

ARA SUBMISSION

ACCC SUPERMARKET INQUIRY ISSUES PAPER

APRIL 2024

The Australian Retailers Association (ARA) welcomes the opportunity to provide comments on the Australian Competition and Consumer Commission (ACCC) Supermarkets Inquiry Issues Paper.

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.

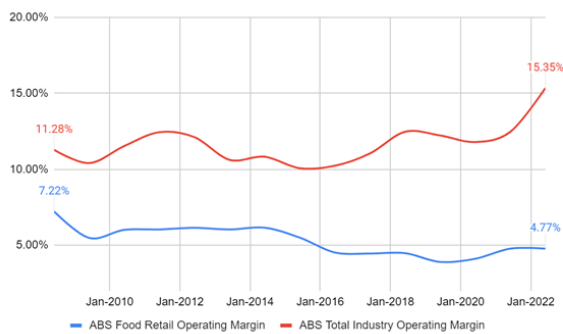
There are numerous inquiries across the country on - or involving - Australia’s largest supermarkets, including this review by the ACCC. We note the Terms of Reference outlined in the ACCC Issues Paper.

1. The structure of the markets for the supply of groceries by suppliers, wholesalers and retailers, including:
 - the level and nature of competition;
 - relationships between the parties;
 - the competitiveness of small and independent retailers, including in regional and remote areas; and
 - the impact of technological change, including the impact of the growth of online shopping.
2. The approach of suppliers, wholesalers and retailers to setting prices for groceries, including the use of data analytics in setting prices.

3. Factors affecting the price of inputs along the supply chain for groceries, including any impediments to the efficient availability or pricing of inputs along the supply chain.
4. Non-price aspects of competition in the markets for groceries, including the impact of:
 - loyalty programs; and
 - discounts offered by retailers for future purchases of groceries or other goods or services.

In response to the issues outlined by the ACCC in its paper, 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.

The ARA welcomes the opportunity to participate in the Inquiry. We believe that this Inquiry and others 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, reflective of global inflationary trends.

ARA RESPONSE TO ISSUES PAPER

Market structure

Provide feedback on

1. *Whether there is effective competition in the supply of groceries in Australia, and particularly between supermarkets.*
2. *Market structures for the retail supply of groceries in Australia.*

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:

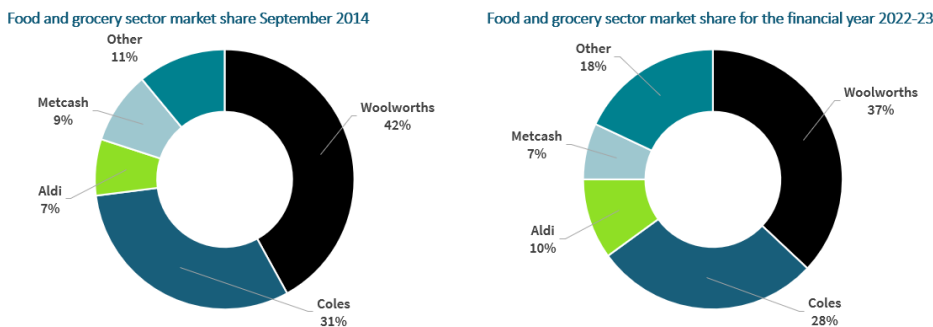
- Major supermarkets such as Woolworths, Coles, Aldi and Costco;
- Local and community supermarkets such as IGA, Spudshed and Drakes;
- Australian grocery chains like Harris Farm;

- 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.



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.

Price and non-price competition

Provide feedback on

- 3. The key areas of competition or differentiation between supermarkets in Australia.*
- 4. The practices supermarkets use to attract and retain consumers, and any changes observed over recent years (up to 10 years).*
- 5. How consumers respond to the supermarket market practices identified in your response to question 4*

Price remains a key driver of consumer choice, which drives intense competition between grocery retailers. Our members also engage in vigorous competition to attract and retain consumers through measures other than price. A summary of key areas of competition and differentiation include:

- **Price competition:** Competing on price remains a primary focus for our members. Promotional discounts and price matching are commonly used to offer competitive pricing and value to consumers.

