J Sainsbury plc

20 October 2006

# Competition Commission Inquiry
# Overview of Sainsbury's position

## Summary

Sainsbury's believes that the UK one-stop grocery market is largely competitive today. However it has changed significantly since the MMC's October 2000 report on the supply of groceries by supermarket groups. While Tesco remains the market share leader, the gap between it and the following pack has widened. Sainsbury's has significantly improved its position since the launch of its recovery plan, Making Sainsbury's Great Again (MSGA), in October 2004.

Sainsbury's has concerns about the way in which the structure of the market has developed over the last five years, how it is likely to develop in the future and the impact this will have on the consumer. The rapid expansion of Tesco has led to high levels of local market share in some areas. This high local market share restricts consumer choice and creates the potential for future consumer harm. This situation is likely to worsen based on current growth trajectories and land holdings.

As a result, the current regulatory and planning regimes must take into account local market share when analysing space growth, in order to avoid too little consumer choice and highly concentrated local market shares. The fascia test has become an increasingly blunt tool in a market where there is a greater variability in store size.

## The grocery market today

The one-stop grocery market is largely competitive today. Sainsbury's is part of a diverse competitor set, all of whom adopt different positioning on price, quality, range and service. We believe that competition is enhanced by Sainsbury's strong and distinctive offer. Sainsbury's offer is designed to appeal to all consumers, driven by a focus on great food at fair prices.

Real food prices have continuously declined since 2000, driven by the intense competition in the market. There is also greater choice for consumers, improved quality and higher levels of service. Sainsbury's sets prices nationally by format and does not use price-flexing to exploit areas of higher or lower market share.

Sainsbury's enjoys strong and balanced relationships with both its branded and own label suppliers and operates in partnership to deliver a choice of innovative, high-quality products at fair prices for our customers. The Supplier Code of Practice helps to underscore this and we believe that suppliers would be well served by the expansion of this code to include all competitors operating in the one-stop market. Furthermore, we do not believe there is evidence that supports the arguments for the existence of either a "waterbed"[1] or "tipping"[2] effect.

In convenience, we believe the market is highly competitive with more than 51,000 stores across the UK. The entry of supermarket groups, including Sainsbury's with around 300 stores, has improved choice, price, quality and service for consumers, as confirmed by customer research.

---

1 An argument has been made to the OFT that large supermarkets might use their buyer power to obtain better terms from suppliers to such an extent that suppliers are forced to charge higher prices to their other customers – the so called 'water-bed' effect.

2 An argument has been made to the OFT that the exercise of supermarket buyer power, allied with and contributing to a reduction in the number of independent convenience stores, is serving to undermine the viability of the wholesale distribution networks serving independent retailers. This could force wholesalers to contract the scale of their operations or raise their prices such that a significant number of independent stores would find themselves unable to operate profitably. Ultimately a 'tipping' point might be reached beyond which the wholesale distribution network would break down.

**The market has changed significantly since 2000**

The structure of the one-stop grocery market has changed significantly since 2000, the time of the last inquiry into the grocery retail sector. While Tesco remains the market share leader, the gap between it and the following pack has widened. Tesco has increased its market share from 29 per cent in 2000 to around 34 per cent today[3].

At the same time, Morrisons has not become the competitor that the Competition Commission envisaged in 2003, following its acquisition and integration of Safeway. The Commission intended Morrisons to divest up to 48 one-stop stores only and a further five small stores. In fact, Morrisons has divested more than 100 one-stop stores and a similar number of smaller stores, with further disposals and closures expected. As a result of these two factors, the combined Morrisons/Safeway market share has declined from 19 per cent in 2000 to 15 per cent today[3].

Since the launch of its recovery plan, Making Sainsbury's Great Again, in October 2004, Sainsbury's has significantly improved its position. We have now established ourselves as a strong competitor in the market through our focus on food and health, by reducing prices on over 10,000 lines and by significantly improving availability and service leading to seven quarters of Like-for-Like sales growth. The overall plan, to restore universal appeal through a sales led recovery, is on track to deliver our target of £2.5 billion sales growth by 2007/08, with £1.3 billion delivered to date.

