

ARA SUBMISSION

ACCC SUPERMARKET INQUIRY INTERIM REPORT

OCTOBER 2024

The Australian Retailers Association (ARA) welcomes the opportunity to provide comments on the Australian Competition and Consumer Commission (ACCC) Interim Report into Supermarkets.

The ARA is the oldest, largest, and most diverse national retail body, representing a \$430 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.

The grocery sector forms a critical part of Australia's retail landscape

The sector services millions of consumers, providing essential products to households and employment for hundreds of thousands of employees. The supermarkets are among the largest private sector employers in the country. Ensuring that the sector continues to be competitive, efficient, and fair is crucial to supporting consumer welfare and the broader economy.

The sector has evolved considerably since the ACCC's 2008 supermarket inquiry, which deemed the sector "workably competitive." Now it is much more competitive, with the arrival and growth of three of the world's biggest and most competitive retailers - ALDI, Costco and Amazon - in Australia. International entrants have increased competition, benefiting consumers, while online shopping growth and extended trading hours have further enhanced convenience.

These advancements in the sector have been accompanied by rising business costs due to the pandemic, global conflicts, and natural disasters, which have contributed to higher prices for consumers.

In an environment marked by rising cost of living pressures, the grocery retail sector plays an important role in helping manage inflationary pressures by maintaining competitive prices and offering choice to consumers. The economies of scale which are a feature of the larger supermarkets, combined with the innovations of independent grocers, allow the sector to meet the diverse needs of Australian communities, across a vast geographic landscape.

The ARA supports the ACCC's recognition of the significant role supermarkets play in supporting and managing resilient and efficient supply chains, including through major natural disasters and other disruptions, negotiating fair terms with suppliers and providing value for consumers through competitive pricing.

We welcome the Interim Report's statement that while concentration in the sector exists, it is not indicative of a lack of competition. Instead, economies of scale enable major retailers to offer lower prices and a wider range of products, ultimately benefiting consumers. This is of particular benefit to those in remote and regional areas, where freight costs can be absorbed and offset by other locations due to this scale. We also highlight the crucial role of independent grocers in contributing to diversity and choice within the sector, despite the challenges they face in terms of scale and resources.

We believe there is a need for a regulatory framework that is proportionate and supports competition while avoiding excessive regulatory burdens on retailers. We agree with the importance of transparency in pricing and promotions, as demonstrated by the positive examples of consumer-friendly practices already implemented by most major retailers and a willingness on the part of the sector to boost wholesale price transparency, to inform on-farm decisions.

Market concentration does not equal a lack of competition

Australia's supermarket sector operates with four major players representing over 80% of the market. However, the ACCC has stated that a concentrated supermarket sector is not in itself determinative of a lack of competition, which we support. This market structure is not unique to the grocery sector in Australia, with similar market concentrations observed in sectors such as banking and telecommunications.

In markets with small populations like Australia, these structures can offer significant benefits, including economies of scale, which keep consumer prices low and ensure consistent product availability in diverse locations. While Coles and Woolworths together represent a large share of the market, as evidenced by the ACCC's own analysis, this does not suggest weak competition. The ACCC noted that supermarkets may achieve cost efficiencies through economies of scale, which can ultimately benefit consumers through lower prices. Furthermore, the discounting strategies employed by these chains indicate there is active competition between them, ensuring that consumers benefit from competitive pricing. This competition extends to ALDI and independent grocers, who also play significant roles in keeping pricing competitive.

The presence of ALDI in the market since 2001 has also introduced a competitive dynamic. While ALDI operates on a different model - offering a smaller, own brand product range at lower prices - its proximity to Coles and Woolworths stores ensures the two major players are incentivised to keep their prices competitive. The ACCC Interim Report found that more consumers are comparing prices and shopping around - some 70% of people are visiting 2-3 stores in a typical week - and cross-shopping. Many consumers shop at ALDI before shopping elsewhere. A key part of this is proximity to competition - for example, as a national average, there are three major competitors within 2km of a Woolworths supermarket.

Independent Supermarkets play an important role

Independent grocers, primarily those operating under the IGA banner, continue to play a significant role in the supermarket sector, especially in regional and rural areas. While they do not match the economies of scale of Coles, Woolworths, and ALDI, independent supermarkets provide localised offerings and a level of personal service that appeals to many consumers.

In Australia, there are ~2,440 stores operated by independent retailers - supported by Metcash, Drakes, Harris Farm and 7-Eleven stores - along with a wide variety of other independent supermarkets and convenience stores. Each competes vigorously for the same customers that would otherwise shop for competing items at major supermarkets.

As noted in the ACCC Interim Report, independent retailers face significant competitive challenges. Their higher operating costs, driven by the smaller scale of operations, often result in higher prices for consumers. Despite this, independent supermarkets remain critical, including in regional and remote communities, providing a diverse range of grocery products.

The ARA believes that supporting independent supermarkets is vital to maintaining diversity in the sector. Policies that reduce the regulatory burden on smaller retailers and encourage competition through incentives for regional businesses could help ensure their long-term viability.

Barriers to entry could be improved

While there are significant barriers to entry in the supermarket sector, including the complexity of supply chains and regulatory hurdles, these challenges are not unique to Australia. The capital-intensive nature of the supermarket business and the complexity of establishing supply chains make it difficult for new players to enter the market. Supermarkets also face extensive planning and regulatory approval processes, which can slow the development of new stores, as acknowledged by the Productivity Commission, and which points to the need for sensible, streamlined planning reform.

Investment in new stores

We note the ACCC has not yet formed a view on the merits of claims in relation to 'land banking' by supermarkets. There is no evidence to date of this practice occurring - that is the purchase of land by existing market players to block the entry or expansion of competitors and delaying its development.

