

For information on
23 February 2004

Legislative Council Panel on Economic Services

CONSUMER COUNCIL'S REPORT ON WET MARKETS VS SUPERMARKETS: COMPETITION IN THE RETAILING SECTOR

Purpose

This paper informs Members of the Administration's response and follow-up actions on Consumer Council (CC)'s *Report on Competition in the Foodstuffs and Household Necessities Retailing Sector* (the Report).

Background

2. On 11 August 2003, the CC released the Report which advanced the view that wet markets were gradually declining vis-à-vis supermarkets and proposed that the Government should initiate action to revitalize the wet markets. In view of the complaints on supermarkets regarding alleged anti-competitive conduct, the Report suggested that the foodstuffs and household necessities retailing sector should institute a self-regulatory mechanism to deal with competition-related complaints.

3. The findings and recommendations of the Report are extracted at **Annex A**. They relate to the following three main areas –

- (a) competition in the foodstuffs and household necessities retailing sector, handling of complaints of anti-competitive practices and assistance to small retailers in this sector;
- (b) operations of wet markets managed by the Food and Environmental Hygiene Department (FEHD); and

- (c) operations of wet markets and retailing facilities managed by the Housing Authority (HA).

The Administration's follow-up and response to the Report

4. Relevant bureaux and departments had studied in detail the findings and recommendations of the Report and convened a meeting with the CC and the Hong Kong Retail Management Association (HKRMA) with regard to the Report in August 2003. The HKRMA expressed the trade's concern, and requested the CC to clarify the following two points in its press statement on the Report,

- (a) the two major supermarkets together accounted for over 70% of the "relevant" market (a duopoly); and
- (b) despite deflation, the two major supermarkets had increased the list price of their goods by about 1.5% during the 1st half of 2003 vis-à-vis the same period 2002 (abuse of their dominant market position).

5. The CC acknowledged at the meeting that, with hindsight, it should have inserted a footnote in the press statement to clarify that the 70% share referred to "the relevant market", which meant in fact only supermarket chain stores and supermarkets in the department stores but **excluded convenience stores, drug stores and wet markets etc.** The CC also agreed at the meeting that there was room for improvement in the methodology of the pricing surveys in the Report and undertook to consult the trade, including supermarkets, on ways to improve its survey methodology so as to reflect more accurately the price levels of goods sold in supermarkets.

6. Separately, the Competition Policy Advisory Group (COMPAG) had reviewed the findings and recommendations of the Report and deliberated on the analyses and observations at a meeting on 19 September 2003. COMPAG

- (i) was of the view that there was ample competition in the foodstuffs and household necessities retailing sector, and that the issue at stake was not the lack of competition but the competitiveness of various suppliers and customer choice, and
- (ii) agreed to the follow-up actions of the relevant departments.

**LC Paper No. CB(1)1017/03-04(03)
(Revised version - replacement page)**

COMPAG directed that the Government should issue a statement (vide **Annex B**) to the CC detailing the Administration's response to the various findings and recommendations as well as the follow-up actions to be undertaken by individual departments and agencies.

Position to date

7. Follow-up actions outlined in paragraph 17 of the Administration's response at **Annex B** have since been implemented with good progress –

- the HA and FEHD are working actively in partnership with their wet market operators and smaller retailers to enhance the attractiveness of public wet markets through various measures;
- the HA's divestment preparatory work, which plans to transfer its retail and carparking facilities to the private sector through a real estate investment trust, is progressing satisfactorily; and
- in response to the *Guidelines to maintain a competitive environment and define and tackle anti-competitive practices* promulgated by COMPAG in September 2003, the HKRMA has taken concrete steps to encourage voluntary discipline in the relevant sector, and is in the process of developing a code of conduct for the sector to promote competition.

Bureaux and departments will consult and report progress to COMPAG.

Advice Sought

8. Members are invited to note the Administration's response and offer their views on follow-up actions by the Administration to the Report.

Economic Development and Labour Bureau
February 2004

COMPETITION IN THE FOODSTUFFS AND HOUSEHOLD NECESSITIES RETAILING SECTOR

FINDINGS AND RECOMMENDATIONS

Hong Kong will benefit from a vibrant food retailing market with multiple operators and where competitive choices are available.

There is a strong case for government to take proactive action in order to minimize the economic impact of the gradual decline of wet markets through re-engineering the government's involvement in the wet market sector and retraining of the workforce.

Preface

1. This Consumer Council study seeks to:
 - (a) examine the various areas in the foodstuffs and household necessities retailing sector, focussing on industry trends and development, government regulations, the state of competition in various markets, and allegations of unfair and anti-competitive conduct;
 - (b) raise questions for public debate on issues that the Council has identified as worthy of further discussion; and
 - (c) offer some practical suggestions as to how the issues that have arisen over the past few years can be appropriately addressed, as Hong Kong enters the first decade of the 21st century.

Industry Overview

2. Since the Council released its first study into food retailing and distribution in 1994, with special reference to supermarkets, there have been a number of significant developments in the industry.
3. The Council's analysis has revealed (amongst other things) that:
 - (a) Whilst wet markets currently have a significant share of the fresh food sector, there are indications of a gradual decline in consumer patronage due to a concern with the shopping environment, in terms of cleanliness and comfort that can be addressed. In the absence of appropriate measures there will be a difficulty for this sector to counter the increasing market share by supermarkets offering similar products and services.
 - (b) There is a prima facie concern with the market share held by the two largest supermarket chains in the packaged foodstuffs and household necessities sector.
 - i. In the six years from 1996 to 2001, there has been a substantial decline of small supermarket operators by approximately 41%.

- ii. From 1993 to 2003, the two major supermarket chains have grown 29% by number of retail outlets (31% for Wellcome and 28% for Park n Shop respectively). Having regard to a number of variables, such as the number of outlets and share of brand names (turnover), they can be considered at the threshold level of market concentration standards in guidelines issued by overseas competition authorities that warrant further attention should any mergers or acquisitions occur in the sector.
 - iii. Market share alone is not by itself indicative of market power. The conduct of market participants, particularly pricing behaviour, is also pertinent. The Council regularly performs pricing surveys of a basket of goods in supermarkets, and these have indicated that supermarket retail prices increased at certain time periods, despite the general downturn in the economy and the retail market. For example, the Council's price survey in 2002, covering five half-yearly periods from January 2000 to June 2002 indicated that there was an upward price trend at supermarket chains. The Council's analysis showed that over these periods, there had been an increase of 3.6% in average list prices of a selected basket of goods, and a relatively smaller 1.5% increase in prices for the same goods when the discount price was taken into account. In the most recent Council price survey for 2003, the average list prices of a selected basket of goods went up by 1.5% during the first half of 2003 compared with the same first half of 2002. Taking discount prices into account a slight decrease of 0.8% was recorded. One supermarket chain suggested that consumers might have benefited from the use of coupons and from multi-pack discounts.
 - iv. Notwithstanding the above pricing observations, it has been pleasing to note that during the recent SARS crisis when some traders exploited the early scarcity of protective masks by charging exorbitant prices, the major supermarket chains and other well established retailers acted as a stabilising force in the market for the public good. They achieved this by quickly meeting demand for the masks and offering them at prices substantially lower than the exploiting traders. This is to be commended.
 - v. Similar to the experience of other comparable advanced economies, complaints have also been levelled at major supermarket chains by other businesses. For example, there have been complaints that market power is being exerted over suppliers to the effect that:
 - a) existing competitors may be deterred from engaging in vigorous price competition, and which
 - b) raises doubts as to the probable success of future new entry.
4. In correspondence with the Council, both supermarket chains denied exerting market power over suppliers. The Council is not a competition authority with powers of investigation and is therefore unable to establish the veracity of the allegations. Rather than having a competition authority with general oversight of

the economy, the Government takes a sector specific approach to addressing complaints of anti-competitive behaviour. The relevant government bureaux and departments involved with administering policy with regard to the retailing of foodstuffs and household necessities would therefore have a role in examining the allegations.¹

