COMPETITION ECONOMISTS GROUP

**Restriction of Publication of Part Claimed**

# TVSN exclusive supplier arrangements

Dr Tom Hird
Jason Ockerby

30 April 2020

# Table of Contents

1 **Overview** **1**

1.1 Analogies in other markets 3

2 **The proposed conduct** **4**

3 **Economics of exclusive dealing** **4**

3.1 Procompetitive rationale 4

3.2 Anticompetitive rationale 6

4 **Risky effort and investment by distributors in supplier brands** **7**

5 **Market positioning** **11**

6 **Brand protection** **13**

7 **Necessary to ensure efficient operations** **14**

8 **Many alternative suppliers for competing DTSCRs** **15**

9 **No damage to competition in the market** **18**

10 **Analogy to other markets** **21**

11 **Appendix: sub-categories aligned** **23**

# List of Figures

Figure 9-1: TVSN revenue as a percentage of Australian retail sales (excluding online) by segment ........ 19

Figure 9-2: Online retail sales as a percentage of total retail sales in Australia ........ 20

# List of Tables

Table 8-1: Proportion of TVSN revenues from its largest suppliers, by category 17

Table 8-2: Proportion of TVSN margins from its largest suppliers, by category 17

Table 8-3: Proportion of TVSN revenue and margin from its largest suppliers, overall 17

Table 11-1: Category matching between TVSN and Statista 24

COMPETITION ECONOMISTS GROUP

# 1 Overview

1. We have been asked by Gilbert and Tobin, lawyers for TVSN Channel Pty Ltd (**TVSN**), to provide our opinion in relation to the competitive effects of certain conduct proposed by TVSN. We understand that TVSN has proposed that it be allowed to refuse to acquire, and therefore market for sale products on its dedicated television shopping channel if those products, or products from that brand or product category have recently been or are to be simultaneously marketed by a competing retailer which predominantly utilises the live presentation or live demonstration format to sell products to consumers within Australia or New Zealand on a dedicated television shopping channel (ie, one that generally operates 24 hours a day, 7 days a week) (hereafter, **DTSCR**).

2. As explained in section 2, we understand that TVSN has proposed that it be allowed to refuse to deal with suppliers that intend to or are currently marketing or selling products on a competing DTSCR.

3. The conduct proposed by TVSN would fall into the category of 'exclusive dealing', though the nature of the conduct proposed is limited to the duration over which products are marketed on competing DTSCRs plus a short period following the purchase of inventory or the planned event, program or promotion for which inventory is purchased. That is, it does not involve arrangements that would prevent suppliers from switching between DTSCRs for an extended period of time.

4. Section 3 explains that the economics of exclusive dealing arrangements is nuanced. Exclusive dealing arrangements can have pro-competitive effects as they allow parties to make greater investments in products that would not be commercially sensible absent those arrangements. Exclusive dealing arrangements can have anti-competitive effects if they result in foreclosure of competitors and lead to higher (quality-adjusted) prices. Differentiating between arrangements that are pro or anti-competitive requires a detailed assessment of the market and the terms of the arrangement.

5. The evidence indicates that TVSN's proposed exclusivity provisions are consistent with pro-competitive behaviour for the following reasons.

6. First, as explained in section 4, the evidence indicates that TVSN is making substantial investments that are specific to the products and brands of its suppliers. If suppliers simultaneously allow their products to be marketed and sold by a competing DTSCR, these TVSN investments can effectively be expropriated. Without some form of exclusivity arrangement, the risk that this will occur will deter TVSN from making these investments.

7. This problem is particularly acute for TVSN as its efforts with suppliers commonly involve a 'trial and error' process. TVSN tries a range of products and some are

unsuccessful, and others are successful. It follows that every successful product embodies an investment at least equal to the average resources spent on unsuccessful products. If the successful products could, once TVSN has discovered, developed and proven them, all simply switch to a competing DTSCR, TVSN would be unable to recover its costs. This will lead to inefficient underinvestment in such activities that would be for the benefit of consumers.

8. Second, as explained in section 5, exclusivity in relation to products and know-how in selling its products will allow TVSN to differentiate itself from its retail competitors. It will allow TVSN to invest more in creating differentiation in its market position relative to its competitors. Whilst the exclusivity arrangements means the same products will not compete with themselves on different DTSCRs, this will be replaced by competition between DTSCRs to supply the product in question at any given point in time which should be as effective (the arrangements will not change competition for the same or similar products not sold on DTSCRs).

9. Third, as explained in section 6, the proposed arrangements allow TVSN to protect its product and brand positioning from the negative consequences of competing DTSCRs providing a poor customer experience. It would also avoid customer confusion in relation to the features and attributes of products.

10. Fourth, as explained in section 7, the exclusivity arrangements will result in operational efficiencies. In the absence of exclusivity, operational planning becomes uncertain and more costly to TVSN. The potential for suppliers to market with other DTSCRs creates costs for TVSN including:

    a. the cost of unsold inventory that must be purchased in advance by TVSN;

    b. the cost of making late adjustment to programming, with consequential effects on purchasing and promoting stocks for substitute campaigns;

    c. the cost of adjusting or having out-of-date collateral including catalogues and events.

11. Fifth, as explained in section 8, at any given time TVSN's existing products being retailed are a tiny fraction of all the potential products available to competing DTSCRs. Consequently, TVSN's exclusivity arrangements cannot plausibly be assumed to prevent competing DTSCRs from reaching and maintaining minimum efficient scale and as such, would not lessen competition.

12. Sixth, as explained in section 9, the market in which TVSN operates in is likely much broader than DTSCRs. It would be likely to at least include alternative forms of home shopping (including catalogue and internet shopping from global and local suppliers) and also constraints more broadly from "bricks and mortar" retailers (e.g., department stores and product category specialists).

## 1.1 Analogies in other markets

13. Many of the points that we have discussed in terms of the rationale for TVSN's conduct have close analogies in relation to the rationale for exclusivity amongst firms in other retail markets and in broadcasting. For example, in the sale of motor vehicles it is common for car manufacturers to have exclusive arrangements with dealerships. These exclusive arrangements require dealers to only sell the products of one manufacturer (i.e., one make of car). These arrangements are desired by manufactures because they allow the manufacturer to protect its investments in increasing the knowledge and selling ability of a dealer. They also protect the manufacturer by allowing them to control the brand positioning of their product. The dealerships too may prefer exclusivity as they have their investment in promoting and selling the particular make of car protected from the manufacturer seeking to sell the car through a competing dealer (allowing that competing dealer to free ride on the investment the dealer makes in promoting make of car and the knowledge of customers).

