
CHAPTER 2

THE RETAILING SECTOR

...we have a long history and we have learnt from that history, and we have certainly learnt from past experiences.¹

Overview

2.1 The retailing sector provides a vast array of products to consumers through a wide range of outlets. Table 2.1 and Figure 2.1 show the sizes of the various sectors of retailing. The figures do not include petrol retailing and retail sales of vehicles and accessories. Figure 2.2 shows the breakdown of total food retailing.

Table 2.1

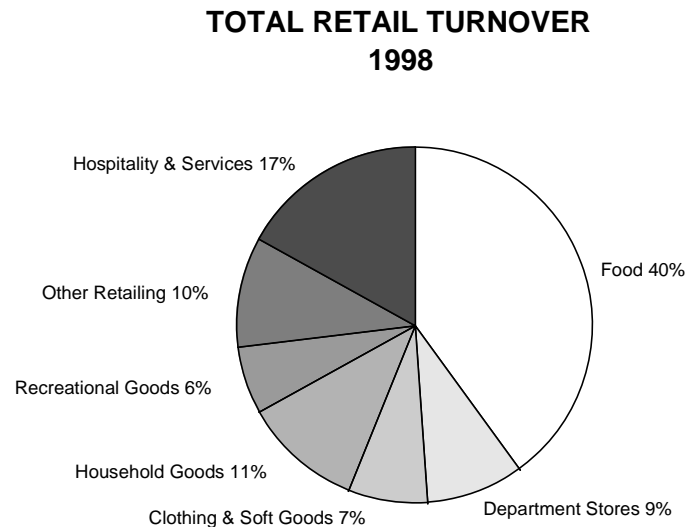
Total Retail Turnover 1998

Category	Monthly Turnover (\$m)	Per Cent of Total
Supermarkets & grocery stores	3275.5	27.44
Takeaway food	583.6	4.89
Other food	848.8	7.11
Total food	4707.9	39.44
Department stores	1150.2	9.64
Clothing & soft goods	805.4	6.75
Household goods (furniture, domestic hardware, appliances recorded music, etc)	1266.9	10.61
Recreational goods (newspapers, books, sports equipment, toys, games, etc)	692.4	5.80
Other (pharmaceutical, jewellery, garden supplies, etc)	1247.7	10.45
Hospitality & services (hotels, clubs, pubs, cafes and restaurants, etc, hairdressing, video hire)	2066.4	17.31
Total - non-food	7229	60.56
Total	11936.9	100

Source: ABS, Retail Trade Catalogue No. 8501.0, November 1998.

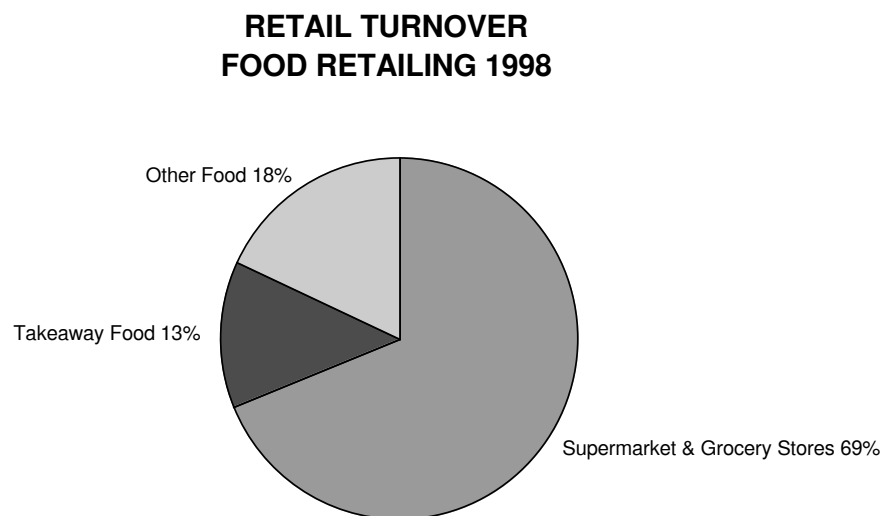
1 Mr Alan Williams, Managing Director, Coles Supermarkets, *Hansard*, Canberra, 6 April 1999, p 30.

