INDEPENDENT CONSUMER & COMPETITION COMMISSION

ISSUES PAPER
PNG Wholesale and Retail Industry Review

23 September 2008

The Independent Consumer and Competition Commission ("Commission") is a statutory body established under the *Independent Consumer and Competition Act 2002*.

The primary objectives of the Commission are; to enhance the welfare of the people of Papua New Guinea through the promotion of competition, fair trading and the protection of consumers' interests; and to promote economic efficiency in industry structure, investment and conduct; and to protect the long term interests of the people of Papua New Guinea with regard to the price, quality and reliability of significant goods and services.

At the time of the Review into the Wholesale and Retail Industry, the Commission has three Commissioners who are:

- Thomas Abe – Commissioner & CEO
- Dr Billy Manoka – Associate Commissioner (Resident)
- Mr. David Dawson – Associate Commissioner (Non Resident)

FORWARD

The Government, as part of its 2007 Budget Strategy, announced its intention to undertake a review of competition and general market practices in the Wholesale and Retail sectors in Papua New Guinea with a view to improving the economic performance of this sector. On 21st September 2007, the Commission received from the Minister for Treasury the Terms of Reference (Appendix A) to undertake this review and has subsequently proceeded towards undertaking the review.

The Commission will be undertaking this review in accordance with the terms of reference from the Minister for Treasury and in accordance with Part VIII of the *Independent Consumer and Competition Act 2002 (ICCC Act)* which sets out the requirements the Commission must meet in undertaking inquiries referred to it by the minister.

Consistent with the requirements of Section 124 (2) of the ICCC Act, the Commission will be undertaking this review in an open, transparent and consultative manner, and therefore public and industry stakeholders' comments and views will play an important part in the entire process.

This Issues Paper is intended to provide a brief overview of the issues the Commission considers to be relevant to the Review and is also intended stimulate discussion among the public and stakeholders. The Commission invites comments and views from stakeholders, key Government departments, interested parties and the general public on issues raised in this Issues Paper.

Submissions to the Commission will be available for public inspection unless the Commission agrees that all or part of the submission should remain confidential. However, in accordance with the provisions Section 124 of the ICCC Act, it is intended to make the Review a process as transparent as possible, and to this end, submissions would normally be available for public inspection unless there are exceptional commercial-in-confidence reasons why submissions should be held confidential.

Submissions to this Issues Paper should be received by **14th October 2008**, and should be addressed to:

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All inquiries should be directed to **Mr Stanley Alphonse,** Executive Manager, Prices, Regulatory Affairs & Special Project Division on:

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Executive Summary

The Government, as part of its 2007 Budget Strategy, announced that its intention to examine the wholesale and retail industry with a view to considering competition issues and the role and place of regulation. As part of this strategy the Independent Consumer and Competition Commission (the Commission) has been instructed by the PNG Government to review the wholesale and retail industry. This review is expected to go hand in hand with other reviews the Commission have completed namely the Sundry Declared Goods, Tin Fish and Tin Meat, Rice and Flour reviews.

This Review is intended to look at a wide range of issues relating to the operation, composition, structure, and regulation of the Wholesale and Retail Industry. This recognises the significance of wholesale and retail industry to the efficient operation of the domestic economy and the reliance on import and export between PNG and the wider world to strengthen and build the national economy through international trade and commerce.

At the conclusion of this review, the Commission will make recommendations on what if any action can be taken by Government to address regulatory impediments or enhance the prospects for increasing competition in the Wholesale and Retail Industry in PNG.

As part of this review the Commission is seeking stakeholders' comments on a number of issues and specific questions that requires appropriate response from the stakeholders. Some of the issues are identified below:

<u>Issues 1</u>
The Commission seeks comments from the public and any interested parties on the scope of goods and services to be included in the review.

<u>Issues 2</u>
The Commission seeks comments from the industry and relevant stakeholders on the operation, structure, size and characteristics of the Wholesale and Retail Sector in PNG

<u>Issues 3</u>
The Commission seeks comments from the industry and relevant stakeholders on the demand for wholesale and retail Services in PNG

Issues 4
The Commission seeks comments from the industry and relevant stakeholders on the methodology the Commission is using to assess the degree of competition on the wholesale and retail industry

Issues 5
The Commission seeks comments from the industry and relevant stakeholders on whether regulation of wholesale and retail margins should continue or not, and if regulation were to continue, should regulation continue in its current form or should regulation take a different form?

Issues 6
The Commission seeks comments from the public and any interested parties on the scope of policies with relation to promoting Competition and protecting consumer interest.

Issues 7
The Commission seeks comments from the public and any interested parties on the level of competition in the supply chain especially on;

- **Domestic Freight Rates**
- **Prices**
- **Level of supply in terms of range, quality and nature**
- **Competitiveness and the diversity of the supply chain**

Issues 8
The Commission seeks views from stakeholders on the likely developments or changes in the existing structure of the wholesale and retail industry including entry of new service providers, over the next decade.

Issues 9
The Commission seeks views from stakeholders on the law and order situation with regard to the additional cost in the overall context of the competition issues.

Issues 10
The Commission seeks comments and submissions from interested stakeholders on whether or not certain labour laws are being observed

Issues 11
The Commission seeks comments and submission on the minimum health and quarantine requirement

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1.0 INTRODUCTION

1.1 Background

On 21st September 2007, as part of the Government's 2007 Budget Strategy, the Minister for Finance & Treasury formally requested the Commission to undertake a comprehensive review into the Wholesale and Retail industry in Papua New Guinea.

1.2 Legislative Requirements

The Commission will be undertaking this review under Part VIII of the ICCC Act which contains guidelines the Commission must adhere to when undertaking inquiries which have been referred to the Commission by the Minister or inquiries which the Commission has initiated itself.

1.3 Purpose of Review and Objectives

1.3.1 Purpose

The purpose of this review is to consider competition issues and the role and place of regulation in the wholesale and retail industry with a view to improving the overall efficiency, effectiveness, and competitiveness of the Wholesale and Retail Industry in PNG.

This review will look at a wide range of issues relating to the operation, composition, structure, and regulation of the Wholesale and Retail Industry especially with a strong focus on the wholesaling and retailing of goods and services supplied to households in PNG.

