

# TESCO MAIN SUBMISSION TO THE COMPETITION COMMISSION (CC) INQUIRY INTO THE UK GROCERY RETAILING MARKET

## 1. SUMMARY

### **This document**

1.1 This document presents a summary of our main submissions to the CC inquiry. It is intended to help the CC by providing an overview of our views of the market, and on the issues raised by the CC.

1.2 This first section provides an overall summary of our views. In Section 2 we provide some background to the reference. Market definition is covered in Section 3 whilst our views on competition within the market are presented in Section 4. Section 5 describes how customers have benefited from this competition and Section 6 summarises our strategy and contribution to these benefits. Section 7 covers retail competition, Section 8 the supply chain, and Section 9 land and planning.

1.3 The CC considered facets of grocery retailing in 2000, 2003 and 2005. Of its 2000 findings in respect of one stop shopping, the CC's then Chairman stated that, "*in relation to what is for consumers their single biggest weekly item of expenditure, competition has been hugely successful*"<sup>1</sup>. In its Safeway and Somerfield inquiries, the CC looked hard at the expected consequences of each of the referred mergers and intervened where it thought appropriate to remedy an expected substantial lessening of competition. However, on each occasion the CC had substantial evidence that in the market as a whole competitive rivalry worked effectively and demonstrably to the benefit of consumers.

### **Summary of our views**

1.4 In its report of 2006, the OFT acknowledged that the retail grocery market is operating so as to produce tremendous *benefits* for consumers. But it did not draw the obvious conclusion – that consumers are benefiting because of the intensity of competitive rivalry. Yet rivalry is the driving force in the current grocery retail market, which is widely recognised as being fiercely competitive. The OFT's reasoning for referring the market to the CC for inquiry was based on speculation as to what might happen in the future, rather than any evidence of anti-competitive conduct or consumer detriment, the main criteria under the Enterprise Act 2002 (the *Act*).

1.5 The significant benefits experienced by grocery consumers over recent years provide strong evidence that the market is operating effectively – indeed, more effectively than many other markets in the UK. Those significant benefits include the following:

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<sup>1</sup> Quotation from a speech given in 2002 by Sir Derek Morris, then Chairman of the CC and the Chairman of the panel in the 2000 Inquiry.

- (a) **prices are falling** and have done so consistently for several years. The OFT estimates real decreases of over 7 per cent between 2000 and 2005, and falling prices have saved consumers more than £3 billion over the last three years;
- (b) **product choice and range increases every year**, with new products constantly being introduced. The OFT estimates that larger stores have seen a 40 per cent increase in product range over the last five years;
- (c) **product quality is increasing**, with innovations in the supply chain resulting in more (and cheaper) choices of organics, high quality ready-meals, specialist bakery products and breads, locally-sourced meats and produce, environmentally friendly household products, ethnic products such as Halal meats and improved food safety;
- (d) **service levels are high and improving**, with more in-store facilities, longer opening hours, less customer queuing, better trained staff and increased home delivery – our evidence shows that 85 per cent of shoppers regard their shopping experience as either excellent or good;
- (e) **customer satisfaction levels are high and rising** – our evidence shows that 85 per cent of shoppers in supermarkets generally say the shopping experience has improved over the last five years and 70 per cent of shoppers in convenience stores agree; and
- (f) **environmental footprint is improving** - many of the larger supermarkets are making commitments to extensive and long-term sustainability initiatives that respond to the growing importance of the environmental challenges that we all face. For our part we plan to halve energy consumption of our new stores by 2010, and we have set aside £100 million for technologies that promote environmental sustainability of our business.

1.6 We do not know of any evidence that contradicts these facts, and they are recognised by almost all independent commentators including Verdict, the Institute of Grocery Distribution (*IGD*), Mintel and many financial analysts.

1.7 Another consumer benefit is high fascia choice - research shows that 94 per cent of customers in GB have a local choice of three or more different supermarket fascias - choice of all grocery fascias is higher still. Customer switching is very common and customers are shopping around more – independent research shows that the average number of fascias used by customers in a four week period has increased from 2.8 in 2003 to 3.0 in 2006 and the value of switching has almost doubled over the past five years.

1.8 In addition, choice is increasing in many parts of the country. While we do not agree with the postcode methodology employed by the CC in 2000, we have revisited the 53 Postal Areas where Tesco was found to have a share of more than 25 per cent. In 98 per cent of the Postal Areas, at least one competitor has opened a new store since January 2001, and in 70 per cent of the Postal Areas *three* or more competitors have opened new stores.

1.9 Grocery consumers have a wide range of retailers to choose from. Our rivals include Wal-Mart/Asda, Sainsbury, Morrison, Waitrose, Marks & Spencer, Somerfield, Aldi, Lidl and Netto, other smaller supermarkets, Costco and Makro, the Co-Ops, symbol groups and thousands of independent retailers, including non-food retailers, such as Boots and Woolworths, each of which has or can build a profitable business model to secure its place in the grocery retail market.

1.10 From our own small beginnings, our leading position has been won through fair competitive rivalry and normal competitive conduct. It is not that long ago that Tesco was in trouble, written off by many analysts. We set out a new strategy that was based on listening to customers and responding, as best we can, to their needs. This is still something that differentiates us from our competitors and underpins our success. It has allowed us to prioritise our actions, to improve and accelerate our innovations, to expand into new product areas, to operate from smaller stores and to be flexible in how we open new stores and how we acquire the land we need to grow. Many of our innovations are small, but others are large, and carry with them a commensurate amount of risk. Indeed, we consider that a willingness on our part to take greater risks than some of our rivals has been another secret of our success over recent years.

1.11 However, we cannot sit back. We know from experience that customers are very mobile and that mistakes are punished quickly. Our research shows how quickly customers will leave if our prices are poor, or if we do not match their expectation on product quality or availability (something we experienced in 2002/03). Our competitors know this as well. Over the past few years some have done very well, whilst others have done less well. This is all part of the competitive process and, if history tells us anything, it is that retailers' fortunes ebb and flow and those that were doing poorly in the recent past (such as Sainsbury or Marks & Spencer) will improve, whilst those who have created a good offer (such as Waitrose and the discounters) will expand. This constant pressure to do well, and to keep adapting to changing consumer demand, is what has produced the consumer benefits listed above.

1.12 Of course, we do understand that some of our customers, suppliers and other partners have concerns about specific aspects of the market. Some of those concerns were identified by the CC in its Statement of Issues of 14 June 2006 (*the Issues Statement*), and we attempt to address them below and in our more detailed responses to the CC. We trust that the CC, when it has reviewed the mountain of facts in front of it, will conclude that the grocery market continues to work well for consumers. We do not believe that these facts paint a picture of a market with competition problems, or a market with a poorly functioning supply chain. Quite the opposite.

1.13 We believe that the evidence shows that competition is strong across all sectors of the market. The primary reason for the increase in national concentration is the result of a merger which was regarded by the CC as pro-competitive (*Morrison's/Safeway*), and the ongoing healthy process of competitive rivalry, in which retailers are rewarded for innovation and improved performance with additional customers.

1.14 Supermarket entry into convenience retailing appears to us to be a classic case of innovation by us and by Sainsbury – we moved into new formats in town centres, stimulating the sector and offering increased choice and better value for money. This is not conduct that has an adverse effect on the competitive process, even if some retailers have found the challenge of this new entry difficult to address. Other retailers, including independents, have responded to this enhanced rivalry and have raised their game, whilst others are entering the market for the first time.

1.15 Further, the exit of a limited number of independents should be seen in context, as it is part of a broad societal trend that has been taking place for the last fifty years. As the IGD has pointed out in respect of non-affiliated independents, “*This is a continuation of a long term trend, although the rate of decline halved in the latest year*”. Nor is the trend necessarily attributable to supermarket entry, starting as it did before our and Sainsbury’s entry into the sector. The IGD went on to note that “*operators... face particular trading challenges, including issues of succession planning, increasing staffing costs, the impact of new legislation and the financial requirements of developing a modern convenience offer*”<sup>2</sup>.

1.16 We believe that the evidence will also demonstrate that:

- (a) pricing policies are competitive and the OFT’s concerns about possible price flexing and below cost selling are misplaced since they are *de minimis*;
- (b) the supply chain works effectively, as it must if we are to provide new and improved products at lower cost each year. Our incentives are to work with suppliers continually to improve our offer and to ensure that the supply-base itself remains competitive and efficient. There are no signs of any competition problems. In particular, the “waterbed” and “tipping point” theories are unsound and unsupported by any evidence – indeed the evidence is firmly against them;
- (c) whilst the planning system adds a level of complexity to UK retail markets, it does so in the context of the wider policy objectives that it seeks to achieve. From a competition perspective, the real issue is whether the planning regime significantly affects the growth opportunities for retail businesses to the detriment of customers. The facts show that it does not, as demonstrated by the significant expansion of stores over the past five years; and
- (d) we research, acquire and develop land for the purpose of opening new stores or extending existing stores. We work with the grain of the planning regime and go deep into city areas with ambitious and risky regeneration programmes. We take risks and we lose sites where we do not get the approvals. But we do not engage in a spoiling game.

1.17 Throughout our response the CC will see that our focus is on the customer and our determination to serve the customer better than our competitors so as to earn their lifetime loyalty. All of our conduct, from acquisition of land to development of stores

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<sup>2</sup> *Convenience Retailing 2006*. IGD, page 6.

of different kinds, from the dynamic development of our supply chain, from the way we reward and develop our people, from our involvement in the communities in which we operate, and from our day-to-day service of the customer has that one aim. And competition drives it.

## 2. THE REFERENCE IN CONTEXT

2.1 This Inquiry results from a referral to the CC by the OFT in May 2006 under section 131 of the Act. The focus of a market investigation under section 134 of the Act is to find out whether a market is functioning effectively. The Act requires the CC to examine whether there are any features of the market under investigation that prevent, restrict or distort competition. If there is any such feature it is treated by the Act as an adverse effect on competition. The CC is also under a duty to identify whether any adverse effect on competition has a detrimental effect on customers in the form of (a) higher prices, lower quality or less choice of goods or services in any market in the United Kingdom (whether or not the market to which the feature or features relate); or (b) less innovation in relation to such goods or services.

2.2 In recent years, the competition authorities have on several occasions considered aspects of the retail grocery market, including some of the aspects now before the CC once again. On each occasion the evidence has broadly indicated that the market is competitive and working well for consumers.

2.3 The CC considered facets of grocery retailing in 2000, 2003 and 2005. Of its 2000 findings in respect of one stop shopping, the CC's then Chairman stated that, "*in relation to what is for consumers their single biggest weekly item of expenditure, competition has been hugely successful.*" In its *Safeway* and *Somerfield* inquiries, the CC looked hard at the expected consequences of each of the referred mergers and intervened where it thought appropriate to remedy an expected substantial lessening of competition. However, on each occasion the CC had substantial evidence that in the market as a whole competitive rivalry worked effectively and demonstrably to the benefit of consumers.

