Restriction of publication in part claimed

Submission - "Automotive retailer whom operates within the Newcastle / Hunter Valley Region" [redacted]

Date: 27 May 2019.

Attachment B - Response

Please find detailed below our response to your request for our views.

1. Please provide a brief description of your business or organisation and the reasons for your interest in the proposed acquisition.

We are an automotive retailer whom operates within the Newcastle / Hunter Valley Region.

Our interest in the proposed acquisition is the perceived negative impact on competition that will result from the further concentration of ownership of car dealerships in our Region.

Car retailing

2. Please describe how competition works in the automotive retailing industry. Are there any industry developments or trends that may impact or lead to changes in the existing dealership model for selling new cars?

Competition within the automotive retailing industry is determined by traditional supply and demand factors.

- Demand – The desirability of vehicle offerings from the various manufacturers in the eyes of the consumer. A model in demand by consumers will increase consumer competition for the vehicle and while demand outstrips supply then the margins earned on the model will improve.
- Supply - A vehicle model that is not in demand but has available supply will remain in dealer inventory. While the vehicle remains in dealer inventory there are holding costs that continue to be incurred until such time as the vehicle is sold.

The balancing act is gauging the demand and supply for individual model lines.

Supply is now largely dictated by the production capabilities of the manufacturer's overseas facilities. These facilities will produce volumes of vehicles for the Australian market. Volumes which are determined 6-12 months in advance.

The local offices of the manufacturers must clear the supply of inventory from their operations.

Should demand for their product decline then clearing the inventory remains a challenge for them just as much as for the Dealership.

3. How far in both distance and time are consumers prepared to travel to purchase new cars, and how may this vary by the location of prospective buyers and dealers? What other factors can affect consumers' willingness to travel?

Consumers willingness to travel is dependent upon their perception of possible cost savings on new vehicle purchases or the scarcity of the vehicles. If consumers are lured from, say, Sydney to Newcastle then they will only travel if the vehicle they want is at a significant discount to the market value of the vehicle.

4. How significant are AP Eagers and AHG as competitors in the industry, and in relation to each other? In your answer, please have regard to price and discounting, locations, brands, service and added inclusions.

Regardless of the location, AP Eagers & AHG because of their existing sizes already have a dominating influence in the market. Within the Hunter Valley, AHG holds multiple dealerships for Subaru, Kia and Isuzu, LDV and VW while AP Eagers holds multiple dealerships for Ford, Nissan, Honda, Hyundai, and VW.

Their consolidation of inventory holdings and economies of scale enable them to have lower operational costs than standalone dealerships or smaller dealer groups.

These dealerships operate within the mainstream volume market and the franchises largely compete against each other for market share. However, should the merger proceed then all these dealerships will fall under the control and influence of a single corporate board. Which will allow for further reductions in their operational costs and enable them to have greater influence on the sale of vehicles in the area.

5. Please identify who you consider to be the key alternative car dealerships to those owned by AP Eagers and AHG in:

How do they compare to AP Eagers and AHG with regard to price and discounting, location, brands, service and added inclusions?

a. Brisbane
b. Melbourne
c. the Newcastle/Hunter Valley region of NSW.

As we operate in the Newcastle / Hunter Valley region would consider ourselves to be one of the alternative dealerships.

Other competitors within this market are smaller family owned dealerships and smaller dealer groups.

AHG and AP Eagers entry into this region was as a result of acquiring / consolidating smaller dealer groups or existing larger dealer groups within the Regions such as the Bradstreet and Klosters dealer groups.

d. Sydney, and
e. nationally.

6. Please provide details of what is involved in establishing a new car dealership, including the manufacturer requirements that need to be met, government licensing criteria, and any other costs and time involved. Are you aware of any recent examples of people attempting to establish new dealerships?

Before you can establish a new car dealership there first must be an opportunity to either represent a franchise that is currently not represented in the Region or acquire an existing dealership from the current owners.

As all mainstream manufacturers are represented in the Newcastle / Hunter Valley region establishing a previously unrepresented dealership is highly unlikely.

New entrants into the Australian market in recent years have been from Chinese manufacturers and these have only had limited success in conquering and maintaining a share of the Australian Market.

