

Resale price maintenance notification:
response to ACCC Draft Notice

Lodged by:

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1 Background

On 21 March 2023, Graco Australia Pty Ltd (**Graco**) lodged a Resale Price Maintenance Notification with the ACCC (the **Notification**). In the Notification, Graco proposed to require its distributors to advertise its airless and air assisted paint sprayers from entry-level to professional trade products (the **Notified Products**) at or above a minimum advertised price set by Graco (the **Notified Conduct**).

On 31 August 2023, the ACCC issued a draft decision in which it proposed to revoke the Notification on the grounds that the likely benefit to the public would not outweigh the likely detriment to the public from the Notified Conduct (the **Draft Notice**).

This submission contains Graco's response to the Draft Notice. Information confidential to Graco is highlighted **[CONFIDENTIAL TO GRACO]**. In this submission, Graco responds to the ACCC's consideration of the following:

- the future with and without the Notified Conduct (**Section 2**)
- the public detriments resulting from the Notified Conduct (**Section 3**); and
- the public benefits resulting from the Notified Conduct (**Section 4**).

2 Future with and without the Notified Conduct

The ACCC considers that *without* the Notified Conduct distributors are likely to continue to compete on price by offering significant discounts from RRP on the Notified Products. Graco disagrees with this and considers that *with* or *without* the Notified Conduct, distributors will compete on price by offering discounts on the Notified Products. In particular, *with* the Notified Conduct, customers will still be able to negotiate discounts through in-stores quotes, discounts offered through secure internet sites and through discounts offered in online shopping carts (further detail on this is set out below at 3.1(a)). What will change as a result of the Notified Conduct is the aggressive discounting and free-riding of certain online distributors.

The ACCC also considers that *without* the Notified Conduct Graco will have a strong commercial incentive to continue to run spray equipment demonstrations and at distributors' stores and at industry events. Graco agrees with this, but Graco relies on its distributors to demonstrate and discuss in detail the Notified Products with their customers because it cannot do it all itself.

However, Graco agrees with the ACCC's assessment that *without* the Notified Conduct:

- distributors may decide to reduce the range of the Notified Products they stock or display or may cease selling them altogether due to low retail margins; and
- distributors could decide to reduce or cease consumer education activities on Paint Sprayers such as the production and publication of how-to videos and in-store demonstration or off-site paint spray demonstration days.

3 The Notified Conduct is not likely to result in significant public detriment

In the Draft Notice, the ACCC outlines three public detriments that the ACCC considers may arise as a result of the Notified Conduct, namely:

- higher prices for the Notified Products;
- higher prices for competing products; and
- loss of retail product range and choice.

3.1 Higher prices for the Notified Products

The first public detriment identified by the ACCC is higher prices for the Notified Products. The ACCC considers that consumers of Graco products, and particularly contractors, '*are very price driven in relation to paint sprayers and are more interested in getting the best price rather than a demonstration*' (at [5.4]). It considers that the Notified Conduct is likely to increase the margins earned by distributors and therefore the prices paid by consumers. The ACCC concludes that this detriment is likely to be significant, given discounts are regularly 20-30% below RRP.

In response, Graco submits that:

- while some consumers will be interested in price, price is not the only way in which distributors compete and product training, explanation and demonstrations are important as well;
- the Notified Conduct is not likely to substantially increase the prices paid by consumers for the Notified Products; and
- even if the Notified Conduct is likely to increase the prices paid by consumers for the Notified Products, this detriment would not be significant.

Product training, explanation and demonstrations are important, not just price

In Graco's experience, customers including contractors do not always prioritise obtaining the lowest price for a product over receiving a product training, explanation and demonstrations.

This is evidenced by:

- **the number of requests for training and demonstrations that Graco receives from distributors and customers.** For example, between January 2023 and September 2023, Graco received 743 requests for demonstrations, trade days, product service issues, and product trials; and
- **the innovative sales practices of certain distributors who are seeking to provide more demonstrations as part of their sales pitch** – these include trade days and larger-scale training events hosted by paint stores in order to educate the end-user market. For example, **[CONFIDENTIAL TO GRACO]**. Graco considers that the popularity of such events indicates the significance attached by customers to product demonstrations when deciding whether to invest in paint-spraying equipment.

