



Roxanne Blumenthal
STYROX001

***The Competition Commission's Non-Referral of Exclusivity Clauses in
the Shopping Centre Lease Context: A Monumental Misjudgement***
A Section 5(1) Analysis of Anticompetitiveness

LLM

Supervisor: Judge Dennis Davis

Word Count: 21653

Research paper presented for the approval of Senate in fulfilment of part of the requirements for the LLM in approved courses and a minor dissertation. The other part of the requirement for this qualification was the completion of a programme of courses.

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The Competition Commission’s Non-Referral of Exclusivity Clauses in a Shopping Centre Lease Context: A Monumental Misjudgement

A Section 5(1) Analysis of Anticompetitiveness

“EXCLUSIVITIES AND LETTING RESTRICTIONS

10.1 Save for the Supermarket [Pick n Pay] and Checkers, the lessor shall not permit the following businesses to be conducted in the shopping centre on the property:

10.1.1 a hypermarket or supermarket; or

10.1.2 a store with either a single or several food departments, the aggregate square meterage of which exceeds 100 (one hundred) meters; or

10.1.3 a café or delicatessen which sells fresh fish or meat; or

10.1.4 a grocery, fresh fish shop, butchery, bakery or fruit and vegetable shop.”

The above clause embodies a typical construction of the suspect of anticompetitiveness upon which this paper focuses.

This paper focuses on the common practice in commercial agreements of including exclusivity clauses in shopping centre lease agreements between a supermarket anchor tenant and the landlord of a shopping centre. It is the contention of this paper that such clauses are anticompetitive when considered specifically in light of section 5(1) of the South African Competition Act.¹ In reaching this conclusion, relevant sections of the Act will be interpreted and analysed in the pertinent context, as will relevant case law and comparable foreign jurisprudence. The findings of South Africa’s Competition Commission in 2013 with regard to the competitive nature of exclusivity clauses in the context of section 5(1), and the basis for their findings will be scrutinised. A conclusion, warranted and supported by the inferences drawn from an analysis of the aforementioned sources (legislation, case law and foreign jurisprudence), will be reached accordingly in

¹ 89 of 1998 (the Act).

support of a stance of resistance against exclusivity clauses in shopping centre leases between landlord and supermarkets. An argument in favour of a blanket prohibition of exclusivity clauses in shopping centre leases due to their anticompetitive nature that outweighs their efficiencies and justifications according to section 5(1) of the Act, is the predominant direction of this paper. Additionally, pertinent elements and theories of competition law in general will be stated and analysed in order to support this aforementioned contention, as well as the other various contentions made. Similarly, discourse regarding the cultural conditions of certain markets will be presented in order to adequately justify the competition law contentions made.

An appropriate point of departure is to first examine the backdrop against which the Act was formulated and the motives and goals that the Act aims to achieve. The nature of exclusivity clauses in the lease agreement context, the incentive to include them for both the lessor and the lessee, and the repercussions that they produce for both the lessor and the lessee, will be examined thereafter.

The Purpose of Competition Law Enforcement: Section 2 of the Competition Act

Section 2 of the Competition Act states that:

The purpose of *this* Act is to promote and maintain competition in the Republic in order –

- (a) to promote the efficiency, adaptability and development of the economy;
- (b) to provide consumers with competitive prices and product choices;
- (c) to promote employment and advance the social and economic welfare of South Africans;
- (d) to expand opportunities for South African participation in world markets and recognise the role of foreign competition in the Republic;
- (e) to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the economy; and
- (f) to promote a greater spread of ownership, in particular to increase the ownership stakes of historically disadvantaged persons.

It is with this rhetoric as a backdrop that one is able to judge whether specific conduct or transactions are anticompetitive and thus justify a claim under the Act. This section, embodying the Act's purposes, is unique in the sense that it includes both the traditional

efficiency motives that can be found in the United States (U.S.) and European Union (E.U.) antitrust regimes, as well as certain novel and innovative objectives which are tailored to meet the requirements of the South African competition regime given the historical context from which the country comes.

The discussion that follows includes an examination of the various functions that competition laws serve in different jurisdictions, as well as the primary focus of the competition laws in each respective jurisdiction considered. The individualistic and ‘mixed’ nature of the content intrinsic to South Africa’s Competition policy will be examined, compared to other jurisdictions, and accounted for. The intended outcome of this enquiry is to reveal that South Africa’s unique competition policy does not equate harm to competition merely with harm to efficiency or harm to the competitive process, but includes under the umbrella of harm to competition a lack of fairness and a lack of protection of competitors from competition.

The Focus of the Antitrust Laws in Other Jurisdictions – A Study by Eleanor Fox²

Fox advances an analysis of the different priorities and areas of focus of various jurisdictions. This analysis places into perspective both the originality as well as conformity that exist in the priorities of the South African Competition Act. Fox proposes that there are three categories relevant to the consideration of whether certain conduct harms competition, each incidentally reflective of certain jurisdictions’ competition law regimes either in whole or part or a combination thereof.

The United States of America: Harm to Competition is Harm to Efficiency; The Only Anticompetitive Harm is an Output-Limiting Harm³

“‘Consumer welfare’ and ‘output limitation’ became words that anchored the conversation of antitrust, [with] ‘consumer welfare’ [being] the label given for the *raison d’être* of the new regime...”⁴

² Eleanor Fox is the Professor of Trade Regulation at New York University School of Law.

³ Eleanor M. Fox ‘We Protect Competition, You Protect Competitors’ (2003) 26 (2) *World Competition* 149 at 151 (Efficiency, in this context means the artificial limitation of output and rise in price).

⁴ *Ibid.*

The first category that Fox explores defines harm to competition in terms of the outcome of the particular conduct or transaction; in other words, whether output of the relevant product will probably be artificially reduced and prices will rise as a result.⁵ Therefore, in terms of this category, the primary purpose of the competition laws are to regulate or prohibit conduct or transactions that artificially reduce product output resulting in an increase in price.⁶ The jurisdiction most closely affiliated with these concerns is (as recognised by Fox, and as can be gleaned upon an examination of the jurisprudence of the Supreme Court of the United States) the U.S., whose primary purpose of the antitrust laws is to promote consumer welfare by banning economically inefficient transactions and practices,⁷ and to ensure the unrestrained interaction of competitive forces which are thought to result in the most desirable allocation of resources, namely the lowest prices and highest quality of goods for consumers. In *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*⁸ White, J laid precedent by stating that a restraint or transaction is subject to the *per se* illegality rule (and thus deemed to be an unreasonable restraint on trade for the purposes of s 1 of the Sherman Act⁹) if it is one that would always, or almost always, tend to restrict competition and decrease output, as opposed to one that would increase economic efficiency and render markets more, rather than less, competitive.¹⁰ This precedent was followed in *National Collegiate Athletic Association v. Board of Regents of University of Oklahoma*¹¹ where Stevens, J stated that “[...] by curtailing output and blunting the ability of member institutions to respond to consumer preference, the NCAA has restricted rather than enhanced the place of intercollegiate athletics in the Nation’s life”; this detriment to consumers was considered an unreasonable restraint on trade.

⁵ Supra (n3) at 150.

⁶ This rationale is premised both on the theory of ‘economies of scale’, which reasons that the greater the quantity of a good produced, the lower the cost of producing the good will be, which will result in a lower selling price of the good to consumers. In addition, a reduction in product output will result in an increase in consumer demand for that product, which will result in an increase in consumer willingness to pay a higher price for that sparse product; this increase in willingness will be an incentive for producers to increase the price.

⁷ Robert Pitofsky, Harvey J. Goldschmid & Diane P. Wood *Trade Regulation: Cases and Materials* 6 ed (2010) 6.

⁸ 441 U.S. 1 (1979) (*BMI*).

⁹ 15 U.S.C. §§ 1-7.

¹⁰ *BMI* op cit (n8) at 19.

¹¹ 468 U.S. 85 (1984) (*NCAA*) at 120.

Similarly, in *FTC v. Indiana Federation of Dentists*,¹² it was held that the withholding from customers of a service that they desire was considered an anticompetitive reduction of output. In *California Dental Association v Federal Trade Commission*¹³ Souter, J for the Supreme Court of the United States, stated: “In *National Collegiate Athletic Association v. Board of Regents of University of Oklahoma*, 468 U.S. 85 (1984) we held that a ‘naked restraint on price and output requires some competitive justification...’” Another case reflective of this stance is that of *Toys “R” Us, Inc. v. F.T.C.*¹⁴ where Seventh Circuit Judge Wood held that the policy implemented by Toys “R” Us, which pressurised suppliers to limit the supply of popular toys to warehouse clubs, was an output limitation to the warehouse clubs that diminished consumer welfare by denying the clubs (who were the consumers in this vertical scenario) merchandise, forcing them to buy products they did not want and frustrating end-consumers’ ability to make direct price comparisons of club prices and Toys “R” Us prices;¹⁵ this output-limiting harm to consumer welfare was considered anticompetitive harm.

The aforementioned forms part of, but is not limited to, the U.S. Supreme Court jurisprudence that exists, that supports the notion of product output reduction as an underpinning of U.S. antitrust law enforcement as proposed by Fox.

The U.S. approach above is one that is associated with the Chicago School, which puts consumer welfare at the forefront of antitrust enforcement, intervention being justified in the event of inefficiency - inefficiency in the sense of artificially reducing output and raising price.¹⁶ The Chicago School assigned to competition the primary objective of promoting *economic* efficiency, meaning the optimisation of allocative and productive efficiency: allocative efficiency existing when productive resources are used for the purposes that consumers value most or when all the demand on the market is satisfied; productive efficiency existing when the productive resources are used in a fashion such

¹² 476 U.S. 447, (1986) (*Indiana Federation of Dentists*) at 459.

¹³ 526 U.S. 756 (1999) (*California Dental Association*) at 763.

¹⁴ 221 F.3d 928 (2000) (*Toys R Us*).

¹⁵ Pitofsky op cit (n7) 487.

¹⁶ Fox op cit (n3) 152.

that they reduce their costs in an optimal manner,¹⁷ thereby reducing the eventual price for consumers. Under the Chicago School approach, antitrust enforcement does not concern itself with the protection of small firms from the exclusionary conduct of larger firms, instead asserting that if the former are excluded by the latter due to vigorous competition in the form of increased efficiency or innovation which leads to increased consumer welfare, the latter would not be in violation of the antitrust laws.¹⁸

As will be discussed below, the abovementioned focus on efficiency and output-limitation is not entirely ignored by the objects clause of the South African Act, and its objectives can thus be likened to those of the U.S. However, with regard to the objective of protecting competitors *from* competition, the U.S. stands in stark contrast to the position held by the South African Act and the jurisprudence that emerged in this regard. The Supreme Court of the United States, in *Brown Shoe Co. v. United States*¹⁹ unequivocally stated that “it is competition, not competitors, which the Act protects”,²⁰ and this was confirmed in, *inter alia*, *Atlantic Richfield Co. v. USA Petroleum Co.*,²¹ *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*²² and *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*²³ This confirmation that harm *from* competition can never be a violation of U.S. antitrust law, and that mere unfairness to a competitor does not present an antitrust problem,²⁴ presents a blatant difference in the priorities of the U.S. antitrust laws and those of South Africa’s.²⁵

¹⁷ William E. Kovacic ‘The Intellectual DNA of Modern U.S. Competition Law for Dominant Firm Conduct: The Chicago/Harvard Double Helix’ (2007) 1 (1) *Columbia Business Law Review* 1 at 22; Damien Geradin, Anne Layne-Farrar & Nicolas Petit *EU Competition Law and Economics* 1 ed (2012) 73.

¹⁸ Simon Roberts ‘Competition Policy, Competitive Rivalry and a Developmental State in South Africa’ in Omano Edigheji (ed) *Constructing a Democratic Developmental State in South Africa Potentials and Challenges* (2010) 227.

¹⁹ 370 U.S. 294 (1962) (*Brown Shoe*).

²⁰ *Brown Shoe* supra (n19) at 344.

²¹ 495 U.S. 328 (1990) at 338.

²² 429 U.S. 477 (1977) at 488.

²³ 509 U.S. 209 (1993) (*Brooke Group*).

²⁴ Fox op cit (n3) 154.

²⁵ The specific details of this difference will be discussed under the heading: *Developing Countries – The Significance of Fairness: Harm to Competition Includes Harm to the Competitive Dynamic Among Small Firms; Competition Laws Protect Competitors from Competition.*

The European Union: Competition Laws Protect the Competitive Structure and Operation of Market Mechanisms

“[The competition laws] protect openness of markets, access to markets, and the right of market actors not to be fenced out by dominant firm strategies not based on competitive merits.”²⁶

“[D]o would-be entrepreneurs have equal or ‘fair’ access to the means necessary to attempt a creative breakthrough? Do successful competitors in innovative processes have a ‘fair’ return for their efforts, or access to a ‘fair’ mechanism for determining rewards?”²⁷

The second category advanced by Fox defines harm to competition in terms of conduct or transactions that undermine the market mechanism, including unjustified exclusionary practices.²⁸ In other words, conduct that jeopardises the competitive process in a market will warrant a competition law claim, in the absence of proof of a procompetitive justification. Under this category, the primary purpose of the competition laws is to ensure that the markets are free from conduct that classifies as anticompetitive obstructions. The protection of the market in this manner has a follow-on effect of consumer advantage since, as Frédéric Jenny explains, “more market competition means that the efficiency gains in production and distribution are passed on to consumers and that innovations reach the market place.”²⁹ Similarly, The European Competition Commissioner, Mario Monti, states that “the fundamental role of the market and of competition [is] guaranteeing consumer welfare, encouraging the optimal allocation of resources and granting to economic agents the incentives to pursue productive efficiency, quality and innovation.”³⁰

Taking into consideration the above justifications for EU Competition law, the similarities between the EU and US models become manifest, specifically with respect to the fact that

²⁶ Fox op cit (n3) 155.

²⁷ Paul Geroski and Alexis Jacquemin ‘Dominant Firms and their Alleged Decline’ (1984) 2 (1) *International Journal of Industrial Organization* 22.

²⁸ Fox op cit (n3) 150.

²⁹ Frédéric Jenny ‘Globalization, Competition and Trade Policy: Covergence, Divergence and Cooperation’ in Clifford A. Jones & Mitsuo Matsushita (eds) *Competition Policy in the Global Trading System: Perspectives from the EU, Japan and the USA* (2002) 297.