5. Nevertheless, when these issues have been discussed between the Council and the relevant parts of Government, the response from Government suggests a view that because the complaints or allegations which emerge from time to time usually die down after a while, this may indicate a proper functioning of market forces that has sorted things out. However, a complainant may discontinue pursuing a complaint or dare not publicly come forward, due to other reasons. The Council suggests that an objective examination of complaints of anti-competitive conduct and the extent of control of the retail distribution network and its implications to small traders and suppliers needs to be undertaken by an authoritative body that:
 - (a) has the confidence of sector participants; and
 - (b) will pursue allegations to ascertain whether there are actually detriments to consumer welfare that are going unchecked.
6. As indicated in Chapter 4 of the Council's report, the foodstuffs and household necessities retailing sector has been the subject of detailed examination by competition authorities in other countries which have examined similar allegations of misuse of market power and concerns with high levels of concentration in relevant markets.

Government Policy in the Retailing of Foodstuffs and Household Necessities

7. Whilst there is limited government intervention in the foodstuffs and household necessities retailing sector, government bureaux and departments still exercise a role that has some influence. For example, through licensing various methods of food retailing, allocating land for commercial use, planning retail space for supermarket type retailing operations and wet markets in public housing estates, and in constructing facilities for and managing the operation of public wet markets.

Wet markets

8. Apart from the fact that wet markets are an important competitive element in food retailing, wet markets can also be seen as an integral part of the cultural fabric of Hong Kong and one of the defining features that gives the city its unique character. Importantly, wet markets are also a large source of employment, not only for the actual wet market traders and their assistants, but the many goods and service providers who provide logistical and other support.
9. Various surveys indicate that public and private wet markets enjoy considerable patronage, and substantial numbers of consumers indicate a preference for them. However, this preference is tempered by the concern over the shopping environment. Supermarket chains have taken the opportunity to develop wet

¹ For example, the Government's Competition Policy Advisory Group Annual Report of 2000 – 2001 notes in regard to complaints of anti-competitive conduct that "As a general rule, investigations into and follow up actions on the complaints are carried out by the relevant bureaux and departments." See www.compag.gov.hk.

market type facilities within their premises, recognising the preference that consumers have for wet market produce and the supermarket's ability to satisfy consumer demands for a comfortable shopping environment. Clearly, there is a need for wet market operators to recognise the necessity of improving the shopping environment in order for them to remain competitively viable.

10. Nevertheless, due to the need to fully meet re-siting commitments, some markets managed by the Food and Environmental Hygiene Department (FEHD) have been over-provided with stalls. At the time of their construction there was no critical assessment of how many wet markets were actually required. Little regard was paid to competition posed by nearby markets; either in private developments or by supermarkets in the vicinity.
11. As a result, there is most likely an oversupply of markets across the territory and clustering of a number of markets in the same location. This has also affected the occupancy rates and in some cases led to sub-standard stall sizes in some markets. In addition, most of the tenants, being former hawkers re-sited into the public markets managed by FEHD, have not been able to adapt to the enclosed market environment. They find it difficult to compete with the new format and style of business practices, such as tidiness and clear price labelling. Since they and their offspring have the right to operate their business in the public market in perpetuity and as they are only paying below market rent, this gives little incentive to enhance their competitiveness.

What Needs to be Done

12. Hong Kong is becoming increasingly aware of the need to creatively manage the changes necessary to meet the economic challenges it now faces. One of those challenges is finding the appropriate way to address the disadvantage in the wet market sector as a competitor to supermarkets. If the sector was to contract by a large degree, whilst Hong Kong remains in the current economic "low tide", the consequential large-scale dislocation of the unskilled workforce will add to the current historically high unemployment rate.
13. Questions therefore arise as to:
 - (a) whether a decline should be accepted as an inevitable consequence of changing consumer demands and the current operators' inability to match the resources of supermarkets; and hence it should be left to those small traders to struggle for their survival; or
 - (b) whether some measures should be taken to assist the traditional wet market sector to adapt to change and remain viable competitors, thereby reducing the dislocation that could occur and ensuring that a cultural characteristic of Hong Kong remains; albeit in a somewhat altered form.
14. Needless to say, managing and facilitating the process of change is a better strategy than having to deal with unwanted and undesirable outcomes in the future. In a way, the evolutionary process of the food retailing sector today appears to be taking a similar course to the restructuring of Hong Kong's economy ten or more years ago; from a manufacturing-based to its current service-based economy. Many entrepreneurs have attained great success moving their manufacturing bases to the Mainland. However, the issue of retraining and employment of the dislocated low skilled labour force has emerged and remained the responsibility of the government. While dislocation

of workforce as emerged from the study is not a consumer issue, the decline of the wet market industry will affect consumer interest in product choice, price and quality. Hence, the Council is obliged to point this out.

15. The Council puts forward the view that there is a strong case for proactive action to be taken to minimize this dislocation through, where economically feasible, the re-engineering of the wet market sector and retraining of the workforce.
16. Government could perform a facilitation role to help create a vibrant and competitive environment for market participants. The Government currently plays an important proactive role through investing in road construction and developing other infrastructure. For example, the preparation of land intended for residential and commercial developments, and for the airport and container terminals. In the same way, measures can be taken to provide a favourable environment, through pro-small business policy initiatives and other measures for market participants, in the foodstuffs and household necessities retailing sector.
17. This is in line with the Government's vision as noted in the 2002 Budget speech where it was noted that:

*".....economic activities in the local community closely linked to our daily life are also important. This local community economy covers a wide range of activity, including cultural, recreational, sports, social and personal services; and there are many different types of players, such as small traders, local domestic helpers and fitness instructors. Development of the local community economy can promote domestic consumption, create employment opportunities and highlight Hong Kong's unique characteristics".*²
18. There are four areas of concern in the foodstuffs and household necessities retailing sector that the Council believes should be addressed. They are as follows:
 - (a) Improving the efficiency of the Hong Kong foodstuffs and household necessities retailing sector.
 - (b) Ensuring diversity, whilst maintaining traditional strengths, in fresh produce retailing.
 - (c) Maintaining a level playing field, responsive to the needs of all competitors.
 - (d) Ensuring that consumers can have trust in the market place.
19. The Council's recommendations in this regard are addressed below. It is to be emphasized that the Council is not calling for direct subsidy; nor is it advocating direct government intervention in markets, beyond what Government is currently doing. Neither does the Council intend to penalize success in the supermarket sector. The Council is advocating for an environment that ensures a vibrant marketplace and a win-win situation for business and consumers alike.

