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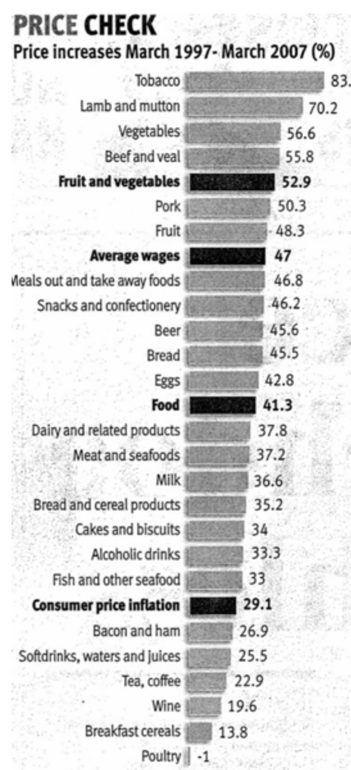
The Secretary
Senate Community Affairs Committee
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Secretary,

INQUIRY INTO THE COST OF LIVING PRESSURES ON OLDER AUSTRALIANS

We congratulate the Senate for initiating an Inquiry into cost of living pressures and suggest that these are felt by the community as a whole, but particularly by older Australians on fixed incomes.



The problem is clearly demonstrated by a chart published by *The Australian* on July 12 this year which showed how food prices had increased over the past ten years in comparison with inflation.

The data shows that, although the CPI had increased by only 29.1% over this period, average food prices had increased by 41.3%.

Average wages have kept up with these price increases, rising 47%. *However, people on pensions and on other sources of fixed income have not seen these increase at the same rate.*

The above data (sourced from the ABS) shows that fresh foods such as vegetables, fruit, and a range of meat varieties have had significantly higher rates of price increase than either CPI or food in general.

It has been suggested that these increases are drought related, but the available data has been analysed by PricewaterhouseCoopers and the results show that this is not the case. Rather the rate of price increase in food as a whole and in fresh food in particular can be traced to an increasing concentration of the retail grocery market and the vertical integration of fresh food supplies.

> **Woolworths and Coles between them now account for around 80% of grocery sales.**

This degree of market concentration removes effective competition and allows a duopoly to extract higher margins at the expense of consumers.

We contend that, without this factor, the increase in CPI over the last ten years would have been even lower, due to the China factor which has tended to depress CPI worldwide. Whilst Chinese imports have helped to reduce the CPI in Australia – in electronics for example – the full benefit of this factor has not been felt in Australia because of food price inflation.

> **We conclude that food price inflation has pushed total CPI higher than it could have been, and has resulted in a need to increase interest rates.**

Obviously older Australians have been impacted by these price increases and, to some extent, by the resulting increases in interest rates.

We attach, for your information, a copy of a report prepared by PricewaterhouseCoopers titled: '*The economic contribution of small and medium-sized grocery retailers to the Australian economy, with a particular focus on Western Australia'.*

The report was commissioned by us at NARGA to provide a snapshot of the grocery sector in Australia and to detail the outcomes resulting from increased concentration of the retail grocery market.

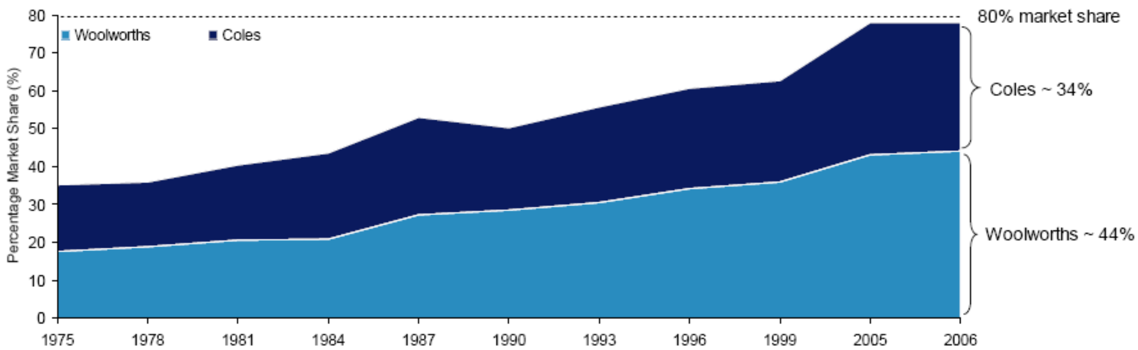
The retail grocery market in Australia is dominated by two chains, Woolworths and Coles, that together comprise 80% of the market. Both companies have wider interests and have substantial shares of the petrol, liquor and general merchandise market – together accounting for some 40% of all national retail sales – now that Westfarmers is taking over the Coles Group.

