Beer maker takes on supermarket bullies

Catherine Sutton-Brady

The University of Sydney Business School,

Sydney, NSW 2006, Australia.

Catherine.suttonbrady@sydney.edu.au

And

Patty Kamvounias

The University of Sydney Business School,

Sydney, NSW 2006, Australia.

Patty.kamvounias@sydney.edu.au

Work-in-Progress Paper

Presented at 28th IMP Conference, Rome, Italy

September 2012

Beer maker takes on supermarket bullies

Purpose: This paper investigates recent price wars in the Australian retail industry and its impact on networks and relationships in that industry. Two major Australian supermarkets account for 80% of grocery sales in the Australian market and as such are considered powerful players in the market. This paper looks in detail at two recent price wars and the reaction of the relevant suppliers. It attempts using the theory of networks and relationships to explain the differing reactions.

Research Method: Data is gathered over a 12 month period from leading Australian newspapers, allowing the story of the price wars to be followed in detail.

Research Findings: The paper focuses on two price wars that the two major supermarkets fought against each other, one was a milk price war the other a beer price war. The paper shows the completely different reactions of the suppliers to the bullying tactics of the supermarket chains. It also looks at the impact on the network of the differing reactions, showing very different network effects in both sectors. The paper also looks at the relevant competition law, which allowed the beer maker to exercise some power in an otherwise powerless situation.

Main Contribution: This paper shows that despite the fact that the supermarket chains have unparalleled purchasing and selling power, and a seemingly unassailable position in the network they can be outmaneuvered by a player willing to take a legal stance. It also shows the negative impact throughout the network of taking on the big players.

Keywords: Buyer-supplier relationships, price wars, retail industry, power, competition law.

Work-in-Progress Paper

Beer maker takes on supermarket bullies

INTRODUCTION

Numerous studies have highlighted the power exerted by major supermarket chains in the retail industry (Gedeon, I-M., Fearne, A. & Poole, N. 2008; Harrison, D., Prenkert, F., Olsen P.I. & Hoholm, T. 2011; Hingley, M. & Hollingsworth, A. 2003), to date the majority of these studies have concentrated on players in the European and US markets, this paper investigated this phenomena within an Australian context. It focuses specifically on two recent price wars waged by the major players in the Australian grocery industry and charts the reactions of the suppliers to these price wars. The paper begins with a snapshot of the Australian context and introduces the main players. The method used to undertake this study is then introduced. This is followed by introducing the two cases and comparing and contrasting the reactions. It concludes with a link to the literature highlighting the intended contribution of this work in progress paper.

THE AUSTRALIAN CONTEXT

Grocery Retail Sector

The Australian retail sector is dominated by two major players, Woolworths and Coles (owned by Wesfarmers). In 2011 Woolworths was the leading player with 33% market share, while Coles held 29% (Euromonitor 2012). In 2011 particulary there was a dramatic shift in power in this chain, with these major players controlling what goes out to consumers and the increased use of private label brands. 2011 was also the year that saw the start of aggressive price wars between the two, which drove down prices across the board. The expectation is that the use of aggressive pricing tactics will continue well into the future as the players strengthen their grip on the market (Euromonitor 2012).

While Australia does have a concentrated grocery retail sector, concentration levels are not as high as some European countries. The interesting factor though is that the concentration is horizontal as well as vertical. The sector has also followed the lead of many European and US retailers by expanding their retail offering into areas such as liquor and fuel, a pertinent fact for this study. Unlike other countries liquor cannot be sold in supermarkets but is sold through “bottle shops”. In recent years the two major players have almost completely cornered this market and are now responsible for 80% of all alcohol retail sales. While there are many outlets operating under different names most are owned by Woolworths and Coles. Woolworths has its Woolworths Liquor Store (next to its supermarkets) but also own Dan Murphys, Cellarmasters and BWS, while Coles in direct competition have Liquorland (next-door to their supermarkets), 1st Choice and Vintage Cellars.