1.3.2 Specific Objectives of Review

Under the Terms of Reference from the Treasury, the Commission is required to report on specific matters relating to the Wholesale and Retail industry, in particular the Commission will;

- Report on the current operation of the Wholesale and Retail Industry in PNG with a particular focus upon:
    - the size and other characteristics of the domestic industry
    - the competitive behaviour of participants in the industry,
    - impediments to competition in the industry, both regulatory and non-regulatory,
    - the relationship between larger vertically integrated businesses in this industry with smaller retailers and wholesalers,

- o any particular issues impacting on competition at the wholesale and retail level arising from the spatial characteristics of the country,
- o the interaction between the Wholesale and Retail Industry in PNG with importers and domestic manufacturers, and
- o the range of government policy and regulatory requirements impacting on the industry, including the consistency in these regulatory requirements at the national and Provincial government level across the country

- Identify issues and areas where Government action may be appropriate to improve the overall competitiveness, efficiency and effectiveness of the Wholesale and Retail Industry in PNG

- Comment on the need for the continuation of some form of control on wholesale and retail mark ups where the ICCC has determined under the Prices Regulation Act that price regulation is required, and identify options that could be used to set mark ups should there be an need for the continuation of some form of regulation in certain instances and for certain goods and services, and,

- Make recommendations on what action by Government may be appropriate to rectify any problems in the current structure, regulation and operation of the Wholesale and Retail Industry with a view to improving competition and competitiveness in the industry.

1.4 Goods and Services covered in this Review

The specific goods and services which will be covered in this review will include but will not necessarily be limited to the following:

- Fresh, and frozen meat, vegetables, dairy products and other related consumables
- Tinned and dry foodstuffs
- Bread and other bakery products
- Confectionary
- General household consumables
- Personal health care products
- Alcoholic and non alcoholic beverages
- Tobacco and cigarette products
- Household furniture, furnishings, electrical and non electrical goods

- Clothing and footwear
- Linen, blankets towels, manchester, and related products
- Books and stationary
- Motor vehicles, parts and accessories
- Hardware and related products

In a general sense, the review will not focus on industries which have been the focus of other Reviews undertaken by the Commission, such as the Petroleum Industry Pricing Review, the PMV & Taxi Fare Review, the Air Niugini - Qantas Code Share Authorisation Review and similar reviews, except to the extent of providing comment on where such price controlled industries impact, either positively or negatively on the pricing or competitiveness of the wholesale or retail delivery of good and services to household consumers.

For the purposes of this review, the Commission intends to divide the above list into the following broad groups to assist the Commission in making meaningful decisions that will benefit Papua New Guineans. The broad groups will consist of "Basic Household Needs", which are goods and services essential for maintaining basic living standards, "Discretionary Household Goods", which are goods households are likely to purchase using disposable income and "Luxury Goods" which are goods households would demand more of as income would rise.

Grouping the above list under the three broad groups, the Commission has come up with the following;

Basic Household Needs

- Fresh, and frozen meat, vegetables, dairy products and other related consumables
- Tinned and dry foodstuffs
- Bread and other bakery products
- Clothing and footwear
- Personal health care products

Discretionary Household Goods

- Confectionary
- Alcoholic and non alcoholic beverages
- Tobacco and cigarette products
- Household furniture, furnishings, electrical and non electrical goods

- Books and stationary
- Hardware and related products

Luxury Household Goods

- Motor vehicles, parts and accessories

Following the review, the Government will consider the policy recommendations put forward by the Commission, and further consider whether any policy response may be required to improve the overall efficiency, effectiveness, and competitiveness of the Wholesale and Retail Industry in PNG including adoption or revision of relevant regulatory arrangements.

The Commission seeks comments from the public and any interested parties on the scope of goods and services to be included in the review.

1.5 Conduct of the Review

The Commission will be conducting this review in accordance with Part VIII of the ICCC Act. In particular, section 125 of Part VIII of the ICCC Act requires the Commission to undertake a review in accordance with any direction issued by the Minister and also in a manner in which the Commission considers appropriate.

In addition to the requirements under Part VIII, the Commission will undertake this review in an open, transparent and consultative manner in accordance with world's best practice. This consultation process will include soliciting views and comments from all major stakeholders including major wholesalers, retailers, other smaller operators, key Government Departments, the PNG Business Council, PNG Chamber of Commerce, Business houses and other interested parties and the general public.

The Commission will consider all matters raised in response to this Issues Paper and following further consultation with stakeholders will release a Draft Report which will again provide the opportunity for further consultation.

The Commission intends to hold public hearings after the release of the draft report in Port Moresby, Lae, Mt. Hagen and Rabaul in order to provide an opportunity for stakeholders to present their views on any issues associated with this Review. The Commission will take into account the comments and views from the public hearings and submissions on the Draft Report when it drafts the final report. Table 1.5 below sets out the Commission's expected timetable for this Review.

The timetable for the current Review is as follows:

Table1.5

Activity	Timeframe
Release of Issues Paper	23 September 2008
Close of Submissions on Issues Paper	14 October 2008
Release of Draft Report	25 November 2008
Public Hearings to be held in Port Moresby, Lae, Kokopo and Mt Hagen (if required)	First Week of December
Close of Submissions on Draft Report	19 December 2008
Public Release of Final Report	16 January 2008

2.0 THE WHOLESALE & RETAIL SECTOR IN PNG

2.1 The Wholesale and Retail Industry and the PNG Economy

The Wholesale and Retail industry plays a significant role in the PNG economy, firstly by providing the basic and discretionary goods needed by PNG households to maintain appropriate standards of living and by providing employment to Papua New Guineans either directly through the formal sector or indirectly through the large informal sector.

The goods that are supplied by these industries are either imported or produced locally. For the imported goods, the importers who are mainly wholesalers or retailers sourced their goods from abroad and to some extent imported inflation and international price movement do impact on the prices of goods supplied in the domestic retail and wholesale industries. Other factors that have impacted the price of domestic goods are the inflation, the exchange rate and fuel price.

With the domestic economy performing well supported by high prices in the mineral and commodity sectors, the revenue generated has been of little help to ease the increasing cost of the goods supplied by wholesale and retail industries recently. The underlying CPI for the last 12 months ending June 2008 is estimated at 10.7 percent reflective of the increasing cost in the supply of goods and services in the country which is high compared to the same period last year.

Unlike other goods listed, factory gate prices of rice, flour and sugar are monitored by the Commission on quarterly basis against some benchmark prices from National Statistical Office (NSO) and Australian Bureau of Statistics (ABS). The movement in prices of these goods at the factory gate will also have impact at the wholesale and retail prices once freight and other costs are accounted. Represented in Figure 1 and 2 are movement in price index for rice and flour respectively against the benchmark price to the period ending March quarter 2008.The general pattern of the movement in the factory price index against the benchmark price index is important from a perspective when prices at the wholesale and retail industries are behaving in an unanticipated manner.

