

# Economic Structure and Performance of the Australian Retail Industry

## Submission

Michael Geale & Tim McCullough  
ForTheRiders Bike Shop

### INTRODUCTION

This submission will address the following areas of the Inquiry:<sup>1</sup>

*“3. The broader issues which are contributing to an increase in online purchasing by Australian consumers and the role of online purchasing in providing consumers with greater choice, access and convenience.*

*4. The sustainability and appropriateness of the current indirect tax arrangements in this environment, including the impact on Commonwealth and State and Territory budgets, and the extent to which technology could reduce the administrative costs of collecting indirect taxes and duty on imported goods.”*

This submission will address these questions from our perspective as a bicycle retailer and will provide relevant examples from our industry.

---

<sup>1</sup> <http://www.pc.gov.au/projects/inquiry/retail-industry/terms-of-reference>

## **BACKGROUND: FORTHERIDERS AND THE BICYCLE INDUSTRY**

ForTheRiders is a Brisbane-based mountain bike (MTB) retailer. We have been operating since 2003, with a physical store in Annerley and an online presence. ForTheRiders specialises in high-end mountain bikes, parts and servicing and delivers products Australia-wide.

The Australian bicycle retail industry is estimated to contribute over \$1 billion per year to the Australian economy.<sup>2</sup> Bicycle retailers, of which there are over 1100 in Australia,<sup>3</sup> have until recently been predominantly small, independent stores. The industry has recently seen the entry of large chain stores, such as Goldcross (a subsidiary of SuperCheap Auto). From our assessment and through conversation with industry representatives, it appears that online retailing by Australian bicycle shops is limited.

Cycling has been rapidly gaining popularity in Australia. There was a 32% increase in the numbers of people cycling from 2000 - 2009,<sup>4</sup> and our experience has shown an increase in the numbers of people participating in recreational riding, including both BMX and MTB.

---

<sup>2</sup> [http://www.bikeoz.com.au/images/Documents/bike\\_sales\\_in\\_australia\\_july\\_06.pdf](http://www.bikeoz.com.au/images/Documents/bike_sales_in_australia_july_06.pdf)

<sup>3</sup> Accounts Department, Shimano Australia.

<sup>4</sup> Cycling Promotion Fund, <http://www.cyclingpromotion.com.au/content/view/498/150/>

## AUSTRALIAN BUSINESSES ONLINE

In the Issues Paper, the Commission asked:

*"Why have Australian retailers been relatively slow to take-up online trading? What impediments are there to the greater use of online trading by Australian retailers?" (p. 16)*

### ***Restrictions from suppliers***

Having recognised the growing popularity and potential for internet shopping, the initial business plan for ForTheRiders was to be solely an online retailer. However it became clear that suppliers did not, and still do not, support this business model. Many wholesalers<sup>5</sup> will supply goods only to bricks and mortar stores, making it virtually impossible to set up an online-only business in the bicycle industry.

We therefore built a business that operated from a physical store, though we still planned to make the web store the dominant part of our business. The commercial realities of competing in this arena have made this incredibly difficult. The various barriers encountered are discussed throughout this submission.

Another barrier imposed by suppliers to online retailing is the sale of complete bikes. The majority of Australian distributors<sup>6</sup> do not allow their bikes to be sold in any manner other than in store. Dealers assert that this is a legal requirement and ensures rider safety, as a qualified bicycle mechanic has assembled the bike. No specific legislation to verify this could be located.

These restrictions from suppliers mean it is almost impossible for an Australian bicycle retailer to be solely an online business. Even if they want to operate a web store, they are required to invest time and money into a physical store (which includes rent in an area suitable for retail, insurance, sales staff).

### ***Infrastructure costs***

Online retailing is often misrepresented as being a simple matter of having a web page. Setting up a user-friendly, secure, well-developed web store takes a significant amount of time, money and knowledge. It can be very costly and challenging to integrate systems (such as inventory management and customer details) between a physical store and a web store.

To set up an integrated system and website for our business incurred costs equal to over 10% of our annual expenses,<sup>7</sup> which is our second highest expense behind wages. The process took over twelve months to become operational.

---

<sup>5</sup> For example, two large suppliers with this policy are Shimano Australia and Monza Imports.