- **Product range and quality:** Our members differentiate themselves by offering diverse product ranges encompassing various brands, quality tiers and specialty items. Emphasising high-quality products, including premium and organic options, helps attract consumers seeking superior value and experience.
- **Convenience and accessibility:** Convenient locations, extended opening hours and diverse shopping formats, including online and click-and-collect services, boost consumer accessibility and convenience. Supermarkets strive to meet evolving consumer habits and preferences by providing flexible options.
- **Loyalty and rewards programs:** Some of our members choose to invest in loyalty and rewards programs to provide further value to customers. A number of retailers - not just supermarkets - offer loyalty programs.
- **In-store experience:** Investing in store layout and amenities enhances the in-store shopping experience. Factors such as cleanliness, organisation, and staff friendliness contribute to overall customer satisfaction and loyalty. Both Woolworths and Coles offer a 'quiet hour' for customers with sensory needs.

Our members provide weekly specials on thousands of everyday products, as well as seasonal specials, product markdowns and festive sales during Christmas and Easter.

In August 2022, Coles locked the prices of 1,100 products for five months, setting a precedent for price stability. Subsequently, in October 2022, January 2023, and June 2023, Coles intensified its commitment by dropping and locking the prices of 150, 300, and 480 items, respectively.

Woolworths implemented a six-month price freeze on 200 grocery essentials in the lead up to Christmas 2022. This was complemented by the launch of four seasonal campaigns and a dedicated Christmas Prices Dropped initiative, all aimed at providing customers with value.

Our members' loyalty programs also provide customers with the opportunity to make further savings. Coles' Flybuys loyalty program helps customers to save money through individual offers, earning rewards on every eligible dollar they spend in supermarkets and by collecting points through our network of partners.

Woolworths' Everyday Rewards program offers customers points for every dollar they spend and the points can then be used toward \$10 off a future shop or converted to Qantas Frequent Flyer points.

The introduction of these comprehensive pricing initiatives reaffirms our members' dedication to ensuring that pricing practices align with consumer expectations and transparency standards in the retail sector.

Furthermore, investing in technology to boost pricing competition ultimately enhances customer experience, through the offering competitive rates while integrating seamless, user-friendly solutions that streamline interactions and elevate satisfaction levels.

Pricing and margins

Provide feedback on

- 6. The factors determining pricing for groceries, including policies and strategies for setting discounts and promotions.*
- 7. Whether supermarket prices, profits and margins have increased or are in excess of those likely in a competitive market*

Profit margins for Australian supermarkets are comparable with leading global grocery retailers in Canada, United States and United Kingdom. Like these markets, Australian supermarkets operate in highly competitive environments.

Over the past five years, our members have maintained a stable Net Profit After Tax (NPAT), demonstrating resilience amidst fluctuations in costs and prices and pointing firmly away from allegations of excessive or unreasonable profits.

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.

A profitable business allows our members to continually adjust their operations and strategies to keep up with consumer needs and expectations across a complex geography, parts of which are not attractive to hungry global new entrants for whom capital cities are the primary lower cost to serve targets. For supermarkets, sustainable profits have underpinned significant investments in new distribution centres, which are key to boosting supply chain resilience and food security across Australia.

The global economic landscape has experienced a dramatic shift, resulting in customers prioritising value, to address concerns about living costs. Increasing expenses, from mortgage and rental payments to higher electricity and fuel prices, are exerting pressure on household budgets. Although our members cannot directly influence these mounting costs, they actively contribute to supporting Australian families by delivering value across their product range.

It is unsurprising that, given the transparency and discretionary nature of spend on groceries, the focus in the cost-of-living crisis has disproportionately turned to grocery prices, rather than comparatively larger buckets of household spend where transparency is low and switching inertia is high. Utilities, housing costs, finance and health and wellbeing spend has been hit by inflation, causing customers to notice the reduction in their grocery spend. The connection between the rising costs across all major household spend categories is however often lost in the public discourse.

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.

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.

Profits are primarily used to either invest in improving the customer experience of their members, or to pay dividends to shareholders, the overwhelming majority of whom are mums, dads, families and retirees or superannuation or other funds of which those Australians are beneficiaries.

In contrast to international markets, our members maintain consistent retail prices across both physical and digital platforms. This commitment to price parity ensures that customers can access the same competitive prices whether they choose to shop in-store or online. By providing this consistency, customers have the convenience of comparing prices and making informed purchasing decisions before or during their shopping experience.

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.