14. Similarly, in free to air (FTA) television broadcasters and subscription TV providers, exclusivity is the norm when dealing with TV station contracts with content providers. This is for precisely the same set of reasons TVSN desires exclusivity:

    a. TV stations make investments in promoting and discovering programs. If, once a program is found to be popular, the content owner could simply sell it to another TV station then the original investment in promoting and discovering programs would be unlikely to be made;

    b. TV stations choose a suite of exclusive programs in order to position their overall brand offering in a particular way. The ability to do this is greatly enhanced by the ability to show exclusive content. In addition, one station attempting to brand some content as "premium" (e.g., prime time) would be undercut if another station treated it as low quality (e.g., 5 pm);

    c. TV stations would suffer from horizontal externalities if they did not have exclusive content. One TV station would be less likely to promote a show if it was, or could be, showing on a rival channel. Similarly, there would be negative externalities if viewers could (deliberately or accidentally) 'skip ahead' to watch future episodes of a series on another station; and

    d. TV stations scheduling and promotions would be materially more complicated if they had to factor in the actual, or possible, provision of the same content by other stations. Imagine, for example, a TV station planning to show "Game of Thrones" at a particular set of times only to find that a competitor was intending to show it half an hour earlier on the same day.

15. Finally, there is little reason to believe that the availability of products for DTSCRs would be more limited than the availability of content for FTA and subscription TV.

Both are similar in that new 'product' and 'content' can, and is, endlessly created to match evolving customer tastes.

# 2 The proposed conduct

16. We understand that TVSN has proposed that it be allowed to refuse to acquire, and therefore market for sale products on its dedicated television shopping channel if those products, or products from that brand or product category have recently been or are to be simultaneously marketed by a competing retailer which predominantly utilises the live presentation or live demonstration format to sell products to consumers within Australia or New Zealand on a DTSCR.

17. This conduct may be described as a form of exclusive dealing. The nature of the exclusivity is, however, limited in nature, in that TVSN is not seeking to contract with suppliers for an extended period. TVSN does require that there is a relatively short-lived time period between when a product supplier provides its last sales to TVSN and when the supplier's products can be sold on another DTSCR (and vice versa). However, this time period is intended to allow for the fact that DTSCRs have inventory, and this will take time to clear.

18. This means that suppliers may switch supplying products from TVSN to alternative DTSCRs, with a short delay, even if this involves utilising the investments made by TVSN. The conduct would however mean that TVSN may refuse to acquire those products or deal with those suppliers for a period.

# 3 Economics of exclusive dealing

## 3.1 Procompetitive rationale

19. There is an extensive economic literature on exclusive dealing.[1] A particular situation considered in the literature is when a manufacturer sells products through distributors subject to arrangements that require:

[1] Klein, B. and Lerner, A.V., (2006) "Procompetitive Justifications for Exclusive Dealing: Preventing Free-riding and creating Undivided Dealer Loyalty" Draft November 12, 2006, https://www.justice.gov/atr/procompetitive-justifications-exclusive-dealing-preventing-free-riding-and-creating-undivided

- the distributors not to carry products from competing manufacturers (an example of this would be Toyota requiring an independent distributor to exclusively sell Toyota vehicles[2];
- the manufacturer not to distribute products via competing distributors within a certain geographical area[3].

20. The second point above is analogous to the TVSN conduct, which involves the distributor (TVSN) requiring suppliers to be exclusive to its distribution channel within a certain distribution space (DTSCRs) within a broader market.

21. The economic literature does not provide any general conclusions in relation to the competitive effects of firms refusing to deal with suppliers of, or to, competing firms. Assessing the competitive effects of such conduct requires an evidence-based inquiry of the market to determine any impacts on competition.

22. The decision of firms to not deal with suppliers of competing firms can be a legitimate competitive action. In many cases, these decisions are procompetitive in the sense that these actions benefit consumers by enabling suppliers and distributors to make beneficial investments in the product and the marketing and promotion of the product which benefit consumers.

23. In the absence of exclusivity provisions, the investment by distributors creates externalities that, if not internalised, will discourage such investments. These externalities include:

    a. Vertical externalities – where the efforts of the distributor to promote, refine and develop the product confers benefits on the supplier that are not reflected in contractual arrangements. If the distributor cannot contractually capture these benefits, such efforts will be inefficiently discouraged[4]; and

    b. Horizontal externalities – where efforts of the distributor to promote, refine and develop a product confers benefits on other distributors. If one distributor engages in effort that has a spill over benefit to other distributors (e.g., promoting a product also sold by other distributors) this creates an external benefit to those other distributors. This horizontal externality can also be negative, where the

---

[2] Sass, T.R. (2005), "The competitive effects of exclusive dealing: Evidence from the U.S. beer industry" International Journal of Industrial Organization, Vol 23 provides a summary of recent theoretical results and finds that exclusive dealing enhances social welfare in the U.S. beer industry.

[3] See Lafontaine, F., and Slade, M., (2014), "Franchising and Exclusive Distribution: Adaption and Antitrust," The Oxford Handbook of International Antitrust Economics, Vol 2 for a discussion on the use of exclusive geographic clauses in franchise agreements.

[4] Hart, O. and Moore, J., (2007), "Incomplete Contracts and Ownership: Some New thoughts," American Economic Review, Vol 97, No. 2, finds when buyers can make ex-ante investments in a product, the buyer will have less incentive to invest if the buyer has to share a portion of the surplus from the investment with the seller.

actions of one distributor harms the interest of other distributors (say by offering a poor experience with a product or service).[5]

24. Exclusive dealing is a commonly used mechanism to address vertical externalities and yield a better alignment of incentives between distributors and suppliers. Exclusive dealing can encourage a level of investment in promoting, refining and developing products that is closer to being at the efficient level from the perspective of both supplier and distributor.

