitors to one another (both online and offline) than discounters or Amazon are to JS and ASDA.
- 2.10. In summary, the competitive alternatives to the Parties available to customers in any given geographic area is **limited to other Major Multiples**. Discounters, convenience shops and on-line offers do not directly constrain the Parties in any meaningful fashion. Any future growth in the online grocery segment throughout the UK will predominantly benefit the Parties and Tesco.

3. Degree of concentration in the Market:

Significant presence of Major Multiples

- 3.1. The CMA **[CONFIDENTIAL]** the relevance of the degree of concentration in the market and whether a small number of retailers account for a significant proportion of the market. The degree of concentration resulting from the Proposed Merger has material implications for the total supply chain.
- 3.2. As stated above, discounters have a relatively small presence in the market. **[CONFIDENTIAL]**, on a wide frame of reference of total grocery, a combined ASDA/JS will have a share of supply of **over 30%** and will, together with Tesco, account for **almost 60%** (with the next largest player being Morrisons with only c. 10%). On a narrow reference of Major Multiples, the Proposed Merger will have a share of supply of c. 42% and will, together with Tesco, account for almost 80% (with the next largest player being Morrisons with only c. 14%).⁷
- 3.3. This degree of concentration may be compounded by barriers to entry for larger grocery store formats, such as cost, availability of real estate, planning permission and other investments and strategic choices.
- 3.4. The existing level of concentration has led to a degree of interdependence between the Major Multiples, whereby actions taken by one is likely to have a direct impact on the others. For example, **[CONFIDENTIAL]**’s review of its price guarantee campaign is likely to have had a direct impact on the strategy of the other Major Multiples. Under such circumstances, as observed by the CMA, the high degree of concentration resulting from the Proposed Merger may make it easier for the Major Multiples to align their behaviour, without the need to reach any express agreement.

⁵ **[CONFIDENTIAL]**.

⁶ <https://www.bloomberg.com/news/videos/2018-04-30/sainsbury-cfo-says-asda-deal-very-focused-on-competing-with-amazon-video>

⁷ **[CONFIDENTIAL]**.

- 3.5. Further, regardless of how the market is viewed, at the very least the Proposed Merger has the potential to create a duopoly between Tesco and the Parties. ***This could facilitate collusion between Tesco and the Parties, ultimately harming consumers.***
- 3.6. Finally, given that online players and discounters are not a direct competitive threat to the Major Multiples, in the absence of any meaningful competition, a dramatic increase in concentration in the UK grocery market, taken to its logical conclusion, is very likely to have the consequence of increased prices for a lowered range, causing significant damage to consumers.

4. Reduced product choice for consumers

- 4.1. The Proposed Merger is likely to lead to consolidation of ranges in the Parties' stores and also rationalisation in the number of stores. This is essential to achieve the synergies of GBP 500 million claimed by the Parties. In addition to a rationalisation of existing ranges, joint procurement arrangements will also remove important channels for all suppliers to bring new products to market.
- 4.2. **[CONFIDENTIAL]**, this will lead to a ***material reduction in choice for consumers***, and given the range shortage in discounters, and the geographic limitations of online-only players, there is ***no alternate avenue for increased product choice for consumers***.
- 4.3. **[CONFIDENTIAL]** the Proposed Merger's impact on national and local grocery strategies (e.g., stocking decisions and local or regional sourcing).

5. Significant buyer power

- 5.1. **[CONFIDENTIAL]**, the Parties have significant buyer power, which will increase significantly because of the Proposed Merger.
- 5.2. Each of the Parties is a top 3 customer for most suppliers. Post-Merger the Parties are likely to be the single largest customer.
- 5.3. In contrast, individual suppliers **[CONFIDENTIAL]** account for an insignificant proportion of the Parties' total purchases.
- 5.4. **[CONFIDENTIAL]**⁸.

