

Summary of hearing with Waitrose held on Tuesday 26 September 2006

1. Waitrose told us that it was a national one-stop supermarket operator. The groceries market had high barriers to entry caused largely by the planning regime. Waitrose was a beneficiary of the Safeway and the Morrisons disposals. Such an opportunity to build market share in a short period of time was rare. Waitrose wanted to build market share because scale was important within the UK shopping grocery environment, but suitable sites came on to the market infrequently.
2. Waitrose said that the current planning regime was blind to fascia and did not take into account consumer choice. This meant that incumbents could acquire sites and reinforce market position, rather than add diversity to a catchment area. Waitrose considered that planning permission should ensure that there was a pro-competitive outcome when new sites became available.
3. Waitrose said that it attracted a much broader customer base because it offered fresh food and grocery lines often not available elsewhere. Its offer was distinctive and not targeted at competing retailers. All retailers imposed competitive constraints on each other because it was a competitive market but Waitrose competed primarily in the one specialized market and was not interested in entering the convenience store sector. It operated one-stop-shop supermarkets with a preferred store size of 2,232 sq metres (25,000 sq feet). 15 per cent of its store space was below 1,394 sq metres (15,000 sq feet), which it aimed to extend to 2,323 sq metres (25,000 sq feet).
4. Waitrose said that its ability to compete in the one-stop-shop market was constrained by the availability of sites in the UK and planning barriers to entry. This meant that Waitrose was forced to consider new stores of between 1,115 and 1,394 sq metres (12,000 and 15,000 sq feet), which restricted it offering more choice to customers. Such stores were also suboptimal economically, being more expensive to run and more costly staff-wise.
5. Waitrose said that it had a non-food format called 'Food and Home', although development of this format was constrained by the scarcity of store sites. Waitrose also had Internet sales through Ocado, of which it owned 30 per cent. Ocado had a turnover of around £5 million a week, which was equivalent to about 13 average Waitrose stores. Internet sales represented 1.3 per cent of the grocery market and would probably grow to only 5 per cent. Internet sales were a very small part of the marketplace and depended heavily upon having a physical store as a counterpart. It was doubtful whether pure Internet retailers would be hugely profitable.
6. Waitrose said that it had a Site Acquisition Team that trawled the country for available sites. Local Development Plan frameworks governed what Waitrose bought, restricting it to consider locations identified as having a need and sites allocated for food use. Waitrose did not property speculate, as it was a food retailer and needed to buy sites that would serve that role. The challenge with the existing planning framework was identifying a suitable area and need. The sequential test meant starting with the least economic site and the least desirable in terms of customer access and convenience. Such a site also tended to be very expensive. It was a very difficult process.
7. Waitrose said that the existing planning framework, which forced retailers to sell in the town centre, was fine, as was the sequential test, but an incumbent one-stop shop could

easily extend the process. Very few sites fitting the planning criteria became available. If it were not for the opportunistic acquisitions that had come its way, Waitrose would have been losing market share as a consequence of the scarcity of land caused by the planning framework.

8. Waitrose told us that while it did not land bank itself, the behaviour was one way to frustrate new entrants from entering a market. For the incumbent, the holding cost of land was probably less than the competitive impact of a new entrant. Economically, it made sense to land bank because land values rose over time. Waitrose said that its competitors quite often bought land with the expectation that the Local Plan would change over five years.
9. Waitrose told us that whenever a new competitor opened, Waitrose assessed the likely impact and decided whether to take defensive measures, which could include store refurbishment and range maximization. Waitrose might also add services that the competitor was offering such as home shopping. Except for petrol, Waitrose operated one standard pricing regime throughout its estate, so it would not necessarily down-price a store. While Waitrose might follow with below-cost pricing, it did not price locally or below cost in one store as a result of a competitor coming in. Waitrose would rather compete on quality, range and service, rather than price. Waitrose was a price follower, not a price leader.
10. Waitrose told us that it agreed with the market definition applied by competition authorities in recent years: principally that separate markets could be distinguished on the basis of one-stop shopping and top-up shopping and that competition was primarily played out at the local level. But Waitrose also recognized that the satellite operation of stores (including convenience stores) around a one-stop shop could have an impact within certain local markets.
11. Waitrose told us that scale was important because it enabled a more competitive operation. Therefore, Waitrose's recent 24 per cent expansion had enabled it to lower its prices because it had gained greater scale and greater efficiencies. Waitrose was now able to buy at better prices and gain better terms from its suppliers.
12. Waitrose told us that with respect to its suppliers it had a remedy process in place to address any disputes. It also trained and monitored its buyers against its own Code of Practice. It believed it had safeguards in place that hopefully cured 99.9 per cent of all problems with its suppliers. E-auctions were inappropriate as a source of supply because security of supply and provenance was important to Waitrose. It worked very hard to improve quality over a long period of time, which could not be done by e-auction.
13. Waitrose told us that for the supply of beef, lamb, pork and eggs, it had 'farmer clubs', which meant dealing directly with the farmers. It was important for Waitrose to know where its fresh products were produced and to ensure that supplying farmers had a viable return. It had a number of suppliers which supplied it exclusively, although these suppliers were free to supply other markets.
14. Waitrose told us that one of its main concerns was the lack of variety of brands in the UK market, which had been the result of consolidation of the supermarket industry and supplier base. Waitrose was interested in breadth of range and encouraging new suppliers into the market. It had launched a Small Suppliers Charter and the Small

Producers Award. Waitrose now had just under 1,000 locally-produced lines from about 300 suppliers in 135 shops.

15. Waitrose had used restrictive covenants in the past, but was not opposed to having the practice stopped. Waitrose itself had not been affected by the use of restrictive covenants. Tesco had twice the market share of its nearest competitor and an unbuilt estate of sites, which provided it with a five-year pipeline of stores.
16. Waitrose told us that there would be further consolidation within the sector. In terms of return on capital, there were only two retailers at the moment making effective return on capital above their cost of capital. The returns of the other operators were under the cost of their capital. There was about 10 per cent of market share held by vulnerable retailers at the moment that would probably go to the strongest player.
17. The biggest threat to Waitrose was not being able to expand. With food, pay, energy, rent and rate inflation there was enormous pressure on the cost base. Unless Waitrose was able to spread that cost over a larger sales base, its business would become less economic over time. The strength of Tesco was in being able to increase its sales over its base cost.