The increasing level of concentration has seen a number of chains fail and has reduced the grocery wholesale sector to one supplier servicing the remaining 20% of the market made up, primarily, of independent stores.   The report makes the following observations (among others):

Contribution to food price inflation, CPI and interest rates

The market dominance of Woolworths and Coles - at 80 per cent - is contributing to food price inflation.

Figure 2.10: Growth in market share of Woolworths and Coles, 1975-2006



Source: Retail World, ACNielsen

PricewaterhouseCoopers reports (page 6) that "...*food is one of the largest contributors to growth in the CPI...food prices have consistently grown at a higher rate than the CPI and in the most recent years food price inflation has risen significantly.*

"Therefore, it appears that food price inflation has potentially boosted supermarket and grocery store turnover as a proportion of total retail turnover.

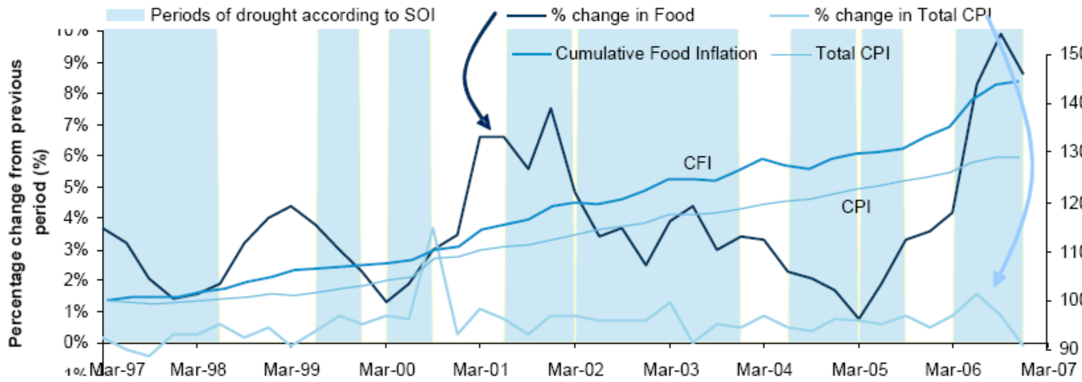
"There are also suggestions that the measured level of food price inflation may underestimate the true rise in the cost of grocery goods.

"That is, the MGRs may be running 'loss leaders', or providing lower prices, on high volume food staples included in the CPI food basket, thereby hiding the rise in prices of other grocery goods which are growing at a greater rate.

"It is also interesting to note that certain approximate periods in which sustained drought conditions have persisted, according to the calculation of negative values for the Southern Oscillation Index (SOI) as measured by the Bureau of Meteorology, coincide with rising food inflation. However, there does not appear to be any consistent pattern or correlation between negative SOI values and food inflation."

In other words, Woolworths and Coles, with 80 per cent of the grocery market between them, cannot blame the drought for higher prices.

Figure 2.3: Comparison of food price inflation and total CPI



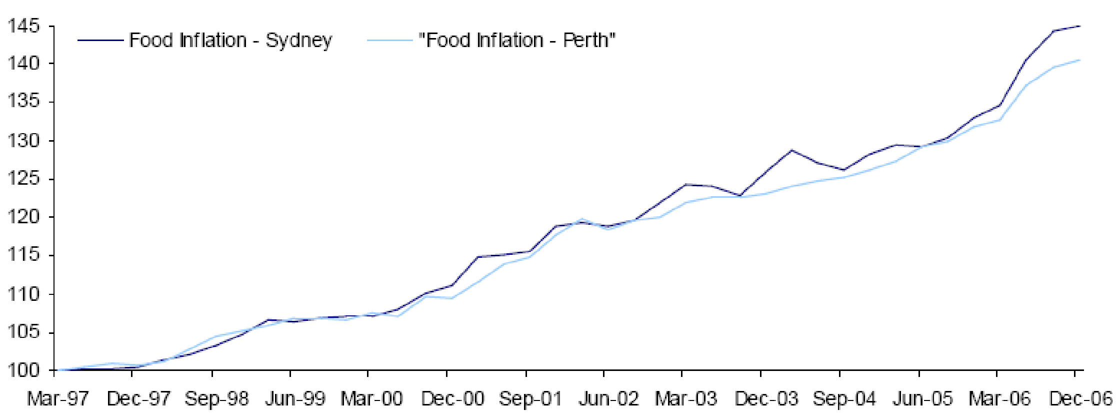
Source: ABS Cat. 640102

If food price inflation or broader grocery price inflation is feeding into CPI, then it is also likely to be feeding into interest rates, hitting consumers with a double impact. The massive share of the Australian grocery market held by Woolworths and Coles, impacting on growers, manufacturers and retail competitors, is inevitably being translated to higher grocery prices.

