

The Australian supermarket sector is highly concentrated

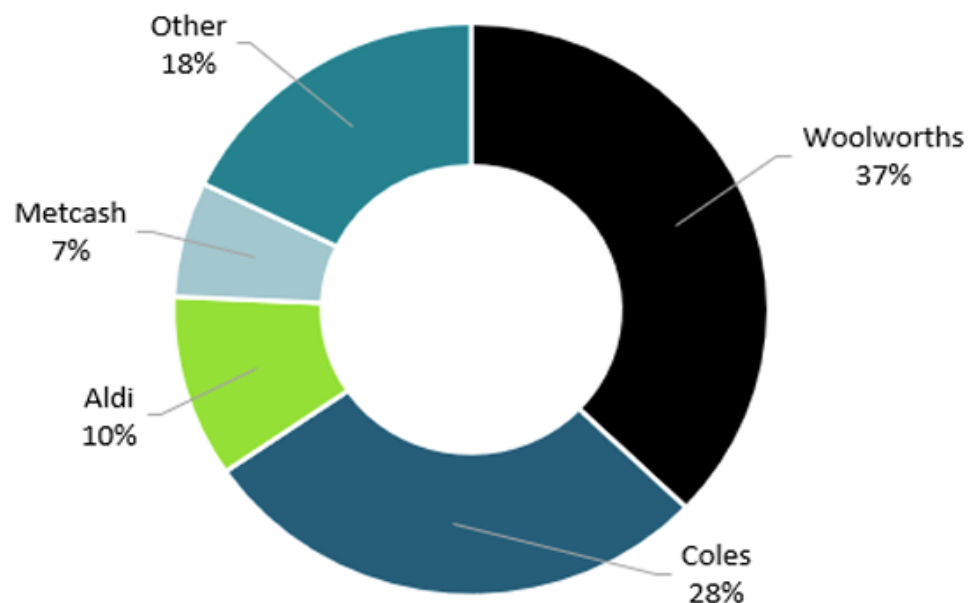
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Submission to the Senate Select Committee on Supermarket Prices

Woolworths and Coles bestride Australian retailing. The two supermarket chains have combined sales of around \$80 billion.² Between them, they account for two-thirds of the food and grocery sector.

Figure 1. Food and grocery sector market share for the financial year 2022–23¹



Source: Food and Grocery Code Independent Reviewer, Annual Report 2022-23, p 4.

They are among the largest employers in Australia: Woolworths employs around 200,000 and Coles 120,000.³

¹ The author is a senior lecturer at the University of Canberra but views expressed are his own.

² Woolworths reported supermarket sales of \$41 billion in financial year 2023; *Annual Report 2023*, p 32. Coles reported supermarket sales of \$37 billion in financial year 2023; *Annual Report 2023*, p 30.

³ Source: 2023 annual reports.

They are the 14th and 22nd most valuable companies listed on the Australian Stock Exchange, worth \$45 billion and \$22 billion.⁴ Woolworths is one of only two Australia companies in *Fortune's* global 500 largest firms.

Two large firms with such high market shares raise concerns about whether competition is adequate. Predatory pricing may lead to further concentration in the market. The threat of aggressive price-cutting, or difficulties created in obtaining good sites⁵, may also deter new entrants in the market. Suppliers, such as local farmers, may fear offending such large purchasers. There are legitimate concerns that the margins between prices charged to consumers and those paid to suppliers are wider than they would be if there were more competitors in the market.

An ACCC (2008) report concluded that 'grocery retailing is workably competitive'. It noted, however, 'the limited incentives for Coles and Woolworths to compete aggressively on price'. When this report was written, Woolworths and Coles had market shares of around 30 and 25 per cent.⁶ So the market has become even more concentrated over the intervening years.⁷

The ACCC has referred to a rule of thumb that a market is considered 'concentrated' if the four largest players have a combined market share of over 75 per cent or the Herfindahl-Hirschman Index⁸ is greater than 2000.⁹ Currently the four largest supermarket chains have a combined market share of over 75 per cent, arguably over 80 per cent, and the HHI is above 2,300.¹⁰

And as minister Leigh (2022) and Philipporn (2019)¹¹, for example, have noted, market concentration is associated with higher prices (as well as lower investment and productivity growth).

⁴ Source: marketindex.com.au/asx200. As at 2 February 2024.

⁵ ACCC (2008: xix) referred to 'credible evidence of incumbent supermarkets using planning objection processes to deter new entry in circumstances where the incumbent supermarket had no legitimate planning concerns'.

⁶ ACCC (2008: 48).

⁷ One contribution to this is the demise of Franklins, which has been a significant third chain in New South Wales.

⁸ The sum of the squares of the market shares of each firm in the market.

⁹ ACCC (2008: 49).