³⁰ Barry Hawk (ed) *International Antitrust Law & Policy: 2000 Fordham Corporate Law Institute* (2001) 257.

consumer welfare and efficiency considerations are the primary concerns of competition law enforcement. There are differences, however, and those materialize in the form of the most appropriate means via which the common, primary concerns are to be addressed and advanced. For the United States, artificial output-limitation - the primary concern that is sought to be addressed - is the essence of anticompetitive behaviour that jeopardises consumer welfare and efficiency, and thus regulation focusing primarily thereon is the ideal manner in which the purpose of competition law is to be achieved. For the European Union, on the other hand, conduct that threatens the open market, and competitive process unimpeded by private firm obstructions is the essence of anticompetitive behaviour, and are the primary concerns sought to be addressed; thus regulation that focuses primarily on addressing those elements is the ideal manner to achieve the purpose of competition law.

There exists in the European regime pertinent regulations aimed at achieving the aforementioned purposes. Article 82 of the Treaty of Rome³¹ establishing the European Communities prohibits the abuse of dominance thereby regulating the behaviour of dominant firms so that they do not unfairly use their power and take undue advantage of other market players such as buyers, sellers and competitors.³² Similarly, Article 3(1) explicitly recognises the protectionist objective of the competition laws by requiring a system that ensures competition in the internal market is not distorted, thereby condemning unjustified exclusionary practices as having the result of distorting the normal functioning of the market on competitive merits.³³

A significant illustration of the Court of Justice's contempt towards conduct that impairs undistorted competition on the common market, is inherent in the judgment of *Hoffmann-La Roche & Co. AG v Commission of the European Communities*.³⁴ The court states that a contract between two manufacturer competitors whereby the one agrees to buy its product exclusively from the other above the former's own manufacturing capacity, is "incompatible with the objective of undistorted competition within the common market,

³¹ 1957.

³² Fox op cit (n3) 157.

³³ Fox supra (n33) at 156.

³⁴ Case 85/76, [1979] ECR 461 (*Hoffmann-La Roche*).

because [it is] not based on an economic transaction which justifies this burden or benefit but, [is] designed to deprive the purchaser of, or restrict his possible choices of supply, and to deny other producers access to the market.”³⁵ In *Tetra Pak International SA v Commission of the European Communities*,³⁶ a dominant manufacturing firm implemented unjustifiable³⁷ tying and exclusive dealing contracts. The Court of Justice confirmed the Court of First Instance’s declaration that a firm in a dominant position who implements the practices of exclusive dealing or tying, is abusing its position since it is depriving customers of the ability to choose their sources of supply and denying other producers access to the market.³⁸ The Court of Justice acknowledged and applied Article 86, which requires special responsibilities of a dominant firm such as Tetra Pak, who has “freedom of conduct compared with other economic operators, [...] such as to impose on it a special responsibility under Article 86 to maintain genuine undistorted competition on those markets.”³⁹

In sum, the focus of the EU competition laws can, therefore, be likened to the idiosyncrasies of the Chicago School abovementioned, but only in part, since the most characteristic feature of the EU regime’s focus is on the right of market actors to enjoy access to the market on their merits and to ensure that non-dominant firms have the freedom to trade without artificial obstruction by dominant firms; The preservation of this freedom is integral to the legitimacy of the competition process and stands to benefit all market players including competitors and consumers.⁴⁰ This is not to say, however, that US law does not protect against harm to the dynamic and beneficial facets of the competition process at all, unless the effect of output-limitation is evident in the exclusionary practice: in *Indiana Federation of Dentists* the Supreme Court held that the dentists’ conduct disrupted the proper functioning of the price-setting mechanism of the

³⁵ *Hoffmann-La Roche* supra (n34) at para 90.

³⁶ C-333/94P, [1996] ECR I-5951 (*Tetra Pak*).

³⁷ The test to determine whether the practice is justifiable comes from *Stergio Delimitis v Henninger Bräu AG*, [1991] ECR I-935 para 21-27 where it must first be asked whether the restraint or conduct has a ‘sealing-off’ effect’, making access to the market difficult; if the answer is in the affirmative then the restraint or conduct is anticompetitive and must be objectively justified (Fox op cit (n3) 158).

³⁸ *Tetra Pak* op cit (n36) at para 137.

³⁹ *Tetra Pak* supra (n38) at para 22.

⁴⁰ Fox op cit (n3) 157-158.

market by deciding themselves that customers did not need that which they demanded.⁴¹ When one is cognisant of the general trends, however, it can be said, with a degree of confidence, that the concerns of output limitation and protection of the competitive process are at the forefront of the focus of the US and EU regimes respectively.

Developing Countries – The Significance of Fairness: Harm to Competition Includes Harm to the Competitive Dynamic Among Small Firms; Competition Laws Protect Competitors from Competition⁴²

Under the regime of many developing countries, Fox notes, is an approach to anticompetitive conduct that is informed by *fairness*. Fairness, in this context, is a standard used to protect competitors from competition itself. The Indonesian case of *Indomaret*⁴³ involving the proposed development of larger franchise stores that stood to jeopardise the preservation of small, independent stores, effectively illustrates the fairness principle: the former were enjoined by the Indonesian Competition Commission in order to protect against the destruction of traditional local communities.⁴⁴ Fox encapsulates the fairness doctrine by noting that ‘the Commission may have perceived that the social costs to the people as citizens of the local communities were greater than the gains from low prices and variety realized by the people in their role as consumers.’⁴⁵ Therefore, as Fox succinctly categorises competition policies of this type: harm to competition includes harm from low prices or other efficient strategies that directly benefit consumers.⁴⁶ This additional focus on fairness as opposed to a sole focus of consumer welfare in a competition law regime, stands in sharp contrast to the US and Chicago School approaches discussed in the above paragraphs.

The case for a fairness component in competition law and policy was memorably made by Kyu-Uck Lee⁴⁷ where he explained that if the outcome of competition is to be accepted by the society at large, then the process of competition must not only be free but also conform

⁴¹ *Indiana Federation of Dentists* op cit (n12) at 461-462.

⁴² Fox op cit (n3) 162.

⁴³ P.T. Indomarco Prismaatama, 03/KPPU-L-1/2000.

⁴⁴ Fox op cit (n3) 163.

⁴⁵ *Ibid.*

⁴⁶ Fox op cit (n3) 150.

⁴⁷ Professor Lee was then the president of the Korea Institute for Industrial Economics & Trade and Chairman of the Competition Advisory Board for the Korean Fair Trades.

to a social norm; that is, it must also be fair.⁴⁸ If it is not fair, Lee continues, ‘the freedom to compete loses its intrinsic value. Fair competition must go in tandem with free competition. These two concepts embody one and the same value. This may be the reason that competition laws of several countries [...] clearly specify “fair and free competition” as their crown objective.’⁴⁹ Lee then places the fairness component and its import in the specific context of developing countries:

‘In a developing economy where [...] economic power is not fairly distributed, competition policy must play the dual role of raising the power [...] of underprivileged economic agents to become viable participants in the process of competition on the one hand, and of establishing the rules of free and fair competition on the other. If these two rules are not met, unfettered competition will simply help a handful of privileged big firms to monopolize domestic markets that are usually protected through import restrictions. This will then give rise to public dissatisfaction since the game itself has not been played in a socially acceptable, fair manner.’⁵⁰

The fundamental notion that should be extracted from Professor Lee’s position, is that cultural and normative conditions affect the discourse of competition policy and what is considered to be anticompetitive. The relation of Professor Lee’s observations to the unique, ‘hybrid’ nature of South African competition law, particularly its focuses and functions, is particularly appreciable.

South African Competition Law – An Amalgamation of Efficiency and Social Objectives

“The Act reflects the government’s aims to incorporate particular public interest policies that reflect the changing socio/economic and political context within which the Act was promulgated.”⁵¹

⁴⁸ Kyu-Uck Lee ‘A “Fairness” Interpretation of Competition Policy with Special Reference to Korea’s Laws’ in *The Symposium in Commemoration of the 50th Anniversary of the Founding of the Fair Trade Commission in Japan, Competition Policy for the 21st Century* (1997) 61 KFTC (on file with author)

⁴⁹ Ibid.

⁵⁰ Ibid.

⁵¹ Kim Kempel ‘The Role of South African Competition Law in Supporting SMEs: Can David really take on Goliath?’ 1 - Summary of a paper prepared for 48th ICSB World Conference “Advancing Entrepreneurship and Small Businesses” 15-18 June 2003, Belfast, Northern Ireland, available at <http://www.comtrib.co.za/assets/Uploads/Speeches/kim.pdf> accessed on 18 February 2015.

Lewis describes the South African Competition Act as being deeply rooted in a dominant narrative of a “concentration of ownership of private wealth in the hands of a small number of large corporations [...] that were in turn controlled by a select group of white families”; with the counterpoint of this concentration of private wealth and economic power being the dispossession, poverty and unequal and unfair treatment of the majority black population.⁵² As a result, Davis states, with specific reference to the Act, that “the preamble and s 2 [...] enjoin an interpretation of the entire Act which is congruent with the promotion of an economy that will benefit all South Africans, will address historical disadvantage, and will promote the democratisation of the economy.”⁵³

⁵² David Lewis *Thieves at the Dinner Table: Enforcing the Competition Act* (2012) 5.

⁵³ D M Davis ‘*The Development of Competition Law and Economics in South Africa*. By Kasturi Moodaliyar & Simon Roberts (eds): Book Review’ (2014) 131(3) *South African Law Journal* 712 at 712. The Preamble of the Act states:

The people of South Africa recognise:

That apartheid and other discriminatory laws and practices of the past resulted in excessive concentrations of ownership and control within the national economy, inadequate restraints against anticompetitive trade practices, and unjust restrictions on full and free participation in the economy by all South Africans.

That the economy must be open to greater ownership by a greater number of South Africans.

That credible competition law, and effective structures to administer that law, are necessary for an efficient functioning economy.

That an efficient, competitive economic environment, balancing the interests of workers, owners and consumers and focussed on development, will benefit all South Africans.

IN ORDER TO –

provide all South Africans equal opportunity to participate fairly in the national economy;

achieve a more effective and efficient economy in South Africa;

provide for markets in which consumers have access to, and can freely select, the quality and variety of *goods and services* they desire;

create greater capability and an environment for South Africans to compete effectively in international markets;

restrain particular trade practices which undermine a competitive economy;

regulate the transfer of economic ownership in keeping with the public *interest*;

establish independent institutions to monitor economic competition; and

give effect to the international law obligations of the Republic.

With this milieu in mind, the plurality of goals of South Africa's Act becomes evident: Sections 2(c) onwards can be perceived as a recognition of the need for protection *from* competition, as well as encapsulating the potential that competition law has to address the injustices of our country's past through public interest considerations. Furthermore, section 2(c) onwards encapsulates Kyu-Uck Lee's narrative of competition policy in developing economies, a group of which South Africa forms part, as one that is fair and conforms to a social norm where it (competition policy) plays the dual role of raising the power of underprivileged economic agents to become viable participants in the competitive industry, and establishing the rules of free and fair competition.⁵⁴ Sections 2 (a) and (b), on the other hand, can be perceived as a reflection of the traditional and perhaps mandatory-like efficiency motives and considerations that require encapsulation in any effective competition law regime, and which can be observed in both the US and EU regimes as made evident above, i.e. those that protect and promote the competitive process through the advancement of rivalry among market actors, the prohibition of interference with the natural flow of competition through exclusionary practices and ensuring that the market works freely, to the advantage of the entire citizenry, and that consumers have a wide range of choice of product at a competitive price.⁵⁵

The former, public interest based components – included in section 2 and the preamble of the Act - compared to the latter mandatory-like efficiency considerations, are unique to the South African Competition Law Act and the result is that there is “little assistance which can be gleaned from other jurisdictions on how to balance the issues of public interest with standard cognisable competition considerations.”⁵⁶ Despite this factor, much of these unique intentions and objects of the Act can be gleaned from the actual language thereof which, as aforementioned, is profoundly indicative of the historical context from which it arose. When balancing the two competing interests, it is similarly important to reiterate the abovementioned words of Professor Lee which resonate with the underlying objectives of South Africa's Act. Those words emphasise that if competition policy does not raise the power of underprivileged economic agents to become viable participants in the

⁵⁴ Kyu-Uck Lee op cit (n48).

⁵⁵ Fox op cit (n3) 151; Davis op cit (n53) 712.

⁵⁶ Davis op cit (n53) 713.

competition process, as well as establish rules of free and fair competition, then unfettered competition will result, and a handful of privileged big firms will easily be able to monopolize domestic markets, giving rise to public dissatisfaction, as the game will not be seen to be played in a socially acceptable, fair manner.⁵⁷ It is now plain that the existence of the public interest considerations in the Act cannot only be attributed to South Africa's historical context, but also to the role that they play in realising fairness in the competitive game; fairness understood in its extensive sense as outlined above.

The Nature and Purpose of South African Competition Law: An Incongruity with Exclusive Leases

The various purposes enshrined in South Africa's Competition Law regime are profoundly jeopardised by the practice of exclusive leases in the shopping centre context. In the pages that follow, it will be demonstrated that exclusive leases negatively impact the specific purposes enshrined in sections 2(a) – (c) and (e) of the Act. Whether the Competition Commission adequately balanced and considered social and efficiency interests (within the terms of their proper meanings that have been discussed above) in order to achieve a well-rounded sense of justice when arriving at their conclusion that exclusive lease agreements did not satisfy the tests in the Act to justify a claim or produce anticompetitive effects, will be examined in the following pages. Specific reference to the aforementioned sections and the manner in which exclusive leases violate their substance will be predominantly focused on in the section that determines whether exclusives have the effect of substantially preventing or lessening competition in a market.

It is instructive in the first instance to undergo an impartial assessment of exclusive lease agreements, namely the nature thereof, the incentives therefor and repercussions thereof.

⁵⁷ Kyu-Uck Lee op cit (n48).

Nature of Exclusive Lease Agreements⁵⁸

The type of exclusive lease agreements upon which this paper focuses, are those within a shopping centre context where the lessee or tenant is a retail store or supermarket and the lessor is a developer or landlord of land that has been purchased for the purpose of conducting the business of a shopping centre. These particular exclusive clauses in shopping centre lease agreements impose limits on the use of the shopping centre's other leasable premises;⁵⁹ the most common of exclusivity clauses within the shopping centre context – and the type around which this paper centres – are those that, at the behest of the lessee, prohibit the lessor from renting space in the shopping centre to other general or specialised businesses that would compete with the lessee's store, and/or grant the lessee the exclusive right to sell certain lines of merchandise within the centre.⁶⁰ Such clauses ultimately prohibit landlords from permitting excessive competition from another supermarket and speciality food store in the same shopping centre.⁶¹

Incentives for, and Repercussions of Exclusives in Shopping Centre Leases

The common practice of including long-term exclusives in lease agreements has been said to stem primarily from a landlord's need to secure the necessary funds for financing the construction of the centre which is to be built on the purchased land.⁶² Pollack explains that credit-providing institutions are, unsurprisingly, more inclined to finance a shopping centre if they are satisfied that the venture will be successful and longstanding; integral to the assurance of such attributes in a shopping centre scheme is the presence of large

⁵⁸ The term 'exclusive lease agreements' will be used interchangeably with 'exclusives', 'exclusive clauses' or 'exclusivity clauses in lease agreements'.