² Budget Speech March 2002, paragraph 31.

QUESTION 1. – WHAT ARE THE BEST MEANS TO IMPROVE EFFICIENCY IN THE FOODSTUFFS AND HOUSEHOLD NECESSITIES RETAILING SECTOR?

20. There is a disparity in resources and expertise available between large retailing chains and small traders insofar as their means to improve efficiency. While supermarkets appear to be readily adapting to the challenges ahead for the sector, the same cannot be said for small to medium enterprises such as wet market traders.
21. There is a trend in advanced economies to target assistance to small and medium enterprises (SMEs) rather than leaving them entirely to their own devices when faced with substantial market power held by other larger competitors. For example, the Australian government has issued a report regarding assistance to be given to SMEs in the agricultural sector *Securing the Future of Australian Agriculture*³ and the Australian Competition and Consumer Commission (ACCC) assists SMEs in a number of ways, such as developing their collective bargaining skills and providing assistance when SMEs are subjected to unconscionable conduct in business transactions.⁴ The United Kingdom (UK) also issued in January 2003 a report *Competitive Analysis of the Retail Sector in the UK* where it is suggested that government should investigate how best to enhance the skill set of smaller retailers in terms of the supply chain and other practices.⁵
22. Further, in other large metropolitan economies, such as New York and Boston, the city governments have schemes to revitalize commercial streets by stimulating private investment, reducing vacancies, improving the commercial environment and increasing profits for local businesses. Some years ago, the Boston municipal government saw the need to reform the small business sector and appointed a specific task force to come up with a plan to revitalise the sector, and funding and technical assistance to help small operators.⁶ To improve its city image, the Shanghai government helped car cleaners in setting up a co-operative. After having gone through training, a modernized workforce emerged and major streets were rid off the untidy scene created by an untrained and disorderly workforce. Under a project dating as far back as 1979, the Taipei City Government has been modernizing the Nanmen market, a 105-year-old traditional wet market. Today the place is seen as a clean shopping emporium with new facilities and a modern style of management. The booths are orderly and have standardized signboards, and the entire market utilizes a reliable food refrigeration system. After the improvements were made, Nanmen vendors saw their sales increase. In 1998, Taiwan's Ministry of Economic Affairs launched a five-year program to upgrade the traditional food and vegetable markets and

³ The report can be downloaded from website <http://www.ncc.gov.au/pdf/CIComAg-001>.

⁴ See Section 51AC of the Australian *Trade Practices Act 1974* – Unconscionable conduct in business transactions, and the ACCC's Small Business Program. See www.accc.gov.au.

⁵ The report, issued in January 2003, can be downloaded from website <http://www.dti.gov.uk/retail/index.htm>.

⁶ In 1995, Mayor Thomas M. Menino created Boston Main Streets, the first urban, multi-district Main Streets program that provides funding and technical assistance to 21 neighbourhood-based Main Streets districts throughout the City of Boston. The program focuses its effort on providing merchants and community residents with the tools for their historic commercial districts to compete in today's market. The Main Streets program helps the local districts capitalize on their unique cultural and historical assets while focusing on the community's economic development needs. Examples include small business recruitment, business retention and addressing competition from shopping malls and discount retailers.

solve the problem of illegal markets throughout Taiwan. The Nanmen market serves as a model for the island wide modernization campaign.⁷

23. The Council is of the view that some specific targeted assistance could be given to revitalize the wet market sector into an efficient and innovative industry, given the desire by consumers for competitive choices and the level of employment that these small enterprises bring to Hong Kong.⁸
24. The Council is pleased to note that FEHD is providing training to wet market operators. The purpose of the training is to improve the customer service aspect of market stall lessees' interaction with their customers, and to sharpen their awareness as to the importance of food safety and environmental hygiene in a market setting. In addition to this, the Government's Small and Medium Enterprise Office (SMEO) under the Trade and Industry Department and the Trade Development Council have both developed commendable business promotion and training activities for SMEs. The Council believes these initiatives, and efforts of other institutions, can be utilised to assist in improving the competitive position of participants in the foodstuffs and household necessities retailing sector. For example, by promoting the utilisation of state of the art management information systems.
25. The Council recommends that the SMEO or other relevant institutes develop specific programmes aimed at assisting small traders in the foodstuffs and household necessities retailing sector.
26. Wet market operators should be alerted to the threat to their continued survival and their responsibility to understand the need to make a paradigm shift in the way they operate. For example,
 - (a) a "wet" market for fresh produce need not always be so wet as to irritate and deter consumers from patronising the area;
 - (b) operators must upgrade their knowledge and skills on technology that can provide efficient business solutions for supply side management;
 - (c) identify what service levels are necessary to improve competitiveness, such as issuing receipts and longer opening hours, in order to increase the customer base.

QUESTION 2. – HOW TO ENSURE DIVERSITY WHILST MAINTAINING TRADITIONAL STRENGTHS IN FRESH PRODUCE RETAILING – GOVERNMENT'S FACILITATION ROLE?

27. Hong Kong will benefit from a vibrant food retailing market with multiple operators, where competitive choices will be available. A rethink of government policy is warranted at this critical point.
28. The Housing Authority (HA) and FEHD are both involved in maintaining the traditional role that wet markets have in serving Hong Kong consumers with fresh produce. A major reason for their involvement is to serve the public desire

⁷ See website <http://www.taiwanheadlines.gov.tw/20000418/20000418fl.htm>.

⁸ Asia Pacific Economic Cooperation every year has Small and Medium Enterprise Ministerial Meetings on policy development towards small enterprises, discuss the suggestions from the SME Working Group. It also creates APEC SME Network of Networks to facilitate information exchange for SME in the region.

for buying fresh market produce. In the case of FEHD, wet markets serve to house those persons holding a hawker's licence. The sector is characterised by many individual operators who cannot afford to rent private shop premises. They rely on government to ensure that there is the necessary infrastructure and availability of low cost market facilities for them to continue to offer a service. In effect, both government departments have for some time taken on a role as major developers, or entrepreneurs for the maintenance of the wet market sector.