2.4 The mergers that took Tesco and Sainsbury into convenience retailing were cleared but not waved through by the OFT: they were subject, at least in Tesco's case, to the most rigorous scrutiny in case they might give rise to a substantial lessening of competition. None was found. Moreover, in 2005, the OFT found no breaches by Tesco of the Supermarket's Code of Practice when its audit was published in March 2005.

2.5 As recently as October 2005 the OFT concluded that there was no need for a full referral of the grocery market. Even when making the current reference to the CC, the OFT devoted a substantial part of its Report to a description of the Price, Quality, Range and Service (**PQRS**) benefits and improvements secured by consumers in this market. They are benefits directly attributable to the market structure and the practices of retailers now under investigation, which are the antithesis of features that have an adverse effect on competition within the meaning of the Act.

2.6 Nonetheless, the reference has been made, and we are confident that the CC will base its analysis on a detailed review of all the facts. We are also confident that,

as indicated in its Issues Statement, the CC will take care to distinguish competition issues from the non-competition issues that may be raised by some parties but which are beyond the scope of this Inquiry.

### **3. MARKET DEFINITION**

3.1 We think that this Inquiry gives rise to an important opportunity to examine the retail grocery market in the round. We welcome the fact that the CC will not be confined by previous models or definitions.

3.2 Previously, due to constraints in its terms of reference, the CC's focus has been on individual sectors of the grocery market, rather than on the market as a whole, and its analysis has to an extent developed piecemeal. We believe that the resulting analysis fails to capture how the market as a whole operates, in particular in the light of recent changes.

#### **The product market is that for grocery retailing**

3.3 In respect of the product market, we consider no longer tenable the distinctions that the CC has previously drawn between primary, secondary and convenience shopping. These distinctions are inconsistent with the diffuse and mobile consumer demand for groceries that now exists. The entry by larger operators such as Tesco and Sainsbury into convenience stores and the growth in internet shopping are in part a reaction to this changing pattern of demand.

3.4 The CC should also give careful consideration to the position of Marks & Spencer and the discounters. In the 2000 report, Aldi, Lidl and Netto were excluded from the CC's economic market for "one stop shopping", even though they qualified as grocery retailers with stores above the reference level. In *Somerfield*, the CC concluded that neither Marks & Spencer nor any of Aldi, Lidl or Netto were effective competitors in the narrow sector of the grocery market on which the CC then focused. However, we consider it to be plain that they fall within the grocery retail market as a whole. These retailers pose a significant and increasing competitive threat to Tesco and others within the market. In fact, the ability of these operators to focus on subsets of our customers makes them particularly dangerous rivals.

3.5 We consider therefore that the issue of product market definition is ripe for reappraisal. We would suggest that, as it is not limited in its reference to artificial market segments, the CC adopt as its starting point the broader market consistent with the facts, including the following.

- (a) **High degree of overlap.** The CC's 'traditional' approach ignores the high degree of overlap between the types of shopping trips that customers can undertake to satisfy their needs and the types of shops where they can satisfy them. The purpose of a shopping trip is too fluid simply to be categorised either as one stop or secondary.
- (b) **Wide range of stores.** Customers can and do use a wide range of stores to satisfy their shopping needs. To the extent that shopping behaviour may be classified as "more primary" or "more secondary", customers can and

increasingly do carry out larger trips at smaller stores and smaller trips at larger stores.

- (c) **Store selection.** Customers can and do choose to make up the basket by store selection: buying one part of their shopping needs in one store and other parts in one or more other stores. And they can easily vary the balance of their shopping as between stores in which they shop. In other words there can be competition at the margin, in the sense of product-by-product selection between different stores, and switching can thus occur at the micro level.
- (d) **Customers are all different.** Customers' reasons for preferring different stores change all the time and different competitors will appeal to these preferences by focusing on different aspects of PQRS. Tesco and other retailers who attempt to be a broad church therefore have to do different things to satisfy different types of customer, and face competitive pressure from a wide range of retailers. Indeed, even on relatively generous criteria, only a small percentage of our customers exhibit the characteristics of pure one stop shoppers (i.e. shoppers who conduct only large weekly shops).
- (e) **Individual stores cannot discriminate between different types of customers and/or shopping trip (e.g. one stop or convenience).** At such time as customers enter the store, regardless of the nature of their trip, that store cannot discriminate and/or behave differently towards them e.g. raise or lower prices. The CC's current analysis can only be rendered consistent with the "hypothetical monopoly" test by assuming that they can.
- (f) **The marginal customers are critical to success.** With increased choice of store comes increased exercise of choice between stores. The marginal customer, whose goodwill and spend can make the difference between profit and loss, will be influenced by the small but important differences in PQRS offered in all formats by different types of retailer.

3.6 All of the above considerations still permit the CC to arrive at a view on the relative competitive impact that different grocery retailers (and non grocery retailers) have on each other. Extending the size of the relevant product market does not change any relevant facts about how competition works – which is the starting point of the investigation.

### **The geographic market is national**

3.7 In its 2000 report the CC concluded that the relevant geographic market was not national but local, albeit with national elements. An isochrone (i.e. drive time) methodology was used to define the geographic limits of local markets, urban and rural, for the purpose of determining which supermarkets and other stores competed within any local area. This methodology has been subsequently employed but does not lead to the conclusion that each catchment area delineated by an isochrone, for the purpose of legal and economic analysis under section 134 of the Act, amounts to a standalone local geographic market.

3.8 The following considerations suggest a national geographic market, rather than a huge number of local markets, each with their own distinct competitive features.

- (a) **We live in an age of rapid flow and transparency of information** to all consumers. Brand competition, including national advertising is part of the competitive process, as is the use of the internet by Tesco to publish its prices at all its stores across the country. The value of the brand is quickly eroded if a retailer cannot deliver its offer consistently across the country. The brand equity, in effect, conveys a promise to customers about what they can expect at every store in the country.
- (b) **Retailers in one geographic area are constrained by retailers in another** as virtually all the catchments overlap and this forms what economists call “chains of substitution” across the UK. The presence of such chains can be established on the evidence and underpins the arguments for a national market. There are no readily identifiable local or regional markets.
- (c) Across the UK, there are retailers who have **national strategies** relating to pricing, branding and range that barely vary in different local areas.
- (d) **Some customers travel further to shop.** The evidence suggests that the drive times conventionally used by the CC in urban and rural areas exclude a significant number of customers, including but not limited to marginal customers, who drive further to shop, which not only casts doubt on the accuracy and relevance of the methodology, but also points to what customers might be expected to do were the hypothetical monopolist to worsen PQRS significantly.

#### 4. COMPETITIVE RIVALRY

##### **The market is fiercely competitive**

4.1 In the OFT’s reasons for the referral, competitive rivalry barely gets a mention. Yet that is the driving force in the current retail grocery market, which is widely recognised as being “fiercely competitive”.<sup>3</sup> Brokers have pointed out how intense the rivalry is: S.G., for example, makes clear that “*food retailing is becoming ever more competitive*”.<sup>4</sup> Government is of the same view: “*Though concentrated, UK grocery retailing is very competitive, bringing many benefits to consumers. This has in turn increased competitive pressures on supply chains, which has posed both opportunities and threats to individual suppliers. By competing to gain market share against independents and each other, the multiples have responded in innovative, dynamic and generally profitable ways to socio-economic change and rising*

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<sup>3</sup> IGD News, 16<sup>th</sup> February 2006.

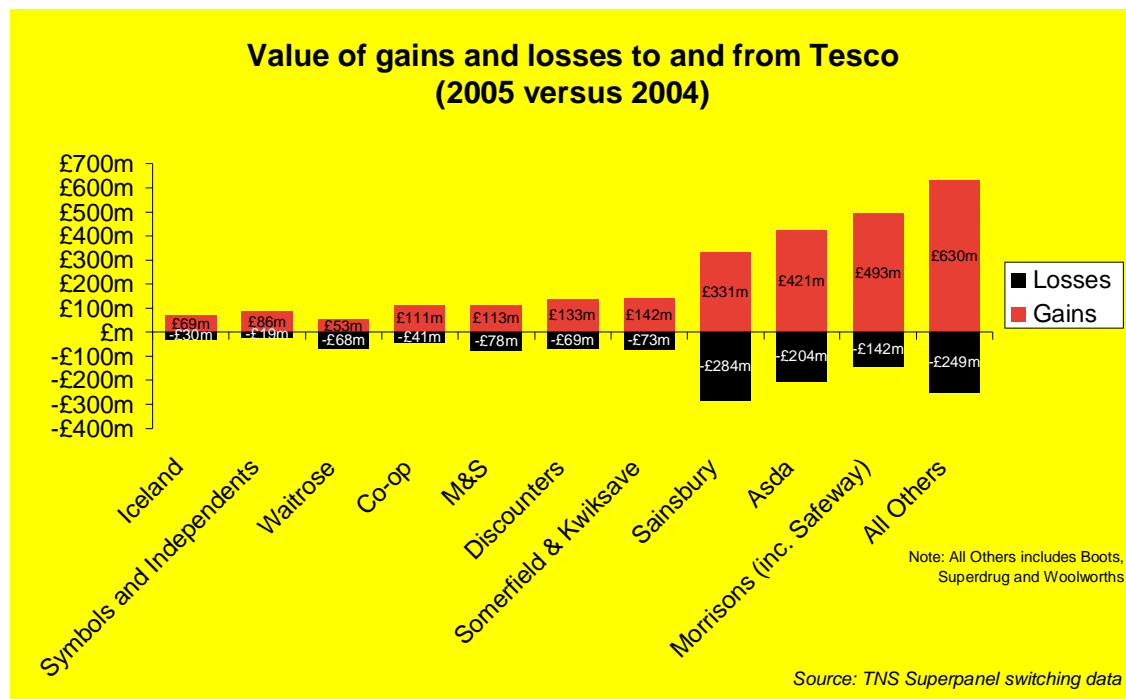
<sup>4</sup> Société Générale, 2006.

consumer expectations within the evolving regulatory and cultural framework in which they operate.”<sup>5</sup>

### Grocery consumers shop at many stores and switch between them readily

4.2 There is an enormous amount of data in the public domain about how and why customers do their grocery shopping. One of the most striking features of this data is the extent of customer switching between retailers in the grocery market. In essence, they have a wide variety of retailing options, and exercise choice continuously. Market share changes are the net result, in every case, of gains and losses of customers. In *Safeway* the CC saw that although Safeway gained business from major rivals it lost far more than it gained, thus contributing to the fall in its sales and profits. We, by contrast, have in recent years gained more than we have lost, thus our increase in market share. However, our performance against each of our rivals is not uniform.

4.3 The table below shows the value of gains and losses for Tesco over the period 2004 to 2005: our competitors include (from left to right in the table) Iceland, Symbols and independents, Waitrose, Total Co-Op, Marks & Spencer, Aldi, Lidl, Netto, Somerfield/KwikSave, Sainsbury, Asda, Morrisons/Safeway and All Others (a grouping that contains retailers such as Boots, Superdrug, Woolworths, Farm Foods, and independents).