The Notified Conduct is not likely to substantially increase consumer prices for the Notified Products

The ACCC considers that the Notified Conduct is likely to increase the prices paid by consumers for the Notified Products for two reasons. First, the Notified Conduct will disincentivise price competition between retailers. Second, there will not be sufficient competition to limit or negate this detriment.

(a) Disincentivising price competition between retailers

The ACCC notes that price competition for paint sprayers primarily occurs through online and print advertising aimed at attracting customers physically into stores, and that in-store negotiation is not prohibited under the Notified Conduct. Nevertheless, it considers that an increase in the prices paid by consumers is likely as consumers would lose most or all leverage to effectively negotiate discounts (as online prices would essentially be the same).

Graco disagrees with this and considers that the Notified Conduct will not reduce retailers' incentive to compete on the prices for the Notified Products. This is due to the following:

- **The Notified Conduct does not reduce the ability of customers to negotiate discounts with distributors.** Customers will continue to be able to negotiate discounts through:
 - any in-store merchandising, quotes, or contracts;
 - secure internet sites that are not viewable by the public and that are used to conduct business-to-business transactions; and
 - items in internet 'shopping carts' after the customer places the product in the cart by clicking 'order', 'add to cart', or an equivalent demand.
- **Customers have countervailing power.** In Graco's experience, customers are not loyal to one distributor and commonly 'shop around' to obtain the best price or service for a paint sprayer. The risk that existing customers will purchase from alternative distributors will continue to incentivise distributors to compete on prices for the Notified Products. This incentive will be particularly strong for distributors with an existing customer relationship with large contractors who buy in bulk. For example, [CONFIDENTIAL TO GRACO] buys Graco products in bulk from [CONFIDENTIAL TO GRACO]. [CONFIDENTIAL TO GRACO] has contacted Graco's sales representative to negotiate deals in order to ensure that [CONFIDENTIAL TO GRACO] is able to obtain the lowest price possible for Graco paint sprayers. In Graco's experience, this is not limited to just [CONFIDENTIAL TO GRACO]. Other large customers such as airports and councils will frequently obtain quotes from a number of distributors to obtain the best price for the Notified Products. Where this occurs, the distributors will in turn request discounts from Graco. The Notified Conduct will not reduce the incidence of this occurring.

(b) **Insufficient competition**

Second, the ACCC considers that there will not be sufficient competitive constraint to limit or negate this detriment by restraining the prices set by Graco under the Notified Conduct. The primary reason for this is that the market for the supply of paint sprayers in Australia is highly concentrated, with only two established manufacturers: Graco and Wagner.

Graco considers that there will be sufficient competition to constrain the prices set by Graco. Although Graco and Wagner are the two largest suppliers of paint sprayers in Australia, there are a wide range of alternative paint spraying products at different price points.

Other manufacturers of paint sprayers supplying Australia include Atomex, Rongpeng, Ningbo, DP Airless, TriTech, QTech, Ozito and Certa. In particular, Atomex will provide a significant constraint as it is a large supplier that supplies similar products to Graco, that is airless paint sprayers. While the features on Graco and Atomex sprayers are different, they can be used for the same end applications. Moreover, Atomex is distributed in Australia exclusively through the largest dealer in Australia, AA Spray, that sells direct to end users. Graco estimates that AA Spray's sales of Atomex paint sprayers are around

[CONFIDENTIAL TO GRACO] per year.¹ In addition, there are other suppliers of paint sprayers which are manufactured in China and sold on eBay in Australia.

3.2 Higher prices for competing products

The second public detriment identified by the ACCC is that higher retail prices for the Notified Products may encourage manufacturers and distributors of competing products to increase their prices.

For the reasons outlined in Section 3.1 above, Graco considers that the Notified Conduct is not likely to increase the prices paid by consumers for the Notified Products. Accordingly, the second public detriment identified by the ACCC is also not likely to materialise.

