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23/9/07

Tesco/Co-op & Groceries Market Inquiry Secretaries
Competition Commission
Victoria House
Southampton Row
London WC1B 4AD

Dear Sirs

As a member of the Association of Convenience Stores and one of the SME category main parties to the CC Groceries Market Inquiry Pareto Retail Ltd have an interest in the current Tesco/ Co-op Slough Inquiry in so far as the critical issues of market definition; planning, entry analysis and broad retail competition apply to both inquiries. Pareto therefore believe it would be constructive to write a letter intended for concurrent publication on the web sites of each inquiry.

In the first instance Pareto wish to comment upon the original letter submitted by Slough Borough Council (SBC) to the main Groceries Market Inquiry on 4/6/06. In their second paragraph the SBC emphasize that their primary concern stems from the size of the new Tesco store, which at 13,360 m² represents a third of the total convenience floor space in Slough (the term 'Convenience' is understood to be used in the planning context, but in broad terms this can be taken as a proxy for total grocery retail space). It is also noted that the Tesco Slough development constitutes one of the largest supermarkets in the UK. Indeed taking an SME lobbying perspective Pareto would approximate that this store potentially represents £100 million of groceries retail capacity, some 40% of the total groceries demand that might be expected of a conurbation such as Slough, with a population of ca 120,000.

Pareto would also give precedence to the SBC concern in their third paragraph that there is a developing anxiety amongst the local community regarding the increased presence and perceived unfair competitive advantage enjoyed by the larger retailers

(these arguments are developed in further sections referring to increases in small shop foreclosure; decreases in town centre footfall/viability, lack of consumer choice and the difficulties council have in ensuring supermarket developments are compliant with Local Development Framework planning objectives).

In all, it appears to Pareto that the SBC were presenting a very eloquent and professional case that the CC should use its unparalleled investigative capabilities to ascertain whether these type of concerns have an empirical grounding, at least so far as Slough is concerned?

On first review of the various Tesco/Co-op Slough inquiry working papers and appendices, it appears that the CC work to date falls somewhat short of answering the exam questions that the SBC originally postulated. Whilst recognizing that the Inquiry group are to a degree constrained by the original OFT reference under Section 35 of the Enterprise Act as to whether Tesco's acquisition and treatment of the adjacent Co-op site constitutes a relevant merger that might result in a Substantial Lessening of Competition (SLC); there is an inherent danger that the CC may be applying, according to the original SBC stated concerns, an insufficient set of tools to analyse the full range of symptoms and establish the underlying casual defects. Moreover, there is a real and substantive risk that these scoping deficiencies might then give rise to a compounding of error if inappropriate conclusions are applied to the overall Groceries Market Inquiry.

It is on this basis that Pareto would wish to comment in detail on the Tesco/Co-op Slough methodology and findings to date as follows:

1. MARKET DEFINITION: Whilst acknowledging that it is sometimes difficult for resource constrained parties, on quick inspection, to follow the flow of the CC's workings (managing on occasion to combine insufficient summary with undue excision of key facts) it would appear that the CC have not conducted an appropriate empirical evaluation of the changing structure of Slough's grocery market. Pareto would argue that Slough presents an ideal opportunity to conduct a detailed analysis of the nature of the relative changes in demand and supply due to consolidation in a local retail market. Taking the 6 year period from 2001 Pareto would ideally like to see:
 - a. A retrospective evaluation of the change in c-store supply by ownership type and spatial distribution, including a 5 minute walk time isochrone accessibility evaluation. This exercise would offer the

opportunity for the CC to scientifically evaluate the relative merits and entry/exit data accuracy of the various shop databanks including the IGD/Knowledge store, Experian Goad and what might be referred to as the District Rating Valuation Office's shop census data.

- b. Similar for Top Up and One stop stores, but using 5 minute and 15 drive time isochrones respectively.