4.4 To understand the real impact of our competitors, one needs to adjust for their relative size, i.e. the fact that many of them occupy less retail space across the country than Tesco. Comparing like-for-like, Waitrose and Marks & Spencer are *as effective*

<sup>5</sup> *Economic Note on UK Grocery Retailing* produced by Food and Drink Economics branch, Defra, May 2006.

competitors as Sainsbury and Morrison when consumers have the opportunity to choose between them in areas where Tesco is a competitor. Other retailers are also more competitive on a like-for-like basis than is suggested on the basis of the unadjusted data.

4.5 We can see from these data that consumers who shop at Tesco also shop at many other stores, that they exercise preferences as between different grocery retailers, that competition to Tesco is not limited to the three largest supermarkets and that retailers who do not give consumers what they want get fewer consumers into their stores.

### **The battle for market share and profitability**

*Competitive rivalry is continuous and no retailer can afford to rest on its laurels*

4.6 There is a large number of significant players in the market, with diverse product and different business strategies on each of the components of the PQRS offer. These features of the grocery market lend themselves to continuous rivalry, in which no established position can be regarded as secure.

4.7 We show in paragraphs 5.1 *et seq* below the effect of competitive rivalry on consumer benefit, across a range of performance measures, including lower prices, better quality and range, better service to the consumer and a substantial choice of where and when to shop. In this section we look at the relative success and failure of some of the larger operators. The market continues to change radically but the basic criteria for success or failure remain. They apply as much to us as to anybody else regardless of our current size. Customers will continue to reward those that meet their expectations better and punish those that do not.

4.8 **Wal-Mart/Asda:** In the early 1990s, for example, Asda came close to collapse. This was averted in 1991 only by a rescue rights issue and the replacement of the senior management team. Yet within two years Asda was opening new stores again, and by 1995 had been sufficiently successful in regaining customer and investor confidence that it was able to start expanding again on a significant scale. In 1999 it was bought by Wal-Mart Inc. for £6.7 billion and is now expanding rapidly with a large new store programme, the introduction of mezzanines into many stores, and the launching of “Essentials”, its new small-footprint format.

4.9 **Sainsbury:** It has been well-documented that Sainsbury has experienced difficulties over the past five years. In particular, the introduction of a new distribution system during 2002/03 led to severe availability problems – customers simply could not get what they wanted. Similarly, on property, CEO Justin King, stated in May of this year that “*Sainsbury was effectively out of the market for ten years*” and that “*growth ground to a halt*”. But these problems appear to have been resolved and we expect to face even fiercer competition from Sainsbury in the future. Sainsbury has taken a number of initiatives to improve its offer since 2000. It has invested in lower prices, backed by an aggressive advertising campaign (“1,000s of low prices”), introduced several new ranges (such as “Basics”, “Taste the Difference” and “Be Good to Yourself”) and Nectar, its loyalty card, improved availability and developed its portfolio of convenience stores, “Sainsbury’s Local”. Between 2004

and 2005, its share started to increase for the first time in six years, and Investec has recently stated that, “*We believe Sainsbury’s recovery poses the most significant threat to Tesco*”.<sup>6</sup>

**4.10 Discounters:** Recent years have also seen a dramatic growth in Aldi, Lidl and Netto. In Germany, local supermarkets, including Aldi and Lidl, have just forced Wal-Mart to exit the German grocery market. They, and Netto, the Danish group, are well-established international companies with strong track records and plans to expand their presence in the UK. They have taken customers from us and from other competitors and achieved significant market share growth by:

- (a) expanding their range of products significantly to offer more fresh and more branded products than before;
- (b) maintaining their policy of very low prices on key products; and
- (c) growing their number of stores. Aldi and Lidl are expected to increase the number of their stores from 700 today to around 1,100 in the next four years.

Allegra Strategies praise Aldi and Lidl as “*two of retail’s most unsung, but quietly emerging, stars*” in their 2006 report “UK Retail Stars”.

**4.11 Safeway/Morrison:** Safeway provides a remarkable illustration of the effect of competitive rivalry on a business which, by 2003, had plainly lost its way and was losing customers to all its rivals. The CC found in *Safeway* that it was acting as an effective constraint on the businesses of its major rivals. Nevertheless Safeway had concluded that it was in the best interests of its shareholders to sell the business. Safeway was acquired by Morrison, which had a very strong price and availability offer. It has not been an easy process to convert Safeway to Morrison. It has taken perhaps longer than it should have done to bring about a successful acquisition. But the corner appears to have been turned, and market confidence in Morrison is rising. Our Competitor Pulse and Image and Advertising surveys show that customers have noticed an improvement in Morrison’s performance. A recent Financial Times article (August 4th 2006), entitled “*Morrison leaves its troubles behind*”, reported that “[*Morrison*] delivered its best trading figures in more than two years...”, and quoted its outgoing chief executive as saying “*This is the best performance since the Safeway acquisition in terms of sales.*” And it has realised substantial cash for expansion in its business from a successful divestment programme.

**4.12 Tesco:** At one point in the early 1990s Sainsbury’s market capitalisation was two and a half times that of Tesco. We were seen by analysts as occupying a fatally weak position in grocery retailing: not competitive on price with Asda and others; not competitive on quality with Sainsbury. We had been hit hard by the recession. Something had to be done to revitalise and refocus the business. That led to the strategy of offering better value for money, which helped turn the business round. By 1995, an exceptionally short time, we had become market leader - a position which by continuing to offer customers what they want we have retained. In addition we took a

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<sup>6</sup> Investec Securities, 2006.

calculated risk in our land acquisition programme during the 1990's when our future in the market was being seriously affected by our perceived weakness as against Asda and Sainsbury. The economy was weak – and others flinched from exposing their investors to the risks of investment in commercial retail property. Because we also got our competitive offer right, we were able to offer our products to more customers as economic conditions improved.

4.13 But we can never relax. Competition remains strong and, if we get things wrong, we will rapidly lose ground to our competitors. For example, in 2002/03 we introduced a new continuous replenishment system. The introduction did not go well, and resulted in availability problems in our stores, which in turn led to a large number of our customers switching to other retailers. Since then we have striven to improve availability and continue to do so, and over time have succeeded in reducing the number of customers switching away from us due to poor availability.

4.14 The common feature of all these examples from the past is that success and failure can come very rapidly – and that mistakes can be rectified. If they are not, the effect can be seriously adverse on profitability, which can lead to a failure to invest for the future – including investing in people. In particular, to stop listening to the messages from customers is a recipe for failure. All supermarkets have their own policies on how to improve their competitive position. Waitrose, Marks & Spencer, Sainsbury, Aldi, Lidl and Netto, to take six of the many companies in rivalry with Tesco, are currently showing how customers can be won so as to increase their performance.

4.15 The market is huge and the prospects of financial reward considerable for those that succeed - but to sit back and assume that the world will come to you does not work. The OFT has referred to a growth in national concentration and a concern about local concentration in some areas, as if that in some way blunted competitive rivalry and reduced consumer choice. But the evidence goes the other way. It shows how many firms change and adapt their policies to improve their competitiveness. Tesco and Sainsbury (as well as Musgrave, a new entrant from Ireland, through its acquisition of Budgens and Londis) have stimulated the convenience sector of the market, which is growing faster than the market as a whole. Other retailers grasp the opportunities to compete in that format and other formats. It is simply not credible to put Tesco and a small number of other retailers into a box called “one-stop shopping” and assume that nothing that goes on outside that box has any impact on us; or to put those retailers into a market called secondary shopping and conclude there is asymmetric competition between them and those operating smaller stores. The reality of customer behaviour is more diverse and complex – retailers that respond well to that uncertainty thrive and those that do not will be punished by customers.

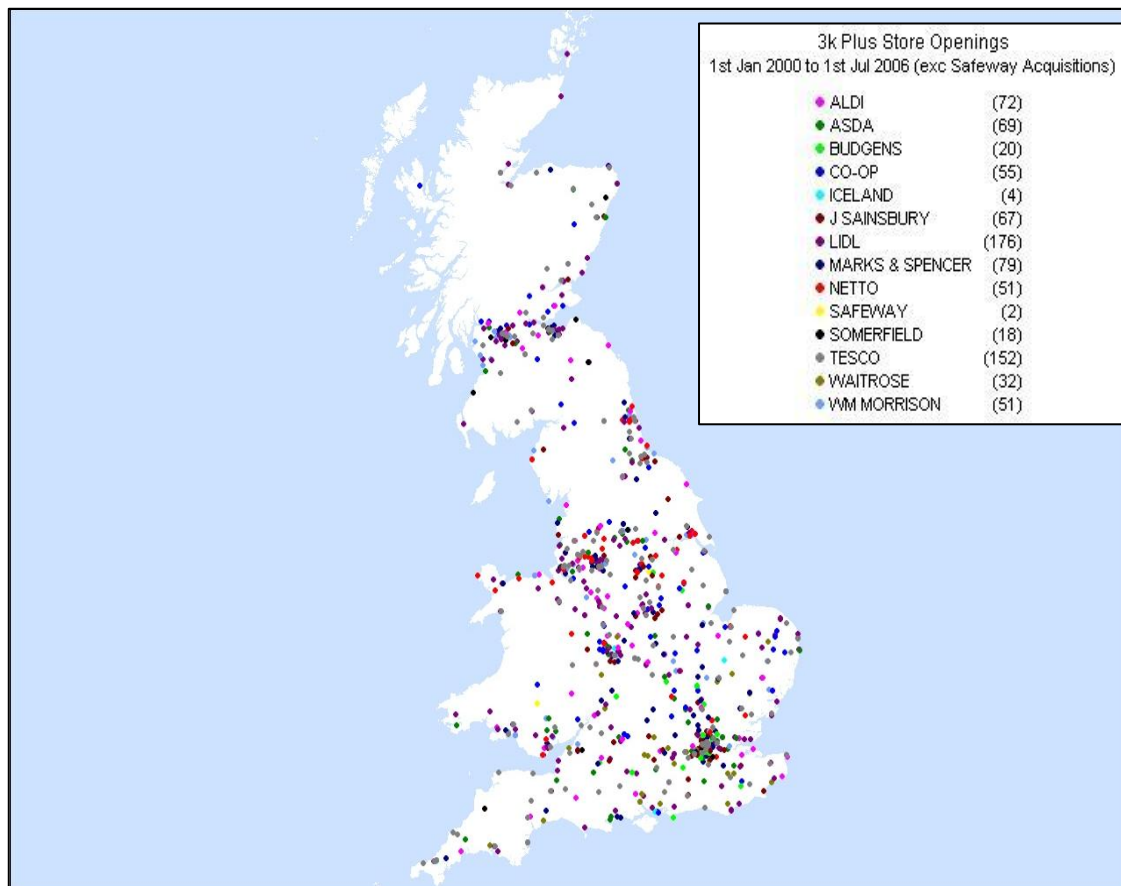
### **New entry and expansion**

*There is good evidence of both new entry and expansion right across the market*

4.16 The effect of new entry and expansion is to bring more competition from more retailers into more locations. The issue of local concentration is not in our view material having regard to the availability of choice in almost every area of the country

and the prospect of new entry were any such local advantage to be exploited against the consumer.

4.17 Existing competitors are significantly expanding their operations, as illustrated in the map below, which shows stores gained in GB by the retailers listed since 2000.