25. Similarly, exclusive dealing arrangements can go some way to addressing horizontal externalities by allowing distributors to differentiate themselves from other distributors. Exclusive access to products allows a distributor to create 'distance' between itself and other distributors preventing its investments in products from more readily being captured by competing distributors.

26. In addition to creating externalities, non-exclusive arrangements between distributors and suppliers create risks of economic 'hold-up'. Economic hold-up involves the case where one party makes irreversible investments that only yields a return if the relationship with another party continues (often called 'relationship-specific' investments), whilst the other party has the opportunity to benefit from those investments in transacting with others. This gives the other party power over the party making the investments (once they are made).

27. For example, a distributor that makes an investment in a promotional campaign that gives rise to higher demand for a product will only benefit if the supplier continues to use the distributor as its avenue to market over the period that demand is raised. If, however, the supplier could utilise another distributor to get to market (and enjoy the benefits of the campaign without the costs) they would have an incentive to do so. This would reduce the value of the initial promotional investment to the original distributor and make it less likely to happen in the first place.

## 3.2 Anticompetitive rationale

28. In some cases, the decision to not deal with suppliers of competitors may be harmful to consumers if it results in foreclosure. This would occur if the refusal of a dominant distributor to deal with suppliers of other distributors results in other distributors being unable to access sufficient quantity or quality of product to continue to provide the same competitive constraint on the dominant distributor.

[5] See Lafontaine, Francine and Slade, Margaret E. (2008) Exclusive contracts and vertical restraints : empirical evidence and public policy. In: Buccirossi, Paolo, (ed.) Handbook of antitrust economics. Cambridge, MA: MIT Press. Lafontaine and Slade discuss how a dealer's (distributor's) incentive to invest is effected by exclusivity "*manufacturer wants the dealer to invest ex ante in specific facilities or human capital in order to provide better service to consumers. Unless the dealer can be assured that his investments are fully protected, he will choose to underinvest or not invest at all…*".

29. The typical concern is with a distributor that is already dominant in the market seeking to lock-up suppliers to foreclose entry or cause exit by smaller distributors. The time period for which exclusivity is demanded will influence the effects of exclusivity arrangements. The longer the time period, the more difficult it may be for smaller distributors to enter or cause smaller distributors to exit.

30. Anticompetitive effects may also occur if a dominant distributor were to lock-up 'must have' suppliers or a sufficient number of suppliers to prevent smaller distributors from reaching minimum efficient scale. Differentiating between cases where actions are pro- or anti-competitive requires a factual analysis.

# 4 Risky effort and investment by distributors in supplier brands

31. The arrangements between TVSN and suppliers have important implications for the incentives for TVSN to engage in effort and make investments in developing, marketing and promoting a supplier's products and brands.

32. The efforts of TVSN to promote a product or brand provides it with direct benefits from increased sales. However, these efforts also confer an indirect benefit to the supplier of the products in the form of increased profits to the supplier.[6] The inability of TVSN to capture all of the incremental benefits that accrue because of their actions creates what economists refer to as "vertical externality".

33. These externalities can lead to a sub-optimal level of investment in the activity that creates them, when viewed from the perspective of TVSN and suppliers combined. For example, investment by TVSN in assisting with the development of products and with the promotion of brands would be less than desirable if they cannot capture the full benefits of doing so. This will lead to underinvestment in such activities that would be for the benefit of consumers.

34. It would be possible to address these externalities if TVSN were to vertically integrate with its suppliers (and in some cases we understand that TVSN has developed its own brands and products). Vertical integration would allow them to internalise the benefits[7]. However, vertical integration would likely come at some efficiency costs as

---

6 Similarly, the actions of a supplier to increase sales of the product or brand (e.g., though improving the quality of the product) provides it with a direct benefit but might also confer an indirect benefit to TVSN of the product.

7 According to Holström, B. and Roberts, J., (1998) "The Boundaries of the Firm Revisited," Journal of Economic Perspectives, Vol 12, No 4, "if the supply relationship faces more extensive hold-up problems, the best solution may be vertical integration, with all the parts of the body being procured internally rather than outside."

TVSN management is likely most skilled and efficient at its current activities and may not always be the most efficient designer/manufacture/procurer of products. Similarly, in a fully vertically integrated arrangement, suppliers would be upstream divisions of TVSN which would make it more difficult to provide incentives for product development and cost minimization compared to a competitive supply ecosystem.

35. Of course, vertical integration is just an extreme way to achieve exclusivity with suppliers. Contractual arrangements that include some requirements for exclusivity can also address the same externality whilst retaining the benefits of competition amongst suppliers. However, without some level of exclusivity, the benefits that TVSN creates for itself and for suppliers in developing and promoting a product can be captured by suppliers if they simultaneously market their product through other DTSCRs.

36. Similarly, if products are marketed on multiple DTSCRs, the effort that TVSN makes in developing and promoting products and brands also gives rise to "horizontal externalities". These horizontal externalities confer benefits on competing DTSCRs when TVSN promotes products and brands on its DTSCR. In this case, when TVSN engages in effort and investment to support a supplier's product this will indirectly benefit other DTSCRs that are simultaneously marketing the same products and brands.

37. We understand that TVSN engages in substantial amounts of work with individual suppliers to support the brands and products marketed on TVSN. That is, it makes substantial investments that are specific to the products of suppliers (in economic terms, these investments are 'relationship-specific'. Relationship-specific investments are at greatest risk of hold-up/expropriation). This includes effort and investment by TVSN to:[8]

    a. Identify, build and promote the brands of suppliers, including screening suppliers, seeking opportunities through trade shows and taking previously unknown brands to market.

    b. Assist with product development and refinement, such as identifying which particular products would most likely be successfully marketed through television.

[8] It may be that TVSN is in a number of areas making greater relationship-specific investments than suppliers in the factors that are likely to drive sales success in the dedicated shopping channel. In these cases, it would be unsurprising that it would be TVSN, rather than suppliers, that are seeking a level of exclusivity. This would contrast with supplier/distributor models in other markets where the supplier is making greater relationship-specific investment in training and know-how for distributors and therefore the supplier seeks exclusivity from distributors (such as occurs in selling motor vehicles).

c. Develop market and promotional strategies and material relating to brands and products, including developing collateral/assets for each brand and how it will best be promoted.

d. Work with suppliers to improve systems for sales and returns to increase the customer experience.

