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Inquiry into Australian Retail Industry  
Productivity Commission  
GPO Box 1428,  
Canberra City ACT 2601

Dear Sirs

I wish to make a submission to the Productivity Commission inquiry into the economic structure and performance of the Australian retail industry.

The Assistant Treasurer referred this issue to the Productivity Commission on 3 February 2011, in response to calls by major players in the retail sector for the government to impose the GST on direct imports of online purchases, out of concern for the loss of GST revenue for the Australian Government, but also to improve the relative competitiveness of the Australian retail sector (ie. "level the playing field").

I believe that the real motivation was not the loss of GST revenue for the Australian Government. But rather, an attempt to get government to introduce regulation which would

- make imported online purchases more expensive and thus narrow the gap between online pricing and Australian retail prices,
- add cost and complexity to the process of direct importing by consumers, and
- to discourage online sellers from supplying into the Australian market, on account of increased cost and added complexity.

Plain and simple - what the retail sector is asking for is **protection from competition**. In this situation the vehicle for protection would be the GST, which would serve the same function as tariffs in relation to the manufacturing sector.

### **Free Trade**

Australia has been pursuing free trade policies, with sector by sector tariff reductions and/or elimination, for the past 30 years or more.

If the Australian government was inclined to reverse any aspect of the drive towards trade liberalisation and re-introduce certain forms of protection, it should first consider the relative merits of which sectors of the Australian economy should have priority. That is, should the retail sector be the first priority for increased protection?, or should it be manufacturing or agriculture which have been more seriously impacted by globalisation over a longer period of time.

To date the retail sector has largely been shielded from the negative impacts of globalisation (ie. real competition). At the same time, major retail chains such as Harvey Norman, Myer, Woolworths, Wesfarmers (Coles), David Jones, JB HiFi, and

Solomon Lew's stable of brands under the Premier Group, etc, etc, have been at the forefront of taking advantage of globalisation, in sourcing cheaper and cheaper goods from off-shore, at the expense of, and ultimately the demise of much of Australia's manufacturing base.

On this basis alone, I believe that manufacturing and agriculture, which are actively discriminated against by the Australian retail sector in their own home market, are more in need and deserving of protection from overseas competition than the retail sector. Manufacturing and agriculture at least have the ability to export, and thus contribute to national income, and also support skilled labour in the Australian workforce – which the retail sector cannot.

### **Has Globalisation Delivered Expected Benefits to Consumers**

Given that the Australian retail sector has been a major beneficiary of globalisation, it is necessary to consider whether these benefits have been passed on to the Australian economy more broadly, and to Australian consumer in particular.

Free trade and tariff reduction was supposed to make all areas of the Australian economy world competitive, and ultimately deliver cheaper goods and services to Australian consumers. In this process Australian manufacturing has mostly moved off shore or been replaced by imports, and the Australian market for consumer goods is now dominated by imports from low cost manufacturing countries such as China.

Accordingly the outcome of the process of tariff reduction, international competitiveness, and globalisation should have delivered world competitive retail prices for Australia consumers.

However, this has not happened. In fact when it comes to retail, the outcome has been the opposite, and AUSTRALIA IS NOW ONE OF THE MOST EXPENSIVE PLACES IN THE WORLD TO SHOP.

### **Issues for the Productivity Commission to Consider**

It is obvious that the benefits of free trade and globalisation have not flowed through to Australia consumers.

**In view of this, I believe that the following two questions should be major issues considered in this inquiry:**

- **why is Australian retail the most expensive in the world, and**
- **why have free trade policies and tariff reductions/elimination failed to deliver benefits for Australia consumers, in the form of world competitive retail prices.**

Factors which should be examined would include:

#### *Gatekeepers for Australian Consumers*

This is one of the most important areas. Because Australia is physically isolated from the rest of the world, Australian retailers have until now largely had a captive market, and it has been virtually impossible for Australian consumers to bypass them.