2. RETAIL COMPETITION: Pareto note that in addition to the two main sites under review by the CC in Slough, SBC have referred to concerns about a number of additional smaller Tesco sites. Pareto can see no reference to the previous and current overall Slough market shares of the key parties. Thus, are the CC ignoring an important opportunity to identify the relative competitive performance of the players including key independent operators in the Slough market? It is argued that this omission may represent a fundamental defect as it is quite possible that a regional independent could have a small but significant share of the market, exercising a competitive constraint on even major players. Indeed Pareto are aware that an independent retailer has been rebuffed in an attempt to purchase the former Co-op site in question, allegedly on a QPRS basis? Moreover, SBC have referred to a public perception that larger retailers may enjoy an unfair competitive advantage. The Slough inquiry presents the CC with an opportunity to comment constructively on this public interest issue drawing not only upon their main groceries inquiry working paper on 'Competition in retailing' but comparing this finding with the actual dynamics and consequences on the ground in Slough. Pareto simply note the CC's main Inquiry findings that there is apparently an ever increasing purchasing price gap between the largest retailers and the largest independent wholesalers (indications are this currently averages ca 12%, a figure almost 400% larger than the average retailers net margins). If this observation is correct, it is argued that it is totally unsatisfactory for the CC to suggest that such that grocery retail competition is broadly satisfactory in either Slough or the UK as a whole. In some grocery categories the price differential represents virtually the entire gross margin for the independent retailer. As a consequence Pareto believe that independent retailers as a genre have of necessity evolved to become more efficient than the Big 4 in consumer terms, surviving

on a much smaller gross margin. Unless the CC formally visit this issue we can only imagine how broad retail competition and diversity would be reinvigorated - if only large independent wholesaler suppliers were able to buy a broad range of goods in key categories at similar prices to the Big 4?

3. PLANNING: It could be argued that the UK's retail planning laws may be fundamentally defective if they allow an already dominant retailer such as Tesco to build a store of ca 150k sq ft. It is Pareto's view that a supermarket development of this size in the UK should always be considered as likely to create 'balance' issues in the store's hinterland, whatever the location. Pareto advocate that 'balance' means a broad offering of One stop, Top up and C-store activity including a significant representation of independent activity at each level. (We particularly would not wish to condone the CC's historic use of a 15 min drive time isochrone competition test as sufficient in anything other than a large merger, especially now that market consolidation in the various relevant segments has reached such high levels that we see serious collusion and abuse allegations emerging on a regular basis).

Pareto draw from the above observations to suggest, so far as the UK groceries market is concerned, that it would be timely if both planning review procedures and the competition authorities' SLC and AEC reviews, might test for 'balanced and sustainable competition'.

Looking forward with specific reference to the CC's Tesco/Co-op Slough (Significant Lessening of Competition) interim findings, Pareto suggest that the CC might not necessarily constrain itself in its recommendations to the divestment of the second smaller Tesco owned site. Indeed, in order to create a template and precedent for reversing the various 'anti-competitive' forces at play within the national groceries market consolidation process, Pareto believe the CC might take this opportunity to systematically review the broader options for recreating a dynamic and competitive groceries market within the curtilage of the LPA in question. Pareto even conjecture that aspects of 'Essential facilities

doctrine' might conceivably be applied as an argument within LPA planning and national regulatory policy development; such that at least 20% of the troubled One stop and Top up retail market segments and 80% of the socially important convenience segment should be supplied by parties other than the Big 4 supermarkets and that Slough might constitute a suitable 'how to' pilot study project in this respect. As well as the connotations for future development proposals it is quite conceivable that such a public policy objective might require the break up or divestment of existing (usually Big 4) supermarket sites.

Finally, notwithstanding the original OFT referral terms, Pareto believe it would be expedient for the CC to exercise its wide powers of discretion to synthesize in AEC as well as SLC terms from the Slough Tesco experience. The CC's counterfactual perspective (para 7 – statement of issues 31/5/07) might thus be modified to state 'The group will need to compare the expected effects of the application of, inter alia, Tesco's dominant market power in Slough against the situation which is most likely to have occurred, had the CC/OFT's 2000 groceries inquiry Supermarket Code of Practice (SCOP) remedy proved effective.'

Yours faithfully

Adrian Costain

MD Pareto Retail Ltd