

Hey, Big Spenders! Whatever Happened to Consumer Confidence?

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There is no shortage of explanations for the alarming state of Australian retail markets. Reserve Bank governor Glenn Stevens puts it down to what he calls the "cautious consumer". Many shop owners claim a tax-free threshold for overseas' goods puts retailers at a commercial disadvantage in an era of burgeoning international online sales. Then there's the impact of volatile international markets, the US debt crisis, surging household costs, a high Australian dollar, the federal government's proposed carbon tax, interest rate fears ... the list goes on.



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Whatever the cause, there is no argument that Australian retailers are facing some of their toughest trading conditions in decades. August figures from the Australian Bureau of Statistics show retail sales rose a paltry 2.6% during 2010-11, the worst result since a national recession in 1962 – including the global financial crisis period of 2008-09.

As consumers go on a veritable spending strike, retail industry heavyweights such as Harvey Norman boss Gerry Harvey are predicting a grim future for some Australian technology retailers, among others. Now the big question is whether the downturn is simply a cyclical trend that will be corrected, if and when international economies rebound, or whether it is indicative of a long-term change in consumer spending attitudes.

[Mark Uncles](#), a professor of marketing and branding expert at the Australian School of Business, says markets are clearly caught in a fog. "I think we can say it's a flat market when you have major retailers like Harvey Norman sounding quite gloomy about the prospects for retailing over the coming years," he says. "After all, they pride themselves on being close to customers and are well placed to gauge consumer sentiment."

Perhaps what's most worrying for store operators is a change in people's savings ratios. Unlike China, for example, where a strong savings ethic has traditionally been part of the culture, Australians have in recent decades been big spenders who rely on credit. In the 1980s, Australia's net saving rate was more than 15% but steadily fell until a decade ago, with households on average spending about 2% more than they were earning. That has turned again to the extent that a February 2011 report from the Reserve Bank indicated Australians are now saving about 10% of their disposable income.

"It's not just that people are looking for bargains, but now they're not even spending all the money they have," Uncles says. "There's now greater readiness to save for a rainy day. That means that some purchasing power is taken out of the retail side of the economy. This is a big change and it puts Australia on a different path from where it used to be."

Most of the signs for retailers in recent months have been poor on the back of the collapse of retail chains, such as booksellers Borders and Angus & Robertson, and fashion businesses, Colorado and Bettina Liano.

The Australian Bureau of Statistics (ABS) revealed that sales for the normally strong month of June had fallen 0.1% – following a 0.6% drop in May – to a seasonally adjusted A\$20.5 billion. In a further indication of the troubles confronting major brands such as David Jones and Myer, department store sales suffered the biggest monthly fall for all industry groups, dropping 3.2% in June and 4.9% over the year.

Not surprisingly, the Westpac-Melbourne Institute Index of Consumer Sentiment reflects such negativity, with consumer sentiment falling 3.5% in August and reaching a 27-month low of 89.6, taking the nation back to global financial crisis levels, but picked up again in September. Angela Kidson, an industry analyst at business research firm IBISWorld, says the retail slump in Australia has been greatly exaggerated.

Although sales are undeniably slow in many sectors, Kidson notes that ABS figures put annual retail growth at 2.6% compared with gross domestic product growth of about 2.4% over the same period. "Retail is tracking slightly above economic growth so, in the context of the current economic situation, retail is really not doing too badly at all. It is a slow level of growth, but it's not dire straits by any means."

Move to Moderation

Kidson believes there has been an adjustment to "debt-fuelled" spending in the years leading up to the global financial crisis in 2008. "Now what we're seeing is moderation back to a lower level of growth."

[Richard Holden](#), a professor of economics at the Australian School of Business, agrees that caution is required in assessing present market conditions. "With all these 50-year big, bad pronouncements, one needs to be a little bit careful," he says. "These troubles and uncertainties can have a really large impact on how people feel about things. Consumer confidence is all dependent on quite subtle things, like 'how do I think the economy worldwide is going to grow in the future' and that can have pretty big implications, particularly for the retail sector."

Everything from the US debt crisis to interest rate uncertainty and the federal government's proposed carbon tax has been held up as the cause of the retail slump. The Productivity Commission, an independent government research and advisory body, also suggests inflexible labour laws, zoning regulations and trading hour restrictions are playing a part.

While Holden doubts the proposed carbon tax has played a genuine role, he believes uncertainty over interest rates – with media reports simultaneously predicting rises and falls later this year – is a factor. "It's that volatility which makes people wonder, 'should I buy a house?' This sort of uncertainty causes people to not want to buy the big-ticket items. Houses are the obvious example, but it's also fridges, cars and other durable goods."

According to Kidson, many consumers are still suffering from the hangover of the global financial crisis. With more international market uncertainty in recent months contributing to rollercoaster share market rides, they are nervous. "People are readjusting and you can see that consumers are being more value-conscious, they're more cautious," Kidson says. While statistics showed a slight dip in household disposable income, "consumers still have money ... so it's really driven by consumer sentiment; it's not a lack of means."