Until the recent advent of internet shopping, and large scale (and cheap) overseas travel, consumers have had little choice but to buy from local retailers. The retailers have exploited this by maintaining price levels higher than the rest of the world, with consumers being mostly unaware of this.

In addition, Australian retailers have many inherent advantages against imports, which has enabled them to maintain their captive market – such as

- electrical connection (Australia's 3 pin plug)
- power supply - 240 volts v 110 volts in the USA
- PAL v NTSC for TVs, Video Cameras and Video Tapes
- Regional Coding – DVDs
- Left hand drive v Right hand drive – Motor Vehicles
- Incompatible sizing systems – labelling (clothing and footwear)
- No opportunity to physically examine the good or try before you buy
- Lack of warranty support
- Inconvenience and cost of returning faulty goods
- High freight costs on imported goods – on top of purchase price
- Impracticality - large items such as fridges and stoves

As gatekeepers, the retail sector has captured the benefits of globalisation for themselves, and have not shared these benefits with the Australian consumer.

#### *Cost of Manufacturing and Economies of Scale*

Many observers suggest that Australia is a small market and suppliers don't benefit from economies of scale. However, this is a misinterpretation of the concept of "Economies of Scale". Economies of scale relates to the manufacturing process (eg. cost of tooling a production line relative to the length of the production run – ie. the longer the production run, the cheaper the cost of manufacture). Most consumer goods sold in Australia come off the same production lines in China as the same products destined for the USA, European and Asian markets. Therefore, the economies of scale are the same, no matter whether these goods are sold in the USA or in Australia.

#### *Importing and Supply Chain Arrangements – Vertical Integration*

A lot of observers confuse economies of scale with buying power (buying in bulk, or the strength of your bargaining power).

There could be something in this as a reason for high wholesale prices. In fact it is probably true that major distributors are keeping wholesale prices high for smaller retailers. However, the larger retailers should have sufficient buying power to achieve lower wholesale prices, comparable with the USA and Europe – if they wanted to.

There is also a lot of vertical integration in the importing and distribution channel, which also helps the major retailers maintain control of their pricing, at levels favourable to them. It may not be to their advantage to have lower wholesale prices for the Australian market (because of issues such as transfer payments, taxation jurisdiction, etc)

### *Shopping Centre Rents*

It could be true that shopping centre rents are high in Australia compared to elsewhere. But even so, the national chain store tenants get more favourable terms than small retailers.

Surely the shopping centres (Westfield, etc.) can only maintain high rents like this if their major tenants were willing and could afford to pay them. There is probably a cosy arrangement here between the shopping centre landlords and their major tenants.

Further, Westfield is a major shopping centre owner in the USA and the UK. The relative rents charged in these markets should be examined to see if there is any substance to the claims that shopping centre rents in Australia are to blame for high retail prices here.

It should also be noted, that most of the big box retailers (such as Harvey Norman) are usually in their own premises, and not in shopping centres. In addition to this, with Harvey Norman's franchise model, the parent company (or associated company) is the property owner of the premises as well. So they can't blame themselves for the high rents that they have to pay to their own property management arm.

### *Loyalty to Australian Producers and Manufacturers*

Australian retailers have never been loyal to Australian manufacturers. I recently purchased an Everdure gas barbecue from Harvey Norman. When shopping for this I was surprised to find that it was made in China, and that an Australian made barbecue was almost impossible to find. Why does Australia import barbecues from China? Is it because it is a traditional Chinese cooking implement of which China has traditionally been a world leading manufacturer? – No. Was it because it was hi-tech which Australian industry does not have the skills to make? – No. Was it because the retailers/importers wanted to take advantage of lower labour costs than are available to Australian manufacturers? – Yes. Was it because Australian (or USA) manufacturers gave China their Intellectual Property, and taught them how to make barbecues for the Australian market? – Yes.