Milk sales

Supermarkets account for 52% of milk sales. This continues to grow as a direct result of the price war of 2011, which has seen more consumers moving away from convenience stores. Private label brands account for 51% of supermarket sales, a percentage that continues to grow yearly (ABS 2012). The dairy manufacturing industry is diverse and includes farmer-owned co-operatives, publican ad private companies, and major multi-national players. Milk production is no longer dominated by co-operatives, which now only account for 35% of market share. There are two major players in the market Lion Dairy and Drinks (with the Dairy Farmers and Pura brands) and Parmalat with the Paul's brand) (www.dairyaustralia.com.au) .

Beer sales

In 2011 in the Australian beer market two major players held 89% market share in volume terms (Euromonitor 2012). The two main players are Carlton United Brewers with 48% market share and Lion Nathan with 41% market share. Carlton United Brewers (CUB) was formerly Foster's Australia but rebranded in July 2011 to capitalise on its history and community association. In September 2011 it was bought by SABMiller for A$12.3 billion (Euromonitor 2012). Both companies have been struggling with declining beer sales and tough competition from imported lager, private label and craft beers. In volume terms 20% of sales is on-trade and 80% of sales is off-trade Euromonitor 2012. This split means that the retailers Coles and Woolworths are vitally important to the beer manufacturers given their stranglehold on the liquor market with regards to outlets and the fact that they have 50% market share.

DOCUMENTARY ANALYSIS

While these price wars were fought publicly and the reactions of the parties involved were well documented, the commercial sensitivity meant it was impossible to find anyone in any of the companies willing to discuss it openly. Therefore as a researcher attempting to understand exactly what is going on and interpretive the motives of both suppliers and buyers in these relationships the only choice of method is documentary research. While this may be seen by many to be a limitation of this study, documentary analysis can provide a researcher with rich insights into an area where no other course of analysis is possible because of the contemporary nature of the research area. Indeed Davis and Schneider (2010) advocate the use of documentary evidence where data that explores the intent, purpose and creation of meaning is unavailable through any other source, as is the case with this study.

A document is defined as a written text (Scott 1990); therefore documentary analysis deals with analysing written texts. In literature on research methods the use of documents does get limited coverage (Hargreaves, 2008) however many authors do agree to their value as sources of information (Scott 1990). It should be noted that while documentary analysis may not be common in marketing literature it has been used extensively in archaeology and history (Hodder, 2000).

It is acknowledged that documents will not necessarily tell you the whole story, however Scott (1990) maintains that the story they do tell will be interesting in its' own right. One of the overriding issues with regard to documentary analysis is the quality of the data. Scott (1990) outlines a simple set of criteria to allow researchers assess the quality of the data they are analysing. The four criteria are

1. *Authenticity – Is the evidence genuine and of unquestionable origin?*
2. *Credibility – Is the evidence free from error and distortion?*
3. *Representativeness – Is the evidence typical of its kind and, if not, is the extent of its untypicality known?*
4. *Meaning – Is the evidence clear and comprehensible?*

(Scott, 1990 p.6)

For the purposes of this study the documents analysed were newspaper reports from March 2011 to March 2012, of Australian published newspapers. Additionally company information was gathered through an analysis of the companies' annual reports and industry reports on the Australian retail sector. It is well documented that assessing the quality of mass produced newspapers can be an issue. Authenticity can be an issue since newspapers often misprint data and this data may be vital to the study in question. However for the purposes of this study a close examination of the sources used show no obvious misprints or errors, the researcher in this case is confident of the authenticity of the data. Likewise in the case of credibility it is felt that the sources analysed are credible and appear to make no attempt to distort the facts reported. The representativeness issue is one particularly pertinent in historical documentary analysis and not as big a problem in contemporary research. Therefore representativeness is not seen as a problem for this particular study since a wide range of newspapers were easily accessed and the range utilised ensures a representative sample. As Scott (1990) points out the ultimate purpose of documentary analysis is ‘to arrive at an understanding of the meaning and significance of what the document contains.’ In the case of contemporary documents written in English meaning is easily comprehended. However analysis of the text is open to many interpretations and while these interpretations may often revolve around deciding how to evaluate the text, working out if it fits with a more general understanding etc. Hodder (2000) maintains that the analyst does have ‘patterned evidence’ which can be evaluated.

