LIQUOR RETAILING AND THE WOOLWORTHS/COLES JUGGERNAUT

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Woolworths and Coles Myer are the corporate monoliths of the domes Australian market. They outrank even the four major banks in marl reach. Both the retailers and the banks rate highly in the attention of financial press because they are profit engines *par excellence.* T finance media worries about these companies more when the profit sa (as it did at Coles under previous management) than about unethi behaviour.

Woolworths and Coles dominate grocery retailing to an ext unparalleled in other countries, with a combined market share of ab 80%. Smaller retailers have complained perennially to the authorit about the grocery market duopoly, and have gained sympathy from ba benchers. A Parliamentary Inquiry was held in 1999 which ma supportive gestures (Joint Select Committee on the Retailing Sect 1999), but no substantial government action resulted.[1] Small retail face the hurdles that the rise of the duopoly has (at least for now) brou lower prices for consumers, and that in any case the market dominar appears impossible to unwind.

Woolworths and Coles have reached a relative impasse with groc market share. Given indecision from the experts and inaction fr governments, the two companies are now applying the full range strategies developed in the grocery sector to other key retailing secto

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1 A Retail Grocery Industry Code of Conduct was established in 2000 but, a voluntary code, it relies upon the retail giant to display ethical practices to wl they are not naturally disposed.

The companies have rapidly created and extended a market dominance in petrol retailing. Woolworths has also attempted to incorporate the retailing of pharmaceutical products in general supermarket retailing. That market remains relatively restricted because the Pharmacy Guild is a fearsome lobbyist, but Woolworth's CEO Roger Corbett is working assertively on breaking down current restrictions on pharmaceuticals retailing.

After petrol, packaged liquor has been the main 'war zone' for Woolworths and Coles. Independent liquor retailers are more fragmented than the pharmacists – the lobby organisations are State-based, and the large retailers are themselves influential players in some State organisations.

This paper examines the dimensions of the push by Woolworths and Coles into liquor retailing and the relevant regulatory environment. A summary is provided of the rapid growth in market share, essentially by means of acquisitions. Some key strategies are examined by which the retailers have assertively exercised their market power to further enhance their market share. To the detached observer, these strategies constitute unconscionable behaviour. There follows a discussion of the conceptualisation of competition, with a claim that both controversy and silences weaken the utility of the current conventional wisdom to elucidate the practices of the giant retailers. The regulatory environment is then discussed. First, the evolving licensing structures for liquor retailing in the States (and the responses by the retailers) is selectively treated. Second, the legislation and recent regulatory response at the federal level is outlined at length. The paper concludes and regrets that ultimately there is no effective regulatory impediment to Woolworths and Coles acquiring a dominance in liquor retailing comparable to that already attained in grocery retailing.

Coles and Woolworths' Escalating Significance in Liquor Retailing

According to conventional media accounts, take-out liquor retail sales are worth about $11.5 billion a year (Evans, 2005). Estimates of market share of the big two are clouded by the fact that figures given are often in percentage of licenses held, which understates their place in the market. Share of turnover is the standard criterion for determining market share. Trade insiders claim that a more accurate figure for take-out sales would be somewhat over $9 billion of a total liquor market of about $17 billion.

Coles and Woolworths have seen the major independent outlets as attractive takeover targets to enhance market share relatively quickly. Coles purchased the Liquorland group in the mid-1980s, signalling its entry into liquor retailing activities. Coles then bought Vintage Cellars in 1992, the Australian Liquor Group (including Philip Murphy) in 2001, and the sizeable Theo's business in 2003. Woolworths bought Victoria's Dan Murphy in 1999, Tooheys Bros in Sydney in 2000, the Liberty Liquor group (including Harry's Liquor) in 2001, the Booze Brothers Chain in South Australia in 2000, the Super Cellar group in South Australia in 2003, Bailey & Bailey in South Australia in 2003, and ALH in late 2004. Woolworths also acquired 18 licenses from the purchase of Franklins' grocery chain in 2001. Coles and Woolworths have also been buying selected independent outlets, especially those strategically place, whether in suburban Sydney or country towns (Independent Liquor Group, 2003).

It is estimated that by March 2005 Woolworths owned about 950 liquor outlets nationally and Coles about 625 outlets (Evans, 2005). Woolworths has about 26% of the national market and Coles about 19%, with a combined market share of about 45%. The bulk of this share has been acquired in the last five years.

The rapid growth in market share has been built on successive acquisition of liquor retailing chains. However, the two retailers have also engaged in a number of strategies to enhance their dominance, all of which involve an assertive use of their market power (understood as across the retail sector in general). These strategies will be addressed in the following section.

Market power has to be understood as across the retail sector in general. One manifestation of the structural power of the two retailers is the low rentals that they pay for space in shopping centres, their typical location. Shopping centre landlords treat the retailers as 'anchor tenants', so that all other shopping tenants cross subsidise the large retailers through the rentals they are forced to pay for the privilege of proximity to the giants. Coles and Woolworths thus can leverage this gain to cross-subsidise other activities.