4.18 There is also a significant amount of new entry by smaller retailers, including the growth of farm shops and farmers' markets, all of which add to the competitive mix and the dynamic rivalry that we face. Other new forms of entry occur such as that by Whole Foods, an organic grocery retailer from the US, which is to open its first UK store in 2007.

4.19 In other words, customers have a significant level of choice available to them. Independent market research by Warwick University shows that 93 per cent of customers in Great Britain have a local choice of three or more different supermarket fascias. Our own research in 2006 shows that the figure is now 94 per cent rather than 93 per cent, and that 90 per cent of the population have access to five or more stores greater than 3,000 square feet within 15 minutes of their homes. Additionally, as part of our work with the OFT prior to the reference, we conducted some small-scale consumer satisfaction surveys in places alleged to have high Tesco local concentration. These demonstrated that satisfaction levels in these areas were the same as our national averages, which leads to the conclusion that there is no consumer detriment in areas where Tesco was thought to have a relatively strong local position.

## 5. CONSUMER BENEFITS

5.1 This competitive activity and innovation has generated huge benefits for UK customers and the economy more generally.

5.2 Prices have fallen dramatically as a result of the intense competitive rivalry at the retail level. Grocery deflation over the past three years will have saved UK consumers more than £3 billion by the end of 2006. Based on ONS data, the OFT estimated that real prices for food fell by 7.3 per cent between January 2000 and December 2005, as illustrated in figure 4.6 in the OFT's reason for referral. Although currently somewhat affected by very high energy prices, we continue to seek to deliver lower prices for consumers.

**Figure 4.6: Trend in real food prices since 2000**



Source: OFT calculations based on ONS RPI data

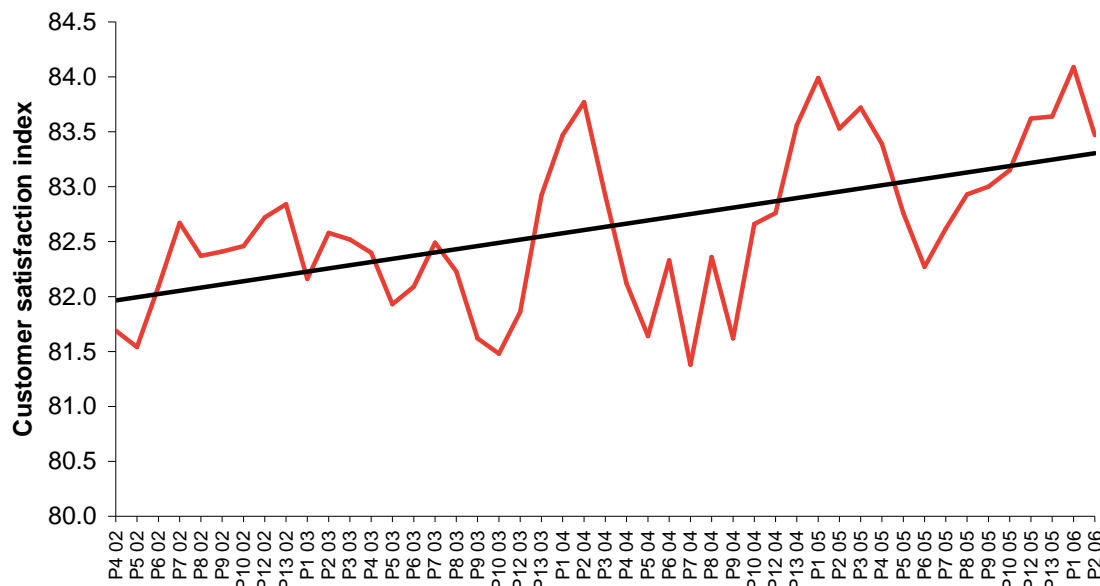
5.3 Last year alone, we reduced our prices by 1.8 per cent in real terms. For a sustained period our prices have fallen faster than food prices as a whole and faster than RPI. Overall Tesco's prices have fallen by 15 per cent in real terms since 2000.

5.4 It is not only prices that have been improving – consumers have witnessed improvements and are experiencing increased satisfaction across all aspects of PQRS. In our Competitor Pulse survey, 85 per cent of customers of Tesco, Wal-Mart/Asda, Morrison, Sainsbury and the discounters rated their shopping experience as either excellent or good.

5.5 The OFT found that over the past five years the range of products stocked by the four largest supermarkets in their larger stores has increased by 40 per cent to 41,500 products – a dramatic increase. Our Competitor Pulse survey suggested that 95 per cent of those surveyed agreed that there was a good range to suit their budget, and 84 per cent of shoppers were able to buy everything that they went for. In the last

year, we alone added 350 new suppliers and thousands of new products, and the satisfaction of our customers with our range continues to rise.

### Index of customer satisfaction with range



Source: Tesco

5.6 The additional products now being offered provide excellent value for money. The OFT noted that there is evidence that consumers may increasingly value the quality of product over pure competition on price, and that concerns about healthy eating and buying local produce has meant that butchers, bakers, fishmongers, greengrocers, market stalls and farm shops were trading more successfully in 2005 than in any year since 2000. It reported that over the last year independent retailers experienced a 43 per cent growth in sales of organic goods.

5.7 In addition to independent stores, larger retailers, including Tesco, have also successfully responded to this changing consumer demand. Sainsbury has announced that it expects its sales of healthy eating products to account for 40 per cent of sales within two years. Over the last year we have broadened all our organic food ranges and increased our organic food sales by 26 per cent, on top of already strong growth in previous years. We have introduced new quality ranges, such as our Wholefoods range, and improved our food product offer in other ways, such as through our nutritional labelling and by introducing our 'Free from' range to make shopping easier for those with allergies and intolerances.

5.8 As for service, the OFT recognised that the evidence before it suggested that consumers have come to expect more from their local store, and that store amenities have improved over the last five years. Our data tells the same story. Further, our Competitor Pulse survey indicates that, during 2005, 87 per cent of those surveyed found the time waiting at a checkout to be acceptable or very good, and 93 per cent of shoppers agreed that it was easy to find the products and services they wanted.

5.9 In relation to retail competition, these innovations, driven by intense rivalry, result in the high standards and improvements across the broad retail market, discussed above. Consequently, we believe that the CC should conclude in this Inquiry as its predecessor did in 2000, namely that:<sup>7</sup>

*“The key point is that, albeit within some perfectly intelligible constraints, supermarkets were competing to meet the demands of consumers, demands which have changed hugely in the last two or three decades as a result of changing work patterns, mobility, use of time, preferences and incomes. As the very detailed surveys which we carried out demonstrated, this has met with overwhelming consumer approval. Not all was perfect... but in relation to what is for consumers their single biggest weekly item of expenditure, competition has been hugely successful.”*

## **6. TESCO’S STRATEGY**

### **Strategy for growth depends on focus on customers**

6.1 Our core purpose is “to create value for customers to earn their lifetime loyalty”. This underpins a well-established and consistent strategy for growth introduced in 1997. The strategy for growth covers four areas, each of which is being implemented against substantial competitive rivalry: grocery retailing in the United Kingdom; international; non-foods; and retailing services. In none of those areas, least of all its core grocery business in the UK, does Tesco rest on its laurels.

6.2 We are governed by our adherence to two key values, which are embedded in the business and are carried through into detailed plans and policies. The first is that “no one tries harder for customers”. When the CC reads our detailed response it may conclude that we are obsessed with the subject and ask whether the detail really is essential. We mean what we say and put it into practice every day of the year, aiming to get it right for every shopper in the country. The second is “treat people how we like to be treated”. Again that is without meaning and substance unless practised: it is seen in practice in the best pay and benefits in the sector, training and development programmes for our people, our involvement in the community, working in partnership with our suppliers and in how we treat our customers.

### **Diversity of customer base requires detailed understanding of what the market wants**

6.3 Probably the biggest difference between Tesco and its competitors in recent years has been this sharp focus on the customer. This focus drives the business. Much of the time of our Chief Executive is spent in stores, talking to staff and customers, and that commitment is pervasive throughout the business, with all head office senior and middle management spending a week in stores (Tesco Week in Store, or “TWIST”) every year. Customer information is used to provide the necessary insight on which all decisions can be taken. This enables us to assess our

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<sup>7</sup> Quotation from a speech given in 2002 by Sir Derek Morris, the former Chairman of the CC and the Chairman of the panel in the 2000 Inquiry.

risk in the development of major strategies, such as moving into new markets. Crucially, this focus on the consumer enables us also to develop the hundreds of innovations, both small and large, that keep us ahead of our rivals – be they in product specification, distribution, design and refit of stores, staff training, or operating processes in store.

### **Continuous improvement and innovation**

6.4 At Tesco, everyone looks for ways to do things “*better, simpler and cheaper*” for customers and staff. We typically improve not through large eye-catching initiatives, but by continuous focus on delivery through many small improvements. One example is to use reusable plastic crates to replace cardboard boxes and other packaging. This may not sound much, but it has been adopted widely in the international supply chain. There are a host of other innovations every year, each of which improves our customer offer and/or contributes to greater efficiency - savings that are passed on to our customers. These include the variety of own brand ranges for different customer needs; the efficient time-and-motion innovations at our distribution centres; and the introduction of self-scan checkouts and larger continuous conveyor belts to improve packing speed at the checkout. These are not huge changes but, along with thousands of others amount to a significant ongoing process of innovation that delivers what our customers want.

### **The Every Little Helps (ELH) Shopping Trip**

6.5 “Every Little Helps” is far more than an advertisement. We use it to describe what we understand customers want from their shopping trip and businesses that deliver this well will benefit, while businesses that fail will struggle. ELH is five very simple promises. Our business makes sure that the promises are kept. They are:

- (a) Prices are good
- (b) I can get what I want
- (c) The aisles are clear
- (d) I don’t queue
- (e) The staff are great

6.6 Those simple promises then demand an extraordinary amount of dedication and attention to detail to deliver them day after day for millions of different customers with different needs in different locations. The promise that the “prices are good” means that Tesco will be the best value for money retailer. There is a national basket monitored regularly across the market. The promise that “I can get what I want” requires highly efficient stock replacement and a widening range of products to suit the tastes and pockets of its diverse range of customers. The promises that “the aisles are clear” and “I don’t queue” require an enormous amount of detailed logistical and store planning effort in order to match store capacity and layout to demand. The promise that “staff are great” connects back to our values that we must “treat people as we would want to be treated”.

## **Tesco's relationships with staff and communities**

6.7 In order to implement our strategy, we recognise the importance of building good, sustainable relationships in order to earn the lifetime loyalty of our customers – our suppliers and employees. Our supplier relationships are discussed in more detail below. In respect of employees, we have a longstanding partnership with the trade union USDAW and an unparalleled commitment to training and personal development.