Zoning restrictions, environmental approvals, and infrastructure constraints can significantly delay the development of land and the opening of new stores. These barriers not only affect new entrants but also limit the expansion of existing supermarket chains into new areas, particularly in urban centres where competition could drive down prices. When the planning process to develop a parcel of land can take between five to seven years, it exponentially increases the risk and cost to invest. Improving planning systems and delivering more flexibility in the zoning of land will create greater opportunities for more investment.

Low margins define the sector

Grocery retail is a high-volume, low-margin sector and Australia has one of the most efficient and competitive grocery sectors in the OECD. The major supermarkets make a reasonable but not excessive profit – which is consistently around 2 or 3 cents in the dollar - and much of that goes back to Australian households in the form of superannuation and dividends.

The profitability of Australian supermarkets is often misrepresented. The ACCC Interim Report highlights that Australian supermarkets achieve EBIT margins of around 5%, slightly higher than some international peers but on par with others like Walmart (USA) and Tesco (UK).

It is important to recognise that the regulatory and tax environment in Australia plays a significant role in determining profitability. For example, Coles and Woolworths report lower net profit margins compared to their international counterparts due to Australia's relatively high corporate tax rate, among other reasons. Woolworths, for example, paid \$1.35 billion in taxes in FY24 - the same amount they paid to shareholders in the form of dividends. The ABS data also shows that other industries such as mining, telecommunications, and real estate achieve far higher profitability levels compared to supermarkets' profit margins relative to total sales.

Further, Australian supermarkets operate in a highly competitive environment. The ACCC's acknowledgment that inflationary drivers, including global supply chain disruptions, geopolitical tensions, and rising interest rates, have influenced grocery price increases, provides a more balanced perspective on supermarket profitability.

Bargaining Power

The ARA acknowledges the ACCC's recognition of the bargaining power dynamics between supermarkets and large suppliers and supports the ACCC's further investigation into this area to understand how current dynamics impact consumer pricing and competition.

This dynamic allows for greater price negotiation, benefiting consumers by keeping prices in check. There is a real prospect that the proposed provisions in the Draft Code will lead to higher grocery prices due to the regulatory burden and the effect that penalties will have on buyers negotiating with large multinational companies.

Grocery Supply Chains and Supplier Relations

One of the key themes of the Inquiry has been in regard to retailers' relationship with suppliers. The four major supermarkets are foundation signatories to the current voluntary Food and Grocery Code and take seriously their commitment to comply with the Code and enter into good faith dealings with suppliers, seeking to be a long-term partner of choice for suppliers.

The ARA has supported the Code becoming mandatory, a consultation process which is underway, in which we and our members are actively participating. Our members have made public commitments to drive greater education of suppliers, particularly in the fruit and vegetable industry, of their rights under the Code, and to

participate in industry-wide solutions to provide greater wholesale price transparency to inform on-farm decisions.

The ARA asserts that the relationship between supermarkets and their suppliers is largely positive, and that the ACCC has found no substantial evidence to suggest widespread unfair treatment of suppliers. Coles, for example, reported a produce rejection rate of just 1.49% for the 2022-2023 financial year, indicating that most suppliers are meeting quality expectations.

The ARA acknowledges the concerns raised regarding power imbalances in these relationships, but recent reforms, including those related to unfair contract terms and payment times, have gone a long way to addressing these issues.

Supermarkets must maintain strong relationships with their suppliers to ensure a steady flow of fresh and high-quality products. The ARA believes the current system of weekly price negotiations benefits both parties, allowing flexibility for suppliers while ensuring supermarkets can provide competitive pricing to consumers.

Cross-Shopping demonstrates choice and market diversity

Consumers have become more price-conscious, often shopping at multiple stores to compare prices and maximize value. The ACCC acknowledges that more consumers are comparing prices and cross-shopping, with 70% visiting 2-3 stores in a typical week. This demonstrates that consumers are actively seeking the best value, indicating that the market remains competitive. Cross-shopping allows independent retailers to thrive by providing niche offerings that cater to local or specific demands that the larger chains may not meet.

This behavior drives competition across the entire sector, as all retailers - large or small - must work to retain consumer loyalty through competitive pricing, product quality, and range.

Loyalty Schemes provide additional value to customers

The ACCC found that most consumers do not perceive loyalty programs as having a significant impact on their choice of store or product selection. Nonetheless, supermarkets continue to invest in these schemes as a way to engage with their customers and offer additional value.

Moreover, Woolworths was identified as the only supermarket to provide transparency regarding promotions and unit pricing through its apps and websites, which enables consumers to make informed choices. This is a positive step toward greater transparency in the sector, and we encourage other supermarkets to adopt similar practices.

CONCLUSION

The supermarket sector plays a vital role in Australia's economy, offering affordable, high-quality products to consumers while supporting local suppliers and farmers. To ensure this sector remains competitive and continues to provide value, it is important that regulatory frameworks strike a careful balance between

promoting healthy competition and avoiding over-regulation, which could hinder innovation and raise costs for consumers.

The grocery sector is highly complex, influenced by factors such as geography, supply chain logistics, and unique regulatory requirements. Additionally, the industry faces multifaceted pressures, including rising costs of energy, labour, and logistics, which contribute to higher prices. Therefore, it is essential that any future regulatory oversight takes into account these intricate market dynamics and the role of global forces on pricing.

The ARA remains committed to collaborating with the ACCC and other stakeholders to foster a competitive, fair, and transparent grocery sector. We welcome further consultation and look forward to contributing to discussions that ensure the final report reflects the realities of the Australian retail landscape and helps create a sustainable future for both businesses and consumers.

Thank you for the opportunity to provide a submission to this inquiry. Any queries in relation to this submission can be directed to our policy team at policy@retail.org.au.