

# Comments on the proposed amendments to parallel impor- tation laws for books

Submission to the Productivity Commission Inquiry on Parallel Importation of Books

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## About

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## About the Author

**Joshua Gans** is an economics professor at Melbourne Business School in Australia. His research focuses on microeconomics, competition policy and innovation. He is the author of several textbooks and policy books, as well as numerous articles in economics journals. Gans received a Bachelor of Economics (Honours) and the University Medal from the University of Queensland before going to Stanford University to study for his Ph.D. in Economics. He graduated from Stanford in 1995 and moved to Melbourne Business School in 1996 as an Associate Professor and became a full Professor in 2000. In 2007, Gans received the inaugural young economist award from the Economic Society of Australia. This is an award given every two years to the best economist working in Australia, who is aged under 40. (See [www.mbs.edu/jgans](http://www.mbs.edu/jgans) for more details).

## Disclaimer

Professor Gans has written several books. His textbook, *Principles of Economics* (co-authored with Stephen King, Robin Stonecash and Gregory Mankiw) is one of Australia's biggest selling economic textbooks and is published by Cengage Australia. He recently published *Parentonomics*, in Australia by New South and, in the rest of the world, by MIT Press. For this reason, he has a vested interest in the profitability of book publishing in Australia.

## Introduction

The purpose of this submission is to briefly outline the economic case for and against parallel import restrictions. I then evaluate whether the proposed relaxation of those restrictions by the Productivity Commission (PC) will assist in improving outcomes for Australian authors at the minimal expense to Australian consumers. I find that these restrictions do not resolve key trade-offs in an optimal way and complete deregulation is preferred.

## Basic Economics

Restrictions on parallel imports is a direct form of trade protection. It prevents booksellers from sourcing the supply of books on the world-wide wholesale market and requires them to deal directly with the Australian publisher of a work. This raises the cost of procuring books and these costs are passed on to consumers with the resulting traditional dead-weight losses from under-consumption.

Publishers argue that these restrictions are necessary in order to ensure a sufficient return on the creation of books by Australian authors. In particular, a publisher may want to make Australian books available outside of Australia at a lower price than within Australia. This form of price discrimination is often practiced in information selling markets and takes a variety of forms (including region coding of DVDs and computer games,<sup>2</sup> or publisher restrictions on electronic sales across national boundaries, as in music, movies and TV). Price discrimination often requires there to be restrictions on cross-market selling in order to be sustainable but these restrictions may come from intrinsic factors such as transportation costs and versioning (that is, tailoring a book to different markets).<sup>3</sup> It raises profits to the publisher and, so long as it does not result in fewer items being sold in any market, can be economically efficient.

The problem is that while there may be some books for which price discrimination is economically efficient, restrictions on parallel imports impact on *all* books. Importantly, whether they are published in Australia or by Australians or not. In terms of their impact on Australian consumers, these restrictions raise the price of all books sold in Australia.

In addition, if the Australian book-selling industry is not perfectly competitive, there exists a double mark-up problem. For publishers, this problem means that they have to set the wholesale price lower so as to ensure that booksellers stock more items. Economists have demonstrated that when this situation arises, parallel import restrictions can be desirable if transportation costs are high.<sup>4</sup> However, it is my understanding that for all but best selling books requiring fast re-stocking, books sold in Australia, whether published by an Australian author or not, are printed overseas. Consequently, the relative transportation costs are low or, from the perspective of relevant economic theory, irrelevant. In this situation, it is economically efficient to remove parallel import restrictions.

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<sup>2</sup> See Emily Dunt, Joshua S. Gans and Stephen P. King, "[The Economic Consequences of DVD Regional Restrictions.](#)" *Economic Papers*, 21 (1), March 2002, pp.32-45.

<sup>3</sup> For instance, the Australian and US versions of *Parentonomics* differ in their language to be accessible to different English language readers. Textbooks are also often differentiated in terms of local content.

<sup>4</sup> K.E. Maskus and Y. Chen, "Vertical Price Control and Parallel Imports: Theory and Evidence," *Review of International Economics*, 12 (4), 2004, pp.551-570.

## Partial Restrictions

The PC has proposed limiting the protection from parallel imports to twelve months from when a book is first published in Australia. This is a welcome relaxation of the law from the perspective of economics. The question is: who remains for the parallel importation restrictions to protect.

First of all, the PC noted that there was a general concern for untested, first time Australian authors. However, it would be extremely rare, given their untested nature, for those authors to have international distribution of their books in the first 12 months following their Australian release; let alone with enough time to organise a parallel importation of those books.<sup>5</sup> Consequently, those books are naturally protected over the first 12 months regardless.

An exception to this may come if electronic distribution of books across national boundaries was freed up. These are currently hampered by publisher licensing restrictions that prevent international sales. But if those restrictions were to practically fall away as a result of other developments, international distribution could occur quickly. Nonetheless, in this case, the global market will drive prices to a common level regardless.

Second, there was some discussion of textbooks developed in Australia that may be subject to cheaper imports. Once again, for newer books, adoptions within the first twelve months are slower than when a book becomes established. So even if these books were available and sold overseas, it is unlikely a 12 month restriction will play an additional role in protecting those books from import competition as compared to no restrictions at all.

Third, the main books that will be protected by a 12 month restriction are those with a higher expected initial sales volume by already established authors (e.g., JK Rowling and Stephenie Meyer). This is likely to be a handful of Australia authors but constitute a large volume of book sales (see Figure 2.2 of the Draft Report).

In this respect, it can be seen that a 12 month restriction does little to protect the riskiest Australian author prospect and instead, protects the most lucrative book sales -- quick best-sellers by overseas authors. Thus, for the most part, as a partial restriction, it is targeted to continue to harm consumers where they are most vulnerable to harm but not to confer any offsetting benefits in terms of support of local authors.

## Entry

As a partial removal of parallel import restrictions still leaves high wholesale prices for the most stable and assured demand for books, it creates a significant barrier to entry -- particularly, from international chains such as Amazon who can manage global supply chains efficiently to bring lower prices to consumers. If restrictions were removed entirely, Amazon, for instance, could set up local warehousing and payment facilities. They could then use their international supply logistics to bring Australians more cheaply their entire book range and give Australia a comprehensive on-line bookseller. At the moment, this is constrained because of transportation costs.

## Summary

The economics overwhelmingly justify the removal of parallel import restrictions on books. Partial restrictions of the form proposed by the PC only serve to continue to harm consumers with little to no support for Australian publishers and authors. Given the relatively small share of Australian-authored sales, it would be better to opt for deregulation and leave it to cultural policy to address whether to support Australian authorship or not.

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<sup>5</sup> *Parentonomics* was a rare instance whereby an international agreement was signed soon after the Australian publishing agreement. However, even in this case, the book was published elsewhere in the world 9 months following its release in Australia.