6.8 The introduction of “Community” into our Steering Wheel puts the community, corporate responsibility and sustainability at the heart of our business plan and decision-making process. The confines of a market investigation under the Act do not represent the best forum for an exploration of matters of broader societal and public concern. Nonetheless, we take these broader concerns seriously and act on them as the CC has seen.<sup>8</sup> Further details of our work in this area can be found in our Corporate Responsibility Review 2006.<sup>9</sup>

## **7. RETAIL COMPETITION ISSUES**

7.1 The CC's issues under the heading of Retail Competition are to be found at paragraphs 12-25 of the Issues Statement and follow the headings of: (i) market definition; (ii) market concentration; and (iii) other aspects of competition in the market, including below cost pricing and price flexing, identified by the OFT as practices that may be anticompetitive within the meaning of the Act.

7.2 Many of the general issues referred to in this part of the Issues Statement have already been discussed above, in particular market definition, the degree of competitive rivalry within the market and the consumer benefits resulting from it. In the following sections we address only those relating to market concentration and pricing practices.

### **Market concentration (paragraphs 17-19)**

#### *Cause and effect generally*

7.3 The increase in *national* concentration since 2000 is the direct result of normal market evolution in an extraordinarily demanding and growing consumer market. The reasons for the increase are the Morrison acquisition of Safeway and the growth in our market share in response to customer demand. Neither reason was anticompetitive. The CC concluded that Morrison's ownership of the struggling Safeway (a position directly attributable to market forces) would produce four major supermarkets in direct competition with each other nationally. In other words, that increase in concentration was intended to be pro-competitive to the benefit of consumers. Having initially had difficulty with integration, Morrison now appears to have turned the corner in the management of the enlarged business, measured in part by increased like for like sales growth. Our increase in market share relative to our

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<sup>8</sup> For example, on the CC's site visit to one of our Regeneration Partnership Schemes.

<sup>9</sup> Submitted in response to the off-the-shelf request.

“nearest” rivals (ranked in terms of national market share) is attributable entirely to our pro-competitive policies. Those are the two single most important *causes* of the increase in concentration observed by the OFT and do not suggest that the market is becoming less competitive at a time when all the evidence points the other way.

7.4 Generalised statistics on movements in market share as between the largest supermarkets conceal the facts about increasing rivalry more generally and in particular in more local areas as a result of entry and expansion by many of those outside the big four. Waitrose, Marks & Spencer, Aldi, Lidl and Netto, and others are all showing how they can compete effectively, as illustrated by the table at paragraph 4.3 above and the discussion of store openings at paragraph 9.11 below. The increase in national concentration therefore has to be taken in its proper context.

#### *Local market concentration*

7.5 This issue is about reduced fascia choice for some consumers in some areas of the country, compared with the increased choice they would have were they to live in other areas, rural or urban. It is important to place this issue in its appropriate context. As described at paragraphs 1.9 and 4.19 above, research shows that 94 per cent of customers in Great Britain have a local choice of three or more different supermarket fascias available to them. In addition, while we do not agree with the postcode methodology employed by the CC in 2000, we have revisited the 53 postcode areas where Tesco was found to have a share of more than 25 per cent. In 98 per cent of the areas, at least one competitor has opened a new store since January 2001, and in 70 per cent of the postcode areas three or more competitors have opened new stores.

7.6 Retailers’ decisions to select the area in which they locate and the existence of local concentration is the result of the normal evolution of market forces. Equally, local concentration can be the result of historical decisions to locate in small areas of population. Due to the lack of demand, additional investment would be uneconomic. Where new investment might be regarded as inefficient and non-profit maximising, local concentration cannot be within the scope of the Act as an anticompetitive feature. Local concentration could also be a result of local planning decisions.

7.7 In any event, for the reasons described in greater detail at paragraph 3.8 above, competitive conditions in local areas are not determined solely by local considerations. Many important aspects of competition in the grocery retail market are determined at the national level, and various other factors, including chains of substitution, suggest a broader definition of the geographic market than the CC has previously adopted. Any analysis of competition in local areas that fails to take account of these reasons will not reflect the realities of competition in this market.

#### *Concentration in the convenience store sector*

7.8 We believe that the convenience sector is at one end of the continuum that makes up grocery retailing more generally. Even if it were to be considered as a separate market, concentration within the “convenience store sector” is a non-issue. Supermarket entry by Sainsbury and ourselves leaves us and other participants such as the Co-op, Musgrave (an efficient Irish operator, which has purchased Budgens and Londis) and Spar with shares of this sector well below any level that might give rise

to a concentration concern. Supermarket entry in this segment has been demonstrably pro-competitive and the exercise of buyer power has not been exclusionary. The IGD noted in 2005 that “*market growth over the next five years is likely to be between 4.5 per cent and 7 per cent annually, comfortably outperforming the mainstream grocery market*”<sup>10</sup>. Neither our entry into the convenience sector nor the existence of the Tesco supply chain can be expected to have effects that are adverse to competition in the grocery market generally or in this sector.

7.9 It appears to be recognised on all sides that sites for convenience stores are readily available and format changes for acquired stores can readily be addressed to the satisfaction of local authorities. Verdict Research has stated that the move by Tesco and Sainsbury into convenience stores has raised competition and retail standards, bringing to local neighbourhoods fresher foods, new ranges, lower prices, better store environments and increased scale, and has forced smaller players to improve to keep up.

### **Other aspects of competition in the market (paragraphs 20-25)**

7.10 Paragraphs 20-21 of the Issues Statement cover how the processes of competition work to meet consumer demands for grocery and non grocery products. We discussed this at length above. In this section therefore we concentrate on the issues of price flexing and below cost pricing, and in particular consider whether these have detrimental effects on customers.

### **Price flexing (paragraph 23)**

#### *General considerations*

7.11 The issues raised by the CC in paragraph 23 cover, first, the *facts* about price flexing - does it happen locally and has it changed since 2000? Second, *expectations* - is it going to change as a result of changed local market conditions? Third, *causes* - is it determined by local concentration and/or local conditions of competition? Fourth, *effects* - is there evidence of predatory intent or effect in any local price flexing practices?

#### *Tesco price flexing: the facts*

7.12 We sell all our products on the basis of a national price list available for all to see on our website. It is not our policy to vary prices by reference to location. Our Express stores (and 18 of our Metro stores) are on a separate national price list under which they sell products at an average of 2 to 3 per cent higher prices than our other stores because of higher costs.

7.13 The OFT raised some points related to price flexing in the form of local voucher promotions - in other words, not price flexing as it was considered by the CC in 2000.

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<sup>10</sup> *Convenience Retailing 2005, Annual Report, IGD.*

7.14 To a very limited extent, Tesco does engage in promotional activity, generally connected with the opening of a new store or the opening or refurbishing of a competitor's store, but these are limited in duration and have no appreciable effect on competitive strengths in local areas. Of our total in-store product-related marketing spend, 99 per cent is national.

7.15 Meeting competition in local areas, by adjusting price or other aspects of PQRS, as new entry offers more choice, is ordinarily thought of as a normal, sensible business reaction. Indeed, the OFT also offered its own view that "*in some circumstances, local price competition, where there is no predatory behaviour arising from the abuse of a dominant position in an area, could benefit rather than harm consumers – that is, the existence of price flexing could be a characteristic of a well functioning market*".

7.16 In respect of one voucher case cited by the OFT, a complaint from a supermarket owner in Withernsea, the OFT examined whether Tesco's actions constituted predatory pricing and abuse of a dominant position but said that the evidence was not persuasive. More generally, the OFT found no conclusive evidence that any competitors have been driven out of the market as a result of any form of price flexing, including through voucher promotions.

7.17 In our view the above statement of the OFT at paragraph 7.15 is right. We believe that consumers benefit when, as happens, Tesco is targeted by Lidl with a promotional half price offer on produce in neighbouring stores, and Tesco responds. It is also fair and reasonable for us to respond.

#### **Below cost pricing (paragraph 24)**

7.18 As we demonstrate in our detailed response to the CC, we believe that the practice constitutes only a very small proportion of sales. In fact, over the last 18 months, they represented approximately 1/500 of our sales. To the extent that they do occur, they are simply a by-product of intense competitive rivalry. There is significant dynamism in grocery pricing, with prices changing on a weekly, and sometimes daily basis, depending on, for example, market conditions, availability and competitor price moves. Against this backdrop it is not surprising that products are occasionally sold below cost. This should not be a concern, as the effect is to confer a benefit on all our customers throughout the UK. Competition here is seen to bring down profitability of operators in a competitive market to the benefit of consumers.

7.19 This activity is not targeted at convenience operators, and any effects on smaller retailers are minimal. First because of the limited extent of the practice itself. Second because smaller retailers compete with larger retailers across all aspects of PQRS (including, for example, in relation to convenience) and small variations in price are highly unlikely to have a material effect on their relative competitive positions.

7.20 Looking further ahead in the Inquiry, the CC will recall the difficulties in fashioning any remedy for below cost pricing that is manageable and beneficial to customers, and the difficulties that have resulted for example in Ireland and France where the imposition of such a remedy has been attempted. The OFT itself points out

that other retailers may also engage in below cost selling - and thus a remedy limited to the major retailers would be discriminatory and unreasonable.

### **Other policies (paragraph 25)**

7.21 The CC asks whether those practices are specific examples of any more general policy of price discrimination. There is no such general policy and thus no effect on the viability of retailers.

## **8. SUPPLY CHAIN ISSUES**

8.1 The CC sets out at paragraphs 10 and 11 of the Issues Statement matters relating to the supply chain, which turn on the effects on *upstream* and *downstream* markets (including those for non grocery products) on the *behaviour* of grocery retailers towards their suppliers. The CC observes that the behaviour of multiple retailers, including the exercise of buyer power, was considered in detail in the CC Report in 2000, one consequence of which was the establishment of the Supermarkets' Code of Practice (the *Code*). The matter was also considered at length in *Safeway* and referred to briefly in *Somerfield* in terms of possible effects of increased concentration on the ability of retailers with high market share to use their buying power to reduce availability, diversity and quality of products available to consumers.

8.2 We believe that the CC's decision in 2000 rested, in our view sensibly, on the premise that where the retail market is functioning effectively it is most unlikely that retailers would use buyer power to damage the competitive market structure of the supply chain on which they are dependent.

8.3 Using the supply chain so that it *is* competitive and efficient is part of our efforts to improve our own competitive position. In other words, it is entirely normal and rational behaviour for us to engage in. We do not wish to be wholly dependent upon the large multinational suppliers of global brands. We aim for choice for our customers – because that is what they demand. And we want to buy at competitive prices. So, as we show below, we transmit competitive pressures throughout the supply chain, not just to find new and better products, but also to improve the efficiency of our suppliers, thereby reducing costs and driving out inefficiencies and excess profit from the supply chain – gains which the competitiveness of the retail market means must be passed on. As a result we benefit, our customers benefit, and our suppliers benefit, by themselves becoming more competitive – we believe that the UK grocery supply base is one of the most efficient and effective in the world.

8.4 The issues set out by the CC appear to suggest that these benefits may come at a cost to some suppliers, some retailers with less buyer power – and ultimately to the consumer. But all the evidence before the CC in earlier inquiries has pointed in one direction: that the benefits are consistent with sustainable profitability and investment at all levels of the supply chain; that suppliers do not raise price to the retailers without buyer power as a result of conceding lower prices to the retailers with buyer power and are not themselves rendered unviable through the bargaining process. Indeed, it is simply not in our interest to damage our supply chain, as this would be detrimental to our ability to get the best value products for customers into our shops.