Figure 2.1



Source: Franklins, Submission 200, p 4.1.

Figure 2.2



Source: Franklins, Submission 200, p 4.2.

2.2 While the Committee's terms of reference refer to the retailing sector in general, an overwhelming majority of submissions focused on industry concentration in the supermarket and grocery sector.

Grocery retailing

Brief history

2.3 Up to the 1940s, most grocery stores were independently owned. As suburbs developed around Australian cities, many consumers came to rely on shops that took orders and delivered to the home via a cart. Suburban houses did not have any advanced means of refrigeration, hence perishable items like milk, ice and bread were delivered daily. Experimentation with different retailing formats in the 1920s was stifled by the Depression and stagnating incomes in the 1930s, then by World War II.

2.4 In 1949 the food departments of many department stores began to convert to self-service, with the first fully self-service grocery store opening in Sydney in 1950.² Australia's rapid urban growth during the 1950s and 1960s led to these self-service supermarkets emerging as the new shopping format.

2.5 Most supermarkets were individually owned and managed or owned by small local groups, and carried a wide range of groceries and cleaning products. The introduction of large refrigeration units brought an increased range of milk, cheese, dairy and 'deli' products – although clothing and liquor had not yet been introduced.³

2.6 Woolworths and Coles already had chains of variety stores with central State-based warehouses. They each acquired small and innovative supermarket chains such as BCC in Brisbane and Flemings in Sydney, and converted many of their variety stores to a grocery and variety format. They created the first house brands in order to gain sufficient volumes of product for advertising and promotion, and focused on undercutting leading brands. Such home brands included 'Pick of the Crop' for peas and 'Flavour Joy' for cheese.⁴

2.7 By the end of the 1960s, Woolworths and Coles bought out their franchisee butchers and implemented sophisticated food processing techniques. They also built their own meat distribution facilities and began to invest in integrated supply chains through long-term contracts with suppliers.⁵

2.8 In the 1970s and 1980s, higher levels of inflation led consumers to focus more on price. Supermarkets reacted by keeping service to a minimum, narrowing aisles in order to reduce floor space rentals, and by dimming the lighting to cut electricity bills.⁶

2 Coles, Submission 168, Part 2, pp 8-13.

3 Franklins, Submission 200, p 3.1.

4 Franklins, Submission 200, p 3.1.

5 Franklins, Submission 200, p 3.2.

6 Franklins, Submission 200, pp 3.2-3.3.

2.9 Discounters Franklins became popular in NSW; Bi-Lo in South Australia; Shoeys in Victoria and Jack the Slasher in Queensland. These discounters drew market share from both Woolworths and Coles.⁷

2.10 A distinct consumer group with smaller shopping baskets emerged in the 1980s. Convenience stores became popular – despite their higher prices and limited range – with stores such as 7-Eleven opening for longer hours and positioning themselves close to main roads. Food Plus stores attached to petrol stations sold confectionary, soft drink, partly prepared meals and fast food items. State and Territory laws concerning trading hours hampered the ability of supermarkets to compete for this custom. As a result, convenience stores further reduced the market shares of Woolworths and Coles.⁸ They responded by purchasing discount chains such as Jack the Slasher, Shoeys and Bi-Lo, and began renovating their stores. Woolworths and Coles then set out to improve the quality of their fruit and vegetables (which had been introduced into the larger stores in the early 1960s)⁹ and invested heavily in technology and systems to improve efficiency.¹⁰

2.11 In order to compete with the ‘big two’, Franklins and the independent sector needed greater scale to keep their prices down. During the 1980s, Franklins expanded into Queensland, South Australia and Victoria. Davids, the major wholesaler to the independent retailers, began to merge with other independent wholesalers. Meanwhile, the range of items on supermarket shelves continued to expand into areas such as health and beauty products.¹¹

2.12 The 1980s also saw the introduction of electronic aids to selling. Front-end scanning originally appeared in an independent grocery store in Victoria in 1980. This was adopted by Coles in 1982, and by other chains during the next two years.

