

## **EXECUTIVE SUMMARY**

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### **Introduction**

The Competition Authority has undertaken the *Grocery Monitor* project at the request of the Minister for Enterprise, Trade and Employment to monitor the grocery sector in light of recent changes in the legislative and regulatory environment. The request was made following the repeal of the Restrictive Practices (Groceries) Order, 1987 (the 'Groceries Order') on March 20<sup>th</sup> 2006 and the insertion of sections 15A, 15B and 15C in the Competition Act, 2002 which address certain business practices in the grocery sector.

The Competition Authority decided, given available resources, to prepare an initial set of three reports that together provide a comprehensive description of the evolution of the grocery sector with respect to market structure and competition at the wholesale and retail levels, retail pricing trends and the effects of the planning system on expansion and entry at the retail level.

This *Report* (Report No. 3) examines the retail planning system as applied to the grocery sector from 2001 to 2007. The first report (Report No. 1), published in April 2008, examined market structure and competition at the wholesale and retail levels of the grocery sector from 2001 to 2006. The second report (Report No. 2), which was published at the same time as the first report, described retail pricing trends in the grocery sector from 2001 to 2007.

### **Key Findings**

The Competition Authority examined competition issues relating to the planning system through the planning experience of the seven largest grocery retailers in the State between 2001 and year-end 2007. These are ALDI, Dunnes Stores, Lidl, M&S, Superquinn, the SuperValu retailers and Tesco.

The importance of planning cannot be overstated. Planning, through the pursuit of a variety of environmental and sociological objectives, affects the lives of every citizen. In a very fundamental way, planning influences the scarcity value of a basic input into our economy - land. Planning policy, and its implementation, therefore affects the final prices that consumers pay for a wide variety of products, including groceries.

The planning system has influenced the type of grocery retailers that trade in Ireland, where they locate, what they offer consumers and the prices that consumers pay.

The Competition Authority has found that, despite the growth in the number and size of grocery retail outlets in Ireland since 2001, the planning system acts as a barrier to competition in grocery retailing in three ways:

1. Restrictions on the *size* of a grocery retail outlet.
2. Restrictions on *where* a grocery retail outlet can locate.
3. The *uncertainty* regarding planning permission can raise the cost and delay the arrival of a new retail outlet.

These factors limit competition between grocery retailers and also limit competition between different grocery brands. They combine to limit consumer choice and value for money.

Over the period 2001 to 2007, overall grocery outlet numbers increased from 349 to 569 while floorspace devoted to the retailing of groceries has increased from 471,508m<sup>2</sup> to 835,647m<sup>2</sup>. Lidl, ALDI and Dunnes Stores have been the most active in opening new outlets while Tesco, Dunnes Stores and Lidl have been most active in adding floorspace.

However, the size, location and rate of expansion of grocery retail outlets has been restricted in the following manner:

- Ireland does not have any *large scale* low cost grocery retailers, as exist in other European countries;
- Discount retailers face more stringent limitations on size than other grocery retailers;
- The size restrictions on grocery retailers means there is less shelf space in retail outlets and so competition between the branded groceries that sit side by side on supermarket shelves is reduced; and
- Consumers all over the country are denied the benefits of competing grocery retailers in their local area due to prolonged planning delays.

In this *Report*, the Competition Authority makes seven recommendations to promote competition in grocery retailing in Ireland. They each require action

by the Department of the Environment, Heritage and Local Government. The recommendations do not require a sea change in Irish planning policy, but rather a refocusing of the system to better accommodate competition and consumer issues.

### **Competition Issues and Recommendations**

The retail planning system is part of the general planning system. The Retail Planning Guidelines, which were first introduced in January 2001 by the Department of the Environment, Heritage and Local Government, embody retail planning policy. The Retail Planning Guidelines set out requirements for both planning authorities and retail planning applicants. Local authorities are required to produce development plans which incorporate retail strategies and policies that are informed by so-called 'health checks' and, since June 2007, the Department of the Environment, Heritage and Local Government's Development Plan Guidelines. Retail planning applicants are required to produce "retail impact assessments".

### **Caps on Retail Space**

The Retail Planning Guidelines set caps, or upper thresholds, on the size of retail development. The caps for grocery retail are set at different levels within and outside the Greater Dublin Area - 3,500m<sup>2</sup> and 3,000m<sup>2</sup> respectively.

The evidence from the period since 2001 suggests that while grocery retailers have been frequently required by the planning system to curtail the size of their outlets, the number of cases where the retail caps were at issue was relatively few. The number of these cases however can be expected to rise given the trend among certain retailers toward larger outlets.

The real effect on competition of the caps, however, is the fact that some retailers will have been completely discouraged from submitting planning applications for large scale outlets, i.e., of a size greater than the caps allow. Large floorspace requirements are typically associated with high turnover, low margin grocery retailing. The effect of the retail caps is therefore to deter the entry of the most price aggressive grocery retailers.

The Competition Authority recommends that the retail caps be removed and that decisions on the extent of development are left to local authorities to make. Floorspace caps inhibit the scale and extent of expansion by existing retailers and prevent the entry of new ones. The availability of larger sized

outlets would give consumers the ability to exercise choice over a wider range of products at more competitive prices. The present limit thus protects existing retailers at the expense of Irish consumers. Limiting floorspace means that Irish consumers experience less choice (for example, less competition between brands due to lack of shelving space) and, higher prices.

**Recommendation 1: Remove caps on grocery retail space**

The Department of the Environment, Heritage and Local Government should remove the grocery retail caps in the Retail Planning Guidelines and allow local authorities to determine the extent of retail development in their respective administrative areas.

