

28 February 2024

Food and Grocery Code of Conduct Review
The Treasury
By email to: GroceryCodeReview@treasury.gov.au

Dear Dr Emerson,

Re: Price Gouging Inquiry Final Report and Recommendations on the Food and Grocery Code

1. Final Report Attached

The Australian Council of Trade Unions (ACTU) is pleased to submit the final report of the Inquiry into price gouging and unfair pricing practices, which includes recommendations we support to make mandatory the Food and Grocery Code. The report is attached for your reference.

2. Concerns Regarding the Voluntary System

While we acknowledge the government's efforts to address unfair pricing practices through the Food and Grocery Code, the ACTU has significant concerns regarding the effectiveness of the current voluntary system.

We believe that the significant power imbalance between suppliers to supermarkets and the major supermarkets themselves is not adequately addressed by a voluntary model. This imbalance creates an environment susceptible to misuses of market power, potential retribution against suppliers who raise concerns, and disincentivizes the use of the code by participants. The code structure should also be reviewed, as raising grievances under this system carry risks for suppliers who may have retribution by the supermarkets for exercising their rights. Priority should be given to ensuring that no retributive action can be taken, and changes to the Governance of the code, including creating a tripartite mechanism should be considered.

3. Expanding the Code's Scope

The ACTU urges the government to expand the code's scope to include forestry, paper, and tissue products. These sectors have similar experiences to other food and grocery types covered by the code, and their inclusion would provide much-needed protections these businesses and the workers within them.

4. Indicating and Addressing Labour Issues

Furthermore, the ACTU recommends that unions be granted the ability to raise concerns about potential labour issues stemming from unfair contracts within the code's framework. Specifically, we advocate for the code to allow unions to raise concerns where unfair contracts threaten the sustainability of operations, or that the market structure is leading to poor labour outcomes.

We believe that addressing these concerns through significant reform and strengthening the code's governance and operation will be crucial in effectively preventing price gouging, protecting consumers, and ensuring a fairer and more balanced market environment.

Thank you for your time and consideration,



Joseph Mitchell
Assistant Secretary
Australian Council of Trade Unions

**Inquiry into price gouging and
unfair pricing practices**
Chaired by Professor Allan Fels AO.

Reporting to the Australian Council of Trade Unions.

INQUIRY INTO PRICE GOUGING AND UNFAIR PRICING PRACTICES

Final report
February 2024

1. FOREWORD



I have welcomed the opportunity to chair this inquiry for three reasons.

Firstly, there has been much discussion about inflation and its causes including monetary and fiscal policy, international factors, wages, supply chain disruption and war. However, there is hardly any discussion that looks at the actual prices charged to consumers, the processes by which they are set, the profit margins and their possible contribution to inflation.

Secondly, there is also much discussion about market power and its harms. But there is very little discussion of any policies or actions that might be taken to deal with the main harm: high prices.

Unreasonably high prices are not prohibited by competition law. The ACCC, worthy though it is, is restricted to looking at unlawful anti-competitive agreements - for example, when competitors agree on prices. If two firms, for example, coordinate their prices without any illegal communication, that behaviour is outside the scope of the Act. If governments take actions which have the effect of raising prices, that is also outside the scope of the Australian Competition and Consumer Act.

In short, firms are free to charge as much as they like. They can price gouge lawfully as long as there is no unlawful collusion. This has given rise to a policy gap – there is no set of government policies

about excessive prices. This report provides an opportunity to examine whether this should be the case at a time when Australians are so concerned about the cost of living and the impact of prices on their lives.

Thirdly, I am pleased to be engaged with the ACTU in a prices inquiry because the concern of the Trade Union movement is the impact of prices on the costs of living of ordinary Australians. It has been valuable to hear from ordinary people in this inquiry rather than the ‘usual suspects’ that is businesses and business organisations making economic submissions about their prices.

Traditionally, the term price gouging has referred to situations where sellers exploit a shortage of essential goods and services to raise prices to excessive levels. However, in the public mind there is a wider meaning of the term: prices that significantly exceed levels that would occur if there was competition. Such prices substantially exceed costs of supply and a reasonable level of profit.

What we have seen over recent years is a dramatic increase in costs paid by consumers.

Some of the highest price increases occur in sectors which are characterised by having disproportionate market power, a level of power over their consumers, or a level of monopsony power over their supply chain and workforce.

At the same time as consumers experience significant increases in costs. Across food and grocery, energy, and financial services corporate profits are up.

Normally, inflation is a distributed experience, and the experience of those without market power being both squeezed on the supply and demand side is evidence of that. Some of Australia's largest businesses, often supplying inelastic goods, are maintaining or even increasing margins in response to the global inflationary episode.

This is a situation that warrants further investigation.

In particular, it warrants investigation of the state of competition in Australia and of the associated regulatory settings and to learn from the experience of ordinary people as to the impact of these matters. In short, if there is a high price, it usually pays to investigate its causes – typically a lack of competition or a market shortcoming – and possible remedies.

During this inquiry for example it was observed that electric vehicle prices in New Zealand are considerably lower than in Australia. In probing the reasons, it was found that the difference is due to a little known unwarranted import restriction in Australia that does not apply in New Zealand. This explains why prices on electric vehicles are much higher than they should be.

The inquiry is very timely.

The world is facing an inflationary episode. The goal of central banks and governments across the world is to drive down the rate of inflation to a more sustainable level. While there has been an enormous amount of public discourse on the contribution of wages and employment to inflation, too little discussion has been on the role price setters have on broader inflation outcomes.

The Governor of the Reserve Bank of Australia, Michelle Bullock, has noted that the inflation Australia is experiencing now is 'homegrown.' This declaration makes the examination of price-setting behaviour by domestic firms more important, as we cannot simply say that prices have increased elsewhere and are simply being passed on. The exercise of market power and limits on competition in specific markets have exacerbated what began as a global problem.

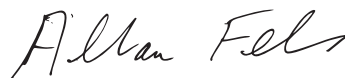
This inquiry has conducted 5 public hearings, received over 750 public submissions and more

than 20 detailed contributions from academics, experts, think tanks, unions, businesses, and their representatives.

These diverse perspectives are vital for a comprehensive understanding of the issues. The public hearings in Melbourne, Sydney, Adelaide, Cairns, and Canberra have allowed us to directly engage with the community and hear a wide range of experiences and insights. These voluntary contributions have deeply enriched the inquiry.

As I stated when I agreed to conduct this inquiry, this is a serious examination of prices and competition in Australia.

This report summarises the key policy issues and draws on the submissions to develop a set of recommendations on price and competition policy which, if adopted, would substantially improve competition and decrease the price pressure faced by ordinary families.



Prof. Allan Fels AO
Chair

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3. EXECUTIVE SUMMARY

The greatest concern of Australians is the cost of living. It has two components: incomes and prices.

Prices in Australia are often too high reflecting the many markets where there is less than fully effective competition.

Not only are many consumers overcharged continuously but 'profit push' pricing has added significantly to inflation in recent times.

There is currently a gap in government policy. It does not pay sufficient attention to high prices. It needs to. It needs to investigate and expose their causes and, as far as possible, remedy the problems: ineffective competition, vulnerable consumers, and exploitative business pricing practices.

This report examines the much neglected topics of price levels and the methods by which prices are set (including profit mark ups).

It begins by examining the impact of high prices and inflation on the cost of living especially of persons on low incomes.

Then it reviews:

- The impact of high prices on inflation;
- Business pricing practices that take advantage of limited competition to extract the maximum possible dollars from the consumer;
- Some case studies of particular industries where there is a strong suspicion or more of price gouging.

PRICES AND INFLATION

This report concludes that business pricing has added significantly to inflation in recent times.

'Profit push' or 'sellers inflation' has occurred against a background of high corporate concentration and is reflected in the surge of corporate profits and the rise in the profit share of Gross Domestic Product. There is much support for the view that prices have added much to inflation. This is to be found in research from OECD, IMF, BIS, European Commission, European Central Bank, US Federal Reserve Bank, Bank of England and many think tanks globally and locally and many detailed research studies. Claims that the rise in profit share in Australia as explained by mining do not hold up. The profits share excluding mining has risen and energy and other prices associated with mining have been a very significant contributor to Australian inflation.

The impact of inflation has been immense. Unique to this inquiry is the submissions and representations from everyday Australians. We have heard stories of real hardship and sacrifice to make ends meet.

BUSINESS PRICING PRACTICES

The report analyses a selection of exploitative business pricing practices that enable the extraction of extra dollars from consumers in a way that would not be possible in markets that are competitive, properly informed and that enable overcharged consumers to readily switch from one supplier to another.

The fact that there is a quite widespread lack of competition in Australian markets means that pricing practices that might be accepted in very competitive markets are unduly exploitative of consumers in that setting.

Loyalty taxes set initial prices low and then sharply increase them in subsequent years when consumers cannot easily detect, question, or renegotiate them and where the 'transaction costs' of changing to other competitors are high. Examples come from banking, insurance, energy, and other areas.

Loyalty schemes are often low cost means of retaining and exploiting consumers by providing them with low value rewards of dubious benefit. These schemes are also often badly run.

Drip pricing where firms only advertise part of a product's price and reveal other prices later as the customer goes through the buying process is spreading including in airlines, accommodation, entertainment, pre-paid phone charges, credit cards and others.

Excuse-flation where general inflation provides camouflage for businesses to raise prices without justification is also more prevalent in the current environment. As inflation starts to fall excessive inflationary expectations and future cost increases can be built into prices.

Confusion pricing involves confusing consumers with a myriad of complex price structures and plans making price comparisons difficult and dulling price competition. It occurs more and more in areas such as telecommunications, financial or maintenance services and other fields.

Asymmetric or 'rockets and feathers' pricing is of much concern in the current environment especially as inflation is starting to come down. When costs rise prices go up quickly 'like a rocket' but when costs fall prices fall slowly 'like a feather falling to the ground'. This practice of delaying price falls when costs have fallen can be very profitable for businesses. A recent example concerned meat prices when prices paid to farmers for lamb fell but retail prices did not, at least until there was publicity including from this inquiry about the delay.

Algorithmic pricing is the practice of using algorithms to set prices automatically (but taking account of competitor responses) raises issues about whether this reduces price competition and is analogous to cartel pricing.

Price discrimination which in its simplest form involves charging different consumers different prices for the same product enables businesses to set prices according to how much each consumer is willing and able to pay. It takes many forms. It is enabled by a lack of competition. If there were competition charging high prices to customers who wish to or have to pay higher prices would not be possible because competitors would bring those prices down to normal levels. This report identifies a number of examples ranging from banks (better rates from customers likely to leave them), electricity (better prices for business customers than for consumers even allowing for lower costs of supply) and medical specialists which offer vastly different prices for near identical services. Of particular concern is the rise of much greater use of price discrimination enabled by the rise of digital platforms, new technology, detailed customer data and sophisticated profit maximising pricing methodologies.

These practices all result from an economy which is insufficiently competitive and gives room for businesses to engage in exploitative pricing practices.

There is a case for a much more active public policy for investigating and analysing practices that operate at unwarranted cost to customers.

In order to address these the report recommends policy outcomes which would:

- remove obstacles to competition by the application of competition law or a removal of government restrictions on competition
- require the provision of better information to consumers
- lessen or remove obstacles to consumers switching to other suppliers
- exposing or sometimes shaming exploitative business practices of the kind shown in this report

All these business exploitative practices rest on a platform of weak competition in many parts of the economy and would be generally reduced by a strengthening of competition law and policy. Accordingly, recommendations to this effect are made in the report.

The prices practices described are not unlawful, but they reflect an imbalance between consumers and the power of business.

Price control is not seen as a solution in most or all cases. However, there is a case for governments exercising much closer scrutiny over these practices and for such scrutiny to be a regular part of the policy agenda.

SECTOR STUDIES

This section of the report examines a number of industries which came up regularly in submissions by academics, other experts and ordinary people. Regulators also have expressed concerns, sometimes in muted terms.


What is common to most such industries is a lack of competitors and entry barriers, some brought about by government restrictions on entry, a lack of consumer awareness and information, and a difficulty for consumers in switching suppliers.

Of great concern is price gouging in the electricity sector, a very concentrated industry at all levels. As the regulators themselves have reported there has been routine price gouging from time to time at the generator wholesale level as it sets prices in the price bidding system. Having regard to the changing nature of the energy market, its high concentration and its history of high prices it is concluded that the bidding system used to determine energy prices is not fit for purpose and consideration should be given to the capacity market approach used in the United States and Western Australia. This is likely to work better in the transition to a low emissions market and well applied should moderate electricity prices. There are also practices in the energy derivatives market which require deeper probing by the Australian Security and Investments Commission (ASIC). At the transmission level of the industry there has been a history of setting prices too high and there is a need for a closest ongoing review of prices to make sure that consumers are not overcharged.

At the retail level (which is accompanied by a high degree of vertical integration with generation suppliers) there is very substantial price discrimination between business and consumers which is hard to explain on the basis of cost differences. This needs deeper investigation by regulators. There are also major problems for consumers in determining what are the best prices in the retail market and much more activity is required to get competition and good prices in retail.

Given the importance of the energy sector and the downstream inflationary effects on the cost of living all this needs urgent attention from Government and regulators.

The banking sector has a significant lack of competition and the major banks' position is protected by the bodies which make up the Council of Financial Regulators in their pursuit of stability. This enables them to charge high prices quickly, engage in unfair pricing practices, and exploit their position in a highly complex industry. In this report we make recommendations to promote the competitiveness of the banking sector, empower customers and ensure that regulators are not unreasonably balancing the sector in favour of stability over customer interest. A particular priority should be to enable the account numbers of bank customers to be as portable as mobile telephone numbers where customers can switch their telecom provider without changing their



As the regulators themselves have reported there has been routine price gouging from time to time at the generator wholesale level as it sets prices in the price bidding system.

number. This dominance by the banks extends into foreign exchange where vulnerable customers are routinely overcharged.

The duopoly in the aviation sector in Australia is dominated by Qantas and there is price gouging by Qantas. This is illustrated by the blocking of Qatar expansion without reasonable justification. The Department of Infrastructure, Transport, Regional Development, Communications and the Arts should in its review remove unnecessary restrictions on competition on both international and domestic aviation and the findings should be reviewed as part of the National Competition Policy. Airports, too, as a natural monopoly are enabled to overcharge and their prices are unregulated.



The report is also concerned that remote and Island communities in Far Northern Australia face a massive supply chain concentration through the sole barge operator, *SeaSwift*.

Both early childhood education and the care sector are riddled with overcharging, principally due to the market's design and the difficulty users have in switching services. Both markets are provided with Government support but prices, on the other hand, are not heavily regulated, leading to an ability for some actors to exploit their position and extract higher prices than would otherwise be warranted. Switching providers in early childhood education and care is understandably hard due to the impact on children, while users of the NDIS are massively overcharged for basic needs. Both shaming and price regulation should be considered to rectify overcharging.

This report concludes there is a strong case for a comprehensive in-depth review of the supermarkets. This has been accepted by the government. The review also supports making the grocery code of conduct mandatory. This should include both making the regulations legally enforceable by the ACCC and making membership of the code compulsory for large retailers.

The report is also concerned that remote and Island communities in Far Northern Australia face a massive supply chain concentration through the sole barge operator, *SeaSwift*. This business absorbed its only competitor in a transaction opposed by the ACCC and has just exited a period of price regulation. Since leaving price monitoring, communities in Far North Queensland have faced massive price increases without oversight.