Even if there were any detrimental effects resulting from buyer power, the undoubted competitiveness of the downstream retail market suggests there would be no consumer detriment.

8.5 One recent development, which - it was suggested - might tip the balance against the consumer was the move by large retailers into the convenience end of the market. But the evidence shows what is entirely to be expected – competition was stimulated by a dynamic and positive reaction by the incumbents to new entry, with continuing benefits to consumers.

### **Good supplier relationships are critical to the success of our business**

8.6 We seek to ensure that our relationships with suppliers are underpinned by our Values. We operate our entire business, be it with customers, staff, suppliers or stakeholders on the basis of “*treating people as we would wish to be treated*”. This extends to all our supply base and we do not just talk about it - we have introduced an annual supplier Viewpoint Survey to help us to identify and act upon supplier concerns.

8.7 We seek to build long term relationships with all our suppliers as a stable supply base provides us with the best chance of meeting our customers’ expectations. Both parties invest a lot of time and effort in building capability and volume, and it is in the interests of neither party for there to be a lot of short-term movement – there are many examples where we stick with suppliers through some short-term difficulty.

8.8 The innovation and flexibility of our suppliers have been major factors in our growth. Treating suppliers badly cannot possibly be within our own commercial interests as that would undermine the source of our product offering and lead ultimately to poor relationships, a smaller and less capable supply base, poorer ranges and the loss of customers.

8.9 Therefore, when we negotiate with suppliers we are firm but fair. Our buyers expect a fair price for the volume of product that we are able to buy from a supplier. We expect the cost price that we agree with our suppliers to reflect a number of elements, including production costs, the uniqueness of the product, the import costs, the volume that we order and the costs of distribution. When we purchase larger volumes, we expect to agree lower unit costs to reflect any economies of scale that might result in the production of the product, and pass on the benefits to our customers.

8.10 It has been argued that the substantial buying power of the largest supermarkets, and Tesco in particular acts against the public interest. Of course, we accept that the fact that we are the UK’s largest retailer gives us additional strength compared to smaller chains or convenience stores. However, we do not think that this effect is especially material in relation to larger retailers - scale alone is insufficient to guarantee success, and it is only skilful retailers that are capable of negotiating the best deals with suppliers, taking costs out of the supply chain and maximising their own efficiency. The theory that scale inevitably leads to competitive success is inconsistent with the fact that Waitrose is currently growing faster than Asda, its larger rival. Nor is it compatible with the fact that the most profitable operator in the

sector for a period of ten years was Morrisons, smaller than its major rivals, until it became larger by acquiring Safeway, when its profitability dropped.

8.11 Where we do have relative buyer power, we use it responsibly in connection with the supply chain. With such a competitive market downstream it is no surprise that we continue (as the CC has previously recognised) to pass benefits in the form of lower prices promptly to our customers, who benefit enormously from the consequences of competition at the retail level. Whilst in recent years we have grown our sales, our operating margin has remained around 6 per cent.

### **Impact on suppliers and wholesalers (paragraphs 10(a) and (b))**

8.12 We believe that the facts point wholly in the direction of the existence of a flourishing and competitive supply chain. The behaviour of grocery retailers towards their suppliers affects retail competition, and positively. In other words, the market functions effectively in the sense of providing the outputs expected of such a market - competitive price levels that encourage investment and innovation and result in new products and services, greater quality, lower prices and a wider range.

8.13 The CC will consider evidence showing that retailer-supplier relationships have helped:

- (a) achieve competitive prices;
- (b) improve quantity and range of product;
- (c) increase levels of investment and innovation; and
- (d) maintain the economic viability of the supply chain.

Without these elements, we believe that it is impossible successfully to carry out a grocery retailing business, as the products provided by our supply chain are at the heart of what we do.

8.14 One of the main themes running through this response to the Issues Statement is that the facts come first. This Inquiry has begun without any evidence produced by the OFT to suggest that the behaviour of grocery retailers has had *any* adverse effect on the competitiveness of the supply chain. That is hardly surprising. The first to complain about the lack of competition, choice, investment, innovation, risk taking in the supply chain would be their customers, the retailers. We have no such complaint – our concern is to establish a supply chain which is competitive and has the incentive to compete in the market through innovation and investment.

### *Tesco's objectives in respect of its supply chain*

8.15 We aim, through a continuing dialogue with our suppliers, to ensure that our supply chain has the following characteristics.

- (a) **Choice:** we have to provide our customers with a wide choice of product from local, regional, national and international suppliers. It is not in our interests to

restrict the number of suppliers capable of providing this product – so we wish to have the advantages of competition and competitive prices across a wide product range, sourced from the most competitive suppliers.

- (b) **Innovation:** without innovation from our suppliers, both as to product and to process, we cannot provide the range of cutting-edge products to our customers at the low prices they demand. We must constantly source new and innovative, value-added products from new and existing suppliers worldwide. We aim to encourage new entry and sustain existing sources, motivated to engage in the search for such products.
- (c) **Growth:** to meet increased demand for Tesco products our supply chain must also be capable of sustaining that growth and investing accordingly.
- (d) **Dynamism:** our supply chain must be capable of taking risk in meeting more efficiently the changing demands of the market, working with us to bring in ideas that will translate into mutual and beneficial growth.
- (e) **Quality and technical safety:** this essential characteristic depends in part upon suppliers' sense of security in terms of continuity of business with Tesco, such that they are willing to make and sustain the appropriate investments, derived from increased awareness of the importance of safety, supported by a strong regulatory framework.

These are not characteristics that a supplier has to demonstrate only once in order to be acceptable to us. Quite the opposite - these are requirements that must consistently be demonstrated by suppliers in order to provide a uniform offering. The rigours of competitive rivalry demand that we have continuity of supply, and this is why we favour the establishment of long-term relationships, rather than seeking short-term “wins” such as low prices, where the supplier in question is not otherwise up to our high standards.

8.16 Moving from the general to the more specific, the demands placed on us by our customers are reflected in the demands placed on our supply chain by us. Any product we sell must meet five basic criteria:

- (a) it is something that customers want;
- (b) it must be sold at a competitive price;
- (c) it satisfies quality and health and safety and other qualitative requirements;
- (d) it satisfies distribution requirements; and
- (e) it contributes to the Tesco brand.

8.17 The supply chain is a tough and demanding market place. Just as Tesco has to be responsive to customer demands, so must the suppliers. Pressures on suppliers come from customers, from the suppliers' search for efficiency and innovation and from changes in world markets and farming, as well as from retailers. It is clear that

some suppliers are better than others at responding to these pressures. Subject to those considerations we expect the evidence clearly to show that there is a healthy supply chain.

8.18 We believe that the evidence will show in particular that we and our suppliers have succeeded in ensuring that the competitive characteristics detailed above are prevalent in the supply chain. There are no symptoms of what may be expected where the market does not function effectively, namely: prices forced down to uncompetitive and unsustainable levels; lack of product availability or choice; lack of investment; or lack of sufficient profits to reinvest for the future. On the contrary, suppliers and their customers are constantly benefiting from the innovations and greater efficiencies derived from working with world class retailers. We speak from experience. Our relationships with suppliers may in some cases from time to time have their tensions, but – on the small number of occasions on which they arise - we aim to resolve them constructively through discussions. And this healthy tension tells us that we are not leaving any stone unturned when looking to improve innovation and efficiency and pass the benefits on to the consumer. All of this is normal pro-competitive conduct, and demonstrates the mutually beneficial relationships that we seek to achieve with suppliers (what we call “win-wins”).

#### **The ‘waterbed’ and ‘tipping point’ theories (paragraph 10(c))**

8.19 The CC raises the “waterbed effect”, and the “tipping point” theories. In neither case do we believe that the relevant theory has any merit. Nor do the circumstances in which these theories (even if viable) might be applicable exist or be expected to exist in the UK retail grocery market.

8.20 The “waterbed effect” theory was tested by the CC in *Safeway* and in *HMV/Ottakar’s*. In *Safeway*, the CC put out extensive questionnaires to suppliers asking for their views on the hypothesis that any of the merged groups would be able to secure *reductions* in their buying prices: in such circumstances would the supplier raise price to its existing other customers? The answer was an emphatic “no”: 58 per cent said no change: 32 per cent said they would *reduce* prices. This accords with our own experience – we believe that many of our suppliers become better able to supply other retailers at competitive rates, as they become more efficient and can benefit from economies of scale.

8.21 The evidence presented by OFT on this issue is so insubstantial as to be worthless. The OFT referred to limited evidence of differentials in buying prices, and suggested that there might be a waterbed effect. However, its evidence, as well as being limited, did not demonstrate that there was a waterbed effect - it simply demonstrated that for some products, different retailers achieved different cost prices. The necessary evidence to demonstrate a waterbed effect is not differential price levels, but that explored by the CC in *Safeway* – that *in response* to an increase in buyer power by large retailers, suppliers *raised* prices to small retailers.

8.22 Moreover, there are theoretical problems with the waterbed effect as well as a lack of evidence. The theory does not explain how suppliers are able to raise prices to small retailers, since it is not clear why any “headroom” in prices would not already have been exploited by those suppliers (nor why such headroom would have been

created by change in buyer power, caused for example by a merger). This argument was considered by the CC in *HMV/Ottakar's* in relation to a merger between two booksellers. The CC rejected the application of the waterbed effect in that merger, on the basis that it “*did not think that publishers’ ability to increase RRP’s would change as a result of the proposed merger. Nor did [it] believe that publishers would reduce discounts to independents or other retailers as a response to an improvement in buying terms for the merged entity*”.<sup>11</sup> We agree with this position. We believe that the theoretical flaws in the waterbed theory apply regardless of which industry the CC is considering and that there is no waterbed effect in grocery retail.

8.23 Similar issues affect the theory that a “tipping point” may arise in wholesaling markets. We have not seen any evidence that would support this theory. The OFT provided only anecdotal information from a number of wholesalers that there may be some reduction in volumes that would lead to their business becoming unprofitable (a statement which would be true for any business). Indeed, the OFT reported that total grocery wholesaling sales had grown and were expected to continue growing in the future. The IGD says the same, noting that the grocery wholesale market has grown steadily since 2000. We also know that the convenience sector, which one would expect to be the hardest hit by any tipping point phenomenon, is the fastest growing sector in the market.

8.24 Moreover, as with the waterbed effect, the tipping point argument suffers from theoretical flaws. Suppose that a wholesaler needed a convenience demand of 10 to be viable, that total demand was 100, and that there were 10 wholesalers. The tipping point theory suggests that if demand falls to 90 as a result of reduced sales in the convenience sector, then all wholesalers – facing now a demand of nine each – would become unviable and exit. But in fact, this situation would only result in the exit of one wholesaler, leaving nine wholesalers each with a demand of 10 (and hence the same ability to access any economies of scale that might exist) – an appropriate response to a 10 per cent reduction in overall demand.

8.25 Given these concerns with both theory and evidence, we do not think that there is any merit in either of the two issues raised by the CC in this paragraph.