⁵⁹ Emmanuel B. Halper 'Supermarket Use and Exclusive Clauses' (2002) 30 (2) *Hofstra Law Review* 297 at 299.

⁶⁰ David C. Baum 'Lessors' Covenants Restricting Competition' (1965) *University of Illinois Law Forum* 228 at 228; Benjamin Pollack 'Shopping Center Leases' (1960-1961) *University of Kansas Law Review* 379 at 389; Alan Schapiro 'Exclusive Rights Clauses in Shopping Centre Leases' (1985-1986) 24 *Alberta Law Review* 510 at 510.

⁶¹ Halper op cit (n59) 299.

⁶² Morris L. Sweet 'Tenant-Selection Policies of Regional Shopping Centers' (1959) *Journal of Marketing* 399 at 399.

retailer tenants that are historically successful,⁶³ have ‘pulling power’ – the ability to attract foot traffic into the centre– and can ‘anchor’ the centre for an extended period of time.⁶⁴

The success of supermarkets – and their consequent attractiveness for shopping centre developments - can be attributed mainly to their provision of optimum convenience for consumers: a wide variety of products are conveniently situated in one place and displayed on shelves in an accessible and organized way; the opening hours are usually long, further catering to convenience; the existence of various brands and their differing prices allow consumers to make comparisons and save money. Reardon, Timmer and Barrett et al attribute the consumer demand for supermarkets to: 1) urbanization: the entry of women into the work place increased the desire for shopping convenience and processed foods which save cooking time and 2) the reduction in processed food (which forms the bulk of supermarkets’ merchandise) prices as a result of the increased level of production thereof (economies of scale) as well as greater variety made available.⁶⁵

A further incentive to include a supermarket in a shopping centre will originate from the shrewd business acumen of the lessor. Since most families do their shopping at a supermarket, when a supermarket is in a shopping centre, consumers are within strolling distance of the other stores in the centre, creating a better chance of consumers exploring the other stores, making the leasable space within the centre more appealing to other merchants, thus creating further profit for the landlord as demand in the centre exists.⁶⁶

It is evident from these considerations that it is the lessor who ‘needs’ the supermarket more than the supermarket ‘needs’ the lessor. The supermarket lessee is thus in a strong bargaining position, as it is mindful of its appeal to both consumers and shopping centre landlords alike, and this may result in pressure being placed on the landlord to accede to

⁶³ Thomas Reardon, C. Peter Timmer, Christopher B. Barret & Julio Berdegué ‘The Rise of Supermarkets in Africa, Asia and Latin America’ (2003) *American Journal of Agricultural Economics* 85 (5) 1140 at 1141.

⁶⁴ Pollack op cit (n60) 379.

⁶⁵ Reardon *et al* op cit (n63) 1141.

⁶⁶ Halper op cit (n59) 299.

the demands of the supermarket lessee, and for the supermarket lessee to abuse this powerful position that it finds itself in.⁶⁷

One of the forms of abuse that may be discharged by supermarkets is through the unlawful restriction of competition. The obvious incentive, accomplished through the inclusion of an exclusive, of the supermarket lessee is to dilute any competition which may encroach on its territory by selling similar goods, and thereby threaten its sales of goods and resultant profits. Referred to by Sweet as 'tenant selection policies', exclusives are said by him to have the general effect of planning or limiting competition, protecting against undue competition from new tenants and limiting the introduction of new merchandise lines by existing tenants.⁶⁸ The power given to tenants, through exclusives, over the selection of additional tenants to the centre as well as over other existing tenants' merchandise operations, has the result of excluding and keeping at a distance other retailers from shopping centres wherein the tenant utilizes space. It is this very incentive and repercussion with which this paper concurs, remains concerned with and shall develop upon later in light of specific competition law concerns in the context of section 5(1) of the Act.

In order to decipher whether this planning or limiting of competition and protection against undue competition justifies a claim under the South African Competition Act, an identification first of the relevant and applicable sections in the Act is required, and secondly an analysis determining whether such agreements are anticompetitive in terms of the essential elements and tests demanded of those sections is required. It is instructive, however, to precede this practical analysis with a concise explanation of the events that led up to the contentious decision by the Commission to not refer the matter to the Tribunal.

⁶⁷ Sweet op cit (n62) 400.

⁶⁸ Sweet supra (n67) at 399.

The Competition Commission

The Competition Commission is one of the institutions that are responsible for the application of the Act.⁶⁹ The Competition Commission is responsible for, *inter alia*, the investigation, control and evaluation of restrictive practices and abuse of dominant positions. The Commission's strong powers of investigation ensure the objective of making markets work better through the promotion of effective competition and by regulating the conduct of businesses.⁷⁰ Part of the Competition Commission's mandate is thus to investigate all complaints, which can be brought by any person,⁷¹ of prohibited or anticompetitive practices across South Africa's economy.

'The Supermarket Investigation'⁷²

In 2009, the Competition Commission initiated an investigation into the four major supermarkets: Pick 'n Pay, Shoprite/Checkers, Woolworths and Spar as well as the two major wholesaler-retailers: Massmart and Metcash ("the supermarket investigation") for alleged contraventions of the Competition Act. The investigation followed from preliminary research within this sector where the following competition concerns were highlighted: long term exclusive lease agreements, information exchange, category

⁶⁹ Minette Neuhoff (ed), Marylla Govender & Martin Versfeld et al *A Practical Guide to the South African Competition Act* (2006) 18. The other two institutions responsible for the application of the Act are the Competition Tribunal and the Competition Appeal Court.

⁷⁰ Kasturi Moodaliyar & Simon Roberts (eds) *The Development of Competition Law and Economics in South Africa* (2012) ix; Neuhoff *et al* op cit (n69) 19.

⁷¹ Section 49B(2) of the Act.

⁷² The official Competition Commission report was unavailable for perusal for this paper due to confidentiality issues; the following account appears from the Competition Commission's media releases and legal firms' reports: Ian Jacobsberg & Janine Reddi 'The War of the Titans' available at <http://www.hoganlovells.com/the-war-of-the-titans-12-01-2013/> accessed on 18 February 2014; Media Release: 27 January 2011 'Competition Commission Findings of the Supermarket Industry Probe' available at <http://www.compcom.co.za/wp-content/uploads/2014/09/Supermarket-Investigation-Release.pdf> accessed on 18 February 2014; Media Release: 24 January 2014 'Commission non-refers Supermarkets Investigation' available at <http://www.compcom.co.za/wp-content/uploads/2014/09/Commission-non-refers-supermarkets-investigation.pdf> accessed on 18 February 2014; 'The Supermarket Investigation: Progress Report' available at <https://www.ensafrika.com/news/the-supermarket-investigation-progress-report?Id=195&STitle=competition%20ENSight> accessed on 18 February 2014; Neil Gopal 'Property Owners Urge Competition Commission Action against Pick n Pay, Spar, Shoprite' available at <http://www.biznews.com/property/2014/10/07/property-owners-urge-competition-commission-to-act-against-pick-n-pay-spar-shoprite-neil-gopal/> accessed on 19 February 2015.

management and concentration of buyer power. In 2011 the Commission publicly announced that there was insufficient evidence to show a contravention of the Act with respect to information exchange, category management and concentration of buyer power; however, it remained concerned with long term exclusive lease agreements which it believed may indeed amount to a contravention of the Act, especially in circumstances where supermarkets have market power.

The types of exclusive leases with which the Commission was concerned, related to those that give supermarkets, who play a role as ‘anchor tenants’ – which typically provide tenants with a lease of a minimum period of ten years with renewal options up to 40 years - the sole right to trade as food retailers in the shopping centre or property development which they are situated. The exclusivity agreements often also include restrictions on the type of non-supermarket tenants the landlord can allow in the centre, thereby preventing bakeries, butcheries and other part-line stores from entering the centre in question. The primary potential concerns that such agreements raised for the Commission were:

- 1) The heightening of entry barriers for smaller and independent firms;
- 2) Anticompetitive effects in circumstances where the Supermarket chains have market power within the relevant local markets. The Commission stated that it believed exclusive leases in these local markets to be unjustified and resulting in the anticompetitive outcome of enabling supermarkets to maintain their position of market power.

As stated in their media releases - a summarized reflection of their official report on the Supermarket Investigation - the Competition Commission found that exclusivity clauses stand to be considered under section 5(1),⁷³ section 8(c)⁷⁴ and section 8(d)(i)⁷⁵ of the Act.

⁷³ **5. Restrictive vertical practices prohibited**

- (1) An *agreement* between parties in a *vertical relationship* is prohibited if it has the effect of substantially preventing or lessening competition in a market, unless a party to the *agreement* can prove that any technological, efficiency or other pro-competitive, gain resulting from that agreement outweighs that effect.

⁷⁴ **8. Abuse of dominance prohibited**

It is prohibited for a dominant *firm* to –
[...]

Another section clearly affected by exclusive lease agreements of this type, is not only the objects clause (section 2) generally - as outlined above in the section discussing the nature of South African Competition Law - but also section 2(e).⁷⁶ Despite the inability of the section 2 concerns to raise a cause of action themselves, they are, and will be shown to be, useful interpretive aids in reaching a conclusion of anticompetitiveness in the section 5(1) context. Potential public interest concerns enshrined in the objects clause, attention to which will be specifically directed at the applicable moment, raised by exclusivity clauses also stand to be considered. Several months after the investigation the Competition Commission concluded with findings that, despite the barriers raised by the practise to entry into grocery retailing, there was not sufficient evidence to meet the tests set out in the Act to demonstrate anticompetitive effects.

In order to decipher whether the Competition Commission's contention has any justifiable basis, that is, that the tests required by section 5(1) of the Act required to prosecute a firm and impose a blanket prohibition on exclusivity clauses in lease agreements, were not met, it is necessary to meticulously examine the way in which each element of section 5(1) of the Act was purportedly applied by the Commission.

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- (c) engage in an *exclusionary act*, other than an act listed in paragraph (d), if the anti-competitive effect of that act outweighs its technological, efficiency or other procompetitive gain;

⁷⁵ **8. Abuse of dominance prohibited**

It is prohibited for a dominant *firm* to –
[...]

- (d) engage in any of the following *exclusionary acts*, unless the *firm* concerned can show technological, efficiency or other procompetitive gains which outweigh the anticompetitive effect of its act –
 - (i) requiring or inducing a supplier or customer to not deal with a competitor.

⁷⁶ **2. Purpose of Act**

The purpose of *this Act* is to promote and maintain competition in the Republic in order –
[...]

- (e) to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the economy;

The Restriction of Competition – A Potential Contravention of Section 5(1) of the Act

The Competition Commission stated that exclusivity clauses stand to be considered under section 5(1) of the Competition Act. Section 5(1) of the Act prohibits restrictive vertical practices by stating that:

‘An agreement between parties in a vertical relationship is prohibited if it has the effect of substantially preventing or lessening competition in a market, unless a party to the agreement can prove that any technological, efficiency or other pro-competitive, gain resulting from that agreement outweighs that effect.’

A thorough consideration of the salient elements of this section is required in order to justify the Commission’s conclusion that exclusive lease agreements do indeed stand to be considered under section 5(1) of the Act, and more importantly, whether exclusive lease agreements, when considered under section 5(1), do not demonstrate anticompetitive effects justifiable of a referral to the Tribunal for prosecution. Due to both its extreme significance and convolutedness in the exclusive lease agreement context, the first element of section 5(1) that will be analysed is that of market definition.

‘...has the effect of substantially preventing or lessening competition *in a market*...’

‘By affording statutory recognition to the concept of the “market” in the Act, the legislature has ostensibly accepted an essential prerequisite for sound competition analysis, namely identifying and circumscribing the relevant market in which effective competition is perceived to be under threat.’⁷⁷

For the sake of practicality, the second element, ‘in a market’, of this two-stage enquiry will be elaborated upon first. Due to the fact that competition takes place in a market, in order to illustrate that competition has been substantially prevented or lessened in a market, the *relevant* market in which the competing parties compete and where competition is allegedly prevented or lessened, must first be defined or delineated.⁷⁸ Neuhoff *et al* have defined the relevant market for the purposes of a section 5(1) enquiry as

⁷⁷ Pierre E. J. Brooks ‘Defining a “Market” in South African Competition Law’ (2001) 13 *SA Mercantile Law Journal* 269 at 269.

⁷⁸ Neuhoff *et al* op cit (n69) 97.

referring to the arena of competition that is relevant to the issue under investigation, namely the products, geographic area and level of supply chain relevant to the analysis.⁷⁹

Case law has demonstrated that defining the relevant market is not as complex and intricate an inquiry as that which may appear from the aforementioned formal denotation provided by Neuhoff *et al.* Brooks goes as far as stating that ‘one is left with the impression that the Tribunal follows an intuitive approach in determining the product and geographic dimensions of a market.’⁸⁰ The jurisprudence of the Competition Tribunal reflects this position. In *The Competition Commission v South African Airways (Pty) Ltd*,⁸¹ a relevant market definition was not arduously or formally defined via a meticulous consideration of the products, geographic area or level of supply chain. The two markets judged to be the relevant ones were simply those of travel agency sales of domestic flights in South Africa and scheduled domestic flights in South Africa.⁸² A similarly loose relevant market categorisation was stated in *Mandla-Matla Publishing (Pty) Ltd v Independent Newspapers (Pty) Ltd*⁸³ where the relevant market was considered to be that of the distribution of newspapers in the isiZulu language newspaper market, and in *Uniplate Group (Pty) Ltd v New Number Plate Requisites CC*⁸⁴ it was again loosely defined as that relating to the manufacturing and supplying of blank number plates in the Gauteng area.⁸⁵ In *Imperial Holdings Ltd and National Airways / Finance Corporation Limited*⁸⁶ the relevant market was defined as that of the small aircraft charter market as opposed to the chartering and leasing of large commercial aircraft. In light of the aforementioned, it is contended that a simple, logical categorization of the product and geographic market involved is necessary for the relevant market inquiry.

⁷⁹ Ibid.

⁸⁰ Brooks op cit (n77) 279.

