

Supermarket Pricing Inquiry

Submission No: 48
Submitted by: Australian Retailers Association
Publication:
Attachments:
Submitter Comments:

ARA SUBMISSION

QLD SELECT COMMITTEE - INQUIRY INTO SUPERMARKET PRICING

APRIL 2024

The Australian Retailers Association (ARA) welcomes the opportunity to provide comments on the QLD Select Committee - Inquiry into Supermarket Pricing

The ARA is the oldest, largest, and most diverse national retail body, representing a \$420 billion sector that employs 1.4 million Australians – making retail the largest private sector employer in the country. As Australia's peak retail body, representing more than 120,000 retail shop fronts and online stores, the ARA informs, advocates, educates, protects, and unifies our independent, national, and international retail community.

We represent the full spectrum of Australian retail, from our largest national and international retailers to our small and medium sized members, who make up 95% of our membership. Our members operate across the country and in all categories - from food to fashion, hairdressing to hardware, and everything in between.

Specifically, we are proud to represent Australia's largest supermarket groups, Woolworths and Coles. as well as new entrants like Costco and Amazon. We welcome the opportunity to highlight the positive ways in which these organisations support local communities and economies right along the retail value chain.

EXECUTIVE SUMMARY

Australia's grocery sector has changed significantly since the last inquiry into supermarkets held by the ACCC in 2008 concluded that the sector was "workably competitive."

Since that time, overseas entrants have entered the market or expanded their operations - boosting competition in the sector for the benefit of Australian consumers. The growth of online shopping and adoption of extended trading hours have provided further benefits to consumers.

However, these improvements have coincided with significant increases in the cost of doing business - as a result of the pandemic, global conflict and natural disasters - that have resulted in higher prices for consumers.

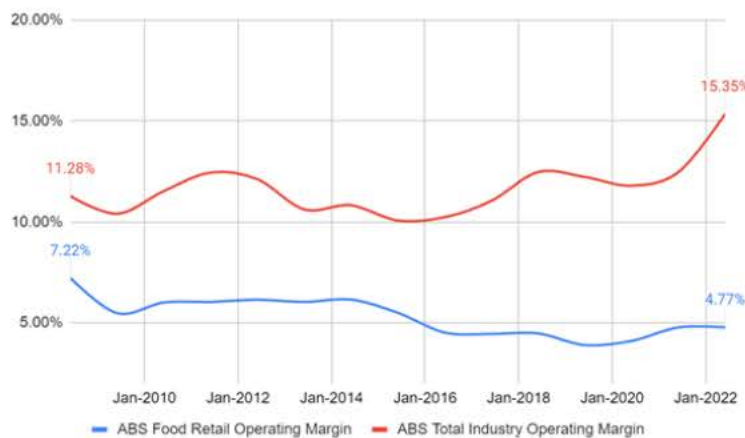
There are numerous inquiries across the country on - or involving - Australia's largest supermarkets, including this inquiry in Queensland. We note the Terms of Reference for the Queensland Supermarket Pricing Select Committee.

1. A select committee, known as the Supermarket Pricing Select Committee (committee) be established to:
 - a. examine the causes and effects of increased supermarket prices; and
 - b. identify opportunities to increase transparency in the supermarket sector for consumers and producers.
2. In undertaking the inquiry, the committee consider:
 - a. rising grocery prices in Queensland and discrepancies between retail and wholesale and farmgate prices, including different-sized businesses;
 - b. the variability in supermarket offerings and pricing across the state, particularly in regional Queensland and in remote Aboriginal and Torres Strait Islander communities;

- c. the long-term trends in profits accruing along the supply chain for perishable produce, with particular regard to impediments to the profitability of primary producers;
- d. the conduct of retailers in negotiations with Queensland producers, and the prevalence and effects of information asymmetry between these parties;
- e. improvements to Queensland's policy environment to increase transparency for producers, including what data will reduce information asymmetry, and/or reduce prices for consumers; and
- f. any other reviews or inquiries occurring in Australia regarding this matter, with a view to complement these analyses by focusing on potential Queensland Government responses.

In response to these issues, the ARA makes the following observations.