<sup>6</sup> Giant Bicycles, Monza Imports (Cube Bicycles), Specialized, Trek.

<sup>7</sup> Excluding cost of goods sold.

### ***A small market***

Compared to the European, Asian or American markets, the Australian national market is very small relative to its size (and therefore distribution costs). With so many 'local bike shops' around the country, it is not lack of access but cheaper prices that drive consumers online. If we cannot offer a reduced cost to consumers online then we cannot expect to see growth in online domestic purchases.

From our perspective as Brisbane-based retailers, we are also concerned that significant investment in an online presence may see *some* growth in sales from around the country, but also a cannibalisation of our existing Brisbane market that diminishes the value of that investment.

### ***Shipping globally***

Competition from online retailers comes in the form of 'mega stores' that ship worldwide and offer large discounts on products, such as the 'world's largest bicycle retailer' *Chain Reaction Cycles*,<sup>8</sup> *Pro Bike Kit* and *Dans Comp*. We suggest there are a number of factors that together make it incredibly difficult and costly for Australian retailers to enter this space, with little likelihood of building a profitable enterprise.

Firstly, businesses such as Chain Reaction Cycles (CRC) started as local operations in the 1980s and were able to capitalise on the densely populated domestic market to build scale (CRC is based in Ireland). They already had the scale to enable them to exert pressure on buy prices and launch ultra-competitive global operations.

Secondly, Australia's geographic location limits our ability to ship at competitive prices to a significant number of overseas destinations. While we may be able to ship to our near neighbours, these countries are limited both in terms of number and their potential as a market for high-end products. Retailers in Australia face high shipping costs both ways; the cost of getting the product from the manufacturer to Australia, which becomes factored into our buy price, and the cost of getting the product to an international purchaser. The mega-stores are generally situated in areas that are globally central (Europe, America, or in the predominantly-Asian<sup>9</sup> countries of manufacture), which reduces their shipping costs both ways.

Thirdly, despite the purported advantages of online retailing opening up a whole new market to retailers, in the bicycle retail industry we now face a situation of global oligopoly. The industry is dominated by a handful of incredibly large players who can exert significant power in keeping their buy prices and shipping costs low.

One of the few options open to Australian retailers is to move offshore and ship directly from the country of manufacture. This is increasingly occurring in a variety of retail sectors<sup>10</sup> and these moves leave a large void in the Australian economy; with significant numbers of jobs

---

<sup>8</sup> [www.chainreactioncycles.com](http://www.chainreactioncycles.com)

<sup>9</sup> The majority of bicycles and related parts are manufactured in Taiwan.

<sup>10</sup> Myer: <http://www.theage.com.au/business/gst-pushes-myer-online-to-china-20101203-18j5d.html?comments=134> ; Dymocks have suggested a move overseas: <http://www.abc.net.au/news/stories/2010/11/18/3070335.htm>

being lost to these overseas operations and lost tax revenue as these retailers move offshore to circumvent Australian tax structures.

We suggest this trend will 'snowball'; as consumers become more accustomed to lower prices and start to see these prices being offered by Australian brands they recognise, the pressure on their competitors to cut costs will drive them to do the same. This erosion of local industry is a dangerous trend for the Australian economy.

### ***A level playing field***

The existing tax exemptions for imported goods are a significant disincentive for Australian bicycle retailers to be online - this is discussed further below.

## DOMESTIC IMPACT OF OVERSEAS ONLINE TRADING

In the Issues Paper, the Commission asked:

*"How significant is the impact of online trading on domestic retail businesses?" (p. 17)*

### ***Quantifying the impact***

The three largest overseas cycling retail stores are said to ship around 1000 parcels per week into Queensland alone.<sup>11</sup> Australia is the fourth largest destination for parcels from CRC,<sup>12</sup> who are the Royal Mail's second largest customer in Ireland (behind the Government)<sup>13</sup> and who ship goods worth £48.6 million internationally each year.<sup>14</sup> While it is difficult to quantify the impact on Australian retailers, those figures indicate a significant amount of sales being lost to overseas retailers each year.

The impact is not just in lost sales. Potential customers often come in and try products on for size, or take up significant amounts of time with sales staff in order to benefit from our specialised knowledge. The potential customer is then armed with the type of personalised knowledge that is not readily available on the internet, and can comfortably purchase from one of our overseas online competitors who can significantly undercut our prices. It is only when the item breaks, or is incorrectly installed, that we see the same customer (now sporting the socks, jerseys and small accessories that are hallmarks of the online shopping experience) back for a repair or assistance.