Industry Trends

Provide feedback on

- 8. The role of supermarket loyalty and rewards programs and how they affect competition.*
- 9. The role of data and data analytics in how supermarkets compete.*
- 10. How online retailing has impacted competition between supermarkets.*
- 11. The role of home brands in how supermarkets compete.*

Loyalty programs

ARA recognises the significant role that supermarket loyalty and rewards programs play in further fostering competition and enhancing consumer engagement within the grocery retail sector. Woolworths and Coles, have pioneered loyalty programs such as Woolworths Rewards and Flybuys, respectively. These programs offer customers various incentives, including discounts, personalised offers and points accumulation for future purchases.

Loyalty schemes are typically issued at limited cost (if any) to customers. They are voluntary, opt-in, have no barriers to exit, and are, by their very nature, designed to tailor and enhance a member's shopping experience. Loyalty programs are not exclusive to supermarkets; they are prevalent across various retail sectors, including airlines, food hospitality, clothing stores and beauty salons.

These programs contribute to customer loyalty, allowing businesses to put downward pressure on the prices of goods through increased sales volume. Loyalty programs are easy to establish and there are hundreds of loyalty programs operating across Australia. There are also many grocery retailers who choose not to invest in customer loyalty schemes and choose to invest elsewhere to increase customer engagement, e.g. ALDI.

Online retailing

The rise of online retailing has significantly impacted competition in the grocery sector, with Woolworths and Coles expanding their digital footprint to cater to evolving consumer preferences and, most importantly, customer convenience. Supermarkets have invested heavily in their online platforms and distribution centres, offering convenient shopping experiences, flexible delivery options and digital loyalty programs to attract and retain customers and to ensure stability of critical infrastructure and food security across the nation.

The entry of global e-commerce giants like Amazon into the Australian market has intensified competition and spurred innovation in the grocery retail sector. Since 2011, Amazon has invested more than AUD \$15 billion in Australia across all businesses in Australia. Amazon Australia continues to expand its Australian workforce with more than 7,000 employees nationwide.

Home brand products

The ARA understands consumers are looking for great value on everyday essentials and our members seek to provide low pricing on the products they sell.

Globally, retailer private labels have continued to evolve from being a low-spec and cheap alternative to proprietary brands, to becoming multi-faceted strategic differentiators with more sophisticated offers.

Responding to cost-of-living pressures, to support the consumers search for value and affordability both members have launched their own and exclusive brands for essential items. Home brand products can retail at an average price of less than 10%-40% below the branded equivalents.

Home brand products are popular and their appeal has risen as cost-of-living pressures have increased. They provide consumers with more choice and value to suit their needs.

Barriers to entry and expansion

Provide feedback on

12. *The factors relevant to decisions on whether to enter or expand in Australia, including any barriers.*
13. *Examples of supermarket entry, exit or expansion (particularly in the last 10 years), including the reasons for the success or otherwise of new entry or expansion and the reasons for exit.*
14. *Whether you foresee any new supermarket entry or expansion in the next 5 years.*

In 2003 Australia was ranked fourth for competitiveness but has since dropped to 19th as more and more red tape and complexity to the cost of doing business.

Opportunities to reduce barriers to business formation, outlined below:

- **Cost of doing business.** The current economic climate may pose more barriers to new business formation, with inflation resulting in higher interest rates on business loans, higher rent, higher wages, and higher wholesale prices. If inflation is not managed, the impacts could include a slowdown in business formation, an acceleration in business closures, and further market concentration. Other factors are the cost of fuel, freight and tax.
- **Labour market constraints.** The current labour shortage is well-documented. These workforce pressures are impacting all retailers, large and small, and pose a risk to the ongoing resilience of the retail sector.

The following barriers also exist at the state level:

- **Payroll tax.** The existence of this tax acts as a disincentive of increasing employment and creates unnecessary complexity for those retailers operating across state borders. This is exacerbated by state-based mental health levies in Victoria and Queensland that are applied in addition to payroll tax. Payroll tax reform in Australia is essential for fostering greater competition within the supermarket sector and promoting economic growth. By reforming payroll tax laws to alleviate the financial burden on businesses.
- **Commercial leasing.** When a business becomes unviable, the ARA believes that tenants should be able to break their lease to allow a new entrant to take their place. However, standard commercial leases do not generally allow this.