29. The fact that government has historically played a role in maintaining wet markets, and continues to allocate government expenditure in maintaining related assets, means that from a public policy point of view it has a justifiable role in addressing the questions now being posed. Moreover, because the wet market assets are publicly owned, the Council believes it is incumbent on the Government to ensure that:
 - (a) the decline of the wet market sector (if it is accepted to be inevitable) is managed in an orderly fashion; or
 - (b) if it is agreed that wet markets are important and should be preserved in some way, that the evolution is efficiently managed.
30. There should be a change in focus which goes beyond the mere provision of low cost space for stalls, because successful food retailing now calls for upmarket promotion strategies, cost efficient sourcing of products, and a strong emphasis on customer service. Information available to the Council indicates that HA and FEHD have devoted efforts in devising new strategies for wet markets and recognize the need for, and are planning to improve and upgrade facilities for their wet markets so as to maintain the commercial prospects for these developments.
31. The Council recognizes that the situation is different between HA and FEHD. Whereas the relationship between the small store operators and HA is that of lessee and landlord, FEHD carries with its market the legacy of re-housing unlicensed hawkers. Changes in these markets will have implications of tenure. The move to revitalize business need the support and ownership of the store operators.
32. The Council believes that Government should employ the creativity and entrepreneurial skills found in the private sector to manage the current markets, for this purpose.
33. The Council notes the proposal by HA announced in July 2003 to sell its shopping malls (which include wet market facilities) and car park assets. The HA's stated intention behind its proposal is to divest the assets in the interests of realising the monetary value in those assets. The Council sees this as a good opportunity to ensure that the assets are used in such a way that their current important role in providing competition to supermarket chains is maintained and developed in a way that ensures continued strong competitive pressure on supermarkets into the future.
34. Prior to the announcement by HA, the Council had formulated the following options in mind:

Option one – unencumbered sale of government owned assets

35. The publicly owned wet market assets of FEHD and HA (including its other non wet market commercial properties)⁹, could be sold on the open market and their use left to the new owners as they see fit. A modification would be to grant a lease with eventual transfer of ownership upon satisfactory demonstration of leadership within the trial period.
36. This is similar to HA's current arrangement of granting a lease to a single operator. The difference lies in ownership; as once the market is in the hands of a commercially oriented owner, the owner will assume full responsibility towards the decoration, maintenance and management of the market; and make appropriate investments.

Option two – establish wet market co-operatives

37. The individual retail areas of wet market complexes owned and operated by FEHD and HA could be sold to wet market traders. As owners of their units (with the Government remaining as the owner of the common areas) they could operate the wet market complex as a co-operative under a Deed of Mutual Covenant. The merit is the total involvement of the stall operators who would try their best to succeed. In so doing, the workforce will also be retained.

Option three - creation of wet market development corporation

38. A statutory corporation could be created to act as an incubator for the continued development of the traditional wet market in Hong Kong.¹⁰ The statutory responsibility of the entity would be to develop wet markets into a new type of shopping experience that uses the strengths of wet markets, i.e. freshness, multiple choices in fresh produce, as a basis for successfully evolving this mode of shopping into a form suited to meet current and future consumer aspirations. The corporation could:
- (a) have a statutory term of reference to ensure the continuation of traditional wet market shopping, and manage its evolution to meet the current and future aspirations of Hong Kong consumers and society;
 - (b) have as its asset base current wet market and commercial properties infrastructure owned by FEHD and HA;
 - (c) utilise existing staff resources of both departments¹¹ that are currently deployed for management of commercial activities; and
 - (d) be privatised at a future date.
39. **The above options are raised to stimulate public discussion on the pros and cons of the options and is by no means exhaustive. As discussed earlier, there is a need for a paradigm shift by wet market operators as well as the government's policy objectives. The Government may consider running a pilot project for one or two of the above options, or to have the**

⁹ The Council recognises that FEHD assets would most likely encounter legal encumbrance problems.

¹⁰ For example, an analogy can be drawn with the proactive policy that government has taken in the information technology sector where it is using private sector initiatives through a statutory corporation, the Hong Kong Science and Technology Parks Corporation, in its attempt to develop the Hong Kong economy into an IT hub.

¹¹ FEHD and Housing Department (HD). As recommended by the Review of Institutional Framework for Public Housing Report, the former Housing Bureau and the former HD merged on 1 July 2002 to form the new HD. The re-constituted HD continues to provide executive support to HA.

pilot projects co-exist in parallel. Experiences gained will point to the way forward.

40. An important point is that the operators of the large supermarket chains must not be awarded the tender for these markets or involved in managing the evolution; otherwise it would defeat the objective of increasing the diversity in fresh food retailing.

QUESTION 3. – HOW TO MAINTAIN A LEVEL PLAYING FIELD?

41. The Council has received complaints from various parties concerned with alleged anti-competitive conduct in the supermarket sector. It has exchanged correspondence and held meetings with related parties in attempts to establish the veracity of the allegations. The allegations have ranged from attempts to induce resale price maintenance, and refusals to supply. Not being an investigative body with powers to obtain information, the Council can only conclude at best that there is anecdotal evidence to indicate that pressure has been exerted on suppliers to discipline competitors that threaten a preferred level of price competition in the market. Such conduct has been considered, in the Government's *Statement on Competition Policy*, to be a category of anti-competitive practice that may warrant further examination.¹²
42. If Hong Kong had a competition authority that had investigative powers, similar to those existing in other comparable advanced economies, the authority could activate its information collecting powers, where the necessary prima facie evidence and therefore "reason to believe" or "reason to suspect" has emerged.
43. In these circumstances, the authority would be in a better position to obtain information that could establish the veracity of the allegations on refusal to supply, or inducement of resale price maintenance, one way or the other, to a higher standard of proof. In the absence of such an authority, and its regulated information gathering powers, the industry will continue to be subject to innuendo and uninformed opinion, as far as allegations of anti-competitive conduct is concerned.

Self regulatory complaints mechanism

44. The Government has indicated in its *Statement on Competition Policy* a support for industry self regulation as one means to "preserve and enhance free competition". The Hong Kong General Chamber of Commerce (HKGCC) in its *Statement on Competition* urges its members to "refrain from restrictive practices, such as collusive or predatory behaviour that impair economic efficiency or free trade" and encourages specific industries, where possible, to develop through their respective associations, a complaints-handling procedure as well as provisions to deal with non-compliance of their members.¹³
45. Therefore, an option for the industry, or for the HKGCC to consider, is to develop a self regulatory complaints handling body that has the authority to examine allegations of anti-competitive conduct in the foodstuffs and household necessities retailing sector.

¹² See sub section 7(c) of the *Statement on Competition Policy* at www.compag.gov.hk which lists "conditioning the supply of specified products...to the acceptance of certain restrictions other than to achieve assurance of quality, safety, adequate service or other justified purposes".

¹³ See Hong Kong General Chamber of Commerce website www.chamber.org.hk *Chamber Statement on Competition* Clause 6.