When some customers bring their bikes in for a service, we will often find poorly fitted parts, which were purchased online and the customer has attempted to fit themselves. This can present serious safety issues. Similar safety issues arise with the ability to purchase parts overseas that are not approved under Australian safety standards, such as a variety of helmets.<sup>15</sup>

---

<sup>11</sup> Figure estimated by Australia Post employee.

<sup>12</sup> Data provided by CRC sponsored rider.

<sup>13</sup> Data provided by CRC sponsored rider.

<sup>14</sup> <http://www.bikeradar.com/road/news/article/chain-reaction-cycles-video-tour-30162>

<sup>15</sup> <http://www.productsafety.gov.au/content/index.phtml/itemId/974624?pageDefinitionItemId=970583>

## PRICE DIFFERENTIATION DOMESTICALLY AND OVERSEAS

In the Issues Paper, the Commission asked:

*"What is the extent of international price differentiation in the global marketing of branded products which impacts on Australia? What other factors explain the differences in prices between domestically and overseas sourced identical products?" (p. 17)*

### **Examples of price differentiation**

We reviewed some of the main websites who are shipping bicycle parts into Australia. Below is a sample of products which demonstrate the price differentials, resulting in our buy prices being almost as much or even more than the landed price for a consumer from an overseas website.

All prices shown below are regular prices and are not special sale prices. These prices are for the identical product and prices are those supplied by Australian distributors.

#### Shimano XTR M980 Crankset

CRC (delivered):	\$446.66
Wiggle (delivered):	\$541.18
Our buy price:	\$601.00 (ex-GST) + \$12 freight inwards (+ freight to a customer).

#### SRAM XX Rear Derailleur

CRC (delivered):	\$247.98
Wiggle (delivered):	\$295.17
Our buy price:	\$221.59 (ex-GST) (+ freight to a customer).

#### Five Ten Impact MTB Shoe

CRC (delivered):	\$135.98
Wiggle (delivered):	\$110.36
Our buy price:	\$116.35 (ex-GST) (+ freight to a customer).

These examples demonstrate the realities faced by Australian bicycle retailers. We have no control over these buy prices and it is difficult to maintain a competitive margin (to cover overheads and still maintain profitability) when overseas retailers can so substantially undercut prices. It is therefore difficult to understand the advantage being given to overseas retailers through the \$1000 import threshold.

## LOW VALUE IMPORTATION THRESHOLD

In the Issues Paper, the Commission asked:

*"What evidence is there that Australian retail businesses are being adversely impacted by the low value importation threshold? To what extent does the threshold motivate Australian consumers to purchase online from overseas suppliers? What other factors explain the differences in prices between domestically and overseas sourced products?"*  
(p. 24)

### **Targeting Australian consumers**

A trend we have observed in the last few years is a significant increase in targeted marketing from the international mega retailers to Australian consumers in Australian dollars. Local forums, message boards, and online communities are increasingly filled with advertising from these large retailers. These local forums have traditionally been focused on the local riding scene and advertising has been for local bike shops.

Print magazines have up until this point resisted including advertising from international retailers, however we are told they are approached "all the time" by these companies.<sup>16</sup>

Emailing marketing from companies such as CRC is geographically targeted, with prices to Australian consumers listed in Australian dollars.<sup>17</sup>

The presence of these international retailers in these traditionally local spaces indicates that they view Australia as a viable market and are prepared to invest in advertising that is specific to Australia.

### **Delivery**

This submission previously highlighted the geographical benefits to some of our large online competitors and the manner in which they can use this to lower shipping costs. Their scale also allows them to drive down, and presumably also absorb, shipping costs, thus keeping the landed cost of goods to a consumer low.

International retailers frequently offer heavily discounted (or free) shipping to Australia. Pro Bike Kit (a large online retailer based in the UK) offers free shipping on orders over \$50, while Wiggle (another large UK based mail-order bicycle retailer) offers free delivery on orders over \$82. Wiggle also features a special note on their website about shipping to Australia, showing they are well aware of the low-value import threshold:<sup>18</sup>

**"Local GST:** Our understanding is that this is not typically applied although you need to check the local situation carefully."<sup>19</sup>

<sup>16</sup> Jonathon Taylor, Editor Revolution MTB Magazine.