In summary, the market is no longer characterised at the top by having a number of players of broadly similar size. Instead, it has moved to a position of one clear market-share leader and a number of smaller competitors.

Sainsbury's has concerns about the potential impact on consumers because of the way in which the market is changing.

Tesco's rapid expansion has led to the development of high local market shares in some areas. This high local market share restricts consumer choice. Tesco's rapid growth has been driven by new space, which has accounted for 70 per cent of its growth in sales since 2000, largely through the development of Tesco Extras and the expansion into non-food.

As a result of Tesco's space expansion, it now accounts for more than 50 per cent of all one-stop store takings within the isochrones around, over 50 per cent of its one-stop stores. Tesco also holds a monopoly or duopoly position in isochrones around 40 per cent of its one-stop stores. These areas of high local market share mean that consumers in these areas have restricted choice, since location and convenience are two key drivers of choice for the consumer.

The situation is caused by Tesco exploiting the planning and regulatory environment that considers "need" for new space and fascia for acquisition and mergers, neither of which provide an appropriate assessment of competition issues or choice for consumers. We believe that only a market share test can achieve this objective.

Tesco's high market share is in areas where there is now a high provision of one-stop shopping space (as measured by square footage per head of population). Tesco's high levels of market share have been achieved by a combination of three factors: opening or acquiring a large store, opening or acquiring a number of smaller stores, or extending existing stores in the same area. Once stores are built, acquired or extended to such a scale that they meet a sufficiently large share of local demand, then the apparent "need" for additional space becomes more difficult to justify in current planning terms. This restricts local choice and creates the potential for future consumer harm.

The fascia test - as used in the 2003 Competition Commission inquiry - for deciding who, on a local analysis, would be able to acquire the 297 Safeway stores, similarly took no account of size of store, sales per sq ft and market share. The outcome of this was that Tesco and Sainsbury's were similarly affected, in spite of the difference in their market positions. In this situation the fascia test was a blunt tool that led to an inappropriate effect. In a market where there is a greater variability in store size and sales, the fascia test is now wholly outdated.

---

[3] These numbers are based on TNS data for the grocery sales of grocers in stores bigger than 15,000 sq ft. Sainsbury's has estimated the split of sales by store size for M&S and Co-op, for whom TNS record total sales only.

Furthermore, it is worth noting that social and transport policies have conflicted with planning policies and have had an asymmetric impact on competitors in the grocery one-stop market. For example, delivery restrictions and car-park fees have tended to prejudice those competitors with a high proportion of stores in town centres and edge-of-town locations.

Tesco's growth strategy means that local market share concentration is likely to worsen over time. In addition to its current 34 per cent share of the one-stop market, Tesco has 55 per cent of the publicly-known industry landbank. Consequently, Tesco's market share could reach 38 per cent by 2010, simply if all one-stop competitors rolled out their current landbanks. Moreover, if recent differential growth rates were projected forwards, Tesco would achieve an even greater market share of 43 per cent.

**Conclusion**

While the planning system does aim to achieve a balance across social, environmental and economic issues through the needs and sequential tests, it does not take account of local market share and this has helped establish an asymmetric market with an adverse effect on consumer choice and competition in certain local markets.

As the ability to grow size and space through extensions is considerably easier than through new stores, the planning regime should consider these on an equal footing. Furthermore, much of Tesco's new space has been in non-food, which increases food sales through increased footfall by widening the draw and, therefore, its impact. The impact of non-food, therefore, cannot be ignored in any local market share test.

In order to protect and enhance consumer choice, the current regulatory and planning regimes need to consider changes that ensure local market share is taken into account before further planning decisions are made, landbank is developed, or mergers and acquisitions are approved. They will also need to consider potential remedies that address the current imbalance at the local level such as land-bank divestments.

**Enquiries:**

**Investor Relations**
Lynda Ashton
+44 (0) 20 7695 7162

**Media**
Pip Wood
+44 (0) 20 7695 6127