46. Alternatively, supermarket operators, being good corporate citizens may consider expanding their current good conduct code, which is principally directed towards customer relations, to include other dimensions, e.g. relationships with suppliers etc. With transparent rules on good practice, the operators would be in a better position to answer what they consider to be unfounded allegations about their conduct.
47. The Council is in the process of creating a *Consumer Protection and Competition Model Code*. The Model Code will comprise "Competition Rules" and "Rules on Structure of a Complaints Handling Committee and Procedure for Assessing Complaints Alleging Anti-competitive Conduct". The Council considers these might serve an appropriate basis for developing such a self regulatory scheme. The Council is happy to offer its assistance in this regard.
48. The Council's preferred option for assessing allegations of anti-competitive conduct is the creation of a general competition law that applies to all economic sectors, similar to that existing in other advanced economies. The above self regulatory mechanism is suggested pursuant to the Government's preferred option as outlined in its *Statement on Competition Policy*, and the realisation by the Council that the Government's current position is not to introduce a general competition law.
49. As a long term solution, the Council is in favour of introducing a competition law framework in Hong Kong; similar to that which exists in other comparable advanced economies. A general competition law would establish legislative boundaries, within "black letter law", as to what standard of behaviour is expected in relation to the range of conduct complained of. Under a competition law framework, with transparent rules and procedures, the various protagonists would be in a position to clarify their concerns, and defences, and there would be public debate on issues such as whether market power actually exists.
50. Moreover, given the increasing concentration of market participants in the supermarket sector, it is reasonable to expect that some government assessment should be made as to what safeguards should be in place to prevent further concentration; particularly if either of the two largest supermarkets should merge. In fact, as noted in Chapter 3, the Government is introducing competition law safeguards to prevent anticompetitive mergers in the telecommunications sector (in the face of telecommunications industry concerns that they are being unfairly targeted). Therefore, from a government competition policy point of view, there is no apparent reason why similar safeguards could not also be put into place for the foodstuffs and household necessities retailing sector. Introducing a general competition law framework would address both the competition safeguard concern and the need for the rules to apply fairly to all in the economy.
51. Problems also arise with regard to allegations of anticompetitive conduct. In the absence of a general framework for examining such practices, it is those with market power who will decide whether and how anti-competitive practices exist in the marketplace. In these circumstances, the disputes that arise between suppliers and purchasers, and competitors, will invariably be settled through withdrawal from the market or the weaker party succumbing to the demands of the dominant market player. The reason being that it is in neither party's interests to prolong a dispute and disrupt supply. Because the peace is negotiated in private, the public interest is not represented.

QUESTION 4. – HOW TO ENSURE CONSUMER TRUST IN THE MARKET PLACE?

52. Consumers suffer if misleading claims and trade malpractices exist in the market place. If the marketing environment is characterised by rivals engaging in misleading conduct, then healthy competition in the market will not exist.
53. It is apparent from reported allegations of frozen pork being passed off as fresh pork¹⁴ that there is a problem with misleading practices in the market place and these practices must be curbed. The Council notes the precautionary measures taken by FEHD in respect of the labelling of imported chilled chicken that will assist consumers to differentiate chilled chicken from fresh chicken. Such proactive measures are to be commended. The Council trusts that continual enforcement of appropriate laws and regulations will curb the problem of misleading conduct in the marketplace.
54. The Government's efforts are also being complemented by industry. For example, a wholesaler accredits a retailer that sells fresh meat on the condition that the retailer observes the wholesaler's standard which is aimed at protecting its corporate goodwill. The Council supports these industry measures as a means of enhancing consumer confidence, and encourages more wholesalers to operate on a similar basis, to ensure that competition can play its part in maintaining high standards of marketplace behaviour.

Concluding Remarks

55. In this study the Council has examined the dynamics that exists in the foodstuffs and household necessities retailing sector and pointed to the gradual decline of the wet market sector. The Council does not intend that success should be penalized in the supermarket sector, rather the Council is putting forward a case that Hong Kong will benefit from a vibrant food retailing market with multiple operators where competitive choices will be available, and a win – win situation can be attained for all.
56. The Council has identified the need for a paradigm shift by wet market operators. It supports government policy makers to adopt new policy objectives and strategies for wet market development, and where financially feasible, the re-engineering of wet market operation and retraining of the workforce. While dislocation of workforce as emerged from the study is not a consumer issue, the decline of the wet market industry will affect consumer interest in product choice, price and quality.
57. We have put forward recommendations and options on these and other issues with a view to stimulating public debate. The Council is not saying these are a panacea for all the problems. Nor is it saying that they are the only options. What the Council is emphasising is that something must be done now if Hong Kong is truly concerned with competition within this sector; with the need to contain our unemployment problem; and in maintaining Hong Kong's competitiveness and truly unique characteristic as Asia's World City.

¹⁴ In 2002, the Council received a complaint by the meat and livestock importer Ng Fong Hong (NFH) alleging misleading sales practices in relation to wet market traders and supermarket operators selling chilled pork as fresh pork. According to NFH, "chilled" pork from Thailand had been mixed together with fresh pork and sold to consumers as fresh pork. NFH stated that this had occurred in many wet market stalls, as well as in at least one supermarket.

The Administration's Response to the Consumer Council's Report on Competition in the Foodstuffs and Household Necessities Retailing Sector

Introduction

On 11 August 2003, the Consumer Council ("the Council") released a Report on Competition in the Foodstuffs and Household Necessities Retailing Sector ("the Report"). The Report –

- (a) pointed out the gradual decline of wet markets vis-à-vis supermarkets and proposed that the Government revitalize the wet markets;
 - (b) noted complaints about anti-competitive conducts by supermarkets and suggested a self-regulatory mechanism to deal with competition complaints in the foodstuffs and household necessities retailing sector; and
 - (c) supported, as a long-term solution, the introduction of a competition law in Hong Kong.
2. The findings and recommendations of the Report relate to the following three main areas –
- (a) competition in the foodstuffs and household necessities retailing sector, handling of complaints of anticompetitive practices and assistance to small retailers in this sector;
 - (b) wet markets managed by the Food and Environmental Hygiene Department (FEHD); and
 - (c) wet markets and retailing facilities managed by the Housing Authority (HA).

The Administration's response

3. Relevant bureaux and departments have examined the findings

and recommendations of the Report. Their general response in respect of the three main areas, vide paragraph 2 is at paragraphs 4 to 16 below. Their responses to specific findings and recommendations are set out in **Annex I**.

Part I Competition in the foodstuffs and household necessities retailing sector, handling of complaints of anticompetitive practices and assistance to small retailers in this sector

Overall competition policy

4. The Government's competition policy is to enhance economic efficiency and free trade, thereby also benefiting consumers. Competition is best nurtured and sustained by allowing the free play of market forces and keeping intervention to the minimum. The Government should not interfere with market forces solely on the basis of the number of operators, scale of operations, share of the market per se, or normal commercial constraints faced by new entrants. The Government will take action only when market imperfections or distortions limit market accessibility or market contestability and impair economic efficiency or free trade, to the detriment of the overall interest of Hong Kong.

5. In line with this policy, the Government maintains a liberal and open regulatory framework in respect of the retail sector. Any person may open a retail outlet in Hong Kong provided that he has obtained a Business/Branch Registration Certificate and the relevant licences for the commodities that he intends to sell. The Government imposes no other administrative barriers.

Competition in the foodstuffs and household necessities retailing sector

6. The Council has adopted the concept of "one-stop shopping" for its competition analysis and identified two separate retail markets –

- (a) a market for fresh produce, with supermarkets and wet markets closely competing with each other; and
- (b) a market for packaged foodstuffs and household necessities, where supermarkets compete with other retail outlets, such as convenience stores, grocery stores, and specialty stores.

7. As far as the fresh produce market is concerned, the Report

has stated that according to AC Nielsen, in 1999, the market share of wet markets vis-à-vis supermarkets in the fresh produce sector was 76%. In addition, according to the Council's surveys in 2001, 70% of the interviewees preferred buying fresh food in wet markets. This shows that wet markets still command a strong demand from consumers and remain the most important source of retail outlets providing foodstuff.