The Structural Manifestations of Market Power

A long-standing reflection of the retailers' assertiveness is in the field of liquor licensing regulation. Small retailers wanting to apply for a license or transfer or modify an existing license have confronted perennial objections by the giants in the State Licensing Courts. The practice of harassment over small business liquor licenses appears to be systemic.

For example, in 1995 in Adelaide, a small food market trader of organic products applied for a liquor license to sell organic wines (Wilsons Organics, 2005). Coles fought the application in the South Australian Licensing Court and appealed an adverse judgement in the Supreme Court, all with highly-paid counsel. Coles lost this battle, but the fact that it was prepared to expend substantial resources on harassment of a minnow is indicative of a strategy of market dominance.

In 2000, a NSW Central Coast publican, Bob Bourne, tried to transfer a dormant liquor licence into a new tavern and retail outlet in West Gosford. Under threat from Coles, Bourne agreed to a covenant preventing any take-out liquor sales. The licensees of the Red Lion Hotel in Rozelle, an inner west suburb of Sydney, sought to expand their business. They faced objections from Coles which ran an outlet 12 kilometres along Victoria Road in Ryde (Mitchell, 2003b).

The ACCC took Coles and Woolworths to court in 2003 over Gosford and Rozelle and comparable cases. However, the practices continued. An attempt by proprietors of a general store in the village of Palmers' Island in North Coast New South Wales has been blocked by Woolworths, which operates a large liquor outlet in the resort town of Yamba. According to the Grafton Daily Examiner (Bancroft, 2005):

> Objections subsequently lodged by Woolworths include that 'the interests of Woolworths are likely to be adversely affected by the

> granting of this application' and 'the needs of the public in the neighbourhood of the proposed premises to which the application relates can be met by facilities for the supply of liquor existing in and outside the neighbourhood of the proposed premises'.

Another important element central to the two retailers' power relates to price discounting. Coles and Woolworths regularly sell liquor at lower prices than their competitors. One would expect that lower prices would be a reflection of the two retailers' ability to generate unit cost economies from their scale of operations. For example, Woolworths is known to be engaged in a long-term project to reduce costs through improvements in supply chain logistics. Formally, this activity is a reflection of the meritorious aspects of the competitive process. However, lower prices are perennially lower than the prices that their small-scale competitors pay for the products wholesale. This phenomenon is especially prevalent in beer sales.

Victoria offers a case study in the assertive price-cutting of Woolworths and Coles. In mid-November 2000, an advertisement by Dan Murphy (a Woolworths' subsidiary) appeared in the Melbourne papers offering a range of Southcorp wines under wholesale price. The popular Queen Adelaide range was the focus of the offerings. It is unclear whether Southcorp initiated the strategy (Southcorp was experiencing a wine glut) or whether it was initiated by Dan Murphy (Westfield, 2002b). Regardless, Dan Murphy obtained an atypical discount from Southcorp, then subtracted that discount from the wholesale price and offered the wine retail at 'cost'.

The effect cascaded through the industry. For example, an independent group then under the Wineslashers banner (now under the Duncans banner within the Southern Independent Liquor Groups) had a long-standing relationship with Southcorp.[2] Wineslashers had supported Southcorp with a Christmas order of 70 pallets, a total of almost 4,500 cases. The next year the order was down to 50 cases.

2 Personal communication, Ian Urquhart, sometime independent group representative, 29 October 2004.

Sales of the premium wines are also affected. The premium wines from Southcorp are conventionally rationed to potential customers, the rationing based on the order size of the lower quality wines. The corruption of the lower end market thus corrupts the higher end as well.

In this exercise, the independents were under-cut, but so also was Southcorp with its substantial discounting 'strategy', leading to substantial losses for Southcorp over several years. Southcorp's brand value was dramatically reduced (Westfield, 2002a).[3] Coles and Woolworths are now applying similar pressure on the two big brewers. Apart from the redistribution of revenues along the supply chain, the retailers' pressure acts to devalue the brands of the manufacturers and suppliers, with long-term adverse implications for their revenues.

In the month before Christmas 2004 the deep discounting practice was repeated. Safeway (the Victorian vehicle of Woolworths) heavily discounted Fosters Group liquor – beer and Beringer Blass wines, complemented by a cross-subsidised docketing discount associated with grocery purchases (as with petrol sales).[4]

Coles responded to Woolworth's cross-subsidisation by offering comparably low prices on comparable products, even renouncing the docket. Cases of Cougar (bourbon and cola) were being offered at $40.00, below the wholesale price. The wholesale price for Victoria Bitter was $32.55; Safeway was offering it at $3.57 less.

Independents then proceeded to take Beringer Blass wines off the shelves, to prevent the adverse price comparison with these wines by customers poisoning the turnover of the rest of their stock.