Prices at the domestic economy are highly influenced by international activities. The world currently is faced with food crises and some countries are now taking short term measures putting export ban on food crops. Such actions could be detrimental to countries who are highly dependent on imported goods as raw materials or for direct consumption and the domestic economy has recently suffered as a result of such actions.

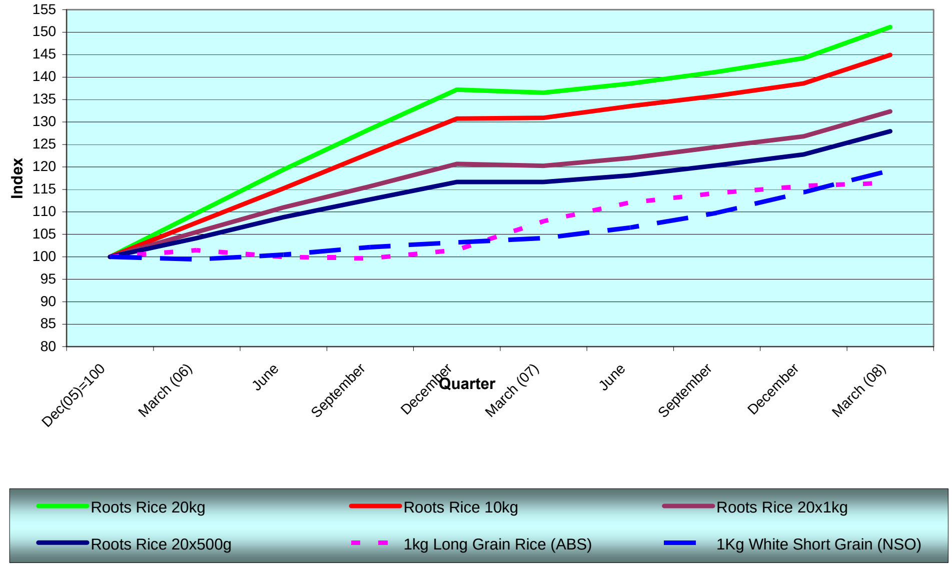

Figure 1. Price Monitoring of Rice - Trukai Vs NSO Vs ABS
4 Quarter Moving Average

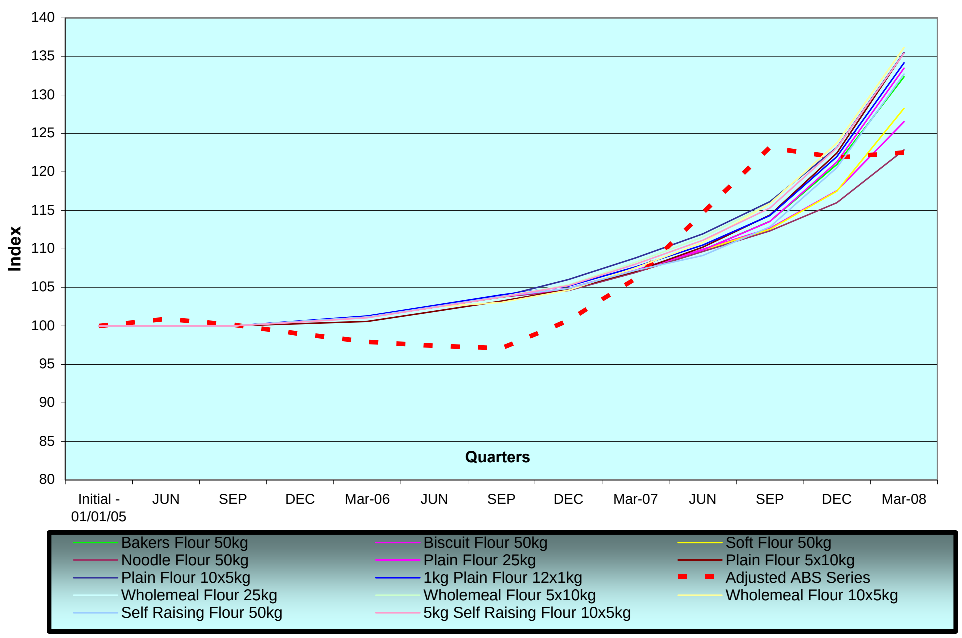

Figure 2. Flour Price Monitoring -4 Qtr Moving Average
GFI Ex Pom Vs ABS

Although the world food crises has improved to some extent and economies recovering from the repercussions, some economies including Papua New Guinea have not fully recovered thus prices of goods and services have either remain unchanged or continued to rise. The domestic economy to some extent has failed to signal the world trend and the savings from the recovery has not been passed on to the domestic markets which has recorded one of the highest inflation.

2.2 Structure, Size and Characteristics of the Wholesale and Retail Sector in PNG

The structure of the wholesale and retail sector in PNG is quite varied. Some businesses simply operate in either the retail or wholesale sector only, while some of the larger businesses have operations in both the wholesale and retail sector.

Some domestic manufacturing companies also wholesale and retail their own products and are responsible for distributing their products from their factories through their branch networks and authorised outlets.

Determining the size of the wholesale and retail sector at this stage is a difficult task given that appropriate data is not readily available for analysis. What can be inferred about the sector is that it is a large sector, given that in the main and minor centres of PNG, the wholesale and retail sector is an important supplier of basic goods to households. In the remote, rural areas of PNG, village stores also provide basic goods, which indicates that the scale and reach of the wholesale and retail sector is extensive.

However, the growth of the sector is potentially limited by a number of factors such as;

- The small nature of the PNG domestic market in absolute and relative terms
- The low level of cash income amongst the majority of the population and small disposable income of Papua New Guineans.
- High internal freight cost which contribute to high retail prices and reduce product affordability.
- The lack of quality road infrastructure network in Papua New Guinea to distribute goods at low cost and on a timely manner.

Taking a snapshot of the industry structure, the Commission has identified a number of manufacturers, wholesalers and retailers in the supply of the goods under review. The numbers in some case represent only manufacturers and in other cases is a combination of manufacturers, wholesalers and retailers. This only include the operations in mainly the urban centres in the country.