<sup>17</sup> <http://www.ChainReactionCycles.com/EmailPreview.aspx?EmailID=1141&PartnerID=7415>

<sup>18</sup> [http://www.wiggle.co.uk/h/option/euro\\_delivery\\_info#Australia](http://www.wiggle.co.uk/h/option/euro_delivery_info#Australia)

<sup>19</sup> A later less prominent notation clarifies that taxes and duty may be payable for items over \$1000. However some of the information provided, such as about the duty that may be levied on parts and accessories, is understated.



CRC offers free shipping for parcels over \$400. For those parcels that do not meet that threshold, shipping is still incredibly cheap. For example, a set of handlebars can be shipped from CRC in the UK to Brisbane, via Royal Mail, for AU\$7.68. Using Australia Post, the minimum cost is \$8 to get those same handlebars our Brisbane metro store to a Brisbane CBD location. To send to a regional interstate location is minimum \$12.50.

### ***Quantifying the impact on our business***

While it is almost impossible to determine exactly how many sales are lost to imports from overseas, it is possible to look at our inventory and sales profiles (which would be reasonably indicative of industry averages).

- 98.2% of our stock on hand is priced at less than \$1100.<sup>20</sup>
- Our average sale value over the last twelve months was \$101.74.
- 98.4% of sales (by quantity) were transactions less than \$1100.

Given the size, scale and global reach of our international competitors, it is fair to assume that Australian bicycle retailers are at risk of adverse impact from the low value importation threshold.

---

<sup>20</sup> A \$1100 threshold was used to reflect the value the comparative value of an imported item, which is currently not subject to GST. Due to differing values in duties, this was not incorporated.

## ADMINISTRATION AND THE COLLECTION OF DUTIES AND TAXES

In the Issues Paper, the Commission asked:

*"How do other countries seek to strike the right balance between compliance with their threshold, revenue collection and administrative efficiency? What technological developments could be employed to reduce administrative collection costs, particularly given international postal agreements? How might continued growth of overseas online shopping affect existing border control and cost recovery arrangements?" (p. 24).*

### A 'burden'

Prime Minister Gillard has stated that collecting GST from parcels less than \$1000 would "cost more in administrative costs than it would recover in revenue."<sup>21</sup>

We assume that this statement refers to a process that would be labour intensive and would require physical examination of every parcel (costs of up to \$100+/parcel<sup>22</sup> are otherwise difficult to rationalise).

International agreements are already in place which facilitate administering such a system in a way that reduces administrative costs. The 191 member countries of the Universal Postal Union (including Australia) agree that all outbound parcels to member countries must display a completed CN 22 or CN 23. This declaration facilitates assessment of applicable taxes and duties without undue administrative burden.

Collecting duties on these parcels does not increase the number of parcels that are physically handled. This means that the majority of expenditure to expand capacity within the system will be to bring on more staff to process and collect payments. This direct investment in Australian jobs complements the indirect benefits to the labour market of supporting Australian retailers.

Prime Minister Gillard has also said that "I would be very reluctant to see Australians who are facing cost of living pressures not able to access shopping on the internet in the way that they access it now".<sup>23</sup> While focusing on the consumer and the benefit derived from escaping the consumption tax and other import duties when they send their money overseas to purchase goods, this view ignores the realities facing Australian retailers. These have been addressed earlier in the submission, but include the duties and related fees paid by importers, which are passed on in the form of increased wholesale prices to retailers. Ultimately, it is these costs which are hitting Australian consumers.

It also leads on to the illogical injustice of requiring Australian retailers to collect GST on *all* sales on behalf of the Government, while the Government claims it is too hard for they themselves to collect GST on purchases from overseas providers (who are making *no contribution* to the Australia economy).

<sup>21</sup> <http://www.smh.com.au/small-business/trends/put-gst-on-all-imports-retail-union-20110509-1eepk.html#ixzz1MUNJLdgZ>

<sup>22</sup> \$100 GST, plus the value of any applicable duties, on a \$1000 parcel.