1. There is effective competition between Australia's major supermarkets in the supply of groceries to Australian consumers. Competition has increased since the 2008 ACCC review with Australia's largest supermarkets competing aggressively on price, product offerings and customer experience.
2. These competitive forces have put downward pressure on profits for Australian supermarkets, with Australian Bureau of Statistics (ABS) data confirming that Food Retailing Operating Margins have reduced from 7.2% in 2008, to 4.8% in 2022 (the last available data source). This trend is in contrast to the increase in Operating Margins across the broader economy over the same period, as per the chart below.



Source: ABS Food Retailing Operating Margins

3. Australian supermarkets continue to compete on price, even in the current environment where prices are increasing across the sector. The key factor impacting higher prices for consumers is an increase in the costs of doing business - including labour costs, supply chain costs, leasing costs and energy costs. While some of these higher costs have been absorbed by retailers, or offset by operational savings resulting from investment in technology, some portion of these higher costs has been passed onto consumers.
4. Our members also compete in areas other than price. The use of loyalty schemes, in particular, allows supermarkets to provide personalised and tailored customer experiences, and the provision of private label products aims to improve choice for consumers who are becoming increasingly budget conscious.
5. Australia's largest supermarkets work with supply chain partners to deliver maximum value and choice to consumers. Where large supermarkets can leverage efficiencies of scale along the supply chain,

supermarkets are in a better position to pass on lower costs to consumers. However, in some categories where supermarkets do not have strong bargaining power, they are price-takers and consumers are generally worse off as a result.

6. The Australian retail sector remains impacted by four years of disruption as a result of the pandemic, post-pandemic economic headwinds, natural disasters and supply chain impacts. Despite this, our sector has continued to invest heavily to serve local communities, support domestic suppliers and employ more than 1.4 million Australians.
7. The biggest threat to this continued investment is the current discourse with government and regulators that threaten to break-up Australia's largest supermarkets, which would almost certainly have a detrimental impact on Australian consumers, through higher price, less choice and a service experience that fails to keep pace to consumer expectations.

The ARA's submission has been informed by extensive consultation with our members in the food and grocery sector, and is based upon our previous submission to the Select Senate Inquiry into Grocery Prices.

ARA RESPONSE

The ARA makes the following observations and recommendations in response the committees' terms of reference.

The key driver of higher prices for consumers is higher costs for retailers

The ARA welcomes the opportunity to participate in this Inquiry, which we believe will most likely confirm what we already know – that the cost of doing business has increased across the board in recent years; and that these higher costs along the retail value chain are key drivers of higher prices.

The same inflationary pressures impacting households are also impacting businesses, with the cost of doing business in Australia increasing across the board in recent years - including increases in wages, fuel costs, energy costs and leasing costs.

According to the Reserve Bank of Australia (RBA), these pronounced inflationary trends arise from diverse factors, encompassing supply constraints arising from geopolitical issues, the pandemic and domestic impacts from natural disasters. In navigating these pressures, supermarkets collaborate with suppliers to address challenges and minimise impacts on prices where possible.

To better understand the factors that influence retail prices, and hence overall inflation, it is imperative to examine the various costs and margins involved in the journey from suppliers to consumers. Five major cost components shape this process:

- the supplier's cost of procuring or producing goods;
- the supplier's operational costs;
- the supplier's sell price, inclusive of the supplier's profit;
- the retailer's operational costs, tax and interest obligations; and
- the retailer's net profit.

As noted, costs have increased across the board in recent years. However, our members have maintained a stable NPAT over the past five years, despite these higher costs, in support of our position that allegations of excessive or unreasonable profits are unfounded.

In FY23, Coles and Woolworths Group both reported NPAT of around 2.6%. That is to say that for every \$100 in sales, our members make an NPAT of \$2.60. Put another way, if supermarkets made no profit (which is not tenable) then the cost of the same \$100 basket would reduce to \$97.40.

It is worth noting that this \$100 also pays to keep staff employed, pays suppliers to keep their teams employed and pays for rent, energy, fuel and tax. It also helps fund reinvestment into areas of the business that contribute to community improvements, such as the development of new stores and distribution centres as well as investments into sustainability and community initiatives.