8. As for packaged foodstuffs and household necessities, the Council considered that there is a prima facie concern with the market share held by the two major supermarket chains and that the level of market concentration of the two chains would have reached the threshold level of the mergers or acquisitions guidelines in countries where there are competition authorities. However, in arriving at this conclusion, the Council has only had regard to the turnover shares and number of outlets of **supermarket chain stores** (including those in department stores) and **convenience stores**, and vertical integration into the convenience store sector. The analysis has not taken into account household product stores chains (which are getting increasingly popular), drug stores (which are popular places for the purchase of toiletries, shampoos and other cleansing products), hardware stores, groceries shops and many other small retail outlets. This raises doubts on the validity of the Council's claim that there is a prima facie concern with the market share held by the two supermarket chains in the packaged foodstuffs and household necessities sector. The Commerce, Industry and Technology Bureau (CITB) suggests that the Council should include household product stores chains, drug stores, hardware stores, groceries shops and other small retail outlets in its analysis of market share for the packaged foodstuffs and household necessities market in the future.

9. CITB notes that competition in the retail market is fierce and that there is no need for Government intervention in the operation of the retail market. There are a large number of players in the market, including supermarket chains, supermarkets in department stores, convenience shops, food stores and household product stores. Even if only the number of supermarkets, chain stores and convenience stores are taken into account, the number of outlets of the two large supermarket chains account for 17 % and 15% of the market share ^(Note 1) respectively. In addition, competition exists in the form of price and non-price competition. To cater for the preference of consumers, apart from reducing the selling price of products, many retail market operators try to

(Note 1) Data extracted from page 46 of the Consumer Council's report on "Wet Markets vs. Supermarkets: Competition in the Retailing Sector".

gain a competitive edge by providing longer operating hours, cleaner environment and the convenience of one-stop shopping. Others strive to maintain their niche by providing personal and flexible services to cater for the specific needs of their customers. As a result, consumers benefit from having a wider choice of goods and service which are of better quality and offered at more competitive prices.

Part II: Wet markets managed by FEHD

10. The Health, Welfare and Food Bureau (HWFB) notes that the development of FEHD-run wet markets is inextricably linked to the history of relocating hawkers. The wet markets were built to free streets and public areas from hawking activities, thus eliminating a serious source of problems related to environmental hygiene, food safety and pedestrian obstruction. The FEHD's involvement in the provision of wet market facilities was therefore not primarily driven by economic considerations.

11. The HWFB observes that the Government's involvement in wet market operation is largely due to historical circumstances. There is indeed no economic reason why the private sector should not be allowed to build or operate wet markets/retail facilities. On the contrary, the private sector can more freely and efficiently respond to over- or under-supply of wet market/retail facilities in various localities around the territory.

12. Food safety and environmental hygiene in the wet markets, therefore, remain the Government's foremost concerns. The Government's policy is to ensure that the foodstuffs offered for sale in these markets are in compliance with food safety standards. The Government is also committed to reducing public health risks arising from unhygienic market environment or facilities. The various initiatives announced by Team Clean (i.e. monthly cleansing day & streamlining procedures for termination of tenancy) in early August are a case in point. Being the regulator for wet markets and fresh provision shops, the FEHD has a duty to ensure that the relevant regulations are enforced in an even-handed manner irrespective of the scale and ownership of retail outlets.

13. The HWFB has committed substantial resources to improve food safety and environmental hygiene of FEHD markets and to ensure that publicly funded facilities are put to the best use. For example, it has earmarked over \$600 million in the next few years for carrying out

improvement works to the FEHD markets. The scope of works includes upgrading of ventilation and/or drainage systems, replacement of floor and wall finishes, lighting improvements, upgrading of entrances, signages, escalators, etc. Such improvement works should also help enhance the competitiveness of the markets concerned and their appeal to members of the public.

14. Public markets completed in recent years have already been equipped with air-conditioning facilities. There are currently 106 FEHD markets/cooked food centres, over 20 of which are air-conditioned. New public markets coming on stream in the next three years, namely, Tai Po Market, Wanchai Market and Tai Kok Tsui Market will also be fully air-conditioned. In line with its previous undertakings to the Legislative Council (LegCo) and the stallholders concerned, the HWFB has concrete plans to retro-fit air-conditioning systems to three more markets where 85% ^(Note 2) or more of the tenants support such works and agree to pay the recurrent costs involved.

Part III Wet markets and retailing facilities managed by the Housing Authority (HA)

15. As far as wet markets and retailing facilities managed by the HA are concerned, the report recognizes that a level playing field for fair competition is one of the basic considerations of the HA's allocation policy for retail space, and that the HA has consistently made effort to improve the shopping environment of small retail shops and wet markets, through various initiatives including enhancement of the management model, upgrading the infrastructure of the retail facilities, and retrofitting air-conditioning for wet markets in older estates, etc.

16. The Council also sees the HA's divestment plan in respect of its retail and carparking facilities as a good opportunity to strengthen competition in the retail sector. The HA is actively pursuing the divestment plan. According to the preliminary divestment proposal, initially the management and ultimately the ownership of those HA's retail facilities suitable for divestment will be transferred to a private company and listed in Hong Kong's Stock Exchange sometime in 2004/05. The HA expects that the entrepreneurial skills of the private sector will have a positive impact on the operation of these retail facilities.

^(Note 2) The 85% threshold is required to ensure smooth implementation of the retro-fitting projects. This is also consistent with the 'user-pays' and 'cost-recovery' principles.

Follow-up actions

17. The Government notes that :
- (a) There is ample competition in the foodstuffs and household necessities retailing sector. **The issue at stake is not one of competition but competitiveness, customer choice and preference.** The Government does not see the need for intervention or a competition law for this sector. The Government will nevertheless monitor the situation closely;
 - (b) In line with its approach to encouraging voluntary discipline, the Government welcomes the Council's suggestion of encouraging a self-regulating mechanism within the trade and is ready to render assistance as and when necessary. We will continue to monitor the situation closely;
 - (c) In keeping with Hong Kong's free market philosophy, the Government will continue to provide small and medium enterprises (SMEs), including those in the foodstuffs and household necessities retailing sector, with necessary support to enhance their competitiveness and efficiency. Regarding the proposal for the Government to develop specific programmes for SMEs in the foodstuffs and household necessities retailing sector, the Government is of the view that it will be more cost effective for the trade to come up with worthwhile initiatives and seek funding support from the SME Development Fund. This will ensure that the programmes being developed will meet the needs of SMEs in the sector and will therefore be well received by them;
 - (d) As regards the three options in revitalizing public wet market facilities outlined in paragraphs 35-38 of the Report, namely, (i) unencumbered sale of government-owned assets; (ii) establishment of wet market cooperatives; and (iii) creation of wet market development corporation, the HA is actively pursuing the divestment plan in respect of its retail and carparking facilities. As regards FEHD-run markets, the

Government has no plan to pursue options (i) and (ii) due to intractable practical difficulties identified, but is open-minded about option (iii). The policy orientation and resources commitments will continue to be driven by promotion of environmental hygiene and food safety predominantly;

- (e) While the Government is committed to improving public wet market facilities and encouraging private sector participation, it will pursue these objectives in line with the time-honoured principles of free enterprise and free trade. It will not, therefore, preclude or restrict any market players from tenders or prohibit their involvement in the management of the public markets as recommended in the Report;
- (f) The Government reckons improving the shopping environment is an important attribute in the foodstuffs and household necessities retailing sector. Other considerations such as customer service, sourcing of quality products, promotion and pricing strategy as pointed out in the Report are also important. The HA and FEHD will work in partnership with their wet market operators and smaller retailers to enhance the attractiveness of public wet markets in this direction.