At the same time (early December 2004) in Sydney, Dan Murphy was offering Toohey's Extra Dry at $31.90 a case and Carlton Sterling at

3 Southcorp is now subject to a hostile takeover bid from Fosters' Brewing.

4 Paradoxically, current conventional wisdom dictates that government business enterprises should not cross-subsidise services because this practice contravenes sound market principles. Cross-subsidisation (say, of rural constituents) for the broader public interest is unacceptable, yet cross-subsidisation across retail fields by private corporations to undermine cost-based pricing is acceptable. The logic and the ethics behind the regulatory acceptance of these divergent scenarios are not obvious.

$22.90 a case. The wholesale price (with GST) was $35.86 and $25.91 respectively.

The chains' strategies for supply chain management certainly contribute to cost reductions, but a significant component of the lower prices appears to be funded by the suppliers. The major reflection of the retailers' market power is in their dominant relationship with their suppliers. Coles and Woolworths predictably achieve discounts from suppliers for large-scale bulk purchases. More systematically, however, Coles and Woolworths are the beneficiaries of special deals that they have initiated over the years and have expanded as their power has expanded.

The standard demand from Coles and Woolworths from suppliers is for wholesaleprice minus 4% rebate for access to shelf space, minus 4% rebate for promotion, with another cut for hypothetical ullages (breakages), minus 2.5 to 3% rebate to settle their debt in the conventional period. Smaller competitors look to sell at wholesale plus 25%; Coles and Woolworths look to sell at wholesale minus a percentage of the rebates extracted from suppliers.

Details of supplier contracts remain secret, and suppliers are threatened with a refusal to deal if contract details are publicised. Surprisingly, Woolworths has admitted its motives. According to Bartholomeusz (2004), 'Woolworths has cited enhanced scale and leverage with suppliers as a benefit of the ALH bid'.

Woolworths reported a $688 million net profit for 2003-04, but also reported the receipt of $547 million in rebates. Coles reported a $616 million net profit, but has ceased to publicise the rebate figure;[5] on previous reporting, the rebate is running at well over $500 million. Comparative figures from previous years are in Table 1. It appears that

5 Previous reporting of rebates has followed Australian Securities and Investments Commission directives, but Coles defends its non-reporting in terms of international accounting standards.

the net profits of the two retail giants are dominated by monopoly extractions.[6]

Table 1. Woolworths Ltd / Coles Myer Ltd. Profits & Rebates ($m.)

	1999-2000	2000-01	2001-02	2002-03	2003-04
Woolworths Ltd					
Net Operating Profit	295.5	428.0	523.2	609.5	687.8
Rebates & Discounts	372.4	473.6	511.8	493.2	547.3
Coles Myer Ltd					
Net Operating Profit	278.3	140.2	345.0	429.5	616.5
Rebates & Discounts	462.2	575.0	650.6	n.a.	n.a.

Source: Woolworth Ltd, Concise Report; Coles Myer Ltd, Financial Report' various years

This practice of demanding rebates from suppliers is entrenched. It appears to be an unsustainable practice for the survival of smaller suppliers. Even if the destruction of competitors leads to the cessation of deep discounting, the two giants would presumably continue to demand rebates from their suppliers.

An *Australian Financial Review* journalist (Mitchell, 2003a) reported that 'Some industry observers says that once the major chains have reached a certain level of market share, they will take their foot off the discounting pedal and allow margins to rise again'. It was reported that other observers think that Coles and Woolworths will continue to compete on price, but the prospect is that price discounting will cease when there is no local competition to worry about. This phenomenon is already being observed in supermarket pricing of meat and fruit and vegetables. A 14 July 2004 survey by the industry watcher FoodX noted that a basket of comparable products was being sold for significantly higher prices by Coles and Safeway in suburban Malvern compared to their prices in Prahran where the big two faced competition from ALDI (FoodX, 2004). The benefit to the consumer is thus at the expense of suppliers and is likely to be temporary.

6 Economists would formally label these sizeable rebates and discounts from suppliers as monopsony extractions.

These practices by Coles and Woolworths deserve to be refracted through a theoretical lens. Unfortunately, we are poorly served with a theorisation of the way in which large corporates deal with less powerful companies across 'the market'.

Conceptualising the Structuring of Power in Market Relations

There is at present an inadequate conceptualisation of the nature of competition. There is a running tension between various schools of thought that is both poorly treated in the academic syllabus and marginalised in the ideological centrality of 'competition' in the defence of merits of the 'market economy'.

The edifice known as 'perfect competition' monopolises the economics textbooks but it generally remains quarantined within the academy. In the administration of competition law, a notion of 'workable competition' has been essential and the 'structure/conduct/performance' model of applied industry economics has come to the rescue. Briefly, the model imparts a substantial deterministic role of the structure of the industry on industry performance in terms of public interest criteria. Other things equal, an industry structure of dispersed non-collaborative firms generates desirable social outcomes. In practice, the 'degree' of competition has come to be measured by the 'concentration ratio', the percentage of industry market share held by industry leaders. The proscription of particular firm conduct complements policy directives regarding preferred industry structure (Scherer, 1970, 16).