**Discount Food Stores**

The Retail Planning Guidelines describe discount food stores as being of a size normally between 1,000m<sup>2</sup> and 1,500m<sup>2</sup>. Planning authorities appear in practice to regard the 1,500m<sup>2</sup> figure as being a binding limit. Where entry to the grocery retail sector has occurred, as with Lidl and ALDI, outlet sizes have tended to be relatively small, even in comparison to the main incumbent retailers. Thus, so-called discount food stores in effect face a much lower retail cap than other grocery retailers. It is unclear whether this is an intended or unintended effect of the Retail Planning Guidelines. In any case, the differential treatment of discount food stores based on pricing strategies is unjustified.

**Recommendation 2: End the discrimination against discount stores**

The Department of the Environment, Heritage and Local Government should delete the reference in the Retail Planning Guidelines to typical discount store sizes and ensure that no distinction is made in the Retail Planning Guidelines between retailers based on their pricing policy.

**Floorspace Projections**

Local authorities are required to produce development plans that contain specific retail strategies. Such retail strategies establish the optimal scale and location for retail development. The Retail Planning Guidelines provide a methodology that local authorities may follow when determining future retail floorspace requirements.

The principal competition concern here is that local authorities may regard their floorspace projections as limits on the total amount of retail development that they can permit within their administrative areas. Estimates of future requirements are very dependent on assumptions about population and consumer spending that may not prove correct. Adhering to a plan without accommodating unforeseen demand would inevitably lead to a lack of adequate provision of space for retail development.

**Recommendation 3: Remove the emphasis on past projections of floorspace requirements**

The Department of the Environment, Heritage and Local Government should amend the Retail Planning Guidelines so as to ensure that planning authorities and An Bord Pleanála place minimum weight on projections of floorspace requirements when assessing planning applications and clarify that individual applications should instead be assessed on their merits.

### **Health Checks**

The Retail Planning Guidelines suggest that local authorities carry out “health checks” to assess the vitality and viability of their respective retail centres. Health checks make use of a wide variety of indicators including those intended to measure diversity of uses, retailer representation and numerous environmental factors. Health checks do not however incorporate indicators of competition.

**Recommendation 4: Include an assessment of competition in health checks of local development plans**

The Department of the Environment, Heritage and Local Government should amend the Retail Planning Guidelines (at Annex 2) so as to require that local authorities undertaking health checks include a competition dimension. Guidance for local authorities on appropriate competition criteria should also be developed.

### **Retail Impact Assessments**

When making planning applications, retailers are required to produce ‘retail impact assessments’. Retail impact assessments include an estimate of how much trade will be diverted from existing retail centres by the proposed new

retail development. The Retail Planning Guidelines set out the main steps that should be taken to arrive at an estimate of trade diversion.

The possibility of losing turnover to new retailers is what drives retailers to provide maximum value and service to consumers. This is the essence of competition. When this possibility is removed, as is the case when trade diversion explicitly informs the decision making process of planning authorities, the established retailer is given the market power to charge higher prices than might otherwise be the case.

**Recommendation 5: Recognise that competition from new retail centres benefits local consumers**

The Department of the Environment, Heritage and Local Government should amend the Retail Planning Guidelines so as to effectively reduce the level of importance that planning authorities apparently place on trade diversion when considering the retail impact assessment process.

**Consumer Representation**

The level of attention paid to consumer interests in the planning process may be insufficient. Planning authorities in arriving at a decision on any individual application must balance a variety of objectives taking into account a variety of views from different organised interests. Consumers are typically not organised and are therefore at a disadvantage when it comes to tilting the balance in their favour. Planning decisions are more likely to reflect the interests of consumers if their views are formally surveyed and taken into account, especially when future floorspace requirements are being assessed.

**Recommendation 6: Formally survey consumers regarding attitudes and preferences**

The Department of the Environment, Heritage and Local Government should amend the Retail Planning Guidelines (at Annex 3) so as to require that local authorities, when assessing future floorspace requirements, survey consumers in a formal statistically representative manner, to accurately ascertain attitudes and preferences. Guidance for local authorities on appropriate survey methodologies should also be developed.

### **Third Party Appeals**

The Irish planning process facilitates third party appeals. This is unusual across Europe. The effect of appeals by competitors is to prolong the planning process by, on average, 50%.

The analysis in this *Report* suggests that there is consistency in the decision making of local authorities and An Bord Pleanála, with outright reversal decisions being relatively uncommon. This is testament to the effectiveness of the Retail Planning Guidelines. Nevertheless the identity of planning applicants, rather than the nature of their proposed retail developments appears to be the principal driver of appeals by third parties. The Competition Authority recognises the legitimate right of third parties to appeal planning applications. However, given that the effect of third party appeals, especially by competitors, is primarily to delay the planning process and therefore raise the cost of entry, the Competition Authority recommends that further research be undertaken with a view to limiting grounds for appeals by competitors.

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| <b>Recommendation 7: Research ways to limit appeals by competitors</b>  |
| The Department of the Environment, Heritage and Local Government should undertake research into how grounds for third party rights of appeal by competitors may be limited. |

### **Concluding Comment**

The planning environment is a principal determinant of the level of competition in local markets. New retailers, and even the threat of new retailers, are what drive established retailers to provide their customers with the best possible value. Allowing retailers to have a certain comfort that their markets will be protected, that their turnover is in some sense guaranteed, in effect confers market power on those retailers. One implication of this is that prices will tend to be higher than they might otherwise be.

Competition and the associated consumer value that goes with competitive markets, is not the only objective facing society or, as agents of society, planners. Planners must balance a variety of objectives. However, greater cognisance of the impact that planning can have on competition, and therefore on prices and consumer value, is warranted.