At the other end of the spectrum, the prestige / luxury manufacturers are all either represented or their market share is so small that they limit their dealerships to metropolitan locations because of the costs associated with representing these manufacturers.

Manufacturer's approval is required for any change of dealership ownership and they will place stringent conditions on the acquisition. Conditions effecting the manufacturer's "Corporate Image" items such as facilities are very common. These usually require the upgrading of facilities to satisfy their latest design. Designs that come at a considerable cost and are refreshed regularly by the Manufacturers.

There are also government compliance issues with licencing i.e. motor vehicle dealers licence. While largely an administrative process this does impose a cost to acquire and maintain the licence.

The Manufacturers release inventory / trading stock to Dealerships under a Bailment system maintained by finance companies. The "GFC" saw many financiers leave the market and the number of financiers remaining is very small.

7. To what extent is there an advantage in having a network of dealerships at a local, state and/or national level?

With a local network of Dealerships, a Dealer Group can gain operational efficiencies and therefore cost reductions through shared services such as vehicle storage, vehicle servicing and sales functions i.e. the same resources serving the fluctuating demands of multiple manufacturers.

Where the Network operates multiple dealerships for the same manufacturer, they are also able to reduce their inventory holdings and therefore costs. You can reasonably expect to service a larger number of vehicle sales with a reduced inventory. The inventory required to service multiple dealerships is less than the sum of the dealerships individually.

The reduction of operational costs would also allow the business to trade at reduced vehicle margins without affecting the overall profitability of the business. In effect utilising some of the cost saving to gain an advantage in a price sensitive market.

These operational costs savings are not available to smaller Dealerships.

The branding of a Group at a Local, State or National level will allow common campaigns to be utilised. Drawing heavily off the "Brand" and reducing cost and increasing the effectiveness of branding activities.

8. For fleet and government buyers, please describe your organisation's key purchasing considerations, and who you consider to be the suppliers capable of meeting your organisation's needs. Are you able to purchase direct from the car manufacturers?

Not Applicable.

Dealership agreements with car manufacturers

9. In what ways and to what extent do manufacturers influence competition between dealerships, including levels of discounting, promotions and/or added inclusions offered? Would this limit AP Eagers' ability to increase prices following the proposed acquisition?

The sale price of vehicles is determined by the price advertised by the Manufacturer.

The ability of the merged group to increase prices above the manufacturer's advertised price is considered to be unlikely.

The merged group with lower operational costs could sell vehicles at lower prices. Partly offsetting the benefit of lower costs. The economies of scale and lower operational costs would not be available to smaller Dealerships.

Manufacturers influence competition between dealerships through the application of bonuses / incentives to dealerships for securing sales of vehicles.

Typically, the incentives are targeted to improve the sale of vehicle models that are in an over-supply situation. The incentive will allow the Dealership to offer vehicles for sale at a discounted price which effectively reprices the vehicle to a market price.

These incentives are also usually associated with some "Call to Action" media campaign to promote the model.

These promotions are all aimed at increasing the number of vehicle registrations in a given time period so that Manufacturers can measure their relevant performance in the market.

We would expect that a merged AP Eagers / AHG would be able to influence the incentive / bonus schemes for their benefit more than they currently would be able to do so. The benefit being that they could entice the consumer to buy a vehicle at a lower price while maintaining an acceptable gross margin on the sale. The vehicle sales would also present the dealership with an opportunity to sell additional products i.e. Finance and Insurance products and earn income that would otherwise not be available to the Dealership had they not sold the vehicle.

Due to the size of the merged group they maybe able to extract additional incentives / bonus / preferential pricing from the manufacturers that would not be offered to the Dealer Network as a whole. In any sales organisation, your largest customers are usually able to extract preferential terms from the Manufacturer.

10. For car manufacturers: please describe your key considerations in both awarding and renewing dealership agreements, including the importance of the following, and comment on whether the proposed acquisition would affect your future decisions about dealership agreements:
a. whether dealers have an existing network of dealerships locally, by state and/or nationally of yours and/or other manufacturers' brands
b. geographic coverage of your brand locally, by state and/or nationally, and
c. a dealer's demonstrated ability to represent your brand and meet KPIs.