During the 1970s in the US (a country having an active tradition of regulatory antitrust activity) a competing approach evolved, one name for which is the 'contestability' tradition (Baumol *et. al.*, 1982; Bork, 1978). The 'contestability school' (now closely linked to the University of Chicago) denies that an industry dominated by a handful of corporate giants will be anti-competitive; on the contrary, its characteristic behaviour deserves to be labelled 'competitive' and to attract the moral support usually attached to the label itself.

The ACCC has accommodated the structure/conduct/performance and the contestability mentalities in a pragmatic way, sometimes leaning towards the one, sometimes to the other. The tension is particularly acute in the administration of Section 50, the merger provision of the Trade Practices Act. The public statements of Graeme Samuel, the ACCC Chairman since July 2003, embody no coherent intellectual stance; however, with respect to the retail sector Samuel appears to be strongly sympathetic to the contestability approach.

However, in neither of these schools is there a capacity for an adequate conceptualisation regarding relations between small business and big business. The contestability approach tacitly assumes that small business is a hangover from a more inefficient age and deserves obliteration (a libertarian sister to Marxism?). The structure/conduct/performance model tacitly implies the capacity for large firm dominance over small firms, but the details are not pursued.

The one confrontation with market power in the tertiary economics syllabus is via a 'monopoly' model so purist that it transcends applicability. The apparent preference for analytical elegance (and perhaps a reluctance to confront the adverse dimensions of 'free markets') has marginalised examination of the structural subordination by which small businesses face corporate business in market relations.

On the margins of the economics discipline, the American Institutionalists have pursued more explicitly an analysis of the structuring of market power. In 1952, J. K.Galbraith's *American Capitalism* referred to the structural power of big business (Galbraith, 1952). *American Capitalism* attempted to resolve a long-standing ideological and political impasse for economic liberals. In the early decades of the twentieth century, economic liberals hoped that the persisent rise of corporate business would be checked by antitrust enforcement. By the 1940s, these hopes were accepted as naïve. Galbraith's analysis accommodated the permanence of powerful corporate business yet catered to the liberal ideal of a 'self-regulating' system that ultimately checked exploitation of market participants.[7]

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7 Galbraith's analysis replicated in the economic sphere the theorists of pluralism in the political sphere.

Galbraith proposed that market power, residing essentially in the producing sector, could be countervailed by a rising scale of the retailers.[8] The retailers would be a force for good, generating an internal balance within the market that would continue to ensure a pluralism in American politics. Legislation against retail price maintenance is a product of such an age.

Following *American Capitalism*, Galbraith's interpretation of the American economic system became more jaundiced. His later book *Economics and the Public Purpose* (Galbraith, 1973) posited a 'dual economy', comprising a 'planning system' of corporate business and the state and a 'market system' of small businesses. The market system was structurally subordinate to the planning system, and exploitation was structurally entrenched.

Galbraith's analysis, although superficial, has captured some essential characteristics of modern capitalism. However, his challenge of a more elaborate articulation of structured market power has not been taken up within the economics profession. Similarly, there has been a marginalisation of earlier attempts to analyse the intrinsic dynamic associated with the institutionalisation of the profit motive – notably the Marxist tradition, but also strands within orthodoxy.[9] As a consequence, neither the dynamic nor the contemporary structure of the so-called market economy receive appropriate attention from the relevant professionals designated as experts in the area.

In terms of the particular industry under consideration here, Galbraith's saviours in *American Capitalism*, the large retailers, have now surpassed the producers in the possession of structured power. Market power now resides with retailers like Coles and Woolworths.[10] These giants now

8 Galbraith also proposed that the rise of unions would countervail the power of business in the domain of wage labour.

9 For example, the work of the Oxford economist D. H. McGregor (c/f McGregor, 1911).

10 In the U.S. Wal-Mart is the dominant retailer; in the U.K. it is Tesco. Wal-Mart and Tesco have transcended national boundaries and are now global forces. In the Australian grocery market, Coles and Woolworths feel threatened by the entry of German retailer Aldi. This rivalry between giants provides the substance of the

dominate smaller competitors and suppliers, including large corporate suppliers. Fosters floated its subsidiary Australian Leisure and Hospitality Group (ALH) out of the parent group in 2002 because Coles and Woolworths were not going to tolerate a liquor producer also functioning as a retailer.[11] Coles had begun to reduce the stocking of Fosters' lines in its outlets.

The response of the regulatory authorities to the manifestations of retailer dominance and assertive strategies will be treated below. This treatment is prefaced by an examination of State-based regulation that is peculiar to liquor retailing because of its moral implications.

Regulatory Structures Across the States and the Coles/Woolworths Response

Packaged liquor retailing has been subject to special licensing restrictions in all States. The existing regimes are a product of the influence of vested interests (especially privileged liquor outlets like hoteliers and clubs) and of moral concerns that have acted to restrict the number and character of liquor retail outlets. The National Competition Council which presides over National Competition Policy finds the old regimes anti-competitive (as they are), and has pressured the States into examining them with a view to dismantling such licensing restrictions. In general, Woolworths and Coles are leveraging the rollout of National Competition Policy to replace one restrictive regime with another.