Graeme Samuel AC, Chairman of the ACCC between 2003 and 2011, who oversaw the last review of the Food and Grocery Code of Conduct in 2018, stated:

A lot of this could be resolved by looking at the annual accounts. The simplest thing to do is to look at profit margins, and are they reasonable or not? Compared with overseas, Australia is more competitive, lower profit margin, and pricing.

To reaffirm our position, the ARA believes that higher prices are due to higher costs not higher profits.

Driving value and competition in the Australian food retail sector

There is a high degree of both price and non-price competition between supermarkets and other grocery retailers. That competition has increased significantly with the growth of Aldi, Amazon and Costco, and new convenient online food providers such as Hello Fresh and UberEats.

The competitive constraint exerted by independent supermarkets such as IGA, Foodland, Drakes and Harris Farm has increased as new stores have opened across the country. Australian customers continue to demand world class stores and top quality produce. They can and do take their business to alternative nearby stores or online if their shopping experience is unsatisfactory.

Our members strive to negotiate mutually beneficial commercial arrangements with suppliers that often lead to cost savings that can be passed on to consumers. Consumers are savvy and have high expectations of retailers in terms of value, choice and convenience.

Consumers have many choices as to where they can buy their food and groceries including:

- Major supermarkets such as Woolworths, Coles, Aldi and Costco;
- Local and community supermarkets such as IGA, Spudshed and Drakes;
- Australian grocery chains like Harris Farm;
- Small businesses like local bakeries, butchers and greengrocers;
- Direct to consumer and wholesale markets;
- Meal kit delivery services; and
- Fast food, restaurants and take-away services.

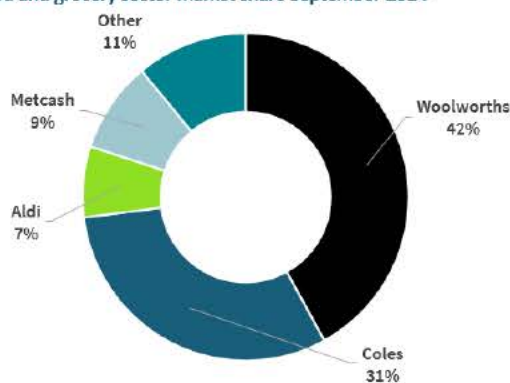
The vast majority of Australians can choose from a range of stores in their local area and the barriers to switching grocery retailers are very low. This is markedly different to the experience of Australians in other essential consumer markets like banking, insurance, energy or telecommunications.

Price is one of the top drivers of consumer choice and this drives intense competition between grocery retailers.

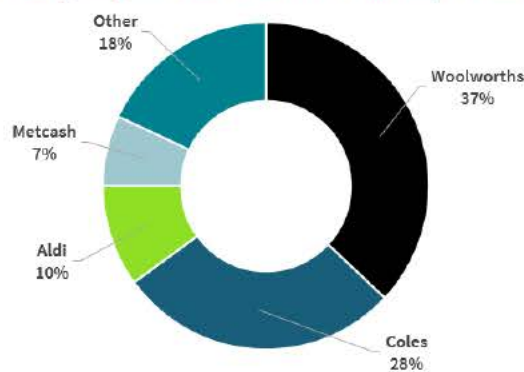
Since 2014 there has been an 8.2% contraction in the combined market share of Coles and Woolworths as Aldi, Costco and IGA gain share and boost competition in the market, encouraging innovation and improving quality across the industry. The 2017 launch of Amazon Australia has provided further customer choice, particularly in packaged grocery and everyday needs. The ARA notes the Terms of Reference for the Inquiry does not include other overseas-headquarters food retailers.

The chart below highlights the increase in market share of other competitors nationally.

Food and grocery sector market share September 2014



Food and grocery sector market share for the financial year 2022-23



Source: IBISWorld

In its 2023 submission to the House of Representatives Standing Committee on Economics Inquiry into promoting economic dynamism, the Productivity Commission wrote in relation to supermarkets:

The sector has observed aggressive competition between Australia’s two major domestic supermarkets despite the high level of concentration.

