Lightswitch Consulting

Connecting you to growth.

Why do Australian Supermarkets use ‘tricks’ to disguise price rises?

Explainer

Phantom brands, ‘seasonal’ discounts and shrinkflation: the pricing tricks used by Australian supermarkets

Coles and Woolworths are accused of inflating prices – but those aren't the only tactics hurting shoppers

- Follow our Australia news live blog for latest updates
- Get our breaking news email, free app or daily news podcast

Supermarkets are using tags on normally priced products that are designed to make them look like specials. Photograph: Jacobs Stock Photography Ltd/Getty Images

https://www.theguardian.com/business/2024/sep/25/phantom-brands-seasonal-discounts-and-shrinkflation-the-pricing-tricks-used-by-australian-supermarkets?CMP=Share_iOSApp_Other

Well, that's an interesting story involving a flashback to the 90’s, a newly imported head of coles, a fairly tale, some dubious retailer practices, a global pandemic and a quote from Amy Shark.

‘You what now? ‘

Level 6, 201 Kent Street, Sydney, NSW 2000 Australia
www.lightswitchconsulting.com
hello@lightswitchconsulting.com

Read on and all shall be revealed…

Back in the late 90's, I was working for Kraft Foods in the UK. British retailers had clocked onto the fact they could raid suppliers budgets to boost profit margins, which were always under pressure. They had a few tricks up their sleeve to grab cash, or delay expenses. One of which was straight out blackmail – 'spend £1m on Computers for Schools next month or we delist half your range' (True story). Another was point blank refusing to take a price increase. Or demanding of suppliers that they would only take the price increase if the supplier negotiated that that every retailer in the UK change their retail prices on the same date. Somewhat ironic given that retailers manage retail pricing. Suppliers whose teams failed to perform the required alignment gymnastics promptly received invoices for lost sales and profit, which were then deducted from payments due for goods bought by the supermarkets. Fun times!.

Australia at this time was much more civil. Retailers understood that COGs went up due to inflation, and would entertain a reasonable (thank you [Neil Rechlin]) conversation about price increases. Tools like pack/price architecture (reducing cost by changing pack size instead of putting price up) were beginning to be used but not widespread. As a result, retail prices increased gently each year, and suppliers supported retailers with regular price discounts. Everyone was kinda happy.

One of the retailers who was working in the UK in the 90's was John Durkin. After 17 years working in Safeway, and some time at Carphone Warehouse, he moved down under to run coles in 2014. At this time, AU retailers employing brits was quite the fashion - a lot of talent migrated south in the early 2000's. The UK market is generally considered about 5-10 years ahead of Australia, and it was a good chance to import ideas and practices which had worked in the also-very-concentrated UK grocery market.

John achieved many things at coles, but he is mostly remembered in the grocery trade for his description of the AU grocery trade as 'Treasure Island'. Which was widely interpreted that there was ample opportunity to raid supplier P&L's to boost retailer profit using tools which had been in use in the UK for the last 5-10 years. Which they proceeded to do (who can forget 'cliffing'?).

It was around this time that both coles and WW started the 'no price increases' conversations with suppliers.

Any supplier who wanted to increase cost price had to jump through a series of hoops, which included sharing your COGS down to source documentation for each ingredient, proving that your costs had indeed increased. Retailers had whole teams of people reviewing the price increase submissions and comparing costs. If the retailer team thought a supplier was paying too much for an ingredient, they would tell you so, and refuse to accept your COGS increase. If a supplier insisted on raising price, without 'dealing it back' via further trade spend, retaliatory action was often taken, and your brands were marginalised in any number of fun ways.

The whole process took 12 weeks, with all other everyday trading discussions put on hold until the 'price issue' was 'resolved'. Unsurprisingly, suppliers opted for cutting their own costs (headcount, training, investment, wage increases) vs fighting for a quarter of the year with the very retail partners they depended upon for sales. And as a result, inventive tactics to 'get price through' become much more common.

However, the tactics didn't fully release the COGS pressure in supplier land. And this pressure continued to build up on the P&L's of grocery suppliers Australia wide. Meanwhile, the Grocers slugged it out with $1 milk and other wonderful bargains designed to entice shoppers to drive to their stores.