38. We are instructed that TVSN's primary sources for brands and products that it might promote are

[Restriction of Publication of Part Claimed]

39. We are instructed that TVSN investigates the marketability of each brand or product as follows:[9]

[Restriction of Publication of Part Claimed]

40. We understand that one example of where TVSN has identified a brand with no market presence in Australia, promoted it and generated significant sales is

[Restriction of Publication of Part Claimed]

[9] Communication from Gilbert and Tobin.

[10] Communication from Gilbert and Tobin

[Restriction of Publication of Part Claimed]

41. [Restriction of Publication of Part Claimed]

42. The problem of suppliers expropriating such investments in developing and marketing products is particularly acute for TVSN as its efforts with suppliers commonly involves a 'trial and error' process. TVSN tries a range of products and some are unsuccessful (i.e., they do not sell sufficient quantities to justify the investment in development and airtime or, in some circumstances, the cost of goods sold) and others are successful.

43. Some initial costly failures are followed up with a longer lasting success. That is, the costs of initial failure and subsequent success can occur with a single supplier.

[Restriction of Publication of Part Claimed]

44. It follows that every successful product embodies an investment equal to the average resources spent on unsuccessful products. If the successful products could, once TVSN has discovered/proven them, all simply switch to a competing DTSCR, TVSN would be unable to recover its costs.

45. This 'trial and error' discovery process is a specific example of an investment by TVSN that can be appropriated by a supplier. Specifically, once a supplier (and a competing DTSCR) knows a product is well suited to television shopping then, absent exclusivity, it can be transferred to a competing DTSCR who can then avoid the costly 'trial and error' process. This would enable a competing DTSCR to offer a higher margin to the supplier than if TVSN had not already made the 'trial and error' investment.

COMPETITION ECONOMISTS GROUP

# 5 Market positioning

46. It is common in markets to see firms seeking to differentiate themselves from competitors[11]. In markets with homogeneous products firms may simply differentiate themselves through location[12]. In that case, the physical distances between the locations of firms creates differentiation. The closer together firms are located the greater the competition for nearby customers but the lesser the ability of firms to cover their fixed costs. The competitive process involves firms unable to cover fixed costs exiting until equilibrium is reached[13].

47. In other markets, firms differentiate themselves through the design of their product and the position of their brands[14]. These forms of differentiation appeal to some customers but not others. For example, firms may differentiate the design of essentially the same product to make it appeal to older or younger customers or seek to position their brands as 'high-end' or 'value' to appeal to different customers.

48. Firms targeting different customers through differentiation create 'distance' between each other just as the firms with homogeneous products create physical distance with each other. Through this process, firms are able to charge a price in excess of their marginal costs which allows them to recover their fixed costs.

49. Exclusive dealing arrangements are therefore a tool for firms to differentiate themselves. They allow firms to differentiate themselves from competitors by ensuring they can offer products or brands that fit with their overall market position and this will not be undermined by competitors offering the same products and brands

50. [Restriction of Publication of Part Claimed]

---

11 See d'Aspremont C., Gabszewicz, J.J. and Thisse, J.F., (1979) "On Hotelling's Stability in Competition" Econometrica Vol 47, No 5

12 See d'Aspremont C., Gabszewicz, J.J. and Thisse, J.F., (1979) "On Hotelling's Stability in Competition" Econometrica Vol 47, No 5

13 See Chapter 8 in Pindyck, R.S.and Rubinfeld, D.L. (2000) "Microeconomics" 5th Edition Prentice Hall

14 Sharp, B., and Dawes, J., (2001), "What is Differentiation and How Does it work," Journal of Marketing Management Vol 17 No 7

51. TVSN has indicated that:[15]

[Restriction of Publication of Part Claimed]

*Without the exclusive agreement, if the same supplier sells through OpenShop, OpenShop will be able to enjoy the increased consumer awareness through investments undertaken by TVSN.*

52. It is true that the effect of product exclusivity arrangements is that customers would no longer be able to acquire the same product through two DTSCRs at the same time. This is, however, offset by the competition to have the product that is exclusively distributed by the relevant DTSCR. That is, competition between DTSCRs selling the same products in the market would be substituted for competition between DTSCRs to be the sole DTSCR of that product for the market at each point in time.

53. Putting aside the investment incentive differences outlined above, competition to be the exclusive DTSCR at each point in time is likely to have similar competitive outcomes to competition by DTSCRs of the same products. This is because the exclusivity period is only for a limited period (i.e., products being marketed at the same time),[16] the same number and types of suppliers would participate in competition for the market as they would in competition in the market, and there would be limited incumbency advantage in the market at any point in time (i.e., there would be limited advantage in distributing a product first).[17]

---

15 Communication from Gilbert and Tobin.

16 It is possible that the use of long-term exclusive contracts can be used as a tool to deny a competitor efficient scale. Aghion, Philippe, and Patrick Bolton. "Contracts as a Barrier to Entry." The American Economic Review 77, no. 3 (1987): 388-401.

17 Geroski, P. Competition in Markets and Competition for Markets. Journal of Industry, Competition and Trade 3, 151–166 (2003).

54. Importantly, the exclusive dealing provisions proposed by TVSN do not “lock up” products or suppliers for an extended period. As we understand the arrangements, the proposal is that products could not simultaneously be distributed through TVSN and another DTSCRs (with some time lags involved to deal with inventories and forward planning).

55. In effect, this means that suppliers would enjoy competition between DTSCRs. This would imply a process of competition in which DTSCRs compete to have the product exclusively distributed on their channel. The DTSCR offering the most attractive proposition and terms (including margin) to suppliers would be successful.

# 6 Brand protection

56. When DTSCRs distribute the same product, they impose (horizontal) externalities on each other. This could be a positive externality in the circumstances where the action of one DTSCR (say the positive promotion of the product) benefits other DTSCR carrying the same product. Customers may be able to learn the positive aspects of the product through one DTSCR but make the purchase through another DTSCR (perhaps at a lower price because the other DTSCR is not incurring the same level of promotional cost).[18]

57. However, this externality would not always be positive. Where there are multiple DTSCRs distributing the same or similar products or the same brand of product, they may impose negative externalities on one another. For example, a product may be marketed on one DTSCR in a way which conflicts with how it is marketed or presented on another DTSCR. This could involve one DTSCR highlighting the advantageous features of a particular product whilst the other DTSCR describes the same product as a ‘no-frills’ product.