Cartels continue to be very profitable and prevalent. More resources should be provided to the ACCC for enforcement. It is heavily out resourced by business defendants. There is also a case for making the criminal cartel conduct provisions easier to enforce.

The price of electric vehicles in Australia is excessively high because of unwarranted import restrictions. Given we are no longer protecting a local car manufacturing industry, the restrictions should be immediately lifted in relation to EVs and in due course fully removed from all imported cars. The outcome would be a sharp fall in electric car prices and later in car prices.

Consumers have much less information than health care providers creating potential for excessive market power, inefficiency, and inequity in health care. High out of pocket charges are a key barrier to access health care in Australia. There is a need for a contemporary study of specialist fees backed by an analysis of restrictions on competition and of the role of information and balances between patients and specialists. This review should be commenced as soon as possible. Limitations on competition amongst specialists, especially entry restrictions, should be reviewed by the National Competition Policy Review. The conduct of such a review would demonstrate whether or not the Commonwealth Government is serious about applying the National Competition Policy universally.


In this same theme, pharmaceuticals prices are kept high by 'ever greening' and 'pay for delay' agreements. A mandatory reporting scheme should be implemented in relation to originator and generic agreements to improve the detectability of pay for delay agreements similar to the United States.

Competition is far less than it should be in Australia. This weakness provides a platform for many sectors to overcharge by setting prices above the levels that would occur in a more competitive market.

Australia should strengthen its competition law (and policy) by establishing pre-merger notification (as exists in most OECD countries), by boosting the provisions of the merger test to prevent a wider range of potentially anticompetitive mergers and by reversing the onus of proof in merger cases as recommended by the ACCC. Australia should also introduce a divestiture law which allows big business to be broken up in circumstances where a Court has found that it has breached a competition law seriously and where a Court determines that divestiture is the best remedy. Such divestiture policies have been successfully applied in the United States and other countries. The Labor government has announced that it will revive the National Competition Policy which involves ending government laws, regulations and actions which are anticompetitive. It is very important that this should be pursued in a strong, comprehensive manner across the whole economy.

This report shows that despite its prevalence excessive pricing, even extreme price gouging, is not unlawful in Australia. The Government needs to make the investigations of excessive prices a much higher priority, including identifying the causes and publicly exposing them. The power of the ACCC to act on excessive prices and expose them as well as to recommend solutions should be strengthened. This should include giving the ACCC power to self-initiate prices investigations and to arrive openly at appropriate policy steps such as the removal of anticompetitive restrictions and other market shortcomings which harm consumers. As well, the power to publicly criticize price levels such as applied in the period when the GST was introduced in 2000 should be reinstated.

As an alternative the government could establish a Commission on Competition and Prices to review Government and other restrictions on competition and high prices caused by a lack of competition.



Australia should also introduce a divestiture law which allows big business to be broken up in circumstances where a Court has found that it has breached a competition law seriously and where a Court determines that divestiture is the best remedy.

4. SUMMARY OF RECOMMENDATIONS

RECOMMENDATIONS RELATING TO PRICES

Recommendation 1.1: The Australian Government should use its power to require the ACCC to conduct more price and market investigations.

Recommendation 1.2: The Australian Government should have power to require the ACCC to undertake market studies as well as price studies.

Recommendation 1.3: The ACCC should have power of its own to initiate price and market studies.

Recommendation 1.4: The GST pricing legislation of 2000-2003 provisions regarding the naming of businesses and industries that overcharge should be reinstated.

Recommendation 1.5: Section 46 of the Australian Competition and Consumer Act should be amended to make it an offence to charge excessive prices in terms similar to the European Union provisions.

Recommendation 1.6: The Government could establish a Commission on Competition and Prices to review Government and other restrictions on competition and high prices caused by a lack of competition.

RECOMMENDATIONS RELATING TO MERGERS AND DIVESTITURE

Recommendation 2.1: The Australian government should establish a pre-merger notification system along similar lines to most OECD countries.

Recommendation 2.2: That in merger matters the onus should be on applicants to satisfy the ACCC and on appeal the Australian Competition Tribunal that the merger is not anticompetitive and is in the public interest.

Recommendation 2.3: The merger test should be augmented to continue to prohibit mergers which substantially lessen competition but there should be an additional provision prohibiting mergers that give rise to substantial market power (a more structural and immediate test) and/or which entrench, create, or add to market power.

Recommendation 2.4: A divestiture power should be introduced into the competition law.

RECOMMENDATIONS RELATING TO COMPETITION

Recommendation 3.1: The Australian Consumer and Competition Act needs to be shortened.

Recommendation 3.2: If the secondary boycott law is retained in the Competition Law there should be a provision that secondary boycotts are only unlawful if they substantially lessen competition.

Recommendation 3.3: Australia should ban non-compete clauses in employment contracts affecting both employees during and post-employment.

Recommendation 3.4: The current National Competition Review should examine policies and laws that prevent Governments from needlessly restricting competition.

Recommendation 3.5: The ACCC receives further funding for strong enforcement of the cartel law. It should also apply the criminal sanctions available for unlawful price fixing and other cartel agreements.

Recommendation 3.5: Treasury should conduct a public consultation to determine the need for improvement in the drafting of the criminal elements of the cartel law in view of recent difficulties in the bank cartel case.

RECOMMENDATIONS RELATING TO SPECIFIC INDUSTRIES

AVIATION

Recommendation 4.1: Airport prices should be regulated in the same way as other utility prices.

Recommendation 4.2: The Australian Government should use the opportunity of its current aviation review to remove international and domestic restrictions on competition. Any remaining restrictions should be reviewed by the Treasury led Competition Policy Review.

EARLY CHILDHOOD EDUCATION AND CARE

Recommendation 4.3: The ACCC should be empowered to investigate pricing decisions made by for-profit providers to ensure gaming is not occurring.

Recommendation 4.4: Prices in relation to disability care and support and aged care should be kept under continuous review by the ACCC.

BANKING AND FINANCIAL SERVICES

Recommendation 4.5: The ACCC should be provided with a standing Ministerial Direction to monitor prices and competitiveness in the retail banking sector.

Recommendation 4.6: The ACCC should be issued with a Ministerial Direction to undertake a further inquiry into pricing practices in foreign exchange markets to develop mechanisms for a fairer transmission of cost information to consumers as well as to provide specific assistance to prevent exploitation of those with low English language proficiency.

ENERGY

Recommendation 4.7: There should be a review of the design and operation of the wholesale market as to whether it requires refinements or a fundamental change in the form of a 'capacity market' as in North America and in Western Australia. This review should be chaired by an independent expert with input and resources from the AER, AEMO, and ASIC. The level of electricity generation concentration should be kept under review, and there should be close scrutiny of the impact on competition, positive or negative, that could occur in the transition to a re-designed energy market.

Recommendation 4.8: ASIC should be provided with a Ministerial Direction to investigate the energy derivatives market to ensure that participants in both the National Electricity Market and the markets for derivatives are not misusing their position in either to gain an unfair advantage or influence the price of energy to meet derivatives conditions.

Recommendation 4.9: Network prices should continue to require close regulatory scrutiny with the long-term interests of consumers put first.

Recommendation 4.10: There should be a regulatory review of the high degree of price discrimination in the retail electricity and gas markets.

Recommendation 4.11: State Governments and regulators should continue to introduce initiatives to improve retail outcomes brought about by current market imperfections.

FOOD AND GROCERIES

Recommendation 4.12: It is recommended that there should be a comprehensive ACCC inquiry into competition and prices in the retail food and grocery industry.

Recommendation 4.13: The Food and Grocery Code Review should be fully mandatory.

Recommendation 4.14: The Food and Grocery Code Review should investigate creating a price register for farmers to assist them in understanding market prices across primary industries.

SHIPPING COSTS IMPACTING FNQ AND NT

Recommendation 4.15: The ACCC should once again have an ability to challenge and overturn unreasonable prices charged by Sea Swift to ensure the service is not exploiting its market position.

ELECTRIC VEHICLES

Recommendation 4.16: Regulations in the Road Vehicle Safety Act 2018 which block parallel imports of electric vehicles be immediately lifted.

Recommendation 4.17: Regulations under the Road Vehicle Safety Act 2018 which block parallel imports of cars into Australia should also be repealed in coming months.

OUT OF POCKET CHARGES BY MEDICAL SPECIALISTS

Recommendation 4.18: The National Competition policy review should conduct or commission a contemporary study of specialist fees backed by an analysis of restrictions on competition and of the role of information imbalances between patients and specialists.

Recommendation 4.19: The ACCC or the Productivity Commission or another appropriate body should, separately, review specialist fees and the policy steps that could be taken to make them more transparent or to reduce them.

PHARMACEUTICALS

Recommendation 4.20: A mandatory reporting scheme should be implemented in relation to originator and generic agreements to improve the detectability of pay for delay agreements similar to the reporting arrangements in the United States.

5. INFLATION: THE CHALLENGE FOR POLICY MAKERS

PRE-PANDEMIC INFLATIONARY TRENDS

Prior to the pandemic era surge in prices, headline inflation growth was below the Reserve Bank of Australia's target range of 2-3 per cent. Between December 2014 and December 2019, year-on-year growth in headline inflation was only within the target range in two quarters – and even then, only just at 2.1 per cent on each occasion. On a trimmed mean basis, the RBA's preferred measure, inflation was below the target band from March 2016 onwards, not returning to the target range until September 2021. During this period, tradable inflation – that being the inflation Australia imports from overseas – averaged around 0.4 per cent year-on-year, while non-tradable (domestically based) inflation averaged at a subdued 2.3 per cent year-on-year, only just within the target band. Across this same period, non-discretionary inflation – the price of goods and services households are unable to avoid – averaged 1.6 per cent, only being within the target range in 7 out of 21 quarters.

TABLE 1. PRICE INCREASES: BETWEEN MARCH 2021 AND SEPTEMBER 2023

Automotive Fuel	45.4%
International Travel and Accom	36.3%
Gas and Other Household Fuel	35.7%
Electricity	22.3%
Oils and fats	34.2%
Insurance	22.6%
New Dwellings Purchases by Owner-Occupiers	31.1%
Groceries:	
• Cheese	27.3%
• Bread	24.1%
• Milk	22.7%
• Ice cream and dairy products	22.5%
• Eggs	19.7%
• Breakfast cereals	19.2%

A key part of the reason inflation was below target in Australia was subdued wages growth. According to the former Governor of the Reserve Bank, Philip Lowe, increased competition among workers contributed to slow wage growth and therefore to below-target inflation. Lowe pointed to competitive pressures from globalisation, with the implicit threat of offshoring, and from advances in technology, with the implicit threat of automation, as contributing to subdued wages growth. According to Lowe, the situation meant that many workers had less bargaining power than they once did.¹

Lowe also pointed to new entrants, like online retailer Amazon along with the rise of other online options in the retail industry putting pressure on margins and forcing existing retailers to lower cost structures and lower the prices charged for consumer goods, most notably the significant deflation of consumer electronics, whitegoods, apparel and other consumables. Competitive pressures on profit margins were noteworthy enough for the RBA to raise with the IMF in their annual country report that lower margins in retail and other sectors were contributing to below target inflation.²

1 Some Evolving Questions | Speeches | RBA

2 Australia: 2016 Article IV Consultation-Press Release; Staff Report; Staff Statement; and Statement by the Executive Director for Australia (imf.org), p. 6

PANDEMIC INFLATIONARY SURGE


The accumulation of supply chain disruptions and the effects of Russian invasion of Ukraine on international commodity markets saw inflation leave the RBA's target band in June 2021, the first occasion inflation had been above target since a brief nine-month period between March 2011 and September 2011. Since the pandemic, inflation has mainly been driven by new dwelling purchases, consumer durables, groceries, and utilities.

Between March 2021 – the last quarter before inflation left the target band – and September 2023, the level of headline inflation has increased a total 14.8 per cent. Trimmed mean inflation, a less volatile series measuring what the RBA considers 'core' inflation, has increased 13.0 per cent. This compares to an increase in the level of headline inflation of 23.2 per cent in the ten years prior to December 2019 and an increase of 22.5 per cent for trimmed mean inflation over the same period.

For workers, the acceleration of inflation has been concentrated in non-discretionary items, covering food, utilities, transport, housing costs and other essential goods and services that cannot be avoided. Between March 2021 and September 2023, non-discretionary prices have increased a total of 16.9 per cent, while wages have only

increased by 8.4 per cent over the same period. The highest seven year-on-year growth rates for non-discretionary inflation in the available series were the seven most recent quarters. Discretionary prices have increased in total by 11.7 per cent over the same period, with the highest year-on-year growth rates also occurring in the most recent quarters. While most acute in the goods and services workers are unable to avoid, inflation has been broad based and has comprehensively eroded workers living standards.

Real wages have declined by 5.6 per cent between March 2021 and September 2023, and the level of real wages is the lowest it has been since June 2009 – suggesting workers have lost over a decade of progress in living standards.



For workers, the acceleration of inflation has been concentrated in non-discretionary items, covering food, utilities, transport, housing costs and other essential goods and services that cannot be avoided.

PRICE INCREASES BY CPI CATEGORY

Between March 2021 and September 2023, the largest price increases have been Automotive fuel, increasing a cumulative 45.4 per cent; International holiday travel and accommodation, increasing a cumulative 36.3 per cent; Gas and other household fuels, increasing a cumulative 35.7 per cent; Oils and fats, increasing a cumulative 34.2 per cent; and new dwelling purchases by owner-occupiers, increasing a cumulative 31.1 per cent.

Over the ten years between December 2009 and December 2019, just prior to the onset of the pandemic, Automotive fuel increased a cumulative 26.4 per cent; International holiday travel and accommodation increased a cumulative 12.8 per cent; Gas and other household fuels increased a cumulative 68.4 per cent; Oils and fats increased 13.5 per cent; and new dwelling purchases by owner-occupiers increased 26.4 per cent.

Among the top 30 price increases over the same period were Cheese (up a cumulative 27.3 per cent), Bread (up a cumulative 24.1 per cent), Milk (up a cumulative 22.7 per cent), Ice cream and other dairy products (up a cumulative 22.5 per cent), Eggs (up a cumulative 19.7 per cent), and Breakfast cereals (up a cumulative 19.2 per cent). The high ranking of price increases in staple groceries points to the extreme price pressures workers are currently facing.

Total Food and non-alcoholic beverages prices, covering the full range of workers' staple shopping, have risen 15.2 per cent between March 2021 and September 2023, compared with a cumulative rise of 15.4 per cent between December 2009 and December 2019.

Other essential spending for workers has shown marked increases over the last two years. Electricity prices, driven by spillovers from Russia's invasion of Ukraine to wholesale prices, rose 22.3 per cent between March 2021 and September 2023, around a quarter of the increase they saw over the 10 years before the pandemic.

Childcare prices have declined 8.2 per cent between March 2021 and September 2023, reflecting a range of subsidies introduced over the past two years to support households. However, the Australian Competition and Consumer Commission's interim report into childcare found that childcare prices had been rising over the 4 years from September 2018 to December 2022 and the rate of increase has been faster than inflation and faster again than wage increases.³

Household essentials like insurance have also seen hefty price rises over the post-pandemic period, with the 15th highest price increase in the Consumer Price Index series. Between March 2021 and September 2023, Insurance prices rose 22.6 per cent. This compares to growth of 47.1 per cent between December 2009 and December 2019, meaning the price of insurance has grown just shy of half again in the last two and a half years what it had grown in the ten years prior to the pandemic.