⁸¹ [2005] 2 CPLR 303 (CT) (*South African Airways*) Despite *South African Airways* being centred around a s 8 abuse of dominance enquiry, a comparison can be drawn between a s 8 and s 5(1) enquiry with respect to the requirement of defining a relevant market: It was held in *South African Airways* that it needs to be established that dominance is present *in respect of some market* for the conduct alleged to be abusive or unlawful; This logically entails that a s 5(1) enquiry would require the need to establish that there was a substantial prevention or lessening of competition *in respect of some market* in order for the agreement under discussion to be prohibited.

⁸² *South African Airways* supra (n81) at 319.

⁸³ [2006] 2 CPLR 499 (CT) (*Mandla-Matla*) 517.

⁸⁴ [2013] 1 All SA 231 (GSJ) (*Uniplate*)

⁸⁵ *Uniplate* supra (n84) at 239.

⁸⁶ (24/LM/Feb00) [2007] ZACT 7 (*Imperial Holdings*) at para 6-7.

An analysis of the *structure* of the market, that is, the position of the party accused of the contravention in that respective market, is necessary.⁸⁷ The position of the party in respect of the market will be decisive in determining whether that party has market power, in other words, it will determine whether that party possesses such a high market share that it has the ability to raise prices above the competitive level in that market,⁸⁸ and behave independently of its competitors. If a firm is positioned in a market such that it has the ability to raise prices and exclude competition, then it will be inferred that the firm has monopoly power.⁸⁹ The more prominent either the upstream supplier or downstream buyer is in their respective markets, the more likely a lessening of competition will be as a result of a restrictive vertical agreement.⁹⁰

The Relevant Market and Market Structure - The U.S. Position

The position of the United States provides clarity on the matter and further vindicates the South African position regarding the manner in which to define the relevant market and the structure thereof, should the position be unclear in any given set of circumstances. In *E.I. du Pont* Justice Reed lays out the test to determine the relevant product market in a given inquiry by stating that whether a product forms part of a given market is dependant upon the availability of alternative commodities for buyers; that is, whether there is a cross elasticity of demand between the products in question.⁹¹ Reed continues to declare that to determine whether products are interchangeable, various aspects from the perspective of the consumer⁹² must be considered, such as the purchase of competing products for similar

⁸⁷ Neuhoff *et al* op cit (n69) 98.

⁸⁸ This is an abridged definition of market power which was declared by Lewis TC in *Natal Wholesale Chemists (Pty) Ltd v Astra Pharmaceutical Distributors (Pty) Ltd* [2001 – 2002] CPLR 363 (CT).

⁸⁹ *United States v. E.I. du Pont de Nemours & Co.* (1956) 351 U.S. 377 (*E.I. du Pont*) at 391. *E.I. du Pont* is the U.S. authority for the definition of monopoly power which is ‘the power to control prices or exclude competition’. This definition can be equated with South Africa’s definition of ‘market power’ which means the power of a firm to control prices, or to exclude competition, or to behave to an appreciable extent independently of its competitors, customers, or suppliers.

⁹⁰ Neuhoff *et al* op cit (n69) 98.

⁹¹ *E.I. du Pont* op cit (n89) at 400.

⁹² Defining the relevant market from the perspective of the consumer is also emphasized in the widely cited case of *United States v. Philadelphia National Bank* 374 U.S. 321 (1963) at 360-361.

uses considering the price, characteristics and adaptability of the competing products.⁹³ In other words, the functional substitutability of the products must be looked at, as well as the responsiveness of the sales of a product to a price change – whether a consumer will turn to another product in the face of that price change. In *E.I. du Pont*, Chief Justice Warren for the dissent noted that when du Pont raised its price of cellophane, its earnings went up; thus resolving that consumers did not turn to other flexible packaging materials as a substitute for cellophane, meaning that other flexible packaging materials did not form part of the relevant product market.⁹⁴ Therefore, one way of determining the relevant product market is to hypothesize a price increase and pose the question of – given this increase, what will the consumer do?

A similar stance is taken with respect to the determination of the relevant geographic market, which seeks to determine what the geographic area is in which the firms compete and thus determines which are the players in the market the firm, that is the focus of the inquiry, is actually up against. *United States v Grinnell Corp.*⁹⁵ confirms this consumer-oriented parallelism with the relevant product market determination by stating that the relevant geographic market is again defined from the perspective of the consumer, where it is hypothesized where the consumer will turn to – that is, which geographic area the consumer will go to - in the event of a price increase.⁹⁶ The geographic market can also be gleaned literally by merely looking to the area in which the specific firm conducts its operations.⁹⁷

⁹³ *E.I. du Pont* op cit (n89) at 380.

⁹⁴ *E.I. du Pont* op cit (n89) 422.

⁹⁵ 384 U.S. 563 (1996) (*Grinnell*).

⁹⁶ *Grinnell* supra (n95) at 588.

⁹⁷ *Grinnell* op cit (n95) at 575.

The Relevant Market in Exclusivity Clauses in Shopping Centre Leases

The Product Market

“In case of a product it may be of such a character that substitute products must also be considered, as customers may turn to them if there is a slight increase in the price of the main product. [...] [C]ommodities reasonably interchangeable make up that ‘part’ of trade or commerce which § 2 protects against monopoly power.”⁹⁸

Based on the above considerations, it can be deduced that the relevant market requiring analysis in the context of a supermarket tenant and a shopping centre landlord, where an exclusive lease agreement is in place and a section 5(1) analysis is relevant, can be said to be that of the downstream market consisting of retailers; specifically those comprising of supermarkets or other stores that have as their common aim the sale of similar, fungible everyday products and brands for consumption or utilisation by the ultimate consumer. The specific product market relevant to the inquiry is thus the selection of goods that are typically stocked by supermarkets. For example, supermarkets, by definition of the Oxford English Dictionary, generally sell foods and household goods, the former of which may be perishable or non-perishable. Therefore, included in this market are not only other supermarkets, but also smaller, independent speciality businesses that sell one or more products that are fungible with those sold by the wider-range-holding supermarkets or stores, such as bakeries, butcheries, greengrocers or convenience stores. From the consumer’s perspective it can credibly be hypothesized that in the event of a price increase of the products of one supermarket or store, a consumer would wish to substitute that supermarket or store’s goods with one who has homogenous goods that are cheaper.

The Geographic Market

In *Grinnell* the court found the relevant geographic market to be a national one, despite the activities of Grinnell’s subsidiaries being conducted on a local scale.⁹⁹ Brooks notes that the failure to take adequate cognisance of consumer interests and their possible responses in making a finding on the parameters of a geographic market, is a serious error.¹⁰⁰ Brooks

⁹⁸ *Grinnell* op cit (n95) at 571.

⁹⁹ *Grinnell* op cit (n95) at 575.

¹⁰⁰ Brooks op cit (n77) 279.

further notes Gellhorn and Kovacic's criticism of this decision on the basis that the geographic market for the services should be defined by the location of the subsidiary that conducts its operations, since that is where the effective area of competition occurs, in other words, that is where the consumer can turn to buy the service in the event of a price increase.¹⁰¹ The geographic area applicable to the enquiry into the relevant market can thus be distinguished from *Grinnell*, and is contended to comprise of that locale that exists within the boundaries of the shopping centre.¹⁰² The convenience of shopping centres, (as discussed above) which motivates many consumers to frequent them, supports the contention that a consumer will likely be unwilling to venture outside of the centre for his/her shopping needs. It is, however, plausible to hypothesize that in the event of a price increase of the products of the exclusive store in the shopping centre, the consumer would be motivated to venture somewhere not too far outside of the centre to a shop with cheaper goods. The plausibility of this contention is, however, disaffirmed, by a reasonable conceptualisation of reality that a consumer would likely factor in the extra travel costs that would be incurred due to having to substitute the store within the centre with another store outside of the centre. This reasonable conceptualisation of reality is confirmed in the findings of various academic writers who have conducted research in the marketing arena. Breuckner, Duvenhage, Yale & Ventakesh have noted that Shopping centres enable consumers to satisfy their shopping goals at one time, with their attraction towards this specific retail format arising from the perceived time economisation that can occur in contrast to having to visit numerous locations as is the case with stand-alone stores.¹⁰³ In addition, they note that centres facilitate proximity in location and time and thus provide convenience for the consumer in an efficiency sense. Consumers therefore prefer to shop at

¹⁰¹ Ibid.

¹⁰² As propounded above, in the section titled **Incentives for, and Repercussions of Exclusives in Shopping Centre Leases**, shopping centres have become a prominent, if not the most prominent means by which consumers fulfil their supermarket-type shopping needs due to the convenience that is provided by the situation of a multiplicity of stores in one confined area. Thus, the shopping centre will be the relevant geographic area to which the market enquiry relates, and to which there exists a potential to substantially prevent or lessen competition.

¹⁰³ Breuckner, J 'Inter store externalities and space allocation in shopping centres' *Journal Of Real Estate Research*, (1993) (7) 1 at 5-17; Duvenhage, A. 2014. The Impact of Size and Profitability on Retail Format Choice in South Africa. Masters Thesis, available at <https://ujdigispace.uj.ac.za/bitstream/handle/10210/12285/Duvenhage,%20A.,%20M.Com.%202014.pdf?sequence=1> accessed on 10 January 2015; Yale, L and Venkatesh, A, 'Toward the Construct of Convenience in Consumer Research' *Advances in Consumer Research* (1986) 13 at 403-408.

malls in an endeavour to reduce search costs. Further research has found that numerous stimuli have been exposed as motivations that elucidate why consumers prefer patronising malls over stand-alone stores: consumers stated that shopping at a mall satisfied their need for entertainment, and notwithstanding the functional and economisation benefits derived from shopping in one centralised location, consumers also view shopping at the mall as being recreational and allowing them to socialise with friends.¹⁰⁴ Survey research has also revealed that patrons have felt that shopping at malls provides them with feelings of comfort that were closely aligned to aspects of the centre that included: mall security, parking space and likelihood to satisfy the entire family's needs.¹⁰⁵

It can thus confidently be asserted that the relevant geographic area can be said to be that within the boundaries of the shopping centre, and not a local one too comprising of other supermarkets or specialty shops within the consumer's suburban jurisdiction.

How to Determine if a Firm has Market Power Via an Analysis of the Relevant Market

A specific consideration of existing firms and potential competitors provides an answer as to what the relevant market is or comprises. This information is a necessary precursor to determine whether market power (i.e. whether a party has the ability to raise prices above the competitive level in a market) is present. Pitofsky *et al* claim that there are three considerations of primary importance in distinguishing the relevant firms, that is, those that have sufficient influence over a firm's power to raise price, from the irrelevant.

The nature of the product and the ability or willingness of users to substitute other products for it

As alternative products become less substitutable, their influence on the defendant's price diminishes.¹⁰⁶ This can be clarified if one imagines a situation where there are a number of

¹⁰⁴ Nicholls, J., Li, F., Mandokovic, T., Roslow, S. and Kranendonk, C 'US-Chilean Mirrors: Shoppers in Two Countries' (2000) *Journal of Consumer Marketing* (2) 17 at 106-119; Terblanche, N. 'The Perceived Benefits Derived From Visits to a Super Regional Shopping Centre: and Exploratory Study' (1999) *South Africa Journal of Business Management* (4) 30 at 141-146.

¹⁰⁵ El-Adly, M 'Shopping Malls Attractiveness: A Segmentation Approach' *International Journal of Retail & Distribution Management* (2007) (11) 35 at 936-950.

¹⁰⁶ Pitofsky op cit (n7) 112.

sellers who sell a product that is completely fungible with the product sold by the other sellers. In such circumstances, if one seller charges even a slightly higher price than the going market price for that product, that seller will find that the sales of his product will decrease.¹⁰⁷ This can be contrasted with a product that is more highly regarded and preferred in a given market and thus not fungible – such as a drug that is more effective than any other in treating a disease –; in such a case the seller of that product can curtail the production thereof and raise price considerably in the expectation that consumers will prefer its product over the existing substitutes.¹⁰⁸

Application and Analysis to Exclusives in Shopping Centre Leases

Based on the consideration of the nature of the product and the ability or willingness of users to substitute other products for it, it can confidently be stated that, allowing exclusives in a shopping centre with the resultant scenario of there being present only one existent seller of specific types of goods in the centre, has the potential to allow that seller to raise the prices of the goods above the competitive level. An exclusive in a shopping centre lease typically prohibits the existence of stores in the centre that sell products that are fungible with those sold by the store imposing the exclusivity clause. The stores that remain in the centre will thus be those that do not have products that can be substitutable with those sold by the exclusivity-imposing store; depriving a consumer of the ability to substitute the goods of the exclusive seller with the goods of another seller of fungible goods, produces the result of the former seller being given the uninhibited opportunity to raise the prices of its products. In this sense, the exclusive seller in the centre will be said to possess market power, that is, the unequivocal ability to raise price and behave independently of its competitors - given that none exist within the vicinity to discipline the seller's pricing practices.

¹⁰⁷ Pitofsky op cit (n7) 113.

¹⁰⁸ Ibid.

Spatial or Geographic Considerations

One factor that impacts the substitutability of alternatives is their location.¹⁰⁹ A firm that owns every outlet of a particular type of product in one geographic area will still be limited by the presence of other independent firms who sell the same product in other geographic areas.¹¹⁰ However, based on the assumption that consumers would not be willing to travel the extra distance to save a small amount on a substitutable product, the firm who owns every outlet in one geographic area may be able to raise his prices above the going rate.¹¹¹ Such action would primarily be thought to occur in retail outlets rather than wholesale outlets, since in the latter case, even a small difference in price would cause buyers to resort to other outlets as such a contrast becomes significant when buying in bulk.¹¹²

Application and Analysis to Exclusives in Shopping Centre Leases

Regarding the spatial or geographic considerations, in a shopping centre which is anchored by one supermarket-type store, it has been shown to be highly dubitable that a consumer, who likely frequents the shopping centre due to the convenience it provides,¹¹³ will be willing to travel the extra distance to a different store with substitutable products. As stated above, such a consumer should be expected to take into account the extra travel costs required to visit the alternate store outside of the centre; this cost further giving substance to the improbability of the consumer's willingness to substitute a different store. This reality of the separate locality of another store, and the isolation that the store imposing the exclusive operates in, negates the possibility of its pricing practices being disciplined, amounting to the conclusion that such a store will possess a high market share within the relevant market and be able to raise its price without being kept in line by other stores, and act independently, thus confirming its market power.

¹⁰⁹ Pitofsky op cit (n7) 113.

¹¹⁰ Ibid.