Kidson says the aforementioned savings ratios are a real sign of the times. "That's a real shift and consumers are just choosing to pay down their debt and to save rather than spend on retail."

A blanket appraisal of retail markets should be avoided, advises Kidson. While there is no doubt that department stores have taken a significant hit as people rein in discretionary spending, sales of pharmaceutical, cosmetic and toiletry goods rose 6.9% in the year to June 2011.

The biggest talking point has been the impact of online retailing and how the strong Australian dollar has led to a flight of activity on international sites – and this issue is key to whether the present downturn is just cyclical or if it reflects a long-term change in attitudes to spending.

Uncles believes online sales are forever changing consumer habits. "If it was just the financial crisis, we might say this is like previous recessions," he says. "Countries have had recessions in the past and retailers have pulled through. But this time around, on top of that is the shift to online spending, together with the phenomenon of people doing offline or online research and then purchasing online."

The "try-before-you-buy" phenomenon among online shoppers is a nightmare for bricks and mortar retailers: for instance, camera buyers check web reviews of products to narrow down their options; then they test models in a physical store; before going home and buying a camera over the Internet after

comparing the cheapest prices across the web. "That's not a very good scenario for a retailer which has invested millions of dollars in physical assets and a sales force, and which historically has had high margins," Uncles says.

The power of the Internet can be seen in a new Deloitte Access Economics report, [*The Connected Continent: How the Internet is Transforming Australia's Economy*](#). It estimates that the Internet contributed A\$50 billion, or 3.6% of Australia's GDP in 2010, with that impact set to further boom. In trying to evaluate the full dollar value of the Internet to Australia, the researchers claimed it already rivals iron ore resources, with the biggest aspect being online shopping.

Deloitte Access Economics suggests Australian e-commerce is witnessing year-on-year growth of about 11%, and the value of online shopping in Australia could reach about A\$26 billion by 2016.

Falling in Line Online

The fascinating thing for market watchers now is seeing how retailers react. The Australian National Retailers Association is calling for an end to restrictions on trading hours to enable stores to better compete with 24-hour online shopping.

Significantly, some traditional bricks-and-mortar retailers are ramping up their online presences. After a controversial campaign led by Myer, David Jones, Target and Harvey Norman to try to force the government to drop a goods and services tax (GST) exemption on international website sales of less than A\$1000, their approach appears to be that if you cannot beat them, join them. Harvey Norman is establishing a new online retail store, while fashion retailer Country Road is trialling free deliveries for online sales.

Kidson believes traditional retailers have little choice but to pursue a meaningful online presence. "Online retail is a trend that's here to stay." But established retailers do not have to ditch their physical presence, she says. Many purchasers will continue to want to see a product in a store and try it out. "It's not a matter of one or the other ... The Internet can be used in conjunction with existing stores to drive growth and expand your market."

Uncles also supports the move, saying it's not too late for bricks-and-mortar players to catch up with nimble Internet-only competitors. "One of the things about online is that people compare prices. If a reputable brand, like Harvey Norman or Country Road, comes along and offers something competitive, then it is likely to be considered as much as anybody else."

The "greater danger" for such brands, according to Uncles, is the impact an online model will have for their offline business. A balancing act will occur if a retailer sells high-margin goods in its physical stores while offering bargains over the Internet. "It would become very apparent to consumers that this retailer, who they know of through its physical assets, is also now providing similar or identical products online at much more competitive prices."

The other headache is retailers' inexorable shift towards seemingly continuous sales. While Uncles says sales are a valid tool for an end-of-season clearout or a post-Christmas bonanza, having too many sales can devalue the retail brand. "The trouble with the perception of continual sales is that customers' reference prices go down, even for new stock ... Unfortunately, retailers seem to have got themselves into that position to the extent that last year even before Christmas we had sales. It is a precarious situation from the viewpoint of putting pressure on retail margins and longer-term survival."

While the headlines have been doom and gloom for retailers, there are always winners as markets shift or transform. It is clear that some online comparison sites are doing well. Think Webjet (airfares), carsales.com.au (motor vehicles) or Wotif (accommodation).

A discount retailer such as ALDI is also seemingly well placed because it has always structured its brand around value for money and discounting and has not had to change that model in present markets. Then there is the impact of the rush to online sales that will require delivery services, which is good news for Australia Post, DHL and other courier services.

With an eye to the future, Holden expects ongoing market uncertainty to contribute to skittish consumers

for some time.

Will US ructions contribute to a new financial crisis? Will rates go up? Will they go down?

"People don't know what's going to happen with something that's really important, like how much they are going to pay on their mortgage next month," Holden says. "The fact there is so much uncertainty gives people pause and I think that's why it's likely to be a very volatile time and retail, of course, bears the real brunt of that."

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