While inflation remains elevated, year-on-year growth has been trending down. Headline inflation growth peaked at 7.8 per cent in December 2022 and has declined to 5.4 per cent as of September 2023. A significant reason for this decline is the resolution of upstream supply pressures and the decline in goods prices: goods price growth peaked in September 2022 at 9.6 per cent and has come down to 4.9 per cent as of September 2023.

However, a range of federal and state policy measures have also contributed to the decline. According to the Australian Bureau of Statistics, moderation in inflation growth in September 2023 was supported by increases to Commonwealth Rent Assistance helping to ease rental price inflation; rebates and concession on electricity bills from the Energy Bill Relief Fund assisted in lowering electricity price inflation; and changes to the Child Care Subsidy facilitated falls in price of childcare.⁴ The combination of these measures contributed to lower inflationary growth than would have otherwise been the case.

While still elevated, inflation growth is expected to continue to ease over the coming years, although the decline is expected to be slow. In its November 2023 Statement on Monetary Policy, the RBA forecast that headline inflation would decline to 3.9 per cent year-on-year by June 2024 and 3.3 per cent by June 2025, returning to the target band in December 2025 with growth of 2.9 per cent.⁵ This is an upwards revision in the path back to target compared to forecasts published by the RBA in February of this year, which had inflation at 3.6 per cent in June 2023 and 3.0 per cent in June 2025, the end of the forecast horizon.⁶ The length of the expected path speaks to the challenge of bringing inflation back to target and the necessity for measures to bring prices and price setting behaviour back under control.

IMPACT OF INFLATION

The impact on the cost living is hard to overestimate.

The vast majority of Australians have suffered real wages declines due to the recent inflationary period.

The Wage Price Data from Food Bank and The Guardian shows that 60 per cent of households facing food insecurity have at least one member in paid employment. This statistic highlights a troubling reality: employment does not necessarily protect against the risk of food insecurity.

3 June 2023 interim report | ACCC

4 CPI rose 1.2 per cent in the September 2023 quarter | Australian Bureau of Statistics (abs.gov.au)

5 Forecast table – November 2023 | RBA

6 Forecast table – February 2023 | RBA

The situation is further exacerbated as a significant 77 per cent of these households are experiencing food insecurity for the first time within the last year. These figures indicate a rapid escalation in the problem, underscoring the need for comprehensive policy interventions. The reports from Food Bank and The Guardian emphasize the growing prevalence of this issue, demonstrating that food insecurity in Australia is not confined to traditionally vulnerable groups but is increasingly affecting those who are actively engaged in the workforce.

According to the same reports from Food Bank and The Guardian, an overwhelming majority of affected households, approximately 79 per cent, attribute their situation to increased living expenses, largely both food and housing costs. This detail sheds light on the economic pressures faced by many Australian families who, despite earning wages, struggle to keep pace with the rapidly rising cost of living. This imbalance leaves them vulnerable to food insecurity, having to make difficult choices between essential needs.


Worse still are reports indicate that indicate many individuals and families are reducing their food intake or skipping meals altogether to cope with financial constraints. This pattern of compromised nutrition is not just a matter of food security but also has profound implications for the overall health and well-being of these individuals.

The ramifications of such dietary compromises extend beyond immediate physical health concerns and have a broader impact on mental and social well-being. The reports by Food Bank and The Guardian bring to light the psychological and emotional strain placed on individuals and families who are unable to meet basic nutritional needs. The stress and anxiety associated with food insecurity can lead to long-term mental health issues, further exacerbating the challenges faced by these households. Moreover, the social aspect of eating, an essential part of community and family life, is disrupted, leading to isolation and a decline in social well-being.

Energy was one of the most highlighted issues in submissions to the inquiry. Low-income households are especially vulnerable to energy price hikes, as they typically spend a higher proportion of their income and expenditure on energy. This situation is exacerbated by their limited capacity to reduce energy demand due to factors such as housing age, the condition of their homes, and the size and composition of their households.

Associate Professor Lynne Chester from the University of Sydney is a highly experienced economist with significant contributions on energy inequality, energy regulation and social stratification. In Professor Chester's appearance at the Sydney hearing, she demonstrated that these households have attempted to mitigate the impact of rising energy bills by adopting various measures such as limiting the use of lights, reducing the usage of heating and cooling systems, and only using appliances like washing machines and dishwashers when full.

Professor Chester gave an account of the severe lifestyle changes and sacrifices low-income households must make to cope with escalating energy costs. These include cutting back on essentials like food and healthcare, leading to physical discomfort, reduced mental well-being, and increased social isolation. Particularly harrowing were the accounts of people spending their days out of the home in shopping malls just to access free heating or cooling. The distress caused by high energy bills extends beyond financial hardship, affecting the social and emotional well-being of both adults and children in these households.



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Evidence from ACOSS underscores the severe strain on households, especially for people on the lowest incomes, such as those receiving the Jobseeker Payment or other income support. This group, already struggling to cover necessities, is disproportionately affected by the rising cost of essentials. The ACOSS Report on Cost-of-Living September 2023 highlights that individuals on income support are often caught between inadequate incomes and soaring prices, a situation that has intensified in recent times. For instance, ACOSS has found that a significant percentage of people on income support are in rental stress, with many paying over 30 per cent of their income on rent, a clear indicator of the financial hardship faced by this group.

Furthermore, the ACOSS report sheds light on the critical issue of compromised healthcare access among those on income support. Due to financial constraints exacerbated by inflation, a notable proportion of individuals on these payments are unable to afford necessary healthcare or medications. This lack of access to healthcare services is not only a direct consequence of financial hardship but also a critical concern for the overall well-being and health of these individuals. The report also indicates that many recipients of income support are resorting to reducing their food intake, with a significant number of them eating less or skipping meals. This aspect of the report highlights the dire circumstances faced by those on income support, where even basic sustenance becomes a challenge.

According to the ACOSS Report on Cost-of-Living September 2023, the impact of inflation on individuals receiving income support in Australia is most profound in housing. ACOSS finds that more than 94 per cent of respondents who rent privately are experiencing rental stress, defined as spending more than 30 per cent of their income on rent. Additionally, more than half of these individuals are spending 50 per cent or more of their income on rent alone, further exacerbating their financial strain and leaving them with minimal funds for other essential needs such as food and healthcare.

The impact of inflation on rural and remote communities in Australia is profoundly amplified by the personal stories presented at the public hearings.

Tommy Sebasio from Bamaga, speaking at the Cairns hearing, highlighted the extreme prices for basic necessities in remote areas. He mentioned paying an astounding \$19 per kilo for mince and filling his car with diesel at \$2.87 per litre. Mr Sebasio stated these costs are not just financial; they also threaten the disintegration of community and culture, particularly for those relying on the sea for their livelihood or travelling for cultural work.

Elida Faith, another witness at the Cairns hearing, discussed the broader economic challenges faced by families in these communities. High costs of essentials like toothpaste and the difficulty of securing stable employment add to the financial strain on households. Additionally, the high insurance costs in cyclone-prone areas like Cairns further exacerbate the cost-of-living crisis.

Leticia Choppy, an Aboriginal and Torres Strait Islander woman, highlighted the struggles of finding affordable, quality insurance in Cairns, a region prone to natural disasters. The high food prices, especially for fresh produce, add to the challenges in remote communities where essentials are more expensive and often of lower quality due to transportation issues.


Parents are also struggling with the cost-of-living increase. Childcare affordability in Australia, as indicated by data from various sources, presents considerable challenges for families. According to The Guardian ("Childcare fees in Australia: see how much costs have risen in your area," 2023), there is a substantial variation in the hourly cost of childcare across the country, ranging from about \$10 an hour in parts of Hobart to over \$16 in Sydney's eastern suburbs. This significant disparity in childcare costs across different regions highlights the financial burden faced by families, particularly in metropolitan areas where living expenses are typically higher.

Inflation, which has increased by 1.2 per cent, coupled with significant rises in essentials such as automotive fuel, rents, and electricity, places additional financial strain on families as found in the Australian Bureau of Statistics (ABS, "Living costs rising fastest for employee households," 1 Nov 2023). This economic pressure is further stressed by the cost of childcare, making it a major concern for many households. Women's Agenda reports that only 30 per cent of Australian parents with kids under six find childcare costs manageable ("Parents with kids under 6 struggling financially," 30 Oct 2023), underlining the widespread difficulty in affording childcare amidst other rising living expenses.

Women's Agenda notes that about 85 per cent of parents feel the need for both parents to work due to the cost of living, and 60 per cent would change their work hours if childcare were more affordable ("Parents with kids under 6 struggling financially," 30 Oct 2023). This situation not only impacts families' financial stability but also their work-life balance and overall family well-being.

The consequence of both the economic evidence and accounts of the experience of those doing it tough is a persistent erosion of living standards, as prices outpace wages. What has not been squeezed in this inflationary episode is profits. Despite prices increasing across many supply chains and for consumers, profits have not been squeezed across so many critical sectors as one would expect.

This all raises questions of the role of profits and prices in generating inflation and its impact on the cost of living. This is discussed in the next section of the report.



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POWER, PROFITS AND PRICES: THEORY AND EVIDENCE

COVID AND ITS ECONOMIC AFTERSHOCKS

The upsurge in global inflation following the COVID-19 pandemic and its aftershocks has resulted in significant economic and social disruption in Australia, like other countries. Both the causes and consequences of this inflation have been quite distinct from previous inflationary episodes. In particular, the upsurge in prices in the wake of post-lockdown reopening did not result from generalised macroeconomic 'overheating' or accelerating labour costs (as portrayed in textbook explications of classic 'wage price spiral' dynamics). Instead, the leading role in this inflation was played by disruptions on the supply side of the economy: a breakdown in supply chains resulting from lockdowns and interrupted production, shortages of many essential commodities (from semiconductors to motor vehicles to building products), chaos in logistics and transportation networks (most obvious in international shipping), and then a global energy price shock following the invasion of Ukraine. Put together, these multiple crises imposed a sharp and lasting blow to productive capacity in many parts of the economy. They also created the conditions for certain companies, especially those occupying positions of strategic importance in the overall economic supply chain, to take advantage of that chaos and increase their prices – extracting larger profits and contributing centrally to the resulting acceleration of inflation. This process has come to be known as profit-led, or seller's, inflation.

To be sure, there was a demand side to the market imbalances that contributed to the sudden outbreak of inflation after the pandemic. For companies to be able to charge much higher prices, they need a base of customers with purchasing power to pay those prices. The fast and powerful supports provided to both businesses and households by governments around the world, complemented by aggressive and unconventional monetary policy (including quantitative easing, utilised for the first time in Australia during the pandemic), sustained aggregate purchasing power and prevented a much worse and longer-lasting macroeconomic collapse. Those fiscal supports helped average people survive the lockdowns without losing their homes, even if their jobs disappeared. They also sustained links between firms and their workers, allowing for a faster and more efficient restart of production when health conditions allowed. And they facilitated a rebound in spending, employment, and output in the months after lockdowns ended that was faster than most economists believed would be possible in the early days of the pandemic.

But the success of these emergency supports should not be misinterpreted as evidence that government assistance was somehow excessive, fuelling ‘excess demand’ and subsequent inflation. Even with emergency COVID supports, real per capita consumption in Australia remained below pre-COVID trends: after the lockdowns ended, consumers were buying much more than they could during the lockdowns, but less than they would have if the pandemic had not occurred. That undermines the argument that consumer demand was too strong relative to Australia’s productive capacity. While demand exceeded supply during the initial post-lockdown period, it was driven by the reduction in capacity arising from the pandemic, rather than demand was excessive relative to pre-pandemic norms. Rather, this gap was clearly the result of the damage done to output and capacity by the pandemic.

Companies took advantage of the resulting shortages and disruptions to increase prices well above their costs. Businesses in many (but not all) industries were willing and able to push up prices, yet still sell their products. Their actions constituted the leading edge of post-pandemic inflation. This has resulted in a rapid redistribution of national income (with real incomes falling dramatically for workers and other constituencies but swelling to record highs for the corporate sector). And they are manifested by the hundreds of instances of specific price-gouging which have been reported to this inquiry. Price gouging by businesses has contributed to high inflation and on-going macroeconomic disruption in Australia.

MEASURING PROFITS AND PRICES

Evidence regarding the unprecedented surge in business profits in Australia in the wake of the COVID pandemic can be compiled from numerous sources. Individual financial returns are reported by publicly traded companies. Across corporate Australia, aggregate profits rose rapidly after the relaxation of initial COVID lockdowns and subsequent upsurge in prices. This surge in profitability was reflected in a parallel surge in equity valuations for publicly traded companies, which rose to record highs by the second half of 2021 – and have remained near those peaks ever since.

National accounting aggregates demonstrate the surge in profits in the post-pandemic period. Corporate gross operating profits rose 45 per cent between end-2019 and mid-2022 (see Figure 1). They stayed near those record highs in late 2022 and early 2023; they have partly moderated recently but remain high by historic standards. But even after the economy re-opened and emergency subsidies ended, profits continued to grow. For 2022 as a whole, corporate profits equalled 28.7 per cent of GDP – the highest for any calendar year on record.

The growth of corporate profits vastly outstripped the expansion of real output after the pandemic; the spectacular rise in profits cannot be explained by increases in real output or sales for companies. Instead, it reflected a rapid run-up in nominal prices for each unit of output. A measure of unit profit costs (analogous to the more commonly reported unit labour costs) can be computed by comparing the growth of nominal profits to the expansion of real output (see Figure 2). Unit profit costs surged by

FIGURE 1. CORPORATE OPERATING SURPLUSES, 2015-2023

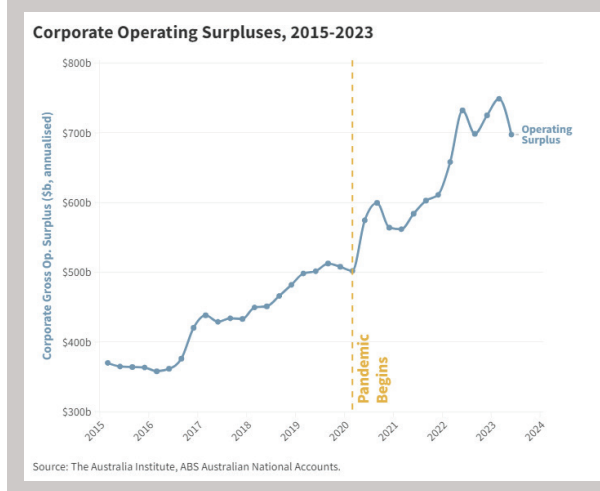
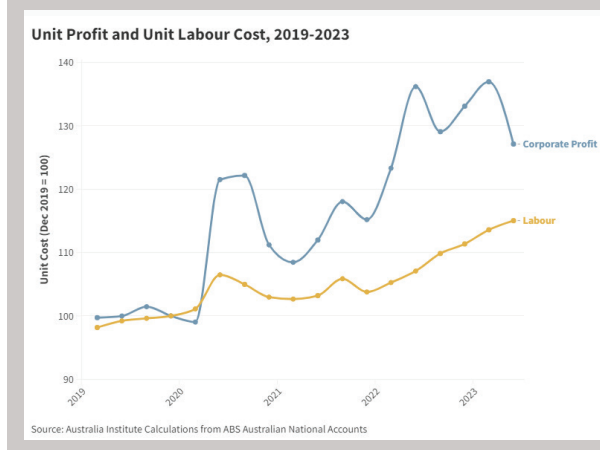


FIGURE 2. UNIT PROFIT AND UNIT LABOUR COST, 2019-2023



over 35 per cent from end-2019 to early 2022, alongside the parallel acceleration of inflation. In contrast, unit labour costs increased very slowly after the pandemic, not gathering much momentum until well into 2022 (as workers struggled for wage increases to match past and ongoing inflation). Unit profit costs have moderated more recently but have still increased by almost twice as much as unit labour costs in the period since the pandemic began. This casts more doubt on the assumption that post-COVID inflation resulted from the same sources (excess demand and rising labour costs) as was the case in the 1970s and 1980s. Other factor incomes have also lagged well behind the historic expansion of corporate profits in the wake of the pandemic (including small business mixed income, surplus on residential buildings, and government indirect taxes).