Impact on negotiations with suppliers

- 5.5. As the CMA notes, important commercial aspects such as negotiations with suppliers on individual investments and promotions are set centrally and are not differentiated by local areas. **[CONFIDENTIAL]** the Merger will further increase the balance of power in commercial negotiations in favour of the merged entity and ***will*** give rise to an incentive to worsen these "***national, uniformly-set parameters of competition***".
- 5.6. In particular:
- a. **[CONFIDENTIAL]**. A further swing in bargaining power in favour of the Parties will lead to the Parties:
- pushing for unrealistic price cuts and disproportionate investment from suppliers without any tangible **[CONFIDENTIAL]** (to increase retailer margins and drastically reduce supplier margins);
 - refusing to list new products, de-listing or threatening to delist individual product lines or a significant volume of a supplier's products;
 - positioning private label products to the detriment of branded products;

⁸ **[CONFIDENTIAL]**.

- eroding product brand value as a result of continuous price erosion and de-listings; and
 - engaging in other detrimental activities which [CONFIDENTIAL] may not be able to predict at this stage.
- b. [CONFIDENTIAL]⁹, [CONFIDENTIAL].
- c. [CONFIDENTIAL].
- d. [CONFIDENTIAL].

5.7. [CONFIDENTIAL].

Impact on incentive to innovate

5.8. [CONFIDENTIAL].

5.9. [CONFIDENTIAL]¹⁰.

5.10. Further, the Proposed Merger will lead to a reduction in stores and range consolidation, which ***reduces the avenues to bring new and/or improved products to market***. Discounters and online-only players are no substitute for Major Multiples due to range (and for online – geographic) limitations, increasingly squeezing the potential to provide consumers with the best choice at the best price.

6. Other impacts

6.1. The CMA raises the concern that the increased buyer power of the merged entity might raise the purchasing costs of rival retailers, which, under certain circumstances, may result in price increases to certain customers. [CONFIDENTIAL].

6.2. [CONFIDENTIAL].

7. Conclusion

7.1. A competitive market guarantees consumers the best product choice at the best price. The ***Proposed Merger only serves to deteriorate conditions in an already concentrated market, to the significant detriment of consumers and suppliers***.

7.2. Any proposal for divestiture considered by the CMA is not going to resolve the issue of lack of direct alternatives to the Parties.

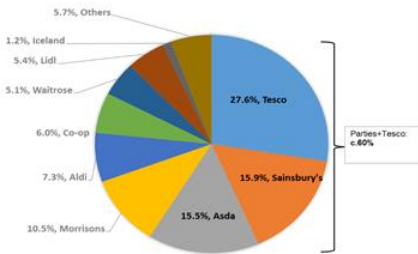
7.3. In any event, given its presence, Tesco is unlikely to purchase any divested stores. Morrisons/Waitrose may at best consider acquiring an extremely limited number of stores. The remaining players in the market are not active in this store format and will not purchase any stores marked for divestment. There is a high likelihood that each store marked for divestment may not actually sell groceries and hence will not be able to contribute towards restoring market competitiveness.

⁹ [CONFIDENTIAL].

¹⁰ [CONFIDENTIAL].

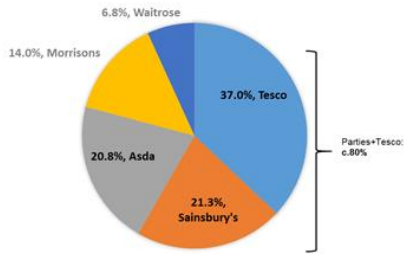
Asda / Sainsbury's

Total Grocery



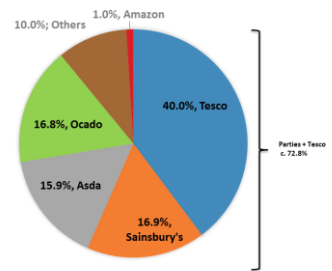
Source: confidential

Major Multiples



Source: confidential

On-Line Grocery (only 5% of Total Grocery)



Source: confidential