58. There is also the potential to create brand and product confusion. TVSN have indicated:[19]

[Restriction of Publication of Part Claimed]

18 As discussed above, if this externality is not addressed it can discourage the level of investment in this product.

19 Communication from Gilbert and Tobin.

[Restriction of Publication of Part Claimed]

# 7 Necessary to ensure efficient operations

59. We understand that TVSN engages in substantial forward-planning with suppliers in relation to products that will be marketed on the channel, with lead times that can range from 3 to 18 months. This activity includes planning for programming, the development of collateral and the purchase of stock.

60. In the absence of exclusivity arrangements in relation to products and brands, this planning becomes highly uncertain and more costly to TVSN. The potential for suppliers to market with other DTSCRs creates costs for TVSN including:

    a. the cost of unsold inventory that must be purchased in advance by TVSN;

    b. the cost of making late adjustment to programming, with consequential effects on purchasing and promoting stocks for substitute campaigns;

    c. the cost of adjusting or having out-of-date collateral including catalogues and events.

61. In order to run campaigns, TVSN must plan and commit to purchase stock. Depending on the product category and size of the order some suppliers require purchase orders well in advance of the promotion. For example, we understand that TVSN are already placing purchase orders for stock that will be presented in November this year and in relation to fashion, orders were being made in March for February shows next year. Another example is in relation to TVSN's Australian opals campaign on Australia Day weekend. The stock for this campaign was purchased 12 months in advance due to the rare nature of the stones.

62. While programming can be adjusted, this involves lost promotion of the substitute product prior to the feature, which would likely have a ripple effect in terms of the impact on other brands and more importantly can create a stock problem. We understand that, depending on the timing of these adjustments, they will also need to be reflected in collateral including the TVSN Shopper's Guide which is produced every month, posted on the website and sent out in print. TVSN also produces a Christmas and Mothers' Day catalogue (for the website and print) which has a lead time of around 6 months.

63. In addition to producing live television programming, TVSN creates and promotes upcoming featured brand events [Restriction of Publication of Part Claimed] to generate customer interest. We understand these events require time to organise and promote and TVSN needs to know that they can rely on

those brands to still be on TVSN and aligned with the TVSN business model when the event takes place. These events and the featured brands are also incorporated in the TVSN Shopper's Guide.

[Restriction of Publication of Part Claimed]

64. The exclusivity arrangement proposed by TVSN will allow these operations to run more efficiently and at lower risk to TVSN.

# 8 Many alternative suppliers for competing DTSCRs

65. The requirement for suppliers to exclusively deal with a single distributor has, in theory, the potential to harm competition if this denies competing distributors the ability to secure sufficient products to allow them to enter or remain in operation.

66. For example, an exclusivity arrangement may be harmful to competition if it either:

a. denies a competing distributor access to a sufficient quantity or quality of products for it to reach a minimum efficient scale. It may be in the mutual interests of suppliers and the distributor to deny this scale to a competitor (as long as the distributor shares the gains from lessening competition with suppliers); or

b. denies a competing distributor access to 'must have' products that are needed for it to attract customers to its channel. This type of problem has been alleged in some broadcasting markets where some alleged 'must have' programming (typically locally popular sporting content) has been denied to competing cable and terrestrial broadcast networks.

67. In order for this to be a concern in the current context, it must be the case that TVSN's exclusivity proposal would allow TVSN to 'lock up' a sufficient number of products or suppliers so that competing DTSCRs are effectively prevented from reaching minimum efficient scale.

68. This type of outcome conflicts with the terms of the exclusivity that TVSN is seeking. TVSN's exclusivity arrangement would not prevent suppliers switching to alternative DTSCRs. The arrangement proposed by TVSN therefore does not 'lock up' products or suppliers.

69. If there were a limited pool of quality suppliers to DTSCRs[20], then it could be true that exclusivity arrangements may create a barrier to entry for a competing DTSCR (point a. above). However, it appears extremely unlikely that there are a limited number of alternative quality suppliers available to DTSCRs. TVSN sells mainstream products that are very commonly supplied around the world and, TVSN is, we understand, continually sourcing new suppliers. As such, it would reasonable to conclude that there is effectively an unlimited number of alternative quality suppliers that could be used by competing DTSCRs.

70. Similarly, it would be extremely unlikely that the current suppliers sold through TVSN have intrinsically lower costs for the physical products they produce than would alternative suppliers. There is no reason that a competing DTSCR would have a higher cost of trialling and developing a portfolio of products other than those sold by TVSN.

71. However, it is the case that competing DTSCRs may find it lower cost to sell products and brands that TVSN has already proven can be successfully sold on a DTSCR. However, this is simply because the competing DTSCR gets to “free ride” on the investment in trial and error made by TVSN in developing its portfolio – as well as the investment in developing successful product specific marketing strategies.

72. The fact that a competing DTSCR would incur higher costs when using alternative suppliers is not an anti-competitive barrier to entry.[21] This is because they are costs which were incurred by TVSN and, most importantly, if these costs were incurred by competing DTSCRs with alternative suppliers, they would be in an equally competitive position as TVSN.[22] As discussed above, the exclusivity sought by TVSN is limited and would allow suppliers to switch between competing DTSCRs.

73. In any event, in practice, it is hard to conceive of a situation in which TVSN’s conduct could limit other DTSCRs from attracting a sufficient number or quality of suppliers. Unlike other markets where it may be plausible that there are ‘must have’ products that a retailer or broadcaster may need, there is an almost unlimited range of suppliers that competing DTSCRs could source from around the world.

---

20 We are not aware of any evidence that suggests there are a fixed pool of potential suppliers to dedicated shopping channels. We understand that TVSN is continually seeking and acquiring new suppliers.