Over the past decade, there have been notable instances of supermarket entry, exit, or expansion in Australia, each with its own set of challenges and outcomes. For example, the entry of discount supermarket chains like Aldi, Costco and Amazon has disrupted the market and intensified competition, prompting existing operators to adjust their pricing and marketing strategies.

Success in supermarket entry or expansion often hinges on factors such as location strategy, product differentiation, and operational efficiency. Supermarkets that offer unique value propositions, such as specialty organic or gourmet products, may carve out niche markets and achieve sustainable growth. Conversely, ventures into overcrowded market segments or regions with limited consumer demand may result in failure or underperformance.

Awareness of other non-traditional grocery retailers which have successfully and rapidly expanded into the competition for winning share of Australian consumers' wallet is also essential. More than ever customers are

turning to retailers such as Chemist Warehouse, Bunnings, discount department stores such as The Reject Shop, and speciality food and non-food online retailers for all or parts of all their grocery shop. In addition, navigation of the complex Australian regulatory environment is vital to competing successfully in Australian grocery retail.

Looking ahead, the prospect of new supermarket entry or expansion in the next five years is contingent on various market dynamics, including consumer preferences, economic conditions, and reduced regulation. Innovative business models and evolving consumer trends may create opportunities for new entrants.

Regulatory hurdles can deter investment and innovation, limiting the entry of new competitors and stifling market dynamism. Additionally, factors such as navigating complex planning and zoning regulations further compound the challenges faced by aspiring entrants.

By addressing regulatory burdens and streamlining approval processes, policymakers can create a more conducive environment for supermarket expansion, encouraging new players to enter the market and ultimately benefiting consumers through increased choice, lower prices, and improved service quality.

ARA anticipates potential new supermarket entry or expansion in the coming years, driven by evolving consumer preferences, technological advancements and changing market dynamics – particularly in the online space and farmer markets. The rise of e-commerce and omni-channel retailing may incentivise online-based supermarket startups to enter the market and disrupt traditional brick-and-mortar incumbents.

Additionally, demographic shifts, such as population growth in urban centres and changing lifestyle trends, may create demand for new supermarket formats catering to specific consumer segments.

However, regulatory hurdles, including land-use restrictions, zoning laws and planning regulations, may pose challenges for aspiring supermarket operators seeking to establish physical retail locations. Overall, while the supermarket sector remains dynamic and ripe for innovation, overcoming barriers to entry and achieving sustainable growth will require strategic planning, operational excellence and a deep understanding of changing consumer needs and preferences.

Customer experience and convenience

Provide feedback on

15. The experiences of consumers in their dealings with supermarkets.

Our members are investing in cutting-edge technology to elevate customer convenience and team safety.

The digital era has seen a significant increase in online shopping, with demand for express delivery options like same-day and on-demand, within the hour. Responding to this trend, Woolworths made changes to the Woolworths and Everyday Rewards apps and websites to make it easier for customers to shop online, and collect their groceries direct to boot, including in remote and regional areas.

Since 2018, Coles has been working with international technology firms Witron and Ocado to deliver advanced distribution centres in their supply chain network and in support of their online delivery business to build speed

and efficiency in their operations, and enhancing customer experience with better availability, selection and convenience.

Both members have experienced elevated levels of organised retail crime and customer aggression in their stores. In response they have invested in technology to help manage these risks to the team members, customers, and operations. They have also invested deeply in mental health and wellbeing for their teams.

Additionally, there has been an increased security presence in stores along with new body worn cameras being rolled out to ensure staff are safe as we have seen a rise in aggressive behaviour from some customers.

Australian supermarkets operate within a comprehensive and complex regulatory landscape that spans food safety, workplace health and safety, industrial relations, and interactions with suppliers and customers.

The Australian competition and consumer regulatory framework, which in many respects is seen as world leading, includes pioneering measures like the Food and Grocery Code of Conduct and the Unit Pricing Code, which sets Australia ahead of international jurisdictions. Other international jurisdictions are now looking to implement some of the interventions to improve competition following the ACCC Grocery Inquiry in 2008.

The Code governs relationships between signatories and suppliers, with our members being inaugural supermarket signatories in 2015, showcasing a steadfast commitment to equitable good faith practices.

Enforced by the ACCC, Coles, Aldi, Woolworths and Metcash are legally bound by the Code of conduct to the benefit of large global and smaller Australian suppliers alike. The Code is scheduled to sunset on 1 April 2025. Prior to sunsetting, a review of the Code is required to determine whether it remains fit for purpose.