### **The impact of non-grocery (paragraph 10(d))**

8.26 Analysing competition in markets for the supply of non-grocery products arguably calls into question the CC’s jurisdiction. Subject to this, our case in respect of our contribution to the competitive process, upstream and downstream, in non-grocery markets is that we are determined to make our non food business a success, to rival the offers of our non-food competitors and to do so by concentrating on exactly the same principles, methods and Values which we implement in respect of food. Our desire to grow in non-food is a key driver of our need for more space from which to sell our non-food offer. We are not aware of any aspect of our conduct towards the suppliers of non-grocery products that is anticompetitive and do not believe that we can assist the CC any further on this point without specific allegations put to us.

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<sup>11</sup> Paragraph 34 of *HMV/Ottakar's*, CC, 12 May 2006.

## Supermarkets' Code of Practice (paragraph 10(e))

8.27 The Code follows the recommendations of the CC in the 2000 report and is the means by which the OFT can secure the accountability of the larger grocery retailers to their suppliers in respect of certain conduct through a published set of rules.<sup>12</sup> The OFT report in 2005 on the working of the Code shows that it is working well, and the OFT noted in passing that it “*considers that it is legitimate for supermarkets to compete vigorously for supplies on quality and price allowing consumers to benefit from value and choice through effective competition.*” We believe that the Code has had a positive effect on the relations between suppliers and retailers in determining the boundary as between acceptable and unacceptable conduct. But it is not and is not intended to be a substitute for the kind of partnering with the supply base that we believe in.

## 9. LAND AND PLANNING ISSUES

9.1 In the Issues Statement, the CC has set out at paragraph 27 a number of land and planning issues. Paragraph 28 asks whether there is any customer detriment. At Chapter 7 of its report the OFT also set out a number of its concerns as to the effect of the planning system and the practices of grocery retailers in their acquisition of land holdings on competition in the market for the retail of groceries.

9.2 The OFT referred to a regulatory system, which the Government has determined is appropriate for all local authorities and itself when considering the appropriate balance of interests, even if it runs counter to what individual businesses might have preferred, or what the CC's predecessor would have liked to see. This does not preclude the Government implementing changes and reviewing the regime from time-to-time, as it is currently doing through the Barker Review of Land Use Planning (the *Barker Report*). The OFT also referred to practices that are conducted under the full scrutiny of local authorities without any serious evidence that those practices are anything other than consistent with the competitive, rational and timely development of retail grocery sites within the constraints imposed by the planning process.

### The planning regime

#### *The consequences for competition of any planning regime*

9.3 The very purpose of the UK planning regime is to limit on public interest grounds the availability of development land. In that sense the planning system affects competitive outcomes in so far as it operates as a barrier to expansion, but one which is intended to achieve wider benefits to society. This has recently been recognised by, among others, the Barker Report. Moreover, the planning regime has, over the last two decades, become increasingly complex, undergoing a pendulum swing from a relatively lightly regulated approach in the mid-1980s, with a broad presumption in favour of development intended to stimulate economic growth, to the

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<sup>12</sup> We note in passing that a number of respondents to the CC's website have referred to our overseas suppliers and can confirm that our treatment of them is consistent with the Code.

tightly regulated, highly bureaucratic and locally variable approach that we have today.

9.4 The current statutory plan-led system has been further complicated by the introduction of sequential tests – so that town-centre sites should be exhausted for retailing prior to edge-of-town and out-of-town development – and the requirement to show “need” for more grocery retailing space. Undue delay, as a result both of this complexity and of Local Planning Authorities (*LPA*) and the appeal system struggling to deal with their workloads, has been one of the main complaints levelled against the planning system. Working one’s way through the complexity of the regime therefore takes skill, foresight, and industry. On occasions it can lead to undue delay and frustration. Nonetheless, while it raises the costs of entry higher than might be expected of an efficient regime, we do not believe that the planning regime has deterred entry.

9.5 Nor does it follow that the competitive outcomes produced within the constraints of the planning system are *worse* for the consumer as a result. That depends on how retailers have used or worked with the grain of the planning system to introduce competition and choice, and whether substantial consumer benefits have been achieved within those constraints.

9.6 Any change to the planning regime will inevitably involve a balancing of various interests and a political decision. As the Barker Report explains, the planning system serves both to reduce the total amount of land available and to restrict potential uses of land.

9.7 In our view, the starting point must be to determine whether the planning regime has seriously limited competitive rivalry in the retail market or seriously and adversely affected the strategies for growth of the grocery retailers themselves.

9.8 The determination of LPAs and Government to make the system work has forced retailers to recognise that they must find ways in which they bring competition closer to consumers in the town or city centre and indeed go further into the inner city areas for the purposes of regeneration, i.e. using supermarket investment as the centre of a multi-purpose complex. That has had the effect of increasing competition in grocery retailing, not least through supermarket entry into the convenience sector.

9.9 Thus our answer to the first part of the CC’s questions (paragraph 27 (a)) is that the need test, the sequential approach, the duration and complexity of the planning process (including the politically unpredictable decisions by Government and local authority) and the other delaying and complicating factors in the regime certainly make matters more difficult in the implementation of a growth strategy. However, they do not act as a barrier of the kind that prevents the implementation of that strategy through means that respond flexibly to the regulations.

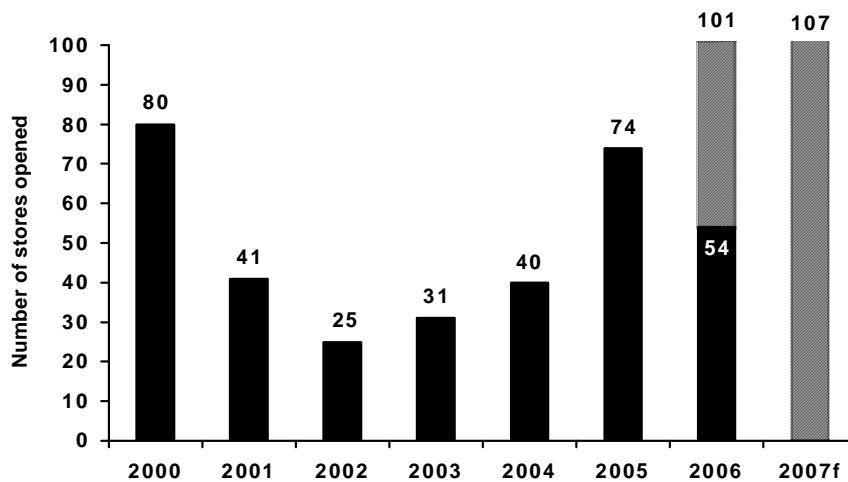
9.10 In particular, we reject any suggestion (paragraph 27(a)(iii)) that there is a limited availability of suitable sites. On the contrary, space for development is available. A survey carried out on behalf of the British Council of Shopping Centres in November 2005 of all retail-led pipeline development projects identified over 50 million sq ft of retail space to be developed over the next ten years. It is widely

recognised that sites for convenience stores are readily available. Verdict Retail estimate that from 2000 to 2005 total grocery retailing floorspace grew by 32 million sq feet, to 573.8 million sq ft. It is anticipated to grow further to just under 600 million sq ft, by 2009.<sup>13</sup>

9.11 Our rivals have found space. Since 2000, Asda has expanded across the UK, opening nearly 70 stores over 1,400 sq m, including thirteen new stores in the South East (seven in London), despite complaints that it could not expand. And there are more to come. Sainsbury could have expanded but, as its chief financial officer Darren Shapland said in May 2006, neglected its store pipeline and was slow to increase its development sites.<sup>14</sup> We have found the sites we need. The discounters, growing exceptionally fast, have managed to find the sites suitable for them: as the table below shows, Aldi, Lidl and Netto have been increasingly successful in opening new stores in town-centre and other locations.

**Stores gained by Lidl, Aldi and Netto (2000-2007) since 2000**

Note: anticipated openings for remainder of 2006, and for 2007, are hatched<sup>15</sup>



Source: Tesco and The Grocer

9.12 As described below, we do not accept that the regime operates in a way which advantages or disadvantages any particular retailer or types of retailer.

*Operators are generally able to work within the planning regime*

9.13 The regime does not operate in a way which advantages or disadvantages any particular retailer or types of retailer (although, as described below, the choices that certain retailers have made in response to the planning regime may have affected their ability to grow).

<sup>13</sup> See *Verdict Retail Futures 09* report (Nov 2004).

<sup>14</sup> *The Grocer*, 5 August 2006.

<sup>15</sup> *Ibid*

9.14 The major change in the approach to retail issues – from the first Planning Policy Guidance in 1988, through the introduction of the sequential approach in 1996, the need test in 1999 to the current Planning Policy Statement 6 - has been the introduction of vastly greater complexity into retail planning. To some extent the planning process has become so complex and uncertain, including serious inefficiencies at the levels of the decision makers, that the development process has itself been delayed. This is a point levelled at the supermarkets by the OFT, as if there were a deliberate investment in undeveloped assets – the so-called “landbank” – to be held against the competition, rather than for the purpose of grocery retailing. There is not. Instead, the complexity of working within the system, including the appeals process, the delays incurred at the decision-making level and the different nature and complexity of site acquisition programmes are all contributors to delay.

9.15 Nonetheless, it is possible for retailers to get on if they work with the grain of the system. One of Tesco’s competitors, Booths put it this way: “*We’re highly selective as to where we develop. It’s a slow steady approach which often requires a great deal of investment in the pre-contractual side*”.

*The impact of the planning regime should not be overstated*

9.16 As previously recognised by both the OFT and the Association of Convenience Stores, planning is comparatively less of an issue in the development of small stores than for larger ones. Sites for convenience stores are readily available and changes for acquired stores can readily be addressed to the satisfaction of local authorities. This situation, and the dynamism more generally exhibited in the convenience store sector has led the OFT to conclude each time that it has considered a merger in the convenience sector that “*barriers to entry for small stores are not at present substantial*”.<sup>16</sup>

9.17 We have described competitive rivalry above. The planning regime may raise costs, including the costs involved in delay, but there is no disproportionate adverse effect on any of our competitors, who are in for the long haul. The planning regime is not the most material factor when considering whether to build a store. The costs of planning would not tip the retailer’s decision one way or the other when set against the overall costs of store development.

### **Use of the planning regime by retailers**

9.18 The burden of the charge made in the OFT report, although couched in the uncertain language of “may” or “suspect”, is that large supermarkets are manipulating the planning regime with the object or effect of restricting competitive opportunities for entry and expansion, thereby enhancing incumbency advantage and limiting supply. We first set out some general observations, which we ask the CC to bear in mind when we turn to specific issues.

9.19 We buy land for the purpose of opening new stores or extending existing stores. The reason that we have more space than our competitors is that we have been

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<sup>16</sup> See for example *Sainsbury/Jacksons* (26 October 2004).

consistent since the early 1980's in wanting to grow our business and have remained so through difficult times. The success of our stores has reinforced our desire to bring Tesco to communities throughout the UK. And to do that we have brought forward opportunities which may have not been obvious to others: because they were not identified in plans, not brought to us by developers, were in very affluent or very poor communities or required flexibility in format and construction. By being patient, consistent, customer-focused, cost effective, innovative and imaginative we have been able to do more, each year.