In many places around Australia Woolworths or Coles have a monopoly position. Cooma and Bateman's Bay in New South Wales are examples, but there are many big shopping centres in the major cities where one or the other has a monopoly, with no direct competitor.

Where independent grocery retailers are strong, such as in the suburbs of Perth, where they have a 32 per cent market share compared to the national market share of 20 per cent, food price inflation is clearly lower, according to PricewaterhouseCoopers. That fact alone should persuade regulators that market concentration is a major problem.

Figure 5.6: Comparison of food price inflation in Sydney and Perth



Source: ABS Cat. 640103

Ironically, the independents' influence over Woolworths and Coles prices is confirmed by a survey commissioned by the Australian National Retailers

Association, whose members include Woolworths and Coles. [ANRA news release 15 June 2007 – *"Aussies pay less for food today than 30 years ago"*].

ANRA found that Perth was the cheapest State capital, requiring the fewest minutes of working time (compared with other State capitals) to buy a limited basket of grocery products, thus confirming that Woolworths and Coles prices are being kept under greater control in Perth than elsewhere in Australia because of the independents' stronger competitive position.

It is understood that the pricing policy adopted by the majors allows for store pricing to be varied according to the level of local competition, with substantially higher prices set in areas where competition is low.

Retail Employment

The retail sector is Australia's largest employer, with small and medium sized family businesses the largest component.

According to the PwC study, the retail sector generates 1.2 million full-time equivalent (FTE) jobs, of which 253,100 are in the grocery sector, the largest contributor to retail employment.

Independent grocery retailers with 35 per cent of stores and just fewer than 20 per cent of grocery sales, provide 57 per cent of these jobs.
But Woolworths and Coles, with 24 per cent of stores and 80 per cent of grocery sales, provide only 43 per cent of jobs.

> **The significance for older Australians is that the independents provide proportionately more opportunities for part-time work for those who want to continue to work or need to supplement their income.**

Independent grocery retailers around Australia make a disproportion-ate contribution to the national economy and are usually the major contributor to their local economy, in terms of the jobs they create and the wealth that is churned back into the local community.
Woolworths and Coles, on the other hand, are supplied by a relatively small number of big growers, processors and manufacturers and return very little wealth to local communities.

This is being exacerbated by their increasing reliance on imported goods to extend their ranges of private label products, forcing many local suppliers off the shelves.

And, contrary to the new store development proposals they put to local government authorities, the PricewaterhouseCoopers report makes clear that Woolworths and Coles are not major contributors to jobs growth.

BRW magazine had reported late in 2006 that:

"In spite of increasing its revenue by 75 per cent since 2001, Woolworths has cut its workforce by 27% or 35,592 people [over the past 5 years]*. Retail rival Coles has also slashed its workforce over the past five years, down from 160,000 in 2001 to 94,000*…[in 2006]*."*

Here is PricewaterhouseCoopers summary of employment statistics in the retail grocery industry:

Market Participants	% Turnover	Stores	Turnover	FTEs	FTEs per store
Top 2 – Woolworths & Coles	78-79%	1,493 (24%)	$59 billion	108,833 (43%)	65
Top 4 – Woolworths, Coles, ALDI & Pick 'n Pay (Franklins)	80%	1,683 (27%)			
Independent grocery banner groups – IGA, FoodWorks, Ritchies	18.9%	2,140 (35%)	$15 billion	144,267 (57%)	32
Other independent grocery retailers	1.1%	3,291 (53%)			
TOTAL	**100%**	**6,183**	**$74 billion**	**253,100**	

Increasing Market Concentration

The first graph in this submission – which shows how the retail grocery sector has increased its level of concentration since 1975, is quite informative.

It covers the period of time over which Australia's trade practices law – The Trade Practices Act 1974 - has been operating. Whilst the Act controls mergers and acquisitions and requires these to be approved by the Australian Competition and Consumer Commission (ACCC), it has not been able to prevent the growth in market concentration in the sector.