Table 2.2: Structure of the industry

Type of Goods	**Industry Structure** No of Manufactures/wholesalers/retailers
Basic Household Needs	
Dairy Products	3*
Fresh, and frozen meat, vegetables, and other related consumables	13*
Tinned foodstuffs	5*
Bread and other bakery products	31
footwear	6
Clothing	15
Personal health care products	6
Discretionary Household Goods	
Confectionary	N/A
Alcoholic and non alcoholic beverages	16
Tobacco and cigarette products	1*
Household furniture	35
electrical and non electrical goods	24
Books and stationary	40
Hardware and related products	29
Luxury Household Goods	
Motor vehicles, parts and accessories	8

Source: PNG Directories & Directory of Manufacturers
NB: The asterisk (*) represent only manufacturers in the industry while others are wholesalers and retailers

The Commission seeks comments from the industry and relevant stakeholders on the operation, structure, size and characteristics of the Wholesale and Retail Sector in PNG

Specific questions on the structure, size and characteristics of the wholesale and retail sector of PNG

- For your business, please provide details of:

- the nature of your business (ie wholesaler, retailer, integrated wholesaler-retailer);
  - the size of your business (annual turnover); and
  - product lines which you carry.

- For your particular market, please provide details of:
  - the number and nature of your competitors (ie wholesalers, retailers, integrated wholesalers-retailers);
  - the relative size of your competitors (compared with your business); and
  - product lines carried by your competitors.

- Please provide details on how the structure of the wholesale-retail sector is different between urban and rural areas of PNG.

- Please provide details of any basic household goods which are not supplied to remote rural areas of PNG.

- Is internal transport of goods a significant cost to wholesalers and retailers? Does the cost of transport have a significant impact on the price of products to consumers?

- What have been the major changes to the structure of the wholesale and retail sectors in the last five years?

2.3 Demand for Wholesale and Retail Services in PNG

The demand for wholesale and retail services in PNG would be generally depend on the prevailing economic conditions of PNG. Generally, a strongly performing PNG economy would result in demand for wholesale and retail services to rise, while a weak PNG economy would result in demand for wholesale and retail services to fall.

Specific factors that would also impact on the demand for wholesale and retail services would include those which impact upon the price for the goods; these would mainly be;

- the cost of transportation (especially fuel costs)
- the PNG Kina/Australian Dollar exchange rate would also have an impact on the demand for goods through their influence on the price of these goods.
- import taxes and excise duty

The Commission seeks comments from the industry and relevant stakeholders on the demand for wholesale and retail Services in PNG

Specific questions on the demand for wholesale and retail services in PNG

- Please provide details of any changes (increases/decreases) in demand for household products in the last five years. When did these changes occur? Were these changes in demand linked to specific products?

- What are the key factors which influence demand for household products? Please provide details on when these factors have had a positive/negative impact on demand.

2.3 Degree of Competition within the Wholesale and Retail Sector

The Commission will be assessing the degree of competition within the Wholesale and Retail sector by using two important tools; these being

- an integrated spatial monopoly model, and
- Porter's 5 forces model of competitive behaviour

2.3.1 Integrated Spatial Monopoly Model

The spatial monopoly model is a tool that assesses the level of competition within one geographic area. In PNG's case, this model recognises that the competitive forces in the more urban areas such as Port Moresby and Lae will be very different to the competitive tensions in other less urban areas and towns of PNG. Hence, the Commission may undertake analysis on the basis of distinct geographical zones.

The likely zones that will be considered are:

Urban: Port Moresby, Lae, Mt Hagen, Kokopo
Sub Urban:
Rural Accessible (with relatively easy access to markets)
Rural remote (with relatively difficult access to markets)

Specific questions on the integrated spatial monopoly model

- *Are these zones appropriate to analyse PNG's wholesale and retail sectors? Please provide details of any other factors which should be considered.*

2.3.3 Porter's 5 Forces

Porter's 5 Forces is a framework that will allow the Commission to clearly identify the issues relevant to the wholesale and retail sectors and to understand the factors influencing competition throughout the industry. The five forces are:

- The degree of threat proposed by new entrants
- The degree of bargaining power of suppliers
- The degree of threat proposed by substitute products or services
- The degree of bargaining power of buyers
- The degree of rivalry among existing competitors.

These key issues are discussed further below;

The degree of threat proposed by new entrants

Ease of entry into and exit from a market is a good indicator of whether wholesale and retail market is competitive or not. To the extent that new competitors can freely enter a market (or leave) there will always be a degree of potential market contestability. In these circumstances an incumbent monopoly operator may choose not to exercise any monopoly pricing powers and thereby not encourage a new entrant from actually entering the market.

The threat of entry in an industry depends on the height of entry barriers that are present and on the reaction new entrants can expect from incumbent services providers. These responses and the height of these barriers can be best described by the following:

- The supply side economies of scale (efficiency and scale of production
- Demand side benefits of scale (the degree to which buys are comfortable with existing suppliers)
- Capital requirements
- Incumbency advantages
- Restrictive government policy.

Specific questions on the degree of threat posed by new entrants

- Please provide details of any new entrants to the wholesale / retail sectors in the last five years? How successful have these new entrants been? On what basis is this success measured?

- Are there economies of scale in the wholesale and retail sectors? Do wholesalers and retailers receive discounts for purchasing products in bulk?

- Do manufacturers, wholesalers and retailers have strong and constant demand for their products? Please provide details of any situations where there is a large accumulation of stock, due to weak demand.

- Do wholesalers and retailers have constant supply of household products? Please provide any details of any situations where manufacturers were unable to meet demand.

- Please provide comment on whether any Government policies prevent new entrants to the wholesale and retail sectors.

The degree of bargaining power of suppliers

The degree of bargaining power of suppliers determines the point where suppliers can extract value through higher prices, limiting quality or services, or shifting costs to other industry participants. The degree of suppliers bargaining power will depend on the concentration of suppliers relative to consumers, the degree of diversity in the industries they serve, the transaction costs of shifting from one competitor to another, the degree of differentiation between products and services, the existence of substitute suppliers, and the degree to which suppliers can threaten to further integrate industry (in the PNG context this is especially relevant due to the high degree of vertical integration throughout the economy).

Specific questions on the degree of bargaining power of suppliers

- Do suppliers (manufacturers, wholesalers or retailers) typically have a wide range of products, or do they specialise with particular product groups. Please provide details.

- Are buyers able to choose from a variety of suppliers to purchase products? Please provide details of costs to buyers associated with changing suppliers?

The degree of bargaining power of buyers

There is obviously a counter point to powerful suppliers in powerful buyers who are able to extract relatively lower prices due their importance to the profitability of suppliers. It is not expected that this will play a particularly big role in the forces which shape the wholesale and retail industry in PNG. However, we will analyse this to establish the degree to which buyers are able to counter market power of suppliers through the establishment of buying groups.