<sup>23</sup> <http://www.abc.net.au/pm/content/2011/s3109921.htm>

If the Government is intent on delivering this tax break to consumers, and views the payment of GST and duties on goods less than \$1000 as not being of sufficient value to cover the costs of collecting this revenue, then it must consider why no such reprieve from GST is offered for purchases of goods for less than \$1000 *within* Australia?

### ***Assessing and collecting taxes and duties***

We suggest that the use of online payment solutions has become so commonplace that it would be a natural system choice for the management of taxes and duties of any amount for both commercial and individual customers. Australian Customs could expand the use of existing systems which currently allow for registration of accounts, online payment and direct-debiting.

When a parcel arrives into the country, Australian Customs simply:

1. Calculates the taxes and duties applicable based on the information provided on the CN22 form attached to the outside of the parcel.
2. Matches the addressee against the database (using name and address details).
3. Charges the customer to their registered credit card or prepaid account (which they could credit using payment methods such as BPAY).
4. Parcel can be delivered immediately, without any storage and with minimal administration and handling.

Not all customers will be registered with the system, and first time or occasional users (whose parcels may need to be stored) could be sent a notification similar to the current process for parcels held by delivery companies or for parcels over \$1000.

Any deviations from the automated procedure (such as an addressee not being registered, or the CN22 form not be accurately completed) would be classed as 'avoidable administrative costs' which would be chargeable to the consumer. An analogous process is the tag system on toll bridges and the administrative fees charged for a manual match and posting of a bill.

Swiss Post collects duties and taxes on most parcels.<sup>24</sup> Their system involves passing on avoidable administrative costs to the recipient, such as:

- Examination fee: CHF 6 (AU \$6.37) for opening a parcel if the seller does not correctly fill out the CN22 form.
- Storage fee: CHF 10 (AU \$10.62) for parcels that need to be detained.

An alternative system could utilise the income tax process. Consumers may choose to register their names and addresses, along with their Tax File Number (TFN), with Australian Customs. Relevant charges can be levied against the TFN and included in the income tax process each financial year.

There are a variety of technologies that can be utilised to expedite this process, many of which are already employed by Australia Post and other delivery companies in Australia. OCR (optical character recognition) is currently being used by Australia Post to automatically read the full address information on hand-addressed mail.<sup>25</sup>

<sup>24</sup> Parcels with a duty payable of less than CHF 5 (AU \$5.31) are exempt.

<sup>25</sup> Australia Post, 'Address Presentation Standards', <http://auspost.com.au/personal/addressing-guidelines.html>

SMS notifications and online payment gateways could also be utilised to ensure a cost-effective and smooth system. The process could be handled exclusively by Australian Customs, or in partnership with other providers.

### ***Enforcing payment of taxes and duties***

We understand that examining every parcel would be labour intensive and therefore potentially costly. To strike a balance, we support the recommendation in the submission from Star Audio Visual Association Inc:

*"There is a distinction between assessing every single package that comes into the country and merely removing the exemption. One option would be to allow purchasers to self-assess GST with heavy fines for fraudulent assessments. While a percentage of purchasers would no doubt take advantage of this process, the majority of purchasers would declare and pay the GST/duty to comply with the law. Customs need only enforce a sample of shipments to deter purchasers from breaking the law in this area."*

We suggest this method need not result in an undue administrative burden and that the majority of purchasers would accurately declare the contents and value of their parcels. The impact on the local economy would be positive, by removing the unfair advantage currently given to overseas businesses.

This method is consistent with other taxation processes, such as income tax assessment, where the individual is required to self-assess and declare their taxable income and faces significant penalties if audited and found to have not submitted an accurate assessment.

## CONCLUSION

This submission has addressed the questions before the Commission from the perspective of an Australian bicycle retailer. While our examples and experiences are industry-specific, we believe that there are many other industries that are under similar pressures from the international market.

These pressures are growing as online retailing increases and Australia retailers struggle to compete with the aggressive, large-scale international vendors. To put small monetary gains for the consumer ahead of supporting and building long-term sustainable industries in Australia is shortsighted and ignores the realities of the new global market.

As Australian retailers, we are not advocating concessions or protectionism for ourselves. We do ask that the government provide a level playing field for our retailers – domestic and international. This means enforcing taxes and duties equally with no exceptions. We suggest that there is a wide range of affordable and readily available technologies to facilitate such a process.