Competition Policy Advisory Group Secretariat
November 2003

The Administration's response to specific findings and recommendations in the Council's report

Handling of complaints of anticompetitive practices through a self-regulatory mechanism or a competition law (paragraphs 41-51)

CITB recognizes that scale of operation or share of the market per se does not determine whether a business is anti-competitive or not. Besides, there is so far no evidence showing that supermarket chains have engaged in anti-competitive acts or have abused their market power to limit accessibility and contestability. Some of the complaints received by the Council may relate to commercial disputes on possible breach of contracts, while others may well be business acts prompted by fierce competition. In general, there is no evidence to prove that these practices are restrictive and detrimental to economic efficiency or free trade.

Self-regulation

2. CITB agrees with the Council's recommendation that there is a role for self-regulation to enhance competition and avoid anti-competitive behaviour within the trade. In this connection, the Competition Policy Advisory Group (COMPAG) has, in consultation with chambers of commerce, trade and industry organisations, as well as the Council, developed a set of guidelines to provide pointers with objective benchmarks and principles to assess Hong Kong's overall competitive environment; define and tackle anti-competitive practices; and ensure consistent application of Hong Kong's competition policy across sectors. The set of guidelines promulgated by COMPAG would be the appropriate basis for developing a self-regulatory mechanism for the retail sector.

3. In addition, the Government encourages retailers, including supermarket operators, to embrace competition through voluntary action. As good corporate citizens, supermarkets may wish to consider stepping up communication with all stakeholders so as to ensure a level playing field for all. The Government will continue to monitor the situation in conjunction with the Council and is prepared to render assistance as and when necessary.

4. With enhanced self-regulation, the Government does not see a need for a competition law or a competition authority in the retail sector for

the time being. In fact, there is no conclusion among the international communities that a general and all embracing competition law is the panacea to anti-competitive behaviour or to ensure fair competition.

Specific assistance could be given to small traders in foodstuffs and household necessities retailing sector by the Small and Medium Enterprise Office or relevant institutes (paragraphs 24 and 25)

5. Many of the wet market and retail service operators are small and medium enterprises (SMEs). CITB's policy is to provide SMEs, including those in the foodstuff and household necessities retailing sector, with necessary support to raise their competitiveness and efficiency while keeping in line with our free market economic philosophy of "maximum support, minimum intervention".

6. For example, the Trade and Industry Department (TID) has set up funding schemes to help SMEs secure loans from lending institutions to address their financing needs and enhance human resource development. Also, it administers the SME Development Fund (SDF) which provides funding support to trade and industrial associations, industry support organisations, professional bodies and research institutes for implementing projects which are conducive to enhancing the competitiveness of SMEs in general or in specific sectors. The department also provides SMEs with a comprehensive range of services through the Support and Consultation Centre for SMEs (SUCCESS), including information dissemination, seminars, mentorship programme, and advisory services.

7. TID will continue to work closely with SMEs and provide them with assistance where appropriate. On the other hand, in order to stay competitive, market operators may also wish to review their business strategy in the light of the changing business environment and consumer taste, upgrade their software and hardware, and improve on efficiency. Trade and industrial associations and industry support organisations which have come up with projects for helping SME market operators enhance themselves may consider seeking funding support from the SDF to implement the projects.

Wet market operators should be alerted to the need to make a paradigm shift in the way they operate (paragraph 26)

8. It is in fact HWFB's policy and strategy that sitting tenants have a pivotal role to play in enhancing the competitiveness of goods sold and services rendered in keeping with changing customer needs. With a view to

sharpening their awareness of the importance of food safety, environmental hygiene and a client-oriented approach in market settings, FEHD has provided customer service training for stall tenants of 10 public markets earlier this year. Similar training sessions will be run for tenants of another 10 markets later this year. FEHD will continue to alert sitting tenants to their responsibility in maintaining the viability of public markets concerned and the importance of adapting to customer needs in everyday business operations.

Government should employ the creativity and entrepreneurial skills found in the private sector to manage public markets (paragraph 32)

9. HWFB and FEHD have been pursuing initiatives in this direction. For example, FEHD has implemented a Market Manager Scheme in four public markets, namely, Fa Yuen Street Market, Hung Hom Market, North Kwai Chung Market and Smithfield Market, whereby well-qualified and experienced personnel from the private sector are engaged to enhance management of the markets. The Department is also looking into the feasibility of out-sourcing the management of several markets within a geographical cluster to private property management companies in a bid to improve cost-effectiveness in running the market premises.

It is incumbent on the Government to ensure that the decline of the wet market sector, if accepted to be inevitable, is managed in an orderly fashion (paragraph 29)

10. HWFB observes that of the 80-odd markets managed by FEHD, the majority are viable ones capable of survival in face of keen competition from supermarkets and other private retail facilities. There are admittedly a small number of FEHD-run markets with relatively high vacancy rates. FEHD is examining the viability of these markets with a view to identifying those that do not justify further resource commitments by the Government. In the interest of judicious use of public resources, the Government may need to close down a few markets with serious insurmountable viability problems.

Three options in revitalising public wet market facilities (paragraphs 35-38)

11. The Council suggests that the Government should consider three options in revitalising public wet market facilities, namely, (i) unencumbered sale of government-owned assets; (ii) establishment of wet market cooperatives and (iii) creation of wet market development corporation. HWFB has the following observations on these options:

Option (i) – “unencumbered sale of government owned assets”

HWFB is in principle agreeable to, and would facilitate, private sector participation. However, for historical reasons, the rentals currently paid by most market tenants are well below the ‘Open Market Rentals (OMR)’ assessed by the Rating and Valuation Department periodically. Over the years, the Administration has experienced substantial resistance from the LegCo, District Councils and stallholders concerned in seeking to bring the rentals back to the OMR level. HWFB’s assessment is that sitting tenants will strongly object to the takeover by the private sector for fear that the stall rentals will sharply escalate in consequence. Moreover, for a deal to be attractive to potential buyers, they would need much flexibility in the eventual selection of tenants, determination of stall rentals, trade mix and venue/stall layout, etc. This is tantamount to having to buy out or relocate all existing tenants before the market is sold, and this will inevitably require lengthy consultations and negotiations with stakeholders.

Option (ii) – “establish wet market co-operatives”

HWFB’s assessment is that most incumbent stallholders are unlikely to be willing to incur additional expenses to buy their own stalls unless the prices are set at unreasonably low levels. Moreover, given the diverse background of individual stallholders and the wide-ranging rentals they are paying, it would be a formidable task for them to reach a common goal to form a cooperative without additional government subsidy. Even if the incumbent traders could agree to form a coordinating body, this option could not resolve the fundamental problem of over-provision of stalls in many FEHD markets.