Specific questions on the degree of bargaining power of buyers

- Please provide details of situations where groups of buyers formed a group to negotiate discounts from suppliers.

- Are independent buyers typically able to negotiate discounts from suppliers. If so, what are the basis for these discounts (ie volume, long term contracts, loyalty)?

The degree of threat proposed by substitute products or services

Substitute goods and services are particularly relevant in the context of most if not all of the good identified in your request for proposal. Most goods have a number of substitutes which should service to minimise the market power of suppliers. However, again this needs to be seen in the context of the PNG economy and the degree of spatial monopoly power in limiting the availability of substitutes.

Specific questions on the degree of threat proposed by substitute products or services

- Are buyers able to purchase substitute household products from competing suppliers.

- Are there costs associated with changing suppliers? Please provide practical examples of substitute products offered by competing suppliers.

The degree of rivalry among existing competitors

The final component of our analysis will be the degree to which rivals within the industry compete against each other. Generally, high rivalry between competitors results in limits on the profitability of competitors as discounting and product introductions generally drive down available profits. Two important factors dedicate the degree of rivalry between suppliers:

- The intensity of the rivalry owing to numerous competitors, slow industry growth, high barriers to exit the industry, highly committed businesses, and an in alibility to read each others signals.

- High degrees of price competition due to the similar nature of products and services, high fixed costs but low marginal costs, the ability of competitors to flex up operations (i.e. excess capacity) and the degree to which the product is perishable.

Specific questions on the degree of rivalry among existing competitors

- Has the demand for and supply of household products increased in the last five years? Please provide details of the growth of particular suppliers.

- Please provide details of any suppliers who have exited the industry in the last five years. What were the reasons for their exit?

- Please provide details on suppliers' strategies suppliers to increase market share. How effective have these strategies been?

- What strategies do retailers employ to signal price offers to consumers? Which strategies seem to be the most effective? How do retailers measure the effectiveness of their strategies?

- Do suppliers have high fixed costs / high marginal costs? What are the major factors impacting on these costs?

- To what degree are suppliers able to increase supply of products if demand increases?

- Are suppliers forced to lower their prices due to pressure from competitors?

- How long to suppliers typically hold product for? Do times differ by product categories? Please provide details.

Having reviewed these five forces the Commission and PwC will be an extremely strong position to review the industry as whole. However, there are number of factors which also need to be considered in our review, including:

- Technology and innovations
- Governments
- Complementary products and services available in the market

The Commission seeks comments from the industry and relevant stakeholders on the methodology the Commission is using to assess the degree of competition on the wholesale and retail industry

2.4 Regulated Wholesale and Retail Margins

An important part of this review is for the Commission to consider whether there is a need to continue the regulation of wholesale and retail margins of certain goods and services.

The table below lists the goods originally which have their margins regulated and the amount by which the margins are regulated. However, most of the goods have been reviewed and apparently were deregulated from price control concurrently with the regulated wholesale and retail margins which ceased to exist forthwith apart from flour, rice and sugar.

Table 2.4: Original List of Declared Goods and Margins

Items	**Allowable % Wholesale margin if goods imported of purchased from local manufacturer for sale to**		**Allowable % Retail Margin for**		**Allowable % retail margin if goods are imported or purchased from local manufacturer**
	Related Entity	Unrelated Entity	Related Entity	Unrelated Entity	
Batteries – Torch and Radio	10%	11%	8%	10%	18%
Butter	10%	11%	8%	10%	18%
Coffee beans – ground and instant	10%	11%	8%	10%	18%
Flour	10%		8%	10%	18%
Margarine	10%	11%	8%	10%	18%
Milk – powdered and concentrated	10%	11%	8%	10%	18%
Poultry – excluding duck, goose and turkey	10%	11%	8%	10%	18%
Rice – brown and white	10%	11%	8%	10%	18%
Soap – laundry, cakes and powdered	10%	11%	8%	10%	18%
Sugar – brown and white	10%	11%	8%	10%	18%
Tea	10%	11%	8%	10%	18%

These regulated margins were first established in the mid 1980's, and have remained unchanged and unreviewed since then.

For flour, rice and sugar, the Commission has conducted separate pricing reviews and has undertake to continue price regulation retaining the existing wholesale and retail margins but express in kina or toea values. The tables below represent the margins of these declared goods.

Table 2.5: Approved declared wholesale and Retail Mark-ups for flour products

Product	**Pack Size (Kg)**	**Mark-up per Kg**	
		Wholesale (toea/Kg)	Retail (toea/Kg)
Bakers flour	50	17.30	17.50
Biscuit flour	50	17.30	17.50
Soft flour	50	17.30	17.50
Plain flour	25	18.10	18.20
Plain flour	10	18.30	18.50
Plain flour	5	18.70	18.80
Plain flour	2.5	18.90	19.10
Plain flour	2	18.90	19.10
Plain flour	1	18.90	19.10
Wholemeal flour	50	17.20	17.40
Wholemeal flour	25	17.90	18.10
Wholemeal flour	10	18.20	18.30
Wholemeal flour	5	18.50	18.70
Wholemeal flour	2.5	18.80	18.90
Wholemeal flour	1	18.80	18.90
Self Raising Flour	50	17.90	18.00
Self Raising Flour	5	18.60	18.70
Self Raising Flour	2	19.20	19.40
Self Raising Flour	1	19.40	19.60

Table 2.6 Approved Declared Wholesale and Retail Mark-Up for Roots Rice Products

Product Brand	**Pack Size (Kg)**	**Mark Up Per Kg**	
		Wholesale (toea/kg)	**Retail (toea/kg)**
Roots Rice	25	17.50	17.60
Roots Rice	20	18.00	18.20
Roots Rice	10	19.30	19.40
Roots Rice	1	21.40	21.60
Roots Rice	0.5	11.50 toea per 0.5kg	11.60 toea per 0.5kg
Roots Rice (Chicken Flavoured)	0.5	12.80 toea per 0.5kg	12.90 toea per 0.5kg