2.13 The use of barcodes and scanners has significantly improved efficiency across the board, linking suppliers to warehouses and ultimately, to the consumer. Barcoding allows thousands of individual items to be monitored and re-ordered after purchase.¹²

2.14 Large supermarkets continue to expand their products and services into such areas as health, magazines, pre-prepared meals and banking facilities. Coles was the first to install EFTPOS, and now has this service available at all its 6,000 checkouts. Customers now withdraw around \$2 billion in cash per year.¹³ The ability to use credit cards and the introduction of retail incentive schemes such as ‘fly buys’ adds a further dimension to shopping convenience, hence the term ‘one-stop-shopping’.

7 Franklins, Submission 200, p 3.3.

8 Franklins, Submission 200, p 3.3.

9 Coles, Submission 168, Part 3, p 15.

10 Franklins, Submission 200, p 3.4.

11 Franklins, Submission 200, p 3.4.

12 Coles, Submission 168, Part 3, p 19 and pp 41-42.

13 Coles, Submission 168, Part 3, p 42.

2.15 The major chains are now experimenting with Internet shopping, which may spur an increase in the number of consumers ordering goods and having them delivered to the home. Future developments include the provision of full banking services and expansion into retail petrol outlets (see Chapter 8).

Present day market structure

2.16 The Australian grocery retailing industry is oligopolistic in nature. That is, the market structure is characterised by a small number of firms, each of which possesses a significant degree of economic influence or market power. Those firms, Woolworths, Coles and Franklins, are commonly known as the major chains. They are wholly owned, but may consist of a number of retail ‘shopfronts’ or store brand names (see para 2.18 – 2.24). Consumers also see franchise chains or banner groups such as Foodland or IGA, as major chains.

2.17 The three major chains deal direct with suppliers, whereas the independents are generally supplied by a wholesaler. The vertically integrated structure of the major chains is geared towards highly efficient distribution systems, with new technologies enabling product to flow smoothly from the supply or production stage through to the final consumer. Independent retailers and wholesalers are not vertically integrated as such, but nevertheless rely on linkage systems for ordering and distribution. Figure 2.3 indicates the extra profit points within the independent sector with respect to the major chains.