21 McAfee, R., Mialon, H., & Williams, M. (2004). What Is a Barrier to Entry? The American Economic Review, 94(2), 461-465. Retrieved April 19, 2020, from www.jstor.org/stable/3592928

22 The economic literature generally defines a barrier to entry in terms of whether it relates to costs that were not incurred by incumbents and therefore do not give rise to excessive profits. Carlton, Dennis, W. 2004. "Why Barriers to Entry Are Barriers to Understanding." American Economic Review, 94 (2): 466-470. The fact that competing DTSCRs may have to incur these costs is not a barrier to entry, as TVSN also incurs these costs (in working with suppliers). As such, if competing DTSCRs do incur these costs it does not give TVSN a cost advantage (it also incurred these costs) and does not, therefore, allow it to earn a profit relative to other DTSCRs (that would be considered excessive).

74. TVSN has provided us with the following estimates of revenues/margins accounted for by the largest suppliers in each product category. It can be seen that, in each product category, the top 5 suppliers account, on average, for only around [Restriction of Publication of Part Claimed]% to [Restriction of Publication of Part Claimed]% each of total revenues. For the next (second top) 5 largest suppliers in each product category the value is [Restriction of Publication of Part Claimed]% to [Restriction of Publication of Part Claimed]%. For the next 10 top suppliers in each product category the value is [Restriction of Publication of Part Claimed]% to [Restriction of Publication of Part Claimed]%. (The results when using margin are very similar).

75. These results are inconsistent with there being a small number of 'must have' suppliers.

### Table 8-1: Proportion of TVSN revenues from its largest suppliers, by category

| Supplier tier | |
|---|---|
| Top 5<br>Second top 5 11th to<br>20th largest | [Restriction of Publication of Part Claimed] |

*Source: TVSN*

### Table 8-2: Proportion of TVSN margins from its largest suppliers, by category

| Supplier tier | |
|---|---|
| Top 5<br>Second top 5<br>11th to 20th largest | [Restriction of Publication of Part Claimed] |

*Source: TVSN*

76. A similar (if not lesser) relationship is observed in TVSN's revenue and margins from its largest suppliers overall, indicating there is not a small number of suppliers that TVSN could 'lock up' to prevent another DTSCR from competing.

### Table 8-3: Proportion of TVSN revenue and margin from its largest suppliers, overall

| Supplier tier | Revenue | Margin |
|---|---|---|
| Top 5<br>Second top 5<br>11th to 20th largest | [Restriction of Publication of Part Claimed] | |

*Source: TVSN*

77. We understand that TVSN has a long history of developing previously unknown brands. These suppliers are identified through

[Restriction of Publication of Part Claimed]

78. This suggests that the supply of products available for TV shopping is, if not infinite, materially larger than the number of products currently sold via DTSCRs in Australia.

# 9 No damage to competition in the market

79. In order for TVSN's exclusivity requirement to substantially lessen competition, it must result in an increase in its pricing power sufficient for TVSN to be able to increase the price of its products by a substantial amount for consumers.

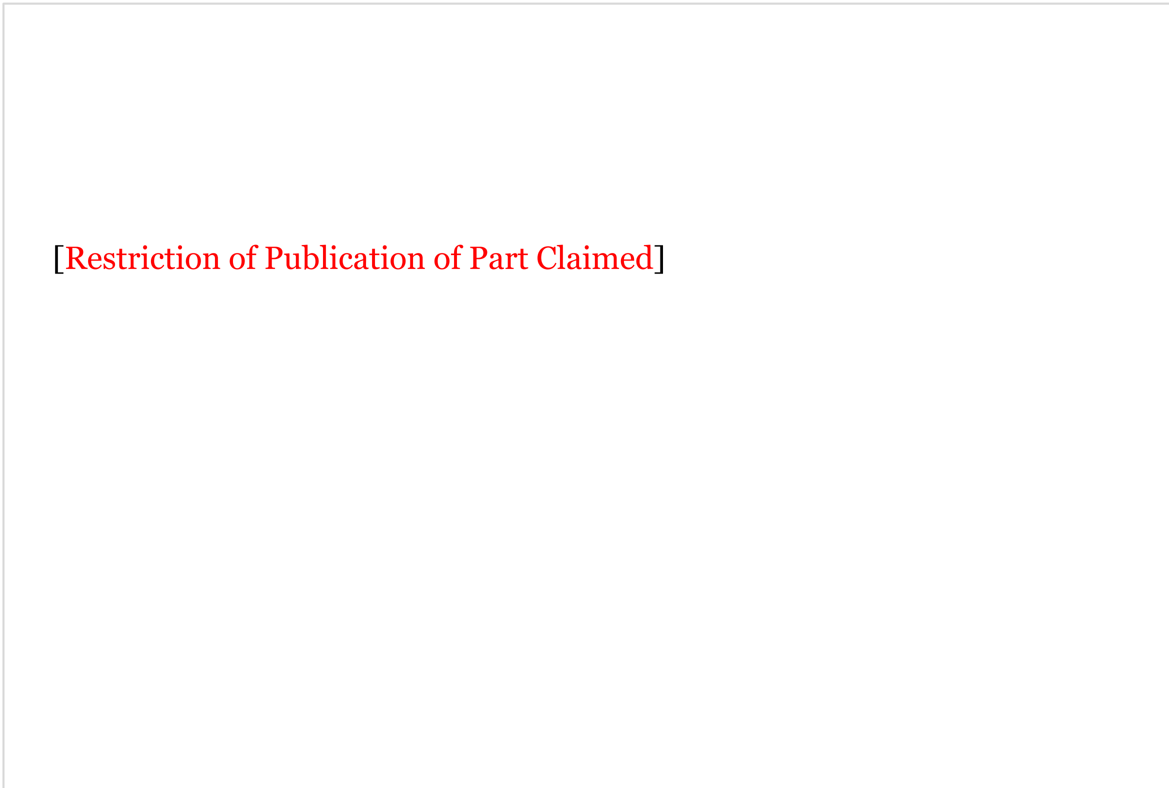
80. That is, even assuming that exclusive dealing might damage a particular competitor (i.e., another DTSCR), a lessening of competition would only occur if the loss of that competitor freed TVSN to increase prices by a substantial amount. However, if there are other competitors in the market or forces that constrain TVSN from raising prices, then a substantial lessening of competition will not occur.

81. This means that even if it were believed that TVSN's conduct was harmful to competing DTSCRs it does not necessarily follow that there is a substantial lessening of competition. This only follows if it is also the case that competition from other retail distribution platforms do not constraint TVSN from exercising undue market power. (Or, equally, TVSN's customers are forced to pay substantially higher prices (accept substantially lower quality), due to weaker competition from other DTSCRs.)