In Queensland, the transition will be particularly smooth, as independent packaged liquor retailers, not being hoteliers, are excluded from that market. A 1999 KPMG report for the Queensland Government appeared

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'contestability' argument. However, this process does not vitiate the arguments regarding structural subordination outlined in the text.

11 Fosters floated ALH rather than resort to a trade sale precisely to avoid ALH being acquired by one of the retailing giants. Fosters also closed down its on-line retailer Wine Planet to placate the retail giants. Given the necessity to buy out co-owners, the closure apparently cost Fosters about $100 million (Bartholomeusz, 2004). This outlay was the cost of acceding to pressure from the retailers, ironic given that Wine Planet was a failing business.

to cater to the established interests both old and new (KPMG Consulting, 1999). The report condoned the continuation of the hotel monopolisation of liquor licenses. Moreover, the three additional retail liquor outlets (detached bottle shops) that come with every hotel license were allowed an expansion of floor space and an extension of distance from the 'core' hotel to 10 kilometres. This development made Queensland hotels more appetising for Coles and Woolworths and they have proceeded to buy them up.

Coles entered the Queensland market in 1998 with the purchase of a couple of hotels. Coles then bought the Leda group of hotels, giving it about a dozen. Woolworths became apprehensive and entered the hotel market as well. In particular, in January 2002 Woolworths (with its hotel managing joint venture partners) bought 11 hotels and 20 liquor outlets in South-Eastern Queensland.

In 2004 Woolworths and Coles battled to take over ALH, the now independently listed company. Woolworths was the successful suitor, paying approximately $1.3 billion, albeit Fosters had obtained only $875 million for the float (Durie, 2004). Nationally, ALH owned 263 liquor shops and 130 hotels, of which 54 hotels are in Queensland. With ALH, Woolworths obtained over 200 liquor outlets in Queensland; 50 of those come with hotels with significant real estate which will likely be converted into large scale Dan Murphy outlets. Even if the liquor industry is deregulated in Queensland, Woolworths and Coles will dominate the post-deregulation scramble for market share.

ALH is a significant prize, but Woolworth's Roger Corbett had previously claimed that his early offer of $2.86 per share reflected the company's worth. With Coles making a counter bid, Corbett had to lift the offer and the final bid translated into approximately $3.76 per share. Purchase of assets at an excessive price may reflect an irrational egotism on the part of the bidders. However, a more plausible interpretation is that these assets are expected to enhance the purchasers monopoly power, and subsequent pricing will be geared to recovering the excessive price paid.[12]

The Victorian scene operates differently. Packaged liquor retailing was deregulated early during the 1980s. Under pressure from the independents the largest retailer, the S. E. Dickens company (subsequently Coles), was constrained to its then 8% of the State's liquor licenses, and Woolworths was included in the same constraint. The large retailers lobbied Premier Jeff Kennett for further deregulation, with Kennett initiating the process with the Liquor Control Reform Act in October 1998. The Bracks Government responded to persistent lobbying by amending the Act in May 2002, completing the deregulation of the industry (ending the constraints on the two giants) and allowing a dramatic increase in licenses (Westfield, 2002c). A transition period was established, with full deregulation to arrive in January 2006. At the time of breakdown of the restrictions, Coles and Woolworths were both in breach of the restrictions. Coles had 6 licenses more than its 8%; Woolworths had 36 more, the number having escalated with 18 liquor licenses acquired in the takeover of Franklins.

Woolworths then set about transferring some of its licenses to shelf companies to hide the excess (Westfield, 2003a). Brian Kearney, director of Liquor Licensing Victoria, condoned the transfers on legalistic terms. Rather than being forced to divest about 40 licenses, the breach was excused. Woolworths and Coles thus started the new era with an excess of $60m worth of liquor licenses and the scene was set for the gradual rise to dominance in Victoria.

In New South Wales, as in Queensland, hotel and club owners have been the beneficiaries of liquor retailing licensing restrictions. A *de facto* alliance has developed with organisations (such as the Network of Alcohol and Drug Agencies) concerned with the destructive capacity of alcohol abuse. Until recently, applications for a new liquor retail license had to satisfy a 'needs' test before the Licensing Court. A needs test also exists in South Australia.

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12 A similar phenomenon occurred with Coles' purchase of the Theo's liquor chain, estimated to be for $260 million, and Macquarie Bank's purchase of Sydney Airport for $5.6 billion.

The National Competition Council viewed the NSW (and South Australian) licensing structure as anti-competitive and recommended that the Commonwealth withhold payments under the Competition Policy agreements. In response, the NSW Government passed an Act in August 2004 that attempted to partially mollify the major players. The Act allowed a foot in the door to new 'competition' (meaning Woolworths and Coles), but catered to social concerns by requiring a Social Impact Assessment to be submitted with any license application.