Figure 2.3

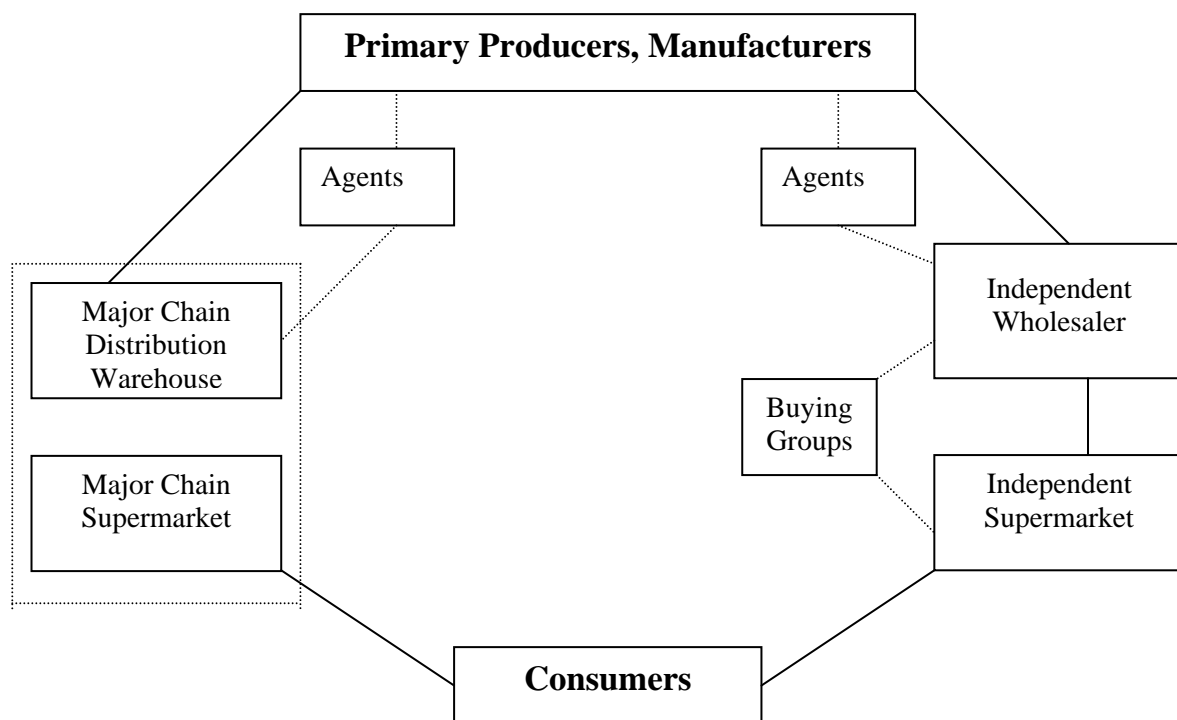
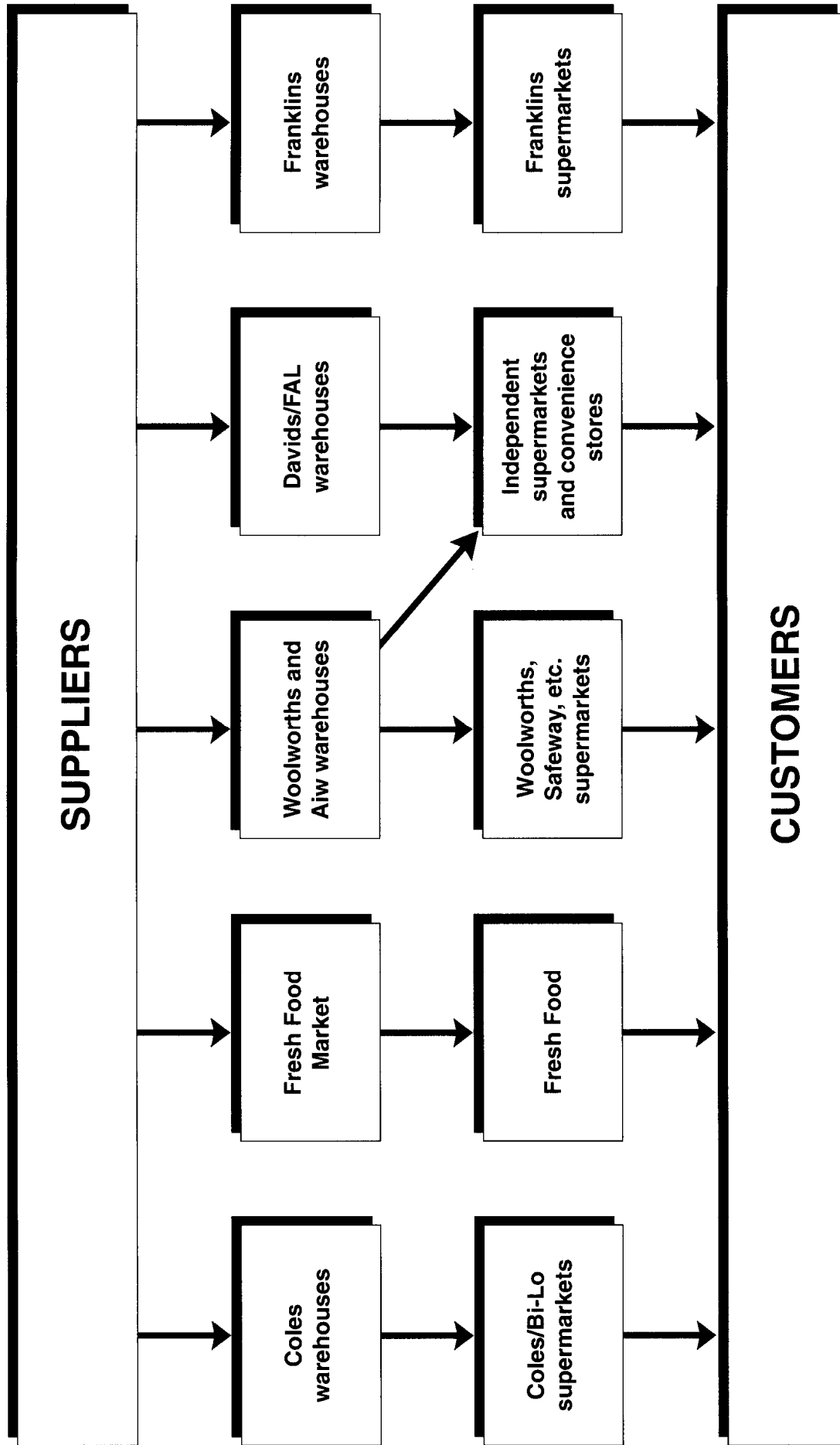