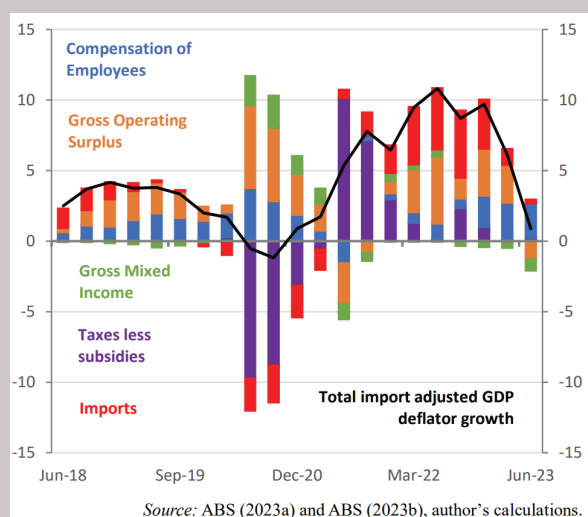
The unprecedented surge in unit profits can be statistically linked to the acceleration in inflation that occurred at the same time. The national income accounts prepared by the ABS calculate a measure of economy-wide inflation in all produced goods and services, known as the GDP deflator. It is based on a comparison of the nominal and real values of produced output in each broad sector of the economy. In Australia (like many other OECD economies), higher unit profits accounted for the majority share of higher inflation in the wake of the pandemic. This is concrete statistical evidence of the macroeconomic impact of excess profit-taking during and after the COVID pandemic. It is the economy-wide corollary to the hundreds of instances of individual price-gouging that have been documented through this inquiry.

The measure of economy-wide inflation (GDP deflator) used in this decomposition exercise differs from the more commonly reported measure of consumer price inflation. The Consumer Price Index includes only goods and services purchased directly by end consumers (and excludes inflation in intermediate goods, inputs, investment goods, government services, and exports); those other effects of inflation are relevant and important. The CPI also includes the prices of many non-produced products and assets (such as used cars, existing homes, etc.). Over time, however, these two measures of inflation trace each other closely (see Stanford et al 2023, Figure 1). And since the CPI is not directly decomposable into domestic input costs and factor incomes, the GDP deflator is preferable for analysing the causes and distributional consequences of inflation from the stand-point of economic production. This explains the widespread adoption of this method by the numerous international researchers and institutions surveyed below.

PRICE-GOUGING AND THE MALDISTRIBUTION OF NATIONAL INCOME

This macroeconomic context is essential for understanding the marked distributional consequences of post-pandemic inflation. If that inflation had been the result of a conventional overheating of domestic purchasing power (centred, according to conventional textbook narratives, in an overly tight labour market), then there is no reason to expect that the resulting surge in nominal incomes should be captured by just one specific sector of society. A generalised overexpansion in spending power and aggregate demand, conventionally assumed to exceed the real productive capacity of the economy, should be reflected in an equally widespread inflation of nominal incomes, as the prices for all scarce factors of production (including wages for workers) are bid up in a fruitless effort to increase output to keep up with that excess demand. This clearly did not happen in Australia after the pandemic. To the contrary, nominal wages lagged far behind prices from the beginning of the inflation (which first became visible in mid-2021). From June 2020, real wages fell over 5 per cent from their level when the

FIGURE 3: FACTOR INCOME CONTRIBUTIONS TO YEAR-ON-YEAR GDP DEFLATOR GROWTH (%) (GREENWELL, 2023)



pandemic began (Figure 4). As of September 2023, real wages were as low as they were in June 2009, and restoring real wages to pre-inflationary levels will take a number of years.

The combination of rapid pro-active price increases by sellers, with lagged wage growth and declining real wages, has produced a marked redistribution of income in Australia following the pandemic, away from labour (and other, smaller categories of factor income) and toward owners of incorporated businesses. Business profits were impacted by several factors through the pandemic and its aftermath. Profits widened during the initial lockdowns, as a result of generous government subsidies (such as JobKeeper payments) that outweighed the negative impacts of lockdowns and reduced sales. Profits retrenched with the phase-out of those subsidies in 2021, but then surged more than ever after the national and global economies began to reopen. That rise in profitability corresponded with the acceleration of inflation, which more than tripled from an annualised rate of 2.4 per cent during the March quarter 2021 (as lockdowns were nearing their end) to over 7.5 per cent during 2022. More recently, corporate profits have fallen back modestly: both in absolute terms, and as a share of GDP. This reduction in profits also coincides with the moderation in inflation, which eased to an annualised rate of about 4 per cent during the first half of 2023.

Through all these various chapters of post-COVID economic adjustment, corporate profit is the only major factor income in Australia that increased faster than nominal GDP since the pandemic began (as illustrated in Figure 5). Despite their recent moderation, corporate profits still account for an additional 2.14 percentage points of GDP relative to end-2019 – a shift that is worth an incremental \$55 billion annually at current GDP levels. Every other factor has seen its share of national output decline.

ECONOMIC THEORIES OF PROFIT-LED INFLATION

According to the pure theory of perfect competition that underpins conventional neoclassical economics, price-gouging and profit-led inflation should be impossible. In that idealised world, the anonymous and irresistible power of competition forces all firms to accept going market-determined prices for their output (and pay going market-determined prices for all their inputs, including capital, labour, and natural resources). Any attempt to charge more for a product than the cost of producing it (including a normal return on the capital invested in the business) would be met with an immediate and complete loss of business, as customers flocked to other suppliers who respect the competitive market price. At the microeconomic level, individual examples of price-gouging or exploitation of consumers should be prevented by this omnipresent competitive discipline. At the macroeconomic level, excess profits could explain changes in economy-wide inflation, for similar reasons. Economists and policymakers who accept this traditional faith in the power of competition to discipline companies seem befuddled by evidence showing both the frequent specific examples of price-gouging (such as those documented through this inquiry) and their aggregate manifestation in profit-led inflation across the broader economy.

FIGURE 4. REAL WAGE INDEX, 2020-2023

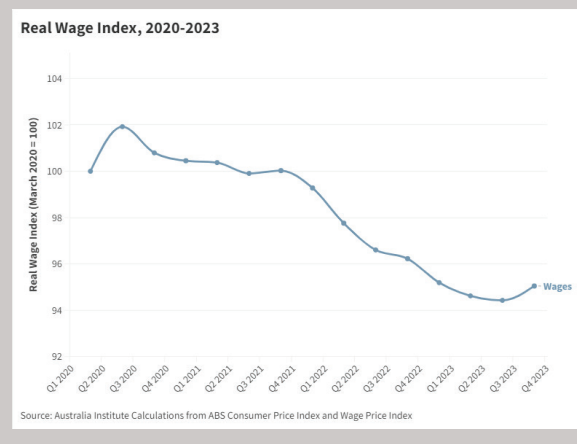
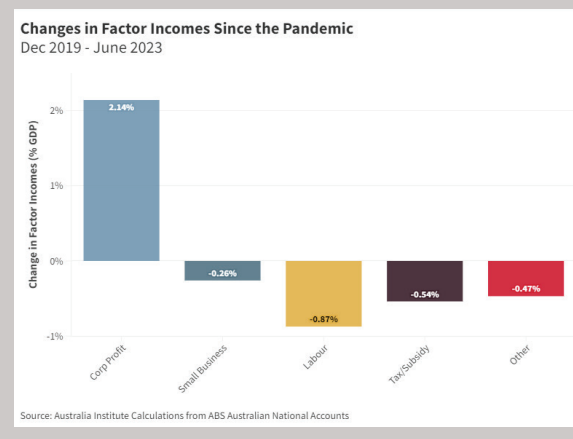


FIGURE 5. CHANGES IN FACTOR INCOMES SINCE THE PANDEMIC



Of course, the real world does not much resemble that idealised vision of perfect competition. Other than a few exceptional cases of anonymous, market-clearing competition between large numbers of buyers and sellers, most markets tend to feature a limited number of participants. Their interactions are strategic, not anonymous: participants anticipate competitors' actions, and try to gain advantage over a limited number of known agents. Market power can be directed against consumers, suppliers, or workers by large companies which exercise pro-active influence over prices for both inputs and outputs. Competition can be intense, but not in the manner envisioned by neoclassical perfect competition. And when industries are dominated by a small number of suppliers, both prices and profits reflect the strategic choices of firms (not anonymous market forces) and their varying abilities to enforce their priorities and interests.

Non-neoclassical (or 'heterodox') economic theories have attempted to integrate understanding of these more realistic notions of competition into their theories of prices, income distribution, and inflation. Some of the factors which these approaches have considered include:

- Corporate concentration (which has increased in recent decades in many Australian industries)
- Limited rationality or imperfect information among consumers (allowing them to be manipulated into paying more than cost for products)
- Government regulations
- Product differentiation (whereby consumers will pay more for certain brands or models, even on the basis of meaningless differences)
- Other non-market forces (such as norms, habits, or social traditions)

These structural features of price determination can be integrated into various versions of 'mark-up' pricing theories. In this approach, firms are not passive price-takers. Rather, they can influence the prices for what they sell (and often for what they buy) through conscious strategies. They may target a desired rate of return on invested capital, appropriated through a surplus over and above production costs (the mark-up). The extent of that mark-up can reflect many determinants, including those listed above, as well as the ability of other stakeholders in the economy (such as labour) to protect themselves against exploitation by large sellers or buyers. Changes over time in those determinants can lead to changes in how firms set their prices, with visible impacts on prices, income distribution, and macroeconomic phenomena (like inflation). Once the unrealistic assumption of perfect competition is rightfully abandoned, then it is not just possible, but in fact normal, that prices would change in ways not explainable or justified by changes in direct production costs. In this context, the possibility of profit-led inflation is not a surprise, and should be considered in regular macroeconomic analysis.

Various economists have explored the specific behavioural mechanisms at work that have allowed companies to increase profit margins so substantially in the wake of the COVID pandemic. They have also shown how initial price hikes imposed in some key sectors (like energy) could spread through other sectors, causing overall inflation to accelerate. Some of these possible transmission mechanisms include:

- **Increased corporate concentration:** The level of market dominance by large firms in key industries did not suddenly change during the COVID pandemic – but it has increased gradually in most OECD countries (including Australia; see Hambur 2023) in the decades since the inflationary episodes of the 1970s and 1980s. The stronger starting point of industrial concentration allowed the price shocks resulting from pandemic disruptions to be amplified by firms more dramatically, and ensured that most of the resulting inflation of nominal values ended up in corporate profits. This argument has been advanced by several researchers on profit-led inflation, including Bräuning et al (2022), Stiglitz and Regmi (2022), and Menezes and Quiggin (2022).
- **Concentration in Australia:** In the Australian context, several researchers have pointed to corporate concentration as a contributing factor behind excess price hikes in several sectors (see Hutchens 2023, Barrett 2023, and Quiggin 2023). This focus on corporate concentration as leading to price-gouging at the micro level, and profit-led inflation at the macro level, is especially germane to the terms of reference of this inquiry.

- **Reduced power of organised labour:** Nikiforus and Gothe (2023) argue that the long erosion of trade union representation and collective bargaining power in most OECD countries since the 1980s (including Australia) has undermined the ability of workers to win wages that keep up with profit-led price hikes. This has facilitated the record growth in corporate profits relative to total revenues or GDP. Ratner and Sim (2021) argue this sea-change in the balance of bargaining power in the economy has altered the traditional dynamics of inflation, formerly captured in the ‘Phillips curve’.
- **Distributional conflict:** A related narrative suggests that weaker institutional capacity to negotiate wages and income distribution could reinforce the channels of profit-led inflation that became visible after the pandemic. Theories of conflict-driven inflation have been proposed for decades (see, for example, Rowthorn 1977 and Rosenberg and Weisskopf 1981); in these theories, inflation arises as a way of resolving conflicting claims for income that exceed the available real output to meet those claims. Economies’ capacity to institutionally mediate conflicting claims can thus influence how effectively they can prevent inflation, or resolve it when it arises; Kläffling (2023), Blanchard (2023), and Weber and Wasner (2023) have suggested that the breakdown of macro-level distributional coordination in recent decades may thus have contributed to the amplification and persistence of inflation following initial post-COVID price shocks.
- **Consumer psychology:** Several economists have considered the follow-on impact on consumer decision-making of the initial rise in inflation after the pandemic. When price changes become larger and more frequent, consumers may become accustomed to them, and hence offer less resistance. Nobel laureates Kahneman (1984) and Krugman (2023), and other writers (such as Alloway and Weisenthal 2023), have pointed to companies’ ability to take advantage of confusion among consumers about what constitutes a ‘fair’ price for any product. So-called ‘excuse-flation’ is reinforced by this confusion, whereby companies justify their own price hikes on the basis of broader inflation – but consumers have little capacity to determine whether those justifications are legitimate.
- **Informal price coordination:** Another follow-on impact of an initial surge in inflation may be the fact that large price increases can reinforce implicit price collusion among dominant firms in concentrated industries. Without explicitly coordinating their prices, firms can congregate their pricing decisions around higher benchmarks, knowing that others are likely to follow. This amounts to an indirect form of collusion facilitated by an initial burst of inflation in strategic sectors (as suggested by Weber and Wasner 2023).

These various streams of research aim to explain why and how companies have been able to leverage the disruptions and uncertainty that followed the COVID pandemic into unprecedented profitability. They emphasise different behavioural mechanisms, but ultimately aim to explain the same outcome: namely, the expansion of corporate profits in absolute and relative terms, and the corresponding redistribution of national income toward corporate owners and away from other factors (including labour, small business, and others). And regardless of the precise channels through which this profit accumulation was accomplished, it stems from a common, underlying force: the desire and ability of companies to lift their prices well above production costs.

EMPIRICAL RESEARCH ON PROFIT-LED INFLATION

The unique causes and consequences of post-COVID inflation, and its lopsided distributional outcomes, have spurred research around the world into the role of pro-active business pricing strategies in sparking and transmitting inflation through the economy. This section will briefly review and summarise several important findings from this research, which has been undertaken in a wide range of government, academic, and policy organisations.