3.3 Loss of retail product range and choice

The third public detriment identified by the ACCC is a loss of retail product range and choice (ie, reduced inter-brand competition). The ACCC considers that the Notified Conduct will guarantee distributors a higher margin on the manufacturer's products, and therefore may lead retailers to prioritise stocking the Notified Products over competing brands to maximise profits, particularly where retail floor space is limited. As a result, the ACCC considers that the Notified Conduct may reduce product range, further entrench Graco as the incumbent supplier of paint sprayers, and increase barriers to entry.

Graco does not consider that the Notified Conduct is likely to entrench it as the incumbent supplier of paint sprayers. Graco considers that, for two reasons, there will be a stronger incentive for distributors to stock a greater range of competing products.

First, unlike in relation to the Notified Products, distributors will not be required to advertise competing products at or above a minimum advertised price (**MAP**). In this regard, Graco agrees with the ACCC's observation at 6.52 of the Draft Notice that:

[S]ome distributors (particularly specialty equipment distributors) may limit or cease stocking the Notified Products as they are no longer able to attract customers to their stores with price-based strategies. This could facilitate the entry or expansion of other paint sprayer manufacturers.

Second, Wagner and the other major suppliers of paint sprayers will not reduce its supply of paint sprayers in Australia as a result of the Notified Conduct. In fact, there may be higher sales of other paint spraying brands due to the fact that distributors can discount these sprayers online.

4 The Notified Conduct is likely to result in significant public benefits

4.1 Increased service-based competition in relation to the Notified Products

The ACCC considered that the Notified Conduct is not likely to generate public benefits through an increased provision of pre- and post-sales retail services. In reaching this conclusion, the ACCC considered five factors. Graco responds to each of these in turn below.

Importance of the provision of retail services

The first factor considered by the ACCC was the importance of the provision of retail services in the sale of the Notified Products to consumers. The ACCC concluded, overall, that the sale of the Notified Products did not rely on and would not be significantly enhanced by high levels of retail services. The ACCC individually considered the importance of providing pre-sales and post-sales service.

¹ **[CONFIDENTIAL TO GRACO]**

(a) Pre-sales service

The ACCC considered that pre-sales service does not require prolonged or significant interaction with sales staff. For consumers considering the purchase of a paint sprayer, pre-sales service predominantly relates to assisting with the selection of the most suitable paint sprayer model. For consumers who have used any brand of paint sprayer before, pre-sales service also covers the operational differences between machines.

In Graco's experience, consumers do **not** find the Notified Products simple to use and do not understand all of the benefits without demonstration.² Further, without proper training and product demonstrations, customers will struggle to appreciate the complex features available on these products, and may through incorrect usage damage the products. This is why Graco frequently runs trade days and other forms of demonstrations. Graco has run 743 such events in the past year and has numerous further events scheduled in 2023, including **[CONFIDENTIAL TO GRACO]**.

(b) Post-sales service

The ACCC considered that the proposition that the Notified Products require significant demonstration and after-sales services was undermined by Graco's broad lack of enforcement of its distributor agreement 'obligations' and its recently negotiated agreements with Bunnings.

Contrary to the ACCC's conclusion, Graco has enforced its distributor agreement 'obligations' on a number of occasions. For example, **[CONFIDENTIAL TO GRACO]** Moreover, Graco addresses the level of activity and volume of purchases by distributors each year and, based on its findings, has reduced discounts or closed accounts. **[CONFIDENTIAL TO GRACO]**

In relation to Bunnings, as previously indicated, Bunnings has only recently started selling Graco products and only sells a limited range of products on the 'DIY' end of the product range. In the event that Bunnings were to continue to supply Graco products or expand the range of Graco products that it sells, Graco would ensure that appropriate product demonstrations and post-sales service were also offered in the Bunnings stores.

Whether distributors are best placed to provide retail services

The second factor considered by the ACCC was whether distributors are best placed to provide retail services or whether they could be provided by others, including Graco. In this regard, the ACCC first observes that the required investment by stores into providing the necessary area, equipment and consumables to facilitate in-store demonstrations is likely to be significant. This is one of the key issues that the Notified Conduct is intended to address. That is, the Notified Conduct would provide distributors with a sustainable margin which would then allow them to invest in higher service levels for consumers.