¹¹¹ Ibid.

¹¹² Ibid.

¹¹³ Supra p 25.

The Prospect of New Competition

Another factor that may limit a firm in its power over price is the prospect of new entrants into the relevant market.¹¹⁴ An existing firm may be perturbed from raising its prices too high and reaching too high a profit margin if it remains conscious of the possibility that a new firm may want ‘a piece of the pie’ and set itself up as a competitor with the existing firm. The likelihood of a new firm entering the market depends on various factors such as the expense associated with obtaining space, the availability of raw materials and skilled personnel and the cost of obtaining a satisfactory share of the market (advertising etc.).¹¹⁵ In *United States v. Waste Management, Inc. and EMW*¹¹⁶ the court looks to whether there is ease of entry into the market in order to determine the market power of a firm, and takes into account the timeliness, the likelihood and the sufficiency of entry into the market in order to determine whether a firm’s actions will be disciplined. As these barriers to entry become more imposing, the likelihood of new competition declines and the influence of such a firm over the pricing policy of an existing firm diminishes.¹¹⁷

Application and Analysis to Exclusives in Shopping Centre Leases

Potentially the most decisive of considerations in support of the existence of market power of an exclusive-imposing supermarket in a shopping centre, is that of the prospect of new competition. Through an exclusive, a supermarket completely eliminates the prospect of new entrants into the shopping centre, thereby removing the discipline mechanisms (in the form of competitors) in the relevant market. A typical exclusive in the relevant context will be a long-term one, thereby decreasing the timeliness of entry into the market; due to this factor, too, the likelihood of entry into the market is nullified. The sufficiency enquiry from *Waste Management* relates to whether a potential entrant will have a sufficient impact on the relevant market to be considered a notable competitor to the firm with market power. In the current context, this enquiry is superfluous due to the fact that the exclusive

¹¹⁴ Pitofsky op cit (n7) 113.

¹¹⁵ Ibid.

¹¹⁶ 743 F.2d 976 (*Waste Management*) at 981.

¹¹⁷ Pitofsky op cit (n7) 114.

produces no occasion for entry into the market. Faced with no competition, the exclusive-imposing supermarket will indubitably have market power; consequently have the ability to raise prices above the competitive level and act independently.

Identification of the Relevant Market through the Existence of Market Power: Lewis TC’s Approach in *Natal Wholesale Chemists* – A Critique: Placing the Cart Before the Horse

“[...] it would be pointless to consider an agreement, decision or practice by reason of its effect if those effects were to be taken distinct from the market in which they are seen to operate...”¹¹⁸

In *Natal Wholesale Chemists (Pty) Ltd v Astra Pharmaceutical Distributors (Pty) Ltd*¹¹⁹ it was stated by the Competition Tribunal, in the context of an exclusive distribution agreement, that it is not a necessary precursor to an enquiry into an alleged restrictive practice to obtain a formal market definition.¹²⁰ This justification owing to the fact that the purpose of defining a relevant market is to identify the exercise of market power, market power being defined in s 1 (xiv) of the Act as “the power of a firm to control prices, or to exclude competition or to behave to an appreciable extent independently of its competitors, customers or suppliers.”¹²¹

Lewis TC enunciates in *Natal Wholesale Chemists* that:

“When examining the exclusive vertical agreements, rather than attempting to define the relevant market in the abstract, we will ask ourselves whether the exclusionary right will give one or both parties to the arrangement the power to raise prices in the market. Competition will be harmed only if, as a result, prices can be raised above the competitive level.”¹²²

¹¹⁸ *Brasserie de Haecht v Wilkin* Case 23/67 [1967] ECR 407 at 415.

¹¹⁹ [2001-2002] CPLR 363 (CT) (*Natal Wholesale Chemists*).

¹²⁰ *Natal Wholesale Chemists* supra (n116) at 376.

¹²¹ *Ibid.*

¹²² *Natal Wholesale Chemists* op cit (n116) at 377.

According to Lewis TC, then, if the exercise of market power, as defined, is identified, then a market relevant for the purposes of the enquiry will have been identified.¹²³ For example, if the firm in question is able to raise appreciably the price of its product without occasioning a significant reduction in demand - then a market relevant for the purposes of the enquiry will have been identified.¹²⁴ Therefore, it is the determination of whether a firm possesses market power that needs to be deciphered in order to ascertain whether there is a relevant market;¹²⁵ in short, stating that the act of establishing an exercise of market power is equivalent to the identification of the relevant market.¹²⁶

This position appears to be contrary to both the U.S. method as well as the aforementioned South African cases.¹²⁷ The former unequivocally states that “...without a definition of [the] market there is no way to measure [the defendant’s] ability to lessen or destroy competition.”¹²⁸ In other words, the relevant market must first be defined in order to see whether a firm within such a market has market power. In Lewis TC’s abridgement of the Act’s definition of market power, he states that a firm will have market power if it is able to raise prices above the competitive level in the market. Knowing, however, what the market relates to and the main and relevant participants or competitors therein, in order to make this determination, seems a necessary precursor to this enquiry. Further, an enquiry into the ability of the firm to raise prices above the competitive level in the market requires knowledge of what the competitive price level in the market is, and this requires an inquiry into who determines or has an influence on the competitive level in the market. A firm’s power to raise prices is limited mainly by the existence of other producers who, by failing to raise their prices, would take over enough of the firm’s business such that the price rise would be unprofitable for the firm.¹²⁹ The primary obstacle that arises is determining

¹²³ “A restrictive practices investigation [...] is concerned with [...] identifying an exercise of market power – in this type of analysis the act of establishing an exercise of market power is equivalent to the identification of the relevant market” (*Natal Wholesale Chemists* op cit (n116) at 377, footnote 20).

¹²⁴ *Natal Wholesale Chemists* op cit (n116) at 377.

¹²⁵ *Neuhoff et al* op cit (n69) 27. The definition of market power will be further expounded on in the upcoming sections, it is included in this section due to its inextricable link to an enquiry into the relevant market.

¹²⁶ *Natal Wholesale Chemists* op cit (n116) at 377 (footnote 20).

¹²⁷ *South African Airways* op cit (n81); *Mandla-Matla* op cit (n83); *Uniplate* op cit (n84)

¹²⁸ *Walker Process Equipment, Inc v Food Machinery & Chemical Corporation* 382 U.S. 172 (1965) at 177.

¹²⁹ *Pitofsky* op cit (n7) 112.

“which existing firms and potential competitors have sufficient restraining influence on the defendant’s power over price to warrant their inclusion in the ‘relevant market’”.¹³⁰ If a market definition or delineation is left out, as Lewis TC would have the one do, it may result in irrelevant upstream or downstream parties, or geographic areas being taken into consideration which, in turn, could affect the market power enquiry; or it could result in an oversight/ leaving out of important products or geographic areas which are relevant to the market and this could also affect the market power enquiry. It seems vital to include this in the inquiry if one wishes to receive an accurate determination of whether a firm is able to raise its prices above the competitive level.

It is thus concluded that the Competition Commission, when adequately performing a s 5(1) analysis, would have to have made a determination of the relevant market in order to decipher whether the firms in question had market power.¹³¹

Application to Exclusives in Shopping Centre Leases – An Inevitable Conclusion

Despite the potential confusion that arises from Lewis TC’s approach, the same, inevitable conclusion can be drawn with respect to the question as to whether an exclusive-imposing supermarket has market power: it can rationally be stated that the agreement between the supermarket and the shopping centre landlord will provide the former with the ability to raise appreciably the price of its product without occasioning a significant reduction in demand,¹³² thereby proving market power according to Lewis TC’s approach. It can similarly be rationally stated that, based on above analysis of the relevant market, an exclusive-imposing supermarket within a shopping centre will indeed possess market power.

¹³⁰ Ibid.

¹³¹ In addition and although not expanded on to a thorough extent in this paper, this position holds too in the EU jurisdiction where The Court of Justice has stressed that a vertical agreement has to be considered in the context in which it occurs, and a definition of the relevant product and geographic markets is first necessary. (Richard Whish and David Bailey *Competition Law* 7 ed (2012) 125-127).

¹³² *Natal Wholesale Chemists* at 377.

‘...the effect of substantially preventing or lessening competition...’

“Whether there has in some respect been a substantial prevention or lessening of competition in [a] market is a factual enquiry. Unless that enquiry generates an affirmative answer the existence of an agreement [...] is irrelevant...”¹³³

The above statement by Wallis AJA in *Netstar* justifies the motives of this paper’s structure with its initial determination of whether there has been a substantial prevention or lessening of competition, before its turn to whether an agreement between the parties in a vertical relationship exists, which will appear in the final paragraphs. As the argument will unequivocally produce an affirmative determination of a substantial prevention or lessening of competition, the latter component of section 5(1) of whether an agreement between the parties in a vertical relationship exists, will be considered thereafter.

Some agreements have as their very object the restriction or prevention of competition, such as the practice of minimum resale price maintenance,¹³⁴ which is irrebuttably presumed to be anticompetitive and harmful to consumers by its very nature; such agreements would be subject to the per se rule, meaning that the defendant may not bring forth any evidence to show the reasonableness of the restraint, its mere occurrence will result in liability.¹³⁵ Where it is not possible to say that the object of an agreement is to restrict competition, however, it is necessary to conduct an extensive analysis of its *effect on the market* before it can be said to violate section 5(1) and be found to substantially lessen or prevent competition.¹³⁶ U.S. jurisprudence supports this notion in *Indiana Federation of Dentists* where it was stated by Justice White for the Supreme Court that in some cases it may be impossible to prove direct anticompetitive effects, and in such cases it is sufficient to prove that the parties to the agreement are able to exercise market power through the exclusive arrangement, as a ‘surrogate for the proof of actual detrimental effects.’¹³⁷ The above discussion of exclusive leases’ effect on the market as well as the

¹³³ *Netstar (Pty) Ltd and others v Competition Commission and Another* [2011] 1 CPLR 45 (CAC) (*Netstar*) at para 29.

¹³⁴ Section 5(2) of the Act

¹³⁵ Neuhoff *et al* op cit (n69) 88.

¹³⁶ Richard Whish and David Bailey *Competition Law* 7 ed (2012) 125.

¹³⁷ *Indiana Federation of Dentists* op cit (n12) at 461.

demonstration and confirmation of market power that an exclusive-imposing supermarket inevitably possesses,¹³⁸ thus has an acute bearing on the anticompetitive effects that are likely to result from such a lease. The showing of market power above involved a showing of a supermarket's ability to control prices, exclude competition or behave independently of its competitors; it is contended that this fact embodies extremely persuasive evidence of an effect of substantially lessening or preventing competition, as it has been interpreted by academic writers and Competition law enforcement agencies alike.

In order to demonstrate that an exclusive lease agreement in the shopping centre context is proscribed by the Act, it must be shown that the exclusive agreement produces anticompetitive effects, which may take various forms. Since the per se rule is inapplicable in a section 5(1) context, a rule of reason analysis must be conducted to determine whether the agreement substantially prevents or lessens competition. The Competition Tribunal has stated that the impact on competition of any form of exclusive arrangement must be measured by the extent of foreclosure that results from the agreement, as well as the possible detriment that comes to consumer welfare.¹³⁹ Neuhoff *et al* explain and expand upon this further by stating that evidence of an anticompetitive effect can involve a showing of evidence that competitors or customers are foreclosed from entering or expanding in a market, and that consumers are being exploited, that is, the agreement results in higher prices or restricted choice.¹⁴⁰

¹³⁸ Supra 'The Relevant Market in Exclusivity Clauses in Shopping Centre Leases'.

¹³⁹ *The Competition Commission and JT International South Africa (Pty) Ltd v British American Tobacco South Africa (Pty) Ltd* (05/CR/Feb05) [2009] ZACT 46 (BATSAs) at para 298.

¹⁴⁰ Neuhoff *et al* op cit (n69) 98.

Exclusive Lease Agreements Between a Supermarket Tenant and Shopping Centre Landlord: the Anticompetitive Effects of Market Foreclosure and Consumer Exploitation

‘Many people believe that possession of unchallenged economic power deadens initiative, discourages thrift and depresses energy; that immunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress; that the spur of constant stress is necessary to counteract an inevitable disposition to let well enough alone.’¹⁴¹

In order to illustrate the anticompetitive effect of exclusive lease agreements in the shopping centre context, an invaluable reference, in support of the contentions that will be made with respect to market foreclosure and consumer exploitation, is a typical exclusivity clause taken from the lease agreement between Pick n Pay and Hyprop Investments in the case of *Pick n Pay Retailers (Pty) Ltd v Masstores (Pty) Ltd and Hyprop Investments Ltd*,¹⁴² which provided for the following:

“EXCLUSIVITIES AND LETTING RESTRICTIONS

10.1 Save for the Supermarket [Pick n Pay] and Checkers, the lessor shall not permit the following businesses to be conducted in the shopping centre on the property:

10.1.1 a hypermarket or supermarket; or

10.1.2 a store with either a single or several food departments, the aggregate square meterage of which exceeds 100 (one hundred) meters; or

10.1.3 a café or delicatessen which sells fresh fish or meat; or

10.1.4 a grocery, fresh fish shop, butchery, bakery or fruit and vegetable shop.”

¹⁴¹ *United States v. Aluminium Co. of America* 148 F.2d 416 (ALCOA) at 427.

¹⁴² (46501/2014) [2014] ZAGPPHC 769 at para 2.

Substantial Prevention or Lessening of Competition via Market Foreclosure

In light of the above exclusivity clause, which is a typical construction thereof, it can confidently be asserted that an exclusive lease agreement between a shopping centre and a supermarket indeed has the effect of foreclosing the market to customers and competitors alike. The effect of the agreement is the simple, undisguised exclusion of potential competitors (in the form of customers of the landlord, i.e. other supermarkets or specialty stores) of the landlord from tenancy in the shopping centre. The product market comprising of everyday fungible goods, as well as the geographic market comprising of the confined, yet concentrated, locale of the shopping centre is thus reserved primarily for the exclusive-imposing supermarket, and the result is that potential customers of the landlord, and competitors of the supermarket – who are one and the same – are foreclosed from entering or expanding in that market; leaving the former with a monopoly within that market.