Table 2.7 Approved Declared Wholesale and Retail Mark-Up for Ramu Sugar Products

Product Code	Product Description	Package	Mark Up per Pack	
			Wholesale Kina/Pack	Retail Kina/Pack
Ramu Natural Mill White Range				
RMWPP1KX10	Ramu Mill White Sugar Poly Pack	1Kg	0.34	0.34
RMWPA1KX15	Ramu Mill White Sugar Paper Pack	1Kg	0.34	0.34
RMWPP500GX20	Ramu Mill White Sugar Poly Pack	500gm	0.18	0.18
RMWPP250GX40	Ramu Mill White Sugar Poly Pack	250gm	0.10	0.10
RMWPC7GX500	Ramu Mill White Sugar Sachet Pack	7gm	0.004	0.004
RMWPP5KX1	Ramu Mill White Sugar Retail Pack	5Kg	1.54	1.55
RMWBB10KX1	Ramu Mill White Sugar Bulk Bag	10Kg	2.93	2.95
Ramu Speciality Range				
RRWPP1KX10	Ramu Refined White Sugar Poly Pack	1Kg	0.45	0.45
RCAPP500GX20	Ramu Castor Sugar Poly Pack	500gm	0.27	0.27
RGOPP500GX20	Ramu Gold Sugar Poly Pack	500gm	0.19	0.19
RSBPP500Gx20	Ramu Soft Brown Sugar Poly Pack	500gm	0.40	0.41
Ramu Premium Bulk Sugar				
RMW25KX1	Ramu Mill White Sugar	25Kg	6.83	6.89
RIGMW50KX1	Ramu Mill White Sugar	50Kg	13.05	13.16

Subsequent to the declaration of these margins, the Commission has been conducting random price inspection on wholesalers and retailers to ensure self prices are not being marked above the regulated margins. To some extent, there is potential for wholesalers and retailers in both competitive and less competitive environment to price above the regulated margins.

In the other pricing reviews undertaken by the Commission, it was noted in those reviews that despite the existence of the maximum wholesale and retail margins, it appears that most wholesalers and retailers do not price up to the maximum margins due to threat in competition. The extents to which these margins have been applied have varied considerably depending on product turnover of the relevant goods being sold.

As stated above, this review will have to determine whether continuation of these wholesale and retail margins will continue or not, and, if they were to continue, should they continue in their current form, or should regulation take a different form.

The Commission seeks comments from the industry and relevant stakeholders on whether regulation of wholesale and retail margins should continue or not, and if regulation were to continue, should regulation continue in its current form or should regulation take a different form?

Specific question on the regulation of wholesale and retail margins

- Please provide details of actual gross margins earned by wholesalers and retailers? Do sales of particular products earn higher gross margins than others? Please provide details.

- Do regulated margins impact on wholesalers and retailers set their prices? Please provide details.

- Please provide details of the profitability of wholesalers and retailers. What is a typical operating profit (profit/turnover) range?

- What are the average margins earned by integrated wholesalers-retailers? Do particular products earn higher margins than other products? Please provide details

- Please provide details of the profitability of integrated wholesalers-retailers. What is a typical operating profit (profit/turnover) range?

- Please provide details on the profitability of fully integrated manufacturers-wholesalers-retailers. What is a typical operating profit (profit/turnover) range?

3.0 ISSUES AFFECTING THE WHOLESALE AND RETAIL INDUSTRY

This section provides an overview of some of the issues which the Commission considers to be relevant in undertaking this review. Although the Commission may not necessarily devote considerable attention to these issues, the Commission will be mindful of them when making policy recommendations to the Government. These issues include;

- Government policy – current policy which have a direct and indirect impact on the wholesale and retail sector
- Transportation – the role and impact of the transportation industry on the wholesale and retail sector
- Industry Outlook
- Law and Order
- Staff and Employee protection requirement, and
- Health and Quarantine requirements

These factors influence the price of all retail and wholesale goods. However, at the same time these factors are often cited by service providers as issues which are outside their control. While outside the direct control of merchants it is important to consider the full impact of each on the underlying price of goods. Each factor has the potential to explain some of the price differences between major centres such as Port Moresby and regional areas. The Commission will be seeking to quantify these differences as part of this review.

The above issues are discussed further below.

3.1 Government Policy

The Papua New Guinea Government believes that the key to economic growth is the development of private sector investment both domestically and abroad. The Government is also aware that in order to attract that investment, it must put in place a policy framework which will bring about that development, including its plans to enhance the manufacturing sector and boost export figures under an export-led Economic Recovery Program.

3.1.1 National Investment Policy

The National Investment Policy provides guidelines for the pursuit of economic development through the implementation of investment projects in the country.

The Policy's Volume I and Volume II were prepared in 1998 and 1999 respectively. It is currently undergoing a review towards formulating the National Investment Policy Volume III in consultation with all the stakeholders, including the private sector. Volume III of the Policy will define the core policy objectives and strategies of the commerce sector and further boost economic growth through structural reforms that remove barriers to investment and support infrastructure development.

3.1.2 Medium Term Development Strategy 2005 - 2010

The Medium Term Development Strategy (MTDS) charts the course of reforms in the public sector in the 21st Century. The MTDS translates the means to overcome ineffective governance and bring about development as defined under export-driven economic growth, rural outgrowth and poverty reduction. The resource owners in Papua New Guinea are encouraged to mobilise their resources, including land, to drive the development process to achieve higher standards of living.

3.1.3 Industrial Development Policies

The main thrust of the Government's economic development and industrial policies is aimed at increasing the value and volume of value-added products. Government policies encourage the development of PNG's non-mining sectors including manufacturing, renewable resources such as agriculture and fisheries, and business services, to promote economic self-sufficiency. The promotion of non-mining sectors of the economy ensures that economic growth can be sustained after the depletion of mineral resources. The policies focus on the industries and business, particularly the private sector investments to create employment and achieve economic growth.

The implementation of industrial policies remains the responsibility of the various statutory authorities which are established for that purpose within the Ministry of Trade and Industry. These are the:

(i) Investment Promotion Authority (IPA)

- Small Business Development Corporation (SBDC)
- Industrial Centres Development Corporation (ICDC), and the
- National Institute of Standards and Industrial Technology (NISIT) through which quality control procedures can be addressed. New ventures can rely upon NISIT for research assistance and information on development and transfer of technology.

(ii) Small to Medium Enterprise Policy

The Small to Medium Enterprise (SME) Policy aims to promote the development of small to medium enterprises in PNG in relation to the transfer and adoption of appropriate technology and the encouragement and strengthening of the linkages between SMEs and their support institutions. The main objective is to instil business culture within the SMEs and ensure their long-term sustainability.

(iii) Tariff Reduction Program

The intention of the tariff reduction program which began in 1999 and further review in 2003 and 2007 respectively was to encourage a more efficient and productive private sector through greater exposure to international competition.