82. The markets in which TVSN supplies its products and services are broader and include more competitors than just DTSCRs. Most directly, home-shopping by catalogue and home-shopping by internet are potential substitutes for consumers with strong preferences for home shopping. In addition, there will be consumers "at the margin" that would substitute between home-shopping and 'bricks and mortar' shopping. The consumers that are "at the margin" are those that would switch in response to a small but significant price change (around 10%). The number of customers "at the margin" may be significant.

83. The following figure provides retail sales in the segments in which TVSN operates (e.g., jewellery, cosmetics, etc). It shows the percentage of sales.[23]

**Figure 9-1: TVSN revenue as a percentage of Australian retail sales (excluding on-line) by segment**

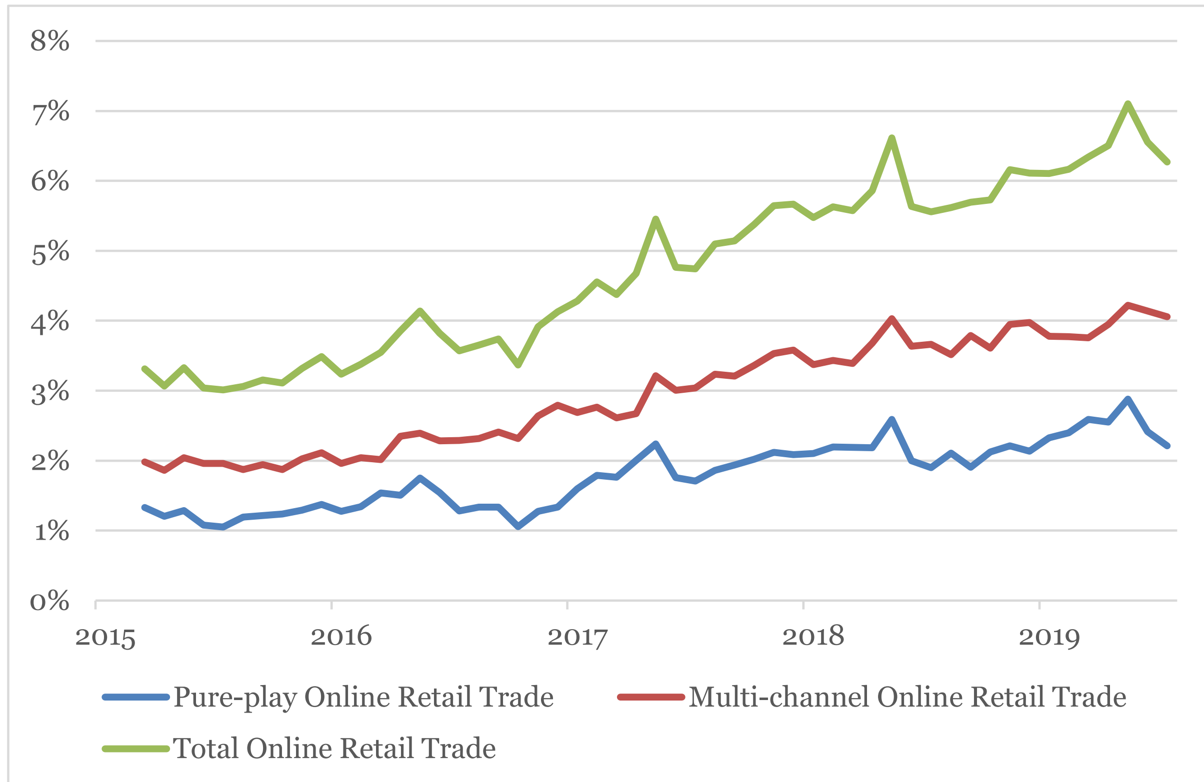



*Source: Statista and TVSN. We match the Statista sub-categories with the TVSN categories. 2019 numbers are estimates only. Statista data are in USD, we use the average AUD/USD exchange rate over the three years (0.73) to convert USD to AUD. Source: Statista and TVSN*

84. The figure shows that sales via TVSN represents only a small fraction of total retail sales (excluding on-line sales) in these segments [Restriction of Publication of Part Claimed]. The following figure shows that on-line sales, which are likely to be predominantly home shopping, are growing significantly, displacing sales in other channels.

[23] The figures combine retail sales figures from Statista along with historic data from TVSN. For the purpose of this chart we assume that TVSN represents all television shopping sales, as the figures are prior to OpenShop's launch in August 2019.

**Figure 9-2: On-line retail sales as a percentage of total retail sales in Australia**




*Source: ABS*

85. An assessment of whether home shopping via DTSCRs is in a separate market to other retail sales platforms requires an understanding of the extent to which customers would substitute between platforms and the margin that is earned on retail sales.

86. If a larger percentage of sales would substitute from one product to another product those products are more likely to be in the same market. In other words, a high elasticity for products sold by DTSCSR would suggest a market for DTSCRs is unlikely to be a separate market to other retail channels for the purposes of analysing the competitive effects of the proposed conduct.[24]

87. We note that the commercial viability of TVSN's conduct does not suggest a narrow market definition. It is likely to be commercially viable for TVSN to require exclusivity because, if it does not, then its DTCSR competitors can free ride on its discovery of

---

[24] [Restriction of Publication of Part Claimed] See Anderson, L.P., McLellan, R.D., Overton, J.P. and Wolfram, G.L. "Price Elasticity of Demand," 13 November 1997. https://scholar.harvard.edu/files/alada/files/price_elasticity_of_demand_handout.pdf

successful brands/products sold via a dedicated TV shopping channel. The conduct is commercial because, absent the conduct, other DTSCRs will free ride on TVSN's past investments.

88. All that is required for this to be the case is that:

- There are attributes about brands/products and their marketing strategy that makes them more or less likely to be successful on DTSCR;
- These attributes are non-obvious and there are costs in identifying them (including costs of trial and error).

89. The commercial viability of the conduct does not depend on non-DTSCRs being weak competitors to DTSCRs.

90. To suggest otherwise would be to suggest that if a car dealer negotiated exclusivity with a car manufacturer for any dealership within 3 km radius then this would imply that the market that car dealer competes within is limited to other dealers within a 3km radius. This simply does not follow. A car dealer requires exclusivity because it has fixed costs of marketing (lot position/signage etc) that a new dealer locating next door with the same product could free ride on.