In other words, they get their barbecues made in China purely because of cost. If they were prepared to support Australian manufacturers, there might be some moral imperative to protect Australian retailers from “unfair” from cheap imports. But when they are prepared to drive Australian manufacturers out of business, and facilitate the offshoring of Australian manufacturing to China, purely because they can get it cheaper there, then they don't deserve any protection and Australian consumer should have the equal right to buy cheap imported goods on the internet. These practices do not support Australian jobs in manufacturing.

The Australian retailers are not against cheap imported goods from China per se. Their stores are full of it. It's just that they want consumers to have to buy it from them (the gatekeepers).

### *Discrimination Against Australian Consumers*

Retailers definitely discriminate against Australian consumers. Whilst bricks and mortar retailers often claim that we are not comparing like with like, and that their cost structures are different (higher), the way to examine this is where products can be

produced and delivered electronically – eg. computer software, and the entire contents of the Apple iTunes store.

The Sydney Morning Herald highlighted the discriminatory pricing against Australia consumers by Apple (iTunes Store), in its 21/2/2011 article *Apple using 'market power' to gouge Aussie iTunes users* (Attachment A).

There are also situations where multinational suppliers have written policies and strategies to force Australian consumers to buy from a local retailer, who sells at a price set by the supplier which is higher than the price set for same product in other markets. An example is cruising holidays. Certain USA cruise companies have what they call a “regional pricing policy” This means that the same cruise (in the USA or Europe) is sold to Australian customers through Australian travel agents at a higher price than through USA shopfront and online travel agents to American customers. If Australian customers book through a cheaper online agent in the USA, the shipping company threatens that they will not permit the person to board if they are not a resident of the USA. This is not a USA Government regulation. It is simply a commercial policy which discriminates against Australian consumers.

I have a preference for supporting the Australian travel agent anyway, but it is certainly unfair to Australian consumers, when the Australian agent can't offer the same deal as their USA counterparts, by virtue of company policy (see Attachment B – Regional Pricing)

#### *Slow to Pass on Benefits of Stronger Dollar*

Australian retailers have been profiteering by being slow to pass on the increases in the strengthening dollar in 2010 and 2011, in the form of lowering prices on imported products. I purchased a laptop computer at Christmas 2010, and I observed that there was no change in the retail price for this item in the 6 months leading up to my purchase, despite significant movements in the A\$ during that period.

This appears to be a widespread problem (Attachment C).

#### *The Internet – Knowledge is Power*

Retailers have been getting away with relatively high pricing for many years. The internet has now given consumers the tools to easily check on prices elsewhere, and parity between the \$A and the \$US has made any pricing disparity starkly obvious. The price gouging of the Australian consumer has finally been exposed and there has been a consumer backlash. You only have to see the deluge of blog comments on newspaper websites whenever they publish an item on this topic, to see how strongly people feel about it. This has put the retail sector under pressure and closer scrutiny, and they don't like it.

#### **Conclusion**

I believe the Productivity Commission should be examining why consumers have failed to materially benefit from globalisation, and why Australian retail prices are so high.

The retail sector has over a long period of time frustrated the free trade policies of Australian governments, by not allowing the benefits to flow through to the Australian economy and consumers.

I believe the retail sector (and maybe supply chain partners, and property managers) have deliberately kept prices high, and have captured the benefits of globalisation for themselves, at the expense of Australian consumers, and it was time something was done about this.

I believe that the GST should not be used as a de-facto trade barrier, and a form of protection for the Australian retail sector

Yours Faithfully

Chris Simpson

Attachments:

A: Sydney Morning Herald – 21 February 2011 – Apple using ‘market power’ to gouge Aussie iTunes users

B: Web Site – Vacations to Go – Restrictions on Australian customers from making bookings through USA based online agents, for certain cruise line companies.

C: Sydney Morning Herald - 15 October 2010 – Gadget buyers gouged as dollar soars.