Several international economic institutions have confirmed the major dimensions of the profit-led inflation phenomenon, including: the unusual rise of profits after the pandemic, their dominant role in driving and explaining price increases, and the necessity of reducing profits in order to reduce inflation to pre-COVID targets coincident with recovery in real incomes for other stakeholders (including workers’ wages). Most of these institutions applied the methodology of decomposing changes in economy-wide prices measured by the GDP deflator into their factor income components (as described above). Key contributions in this research include:

- **Organization for Economic Cooperation and Development (OECD):** For many years OECD researchers used the GDP decomposition methodology to analyse inflation’s causes and effects in

member countries, including Australia (see, for example, OECD 1985). OECD data show the corporate profit share of GDP rose after COVID lockdowns in 25 of 29 countries with comparable data (OECD 2023); Australia recorded the 5th largest increase in the profit share of all countries considered. Applying the standard GDP decomposition methodology, the OECD found that higher unit profits were the leading component of recent inflation in several of those countries (including Australia, Canada, and the Euro zone; see OECD 2023 Box 1.2). In Australia's case, the OECD concluded higher unit profits accounted for over half of Australian economy-wide inflation in the period to end-2022.

- **International Monetary Fund (IMF):** Research published by the IMF also confirms that disproportionate increases in profit payments were the leading cause of inflation in Europe after the COVID lockdowns (Hansen et al 2023a). Using a factor price decomposition method (supplemented by explicit treatment of higher import costs, which have been especially important in European inflation), the researchers concluded that higher profits were concentrated in energy and utilities, but were also important in driving higher prices in other industries. Other IMF research has highlighted the importance of compressing profit margins back to pre-COVID norms, in order to restore real wages while simultaneously reducing inflation (Hansen et al 2023b).
- **Bank for International Settlements (BIS):** Researchers at the BIS applied the familiar factor price decomposition of inflation in order to both understand the factors causing the acceleration of inflation after the pandemic and look forward to measures that would help to bring inflation back to desired rates (Mojon et al 2023). The Bank concluded the sharp decline in real wages in the current inflationary cycle was very different from previous inflation episodes; the strong growth of profits throughout the acceleration of inflation was also distinct from past experience (such as in the 1970s and 1980s). The Bank's annual report concluded that compression in profit margins will be necessary to facilitate a deceleration of inflation coincident with gradual rebuilding of real wages (BIS 2023).
- **European Commission (EC):** Researchers at the EC used the standard GDP decomposition methodology to analyse the factors driving European inflation since the pandemic (EC 2023). They estimate that higher unit profits accounted for over half of inflation in Europe in 2022. The Commission blamed the combination of supply disruptions and firms' increased pricing power for the lopsided distributional impacts of this inflation.

Similar methodologies have been applied by several central banks around the world, in their own efforts to ascertain the causes of, and develop appropriate responses to, post-COVID inflation. Examples of central bank research that has affirmed the unprecedented growth of corporate profits after the pandemic, and their contribution to inflation, include:

- **European Central Bank (ECB):** The ECB has used the GDP decomposition method for many years to analyse inflation and inform policy responses to it (for example, ECB 2006), and its researchers have continued to wield this methodology to better understand post-COVID inflation. Arce et al (2023) estimated that escalating unit profits accounted for over half of inflation in the Euro zone in the latter part of 2022. Members of the ECB board, including the ECB's President, have highlighted the leading role of corporate profits in inflation, calling for unit profits to be reduced in order to achieve target inflation rates while permitting faster wage growth to reverse the recent decline in real wages (Schnabel 2022; Allenbach-Ammann 2023; Inman 2023a).
- **U.S. Federal Reserve:** In early 2023 the Vice-Chair of the U.S. central bank highlighted the role of historically high profit margins and retail mark-ups in explaining the surge in U.S. inflation after the pandemic (Brainard 2023). Federal Reserve researchers have confirmed the role of historically high profits to higher prices in several key industries (Bräuning et al 2022), estimating (using a factor income decomposition approach) that higher profits accounted for over half of the acceleration of US inflation in 2021 (Glover et al 2023). More recently, corporate profits have fallen in the US, as the conditions (such as shortages and supply chain disruptions) that supported unusually high profits have dissipated; this has been accompanied by a deceleration of inflation, providing more evidence of the link between profits and prices.
- **Bank of England:** As post-pandemic inflation gathered steam, the Bank's Governor urged companies to restrain prices and moderate profit growth (Inman 2023b), suggesting he viewed profits as a key

contributing factor to the inflation. Application of the GDP decomposition methodology by the Bank suggested that corporate profits had not increased unduly in the UK, unlike the rest of Europe (Haskel 2023). But more recent Bank research has warned that persistently high profit margins in the UK (concentrated among larger and more powerful firms) could contribute to the persistence of inflation in 2024 (Inman 2023c).

The theory and empirics of profit-led inflation have also been explored by academic and policy researchers in numerous countries around the world. Significant contributions to this growing body of literature include:

- **Economic Policy Institute:** Bivens (2022) published one of the earliest empirical studies highlighting the unique role of rising profits in the initial acceleration of inflation in the U.S. economy. By decomposing economy-wide inflation into profits, labour costs, and non-labour costs, he estimated that higher unit profits accounted for over half of unit price increases in the U.S. to the end of 2021. The share of U.S. inflation accounted for by profits has subsequently diminished (alongside the rate of inflation), as both profits and the pace of price increases moderated later in 2022.
- **Institute for New Economic Thinking:** Nikiforus and Grothe (2023) showed that the increase in corporate mark-ups in the U.S. was historically unprecedented in 2021, powering the acceleration of inflation that year. Mark-ups continued to grow in 2022, but not as rapidly, and concentrated in a smaller subset of sectors; inflation moderated as the growth of mark-ups slowed down. The authors link the growth in mark-ups after the pandemic to decades of gradual corporate concentration that preceded it; this, they argue, facilitated the aggressive price increases imposed by firms amidst the disruptions of the pandemic.
- **Weber and Wasner (University of Massachusetts):** Influential research from Weber and Wasner (2023) locates the most damaging initial price increases after the pandemic in several strategically important sectors of the economy, which they deem “systemically significant.” In these upstream sectors (including energy, other resource commodities, basic metals, and some transportation activities), companies were able to leverage shortages and disruptions into windfall profits. As this initial inflationary impulse was transmitted to other sectors of the economy, the impact on profit margins in downstream sectors varied, depending on the strategic position of each industry in question: some downstream companies could maintain (or even expand) profit margins as inflation was transmitted through the broader economy, others could not and saw profits fall. In a third stage of the process, other stakeholders (notably labour) fight to catch up to inflation, initiating a more familiar conflict-driven process of inflation. The decomposition of inflation into its factor price components will adjust as inflation progresses through these stages: profits are the dominant driver of the initial impulse, but are later supplemented by higher unit costs for other factors, too.
- **Roosevelt Institute:** Konczal and Lusiani (2022) measured the growth in corporate mark-ups in the U.S. in 2022, and found they grew faster than any previous year back to the 1950s. In their view, this explains the surge in prices in the immediate aftermath of the COVID lockdowns. Renowned economist Joseph Stiglitz and a co-author provided further detail on the nature and consequences of higher mark-ups, which they attribute to supply shocks and shifts in the composition of consumer demand during and after the pandemic (Stiglitz and Regmi 2022). They reject the hypothesis that generalized excess demand was the spur for accelerating inflation. Both Roosevelt publications linked the unusually high mark-up recorded after the pandemic to higher corporate concentration, compared to conditions during previous inflationary episodes (such as the 1970s and 1980s).
- **Canadian Centre for Policy Alternatives:** Research by Macdonald (2023) disaggregated economy-wide unit prices into factor price components and an estimated component of intermedia inputs. By his estimates, higher unit profits accounted for 42 per cent of the increase in average economy-wide prices in the two years ending in late 2022. Produced inputs (which themselves embody additional profit margins) accounted for one-quarter of the rise in unit prices, while unit labour costs accounted for one-third.
- **Australia Institute / Centre for Future Work:** This team of researchers used Australian macroeconomic data to document the leading role of higher profit shares in accounting for economy-wide inflation in the wake of the COVID pandemic (Denniss and Saunders 2022; Richardson et al 2022; Stanford 2023;

Jericho and Stanford 2023). This stream of research first demonstrated that labour costs could not be the source of post-pandemic inflationary pressures: wages lagged well behind prices, and labour only accounts for a portion of total production costs anyway (so any growth in unit labour costs, on its own, could ‘justify’ only a smaller increase in final prices). Decomposing economy-wide inflation into its factor price components (following the standard GDP deflator methodology) showed that over half of total inflation to late 2022, and 69 per cent of ‘excess’ inflation above the RBA’s target, were attributable to higher unit corporate profits. This research also confirmed that while the most dramatic increases in profits were experienced in the mining and energy sector (similar to several other OECD countries), profits in other industries also grew measurably as a share of total GDP – especially in a subset of industries (including manufacturing, wholesale trade, and transportation) with strategically important positions in the overall economic supply chain. In their submission to this inquiry (Stanford et al 2023), these researchers noted a recent moderation in corporate profits in Australia, that has coincided with a deceleration of inflation. However, profit margins remain higher than pre-pandemic norms, and will need to be narrowed further – in order to both reduce inflation, and reverse the redistribution of national income toward corporate profits that marked the first years of post-pandemic inflation.

The preceding publications represent just a sub-set of a growing international body of literature developing both the theory and the empirical dimensions of profit-led inflation. This research confirms the leading role of abnormally high profits in the acceleration of inflation which accompanied economic reopening after COVID lockdowns. In Australia and most other industrial countries, corporate profits grew disproportionately in the first years of post-pandemic inflation. Companies were able to leverage the disruptions of the pandemic (including disruptions to supply chains and logistics, shortages of many essential commodities, sudden shifts in consumer demand resulting from lockdowns and their aftermath, and a global energy price shock) by increasing selling prices well above their own costs. The result was profits that grew in absolute terms, and relative to total revenue or national income. As the global economy has stabilized, profits in most countries have moderated – alongside the partial deceleration of inflation which has also occurred in most industrial countries. However, relative to other incomes, corporate profits remain elevated (as confirmed by their larger share of national output). This suggests that more policy action is needed to reduce excess price hikes by business and restore pre-pandemic distributional patterns (including a repair of real income losses experienced by workers and other sectors of society).

IS AUSTRALIA DIFFERENT?

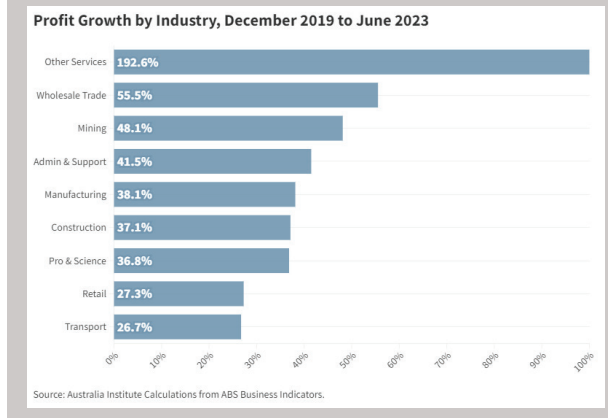
The growth of corporate profits (in both absolute and relative terms) in Australia in the aftermath of the COVID pandemic is undeniable. Official economic data confirms that profits rose dramatically in nominal terms (rising over 45 per cent from end-2019 to mid-2022), in real terms (growing much faster than inflation), and as a share of national GDP (reaching 28.7 per cent of GDP in 2022, the highest in Australian history, up by 4 full percentage points from the average profit share in the five years preceding the pandemic). This historic expansion in profits is clearly correlated with the surge in inflation during that time. More recently, the decline in profits in 2023 is occurring alongside a welcome deceleration of inflation – although both the profit share and inflation remain well above pre-pandemic norms.

Despite this evidence, some business leaders, orthodox economists, and policy-makers deny that record corporate profits have been relevant to the inflation Australia has experienced since the pandemic (see, for example, Read 2023 or RBA 2023). Their core argument is that international evidence on the role of profits in driving inflation is not applicable in Australia’s case, because of the large role played in our economy by the mining and energy industries. It is claimed that if these sectors are excluded, corporate profits have not dramatically increased. And since most of the output of Australian mining and energy producers is exported, their higher prices (and the profits that resulted) have not been consequential to domestic inflation.

These arguments are not convincing. To be sure, the expansion in mining profits was especially dramatic, accounting for a large share of the total increase in corporate profits in Australia after the energy price increases of 2021 and 2022; indeed, by 2022 the mining sector single-handedly accounted for over half of all gross corporate profits across the national economy (Jericho and Stanford 2023). But profits of aggregate non-mining sectors also grew disproportionately to their total revenue and value-added. Gross corporate

profits in non-mining industries surged temporarily in 2020 (by over 5 percentage points of non-mining GDP), before falling back in 2021 and 2022 after JobKeeper and other business subsidies were phased out (Stanford and Jericho 2023). But even in 2022, non-mining corporate profits were about 1.5 percentage points higher as a share of non-mining GDP than in 2019 (before the pandemic). And for a sub-set of industries with strategically important positions in the overall economic supply chain (including manufacturing, wholesale trade, and transportation), profit growth was more dramatic – now rivalling that of the mining sector (as shown in Figure 6). With the partial retrenchment of mining sector profits this year (in line with weakening global energy prices), mining is no longer such a ‘special case’ among Australian industries. Overall, the post-pandemic expansion of corporate profits has moderated in 2023, but is now more widely distributed than earlier in the post-pandemic inflationary episode.

FIGURE 6. PROFIT GROWTH BY INDUSTRY, DECEMBER 2019 TO JUNE 2023



The claim that higher prices for energy and other resource commodities were not relevant to Australian domestic inflation will seem especially far-fetched to any consumers who have grappled with sky-high prices for petrol, gas, and electricity over the past challenging years. While much Australian energy output is exported, almost all of the energy consumed by Australians originates in Australia, and the historically high profit margins captured by private firms from domestic sales of energy made an outsized contribution to the surge in Australian inflation. At the micro level, this inquiry has heard dozens of first-hand accounts from Australian consumers who faced price-gouging from energy companies. Their experiences are absolutely relevant to understanding domestic inflation and the cost-of-living crisis facing so many households. Moreover, higher energy prices also show up in higher prices for other goods and services which use energy as an input in their own production.

International research (such as that of the OECD 2023) confirms that the surge in profits in Australia after the pandemic was among the largest of any industrial country, and that those record profits were the leading factor in the acceleration of inflation after mid-2021. Some of those other OECD countries (including Canada, Norway, New Zealand, and even the U.S.) are also major exporters of energy products; Australia’s status as a major resource exporter is not unique, and certainly does not imply that these profit-led price channels are somehow irrelevant here.

POLICY IMPLICATIONS OF PROFIT-LED INFLATION

From both the macroeconomic evidence presented above, and the individual micro evidence of price-gouging compiled through this inquiry, it is clear that the power of corporations to unduly lift prices has been a central factor in the recent cost-of-living crisis affecting so many Australian households. Indeed, the many case studies of exploitation faced by Australian consumers reviewed by this inquiry constitute the ‘human face’ behind the aggregate statistics of profit-led inflation. The ability of companies to charge unfair prices, amidst the unprecedented economic and social dislocation ensuing from the COVID pandemic, has significantly undermined the well-being of the Australians we heard from. They have been confronted by the worst

The ability of companies to charge unfair prices, amidst the unprecedented economic and social dislocation ensuing from the COVID pandemic, has significantly undermined the well-being of the Australians we heard from.

extremes of price-gouging in the last three years. This aggressive corporate pricing behaviour, in aggregate, also shaped the challenging macroeconomic repercussions of the pandemic – including the acceleration of inflation, and its aftereffects (including high interest rates). Adding insult to injury, numerous of the individual allegations of price-gouging received by our inquiry dealt with unfair behaviour by large commercial banks, which have used their market dominance to extract even more profit from customers through higher interest costs and other charges. Price-gouging by the banks has only exacerbated the consequences of restrictive monetary policy that was implemented in response to profit-led inflation arising from other sectors. In other words, these consumers have been hit twice by the misuse of corporate power: first they experienced general inflation largely caused by profit-seeking after the pandemic, then were gouged again by financial companies leveraging their market dominance to make extra profits even under higher interest rates.