Woolworths Group has a 37% share of the market in 2021 and Coles 28%. The other two main competitors, Aldi and Metcash (which includes IGA and Foodland) had a 10% and 7% share respectively (source: Hunt Export Advice 2023). There are other competitors in the wings offering new delivery options.

Supermarkets reported that they have responded to increases in competition by limiting price increases and enhancing the ‘in-store experience’ — improving the level of customer service and increasing the range of services offered.

Two large players with a competitive fringe have provided a highly competitive market in Australia.

These data points and observations are reflective of a highly competitive sector that is becoming more competitive, with the vast majority of Australians able to choose from a range of stores in their local area and shop around for the best value and product offering. This is markedly different to the experience of Australians in other essential consumer markets like banking, insurance, energy or telecommunications - where the cost of switching is a key barrier for consumers and competition.

Competition levels between supermarkets vary across metropolitan, regional, and remote areas. Metropolitan areas typically have a higher density of supermarkets and in most inner-city areas consumers can access a Woolworths, Coles, Aldi, IGA and independent stores close to home as well as access to online shopping, such as Uber Eats. The ability to expand and compete in metropolitan areas provides our members with capital to invest in regional and rural areas, bringing job security and food security to local communities.

During the Tasmanian hearing of the Select Senate Committee into Supermarket Prices, we note Ms Tania Hunt, Chief Executive Officer, Youth Network of Tasmania made the following remarks in regard to competition and the cost of groceries in regional Tasmania:

“...that there is less competition, and they tend to be smaller supermarkets, or an IGA, for example. Some of those rural and remote communities don't have Woolworths or Coles or larger supermarket chains in their communities.

“Essentially these challenges are further exacerbated for young people living in rural and remote communities. We've heard from young people that the price of supermarket groceries can be up to 50 per cent more expensive than in metro areas.”

Regional and remote areas may face challenges due to the size of Australia, which impacts freight and fuel costs. However, where there are efforts by large supermarkets to expand into regional and remote areas there is increased competition and improved access to groceries for residents. The ability to expand allows supermarkets to keep prices low.

The Food and Grocery Code of Conduct remains the best mechanism for managing disputes between retailers and suppliers

Maintaining robust trade partnerships is a cornerstone of our members' commitment to ensuring optimal outcomes for both customers and suppliers. Despite the fluctuation in product prices, various associated costs persistently remain high, encompassing transport, processing, packaging, labor, and operational expenditures.

The Food and Grocery Code of Conduct serves as the current mechanism to address disputes arising from these and other pressures, providing suppliers the means to independently and confidentially address concerns related to retailers. With the Code sunsetting on 1 April 2025, a review of the Code is required to determine whether it remains fit for purpose.

The ARA notes Dr Craig Emerson has been appointed to undertake this review of the Code, supported by a secretariat within Treasury. This week an interim report was handed down with 10 draft recommendations, including:

- The Food and Grocery Code of Conduct should be made mandatory
- All supermarkets that meet an annual revenue threshold of \$5 billion (indexed for inflation) be subject to the mandatory Code.
- The Code should place greater emphasis on addressing the fear of retribution
- Penalties for non-compliance should apply, with penalties for more harmful breaches of the Code being the greatest of \$10 million, 10 per cent of turnover, or 3 times the benefit gained from the contravening conduct.

As proud founding signatories bound by the Code, Coles and Woolworths have both publicly supported the draft recommendations.

Under the current Code a Code Arbiter, appointed by grocery retailers and wholesalers, diligently investigates and proposes resolutions while ensuring confidentiality and promoting fair dealings. An annual report, publicly

accessible on retailers' websites, details the complaints received and resolved. Upholding confidentiality, the Code Arbiter guards the supplier's identity unless explicit consent is provided. Dissatisfied suppliers can call upon the Independent Reviewer to assess the Code Arbiter's process.

The recent annual report by Independent Reviewer Chris Leptos revealed no formal complaints from food and grocery suppliers against Woolworths and Coles in 2023. In parallel, both members proactively foster supplier relations through an in-house complaint process, reinforcing an environment of open communication.