Woolworths made its first application in December 2004 to the Liquor Administration Board for a new license in the outer Sydney suburb of Castle Hill (ironically a stronghold of evangelical Christianity). Woolworth's list of benefits associated with the granting of a new licence is purported to include 'access to cheaper alcohol' (Evans, 2005). Woolworths and Coles have also been engaged in buying up existing liquor outlets in NSW to acquire the associated licenses, and attempting to use those licenses to replace the purchased outlets with larger structures (Woolworth's Dan Murphy's being the model).

In summary, the two giants have now surmounted the extant regulatory hurdles in Victoria (by having them dismantled) and in Queensland (by buying into the still privileged structure). In NSW, progress is slower, but the companies have the NCC at their back, and the major hurdle lies with the resolve of the Liquor Administration Board. The biggest losers in packaged liquor deregulation are the independent small retailers wanting to enter the NSW market. The costs of the licensing process are prohibitive, about $100,000, so that the only beneficiaries are those independents still holding a licence and the two chains. For anyone wanting to obtain a new packaged liquor licence only the chains will have the resources to wade through the process.

Relevant Legislation and its Current Regulatory Oversight

The NCC that oversees the implementation of National Competition Policy has shown no concern about the incipient monopolisation of a 'deregulated' industry; implicitly, it appears to adhere to a contestability approach to competition.

The Productivity Commission provides the intellectual rationale that underpins National Competition Policy and the operations of the NCC in particular. In its recent mammoth review of NCP (Productivity Commission, 2005), The Commission gives only fleeting reference to potential large business predation (in the context of rural and regional impacts). Without examining evidence, the Commission then discounts the accuracy of those attempting to draw attention to this phenomenon. The Commission's implicit view is that small business is an inevitable casualty of the need for efficiency and lower prices (p.116-117):

> In essence, businesses everywhere — small and large — are facing greater competition from both domestic and international sources. To help meet this competition and the demands by consumers for better value for money, many businesses are looking to achieve greater economies of scale through rationalisation and consolidation.
>
> ... many of the presumptions and arguments underlying [concerns of small business marginalisation and large business predation] are not borne out by the facts. Thus, as alluded to above, additional competitive pressure on (large or small) businesses, whether in regional or city areas, should not of itself be a reason to change public policy (though it is clearly relevant in a transitional or adjustment context).

The ACCC does not have a strong record with respect to the defence of small business. The relevant legislation, the 1974 Trade Practices Act, has weaknesses in the areas relevant to small business, and the ACCC staff appear to be ill-equipped conceptually.

Section 45 of the Trade Practice Act (the Act) generally forbids contracts in restraint of trade. This section is not naturally conducive to catching unacceptable treatment of small business. However, the ACCC, under the previous Chairman Alan Fels, took both Coles and Woolworths to court under Section 45 to address the two companies' pressures on small retailers over liquor licenses (Australian Competition & Consumer

Commission, 2003b).[13] In these cases the restrictive agreements were forced on the independents by Coles and Woolworths. The cases have been dragged out in the Federal Court as the companies have employed their superior resources to wear down not merely small competitors but the ACCC itself.[14]

The case against Coles has recently been concluded when Coles admitted guilt and agreed to settle with the ACCC (Lee, 2005).[15] However, the action of the ACCC in this respect has been taken in isolation from the companies' behaviour in its entirety.

The acquisition of market share is dealt with mostly through merger provision of the Act, Section 50. With respect to a planned takeover or merger, the ACCC applies a 'threshold' test (a product of the structure/conduct/performance model). According to the ACCC's website (Australian Competition & Consumer Commission, 1998):

> Normally if a merger falls within the 'safe harbours' threshold the ACCC does not conduct any assessment as to whether the merger could be anti-competitive. The 'safe harbours' are:
>
> - that the market share of the merged entity is below 40 per cent; and
> - that if the market share of the merged entity is above 15 per cent, the combined share of the four largest market participants after the proposed merger is below 75 per cent.

The threshold test as presently constituted erects a significant hurdle. Most of the Coles and Woolworths takeovers are individually small

13 Fels served writs on the retailers on his last day in office on June 30 2003 (Mitchell, 2003b).

14 The two legal firms employed by the giants are Clayton Utz and Allens Arthur Robinson. Clayton Utz's ethics were displayed when it was found to have advised British American Tobacco to destroy documents to disarm litigation by smokers. Allens was home (until recently) of Bob Baxt, previous chairman of the Trade Practices Commission and foremost champion of big business in its relations with trade practices regulation.