Peräkylä (2005) believes that many researchers who use written texts do not follow any predefined protocol in their analysis rather ‘by reading and rereading their empirical materials they try to pin down their key themes and, thereby, to draw a picture of the presuppositions and meanings that constitute the cultural world of which the textual material is a specimen’. In line with this the following section will discuss the analysis of the newspaper reports in line with literature as outlined above to identify emerging themes and gain an understanding of the changing network dynamics as a result of these price wars.

THE MILK PRICE WAR

The Milk Price war which started in January 2011 lead to both Coles and Woolworths selling their private label milk at A$1 a litre. In comparison branded milk currently sells at A$2.24 per 1 litre, A$3.69 per 2 litres and 5.16 per 3 litres. Much has been written over the last year about this price war and its effect on the dairy industry and most importantly the farmers. The argument made by the supermarkets is that they are consumer champions providing milk at a much lower price. On the other hand it is the suppliers who are feeling the pain of having to supply this private label branded milk. One supplier stated that they were “struggling to breakeven on private label contracts and that the overall brand and private label margins on white milk was expected to be 2%" and that was before the price war (SMH 27/3/11). The situation in Australia is often compared in the discussions with that of the UK where in 2010 the big four grocery chains reduced their own brand milk prices. Interesting while it did not increase their milk sales it did increase their combined overall market share by 4% in just 3 months, clearly what the Australian duopoly are aiming to emulate.

However while it appears to be good for consumers and for supermarkets the suppliers are not happy and probably rightly so since the experience in the UK shows that the price war there had "catastrophic impact" with declining herds and increasing milk imports.(SMH)

The duopoly, that exists as outlined earlier, means these suppliers have very little power to influence this situation, their position in this network is very weak and this has been borne out by their inability to react in any way to this price war. Interesting another player has entered the fray and the government undertook a senate inquiry into the pricing practices of the big supermarkets. They were worried about the long term implications on the economy and more importantly the dairy industry. There was also a worry that this practice will cripple suppliers and kill off smaller suppliers. However in a further erosion of the power of the suppliers (mainly farmers) the inquiry found that the price war was a win for consumers and had not "badly" affected Australia's dairy industry and that the Australian Competition and Consumer Commission (ACC) would act if anti-competitive behaviour occurred (AFR, 6/02/12).

THE BEER PRICE WAR

Shortly after the milk price war started, beer became the new milk in the price war stakes but the reaction of the suppliers was in total contrast to that of the milk suppliers. It should be noted that this price war started before Fosters changed its name to CUB and before it was acquired by SABMiller (as discussed above), so for the purposes of this paper I will refer to the company as Fosters. In March 2011 it became evident that Coles were losing out to Woolworths in the lucrative liquor segment, so Coles decided to engage in an aggressive price war on beer. They choose to discount heavily Fosters beer, so for example a carton (24 x 375ml cans or bottles) of VB (Victoria Bitter) which normally retails for between A$34-A$52, they planned to sell for A$28 well below cost.

Fosters received intelligence of this planned discounting and took the unprecedented action of stopping its delivery of VB, Carlton Draught and Pure Blond to the discount liquor stores of Coles and Woolworths, 1st Choice Liquor and Dan Murphy's respectively (SMH 23/3/11). It was the first time in Australia that a suppler had taken on the Big Two. Coles denied that it had planned on selling that low and when they agreed that they won't supply was resumed. A Foster's spokesman said "*supply was withheld to protect brands against loss-leading…….We take loss-leading of our brands very seriously*" (SMH 23/3/11).

DIFFERENT REACTIONS

It is obvious that the intent in both price wars for Coles and Woolworths was to increase through traffic and treat these products as loss-leaders. The power they have in this industry and their network position lead them to believe they can easily take on the suppliers and get the products heavily discounted. In a sense the differing reactions can be explained by two factors, relative power and law.

The suppliers in the milk wars were disadvantaged by a number of factors. They are smaller in size and therefore are perceived as having less power. The milk war involved brands that are not as well known, as consumers will often just pick up whatever milk is available. A significant issue is also the growth in private label brands as mentioned 51% of supermarket milk sales are private label. Finally they didn't have law on their side as the supermarkets were still selling just above cost.