In this context, this inquiry's focus on the price-gouging experiences of individual Australians complements the aggregate macroeconomic evidence presented above about the role of corporate power in driving recent inflation. As many researchers and institutions have noted (including central banks in many countries), profit margins need to moderate toward pre-pandemic norms, in order to simultaneously reduce inflation while restoring real wages for workers (who, as this inquiry has documented, have been hurt as consumers by exploitive pricing practices). For real wages to recover, nominal wage growth needs to exceed price inflation by a significant margin, for a significant period of time. Some observers fear this will set off a subsequent round of inflation, if those higher wages are in turn passed on by companies in still higher prices. This need not be the case, however, if profit margins are reduced at the same time. Some of that is likely to occur due to the normalisation of supply conditions (as global trade, transportation, and logistics are stabilised). Continued reductions in world energy prices would also help – although Middle East tensions and other unpredictable events could readily set off another cycle of supply-side inflation led by higher prices and profits among energy producers, including those in Australia. But additional measures to control or reduce profit margins would help in facilitating a return to pre-pandemic distributional patterns.

Against this background we turn to an examination of some specific business pricing practices followed by case studies of individual industries that could be or are engaging in price gouging.

6. PRICING PRACTICES: A SMALL SELECTION

Modern businesses engage in pricing practices which, aided by the lack of perfectly competitive markets (characterised by small numbers of competitors, inadequate consumer information and costs and difficulties of switching their custom to other products) enable them to extract more dollars from consumers (and other businesses who are customers) than would occur in perfectly competitive markets. Many pricing practices can be characterised as an attempt by producers, businesses, or suppliers to maximise their capture of the consumer dollar (or 'consumer surplus') in a way that would not be possible in more competitive markets.

THE BATTLE FOR THE CONSUMER DOLLAR: CONSUMER SURPLUS VERSUS PRODUCERS SURPLUS

'Consumer surplus' is an economic term which refers to the difference between what a consumer would be willing to pay for a good or service and what the consumer actually pays. For example, a consumer may pay \$4 for a coffee but would actually be willing to pay \$5. The consumer surplus would therefore be \$1.

'Producer surplus' is the difference between how much the supplier or producer is paid and how much it would be willing to supply the product at. For example, a supplier may be willing to supply coffee for \$4. If, however, it could raise its price and be paid \$5 the producer surplus would be \$1 higher as a result.

These concepts set the scene for a battle between suppliers and consumers as to who gets the surplus—the producer surplus versus the consumer surplus and the amount of consumer surplus that producers can appropriate for themselves by charging higher prices. Or in simpler language, the battle by business to capture the consumer dollar.

An important aim of business pricing is to capture as much consumer surplus as possible. In this case, businesses would do this if they could increase prices by \$1.

PRICE DISCRIMINATION

One important complication to the above analysis is that different consumers have a different willingness to pay. Some consumers may be willing to pay \$5 for the coffee while others are only willing to pay \$4.

An important aim of business pricing practices then is to charge \$5 for those willing to pay that amount and to charge \$4 only for those who are only willing to pay \$4. That is, if possible, to engage in 'price discrimination'.

Price discrimination occurs as a result of trying to exploit the fact that different consumers have a different willingness (or ability) to pay for the same product.

In most cases price discrimination occurs only when there is a lack of competition or another failing in the market. If, for example, a supplier tries to charge a high price to a customer with high willingness to pay the supplier cannot succeed if there is a competitor willing to supply at a lower competitive price.

An obvious policy implication is that if it were possible to bring about an increase in competition or consumer information and awareness or in consumer mobility so that they could readily switch suppliers – consumers would be better off. In such cases some producers or suppliers would be less well-off but they would still be able to receive a price that covers costs and enables a reasonable profit. And the producers who attracted sales as a result of their more competitive offerings would gain through additional sales.

An aspect of price discrimination is that business pricing practices as far as possible may distinguish between customers who would leave them if a competitor appeared and offered better prices or a better deal and those customers who would not in the same circumstances leave them. This might be because of inertia, a lack of knowledge of the competitor and its offerings, or the costs of switching from one supplier to another. In these circumstances businesses try to set prices and other terms and conditions in such a way that they offer a better deal, typically a lower price, for customers likely to switch suppliers whilst ensuring that the prices, terms and conditions stay high for those consumers who are unlikely to switch to an alternative supplier.

Stucke and Ezrachi (2020) in discussing loyalty taxes makes the point that suppliers are likely to provide incentives through discounts and the like to lure new customers, but these offers are not extended to people who are already committed to the product and those who are very unlikely to be hooked. In the case of the former, it is well-known that a new customer for a bank loan can negotiate better terms than those provided to existing customers. Unless the borrower threatens to leave the bank, they will not receive such offers and, by default, will continue to pay at the old rate. Likewise, while the bank will advertise, for example, the standard variable home loan rate, new customers can bargain for a better rate. Banks are discussed later in this report.

Against that background this section of the report examines a small sample of business pricing practices designed to capture consumer surplus and to increase producer surplus.

LOYALTY TAXES

A 'loyalty tax' is a pricing scheme under which customers are lured into purchasing a good or service with a low initial price followed by sharp rises in subsequent years of patronage. These can happen in industries in which it is difficult or costly for consumers to switch to alternative products. In some cases, it is not made clear to customers that they are experiencing a form of loyalty taxing over the course of time. An Australian example has concerned insurance premiums. In order to attract customers premiums are set low for the first year. Then in subsequent years prices are increased sharply. Customers were not told by how much prices had risen from the previous year, nor were they even told what price or premium they paid the year before when their rate renewal notice arrived. Consequently, a majority of customers were unaware of the magnitude and severity of the rises.


In the case of property or home contents insurance one government-imposed policy solution was imposing a requirement on insurers that they state the premium paid in the previous year on their renewal notice thereby allowing consumers to know the amount of the increase.

'Loyalty taxes' apply in a number of financial services areas including insurance, banks (as noted here and later), energy and other fields.

RETAIL ELECTRICITY – A CASE STUDY

Electricity has been a prominent example of large price increases in recent times. Retail sales are dominated by three companies, AGL, Energy Australia and Origin Energy. ACCC has expressed concern that the retail and wholesale electricity markets are still concentrated (ACCC Annual Report 2020-21).

While electricity is a homogenous product that defies differentiation, the terms on which it is made available for sale are a case study in obfuscation. Part of the retail strategy seems to be making understanding as hard as possible so as to discourage genuine comparisons. A UK study found that electricity consumers looking for cheaper prices only achieved 26 to 39 per cent of the maximum gains available to them and over a quarter of consumers who tried to save money were actually worse off (Wilson and Waddams Price, 2007).



Part of the retail strategy seems to be making understanding as hard as possible so as to discourage genuine comparisons.

The result has meant government initiatives and some private organisations are now established to assist consumers in the navigation around plans and options. When plans are hard to understand it is also easy to misrepresent the competitor's prices and the electricity oligopoly has been pursued for just such activities. The big three electricity retailers, Origin, EnergyAustralia and AGL, as well as smaller retailers have been prosecuted for "inappropriate door-to-door marketing activities" (ACCC 2015). The government now requires retailers in New South Wales, south-east Queensland and South Australia to follow a standard way of setting out their electricity prices including the 'reference price'.

The December report of the ACCC Inquiry into the National Electricity Market (Electricity market monitoring inquiry December 2023) found that existing customers pay a loyalty penalty leaving them hundreds of dollars worse off every year. In Victoria for example only half of all residential customers want their power company's cheapest offer. The report said in all states customers on old plans are paying higher average prices than those on newer plans. It also said 'our analysis suggests that retailers recoup their costs over a customer's lifetime, by setting attractively low acquisition offers and making subsequent unilateral price increases for their existing customer base over time' (p.9, Electricity market monitoring inquiry ACCC 2023)

Conditional discounts can be a concerning practice generally, and this is discussed later when we examine financial services. Failing to meet the conditions for a discount can leave you paying more. The ACCC found that '96% of residential customers on plans with an unconditional price more than 25% above the default offer were on a plan with a conditional discount' (p.6 Electricity market monitoring inquiry ACCC, 2023).

The ACCC found further that those on conditional discount plans were more likely to have not switched providers and would be paying even more than the default offer having achieved their discounts. Failing to achieve a discount compounds the penalty, with about a quarter of people in hardship cases (those who are struggling to pay their bills) failing to achieve their conditional discounts (p. 6, p. 61, Electricity market monitoring inquiry ACCC 2023). This can mean hundreds of extra dollars per year spent on electricity for customers already struggling to meet their expense.

A policy solution is to try to reduce the number of customers on old plans as a matter of priority.

Loyalty pricing can be characterised as an attempt by producers, suppliers, businesses to convert 'consumer surplus' into 'producer surplus', essentially by charging prices that exceed competitive levels – if there were perfect information, costless consumers mobility and if there were many suppliers, the practice would not be happy – certainly not on the scale it does at present. There is a strong case for public action to help bring back to consumers the surplus they have lost to producers because of loyalty pricing. Some elements of an appropriate public policy in relation to this problem are discussed later.

LOYALTY SCHEMES

Loyalty schemes has some similar features.

Loyalty schemes have become a prominent marketing tool for many businesses around the world. The ACCC (2023) says "Customer loyalty schemes offer points or discounts to boost repeat business." Airlines call their schemes "frequent flier programs". Cafes and other small consumer businesses that are likely to attract repeat business may offer such things as a discount on the tenth purchase.

In its review of loyalty schemes the ACCC has received reports from consumers that they haven't earned, kept or been able to redeem their points in the way they expected. The ACCC expressed concern about a number of business practices that included schemes that:

- do not present their terms, conditions and privacy policies in a way that consumers can readily understand
- that make unilateral changes to their terms and conditions in a way that may be unfair to Consumers
- collecting, using and disclosing consumer data in ways that do not align with consumers' preferences. This includes loyalty schemes not providing sufficient transparency and meaningful consumer control over the collection, use and disclosure of consumer data, and engaging in the following practices:
 - » seeking broad consents from consumers and making vague disclosures to them about the collection, use and disclosure of their data
 - » providing consumers with limited insight and control over the sharing of their data with unknown third parties
 - » providing a limited ability for consumers to opt out of targeted advertising delivered by third parties on behalf of loyalty schemes.

For example, frequent flier programs suggest people can cash in their points for a free flight only to find out that the cost of purchasing an airfare without using points is like the cost using points when the add-ons, taxes and other charges are included.

The purpose of loyalty schemes is to lock in or at least bias consumer choices to products already chosen. As the ACCC's Customer Loyalty Schemes Report puts it "loyalty schemes are a form of marketing or promotional tool that incentivises consumers to make repeat purchases."

The data generated from loyalty schemes has been used to generate risk profiles of customers. This sort of discrimination can work by allowing online sales to offer higher prices to those customers that are less likely to be sensitive to high prices.

Loyalty schemes are an example of a business practice that is not necessarily undesirable although they are often designed to lock in customers and ward off, at low cost to business, the impact of competition and although they tend to operate in the interests of better off regular customers rather than customers generally.

One of the main concerns is that the operation of the schemes is far from ideal and from this perspective there needs to be general scrutiny of schemes with an emphasis on identifying their shortcomings for customers. There is also a benefit in exposing their nature to customers.

RECOMMENDATION

There should be an ongoing analysis of loyalty schemes and their effects on consumers and the prices they pay by the ACCC.

DRIP PRICING


The ACCC defines drip pricing as "when a price is advertised at the beginning of an online purchase, but then extra fees and charges (such as booking and service fees) are gradually added during the purchase process." The US Federal Trade Commission (2012) has a similar definition: "Drip pricing is a pricing technique in which firms advertise only part of a product's price and reveal other charges later as the customer goes through the buying process. The additional charges can be mandatory charges, such as hotel resort fees, or fees for optional upgrades and add-ons." A White House briefing titled "How junk fees distort competition" (Council of Economic Advisers, 2023) provides the example of two different vendors selling seats for a concert both quoting a price of \$87. But then:

While the advertised price for the two tickets was the same, the final price—inclusive of taxes, service fees, and/or fulfillment fees—ranged between \$123.98 and \$128.26. In one instance, these final prices were only revealed after spending time to input credit card information and an email address. Therefore, a consumer

would have to spend a significant amount of time to accurately be able to compare the true price being charged by the different platforms, and may end up choosing a higher-priced option, even though the good being sold is identical.

Stucke and Ezrachi (2020) point out that drip pricing is a “shiny lure” that involves a “price [which] keeps increasing as the customer goes through the buying process”. Initial prices are much lower than might be expected and indeed, lower than they turn out. We see drip pricing spreading across many seemingly competitive markets including online booking sites like Airbnb and eDreams, airline tickets, car rentals, and prepaid telephone calling cards. They argue that consumers tend to underestimate the total cost when the bill is separated into “components” such as (for a hotel), a daily charge, plus resort fee plus applicable taxes. The effect is disguised by putting some of the components in smaller font or in later pages/paragraphs. The Council of Economic Advisors (2023) notes that there is a variety of add-ons charged by different hotels and the like so that the initial price differentials between offers may bear no relation to the differentials in the all-inclusive price. These tactics are designed to obfuscate consumers and make comparisons near impossible.

On the surface, the markets where drip pricing takes place may seem competitive. On closer examination however, the competitors in the market are competing on how to exploit consumers rather than on offering the best deals or lower costs. Indeed, we may be seeing the early developments in this area as technology, the manipulation of big data and developing analytics will refine some of the techniques, especially with regard to on-line purchases. The future dystopia is market forces increasingly biasing outcomes towards products and services that prey on human weaknesses, our propensity to make irrational decisions depending on the sales pitch and apparent features.



On closer examination however, the competitors in the market are competing on how to exploit consumers rather than on offering the best deals or lower costs.

In some cases, drip pricing may breach consumer law if it is misleading or deceptive. In Australia the ACCC (2015) has taken action against Airbnb and eDreams “engag[ing] in misleading and deceptive conduct and [making] misleading representations by failing to adequately disclose to consumers in Australia particular mandatory fees on key pages of one or more of their online booking platforms.” In the case of Airbnb, it failed to disclose a mandatory service fee and cleaning fee. Meanwhile the eDreams website did not specify a single inclusive price that should have included its mandatory fees.

There is a need for exposure of drip pricing practices especially when the rate of inflation is falling but businesses change the expectations factor in their pricing very slowly.

In March 2017 Jetstar and Virgin were fined for drip pricing (ACCC 2017). The case was that these airlines used drip pricing to lure customers into an online purchase with a price that did not reveal additional fees and charges until later in the purchasing process.

There can also be instances under Australian consumer and pricing law where there is a requirement that when a business states its prices, the statement should specify the price and all its elements in full.

However, most drip pricing does not fall foul of consumer law. This does not mean the practice is always in the interests of consumers. It can be harmful in some cases, even if lawful and there is a need for ongoing exposure of such practices to the public.