Competition along grocery supply chains

Provide feedback on

16. *The structure of the grocery supply chain(s) and market(s) you operate in, including:
 - (a) *an overview of each step in the supply chain(s)*
 - (b) *your role in the supply chain(s) or industry.**
17. *The nature and extent of competition at each level of the grocery supply chain(s) in which you operate*
18. *How vertical integration across retail and wholesale levels of the supply chain(s) by the major supermarkets affects competition.*
19. *How these market dynamics have changed over the past 5 to 10 years.*

Competition within the grocery supply chain is multifaceted and occurs at various levels beyond the retail sector. At the distribution and wholesale levels, competition revolves around factors such as pricing, product availability, and service quality. Suppliers and distributors compete vie for contracts with manufacturers and producers, striving to offer competitive terms and efficient logistics solutions.

Additionally, competition exists among logistics providers and transportation companies, each seeking to secure contracts for the transportation of goods. Overall, competition at these levels is driven by the quest for efficiency, reliability, and cost-effectiveness in fulfilling the demands of retailers and consumers.

The efficacy of supply chain competition is intricately linked to the state of infrastructure and external factors that influence logistics operations. Inadequate government investment in road, rail, and port infrastructure has emerged as a significant barrier to supply chain efficiency. The COVID-19 pandemic and increasing natural disaster events highlight the need for more investment in supply chain infrastructure resilience.

Insufficient funding and delayed infrastructure projects restrict the smooth flow of goods, leading to bottlenecks and delays along transportation routes. Of particular concern is the removal of key supply chain projects from the Infrastructure Australia priority list such as the Great Western Highway, the Truro Bypass project and the reduction or 'slow down' of the Inland Rail project, which has 13 stages attached to it.

The rising cost of fuel has added another layer of complexity to supply chain competition. Fluctuations in fuel prices directly impact transportation costs, affecting the overall cost structure of supply chain operations. These cost pressures can squeeze profit margins for businesses operating within the supply chain, potentially leading to price hikes for consumers.

In addition to infrastructure and fuel costs, geopolitical issues and industrial disputes pose significant challenges to supply chain competition. Political tensions, trade disputes and regulatory changes can disrupt global supply chains, leading to supply shortages, increased lead times and heightened uncertainty for businesses. Similarly, industrial disputes, such as strikes or labour unrest, can halt operations at key distribution hubs or ports, causing disruptions that reverberate throughout the supply chain.

Addressing these challenges requires a concerted effort from governments partnering with industry over a multi-year horizon.

Trading terms and practices

Provide feedback on

20. *Contracting practices and dynamics.*
21. *How these contracting dynamics and terms vary between different buyers and sellers you contract with.*
22. *For suppliers who have direct contractual relationships with retailers, or wholesalers representing retailers:*
 - (a) *The nature and types of rebate arrangements.*
 - (b) *any provision in relation to self-placement or promotional activity. .*
23. *How these contracting practices have changed over the past 5 to 10 years.*
24. *Other trading arrangements, practices and dynamics.*
25. *How these arrangements vary between different buyers and sellers you deal with.*
26. *Whether formalised supply contracts or some other form of supply arrangement would be preferable and why.*
27. *How these trading arrangements have changed over the past 5 to 10 years.*

Our members are best placed to provide feedback about their respective trading terms with suppliers.

Generally speaking though, 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, labour, 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 the Hon Dr Craig Emerson MP has been appointed to undertake this review of the Code, supported by a secretariat within Treasury. The review will assess:

- the effectiveness of the Code provisions in achieving the purpose of the Code to improve the commercial relationship between retailers, wholesalers and suppliers in the grocery sector, and
- the need for the Code, including whether it should be remade, amended or repealed.

Our members look forward to participating and contributing to this review. As proud founding signatories bound by the Code, Coles and Woolworths offer multiple avenues for dispute resolution, empowering suppliers to seek resolution directly, engage a Code Arbiter, request Independent Reviewer intervention, opt for mediation or arbitration, or seek independent legal advice.

The 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, complaints resolved by an independent arbiter, and a culture of fair dealings between our members and suppliers.

Buyer power

Provide feedback on

28. How any buyer power is or might be exercised and the consequences.

29. Any evidence or examples of buyer power.

30. The extent to which larger supermarkets and wholesalers are able to acquire grocery products from suppliers for lower prices or on better terms than smaller grocery retailers and wholesalers.