The ACCC then observes that information about the use of the Notified Products appears to be easily accessible by consumers online through Graco's website as well as user-created videos on YouTube. Moreover, it may be that certain information about usage is better provided at the time of use, rather than at the point of sale.

As Graco has previously stated, online videos are no substitute for in person demonstrations. Primarily, this is because paint sprayers *'are technical equipment that require explanation about use and maintenance'* (as the ACCC outlined at 5.4 of the Draft Notice). Further, online videos cannot assist a customer in determining the right paint sprayer for their particular needs. There

² The unique features of the Notified Products are set out at section five of the Notification.

are many variables in spray applications that can only be properly demonstrated through in-person testing, including:

- the paint type used;
- the type of substrate that is being sprayed (eg, roof, door, walls, ceiling, etc.); and
- the level of the painter/application (eg, beginner, intermediate, professional).

The importance of providing in-person product demonstrations and support is evidenced by the significant investments in training made by both Graco (through its 743 trade days and other training events) and distributors such as Dulux.

Finally, while Graco does offer the services and attend the events listed at 6.86 of the Draft Notice, these are a complement and not a substitute to the sales support of the distributors who originally sold the paint sprayers.

Distributors are well placed, and do in fact, provide the necessary retail services. For example, distributors frequently request demonstration equipment at a reduced price from Graco in order to provide product demonstrations to prospective customers. Graco provides a special deal to distributors who request demonstration equipment in order to support distributors' provision of these retail services. For example, in this calendar year alone, Graco has sold **[CONFIDENTIAL TO GRACO]** pieces of demonstration equipment at a reduced price to facilitate demonstrations by its dealers to the value of around **[CONFIDENTIAL TO GRACO]**. These products were provided to **[CONFIDENTIAL TO GRACO]** different distributors.

Material risk of under-provision of retail services

The third factor considered by the ACCC was whether there is a material risk of under-provision of retail services which the Notified Conduct will address. The ACCC considered that the majority of Graco distributors do currently provide high levels of pre- and post-sales services with respect to the Notified Products, noting that market inquiries suggested the majority of paint sprayers are purchased in-store, not online. On this basis, it concluded that there is not a significant free riding problem in the market.

Graco considers that having regard only to the proportion of distributors who provide retail services, and of sales that occur in-store, obscures the extent of the problem that the Notified Conduct seeks to address. The purpose of the Notified Conduct is to prevent 'bricks and mortar', full-service distributors from being required to price-match aggressive online discounts. In doing so, the Notified Conduct seeks to preserve the margins of such distributors and ensure that they can continue to invest in stock, training and after-sales service.

Although the majority of sales of paint sprayers currently occur in-store, the proportion of sales that occur online is growing rapidly. Graco estimates that the proportion of sales occurring online has increased by approximately 30% in the past two years. Therefore, Graco considers that the increase in online sales will result in distributors not providing sufficient pre- and post-sales services. Indeed, this is already occurring as can be seen from the following examples:

- **[CONFIDENTIAL TO GRACO]** communicated an incident from September 2023 in which it provided one of its long-standing customers with high level and lengthy retail support. This included explaining the business application and purpose of an entire range of paint sprayers, as well as travelling to the customer's house to directly swap a Graco UltraMAX sprayer. **[CONFIDENTIAL TO GRACO]** quoted the customer **[\$CONFIDENTIAL TO GRACO]** for the Graco QuickShot sprayer, and **[\$CONFIDENTIAL TO GRACO]** for a whip hose. **[CONFIDENTIAL TO GRACO]** subsequently offered the customer **[\$CONFIDENTIAL TO GRACO]** for the Graco QuickShot (almost **[CONFIDENTIAL TO GRACO]**% off the RRP), **[CONFIDENTIAL TO GRACO]**, **[CONFIDENTIAL TO GRACO]**

and a [CONFIDENTIAL TO GRACO]. Ultimately, [CONFIDENTIAL TO GRACO] price matched [CONFIDENTIAL TO GRACO] in order to maintain the long-standing customer relationship.