The Commission seeks comments from the public and any interested parties on the scope of policies with relation to promoting Competition and protecting consumer interest.

3.2 Transportation

The vertical integration between a number of these business, linking not only wholesaling and retailing, but also shipping, general transport, importing, and associated activities, raises questions about the level of competition that occurs in the retail and wholesale market for general consumer goods. In general many of the retail outlets are located in remote or rural areas where there may be limited alternative retail access, and consumers have limited opportunity to exercise any choice in their shopping activities.

The Commission seeks comments from the public and any interested parties on the level of competition in the supply chain especially on;

- **Domestic Freight Rates**
- **Prices**
- **Level of supply in terms of range, quality and nature**
- **Competitiveness and the diversity of the supply chain**

3.3 Industry Outlook

In reviewing the wholesale and retail industry the Commission is interested in the likely future direction of the industry, in order to address issues and trends which are likely to emerge over the next ten years. In doing so the Commission is not attempting to forecast market outcomes. However, the Commission is attempting to ensure that all potential market outcomes are considered in the context of a potential improvement in the competitive environment.

The Commission seeks views from stakeholders on the likely developments or changes in the existing structure of the wholesale and retail industry including entry of new service providers, over the next decade.

3.4 Law and Order

Several studies have pointed out that the major impediment to growth of business include law and order problem. Due to high level of crime businesses spend a lot on security costs which may seen as a contributing factor to the cost pass through pricing methodology applied by most businesses.

The Commission seeks views from stakeholders on the law and order situation with regard to the additional cost in the overall context of the competition issues.

3.5 Staff and Employee protection requirement

In operating a wholesale and retail business, businesses are required to meet certain minimum requirement of staff welfare condition.

The Commission seeks comments and submissions from interested stakeholders on whether or not certain labour laws are being observed

3.6 Health and Quarantine requirement

Certain health and quarantine requirement are necessary in the operation of such business. In particular goods that are imported for domestic consumption have to meet the health and quarantine requirements of the country.

The Commission seeks comments and submission on the minimum health and quarantine requirement

1. APPENDIX

Appendix A Official Terms of References

MINISTRY OF TREASURY
Office of the MINISTER

Telephone: (675) 328 8870
Facsimile: (675) 323 2239

Valupindi Haus
PO Box 710, WAIGANI, NCD

21st September 2007

Mr. Thomas Abe
The Commissioner and Chief Executive officer
Independent Consumer and Competition Commission
P.O.Box 6394
BOROKO
National Capital District

Dear Mr. Abe

RE: COMPETITION REVIEW OF THE WHOLESALE & RETAIL INDUSTRY DRAFT TERMS OF REFERENCE

I refer to your letter dated 26th June 2007, pertaining to the above matter.

I attach the Terms of Reference under which the review is to be conducted. Please ensure that the Commission proceeds with the Review as directed.

Again, I thank you for undertaking this review and I look forward to receiving your findings.

Yours sincerely;

Hon. Patrick Pruaitch
Minister for Treasury

Terms of Reference

Competition Review of the Wholesale and Retail Industry

The Government, as part of its 2007 Budget Strategy, has announced its intention to undertake a review of competition and general market practices in the Wholesale and Retail Industry in Papua New Guinea.

The review is to focus upon the Wholesale and Retail Industry as it specifically relates to the supply of goods and services for the household sector. In particular, the coverage of the review will focus upon wholesale and retail outlets that are supplying goods and services to household consumers, being goods and services which include but are not limited to:

- Fresh, and frozen meat, vegetables, dairy products and other related consumables
- Tinned and dry foodstuffs
- Bread and other bakery products
- Confectionary
- General household consumables
- Personal health care products
- Alcoholic and non alcoholic beverages
- Tobacco and cigarette products
- Household furniture, furnishings, electrical and non electrical goods
- Clothing and footwear
- Linen, blankets towels, manchester, and related products
- Books and stationary
- Motor vehicles, parts and accessories
- Hardware and related products

The Wholesale and Retail Industry for the purposes of this review will primarily focus upon those activities associated with the operation of retail outlets such as trade stores, supermarkets, village stores, specialist outlets (eg new and second hand clothing outlets, electrical stores, jewellery stores), food outlets and fast food stores, vehicle (new and second hand) retailers, and general merchants supplying household goods and services. Wholesalers primarily supply these types of outlets and the types of products outlined above. The larger wholesalers/retailers in PNG are often vertically integrated businesses, reflecting the emergence of the wholesale and retail activities in the country from the activities of the trading companies that have held significant interest in PNG for many years both prior to and post Independence.

It is not intended that the review will cover all aspects of wholesaling and retailing in PNG. For example, the review is not specifically directed towards the wholesaling and retailing of general machinery, agricultural equipment or similar types of products that are primarily purchased by other industries as inputs to their business operations. However, as many of the businesses that are involved in supplying wholesale and retail services to the household sector are also involved in providing similar services to the general business sector, there will of necessity be some overlap in the investigations to be undertaken as part of this review.

The review is intended to look at a wide range of issues relating to the operation, composition, structure, and regulation of the Wholesale and Retail Industry. The Government notes that the Wholesale and Retail Industry in PNG is comprised of larger firms, often having both retailing and wholesaling activities, smaller businesses, often owned by Papua New Guineans through family businesses or as sole proprietors, overseas owned businesses (often linked with other activities across the country such as transport, agricultural production, manufacturing, logging and forestry activities), and businesses owned by foreign business people living and working in PNG. The vertical integration between a number of these businesses, linking not only wholesaling and retailing, but also shipping, general transport, importing, and associated activities, raises question about the level of competition that occurs in the retail and wholesale market for general consumer goods. In addition, many of the retail outlets are located in remote or rural areas where there may be limited alternative retail access, and consumers have limited opportunity to exercise any choice in their shopping activities.

Certain types of retail outlets also have to adhere to regulatory arrangements relating to matters such as the storage of frozen or refrigerated products, the licensing of electrical and telecommunications products before they can be sold in PNG, and the general licensing of retail stores, often involving Provincial Government licensing arrangements. The review will need to examine these regulatory arrangements to determine to what extent they act to inhibit or prevent competition from occurring in the market place.