Not Applicable

New car servicing and supply of parts

11. Do you consider that the proposed acquisition will affect competition for new car servicing? Why or why not?

Servicing of vehicles is a "Matter of convenience" in that the proximity of the Dealer's service facility to the consumers place of work or residence is a largest determination of where the vehicle is serviced.

As such the proposed acquisition should not affect competition for new car servicing provided that the merger does not result in a reduction in the number of Dealership service centres.

12. How far are consumers generally prepared to travel to get their new cars serviced? How may this vary depending on any consumer entitlements to free or capped-price servicing and the age of the car?

Refer item 11 above.

Additionally "Free" and "Capped Price servicing" is subsidised by the Dealership that sold the vehicle.

"Capped" prices are determined according to Manufacturer expected costings which are not necessarily in line with operational costs in Dealerships.

Once the manufacturer's warranty on new vehicles has expired then there is a marked decline in the number of older vehicles that are serviced in the Dealerships.

13. To what extent do you consider that independent mechanics compete with dealerships' authorised service centres for new car servicing?

There is a perception that independent service centres are cheaper but they do not have to offer the same level of customer care i.e. loan cars and facilities. Furthermore, the training that Dealership technicians have to undertake to reach specified competency levels dictated by the Manufacturers is not required of independent mechanics.

The rapid increase in the level of automation / computer controlled applications into the newer vehicles requires the continuing professional education Dealership technicans are required to undertake. The intellectual property contained within vehicles and how to properly maintain the vehicle should not be in the hands of the untrained.

The emergence of electric vehicles and the heightened risk of serious injury and possible death to the untrained that these vehicles represent is a growing concern for technicans and Dealerships.

14. To what extent do you consider that the proposed acquisition will affect the availability and/or price of car parts used in servicing new vehicles?

Provided that the merger does not result in a reduction of dealership numbers than the availability and pricing of spare parts should remain unchanged.

The threat of imported and / or counterfeit spare parts is a bigger risk to industry than the proposed merger.

Insurance and finance

15. Do you consider that the proposed acquisition will impact competition for the supply of insurance and finance to consumers buying cars? Why or why not?

If dealerships do not sell a vehicle then they cannot include the sale of Finance and Insurance products into the vehicle sale.

Should the proposed acquisition results in an unfair shift in vehicle sales towards the merged business then the other dealerships will not only lose the vehicle sale but also the opportunity to sell Finance and Insurance products.

AHG and AP Eagers already operate finance brokerage brands but these would also require the vehicle sale.

We would be uncertain how regulatory changes impacting the Sale of Finance and Insurance Products would impact finance brokerage.

16. To what extent do consumers compare insurance and finance options direct from insurance agencies and financial institutions to those offered by the new car dealership?

Consumers always compare options. Provided that the offering from the Dealership is competitive within the market place then the Dealership will be successful in the sale of the products

Public benefits

In assessing the benefits that are likely to flow from the proposed acquisition, the ACCC may take into account anything of value to the community generally.

AP Eagers submits the proposed acquisition will deliver public benefits, including:

. Productive efficiencies, including through a diversified portfolio of motor vehicles, greater geographical portfolio diversification, more financial scale and a more flexible balance sheet.
. Operational and corporate synergies.

. Providing AHG shareholders with the opportunity to benefit from exposure to AP Eagers' proven management expertise and future growth strategy benefit from the greater scale and long-term prospects of a larger automotive business.

17. To what extent do you consider that public benefits are likely to result from the proposed acquisition?

The "Public benefits" listed above may be summarised as improved profitability of the AP Eagers business and a greater return to shareholders.

18. To the extent that the proposed acquisition would result in cost savings, do you consider they are likely to be passed on to consumers?

We would expect that any cost savings generated would not be passed onto consumers but assist in returning the business to shareholder acceptable returns.

Other information or competition issues

19. Please provide any additional information or comments, or identify other competition issues, that you consider relevant to the ACCC's consideration of the proposed acquisition under section 90(7) of the Act.

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