In *Netstar* the Competition Appeal Court stated that there may be some overlap between a prevention and lessening of competition such that an agreement may both lessen the existing level of competition and prevent competition in the future.¹⁴³ Wallis AJA further clarifies the requirement of prevention and lessening of competition by highlighting that the words are qualified by the adverb “substantially”, and explains that any particular prevention or lessening of competition will be a question of fact in each case, but that the very existence of this qualification “demonstrates that what is required is something that is neither trivial or speculative.”¹⁴⁴ He goes on to say, nonetheless, that if there is strong enough evidence to show that, but for the agreement, other persons would probably have entered the market and engaged in competition, then the requirement of a substantial prevention or lessening of competition will almost certainly be satisfied.¹⁴⁵ Applying this logic to the context at hand, it is contended that, but for the agreement, other supermarkets and/or small specialty stores would probably have entered the market and engaged in competition. The justification for this exists in the already- elucidated submission that a

¹⁴³ *Netstar* op cit (n133) at para 29.

¹⁴⁴ *Netstar* op cit (n133) at para 30.

¹⁴⁵ *Ibid.*

shopping centre is, in today's culture, a highly frequented and extremely popular hub of practicality and accessibility for end-consumers; this fact alone undoubtedly creates a desire for competitors to attempt to engage in competition therein. The extent of foreclosure that exclusive agreements produce in the form of the prohibition and consequent complete inability of customers (of the landlord) and competitors to enter or expand in the market – can be considered as compelling evidence of a substantial prevention or lessening of competition.

The Exclusion of Small and Medium-Sized Enterprises

In the above section regarding the nature of South African competition law and the harms that it aims to protect against,¹⁴⁶ it was explained that the Act embodies a plurality of goals, namely those that seek to realise both efficiency and socio-economic or public interest objectives. The latter are encapsulated in section 2(c) onwards (although only section 2(e) will be dealt with due to its pertinence to the relevant context) and seek to accomplish socio-economic objectives through the policy of fairness which includes a protection *from* competition. The purpose and significance of the latter objectives are made comprehensible when considered in South Africa's historical context where the ownership structure of the economy was in direct correlation with the state's discriminatory policies and the state-sponsored monopoly under the Apartheid regime.¹⁴⁷

Section 2(e) of South Africa's Act encapsulates one of its explicit purposes which is to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the economy, meaning that the Act proclaims to protect the interests of small and medium-sized enterprises by promoting their access to markets as well as acknowledging their rights to participate in the economy.¹⁴⁸ An exclusive lease agreement between a supermarket and a shopping centre runs in direct contrast to this plain objective of the Act. The effect of the exclusive, as outlined above, is to exclude potential competitors of the supermarket from entering the market of food and household goods in a

¹⁴⁶ Supra *South African Competition Law – An Amalgamation of Efficiency and Social Objectives*

¹⁴⁷ Supra *South African Competition Law – An Amalgamation of Efficiency and Social Objectives*

¹⁴⁸ Kampel op cit (n51) 1.

shopping centre. The small and medium-sized enterprises that comprise of such competitors and who will be excluded from the market as a result of the exclusives, are those that specialise in the sale of certain goods that the supermarket also sells, such as bakeries, butcheries, greengrocers etc. Kampel rightfully notes that in any defined market, a small or medium-sized enterprise will typically hold a market share of 10% or less, and there is therefore unlikely to be a *substantial* prevention or lessening of competition if the small or medium-sized enterprise exits the market, or is unable to enter or expand in the market.¹⁴⁹ However, in the unique market comprising only of the boundaries of the shopping centre, the market share of the small or medium-sized enterprise will dramatically increase, making its inability to compete in the market, through the foreclosure as a result of the exclusive, indeed a substantial lessening or prevention of competition. The market share that these specialty small or medium-sized enterprises enjoy is further increased if one considers and remains cognisant of the specific culture that dominates the consumer preferences of today, especially with regard to perishable foods. Genova has noted that younger consumers prefer shopping in specialty stores for products such as meats, baked items, cheeses and other deli-type foods.¹⁵⁰ In addition, consumers have become more conscious of the source of their foods, especially meat, where defining characteristics such as ‘free-range’ or ‘grain-fed’ play an important part in their decision as to which product to purchase. Genova confirms this by noting that consumers have expressed a strong desire to understand more about a store, particularly where it sources its foods and who is involved in the various processes.¹⁵¹ Similarly, Solomon observes that there has been a noteworthy consumer shift towards products that are natural or organic and provided by enterprises that possess core values that are aligned with their own.¹⁵² In light of this intelligence regarding current consumer trends, it is contended that a small specialty store with tenancy in a shopping centre will possess a significant market share in the market of perishable foods in a shopping centre, thereby deducing that a substantial

¹⁴⁹ Kampel op cit (n51) 5.

¹⁵⁰ Windsor Genova ‘Younger Shoppers Shifting from Supermarkets to Specialty Food Stores’, 9 June 2014, available at <http://www.wall-street.com/2014/06/09/younger-shoppers-shifting-supermarkets-specialty-food-stores/>, accessed on 5 January 2015.

¹⁵¹ Ibid.

¹⁵² Brian Solomon ‘Buying Organic: General Mills Swallows Annie’s for \$820 Million’, available at <http://www.forbes.com/sites/briansolomon/2014/09/08/buying-organic-general-mills-swallows-annies-for-820-million/>, accessed on 5 January 2015.

prevention or lessening of competition will ensue should such enterprises be excluded from the market.

Diminution of Intra-brand Competition

The above-shown consequence of market foreclosure produces the spin-off effect and creation of another, separate form of suppression of competition: The diminution of *intra-brand* competition, i.e., the competition between the distributors (wholesalers or retailers) of the same products or brands.¹⁵³ The environment in which an exclusive lease agreement subsists, is one in which there is a singular retailer of products; albeit in some instances many different brands of the same products. There is thus no other retailer in the competitive vicinity against which the singular retailer may competitively price its products, resulting in the singular retailer being given *carte blanche* to price at whatever rate it desires.

In *Natal Wholesale Chemists* The Competition Tribunal stated that it is widely recognised that the diminution of intra-brand competition consequent upon exclusive distribution agreements is often compensated for by the pro-competitive benefits that enhance the ability of the producer to compete against its competitors, that is, by strengthening inter-brand competition.¹⁵⁴ This statement by Lewis TC, reinforced by anti-trust scholarship and jurisprudence, can be explained through the following line of reasoning:

Interbrand competition is the competition among the manufacturers who produce the same generic product, albeit different brands.¹⁵⁵ An extreme example of a deficiency in interbrand competition would be a monopoly, where there is only one manufacturer of a specific type of product.¹⁵⁶ Intra-brand competition, on the other hand, is the competition between the distributors (wholesalers or retailers) of the same brand of products.¹⁵⁷ The

¹⁵³ Phillip Areeda, Louis Kaplow & Aaron Edlin *Antitrust Analysis: Problems, Text, and Cases* 6 ed (2004) 561.

¹⁵⁴ *Natal Wholesale Chemists* op cit (n116) at 372.

¹⁵⁵ Areeda, Kaplow & Edlin op cit (n153) 561.

¹⁵⁶ *Ibid.*

¹⁵⁷ *Ibid.*

argument that a diminution of intrabrand competition occurs as a result of vertical agreements (such as exclusive distribution agreements), but that this diminution is likely compensated for by more intensive interbrand competition, is, in essence, due to the distributor's focus on obtaining competitive advantage for its clients' (manufacturer's) brands which will intensify competition with manufacturers of other brands that do not enjoy the services of the distribution agent.¹⁵⁸ Further, when interbrand competition exists, that is, where there are many different brands of fungible products, it provides a significant check on the exploitation of intrabrand market power because of the ability of consumers to substitute a different brand of the same product.¹⁵⁹

The above illustration, however, should be regarded as being exclusively applicable to the reaching of a conclusion of anticompetitiveness in the exclusive distribution agreement context, and not in the shopping centre lease context. As explained below,¹⁶⁰ the shopping centre landlord and supermarket tenant are not in a typical manufacturer-distributor relationship, but rather a service-supplier and customer relationship, and thus the offsetting of the diminution of intrabrand competition that results through the enhanced interbrand competition in exclusive distribution agreements is not herein applicable. In the current context there is a severe diminution of intrabrand competition: a single firm possessing a monopolistic position in a market - that is, a single available source for the purchase of food and household goods - who wilfully acquired and maintained that position via contractual means. Therefore, in an environment where there is a single source available for the purchase of fungible goods and brands required for everyday use, the result is a complete diminution of intrabrand competition, which, if given the opportunity, the Tribunal would likely, deem substantial.

¹⁵⁸ Neuhoff *et al* op cit (n69) 100. Exclusive distribution is typically an arrangement stating that only one distributor is allowed to sell the manufacturer's product. The distributor stocks and promotes only that manufacturer's brand of a specific product. Other manufacturers do not get to use the distribution services of that distributor. This incentivises other manufacturers to better their product in order to utilise the distribution services of the exclusive distributor.

¹⁵⁹ Areeda, Kaplow & Edlin op cit (n153) 561.

¹⁶⁰ *Infra* '**...in a vertical relationship**' where it is explained that a shopping centre lessor cannot be considered a manufacturer of services or products that the tenant distributes.

Substantial Prevention or Lessening of Competition via Consumer Exploitation

“The ultimate goal of any competition policy is to enhance consumer welfare. The premise is that markets are not competitive where it can be shown that prices increase or the choice of product or service available to the consumer is limited as a result of monopolistic conduct.”¹⁶¹

Based on the above commentary, as well as the aforementioned jurisprudence of the Competition Tribunal (namely that the impact on competition on any form of exclusive arrangement must be measured by the possible detriment that comes to consumer welfare) the following paragraphs will present evidence of the detrimental effects of exclusive leases in shopping centre contexts in order to illustrate a substantial prevention or lessening of competition.

Above-Competitive-Level Pricing

Kampel’s above declaration reiterates the viewpoint of the Tribunal, the Appeal Court and Neuhoff *et al* above with respect to the impact on competition of exclusive arrangements being measured by detriment to consumer welfare in the form of exploitation; exploitation meaning higher prices or restricted choice for the consumer. Being beyond the scope of this paper, concrete evidence amounting to actual price increases by an exclusive-imposing supermarket will not be revealed or considered.¹⁶² However, the mere contemplation of the (anti) competitive environment that is created by the arrangement deems such evidence redundant, as it is plain to foresee the boundless opportunity, provided by the exclusive lease, that the supermarket has to increase prices. This contemplation is supported by the following re-statement by Judge Learned Hand in *ALCOA*:¹⁶³ ‘Mere size is not an offense against the Sherman Act unless magnified to the point at which it amounts to a monopoly... but size carries with it an opportunity for abuse that is not to be ignored...’ Unencumbered by the presence of any competition in the vicinity of the market (both geographic and product) to discipline its pricing practices, an exclusive-imposing supermarket is left with free reign to charge higher prices to consumers without

¹⁶¹ Kampel op cit (n51) 1.

¹⁶² In addition, this information was claimed to be confidential and was withheld by the Competition Commission when requested in furtherance of the development of this paper.

¹⁶³ *ALCOA* op cit (n141) at 430.

accountability. Accountability for the supermarket who would inevitably charge higher prices, in a free market, would take place via the pricing practices of the competitors, who would price at a lower rate than the supermarket, who would in turn be forced to either lower its prices or exit the market due to lack of clientele. It is thus asserted, with conviction, that an exclusive lease between a shopping centre and a supermarket indubitably has a detrimental effect on consumer welfare, by way of exploitation through the higher prices that will inevitably be charged.

As outlined above, an exclusive lease agreement produces the effect of foreclosing potential competitors from entering or expanding in the market of food and household goods in a shopping centre, leaving the exclusive-imposing supermarket with a monopolistic position within the relevant market.¹⁶⁴ This creation of monopoly that the exclusive lease allows for and produces requires mention for the purposes of revealing its consumer-detrimental outcome. These dangers of monopoly take the form of injury to the consumer from both a monetary and non-monetary perspective, and will be explained via the following informal and rudimentary economic analysis:¹⁶⁵ A firm with monopoly power will be assumed to possess the desire to dictate and raise price, and will seek to do so, since it possesses substantial market power. Given the supermarket's substantial market share, consumers are often incapable of acquiring the desired products from another supermarket or store, as the exclusive-imposing supermarket is the sole provider thereof. Thus, where no substitute offerings are present, the consumer must either incur this new higher price, or forgo the offering. If the consumer chooses the latter, as they are unable to afford the higher price, the consumer suffers from deprivation of that product, such deprivation which can be deemed detrimental to the objective of consumer welfare that is

¹⁶⁴ The definition of monopoly power from *E.I. du Pont* op cit (n89), is 'the power to control prices or exclude competition'. This definition can be equated with South Africa's definition of 'market power' which means the power of a firm to control prices, or to exclude competition, or to behave to an appreciable extent independently of its competitors, customers, or suppliers. It has already been shown in the preceding sections that an exclusive-imposing supermarket will possess market power.

¹⁶⁵ This information regarding the effect of a monopoly on consumers was obtained via the means of an informal interview, conducted on 20 October 2013, with an Antitrust Law professor from the University of Maryland Francis King Carey School of Law. The principles expressed therein comprise predominantly of *obiter dicta* from *ALCOA; Aspen Skiing Co. v. Aspen Highlands Skiing Corp.* 472 U.S. 585 (1985); *Paddock Publications v. Chicago Tribune* 103 F.3d 42 (1997); *United States v. Dentsply International, Inc.* 399 F.3d 181 (2005)

envisaged by the Act.¹⁶⁶ In addition, when demand for the product decreases, the manufacturer of the product does not realise economies of scale (where increased production results in efficacy that allows for a decrease in cost per unit – this decrease in costs translating into a lower price for consumers), and this translates into a higher price of the product. Consumers that are unable or unwilling to forego the product are forced to pay the higher price, and this results in a wealth transfer from the consumer to the monopolist, again breaching the objective of consumer welfare prescribed by the Act.

Poor Service Delivery

‘[A substantial lessening of competition arises] when it has a significant effect on rivalry over time, thereby reducing the competitive pressure on firms to improve their offer to customers or become more efficient or innovative.’¹⁶⁷

One of the clear purposes of the Act is to promote and maintain competition in order to provide customers with competitive prices and product choices.¹⁶⁸ The significance of this purpose was reiterated in *Msomi t/a Minnie Cigarette Wholesalers & others v British American Tobacco South Africa (Pty) Ltd*,¹⁶⁹ where the applicants claimed that a vertical restriction would eliminate price and service competition amongst distributors; the Tribunal upheld this as a valid claim that possessed the potential to substantially lessen competition.¹⁷⁰ This ‘price and service elimination’ type claim resonates deeply within exclusivity in the shopping centre context. The fact that a supermarket acting as the sole provider of fungible goods in a relevant market, possesses the extraordinary opportunity to raise its prices to an above-competitive level without being disciplined by any competition (thereby exploiting end consumers) has been confirmed above; it is the latter claim of service elimination, which presently requires justification in order to show an a substantial prevention or lessening of competition.