9.20 One outcome of our response to the planning regime has been what the CC refers to as "land bank". The stock of land and contracts held by supermarket operators should be considered not as a bank but as a *pipeline*, expressed in terms of its size and the length of time lands spends in the pipeline before conversion to and operation as a store: the pipeline of land held for the purpose of developing new retail space is a natural product of three important aspects of a retailer's business, and thus its business model, namely growth, the process of conversion itself and risk:

- (a) **Growth** The required growth in our retail space is determined by two main components of our strategy: (i) to remain strong in the UK grocery business; and (ii) expansion of our non-food business. Decisions on the planned percentage increases in growth in these two areas will determine our aspirations for future space growth and productivity.
- (b) **Time in process** Within the current regime, the time it takes from acquiring a piece of land to opening a store will depend on a number of factors. Larger stores, out-of-town locations, multi-use developments, regeneration projects and sites considering sustainable development will take longer, and proportionately longer depending on complexity, than smaller stores in town centres (especially where a development plan is in place and up to date).
- (c) **Risk** The greater the risk of not being able to open a store on acquired land then the more land is needed in the pipeline to ensure that the growth strategy can be implemented. Thus a competitor who takes on more adventurous projects would require a larger pipeline than the competitor who takes less risk. This risk arises from the complexity and unpredictability of the planning regime, the commercial risk of making an investment in a site before planning consent might have been granted and the political risk of being subject to the potential vagaries of a judgment-based democratic process. Our response to these challenges is to be as flexible as possible and also to take on projects that are more risky than previously, and more risky than our competitors appear to want to take on.

9.21 The mix of growth strategy, process complexity and approach results in a pipeline of land for stores that is perfectly consistent with the normal practice of investment in the inputs necessary for the business. Thus we have convenience stores that bring grocery to the heart of communities. Here the pipeline is relatively small and fast moving. We have larger stores at the edge of town and out of town that are built to meet the demand for growth in non food as well as food. Here the pipeline is relatively large and slow moving, partly because of the need to assemble sequentially

compliant sites and obtain planning permission. For example, we have planning consent for a 60,000 square foot store at Yardley, which we estimate will open in the autumn of 2007. We first acquired a parcel of land on this site some ten years prior to this, in October 1997. The delay has been due to the need to acquire some 35 individual parcels of land (seven of which are still to be acquired). Then we have urban regeneration projects and mixed-use developments, which tend to take a long time, but in which we invest because it is consistent with our values: we can leverage our skills and we can contribute to community development. There is nothing here that could not be replicated by our competitors, either by themselves or through property developers, if they wanted to.

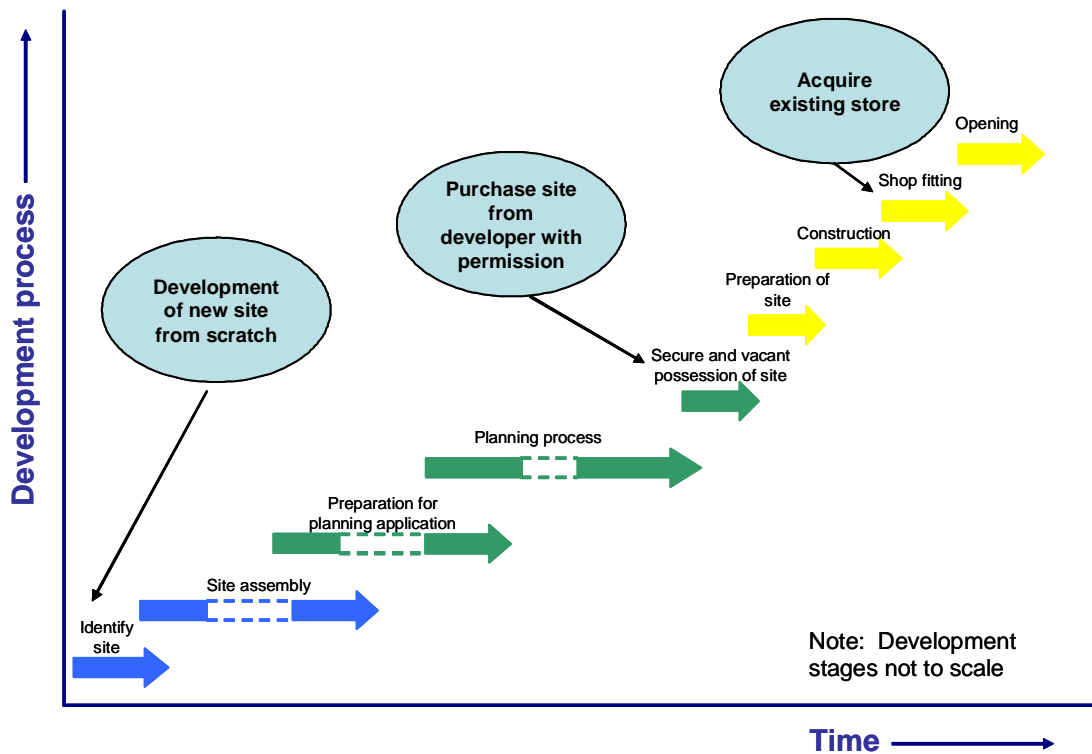
9.22 At paragraph 27(d) the CC asks whether any grocery retailer or group of retailers uses the planning regime or land ownership in a way that deters or restricts entry or expansion by an actual or potential competitor in various ways illustrated in the question. We look at the specific issues suggested in paragraph 27(d) separately.

- (i) ***By acquiring or retaining land banks (including options over land) in a way which serves to exclude or deter actual or potential competitors from entering a market or expanding their operations***

9.23 First, there is nothing anticompetitive in acquiring or retaining a pipeline of land, or as the OFT and CC choose to label it, a “landbank”, in the sense of land which is not currently being developed to become a retail store. “Landbank” issues are not confined to grocery retailing, or to retailing generally – they extend to housing and environmental issues such as waste disposal, minerals and so forth. Indeed the OFT, at paragraph 7.19 of its reasons for reference, recognises that “*it is commercially sensible for supermarkets to have a stock of land on which they are trying to obtain planning permission.*”

9.24 The OFT, however, did not make the connection between the complexities of the planning regime and the landbank issue. In particular, it missed the connection between the acquisition of a site and the negative value (holding cost) of that site until it can be assembled with others for the purpose of making a planning application for the whole. Thus it assumed an optimal time between the acquisition of a site and its use as a grocery store, found that the optimal time had been exceeded and drew the conclusion that this might be for anticompetitive reasons or it might have anticompetitive effects. The general considerations identified above suggest that the use of an average in these circumstances can be most misleading as it fails to give sufficient weight to the time effects of the strategies of particular retailers. In particular, retailers who buy sites “off-the-peg” from developers at a later stage in the development process (an illustrative example of which is set out below) may appear to have held land for less time than more innovative retailers, of which Tesco has been at the forefront. In two thirds of our larger store developments proposed for 2006/07, we are taking the lead (developer) role in putting together and developing the scheme – rather than being the mere recipient of the retail element of a developer’s scheme.

## Stages in site development – illustrative example



Source: Tesco

9.25 There is also a general commercial issue of some importance in this context. In a competitive market, it is difficult to think of a more expensive and unrewarding competitive strategy than to sit on a landbank and do nothing – when there are other sites available to competitors – rather than work imaginatively with developers, local authorities and others to find ways in which the sites we acquire can be transformed into profitable grocery outlets as soon as practicable.

(ii) *By acquiring, divesting or developing land in a way which deters competitive entry or expansion in any locality*

9.26 We work within the rules of a highly competitive and legislated market. The reason that we research, acquire and develop land is for the purpose of opening new stores, or extending existing stores. Therefore, the contracts that we enter are informed by the belief that the site will ultimately acquire planning consent for retail development. Of course, if planning permission is granted, that will have implications for profitable expansion by others in or around that store's catchment area. That does not stem from an intention to deter competitive entry, nor is it an anticompetitive feature but the natural consequence of the nature of the retail development.

(iii) *By otherwise using the planning system in a way which might exclude rivals from entering or expanding (for example pre-empting an anticipated planning application by a rival by applying for the extension or redevelopment of an existing store)*

9.27 We apply for extensions and redevelopment of existing stores as part of normal strategies of renewal and growth. Our extensions, in particular, are usually for the purpose of increasing our non-food offer, and thus will have limited impact on the application of the need test to a grocery competitor's development proposals. Tesco's development may be in order to meet better the enhanced competitive rivalry from a rival store opening and to ensure that our business in those areas remains competitive.

9.28 We work within the rules of a highly competitive and legislated market. It must therefore be our right to present our case as strongly as we can and from time to time to contrast it with other companies' proposals. The restrictive nature of planning means that development proposals are always competing with other potential uses and users of the land (or with arguments for the status quo). Our proposals are of local importance and we therefore have to engage actively in the democratic process of debate about the merits of a scheme. Our aim is to maximise benefits to local people through our proposals and to minimise any disbenefits from implementing the scheme.

(iv) ***By paying excessive prices for land in order to prevent actual or potential competitor from developing it***

9.29 We do not pay excessive prices. We pay prices that are expected to yield an economic return on the investment, having regard to the prospective trading of the store to be built on that site and factors including operational issues, planning prospects and the type of transaction. As this process is not transparent, and as we do not have access to perfect information, there is inevitably a degree of judgment, estimation and risk involved in assessing the 'right' bid. We – like our competitors – are often outbid.

(v) ***By restricting the use or development of land for grocery retailing when it is sold***

9.30 In a small number of cases we may, as vendor, include a restrictive covenant, a lawful and conventional practice, which is not limited to grocery retailing. We do not as a rule impose restrictive covenants when disposing of a site. There are very few examples of this (less than 8 per cent of our disposals since 1 January 2001 have involved a restrictive covenant), and where we have applied such covenants they have had no material effect on conditions of competition.

### **Consumer benefits within the planning regime**

9.31 Tesco's store development programme within the constraints of the planning regime has brought consumers other valuable benefits: regeneration; the development of brownfield sites; investments in community schemes; the stimulation of local economies; energy efficient stores; and sustainable environmental projects of the kind seen by the CC on the site visit.

9.32 At paragraph 28 of the Issues Statement, the CC asks whether any customer detriment arises out of the regime or the way we operate within it. We see the main adverse effect as one of delay, arising out of inefficiencies brought about by complexity, which is the responsibility of central and local Government. While we

try to make a not particularly efficient system work well, by being flexible and taking risks in our approach, we are glad to see that the Barker Review is addressing these issues, including the merits of the need test. However, the planning system results in no competition detriment.

9.33 On the contrary, consumers in the UK have a wide choice of retailing outlet available to them, and the areas of local concentration about which the CC expressed concern in 2000 are now well served by competitors.

9.34 If it were thought necessary to address issues arising from land and planning concerns, despite the absence of evidence of adverse impact on competition in the retail market, or harm to consumers, it seems clear that the target for any remedy should be the planning system itself, its over-complexity and excessive regulation.

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