This level of concentration has been achieved via a number of mechanisms:

- Organic growth (new store openings, increases in store size or sales);
- Partnership with major shopping centre owners (to obtain prime sites);
- Acquisition of all or parts of smaller chains; and
- Creeping acquisition – the purchase of stores one at a time.

The latter two have had the greatest impact and have requires ACCC approval, which has never been denied – although in some acquisitions the number of stores allowed to be purchased from a chain has been restricted. In those cases, however, the two major chains have invariably gained control of the larger proportion of available stores.

The increasing level of market concentration has resulted in the demise of many smaller chains and individually owned stores. This means that, in many areas, the only places where older Australians can shop for groceries are the major chians or smaller convenience stores.

The chains tend to be located in larger shopping centres that are often not easily accessible by older people. Small convenience stores are closer to home, but are significantly more expensive.

According to the ABS 10% of families do not have a car. These families tend to be those of older Australians and single parents. Given the fact that many older Australians have reduced mobility, the level of concentration in the grocery market and the consequent reduction of store numbers, has made groceries, and particularly lower cost groceries, less accessible to older Australians.

> **Grocery market concentration therefore results in reduced access, reduced choice and proportionately higher grocery prices for older Australians.**

The Future

There are obvious concerns associated with this trend continuing as there are already large parts of major cities and regional centres which are local monopolies. Rarely do the chains compete head to head – and in any case they have the same overall product offering.

In some states the level of market concentration attributable to the two majors approaches 90%. Unless something changes, this could reflect the future in other states.

Improving the competitiveness of SMEs

There is urgent need for improvement in Australian trade practices law to ensure that smaller stores can compete on equal terms and continue to provide services to local communities and the necessary competitive pressure to help keep grocery prices in check.

However, there are other things governments can do to make smaller companies more competitive. The cost of “red tape” compliance is hindering the ability of independent grocery retailers to compete with Woolworths and Coles. PwC's report says:

"It is important that policymakers are cognisant of the policy settings pertinent to the retailing industry. This will be critical to ensuring that competition is promoted in the grocery industry and that competitors are not disadvantaged by the extending dominance of MGRs under pressure to deliver increased earning.

"In addition, particularly in the retailing sector, SMEs are disproportionately burdened by compliance imposts and regulatory requirements. Due to the cumulative economic size of SMEs, reductions in "red tape" could be expected to deliver significant productivity and other net benefits to the Australian economy.

"It is also important that the significant beneficial economic impact of SMEs is acknowledged and appreciated. Whilst it may be a small component of the total economy and MGRs generate significantly greater volumes of sales, SMEs constitute the majority of grocery stores and make a critical contribution in their own right to servicing customers in more regional and remote areas, as well as providing greater choice for consumers.

"Independent retailers have an economically valuable role as a balancing competitive force against the MGRs and as enhancers of consumer choice and welfare in the grocery retailing industry.

Independents don't have huge departments full of specialist staff dealing with accounts, workplace relations, regulatory compliance, IT and so on, as the chains do - we have to do it all ourselves - so, every new government compliance burden hurts.

Governments at all levels need to understand the fundamental importance of grocery retailing to the success of the economy and the importance of the independents' role in competing and preventing the major chains from running riot with prices.

An example of where regulatory initiatives have hurt the small business sector is in the changes made to retail trading hour laws under Competition Policy reforms.

Whilst these laws did require review, we believe that insufficient attention was paid to the public interest factor and the impact of the changes on smaller retailers.

Woolworths and Coles lobbied strongly for significant increases in trading hours in every state. As a result, in states which did make major changes, many small stores closed thereby increasing the level of retail grocery concentration.

The proportion of independents is greatest in Western Australia (32% vs 20% nationally) where trading hours have not undergone as dramatic a revision.

We contend that the changes made to shopping hours in the grocery sector have not, on balance, resulted in net community benefit.

This theme is explored in a second paper produced in house titled:

'The Regulation of Retail Grocery Shopping Hours and the Implications for Community Welfare – a discussion paper' (NARGA, July 2007)

A copy is attached. The paper demonstrates how regulatory change, however well intentioned, can have negative consequences that, inevitably, tend to impact older people to a greater extent.

We would be pleased to attend any public hearing to present further evidence and to answer any questions the Committee may have.

Please come back to us if you need any further information.

Yours faithfully,

Ken Henrick
Chief Executive Officer