91. In fact, the more narrowly defined is the market, the less commercially viable would be the proposed exclusivity conduct. If, for example, the market was as narrow as the supply of products to dedicated shopping channels (such that final customers did not regard online/bricks and mortar as a substitute), then in order to achieve exclusivity, TVSN would have to compensate suppliers for giving up the only alternative avenues to sell to the relevant final customer. This would likely be more not less costly.

92. In contrast, if TVSN was seeking exclusivity in its retail channel only (dedicated shopping channels) but it participated in a broader retail market, this would cost it significantly less, as it would not restrict suppliers from pursuing other sales channels (e.g., online, catalogue or bricks and mortar).

93. More generally, the commercial viability of TVSN's market conduct is not necessarily linked to the extent of its market power. As we discuss in our report, the conduct proposed by TVSN appears to have legitimate business purpose separate to any increase in market power including protecting its investments from being held-up, reducing its operational costs and allowing it to position itself in the market (as outlined above).

# 10 Analogy to other markets

94. Many of the points that we have discussed in terms of the rationale for TVSN's conduct have close analogies in relation to the rationale for exclusivity amongst other

retailers (including car dealers) and amongst free to air (FTA) television broadcasters and subscription TV providers.

95. For example, in the sale of motor vehicles it is common to have exclusive arrangements with dealerships. These exclusive arrangements require dealers to only sell the products of one manufacturer. These arrangements are desired because they allow car manufacturers to protect their investments in increasing the knowledge and selling ability of a dealer. They also protect the manufacturer by allowing them to control the branding positioning of their product. The dealerships too may prefer exclusivity as they have their investment in promoting and selling the particular make of car protected from the manufacturer seeking to sell the car through a competing dealer (allowing that competing dealer to free ride on the investment the dealer makes in promoting make of car and the knowledge of customers).

96. Similarly, exclusivity is the norm when dealing with TV station contracts with content providers. This is for precisely the same set of reasons TVSN desires exclusivity:

a. TV stations make investments in promoting and discovering programs. If, once a program is found to be popular, the content owner could simply sell it to another TV station then the original investment in promoting and discovering programs would be unlikely to be made;

b. TV stations choose a suite of exclusive programs in order to position their overall brand offering in a particular way. The ability to do this is greatly enhanced by the ability to show exclusive content. In addition, one station attempting to brand some content as "premium" (e.g., prime time) would be undercut if another station treated it as low quality (e.g., 5 pm)

c. TV stations would suffer from horizontal externalities if they did not have exclusive content. One TV station would be less likely to promote a show if it was, or could be, showing on a rival channel. Similarly, there would be negative externalities if viewers could (deliberately or accidentally) 'skip ahead' to watch future episodes of a series on another station; and

d. TV stations scheduling and promotions would be materially more complicated if they had to factor in the actual, or possible, provision of the same content by other stations. Imagine, for example, a TV station planning to show "Game of Thrones" at a particular set of times only to find that a competitor was intending to show it half an hour earlier on the same day.

e. Finally, there is little reason to believe that the availability of products for TV shopping would be more limited than the availability of content for FTA and subscription TV. Both are similar in that new 'product' and 'content' can, and is, endlessly created to match evolving customer tastes.

# 11 Appendix: sub-categories aligned

97. The following table shows the matching of TVSN segments with sub-categories reported by Statista.

## Table 11-1: Category matching between TVSN and Statista

| TVSN category | Statista sub-category | Statista category |
|---|---|---|
| Fashion | Luggage & Bags | Accessories |
| Fashion | Women's Apparel | Apparel |
| Fashion | Men's Apparel | Apparel |
| Fashion | Children's Apparel | Apparel |
| Fashion | Leather Footwear | Footwear |
| Fashion | Athletic Footwear | Footwear |
| Fashion | Textile & Other Footwear | Footwear |
| Fashion | Luxury Leather Goods | Luxury Goods |
| Fashion | Luxury Fashion | Luxury Goods |
| Fashion | Luxury Eyewear | Luxury Goods |
| Health and Beauty | Cosmetics | Beauty & Personal Care |
| Health and Beauty | Skin Care | Beauty & Personal Care |
| Health and Beauty | Personal Care | Beauty & Personal Care |
| Health and Beauty | Fragrances | Beauty & Personal Care |
| Health and Beauty | Prestige Cosmetics & Fragrances | Luxury Goods |
| Health and Beauty | Analgesics | OTC Pharmaceuticals |
| Health and Beauty | Cold & Cough Remedies | OTC Pharmaceuticals |
| Health and Beauty | Digestives & Intestinal Remedies | OTC Pharmaceuticals |
| Health and Beauty | Skin Treatment | OTC Pharmaceuticals |
| Health and Beauty | Vitamins & Minerals | OTC Pharmaceuticals |
| Home and Outdoor | Living-Room & Dining-Room Furniture | Furniture |
| Home and Outdoor | Bedroom Furniture | Furniture |
| Home and Outdoor | Kitchen Furniture | Furniture |
| Home and Outdoor | Plastic & Other Furniture | Furniture |
| Home and Outdoor | Office Furniture | Furniture |
| Home and Outdoor | Lamps & Lighting | Furniture |
| Home and Outdoor | Floor Covering | Furniture |
| Home and Outdoor | Major Appliances | Household Appliances |
| Home and Outdoor | Small Appliances | Household Appliances |
| Home and Outdoor | TV, Radio & Multimedia | Consumer electronics |
| Home and Outdoor | TV Peripheral Devices | Consumer electronics |
| Home and Outdoor | Telephony | Consumer electronics |
| Home and Outdoor | Computing | Consumer electronics |
| Home and Outdoor | Laundry Care | Home & Laundry Care |
| Home and Outdoor | Household Cleaners | Home & Laundry Care |
| Home and Outdoor | Dishwashing Detergents | Home & Laundry Care |
| Home and Outdoor | Polishes, Room Scents & Insecticides | Home & Laundry Care |
| Jewellery | Watches & Jewellery | Accessories |
| Jewellery | Luxury Watches & Jewellery | Luxury Goods |

*Source: Statista and TVSN*