Option (iii) – “creation of wet market development corporation”

HWFB is open-minded about this option. HWFB considers that for the initiative to be realizable, the new statutory body must be provided with the requisite financial, institutional and professional capacities to grapple with the complicated implementation issues and vested interests involved. HWFB is

prepared to work with whatever agency/task force entrusted to take forward this initiative.

Balancing the allocation of market facilities for different distribution channels is crucial to the development of competition (Chapter 3, paragraphs 3.28 to 3.32 [extract at Annex II])

12. On the HA's policy which permits service-style provision of fresh food in superstores, the report expresses concern that the number of wet market stalls will likely drop with an expected rise in the superstores' market share in the fresh food sector, and remarks that a policy objective to balance the allocation of market facilities for different distribution channels is crucial to the development of competition.

13. The HA considers that the scale of retail provision and trade mix of HA's retail facilities have to be determined with regard to a number of factors including the catchment areas, availability of compatible facilities in the neighbourhood, and customer patronage, and that these factors have also to be balanced with competition considerations. Admittedly the traditional wet markets and small retail shops are facing a challenge from chain superstores. However, HA has to duly take into account consumers' preference as far as the allocation of HA's retail space is concerned if the operation is to remain commercially viable. It is not the policy of the HA to subsidize commercial operation in public housing estates.

14. Nevertheless, HA is committed to improving the shopping environment of the wet markets and retail shops. On a user-pays principle, the wet markets of a number of older estates have been renovated with new air-conditioning installation, and some 30 wet markets completed since 1997 are already equipped with central air-conditioning and improved design. Apart from upgrading the infrastructure, the HA has frequently launched promotion programmes that are particularly welcomed by small retailers. Unlike their chain superstore counterparts, small retailers would not otherwise easily stage sales campaign on their own.

15. Notwithstanding the upgrading of infrastructure and promotion programmes launched by the HA, the HA considers that customer service, sourcing of quality products, promotion and pricing strategy etc. of individual shops as remarked in the report are also important. They have to cater for the customers' needs and adapt to the changing business environment. After all, it is the market force that prevails.

Allowing existing supermarket chains to retain their retail outlets on renewal tenancy through negotiation and by paying current market value has the effect of perpetuating the incumbency of existing retail outlet by the same supermarket chain (Chapter 6, paragraph 6.35 [extract at Annex II])

16. The report expressed concern about the HA's practice on tenancy renewal through negotiation of market rent, which could hinder new entrants from bidding desirable retail space. The HA's policy on tenancy renewal involves consideration of disruption of services for the domestic tenants and a stable prospect for business operation, apart from providing opportunities for competition from new entrants. A stable prospect for business operation invariably attracts investment and interest from potential retail operators, and is very often relied upon in securing "anchor tenants" for newly completed commercial premises, especially those in relatively outlying areas. However, this discretionary arrangement is subject to the terms and conditions of the tenancy agreements, which, similar to the private sector, provide for the HA to conclude tenure upon expiry.

Retailers' ability to quickly respond to market changes being constrained by the rigid application of bureaucratic processes (Chapter 3, paragraph 3.48 [extract at Annex II])

17. The report remarks that some retail operators consider HA's management control rigid, hampering their ability to promptly respond to changing market circumstances.

18. The HA considers the present management control arrangements appropriate and they should not constitute unnecessary barriers to competition for the operators concerned. The management control at issue relates more or less to tenancy arrangement and enforcement, including compliance with the designated trade mix and prohibition of obstruction and encroachment on common areas. Over the years, the HA has actively responded to the changing needs of the retail business environment through various initiatives including the introduction of the Business Opportunity Centre, the single operator model, flexible letting, the trade-widening and "yellow-line" schemes, etc. While the HA sees the need to allow flexibility in managing the retail operation, it is committed to enforcing the tenancy provisions, especially if they concern public health and safety. Clearly tenants' cooperation is required if an orderly, clean and pleasant shopping environment is desired.

Ends

Extracts from Consumer Council's Report on Competition
in the Foodstuffs and Household Necessities Retailing Sector

Recent policy relating to supermarkets

3.28 In mid-2000, HA began to adopt a "wider trade policy", which enabled retailers of commercial premises to sell a wider range of goods and services under expanded trade descriptions. The policy also permitted supermarkets of not less than 800 square metres to operate service-style provision of fresh food (operating on a "superstore" basis) subject to the area being used not exceeding 20% of the leased area. In 2003, there are about 17 supermarkets converted to superstores.

3.29 This new policy was a welcome response to the changing needs of retail operators. However, the scope for expansion by small non-supermarket retailers is largely affected by consumer shopping behaviour and wet market design. The ability to take advantage of this new policy direction might therefore be diminished unless floor area design, which facilitates operators to achieve greater economies of scale, is also addressed.

3.30 As the operation of small market stalls is highly dependent on the facilities provided by the HA, a lack of desired standards in facilities, such as air conditioning and reconditioning of buildings, will affect the growth and expansion of small retailers.⁴⁰ In consideration of the effect on wet market stalls, HA has undertaken a policy that allows affected fresh food produce retailers to terminate their rental contracts without the required three months notice, within the first six months following a situation where supermarkets have been approved to sell fresh food.

3.31 With an increase in the number of public estates with superstores that sell fresh food in direct competition with wet markets, the share of supermarkets in the fresh food sector is expected to rise and the number of wet market stalls to fall. This will inevitably lead to a lessening of competitive choices for consumers. Therefore, while the HA's policy of softening the impact of supermarkets encroaching on wet market operators recognises the effect on their competitive position, there is no policy to address the long term consequences of less competitive choices for consumers. For example, the implementation of the "wider trade policy" in the recent economic downturn has led to an increasing vacancy rate amongst small retailers, which has led to supermarkets taking up the available space, further threatening the survival of remaining small retailers.

3.32 The role that small retailers can play in offering competition to supermarkets is important. Balancing the allocation of market facilities for different distribution channels is therefore crucial to the development of competition.

³⁹ Please refer to Housing Authority's website <http://www.housingauthority.gov.hk>

⁴⁰ As noted in Chapter 5, in the section examining consumer preferences between supermarkets and wet markets, the shopping environment was a major consideration when deciding between the two.

6.34 The Council held discussions with associations of small retailers and individual retailers who operate within Housing Authority premises, to discuss their concerns. The Council was informed that in their opinion their ability to quickly respond to changing market circumstances in operating their businesses was constrained by the rigid application of bureaucratic processes. For example, they claimed that while they are subject to stringent constraints on their available space, their flexibility in deciding what products to sell, and even restrictions in some cases on how to display goods, supermarkets are under a much freer operational environment that is determined by corporate commercially oriented policy.

6.35 As far as the public housing sector is concerned, supermarket operational rights in new shopping malls constructed by the Housing Authority are initially through an open tender arrangement. However, the Government's response to the 1994 Consumer Council report noted that existing supermarket chains could retain their retail outlets on renewal of tenancy through negotiation and by paying current market value, rather than the sites being released for new tender. This has the effect of perpetuating the incumbency of existing retail outlet by the same supermarket chain.