- 31. Any evidence or examples of buyer power being exercised in a manner which impedes or may impede the efficient supply of grocery products.
- 32. The extent and impact of any countervailing negotiating power.

Where 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.

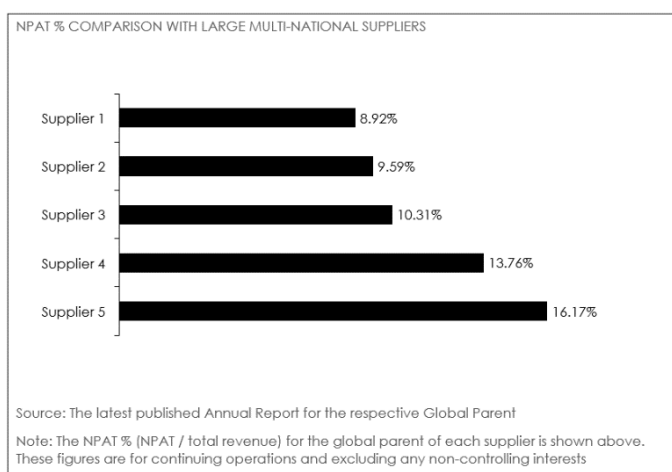
Our members confront a unique challenge as they navigate strategic decisions involved in managing cost pressures from global food suppliers. Some of these suppliers are much larger than Woolworths and Coles and over the past two years have requested significant cost increases well above headline inflation.

The key reason provided by suppliers to support these requests was that they had incurred cost increases in relation to the following items: labour, wheat, packaging, utilities, freight and international shipping.

Most of what consumers pay at the checkout goes to a supplier and, in the Australian context, a significant portion of these supplier payments go to multinational food companies. We therefore welcome an examination of the role that these large, global food suppliers play in applying inflationary pressure to grocery prices.

We note regulators in other markets are increasingly turning their minds to these supply chain issues. In November 2023, the UK's Competition and Markets Authority (CMA) published findings from an in-depth study of supplier margins across a range of essential product categories. The CMA found that over the last two years, around three-quarters of branded suppliers had increased their unit profitability and, in doing so, contributed to higher food price inflation.

This higher unit profitability flows through to higher NPAT for these suppliers, who enjoy higher profit margins than Australian supermarkets. The chart below illustrates the NPAT for five multinational food companies supplying to Australian supermarkets. These higher supply chain profit margins are included in prices paid by Australian consumers.



Margin and price transparency

Provide feedback on

33. *How cost changes along grocery supply chains are reflected in retail prices, and how this has changed over the past 5 to 10 years.*
34. *The key factors influencing profitability and margins at each level of the supply chain and how these have changed over the past 5 to 10 years.*

The ARA acknowledges the complex interplay of factors influencing cost changes along grocery supply chains and their reflection in retail prices. Over the past 5 to 10 years, the landscape of supply chain dynamics has been impacted by various factors, including natural disasters, regulatory changes, and technological advancements. In particular, natural disasters such as bushfires, floods, and droughts have disrupted agricultural production, transportation networks, and supply chain operations, leading to fluctuations in input costs and supply chain disruptions.

Within the supply chain, the pricing structure varies across different stages, encompassing elements such as price per unit, mark-up percentages, and volume-based discounts. Pricing decisions are influenced by a combination of factors, including fixed-price models, variable pricing strategies based on market demand and competitor pricing, and margin-based approaches.

The final retail price is influenced by various factors at different levels of the supply chain, with retailers often absorbing a significant proportion of the cost. This includes costs related to procurement, transportation, wages, tax, suppliers, storage, marketing, and overhead expenses.

Other factors

Provide feedback on

35. *Your ability to respond to shocks or changes in the operating environment.*
36. *Any impediments to undertaking investment necessary to support your business, for example capital expenditure to support the improvement or expansion of your business.*
37. *Any other impediments to the efficient operation of your business.*
38. *Any factors that have improved the efficiency of your business operations.*
39. *How the extent, and types, of impediments to efficient supply or improvise to the efficacy of business operations have changed over the past 5 to 10 years.*

Ability to respond to shocks or changes

Our members navigate dynamic operating environments and respond swiftly to unexpected shocks or changes. The COVID-19 pandemic, extreme weather events like the Lismore or Coober Pedy floods, have highlighted the need for agility and resilience in the face of disruption.