Come 2020, and CV-19 royally stuffed the same global supply chains which had been meticulously cost-optimised to the n^{th} degree. Huge COGS changes were recognised by retailers who were struggling to run shops. So price increases were on the table again. To be fair, such was the tension, it probably would have resulting in physical violence in the meeting rooms if the position did not change.
Actual supply was also patchy, so demand was smoothed out by reducing price discounts. This change in position, and the resulting switch to working together to solve common problems caused by CV19, was seen by some as a major step forward in commercial relationships within the industry.

During this time, suppliers, who had not been able to recover COGS increases for years, now had an open gate. And like a dam when the floodgates are opened, the price increases from suppliers flowed. Stories of price increases of 15-20% or more over 18 months are not uncommon. That's not to suggest for moment that these increases in cost were not justified by CV19, or the preceding years. The pressure had been building for quite a while. And supply chains were very very broken! And bear in mind that price increases are good for the retailers bottom line too – they make more profit when prices go up.

What's not good, as Australia is now finding out, is a high rate of cost-price inflation over a relatively small period of time, coinciding with interest rates which are 2x the average of the preceding 10 years.

And perhaps unsurprisingly, We The Australian People are now asking WTAF?

The kick in the arse for grocery retailers is an erosion of public trust – which is now being followed by a general request for government to 'do something' .

This is going to be an interesting ride…

Level 6, 201 Kent Street, Sydney, NSW 2000 Australia
www.lightswitchconsulting.com
hello@lightswitchconsulting.com

Lightswitch Consulting

Connecting you to growth.

But, as Amy Shark mentions on the track 'Babe' from her latest album – 'Here We Are'.

The question is how do we move forward?

Complex problems sometimes require simple answers. Perhaps the most sensible approach would be to simply agree that suppliers can choose to pass cost increases to retailers, equal to CPI, within a 12 month period of that CPI being announced by the ABS, without question or sanction.

- The price increase could be effective to all orders placed in 4 weeks time from the price increase notice being received.
- The retailer could not discriminate in any way against the supplier for raising price up to CPI. If they do, the case is reviewed by an independent body, and retailer is sanctioned if found to be guilty.
- Any increases over and above CPI would be subject to whatever scrutiny and negotiation each party was happy to have. Although I'd suggest that the practice of retailers requesting sharing of confidential information on cost prices from suppliers should be illegal and subject to penalties.

This approach would have quite a few benefits.

- It would solve the 'dam bursting' cost-price inflation pressure building up again, only to be released at the next crisis point, or in the meantime, leaking out through pricing practices which may erode shopper trust and raise the collective eyebrows of the ACCC.

- It would allow a gentle upward movement of prices over a period of time. Households would have time to adjust their budgets.

- Federal regulations would ensure that this applied to the whole FMCG industry and would stop certain retailers 'opting out' in order to improve their competitive position.

- It would allow retailers and supplier to recover cost increases each year – and afford wage increases if they choose to make those changes.

- Perhaps most importantly, it might also re-invigorate investment in the AU FMCG industry again. We sorely need this in Australia.. Food production globally is under threat. Growing, shipping and selling food is one of the highest emitters of CO_2, and food security is rapidly becoming one of the major issues of this century. Australia is essentially a farm and a few mines on a continent. We need our food industry to be bulletproof. Stimulating industry investment will provide jobs, innovation, and improved yield.

Level 6, 201 Kent Street, Sydney, NSW 2000 Australia
www.lightswitchconsulting.com
hello@lightswitchconsulting.com

There is a pathway to allowing this type of change to happen via the formalising of the FGCOC to be specific about acceptable practices involving cost price increases. It would take a bit of work to put it in place but it's not impossible.

Either way, I'm sure that the FMCG industry as a whole will adapt to the crisis of faith it finds itself in.
Hopefully the adaption doesn't involve a lot of finger pointing at suppliers, and decisions are made which allow retailers to build back some public trust, thus avoiding any future WTAF moments from concerned shoppers, journalists and inevitably, the ACCC.

Level 6, 201 Kent Street, Sydney, NSW 2000 Australia
www.lightswitchconsulting.com
hello@lightswitchconsulting.com