Figure 2.4 Wholesaling and retailing markets for the sale of groceries, fresh products and liquor



Source: Franklins. Submission, p 4.4

The major chains

Woolworths

2.18 Woolworths is Australia's largest grocery retailer and the second largest private sector employer with 1,460 Australia-wide stores staffed by over 110,000 employees. Its supermarkets account for over 81,000 of its employees. Woolworths is also involved in general merchandising through various discount stores. Its retail brands include Woolworths Supermarkets, Safeway, Purity, Big W, Woolworths Variety, Woolworths Metro, Crazy Prices, Rockmans, Dick Smith Electronics and Plus Petrol. Non-retail entities include Australian Independent Wholesalers (AIW) and Chisholm Manufacturing.¹⁴ In addition to servicing Woolworths retail stores, AIW supplies independent retailers in competition with Davids (see para 2.35 – 2.36 below).

2.19 Woolworths is Australian-owned with over 91 per cent being ordinary Australian shareholders. It has no connection with similarly named overseas groups.¹⁵

Coles

2.20 Coles, along with Bi-Lo, forms the grocery division of Coles Myer, which is Australia's largest private sector employer with 150,000 staff. Coles has 410 stores and employs 53,500, whereas Bi-Lo employs 11,795 people in its 156 stores.¹⁶ Coles Myer is a market participant in both traditional and discount department stores, liquor retailing, fast food outlets and women's fashion stores.¹⁷ It operates Myer Grace Bros, Target, Kmart, Myer Direct, South Cape, Red Rooster, Officeworks, Katies, Fosseys and Liquorland.

2.21 Coles Myer is Australian-owned with more than 320,000 shareholders, and trades Australia-wide.¹⁸

Franklins

2.22 Franklins is a 'no frills' food retailer and regards itself as the leading modern day discounter. It employs over 25,000 staff in 270 supermarkets and 30 LiquorSave outlets, with operations in New South Wales, Victoria, Queensland and South Australia.

2.23 Franklins has recently moved to convert many of its retail stores into full-service supermarkets, with a significant offering of fresh produce.¹⁹

14 Woolworths, Submission 229A, p 4.

15 Australian Competition and Consumer Commission, Submission 191, p 7.

16 Coles, Submission 168, p 2.

17 Australian Competition and Consumer Commission, Submission 191, p 7.

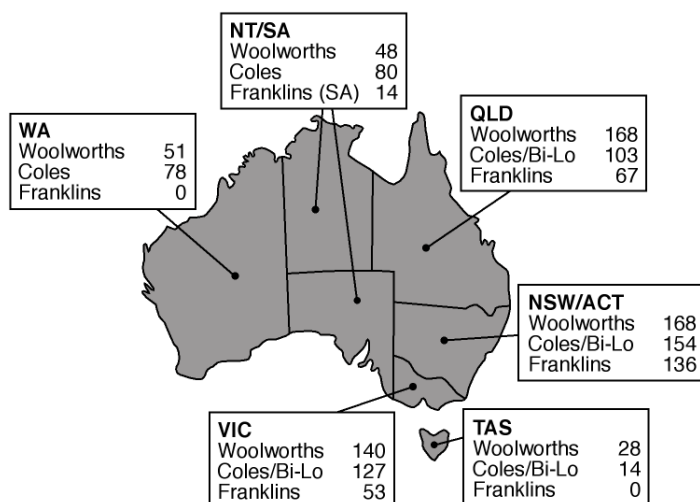
18 Coles, Submission 168, p 2.