¹⁶⁶ *Inter alia*, the latter component of section 2(c) states that the purpose of the Act is to advance the social and economic welfare of South Africans.

¹⁶⁷ Whish & Bailey op cit (n136) 932.

¹⁶⁸ Section 2(b) of the Act.

¹⁶⁹ [2006] JOL 18326 (CT) (*Msomi*) at para 42.

¹⁷⁰ *Msomi* supra (n169) at para 49.

A supermarket that enjoys the comfortable position of exclusivity within a shopping centre is cognizant of its solitary position and function of the sole provider of certain goods within the relevant market. The anchor tenant supermarket will thus possess no incentive to improve upon its service delivery, since consumers who frequent that shopping centre within which the supermarket possesses tenancy, do not have the choice of boycotting the supermarket in the event of poor service delivery, and thus the latter has complete security in its customer base. The lack of choice that consumer's are faced with should not be interpreted as meaning that consumers are literally unable to shop at another supermarket. Consumers are, of course, able to shop for food and household goods elsewhere, outside of the centre, but, as was explained in the sections above, consumers are unlikely to be willing to incur the extra travel and time costs that such a venture entails. In addition consumers are unlikely to be willing to surrender the convenience that the nature of a shopping centre possesses, what with its inclusion of a wide variety of shops that satisfy many purchasing requirements at once. The incentive to qualitatively improve various elements of the supermarket, and to become more innovative and service-oriented, is, made existent by the presence of competition and competitive pressures. With no such competition to speak of, compliments of the exclusive lease, such incentives are eliminated which is likely to the detriment of the consumer. In the absence of competitive pressures to improve and innovate, consumers will likely be exposed to, *inter alia*, unhelpful and uninformed employees, products that may not be fresh or available, an absence of promotional benefits such as 'specials', and a general upkeep of the supermarket that is likely to pertain to the lowest acceptable standards. Such poor service delivery (that not unusually comes at a lower cost to the supermarket, and is thus a reasonable probability) can be deemed a form of customer exploitation in the context of supermarket exclusives that thus act as evidence of a substantial prevention or lessening of competition.

Restricted Choice

In addition to the inevitable consequences of over-pricing and poor service delivery by the supermarket, the consumer, indirectly coerced into settling for the range of products held by the exclusive-imposing supermarket (due to the abovementioned postulation that a consumer will settle for the supermarket within the shopping centre due to the all-

inclusive-type convenience encapsulated by the shopping centre as well as the incurrance of extra travel and time costs¹⁷¹), will be restricted in his/her choice of product. A consumer has the option to purchase those products stocked by the exclusive-imposing supermarket and no other. In other words, should the consumer be dissatisfied with, for example, the fresh produce or the brand of shampoo that is kept by the exclusive-imposing supermarket, the consumer will be unable to seek an alternative within the shopping centre, by virtue of the operation of the exclusive. This evidence of restricted choice can be deemed a form of consumer exploitation as contemplated by Neuhoff *et al*¹⁷² and thus serves as evidence of a substantial prevention or lessening of competition.

Market Foreclosure and Consumer Exploitation: A Breach of the Efficiency Objectives of the Act

The above-shown market foreclosure and consumer exploitation are in stark violation of the efficiency objectives enshrined in the Act, as expounded on above in the chapter headed: '*South African Competition Law – An Amalgamation of Efficiency and Social Objectives*'.¹⁷³ The exclusion of competitors from the relevant market, the extraordinary opportunity to charge higher prices, the restriction of choice and potential for poor service delivery are all effects of exclusive leases and all stand in violation of sections 2(a) and (b), which embody the efficiency goals of the Act. To reiterate, the efficiency motives of the Act aim to protect and promote the competitive process through the advancement of rivalry among market actors, to prohibit the interference with the natural flow of competition through exclusionary practices, to ensure that the market works freely, to the advantage of the entire citizenry, and that consumers have a wide range of choice of product at a competitive price.¹⁷⁴ Upon a reflection of the abovementioned contentions with respect to the effects of exclusive leases, it is asserted that each of the stated objectives of the Act stands in jeopardy with the operation of exclusive leases agreements in the shopping centre context.

¹⁷¹ Supra '**The Relevant Market in Exclusivity Clauses in Shopping Centre Leases**'.

¹⁷² Supra n137.

¹⁷³ Supra p 11

¹⁷⁴ Ibid.

‘...unless a party to the agreement can prove that any technological, efficiency or other pro-competitive, gain resulting from that agreement outweighs that effect.’

An agreement which has been shown to produce the effect of substantially preventing or lessening competition in a market (of which exclusives have indeed been shown to do in the preceding paragraphs) will have the opportunity for redemption if the respondent can show that there exists an efficiency, pro-competitive or technological gain resulting from the agreement that outweighs its anticompetitive consequences.¹⁷⁵ Shopping centre exclusives are thus capable of being justified on the ground that the losses caused by the prevention of competition would be offset by the pro-competitive gains of the agreement. Each of the elements of the defence will first be examined and applied to the pertinent context and then predictions about what defences exclusive-imposing supermarkets could potentially bring, as well as their likely success, will be outlined.

Economic Efficiency

Economic efficiency could be said to be realised in the following conditions: where allocative efficiency exists, that is, when productive resources are used in an optimal way such that all the demand on the market is satisfied.¹⁷⁶ As explained above, a firm who enjoys market power, such as an exclusive-imposing supermarket, will seek to raise prices, and this will decrease the demand for the more expensive product on the market, as some consumers will forgo the purchase. Allocative efficiency is thus not realised through the imposition of an exclusive lease agreements as the production capacity of manufacturers is not being realised to its full extent.

In some instances a firm’s enjoyment of high market power may be as a result of its superior efficiency. This point was highlighted by the Competition Tribunal in *Msomi* who confirmed that competition is typically premised on a plurality of competitors and that an efficient market often leads to the culling of inefficient competitors.¹⁷⁷ Whether an exclusive-imposing supermarket is the most efficient of firms in the market of foods and

¹⁷⁵ Neuhoff *et al* op cit (n69) 96 and 53 where it is stated that this balancing act is referred to as the ‘efficiency defence’; *Mandla-Matla* op cit (n83) at 517.

¹⁷⁶ *Supra* p 44.

¹⁷⁷ *Msomi* op cit (n169) at para 44.

household goods in a shopping centre is unknown due to the artificial obtainment of market that the exclusivity clause in the lease agreement achieves. An efficiency defence of this type, will thus likely be unacceptable.

Pro-Competitive Gain

A pro-competitive gain would be achieved when it can be shown that conduct or market structure leads to a lower price for consumers or assists in opening up markets to competition.¹⁷⁸ It has been extensively shown in the preceding sections that the conduct of and market structure created by an exclusive lease agreement has the inevitable effect of leading to higher prices for consumers and foreclosure of the market for potential competitors. This defence would thus too fail for an exclusive-imposing supermarket.

Technological Gain

Neuhoff *et al* define a technological gain via the means of an example in the field of intellectual property: 'Patent rights are often criticised for creating monopolies. However, it is generally accepted that the awarding of patents encourages innovation and technological progress'.¹⁷⁹ It is within this context that it could be postulated that an exclusive-imposing supermarket respondent would attempt to bring a justification. Justifications of an efficiency, pro-competitive or technological type are allowed on a case-by-case basis,¹⁸⁰ therefore, being deprived of the details of the specific justifications brought forward by the supermarkets, and since the topic of exclusivity in shopping centre lease agreements has not in the past been adjudicated by the Competition Tribunal, it is necessary to postulate the possible justifications and defences that may reasonably be brought forward by the respondent supermarkets.

A reasonably possible justification could be brought by the respondent which would highlight the fact that, in the event that more than one supermarket or store selling the same goods as that sold by the supermarket exists in the centre, it is likely that, due to homogenous goods stocked by each of the supermarkets or stores, one or both of the stores

¹⁷⁸ Neuhoff *et al* op cit (n69) 55.

¹⁷⁹ Ibid.

¹⁸⁰ Neuhoff *et al* op cit (n69) 53.

would inevitably close down. The bracket of consumers in the specific locale wherein the shopping centre exists will likely not be of great enough a number to result in profits being achieved by *both* of the supermarkets; the result is that a less concentrated amount of consumers will frequent both of the existing supermarkets, as opposed to all the consumers frequenting the only one that exists, which will result in an achievement of profit and return on investments for the supermarket. In addition, if two supermarkets that exist within a centre both close down due to the aforementioned rationalisation, then that impacts the shopping centre landlord negatively, too, since the presence of a supermarket has been shown to generate foot traffic in a shopping centre.¹⁸¹

Despite the plausibility of this justification, in *Patensie Sitrus Beherend Beperk v The Competition Commission and Others*,¹⁸² the Competition Appeal Court rejected the efficiency defences of a firm on the grounds that the efficiencies brought forward could still be achieved without resorting to an exclusivity agreement. The same can be said of the above efficiency: In a market where competition is able to take place naturally and freely, and where competitors compete in a vigorous manner via the means of *inter alia* competitive pricing and innovation (that is, in a market that is not imposed by exclusive leases) the inefficient supermarket or store will be culled from the market without the need for the use of an exclusive lease. The majority of consumers who visit the centre will rather frequent the store that prices more competitively, pays attention to quality and innovation and who, on the whole, is a better and more efficient firm. This postulation of the outcome of the natural flow of competition obviates the need for exclusivity in leases, and disaffirms the above-mentioned defence that may be brought by the supermarket.

One justification that is public knowledge, is that expounded by Ricky Mann, writing for the Competition Commission newsletter, who confirms that one of the numerous reasons provided by the supermarket respondents for their behaviour, is ‘the positive externality on the shopping centre due to their presence in terms of attracting customers to the centre, as

¹⁸¹ *Supra* p 15.

¹⁸² (CT 16/CAC/Apr02) [2003] 2 CPLR 247 (CAC) at 499.

well as the need to protect the investment in the store and recoup the investment price.’¹⁸³ The latter justification has strong resonance with one that is for the sole gain of the supermarket itself rather than for the benefit of competition or consumers. Mann further dismisses these reasons on the basis that they are incongruent with the standard approach taken by supermarkets in their exclusivity leases, which is to apply them in a blanket manner and for a long-term duration; this suggests, contrary to the supermarkets’ claim, that the reason for exclusivity does not find origin in a case-by-case analysis of the probable risk assessment of each investment.

It is contended, therefore that the stated and postulated efficiency defences brought by the supermarket respondents above, will undoubtedly fail as being insufficient to outweigh the anticompetitive effects of exclusive leases in shopping centres, and that the Competition Commission

‘... In a vertical relationship’

In order for an agreement¹⁸⁴ to constitute a breach of s 5(1) of the Act and be considered a prohibited practice demonstrating anticompetitive effects, it must be ascertained that the agreement is between parties who are in a *vertical* relationship. The Act defines a ‘vertical relationship’ as “the relationship between a *firm* and its suppliers, its customers, or both.”¹⁸⁵ Furthermore, agreements between parties in a vertical relationship have been defined to mean those concluded between different parties who occupy different levels of the supply chain, such as between a manufacturer or producer of goods or a supplier of services (upstream party), and a distributor such as a retailer or wholesaler (downstream party) that distributes the manufacturer’s goods.¹⁸⁶ In most markets upstream parties or producers do not sell the goods that they produce from raw materials directly to the

¹⁸³ Ricky Mann ‘Commission non-refers supermarkets investigation’, March 2014, available at <http://www.compcom.co.za/wp-content/uploads/2014/09/Competition-Commission-Newsletter-Edition-48.pdf>, accessed on 19 January 2015.

¹⁸⁴ Defined in s 1 as including a ‘contract’ under which a lease agreement falls.

¹⁸⁵ S 1(1)(xxxiii)(c)(ii).

¹⁸⁶ Paul Cook, Raul Fabella & Cassey Lee (eds) *Competitive Advantage and Competition Policy in Developing Countries* (2007) 35; Neuhoff *et al* op cit (n69) 85; Whish & Bailey op cit (n136) 618; Massimo Motta *Competition Policy: Theory and Practice* (2004) 302: “Despite the different labels, the relationship is of the same nature.”

ultimate consumer, but do so through intermediaries such as wholesalers or retailers who then go on to sell the goods to the ultimate consumers;¹⁸⁷ such firms are said to be in a vertical relationship with one another.

Upon consideration of this definition of a vertical relationship, it is difficult to reconcile the Commission's classification of parties to a lease agreement as falling within a vertical relationship, since, although we have a downstream party – namely the supermarket who distributes goods –, there is conceptual difficulty with placing a landlord of a shopping centre in the category of 'upstream party'. A landlord of a shopping centre is certainly not an upstream party in the sense of a producer of goods, however an upstream party is also described as a supplier of services,¹⁸⁸ and it is within this category that it can be assumed the Commission intended to place a landlord of a shopping centre in bringing the practice of exclusive lease agreements under section 5(1) of the Act. A landlord of a shopping centre, who could be either a natural or legal person, owns land and the buildings on the land for the purpose of renting space on the land or within the buildings on the land to tenants. A landlord can thus be construed as a supplier of a service, that is, the service of supplying land or leasable shopping centre space to suitable tenants for a specified time and purpose in exchange for rental payment. A tenant, however, could not, in a conceptually logical fashion, be viewed as a downstream party that performs the function of distributing the aforesaid services of the landlord to customers, as the tenant is itself a customer of the landlord and does not perform the function of distributing the landlord's services.

¹⁸⁷ Massimo Motta *Competition Policy: Theory and Practice* (2004) 302.

¹⁸⁸ Whish & Bailey op cit (n136) 618.

The European Union Position – Placing Further Doubt on the Commission’s Classification of Exclusives under S 5(1)

Article 101 (1) of the Treaty of the Functioning of the European Union (TFEU)¹⁸⁹ prohibits vertical agreements that prevent, restrict or distort competition, while Article 101(3) of the TFEU provides for block exemptions, which state that the prohibition in Article 101(1) could be declared inapplicable in relation to agreements and categories of agreements that fulfil certain requirements,¹⁹⁰ in particular, *inter alia*, those “practices that contribute to improving the production or distribution of goods or to promoting technical or economic progress...”. These sections thus substantially mirror section 5(1) of the Act and an interpretation of the former can thus be of use to that of the latter.