15 Coles claimed that the practices were in the past and that it had since 'implemented a group-wide trade practices compliance strategy' (Lee, 2005). However, despite this claim there is no hard evidence that this compliance strategy has occurred.

scale. Their growth of market share is thus taking place by means of 'creeping acquisitions', a neglected phenomenon with major practical consequences. The ACCC's response to the acquisition of Theo's by Coles Liquorland is representative of the official position (Australian Competition & Consumer Commission, 2003a):

> Post acquisition, Liquorland will have market share figures below the ACCC Merger Guideline thresholds. Information obtained from market participants indicated that the removal of the Theo's Liquor outlets as an independent force was not likely to lead to a substantial lessening of competition in any relevant markets. Woolworths remains Liquorland's largest competitor in liquor retailing. In addition, a substantial proportion of retail sales for off-premises consumption in NSW remains in the hands of the independent sector and this sector, along with Woolworths, will continue to act as a competitive constraint on the merged entity.

Looking at single takeovers in isolation, and given the threshold test, ACCC Chairman Samuel has tended to be contemptuous of complaints about these takeovers. Samuel recently claimed (Evans, 2005):

> The whole issue of liquor, and grocery and petrol are under constant watch by us. Examinations to date have shown the number of creeping acquisitions is very, very small beer.

Small business has been lobbying the federal government about 'creeping acquisitions' for some time. The phenomenon of creeping acquisitions was belatedly put onto the political agenda, after small business lobbying of the Government's backbench. Thus the issue is addressed in the hearings and report of a recent Senate Inquiry *The effectiveness of the Trade Practices Act 1974 in protecting small business* (Senate Economics Referencs Committee, 2004).

However, the staff of the ACCC have been unprepared. An ACCC spokesperson complained to the Committee (p.63):

> the economics of it has not been easy, and we have had various bits of work commissioned as well as doing our own internal work, and we are still in the process of working our way through that.

This response is reflective of the limited intellectual environment in which the ACCC have been trained and nurtured, reflecting the general conceptual inadequacy amongst professionals outlined above. Within the ACCC itself (and its predecessor, the Trade Practices Commission), an informal culture has developed that pits business generically against consumers.[16] In the retail sector, with competition between Coles and Woolworths, the consumer benefits in the short term. From a short-term consumer perspective, the grocery market share of Coles and Woolworths is unproblematic. The same mentality is being implicitly applied to petrol and to liquor.

The Senate Committee bemoaned the lack of progress in inhibiting consolidation in the retail sector. The majority Senators were not prepared to be constrained by the hesitancy of expert opinion, and recommended action (p.64):

> The Committee considers that provisions should be introduced into the Act to ensure that the ACCC has powers to prevent creeping acquisitions which substantially lessen competition in a market.

The Government Senators supported no action in this respect, claiming that the present mergers section of the Act (Section 50) was adequate to inhibit anti-competitive merger/takeovers.

The abuse of structural dominance is covered mostly through Section 46 (abuse of market power) and Section 51 (unconscionable conduct).[17] The Trade Practices Act remains weak in both these sections, and judicial decisions (on Section 46) have reinforced the weakness.[18]

16 This emphasis is reflected in the appointment of Louise Sylvan as Deputy Chair of the ACCC in November 2003. Sylvan was previously a long-time senior staffer at the Australian Consumers' Association.

17 Section 52 (misrepresentation) was also previously relevant, but the coverage of unconscionable conduct of business against business now appears to have been centred in Section 51.

18 The ACCC took Boral through the courts over predatory pricing in the early 1990s recession. There was 'smoking gun; evidence of intent to drive out a smaller competitor. However, the High Court in February 2003 ruled in favour of Boral on the grounds that it did not possess market dominance.

Section 51 was enhanced in 1998 with amendments that introduced Section 51AC to explicitly incorporate 'unconscionable conduct' by large against small business. However, the hurdle to prove 'unconscionability' is high and the ACCC has been quiescent regarding the section.

In considering small business complaints, the Senate Economics References Committee split on Party lines in terms of recommendations. The majority (Labor and Democrat/Independent Senators) recommended substantial amendments to Section 46 (the details of which are not relevant here) to enhance the section's leverage against corporate abuse of its power. The Government Senators were supportive of only some of the majority Senators' recommendations. On Section 51AC the only recommendation of substance from the majority Senators was for the abolition of a threshold test regarding firm size; the Government Senators demurred even on that. There was no support for a strengthening of the wording of the provision to cover 'unfair, harsh or unconscionable' conduct.[19] Unfortunately, the test for unconscionability remains high because of the prevailing culture that 'rough play' is an integral part of the competitive process.

There is an anomaly here in that the Government Senators were led by Senator George Brandis, a lawyer with trade practices expertise. Brandis has made public pronouncements to the effect that the Act is insufficiently protective of small business (Westfield, 2003c), yet he has penned a minority report that perpetuates the lack of protection.

It is not improbable that the Government Senators were under pressure from the responsible Minister, the Treasurer Peter Costello, to undermine the Inquiry's assertive stance for small business. Brandis' minority report expressly denied that Section 50 (the merger section) needed modification to deal with the 'creeping acquisition' issue. Yet the Coles and Woolworth's takeover of liquor retailing exemplifies the creeping acquisition dilemma. The minority report implies that Senator Brandis has placed Party before Principle.