Given the scale of our members, they work effectively with government entities to ensure the smooth movement of goods across the country. For instance, in South Australia, our members collaborated closely with the Department of Infrastructure and Transport to expedite the construction of a makeshift road to facilitate the delivery of essential goods into Coober Pedy after floods damaged parts of the Sturt Highway.

Our members have demonstrated their ability to adapt by implementing enhanced safety protocols, adjusting supply chain logistics and pivoting towards online and contactless shopping solutions to meet evolving consumer needs.

Impediments to investment

Despite the importance of investment in improving and expanding business operations, our members face impediments such as regulatory complexities. Regulatory burdens and compliance requirements may deter investment in innovation and expansion projects, hindering the ability to enhance operational efficiency and competitiveness.

Recent findings from the IMD World Competitiveness Yearbook 2022 reveal concerning trends regarding Australia's competitiveness on the global stage. In 2004, Australia held fourth position for competitiveness, but it has since slipped to 19th place. The latest results indicate a further decline, with Australia now ranked 61st out of 63 countries in entrepreneurship and dropping from 20th to 41st place in workplace productivity.

According to Melinda Cilento, CEO of the Committee for Economic Development of Australia (CEDA):

“Australia’s terms of trade driven by strong commodity prices, employment numbers and pandemic recovery have saved the day – ensuring our international competitiveness ranking improved and did not slip further,” says.

“However, it is clear when compared against the top performing countries, that long-term and well-known weaknesses in the policy environment are holding Australia back.

“Australia’s future competitiveness is not assured without lifting our game on areas such as technology, energy, skills and training, entrepreneurship, tax and productivity.”

The report highlighted that only three percent of executives surveyed said that Australia was cost competitive and five per cent believed Australia had a competitive tax regime.

The three most important trends considered to be impacting businesses in 2022 as ranked by executives were inflationary pressures, geopolitical conflicts and supply chain bottlenecks.

While the ARA acknowledges it is not the role of the ACCC in influencing policy changes related to these key issues, it is important to acknowledge the impact of these broader issues on Australian investment (and resulting competition in the sector) and to advocate for meaningful reforms to enhance Australia's competitiveness, ultimately to the benefit of Australian consumers.

Other operational impediments

The operational challenges faced by supermarkets in Australia are compounded by the geographical breadth of the country, which presents unique logistical difficulties compared to smaller, more densely populated nations.

Major Supermarkets play a critical role in ensuring consistent supply chains that reach even the most isolated communities.

However, navigating Australia's expansive geography poses significant challenges, including long transportation distances and complex distribution networks. To put this into perspective, Australia's land area is roughly comparable to that of the United States, yet its population is significantly smaller, resulting in a dispersed consumer base and higher transportation costs per capita.

Despite these challenges, supermarkets demonstrate resilience by continually adapting their operations to overcome logistical hurdles and ensure the efficient delivery of goods nationwide. This highlights the importance of ongoing government investment in the infrastructure necessary to enhance the nation's supply chain.

Factors improving efficiency

Australian supermarkets are viewed by many analysts as among the most efficient in the world. Supermarkets have implemented strategies to enhance operational efficiency, including investments in technology and data analytics, adoption of just-in-time operations and optimisation of supply chain logistics and customer service. Using technology and data analytics enables supermarkets to forecast customer demand, optimise inventory levels, and personalise customer experiences, to ensure their offers best meet customers' ever-changing demands.

This has also not only increased jobs in the industry, but transformed them. Strategic collaborations with suppliers and partners facilitate streamlined operations and value chain integration, contributing to efficiency improvements, ultimately to the benefit of the customer offer.

Changes over time

Over the past 5 to 10 years, supermarkets have experienced shifts in the nature and extent of impediments to efficient supply and pricing. Technological advancements and demographic changes have reshaped consumer preferences and market dynamics, driving supermarkets to adapt their strategies accordingly. While challenges such as supply chain disruptions and regulatory constraints persist, supermarkets have embraced innovation and collaboration to mitigate these impediments and maintain operational effectiveness.

CONCLUSION

The Australian grocery sector is complex and any analysis of this sector requires an understanding of the unique geographic, supply chain and regulatory factors in Australia 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 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.