- Confidential Attachment A contains a communication from the owner of [CONFIDENTIAL TO GRACO], a [CONFIDENTIAL TO GRACO]-based distributor of Graco products, to Graco. The communication indicates that the costs incurred by [CONFIDENTIAL TO GRACO] in maintaining physical retail services are becoming increasingly commercially unviable. The distributor describes investing significant time in providing retail services to customers who ultimately choose to purchase the relevant product from an alternative, online supplier. It is aware of this practice as the distributor commonly provides post-sales support in the form of product repairs to such online purchasers. The distributor has stopped carrying machinery in its showroom given the difficulties attending the movement of stock. The distributor considers that selling at or close to RRP is necessary for the company to remain profitable. However, it considers that the small volume of products that it sells are sold at such small margins that holding stock is no longer commercially viable. The communication explicitly indicates that if current pricing practices in relation to Graco paint sprayers continue, it will be necessary for [CONFIDENTIAL TO GRACO] to stop recommending and promoting Graco products. Instead, it will favour the paint sprayers of alternative brands, the prices of which are not being reduced to the same extent.

In addition, Graco disagrees with the ACCC's assessment that the Notified Conduct will not encourage more investments in demonstrations. By reducing the extent of advertising price competition between Graco distributors through the MAP, distributors will be encouraged to compete for customers on the basis of retail services without losing the ability to discount for customers in store. For example, the Notified Conduct will encourage competition in relation to sales support, service support, product knowledge, training, demonstrations, trade shows and repairs. As outlined above, [CONFIDENTIAL TO GRACO]. Graco anticipates that there would be other similar events if the MAP can be implemented.

Benefits flowing from ensuring an adequate provision of retail services

The ACCC concluded that it was unclear what significant benefits would flow from increased service levels as a result of the Notified Conduct. Graco considers that there is a significant benefit that would flow from the increased service levels (as a result of the Notified Conduct) – the likely increase in the sales of paint sprayers.

As outlined in the Notification, Graco is seeking to encourage paint contractors to convert from traditional painting methods to spray equipment to increase painting efficiency. By substituting brushes / rollers with paint sprayers, paint contractors spend less time on a job and have the ability to increase the number of jobs they can complete. The process of converting contractors from hand painting to sprayers requires a significant number of demonstrations and training. However, these demonstrations and training sessions increase the costs for both Graco and its distributors as compared to businesses that sell products without demonstrations and training. Therefore, through the introduction of the Notified Conduct, distributors will be able to invest in these demonstrations and training, while still maintaining sustainable margins.

4.2 Increased innovation in Graco's Notified Products

The ACCC accepted that new and especially innovative products may require distributors to undergo additional product training and the current market dynamics of strong price competition could have a chilling effect on distributors stocking such products. It furthermore accepted that, over time, this could lead to a decrease or delay in new Graco paint sprayers being launched in

the Australian market. To the extent the Notified Conduct prevents or limits this, the ACCC considered this would likely be a public benefit.

However, the ACCC did not consider, on the information before it, that this is likely to occur to a great extent given customers are generally very interested in new products and distributors are still likely to want to stock them.

Graco considers that product launches are currently undermined by heavy discounting. In Graco's experience, distributors are less supportive of new and especially innovative product launches that involve significant investment in staff training if they are unable to obtain a viable margin. This impacts the effectiveness of campaigns when new products are launched, damaging the necessary promotion of Graco's new technologies and innovations.

For example, in 2021, Graco launched a new product: the 390PC Cordless Airless Paint Sprayer. This product was the first and remains the only high-performance cordless, stationary, airless paint sprayer on the market. Nonetheless, many distributors were reluctant to buy this product. Graco considers that this was a result of two factors. First, early distributors engaged in significant price-discounting in relation to the product. For example, **[CONFIDENTIAL TO GRACO]** offered a discount of **[CONFIDENTIAL TO GRACO]**% on the product before stock had been made available to it. Second, distributors were reluctant to invest in providing product-specific training for staff in relation to the product, as they considered that they would not have appropriate margins to do so. Since the release of the product, Graco continues to have excess stock, as distributors remain reluctant to acquire it.