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19 This latter proposal had been forwarded by the Fair Trading Coalition, representing a broad cross-section of small business groups, but spear-headed by the Motor Trades Association of Australia.

In general, the prospect is that the Howard Government will not legislate any recommendations arising from the Senate Committee Report. The Government has been lobbied aggressively by representative groups from corporate busines .[20] That corporate business has taken a keen interest in inhibiting any legislative amendments favouring small business can be gauged by the propaganda effort waged in the financial press.[21] Small business is formally represented politically by a junior Minister, but the portfolio has never commanded clout.

The culture of the ACCC is now supportive of the two giants' activities across the retail sector. Chairman Samuel gave a speech to the Master Grocers of Association of Victoria in February 2004 emphasising that the ACCC cares only about consumers (Samuel, 2004a). Samuel's dominant preoccupation appears to have been with lower prices. Within this vision, Samuel has claimed that shopper-docket discounts (such as those dispensed to Coles/Woolworths grocery shoppers for petrol purchases in tied petrol outlets) are good because 'pro-competitive'.

> Let me make this point clear. It is essential that the commission's primary focus remains on the interests of consumers – that is to say, the community at large – and is not diverted to protect certain sectors of business from healthy competition.

Samuel repeated this strong view at a dinner speech at the Australian Graduate School of Management in November (Samuel, 2004b). Samuel claimed (pp.1, 4):

> Competition ... benefits those businesses that are able and motivated to take advantage of the powerful forces driving their particular market. The corollary, of course, is that businesses that

20 The Law Council of Australia, a body that ought to display impartiality, has also lobbied strongly for the corporate business position.

21 For example, it was reported in December 2004 that 'The Business Council of Australia plans to head off a renewed push by small business and the Productivity Commission for tougher, industry-specific laws to help secure fairer deals with big business. The BCA is launching a major research project to highlight what is says are strong levels of competition in highly consolidated industries such as the retail grocery, petrol and banking markets, a move designed to debunk claims by small business that mergers and alliances are reducing competition.' (O'Loughlin & Hepworth, 2004)

> are unable or unwilling to respond to the, often daunting, challenge of competition, will languish and may ultimately fail. But this is the essence of an open market economy. ...
>
> What is not clear however, in the claims and counter-claims that are made by small and big business respectively in relation to these matters, is whether the primary case has been made for regulatory intervention. ... The difficulty in this area is that so often those who seek regulatory intervention have failed to first demonstrate the case for intervention.

In these speeches, Mr Samuel and his staff have ignored the broader implications of what they have judged to be oppressive behaviour exhibited towards small competitor liquor license applications, and to which Coles has admitted guilt. They have ignored the differential pricing strategies used by the giants depending on the availability of alternative retail outlets. More fundamentally, they have ignored the elaborate rebate system that has allowed the two giants to deliver such low prices at the expense of suppliers. This rebate system is directly a product of the extraordinary market power of the two giant retailers.

In general, the ACCC continues to adopt publicly an ambiguous (even duplicitous) position. This ambiguity is embodied in a speech by John Martin, the ACCC's small business commissioner, to grape growers in November 2004 (Martin, 2004). Martin claims that perennial complaints from small businesses are without foundation, and that the competitive process is a rough-house affair (p.11):

> It is important to recognise that the law does not exist to inhibit businesses from advancing their own legitimate commercial interests. The law will not apply to situations where a business has merely driven a hard bargain, nor does it require one business to put the interests of another party ahead of its own.

Yet Martin also claims that the ACCC has a range of powerful weapons and is assertively using those weapons in defense of small business rights. This claim is patently erroneous.

Conclusion

There appears to be no regulatory inhibition to Woolworths and Coles Myer acquiring overwhelming dominance in the liquor retailing sector. The implementation of National Competition Policy through the National Competition Council has involved the blackmail of States to deregulate their extant licensing arrangements. Victoria has capitulated to these pressures. Woolworths and Coles have moved behind Queensland's regulations and are poised to dominate that market should deregulation proceed. In New South Wales the 'social impact assessment' process for new licenses seems unlikely to impede the giants' progress towards domination of market share associated with the current licenses.

Both the NCC and the ACCC view the aggression of the two retailers as a boon to the constituency that matters – the consumers. As argued above, this view is short-sighted. It is also profoundly negligent of the businesses who are victims of a structured process of exploitation.

The general political ethos regarding small business emphasises that it provides the dynamic backbone of the free market system. Much of the accompanying rhetoric centres on the reduction of 'red tape' as the vehicle for the alleviation of small business problems in the marketplace. This rhetoric persistently ignores the structural subordination of small business. Woolworths and Coles have established a successful precedent in the grocery sector, and are now applying the same principles in the pursuit of domination of retailing in other sectors now that growth in the grocery market has stalled.

That the authorities judge this essentially monopolistic drive as acceptable represents a distortion of the anti-exploitative ethic that has always underpinned the defense of the market economy itself.

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