Fosters was in a stronger position relatively, to take on the supermarkets. It is the leading beer producer in Australia and its brands are instantly recognized. While private label beer and wine have been introduced by the retailers, consumers are slow to purchase and sales are moderate. It seems the consumer is happy to buy private label milk but when it comes to beer they stick to known brands.

The most significant factor allowing Fosters to take on the retailers was the Trade Practices Act. One would have rightly assumed that withholding supply could be a breach of their existing contract and would fall under the restraint of trade, but Fosters relied on the section related to Resale Price Maintenance. While suppliers are prohibited from engaging in resale price maintenance, Section 48 – "*A corporation or person shall not engage in the practice of resale price maintenance*" which can include

The supplier-

(a) *Making it known to a second person that the supplier will not supply goods to the second person unless the second person agrees not to sell those goods at a price less than a price specified by the supplier.*

(d) withholding the supply of goods to a second person for the reason that the second person: (i) has not agreed as in paragraph (a); or (ii) has sold or is likely to sell, goods supplied to him or her by the supplier….at a price less than a price specified by the supplier … (Section 96 (3))

So Fosters were withholding supply in breach of this section but suppliers are not deemed to be withholding the supply of goods if certain conditions are met under Section 98 (2).

Paragraph 96(3) does not apply in relation to the withholding of the supply of goods to another person who, within the preceding year, has sold goods obtained, directly or indirectly, from the supplier at less than their cost to that other person:

(a) For the purpose of attracting to the establishment at which the goods were sold persons likely to purchase other goods; or
(b) Otherwise for the purpose of promoting the business of that other person.

This section of the Trade Practices Act increased Foster's power in this case. Unfortunately for the milk suppliers these conditions would have been a lot harder to prove.

CONCLUSION

These two cases have given us an interesting insight into the interaction which takes place in this highly competitive industry. It is clear that the network dynamics are changing overtime as the duopoly of Coles and Woolworths becomes more powerful. It is clear that many in the industry are wary of the power they can assert and this is borne out by the reactions of the milk suppliers.

As a direct consequence of these price wars the government is paying closer attention to the industry and is mindful of the power of the big two in this network. It is likely that overtime we will see further changes in the interactions in these complex relationships. Indeed much of the commentary has revolved around this very issue.

“The decision by Foster’s to withhold its beer supply from the two supermarket giants after learning Coles intended to heavily discount it to grab market share demonstrates the law of the jungle that increasingly prevails in Australian industry: the strongest pick off the weak until they encounter an opponent of enough brawn to fight back…It was a different story when the grocery giants decided to take on the milk industry- composed mainly of small farmers-…Foster’s can fight back only because it too, has limited competitors and a degree of market power in distributing its products (The Age, 23/03/11).

The rise in sale of private brands has also meant that the nature of interactions in this network has changed with the duopoly having the ability to exert even more power over its suppliers. This market power has allowed them to sustain a price war by squeezing their suppliers although be it quite legally.

“The strategy of the two big supermarkets to use one product as a ‘loss leader’, offering a heavy discount on that product to lure customers, is not in itself illegal… it does however suggest that the retailer has a degree of market power over pricing that would not be possible in a perfectly competitive world. In a competitive world no one player would be profitable enough to lead such an aggressive strategy and survive for long. But the supermarket duopoly has captured such a large share of the customer market that it has a greater capacity to sustain such a price war” (The Age, 23/03/11).

An unintended consequence of the publicity that these price wars have garnered is that other practices in the industry are having light shed on them. These practices include “ hardball tactics as ‘cliffing’ where suppliers are forced to bid for their existing shelf space and risk losing the lot to a higher bidder” (SMH 21/4/12) In a recent example Greenseas tuna allegedly lost out to John West and the private label brand in Coles. Tactics like this and forcing suppliers to fund discount offers is changing the network and means players who once had a strong position find themselves relegated or even out of the network totally with the dissolution of their relationships.

Finally the changing face of this network is even more evident in the beer sector, where small independent liquor outlets that once had strong ties with Fosters and Lion Nathan are buying less from them and instead pulling their trucks up at Woolworths and Coles discount outlets where they can buy the product cheaper.