¹⁰ Author's calculations based on chart above. The exact numbers will depend on whether the supermarkets such as IGA supplied by Metcash are regarded as a single chain and the composition of the 18 per cent market share held by 'others' such as Costco.

¹¹ A more detailed version of this note can be found in Covarrubias, Gutiérrez and Philippon (2020).

The ACCC inquiry

It is therefore welcome (indeed overdue) that the Australian Government announced on 25 January 2024 that it is directing the Australian Competition and Consumer Commission (ACCC) to conduct an inquiry into Australia's supermarket sector, including the pricing practices of the supermarkets and the relationship between wholesale, including farmgate, and retail prices. This will be the first ACCC inquiry into the industry since 2008. An issues paper is due in February 2024, an interim report by August 2024 and a final report by February 2025.

The Government's announcement came after this committee was established. I would suggest that this committee seek an amendment to its terms of reference so that it releases an interim report in May 2024 and a final report in mid-2025 after there has been time for submissions and hearings to reflect on the ACCC report.

The supermarkets' contribution to recent inflation

The prices of goods sold in supermarkets were clearly part of the acceleration in consumer prices in 2022 and the slowing in 2023; Table 1.

Table 1: Selected CPI components; percentage change over year to December quarter

	2021	2022	2023
Bread and cereal products	1.2	12.2	8.2
Meat and seafoods	2.5	8.2	0.0
Dairy and related products	1.8	14.9	6.4
Fruit and vegetables	0.2	8.5	-0.2
Other food products	1.6	11.0	6.5
Personal care products	1.7	7.8	2.7
Pets and related products	0.9	19.0	2.8
Total Consumer Price Index	3.5	7.8	4.1

Source: Australian Bureau of Statistics, *Consumer Price Index*, December quarter 2023, table 7.

But the data in Table 1 say nothing about whether the supermarkets were just passing on cost increases or whether any addition to their profit margins was also being passed on to consumers.

The ABS compiles statistics on the inputs to the 'retail trade' sector (quite a lot broader than supermarkets). The most recent data, shown in Table 2, refer to 2020-21 so cannot yet illuminate the recent inflationary experience.

Table 2: Inputs to retail trade by industry. 2020-21

Agriculture	4
Manufacturing	6
Other inputs (mostly services)	54
Compensation of employees	57
Profits	36
Production	154

Source: derived from ABS, *Australian National Accounts: Input-Output Tables, 2020-21*, 30 March 2023.

Data on aggregate profits in the retail trade sector appear in the ABS' national accounts. Profits increased as the economy recovered from Covid. The 37 per cent increase in profits from the March quarter 2021 to the September quarter of 2023 well outpaced the 15 per cent increase in the CPI over the same period. But there was not a large increase in the profit share in retailing; the benefits of increased activity were shared with workers. (The economy-wide increase in the profit share, and fall in the wages share, is mainly due to commodity price rises increasing profits in the mining industry.¹²)

Table 3: Retail trade sector: Gross value added (\$ billion)

	Compensation of employees	Gross operating surplus and gross mixed income	Gross value added	Profit share
Mar 2021	14.1	7.3	22.0	0.33
Jun 2021	14.9	7.6	23.2	0.33
Sep 2021	14.6	7.7	22.2	0.35
Dec 2021	14.8	7.7	22.9	0.34
Mar 2022	15.1	8.1	24.1	0.34
Jun 2022	15.7	8.6	25.3	0.34
Sep 2022	16.6	8.9	26.4	0.34
Dec 2022	16.8	9.2	27.0	0.34
Mar 2023	16.9	8.8	26.9	0.33
Jun 2023	17.2	9.8	28.1	0.35
Sep 2023	17.7	10.0	29.0	0.35

Source: derived from ABS, *Australian National Accounts: September 2023*, 6 December 2023, table 45.

The data discussed above are quite aggregated. Hopefully, this inquiry will be able to engage in a more focused examination of pricing by the major supermarket chains and compare movements in input costs (including farmgate prices) and retail prices for some key products.

As an example, the committee could build on its 2010 inquiry specifically on pricing in the dairy industry. The committee then covered a number of issues in pricing, particularly the role played by the major supermarkets' generic products, and attempted¹³ to split the retail price of milk into its component

¹² Reserve Bank of Australia (2023):

¹³ Senate Economics References Committee (2010: 42, 44).

elements. The committee noted that this was a difficult exercise on the data available at the time and called for greater transparency.

The Coles CEO has promised to appear at this inquiry to ‘engage in an informed discussion on the factors that influence supermarket pricing’.¹⁴ But as Paul (2023) argued, the large supermarket chains did not have to wait for this inquiry to become more transparent about their pricing.

References

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¹⁴ Coles media release, 6 December 2023.