Graeme Samuel AC remarked the Code has largely worked, with improved relationships between retailers and suppliers and complaints resolved by an independent arbiter.

The ARA also notes the Federal Treasurer has directed the ACCC to hold a price inquiry into the markets for the supply of groceries. Importantly, the ACCC has been directed to look at the structure of grocery markets, including competition at the supplier, wholesaler and retailer levels. The emphasis on reviewing the entire grocery supply chain, not just the retail segment at the end, is welcome. Our members look forward to assisting the ACCC.

The evolution of online shopping and other mechanisms has created transparency in pricing without the need for regulation

The ARA recognises the importance of transparency in the supermarket sector for the benefit of both consumers and producers. While transparency is crucial for fostering trust and fairness in the marketplace, implementing initiatives such as pricing panels - a suggestion from the Australian Council of Trade Unions - presents significant challenges due to the diverse range of products held in supermarkets.

Pricing panels, while theoretically promising, may encounter practical difficulties when applied to supermarkets. Unlike industries with more standardised products, supermarkets stock a vast array of items, ranging from fresh produce to packaged goods and household essentials. Each of these products may have varying cost structures, sourcing methods and price dynamics, making it challenging to create a standardised pricing panel that accurately reflects market conditions across all product categories.

Moreover, the dynamic nature of retail pricing adds another layer of complexity. Prices in the supermarket sector can fluctuate frequently due to factors such as changes in supply chain costs, seasonal demand and promotional activities. Implementing pricing panels that accurately capture these fluctuations in real-time would require sophisticated data collection and monitoring systems, which may not be feasible for all retailers, especially smaller operators.

Our position is that other measures, already in place, provide pricing transparency to consumers, without the need for regulatory intervention.

Many of our members offer both online and in-store sales channels, allowing consumers to compare prices and offers from home before making a purchase. By investing in user-friendly digital platforms and price comparison tools, retailers can empower consumers to make informed purchasing decisions while promoting healthy competition in the marketplace.

Furthermore, our members have invested in developing robust online propositions and digital tools to enhance the shopping experience and assist customers. These digital tools include features designed to empower customers, such as:

- **Cumulative spend tracking:** Customers can track their total spend in real-time as they add products to their online cart, enabling them to adjust their selections to align with their budgetary constraints.

- **Digital shopping lists:** Before visiting the store, customers can prepare their shopping lists digitally, incorporating specials, seasonal discounts, and ongoing low prices, thereby streamlining their in-store shopping experience.
- **Best unit price tool:** Our members offer a "best unit price" tool, which ranks products based on their price per unit, allowing customers to identify the most cost-effective options effortlessly.
- **Comprehensive specials listings:** Customers have access to a comprehensive database of weekly specials, extending beyond those featured in printed or digital catalogues, enabling them to maximise savings on their purchases.

Through these innovative digital tools, our members provide customers with greater transparency during their shopping experience, facilitating informed decision-making and enhancing overall satisfaction.

CONCLUSION

The Queensland grocery sector is complex and any analysis of this sector requires an understanding of the unique geographic, supply chain and regulatory factors which impact competition, as well as a recognition of the efficiencies that contribute towards competitive pricing, enhanced consumer choice, convenience and experience.

There are multifaceted factors contributing to higher prices, including energy, labour, logistics and taxation.

In our [Pre-budget Submission](#), the ARA made a number of recommendations to address these challenges and their impact on the retail value chain.

The ARA highlights the commitment of its members to transparency, customer value, and innovation through their initiatives such as price freezes, loyalty programs, and the introduction of home brand products.

In navigating the complex grocery sector landscape, the ARA urges regulators and policymakers to consider the holistic view of the supply chain, the impact of global factors on prices and the continual need for innovation and efficiency.

Regulatory oversight in this sector must be mindful of the complex market dynamics in order to foster a competitive and transparent, grocery sector landscape in Australia which is best able to serve the changing needs of Australian consumers.

Thank you again for the opportunity to provide a submission on the proposed amendments to the QLD Supermarket Pricing Select Committee - Inquiry into Supermarket Pricing. Any queries in relation to this submission can be directed to our policy team at policy@retail.org.au.