According to paragraph 26 of the Vertical Guidelines, which sets out the principles for the assessment of vertical agreements under Article 101 of the TFEU, an agreement for the lease or rental of goods is not assessed as a vertical agreement, as no good or service is being sold by the supplier to the buyer. Due to the similarities that exist between article

¹⁸⁹ Formerly Articles 81 and 82 of the Treaty establishing the European Community (EC Treaty). The full text of Article 101 reads:

1. The following shall be prohibited as incompatible with the internal market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market, and in particular those which:
 - (a) directly or indirectly fix purchase or selling prices or any other trading conditions;
 - (b) limit or control production, markets, technical development, or investment;
 - (c) share markets or sources of supply;
 - (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
 - (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.
2. Any agreements or decisions prohibited pursuant to this Article shall be automatically void.
3. The provisions of paragraph 1 may, however, be declared inapplicable in the case of:
 - any agreement or category of agreements between undertakings,
 - any decision or category of decisions by associations of undertakings,
 - any concerted practice or category of concerted practices, which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:
 - (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;
 - (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

¹⁹⁰ Whish & Bailey op cit (n136) 82 and 168; EU Guidelines on Vertical Restraints (2010) para (5) (‘Vertical Guidelines’)

101 and section 5(1), this assessment of article 101 further works against the Commission's classification of exclusive lease agreements as falling under the jurisdiction of section 5(1), since such an agreement is for the rental of space.

'Firm' – Redemption for the Commission's Classification of Exclusives under s 5(1)

The difficulty in classifying the landlord and tenant as upstream and downstream parties in order to bring their relationship under the realm of section 5(1), is, however, redressed by reverting to the Act's definition of a vertical relationship, which does not exist in the TFEU. 'Vertical relationship' is defined in the Act as the relationship between a *firm* and its suppliers, its customers, or both,¹⁹¹ with the term '*firm*' mentioned therein, further defined as '[including] a person, partnership or a trust'.¹⁹² The use of the word 'includes' suggests that the list is an inexhaustible one and corporations could thus be included thereunder. In addition, 'person' is not defined and could thus refer to either natural or legal persons, the latter of which a corporation too falls under.¹⁹³ Therefore, a *firm* could refer to either the supermarket tenant, (a legal person) who would be in a relationship with its landlord supplier, or to the landlord him/her/itself who is in a relationship with its supermarket customer (customer in the sense that the supermarket is paying for the services of the landlord). Under this line of reasoning, a landlord and tenant could be included as those parties falling under the definition of a vertical relationship as defined in the Act, and the Commission's classification under section 5(1) is therefore salvaged in relation to the 'vertical relationship' requirement.

¹⁹¹ Section 1(xxiii)(c)(ii) of the Act.

¹⁹² Section 1(xi) of the Act.

¹⁹³ Further support for the contention that person includes legal persons can be found in s 3(1) of the Act where it is stated that the Act applies to all economic activity within, or having an effect within, the Republic. Economic activity defined as activities that involve production, distribution and consumption of goods and services in society (<http://www.businessdictionary.com/definition/economic-activity.html> accessed on 11 April 2014); corporations and other legal persons form part of such economic activities.

‘Restrictive vertical practices...’

Competition concerns are raised in circumstances where a restrictive vertical practice or a ‘vertical restraint’¹⁹⁴ is observed; that is, where the agreement between parties in a vertical relationship has the effect of substantially preventing or lessening competition in a market and there is no countervailing technological efficiency or other pro-competitive gain.¹⁹⁵ Motta eloquently explains the nature of vertical restraints and the reasons for their coming into existence between parties who are vertically related:

“Consider the classic example of the vertical relationship between a manufacturer and a retailer which distributes its products. In general, both the manufacturer and the retailer decide on different actions, and what is an optimal action for one is not necessarily optimal for the other. As a result, a party can try to use contracts and clauses so as to restrain the choice of the other and induce an outcome which is more favourable to itself. (To put another way, each party’s actions create an externality on the other. Vertical contracts might be used to try to control for these externalities.)”¹⁹⁶

The above explanation by Motta fuels the need to emphasise that the ‘control’ of these ‘externalities’ through vertical agreements may not be competitively viable or legal and should thus be disallowed due to the effect that they have of substantially preventing or lessening competition in a market without a countervailing technological efficiency or other pro-competitive gain, to state the exact words of the Act; it is precisely this factor which must be considered in the current context of shopping centre exclusives.

There are various forms of vertical restraints that have come into existence, and a brief explanation of the potentially pertinent types in relation to the current context will be expounded on in order to determine which type, if any, a exclusive lease agreements of the kind under examination, falls under.

¹⁹⁴ Motta op cit (n187) 302; Neuhoﬀ *et al* op cit (n69) 93; Whish & Bailey op cit (n136) 625.

¹⁹⁵ Section 5(1).

¹⁹⁶ Motta op cit (n187) 302.

Vertical Agreement Constructions Potentially Applicable to Shopping Centre Lease Exclusives

i) Territorial Restrictions

Territorial restrictions, initiated by an upstream party, limit the geographic territory in which a downstream party may resell the upstream party's product, having the effect of a retailer not being allowed to sell a manufacturer's product outside of a specified geographical territory, thereby preventing the retailer from selling the manufacturer's product to customers who reside or have their places of business outside of that area.¹⁹⁷ In short, the retailer agrees to sell to only a particular customer, that is, those in a specified territorial jurisdiction. The primary objective of this restraint is to restrict intrabrand competition (the competition between retailers who sell the same brand) and thereby control free riding.¹⁹⁸ Free riding occurs when one retailer benefits from the services provided by another retailer in relation to a certain product which both retailers sell. For example, some retailers supply the service of providing information or demonstrations to a customer about a product in order to induce them to buy a product; retailers that provide such services usually sell the product at a higher price than those that don't (for various reasons, the most obvious of which is that the latter retailer will have lower costs attributed to, *inter alia*, their lack of employees with sufficient expertise about the various products), and thus the latter may benefit from the services of the former, as customers are likely to buy from the retailer with the lower price, regardless of who provided him/her with the service.¹⁹⁹

Through a territorial restriction, a manufacturer insulates its appointed distributors from competition from other distributors who sell the manufacturer's product.²⁰⁰ Manufacturers argue that protecting dealers from intrabrand competition supports the former's desire that

¹⁹⁷ Neuhoff *et al* op cit (n69) 93; Motta op cit (n187) 304; 'Exclusive Territorial Arrangements and the Antitrust Laws' (1964) 39 *Indiana Law Journal* 785 at 785 Available at <http://www.repository.law.indiana.edu/ilj/vol39/iss4/5>

¹⁹⁸ Shantanu Dutta, Jan B. Heide & Mark Bergen 'Vertical Territorial Restrictions and Public Policy: Theories and Industry Evidence' (1999) *Journal of Marketing* 121 at 121 and 122; Neuhoff *et al* op cit (n69) 87.

¹⁹⁹ Dutta op cit (n198) 122.

²⁰⁰ Ernest Gellhorn, William E Kovacic & Stephen Calkins *Antitrust Law and Economics In a Nutshell* (2004) 359.

customers be attracted to its product through the intensive sales and service efforts by its dealers, and sometimes gain a greater return on investment.²⁰¹ Brand reputation is also conserved through the distribution of manufacturer's products by legitimate, authorized dealers. Dealers contend that by being free of intrabrand competition, they can promote the product more fully through greater sales and service efforts (as they are protected from free riders), and reduce their investment risk.²⁰²

Technical Dissimilarity, Yet Consequential Parallelism

Applying this construction to a shopping centre exclusive is practically difficult and unworkable. In order for an exclusive lease agreement between a shopping centre landlord and a supermarket tenant to be classified under a territorial restriction agreement, the landlord ought to be viewed as a supplier of the service of providing rentable space, and the supermarket tenant the exclusive distributor of the landlord's services within a designated territory. The relationship between a lessor and lessee does not represent this type of classification, and it is thus dubitable that it was under this construction of a vertical restraint that the Commission intended to place exclusives between shopping centre landlords and supermarket tenants.

The similarity, however, between territorial restrictions and exclusivity clauses in shopping centre leases becomes discernible when one considers the fact that one party is given a confined space to conduct their business of running a supermarket, while other parties who conduct the same business are restricted from doing so within that space. In other words, an exclusive lease agreement in a shopping centre reflects a territorial restriction in the sense that one party conducting the business of a supermarket and occupying a specific space within the centre, is the only party that is allowed to conduct that particular type of business within that space.

Therefore, despite the inability of the parties to be categorised accurately and concretely as an upstream manufacturer of goods or supplier of services, and a downstream retailer or

²⁰¹ Gellhorn, Kovacic & Calkins supra (n200) 360.

²⁰² Ibid.

distributor of those goods or services, the overall effect that a territorial restriction produces is the same as that of an exclusive lease agreement in a shopping centre. It is therefore assumed that if the Commission categorised exclusives as a territorial restriction-type vertical restraint in order to analyse it under s 5(1) of the Act, it is as a result of the parallel effects that exist between the two, rather than their technical similarities.

ii) Exclusive Dealing

An exclusive dealing agreement occurs when a retailer (or downstream party) agrees to carry and sell only the brand of a particular manufacturer (or upstream party), subject to the threat of refusal to supply by the manufacturer.²⁰³ In other words, a buyer purchases its requirements exclusively from a single supplier, effectively agreeing not to purchase from the supplier's competitors.²⁰⁴ The effect of such an agreement is that competitor suppliers or manufacturers (upstream parties) of other brands of the same product in question are denied access to the distribution services offered by the retailer, thereby excluding competitors from the marketplace or handicapping their ability to compete.²⁰⁵

The objectives of partaking in an exclusive dealing arrangement have been said to be their promotion of more effective distribution by increasing dedication and loyalty, minimizing free-riding (thereby increasing output) and ensuring retailers of a reliable source of supply.²⁰⁶

In order for an exclusive lease agreement between a shopping centre landlord and a supermarket tenant to be classified as an exclusive dealing agreement, the former would need to be viewed as an exclusive supplier of services to the latter, the latter agreeing to be the only distributor of such services. This, again, is an unworkable application to the lessor lessee relationship in the context of an exclusive lease agreement in a shopping centre. It

²⁰³ Motta op cit (n187) 304; Philip Sutherland and Katharine Kemp *Competition Law of South Africa* (2013) 6-7; Cook, Fabella & Lee op cit (n186) 35.

²⁰⁴ Areeda, Kaplow & Edlin op cit (n153) 534.

²⁰⁵ A. Douglas Melamed 'Exclusive Dealing Agreements and Other Exclusionary Conduct – Are There Unifying Principles?' (2005-2006) *Antitrust Law Journal* 375 at 375.

²⁰⁶ Jonathan M. Jacobson 'Exclusive Dealing, "Foreclosure", and Consumer Harm' (2002-2003) *Antitrust Law Journal* 311 at 312.

is, however, indeed the case that an exclusive lease agreement in a shopping centre context requires the landlord to deal exclusively with one supermarket tenant and not to deal with other competitors of that supermarket. In other words, the landlord is required to provide rentable space to only one supermarket. Melamed defines exclusive dealing agreements generally as agreements in which one party promises to deal exclusively with another and, thus not to deal with the competitors of the other.²⁰⁷

Therefore, as was the case with territorial restrictions, the typical technical construction of an exclusive dealing agreement is not adhered to in the context of shopping centre exclusives, however, the effects thereof, are paralleled; and it is under this parallel effect approach that it can be assumed the Commission sought to place exclusivity leases under in order to analyse it as a vertical restraint in terms of section 5(1) of the Act.

iii) Exclusive Distribution

An exclusive distribution agreement is one where a manufacturer agrees to sell his products exclusively to one distributor, who alone will distribute the manufacturer's goods in a specific area.²⁰⁸ The main concerns with such agreements are that intrabrand competition will be reduced and that an increase in exclusive distribution may lead to foreclosure of other distributors, thereby reducing competition at that level.²⁰⁹

Exclusive distribution agreements have been said to be an incentive to sellers for products that are purchased infrequently, and when only a limited market is available for products, such as Porsche, BMW or high-end watches.²¹⁰

In order for an exclusive lease agreement between a shopping centre landlord and a supermarket tenant to be classified as an exclusive distribution agreement, the shopping

²⁰⁷ Melamed *op cit* (n205) 375.

²⁰⁸ Neuhoff *et al op cit* (n69) 94; *Glaxo Wellcome (Pty) Ltd v Terblanche NO and others* [2001-2002] CPLR 48 (CAC) at 62; *Paddock Publications, Inc. v. Chicago Tribune Co* (1997) 103 F.3d 42 where two news services, the New York Times news service and the Los Angeles Times/Washington Post news service were the exclusive distributors of the Tribune and the Sun-times respectively.

²⁰⁹ Whish & Bailey *op cit* (n136) 639-40.

²¹⁰ William M Pride and O.C. Ferrell *Marketing* (2010) 401.

centre landlord would need to be viewed as an upstream party who provides his services to only one distributor, who alone distributes those services, namely the supermarket tenant. Since the supermarket lessee and shopping centre lessor relationship again cannot be rationally reconciled with this construction, it is assumed that, if the Commission intended to bring exclusive leases under the exclusive distribution construction in order to analyse the former under section 5(1) of the Act, then it would be again based on the parallel effect approach: that the effect of an exclusive distribution agreement parallels that of an exclusive lease agreement in a shopping centre context, in the sense that it excludes other distributors from being able to partake in the distribution of certain products in a specific area.

The above analysis represents an attempt to justify the Commission's placement of exclusive lease agreements in shopping centres under the jurisdiction of section 5(1) by fitting such agreements into one of the established categories of vertical restraints. Based on the above analysis, it is apparent that it is unfeasible to attempt a rigid, technical placement of exclusive lease agreements into any of the developed and pertinent categories of vertical restraints. However, the parallel effects that exist between the various categories and shopping centre exclusives provide a sound basis for the assumption that it was based on a purposive approach to the various potentially applicable vertical restraint constructions that the Commission adopted in order to place them into one of the categories, rather than a literal one.

Conclusion

Despite the practical inapplicability of shopping centre exclusives to one of the various vertical restraint constructions, it does not follow that exclusives do not qualify as a type of vertical restraint, since, according to section 5(1), a vertical restraint is observed where the agreement between parties in a vertical relationship has the effect of substantially preventing or lessening competition in a market and there is no countervailing technological efficiency or other pro-competitive gain. Since it has, to the fullest extent possible, been shown in the preceding sections of this study, that exclusive shopping centre

leases do indeed satisfy these elements, it can conclusively be asserted that the Commission's decision to not refer such a practice to the Tribunal for adjudication, was an erroneous one. The dangers and competitively damaging repercussions for South African competition law that this failure to prohibit such agreements produce, remain in the market today and time will be the only indicator as to whether the Tribunal will alleviate such dangers through comprehensive adjudication on the matter.

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