19 Franklins, Submission 200, pp ii - 1.9.

2.24 Franklins is owned by Hong Kong-incorporated Dairy Farm International, which has supermarkets and other retail outlets throughout Asia and Australia.²⁰

Figure 2.5

Major Chains' Supermarkets in Australia



Source: Franklins, Submission, pp 1.2-1.3

The independent retailers

2.25 Independent retailers make up the remainder of the retail grocery sector. The independents vary in size from small corner stores to full-size supermarkets.

2.26 Many independents operate almost entirely in what are called ‘banner groups’, which are supplied by a wholesaler, but wholly owned, in most cases, by the independent retailer. The stores operating within a banner group typically present a common face or image to the public. They consist of similarly-sized shops, each carrying a similar product range, and backed by common signage, shared advertising and promotional funding, and coordinated pricing (for example, the pricing of ‘specials’). They cooperate, often very closely, with a particular wholesaler, seeking to match the economies of scale in purchasing and other efficiencies in distribution, which are available to the vertically integrated major chains. The IGA banner group is the most notable, with three distinct supermarket categories based on size.²¹ Most banner groups operate within their home State, with a few operating nationally.²²

2.27 The main representative body of the independent supermarket sector is the National Association of Retail Grocers of Australia (NARGA). NARGA is a

20 Franklins, Submission 200, p 1.9.

21 The three supermarket categories are IGA Supermarkets, IGA Everyday and IGA Express. IGA is supplied by wholesaler Davids.

22 Australian Competition and Consumer Commission, Submission 191, p 7.

confederation of State-based independent retailer organisations and directly represents around 7,300 small and independent retailers employing around 97,500 staff. Of these, the supermarket and grocery stores sector consists of 4,850 Australia-wide stores.²³

The wholesalers

Dauids Limited (Dauids)

2.28 Dauids, which commenced wholesaling operations in 1935, is the largest Australian wholesaler and operates in all States and Territories, except Western Australia. Its core business has been grocery wholesaling and distribution, primarily in New South Wales, however, it also runs a number of stores of its own which are being sold as part of the restructuring initiated by owners Metro Cash and Carry Limited Metro.²⁴

2.29 Dauids' independent retail customers range from small corner stores to full size supermarkets, which provide similar product choice as any one of the full-size major chain stores. Dauids also serves independent retailers with multiple supermarkets – some with up to ten stores.²⁵

2.30 Dauids employs around 3,500 people at 56 warehouses and around 6,600 people in its company-owned supermarkets throughout Australia.²⁶

2.31 In the early 1990s, Dauids considered that if it could increase its size, by joining together all of the independent wholesalers in Australia, it could attain the necessary efficiencies and volume of purchases to compete with the three major chains on an equal footing. Thus, Dauids undertook a program of acquisitions of regional and State-based independent wholesalers to build itself up as a 'fourth force'. It was considered that independent retailers could survive only if they were part of a larger group that could deliver the benefits of scale and scope in terms of buying and marketing, merchandising, store design, information technology, signage etc., while retaining the advantages of an owner operator at the store level.²⁷

2.32 Since Dauids was floated in 1994, it has increased its market share in grocery distribution through a series of acquisitions, particularly in South Australia, Victoria and Queensland. However, it experienced considerable management difficulties, resulting partly from its acquisitions, and in 1998 Metro Cash and Carry Limited, a publicly listed South African Company, purchased a 78 per cent stake in Dauids.²⁸

23 National Association of Retail Grocers of Australia, Submission 201, p 22.

24 Dauids, Submission 166, pp 3-4.

25 Dauids, Submission 166, pp 3-4.

26 Dauids, Submission 166, p 3.

27 Australian Competition and Consumer Commission, Submission 191, pp 18-19.

28 Business Review Weekly, *Metro Buys a Warehouse of Trouble*, Neil Shoebridge, 5 Oct 1998.

2.33 Since the takeover, Davids has acted to consolidate its 29 banners into three channels (based under the IGA banner), with the aim of obtaining better marketing economies of scale.²⁹

2.34 Davids operates via four business channels, with a central corporate support division providing financial, information technology, merchandising and logistics services. The business groups are:

- Distribution/Retail: supplies groceries, meat, fruit and vegetables and general merchandise, to over 4,000 independent retailers.
- Cash/Carry: self-service grocery and liquor cash & carry distributor to smaller retailers and caterers.
- Food Service: distributor to restaurants, cafes, fast food outlets, hotels and other institutions.
- Australian Liquor Marketers (half-owned by Davids): Australia's largest wine and spirit wholesaler, it operates nationally distributing products such as spirits, wines and some packaged beers.³⁰

Australian Independent Wholesalers (AIW)

2.35 AIW is a wholesaling division of Woolworths. It was a small regional wholesaler when acquired by Woolworths in 1996.³¹

2.36 As well as servicing Woolworths, AIW supplies independent retailers in competition with Davids. It now supplies over 300 retailers in eastern Australia previously supplied by Davids.³² Its fight with Davids for market share has been reported to have been vigorous.³³

Foodland Associated Limited (FAL)

2.37 FAL is the major supplier and sole independent grocery wholesaler in Western Australia. It offers a full range of retail, financial incentives and marketing support services to FAL franchise and other independent retail customers. FAL also owns the 24-store Action Food Barns (Action) retail group, and has substantial wholesale and retail interests in New Zealand. It is the third largest retail organisation listed on the Australian Stock Exchange, and employs over 19,500 people.³⁴

29 IGA Supermarkets, IGA Everyday and IGA Express make up the 3 banner groups.

30 Davids, Submission 166, pp 3-4.

31 ACCC Submission 191, p 20.

32 ACCC, Submission 191, p 7.

33 Business Review Weekly, *A few supermarket casualties in the war of independents*, Neil Shoebridge, 8 March 1999.

34 FAL website at <http://www.fal.com.au>.

2.38 FAL was established as a grocery partnership in Fremantle in 1893, and was incorporated in Western Australia in 1926 as a supplier to small grocers. It distributes grocery and ancillary products to more than 700 retail stores.³⁵

2.39 FAL's wholesale business is based at a large warehouse in Canning Vale, south of Perth, with two smaller warehouses in the northern suburbs of Perth and Kalgoorlie. More than \$50 million in stock is warehoused at Canning Vale alone.³⁶

Differences between the major chains and the independent sector

2.40 The vertically integrated structure of the major chains facilitates a number of advantages in purchasing, warehousing and pricing practices:

- Vertical integration enables the major chains to derive their entire profitability from retail operations, while in the independent sector, both the warehouse and the retail stores make separate profits. In addition, buyer groups are also part of some independent supply chains.
- Independent wholesalers carry the debt risk for many of the retailers they supply, while deliveries to retail stores in a chain are an internal transfer.
- Compared with the centralised buying practices of the major chains, independent wholesalers may have fewer opportunities for 'investment buys', where quantities are purchased from suppliers prior to promotions or known price increases.
- Centrally co-ordinated store orders for the major chains involve larger warehouse pick-up runs, enabling them to exploit efficiencies in distribution. By contrast, the average store order from an independent wholesaler is mainly small to medium.
- Being the 'core tenant' in large shopping centres, the major chains pay substantially less rent per square metre than other small retail tenants. In addition, the major chains enjoy more flexible terms and conditions in their leasing arrangements.
- Economies of scale enable the major chains to utilise electricity and floor space more efficiently than small retailers. As a general rule, the smaller the business, the more costly and labour intensive it is to run.
- The major chains can centrally co-ordinate promotional activities and exploit generic advertising advantages.
- There can be tax benefits associated with vertical integration. Wholesale Sales Tax (WST) is generally paid on the final wholesale selling price of goods, usually a value incorporating the costs incurred up to and including that sale. Those costs could be activities such as advertising, storage and transportation of

35 ACCC, Submission 191, p 7.

36 Foodland Associated Limited, Submission 190, pp 7-8.

products. Those costs will not be within the tax base when performed by a vertically integrated retailer. However, it is likely that concerns raised by wholesalers and independent retailers in relation to the differences in the effect of WST will be resolved with the new tax system to take effect from 1 July 2000.³⁷

- Evidence before the Senate Employment, Workplace Relations, Small Business and Education References Committee' inquiry into the New Tax System notes that the GST may see significant cash flow advantages accrue to the larger firms.³⁸

37 ACCC, Submission 191, pp 10-11.

38 *Hansard*, Sydney, 23 February 1999, p 280.