EXCUSE-FLATION

Frequent and large price increases can affect the ability of consumers to judge the fairness of posted prices, and resist those that are excessive. Companies can use broader inflation trends as ‘cover’ to justify higher prices for their own products, even if their own production costs have not increased accordingly. Several

reports indicate that the resulting consumer uncertainty has been a factor in validating price hikes, and corresponding widening of profit margins, by firms (Krugman 2023; Alloway and Weisenthal 2023). Broader inflation gives companies an ‘excuse’ to raise their own prices, whether they need to or not—giving rise to the moniker ‘excuse-flation’.

A related point is that inflation can provide an opportunity for a business to signal in a subtle manner to competitors how much it intends to raise prices e.g. by directly or through an industry association (or other subtle means such as private media briefings). When inflation is high there is a good case for governments exposing such practices sometimes by threatening ACCC investigation as to whether cartel behaviour may be involved or by exposure and condemnation of such statements.

CONFUSION PRICING

A more deliberate and manipulative manifestation of this problem is the practice of intentionally confusing consumers with a myriad of complex price structures and plans, which makes it very difficult for consumers to comparison shop or judge the fairness of any specific price (Chioveanu and Zhou, 2013). This practice has been recognised and researched in business and legal literature (see Chauhan and Sagar 2021 for a survey). The practice is common in selling products that involve ongoing relationships between the consumer and the merchant (such as contracts for telecommunication, energy, financial or maintenance services, often tied to initial purchases of a tangible product like a smart phone). Numerous examples of this practice have been documented in Australia (Kalayci 2015), and the complexity of pricing and contractual arrangements has continued to evolve. Online marketing and digital products seem particularly fertile ground for firms to offer deliberately complex and misleading contract terms (Consumer Policy Research Centre 2022).

Evidence is mounting that these and related practices (such as hidden subscription commitments and other misleading arrangements) have added significantly to the current cost-of-living crisis facing Australian households (Treasury 2023). New laws have recently come into effect in Australia regulating some unfair and misleading contract terms (Edgar et al 2023). More reforms are required, however, to broaden the scope of restrictions on confusion marketing, and ensure that consumers are able to make informed comparisons and choices.

ASYMMETRIC PRICING OR ‘ROCKETS AND FEATHERS’

The timing of price rises, and price falls is often asymmetric. That is when costs rise, prices rise faster, then they fall when costs fall. This is sometimes described as the ‘rockets and feathers phenomenon’. Price increases are like rockets—they ascend with great speed. Price falls are like feathers—they float slowly to the ground.

The rocket and feathers effect applies quite widely in the economy including to petrol prices which appear to rise more quickly in response to rises in crude oil prices than they fall in response to reductions in crude oil prices.

This phenomenon appears to occur in a significant number of other markets. They include: fruit and vegetables, bank interest rates, insurance premiums and generally goods whose prices upwards and downwards are affected by exchange rate changes. A recent example that drew much media attention concerned the price of meat. Lamb prices for farmers fell heavily many months before this was passed on in prices. On the other hand, there is some evidence that when lamb prices rose retail prices rose more quickly.

With many recent rises and falls in input prices due to supply disruptions caused by COVID, war and other fluctuations, the impact of asymmetric pricing cannot be overstated. It is also relevant when the rate of inflation is falling. Where firms base their prices on an expected rate of inflation that is higher than is likely to occur there is a comparable rockets and feathers effect across the economy.

ALGORITHMIC PRICING PRACTICES

In their analysis, Ezrachi and Stucke (2017, 2020) explore the significant impact of algorithmic pricing practices on modern market dynamics, highlighting how these practices reshape the competitive landscape

in ways that are new and often challenging for consumers to navigate. They emphasize that the development of self-learning and independent computer systems, such as machine learning algorithms, has introduced complex legal and ethical dimensions to the relationship between humans and machines, particularly in terms of control and accountability.

Ezrachi and Stucke note a paradigm shift in commercial practices and pricing mechanisms due to increased automation and technological advancements. This shift is characterized by a move away from traditional, human-led pricing decisions to those dominated by algorithms. This change is underpinned by a growing reliance on the internet and digital technologies, which has not only accelerated the decline of high street trade but also broadened the scope of digitalized markets, encompassing everything from stock trading to online retail and services.

Furthermore, Ezrachi and Stucke highlight that with the rise of data-driven business models, companies are increasingly turning to algorithms that learn from data to make predictions or decisions. This marks a stark contrast to the past when pricing decisions were made by humans after monitoring market activity, a process that was slower and less responsive to real-time market changes. In contrast, modern algorithms can assess and adjust prices instantaneously, allowing for dynamic pricing and market segmentation that can optimize prices based on factors like stock levels and anticipated demand.

A critical aspect of their analysis focuses on the spectrum of possible illicit conduct in the realm of competition enforcement. Ezrachi and Stucke argue that we are moving from an era of explicit collusion, typically among executives, to a more complex environment where algorithms independently adjust to each other's prices and market data. This subtle form of collusion, facilitated by algorithms, may not involve anticompetitive intent or explicit agreement among firms, yet it can lead to market conditions where prices are inflated beyond competitive levels.

Ezrachi and Stucke categorize different scenarios of algorithmic collusion, ranging from direct human instructions executed through computers to more intricate cases where algorithms subtly enhance market transparency and predict behaviour. These algorithms can lead to conscious parallelism and higher prices, or to parallel accommodating conduct, which, while individually rational, collectively weakens competitive incentives to reduce prices or offer better terms to customers.

They cite instances, such as in the petrol station business in Germany, where enhanced market transparency, facilitated by algorithmic pricing, paradoxically led to increased prices rather than promoting competition. Retail petrol prices increased significantly when compared to a control group, illustrating the unintended consequences of algorithmic transparency in pricing.

Ezrachi and Stucke highlight the emergence of a 'hub-and-spoke' conspiracy model in this context. When multiple competitors use the same third-party pricing algorithm, it enables a single company, the 'hub', to have a substantial impact on industry prices. This situation raises concerns about the potential for reduced competition and the creation of market environments where consumer choice is limited and prices are artificially high. This is in contrast to the traditional 'messenger' model where companies collude through direct communication.

The advent of these pricing behaviours poses new challenges for regulators which will only be exacerbated by the increasing complexity and availability of Artificial Intelligence. Without an agent making an active decision to collude and with a positive determination of the liability borne by the use of algorithms and AI, offences become impossible to prove.

These pricing behaviours are also impacting workers' wages. Uber, for example, offers drivers different fares for the same route according to evidence provided by the Transport Workers Union. Users know, anecdotally, that information gathered by the app also impacts prices offered by the service—like battery life remaining and number of times the app has been checked for a ride.

The outcome of algorithmic pricing practices is the erosion of consumer surplus, which becomes increasingly captured by firms, increasing profitability and accelerating inflation due to aggressive price discrimination coupled with dynamic price floors. This report discusses price-discrimination below.

PRICE DISCRIMINATION

Price discrimination is widely practiced in business. Although it takes many forms the most obvious is when different customers are charged different prices for the same product by the same firm. This practice can seem unfair, but it may also have an economic justification or at least not be economically harmful. It could take the form of rich customers paying more and poor customers paying less. Sometimes it can be used to generate more supply. For example, a traditional example has been the establishment of public utilities – say railways. If prices are set high for better off customers (who may be rewarded with first class cabins) and low for customers who cannot afford the high prices but who are willing to pay for more humble carriages or seats the benefit may be considerable.

However, in the modern circumstances price discrimination is being carried to extreme proportions.

Technology, data availability and sophisticated pricing methodologies are driving its spread. Price discrimination is not illegal except in the narrow case of ‘predatory pricing’ under the competition law and sometimes it can be marketed as misleading and deceptive manner raising consumer protection law issues.

In this report we briefly discuss two examples. The first concerns the price of electricity and is included in our case study of electricity in the next chapter. This chapter then draws attention to the fact that for every consumer bill of \$1000 there is an apparent ‘excess charge’ of \$205.61 relative to prices charged to large business customers and not accounted for by genuine price differences.

Regarding gas retail prices there is a similar differential – in this case the apparent ‘excess charge’ \$348.24 in every AGL consumer gas bill of \$1000. On the face of this does not seem to be fair, reasonable or the product of very competitive market.

Later in this report we discuss price discrimination by medical specialists.

CASE STUDY BANK PRICING PRACTICES

The final report of the *ACCC Retail deposits inquiry published in December 2023* explores bank pricing practices (Retail Deposits Inquiry, ACCC 2023).

A key finding is that competition for retail deposit customers is often selective and opaque rather than general and transparent.

Incumbent banks have largely responded to price competition with strategies to retain higher value customers through targeted ‘below the line’ pricing or seeking to acquire new customers using time limited price competition (such as introductory interest rate offers).

Indicating how concentrated the sector is, major banks rarely refer to non-major banks in internal pricing papers and ‘some major banks do not consistently aim to match the interest rates of price leaders’ (Retail Deposits Inquiry ACCC, 20223, p. 84).

Banks recognise their customers are ‘sticky’ and they invest in strategies to increase customer stickiness. This enhances banks’ ability to respond to price competition selectively rather than through broader pricing changes which may trigger competitor responses that reduce margins.

The report emphasises that strategic pricing strategies of banks lead to greater complexity for consumers and some poorer outcomes.

The ACCC emphasises that banks typically seek to minimize their retail deposit funding costs and may use short term and limited time offers such as term deposit specials and introductory offer products.

Bonus interest rates and introductory interest rates can boost the headline interest rates consumers can receive, however the actual interest rates received by many consumers are lower.

For savings products, changes in headline interest rates are often driven by changes to a bonus or introductory interest rate rather than the base interest rate.

Furthermore, the tactics banks use to retain or win higher value customers can be very selective and only a proportion of customers may benefit. Offers can be highly conditional to encourage 'sticky' behaviour in customers and establish a 'main financial institution' (MFI) relationship. Alternatively, these offers are only available to specific segments of the customer demographic, such as those in early adulthood or those with larger deposit volumes.

The Commission notes that in the first half of 2023, seventy-one percent of bonus interest accounts did not receive the bonus interest rate on average each month.

It also notes that banks use fees and charges to recoup operational costs from their customers, including those on retail deposit products. However, the fixed nature of fees means they have a more significant impact on retail deposit accounts with smaller balances.

More generally, the Commission says, banks strategic pricing at the product and customer level makes retail deposit rates opaque and adds complexity for consumers engaging in the market. Interest rates for the same type of retail deposit product can vary significantly between, and sometimes within, banks. This rate dispersion is most pronounced with savings products.

The report notes that these pricing practices engaged in the context where the consumer engagement is low, comparing products can be challenging, and it is difficult to switch accounts.

We return to a more general overview of bank pricing practices later in this report.

CONCLUSION

The above studies of a selection of business pricing practices indicate that many pricing practices are not in the interests of consumers.

This section of the report has described a small selection of business pricing practices that aim to exploit the willingness and ability of some consumers to pay more than others. We call these attempts to transfer consumer surplus to producer surplus where producers gain by having prices that are above competition levels and that are made possible by the absence of perfectly competitive market conditions.

This absence can reflect:

- limited number of competitors
- limited customer information
- limited consumer mobility that would enable them to switch to other suppliers

In these circumstances there is a case for a more active public policy for investigation and analysis of pricing practices that operate at unwarranted cost to consumers. In some cases the policy outcomes could be:

- practical steps to increase competition by the application of competition law, or the removal of government restrictions on competition
- the provision of better information to consumers
- the lessening or removal of obstacle to consumers switching to other suppliers
- the exposure and sometimes the shaming of exploitative business practices and of the kind shown here.

These case studies illustrate a more general point. The Australian economy is much less than fully competitive. It creates many opportunities for producers to extract their more than fair share of surplus.

The practices described are not unlawful, but they reflect an imbalance between consumers and the power of business. Price control is not a solution in most or all cases. However, there is a case for governments exercising much closer scrutiny over these practices and for such scrutiny to be a regular part of the policy agenda.

7. CASE STUDIES

This section of the report undertakes some case studies of sectors where there is or may be price exploitation or price gouging.

AVIATION

There is a lack of competition in the aviation industry both internationally and domestically.

Since World War II, the industry has been heavily regulated, although there has been a significant weakening of the regulation over the years. During WWII it was decided that post-war restrictive rules would be set which would have the effect of enabling every country to have its own national flag carrier, if desired by that country.

This led to a global industry dominated by bilateral bargaining, whereby an airline would be allowed to enter another country's market providing that country had reciprocal rights. The rules essentially restricted competition. It made entry by third parties difficult.

Domestically Australia adopted a two-airline policy in the 1950s, and since then there remains two dominant airlines. In the early 1990s there was serious entry by airlines such as Compass which saw prices go down very sharply, but these airlines did not survive. In 2001 Ansett collapsed and was ultimately replaced by Virgin. Qantas and Ansett had roughly equal market shares for many years, however, when Virgin entered the market, Qantas share of the market was about two-thirds of the domestic aviation market and it has remained about the same since then.

Since COVID, Qantas's profit has significantly rebounded from COVID shutdown, and profit to June 2023 increased to \$1.7 billion, up 208% from its FY2019 net profit after tax level. This significant profit increase comes at a time of significant damage to its service reputation and as an employer.

Part of the strong financial performance can be attributed to significant Government support to Qantas during the pandemic. Qantas received more than \$2 billion in assistance, including more than \$856 million in JobKeeper. While Virgin also, received Government assistance, it was not enough to keep it afloat and Qantas's main competitor entered into administration and closed its budget arm, Tiger.

FIGURE 7.

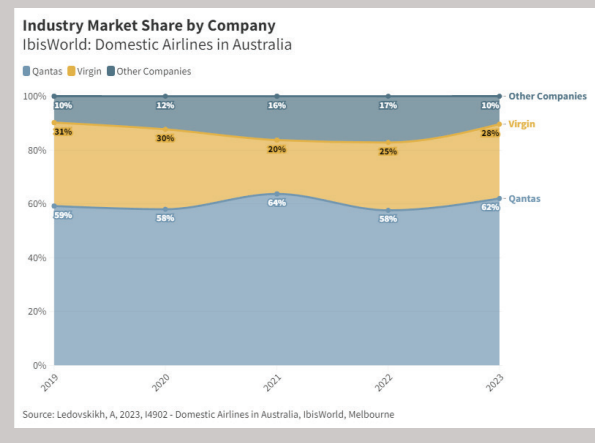
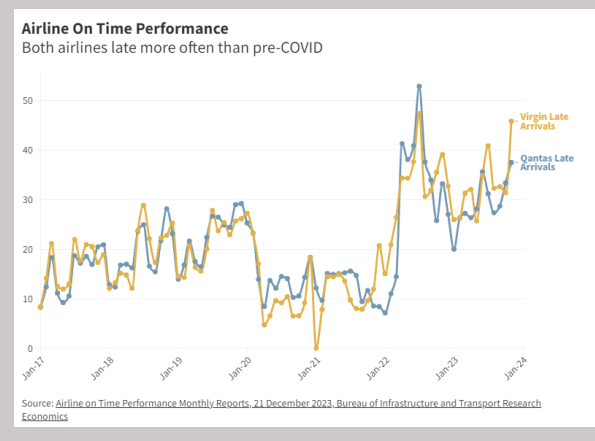


FIGURE 8.