The independent Consumer and Competition Commission have responsibility under the *Prices Regulation Act* to implement price control or price monitoring in certain circumstances and after public inquiry. As part of recent inquiries in to the continuation of prices regulation for certain goods, the Commission has questioned the need for the continuation of some form of regulation of the wholesale and retail mark ups on particular goods and services sold to households. The Commission has also raised concerns about the way in which those mark ups are determined. This review will also consider the extent to which there is a need from a competition and consumer protection perspective for the continuation of some form of regulation of wholesale and retail mark ups where the Commission has determined that price regulation is still required. The Review will also consider possible ways in which any from of regulation of these mark up could be determined

In response to the review's conclusions and recommendations, the Government will consider what if any policy response may be required to improve the overall efficiency, effectiveness, and competitiveness of the Wholesale and Retail Industry in PNG including adoption or revision of relevant regulatory arrangements.

Terms of Reference

The principal objectives and deliverables of the review are to:

- Report on the current operation of the Wholesale and Retail Industry in PNG with a particular focus upon:
  - o the size and other characteristics of the domestic industry
  - o the competitive behaviour of participants in the industry,
  - o impediments to competition in the industry, both regulatory and non-regulatory,
  - o the relationship between larger vertically integrated businesses in this industry with smaller retailers and wholesalers,
  - o any particular issues impacting on competition at the wholesale and retail level arising from the spatial characteristics of the country,
  - o the interaction between the Wholesale and Retail Industry in PNG with importers and domestic manufacturers, and
  - o the range of government policy and regulatory requirements impacting on the industry, including the consistency in these regulatory requirements at the national and Provincial government level across the country
- Identify issues and areas where Government action may be appropriate to improve the overall competitiveness, efficiency and effectiveness of the Wholesale and Retail Industry in PNG
- Comment on the need for the continuation of some form of control on wholesale and retail mark ups where the ICCC has determined under the *Prices Regulation Act* that price regulation is required, and identify options that could be used to set mark ups should there be an need for the continuation of some form of regulation in certain instances and for certain goods and services
- Make recommendations on what action by Government may be appropriate to rectify any problems in the current structure, regulation and operation of the Wholesale and Retail Industry with a view to improving competition and competitiveness in the industry.

The review will:

1. Review and report on the current operation of the Wholesale and Retail Industry in PNG including but not, limited to:

   a. The existing structure, size, ownership and operation of the industry;
   b. The degree of competition between wholesalers and retailers, taking into account the regional and locational issues that will impact on competition;
   c. Likely developments or changes in the existing structure of the Wholesale and Retail Industry including entry of new wholesalers and/or retailers in the foreseeable future.
2. Review and report on the current regulatory arrangements within or applicable to the industry, including but not limited to:
   a. The business licensing requirements for wholesalers and retailers, including but not limited to Provincial Government licensing arrangements;
   b. Health or related requirements on wholesalers and retailer;
   c. Other consumer protection laws and requirements that may impact on the operation of businesses in this industry (including the *ICCC Act* and the *Prices Regulation Act*);
   d. Staff and employees welfare protection requirements.
   e. Overall impact of regulations on the cost of doing business
3. Review and report on current practice in setting wholesale and retail margins within the industry, including:
   a. The importance of 'product turn' in determining margins;
   b. The extent to which margins on similar products vary between outlets of the same retailer situated in different locations;
   c. The use of 'loss leaders' to attract customers to a particular store;
   d. The use of volume discounts in supplying retailers or wholesalers:
   e. The implication for pricing practices of businesses being vertically integrated as distinct from dealing at arms length between buyers and sellers:
   f. The size of margins generally prevailing in the wholesale and retail sectors, factors influencing them and how they compare with those in comparable economies
4. Advise on the opportunities and potential for the entry of new competitors into the Wholesale and Retail Industry including:
   a. Likely areas for new entry;
   b. Potential impact on the industry;
   c. Pre-requisites for the entry of new participants;
   d. Likely benefits for the national economy.
5. Make recommendations on what if any action can be taken by Government to address regulatory impediments or enhance the prospects for increasing competition in the Wholesale and Retail Industry in PNG, including but not limited to:
   a. Reforming regulatory and licensing arrangements;
   b. Removing other barriers to entry by new competitors into the industry;

c. Enhancing the countervailing power of consumers and users of the industry's services.

6. Provide observations on methods that the ICCC might use in the setting of wholesales and/or retail margins for individual goods and services should such regulation be required

Deliverables

The deliverables from this review will encompass the following:

- Verbal presentation with overheads and other summary material on the findings from stages 1 to 3 of the terms of reference as outlined above and preliminary comments on stage 4
    - o To be made to the authorising department and to occur prior to the finalisation of the Draft Report and in ample time for the authorising department to make comments on the findings of these initial stages
- Preparation and presentation of a written Draft Report for consideration and comments by the Government and other interested parties
    - o The presentation to be by way of a public presentation to a select audience and discussion on the Draft Report
    - o Opportunity for submission of written comments on the Draft Report
- Preparation and presentation of a fully documented written Final Report to Government

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Appendix B Overview of Main Legislation

	LEGISLATION	SCOPE
1	***Food and Sanitation Act***	The legislation provides for securing wholesome, sound and safe food for human consumption
2	***Investment Promotion Act***	Provides for the promotion of investment in the interest of national, social and economic development
3	***Internal Revenue Commission Act***	
4	***Fairness Transaction Act***	It provides to give effect to certain transaction to ensure that they operate fairly with out causing undue harm to or imposing too great a burn on, any person and in any way that no person suffers unduly because he is economically weaker than or is other wise disadvantage in relation to other person
5	***Packaging Act***	Provides packaging and for making of the packages in which certain articles are sold and sale of those articles and for related purposes
6	***Trade Measurement Act***	It provides for weights and measures
7	***ICCC Act***	Provides for promotion of competition and fair trading and regulation of prices for certain goods and services and protection of consumer interests
8	***Prices Regulation Act***	Provides for monitoring and regulation for prices of sale and supply of certain goods and services
9	***Bread Act***	Provides for size and weight of loaf bread
10	***Baby Food Supply Act***	Regulate or restricts the right of freedom of expression conferred by section 46 of the constitution so as to protect public health from bad consequences of the unhygienic, inefficient or wrong use of items connected with baby feeding
11	***Business Group Incorporation Act***	For incorporation of customary group for business or other economic purposes and control and regulation of control of these groups
12	***Commercial Advertising Act Protection of Public Interest***	On the aspects of consumer welfare by protecting the public from any untrue, inaccurate, misleading or misrepresentative or unreasonable manner of commercial advertising
13	***Customs Act***	With relation to control of goods
14	***Customs Duty***	With relation to fees charge for importing and exporting of goods