It is obvious from recent discussions that this dynamic network continues to change as suppliers feel the squeeze as an almost direct result of the price wars. Will we be left with a network where only the big can survive that is very much a concern in the Australian market at present? Just last month Unibic (who makes the iconic Anzac biscuit) collapsed after soaring commodity prices and deep discounting by the supermarkets meant they could no longer survive (SMH 21/4/12). In the same article it was noted that nobody else will speak out because it would be a virtual death knell given the extraordinary level of market concentration.

In response to this and many other allegations the ACC have called on suppliers to "dob in your supermarket", they state that they have a "priority to uncover possible abuses of market power" (SMH 21/2/12) The degree of power is highlighted by the fact that they are guaranteeing protection and confidentiality. This will be interesting to follow and see if we see any change in the way the supermarkets interact as a result of this scrutiny from the ACC.

This work-in-progress paper has shown that despite the fact that the supermarket chains have unparalleled purchasing and selling power, and a seemingly unassailable position in the network they can be outmaneuvered by a less powerful player willing to take a legal stance. This is a potential contribution to the literature on the power potential of the less-powerful within networks (Fairhead and Griffin, 2000). It also shows the negative impact throughout the network of taking on the big players. It has also shown the ever-changing face of this highly competitive network. The challenge we now have with this work-in-progress paper is to work out how it can be aligned more clearly with existing literature. This alignment will allow us to ascertain the contribution this study can make.

References

Clarke, I. (2000) “ Retail power, competition and local consumer choice in the UK grocery sector” European Journal of Marketing, 34. 8 975-1002.

Davis, T. & Schneider, T. (2010) “Between Antinomies and Gastro-anomy: Mapping Australian Health Food Culture across the post-war decades”, *Consumption, Markets and Culture,* 1(2).

Fairhead, J. & Griffin, R. (2000) “A Political sensemaking process (PSP) model of rapid network development and dissolution. Discourse as deus ex-machina” Proceedings of the 16th IMP Annual Conference, Bath, England September 2000.

Fearne, A,, Donaldson, A., & Norminton, P. (1999) “Pricing Strategy & Practice – The impact of alternative promotion strategies on the spirits category: evidence from the UK” The Journal of Product and Brand Management, 8. 5. 430-442

Gedeon, I-M., Fearne, A. & Poole, N. (2008) “ Buisness Relationship Disolution: Empirical Insights from the UK Supermarket Supply Chains” Proceedings of the 24th IMP Annual Conference, Uppsala, Sweden September 2008.

Hargreaves, J. (2008) “The under-used resource of historical research”, *Nurse Researcher,* 15(3): 32-44.

Harrison, D., Prenkert, F., Olsen P.I. & Hoholm, T. (2011) “Power Games in Networks: Allocation Mechanisms in a Neo-Mercantilist Nteworked Economy” Proceedings of the 27th IMP Annual Conference, Glasgow, Scotland September 2011.

Hingley, M. & Hollingsworth, A. (2003) “Competitiveness and power relationships: Where now for the UK food supply chain?” Proceedings of the 19th IMP Annual Conference, Lugano, Switzerland 4th-6th Sepetember

Hodder, I. (2000) "The Interpretation of Documents and Material Culture," in: *Handbook of Qualitative Research*, ed. Norman K. Denzin and Yvonna S. Lincoln, Thousand Oaks, Ca: Sage, 13-21.

Klein, B. & Murphy, K. (2008) “Exclusive dealing intensifies competition for distribution” Antitrust Law Journal, 75. 2.

Ostendorf, J. Mouzas, S. & Chakrabarti, R. (2011)" Captive in Business Networks" Proceedings of the 27th IMP Annual Conference, Proceedings of the 27th IMP Annual Conference, Glasgow, Scotland September 2011.

Peräkylä, A (2005) "Analysing Talk and Text," in: *Handbook of Qualitative Research*, ed. Norman K. Denzin and Yvonna S. Lincoln, Thousand Oaks, Ca: Sage, 869-886.

Scott, J. (1990) A Matter of Record, Polity Press, Cambridge.

Skinner, S. J., Gassenheimer, J.B. & Kelley, S.W. (1992) "Cooperation in Supplier-Dealer Relations" 68.2. 174-193