Qantas' service delivery returning from the pandemic shut down became so derided the term 'Joyced' entered into popular Australian usage to 'describe being severely inconvenienced at an airport by flight cancellations or luggage going astray' (Fildes and Georgiadis, 2022). Internal documents published by the Australian Financial Review showed that 'the percentage of consumers who said they trusted Qantas had fallen from 70 per cent in August to just 49 per cent' (Loussikian and de Kreseter, 2023). Both airline's cancellation rate since COVID has dramatically risen. In 2017-19, Qantas' cancellation rate was 2%, which has increased to 4.4 per cent in 2022-23.

Despite the reputational issue, during 2022 Qantas reduced capacity on its domestic services. In June 2022 it announced to the ASX that it was "adjusting its domestic capacity levels for much of FY23 to assist with the recovery of sustained high fuel prices". In May Qantas cut capacity by 10 per cent. During July and August, it expected to reduce capacity a further 5 percentage points and then planned a cut of 10 percentage points in October.

Qantas' said at the time that "The customer impacts from these schedule changes are expected to be minimal, with capacity being removed mostly from high frequency routes. Those affected will be contacted directly with alternatives as close as possible to their original timing, usually within 1-2 hours" (Qantas 2022). This assessment is not credible.

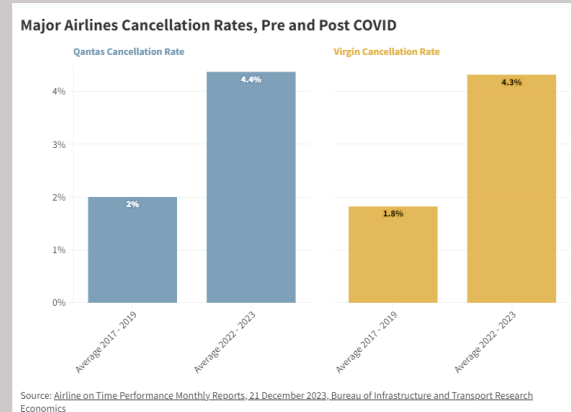
During this time Qantas was also cancelling flights at a higher rate and frustrating customers. Qantas has been accused of making cancellations as part of a deliberate strategy of "slot hoarding" (Visontay 2023).

Qantas' ability to reduce supply while increasing prices and suffering no material loss of market share, may have affected CPI in December 2022, and therefore may have impacted the Reserve Bank's inflation expectations and rate increases.

Most recently, the ACCC has taken action against Qantas for advertising and selling tickets for flights that it had cancelled. In its defence, Qantas is reported as saying "it doesn't sell customers tickets to any particular flight, but rather a "bundle of rights" that includes alternative options in the event of cancellations" (Visontay 2023).

The recent events surrounding the blocking of Qatar airlines to the Australian market are very well-known

FIGURE 9.



Qantas fare increases over the three months to December 2022 were large enough to produce a sizable increase in the "holiday travel and accommodation" contribution to inflation, possibly up to 25 per cent of the increase that quarter as it appeared in the ABS CPI measure (ABS 2022). A quarter of the inflation that month was mainly due to Qantas aggressively raising airfares although Virgin may have also contributed.

and need little reference here. In essence Qatar offered a solution to the extremely high prices that were being charged for international travel. Qatar offered to add heavily to capacity by making available multiple planes and multiple seats. The likely effect could have seen 40 per cent off the price, according to Virgin CEO Jane Hrdlicka, speaking on RN Breakfast (29 August 2023).

However, this proposal was blocked by the Australian government. Quite clearly it was acting in the interests of Qantas. Following the expression of public concern, the Government has launched a discussion paper on future aviation policy. It is important that this paper deals with serious restrictions on competition. In the domestic market, of particular note, is the difficulty of new entrants to the industry gaining slot allocations at major airports - the same problem that dogged third airlines trying to enter the market in the 1990s. There are also many restrictions on international competition.

As noted elsewhere in this report, during the period 1995 until about 2007, the Commonwealth imposed quite strict requirements on State Governments to comply with the underlying principles of the NCP.

In particular, public independent reviews of anything anticompetitive was required, with the Commonwealth putting pressure on states to with financial incentives and penalties to ensure compliance. What was little noticed at the time was the Commonwealth itself did not engage in comprehensive reviews. The strongest example is in the aviation industry.

This is why it is important that a 'third party' review of aviation competition should be undertaken by the NCP review processes. Commonwealth and State governments have agreed that there will be resumption of a NCP, and aviation policy should be part of it.

Although there has been at least one significant price war between Qantas and Virgin (some years ago), pricing in the market has been essentially stable. Evidence from the 1990s indicates that the presence of a third major player in the market can have a significant effect on prices.

Currently, there appear to be a number of policies and practices that make substantial entry by a third player difficult, for example, restrictive slot allocation practices at major airports. These and other conditions need to be reviewed. Similarly, competition for international flights is also limited by regulations – principally regulations imposed under international air services agreements.

A recent speech by the Hon Dr Andrew Leigh, MP Assistant Minister for Competition Charities and Treasury observed that by analysing microdata from the Bureau of Infrastructure and Transport Research Economics, increased competition within routes dramatically affects airfares. With a second airline reducing fares by 29% and a third operating airline reduces prices again by 31%. Consumers would be paying less than half of the monopoly price on a given route if three airlines were competing against one another.

The Government is currently reviewing aviation policy. The current review is being conducted by the 'sponsoring department' of the airlines – that is the Department of Infrastructure, Transport, Regional Development, Communications, and the Arts. The Commonwealth and State governments have just announced that they will attempt to revive the National Competition Policy which operated from 1995 until 2006 before fading into insignificance. One feature of that claimed policy success, which is typically not mentioned, is that the Commonwealth was less than fully serious in the application of principles of competition policy to its own activities including aviation policies.

RECOMMENDATION

The current review of aviation policy led by the Commonwealth Department of Infrastructure, Transport, Regional Development, Communication and the Arts should remove restrictions on international aviation which are harmful to the interests of consumers. It should also review and remove anticompetitive restrictions on allocation of slots at airports. Regarding any remaining restrictions on competition following this review there should be a separate review led by the Commonwealth Department of Treasury as part of the National Competition Review.

AIRPORTS

Airports have a very high degree of monopoly as has been repeatedly emphasised in ACCC reports. However, its calls for price regulation have always been rejected seemingly with weak reasons. It is recommended that the ACCC recommendations for airport control be adopted.

BANKS

Australia's banking system is one of the most concentrated among advanced economies. Only Germany among the G7 nations has a higher banking concentration than Australia. Australia's 91 per cent concentration is well above the 85 per cent concentration in Canada let alone the 63 per cent concentration in Japan, the 60 per cent in the UK and 50 per cent in the United States.

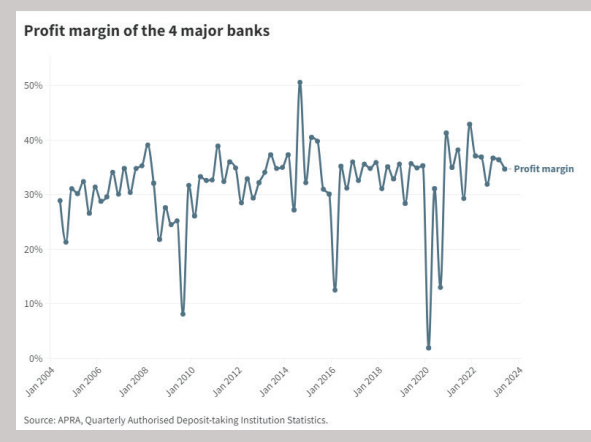
As a result, Australia's major banks are well positioned to achieve gains at the expense of their customers. This is most obviously observed in the response to changes in the cash rate by the Reserve Bank. Over the period from October 2011 until October 2019 the Reserve Bank reduced the cash rate by 400 basis points from 4.75 per cent to 0.75 per cent. Through that period the average standard variable home loan rate for owner-occupiers was reduced only 299 basis points from 7.79 per cent to 4.80 per cent. While few borrowers actually pay the standard variable rate, the average discounted home loan rate which is more representative of the rate of new home loans fell an even less 288 basis points from 7.03 per cent to 4.15 per cent.

Similarly, the average small business overdraft loan fell only 304 basis points. While most Australians view changes to the cash rate as the marker for home loan rate changes, in reality banks are able to avoid passing on the full cuts. In October 2012 for example, all four major banks cut their home loan rates by less than the 25 basis point cut of the cash rate. At such times banks invariably claim funding costs, and yet a majority of bank funding costs now come from domestic deposits. For example, the then Chief Executive of the ANZ, Philip Chronican, argued that "recent stability in wholesale funding markets has been offset by the impact of intense competition for retail deposits." (SMH, 2013) If the competition for deposits were real, we would expect over the period that term deposit rates would have fallen by less than the cash rate, however the interest rate for average 1 year term deposits (\$10,000 minimum) fell 410 basis points, while the average 3 years rate fell 440 points.

Even in the period just prior to the pandemic, when the Reserve Bank reduced the cash rate by 75

Australia's Big 4 banks not only have experienced larger profit margins over the period that the Reserve Bank has been raising rates since May 2022, but they have been able to raise their margins by enough to enable their profits to have been higher through the entire period of the pandemic than they experienced on average in the 15 year before the pandemic.

FIGURE 9. PROFIT MARGIN OF THE 4 MAJOR BANKS



basis points from 1.5 per cent in May 2019 to 0.75 per cent in October that year, the average discounted home loan rate only reduced 53 basis points. Once again, funding costs were used as the justification. In October, Westpac’s Chief Executive (Consumer) Jason Yetton stated that the bank’s decision to cut home loan rates by just 15 basis points rather than the 25 basis point reduction in the cash rate was because it “took into account the reduction of the official cash rate and the commercial pressures of the low interest rate environment”. (Westpac Media Release, 2 October 2019)

However, figures from APRA show that the profit margin of the 4 major banks in 2019 was no lower than it had been for most of the previous 15 years aside from exceptional periods such as the peak of the GFC.

Moreover, a research paper presented by the Reserve Bank in 2023 (Windsor et al 2023), which examined the profitability of banks under differing interest rate found that while the net interest margin of banks was affected by low interest rates, the impact was extremely marginal. They found that “on average across countries, a 100 basis point fall in short-term interest rates results in a 5 basis point decline in net interest margins in the short run.” But they also found the impact on actual bank profitability was negligible. They noted concluded that “the effect of lower interest rates on net interest margins is larger than the effect on asset returns, suggesting that banks can shield overall profitability in the face of lower interest rates”.

Australian banks certainly have shielded their overall profitability during the years including the pandemic and the re-opening. As the Reserve Bank has raised the cash rates, banks have increased their standard variable rates in lockstep. Fortunately for consumers the average discounted rate rose just 361 basis points reflecting the continued strong demand for home loans and record level of re-financing. However, despite the continued reliance on deposits for banks’ funding the average term deposit rate rose just 360 basis points.

Australia’s Big 4 banks have not only experienced larger profit margins over the period that the Reserve Bank has been raising rates since May 2022, but they have been able to raise their margins by enough to enable their profits to have been higher through the entire period of the pandemic than they experienced on average in the 15 year before the pandemic – taking into account the mining boom period, the GFC, and the recovery.

Further evidence of a lack of competition comes through their offerings for mortgage refinancing. As interest rates have increased, banks have wound back programs which seek to win refinanced loans from mortgagees. Commonwealth Bank CEO Matt Comyn recognized this, “We led the change that’s been adopted by most players” (Comyn in Barret, J., 13 Aug 2023, ‘Australian lenders withdraw cashback offers as competition slackens, The Guardian). Mr Barrett noted that “Several major banks, including NAB and Westpac, promptly withdrew their own offers, leaving ANZ the only member of the big four to still offer the cash enticement. But it announced it was halving its top offer from \$4,000 to \$2,000 later this month.” Australian consumers have not been well served by our banks. Other than during a period of total lockdown of the pandemic did banks see any reduction in their profitability, and as consumers suffered from fast rising prices, efforts by the Reserve Bank to limit inflation through higher interest rates only served to see the banks, led by Westpac, the Commonwealth Bank, NAB and ANZ increase their profit margins above long-term levels.

Over the years there have been few signs of strong price competition between the banks. There was a period of greater competition before the Global Financial Crisis when there were many new entrants into the industry, and they provided greater competition in home loans and small business lending but this faded some fifteen years ago and

TABLE 1. PROFITS MARGINS OF AUSTRALIAN DEPOSIT TAKING INSTITUTIONS

	2005-2020	March 2020-March 2023	June 2022-March 2023
All Deposit taking Institutions	29.1%	30.4%	33.7%
All Banks	29.4%	30.6%	33.9%
Big 4 Banks	32.4%	32.0%	35.5%
Other Domestic Banks	19.1%	23.8%	26.0%

Source: Author’s calculations based on APRA, Quarterly Authorised Deposit-taking Institution Statistics.^{7,8}

7 All figures for average lending and deposit rates are from the RBA Tables F.4, F.5 and F.7.

8 In the 18th months from April 2022 to September 2023 a cumulative \$46.5bn worth of new housing finance (excluding re-financing) was borrowed compared to \$32.2 bn in new housing finance in the 18 months prior the pandemic in March 2020. In the same 18 month period to September 2023 a record 455,411 loans were re-financed, some 86% more than the 245,223 re-financing loans undertaken in the 18 months to March 2020

a high degree of concentration resumed. Many new players left the market or were taken over by the major banks, such as St George, BankWest, Bank of Melbourne and others. A review of the profits and history indicates that the profits have been steady, stable and increasing over time and there have been few signs of strong competition in areas such as consumer matters and in relation to small business and farmers.

The ACCC was provided with a Ministerial Direction by Treasurer Chalmers in February 2023 to conduct an inquiry into Retail Deposits which reported in December 2023. The conclusions set out above in this report are confirmed and reinforced by the ACCC report. A major conclusion is that there is little evidence of aggressive broad scale price competition particularly from large banks. Although this finding relates to recent times, it is also true of bank behaviour over the last fifty years or more.

Instances of price competition over the years have nearly always been triggered by small competitors (which these days are the shrinking part of the market). This price competition has been limited, with the ACCC noting that major banks only rarely include references to the prices of smaller competitors in their pricing decisions, generally focusing on other major banks.

The report notes that banks have relied heavily on conditional and time limited interest rate offers in recent years. Increases in headline interest rates for savings products are often driven by increases in a bonus interest rate or introductory interest rate rather than the base interest rates. The conditional nature of bonus interest rates and introductory low interest rates mean according to the ACCC that the amount of interest actually received by consumers (that is the effective interest rate) can be considerably lower than the headline interest rates suggest.

The ACCC found that 71 percent of bonus interest accounts did not receive the bonus interest rate on average each month over the first six months of 2023. That accounts with larger balances were more likely to trigger bonus conditions is at least one indication of the time or resources required to maintain a bonus interest rate, both of which are in short supply for many families. For example, those in irregular work may not meet the minimum regular deposit threshold to trigger bonus interest (ACCC, 2023, p. 94).

The ACCC also found that banks pricing strategies include 'below the line' pricing – offering targeted specials to particular customer cohorts and negotiating more generous interest rates with individual customers who are of higher value to the bank.

There is nothing unlawful in bank behaviour. The ACCC notes that in markets with low consumer engagement and high searching and switching costs the lack of transparency over widespread selective pricing means that any benefits of competition are confined to segmented groups of consumers rather than consumers more generally.

Widespread strategic and selective pricing also adds difficulty for consumers when seeking to locate key product information and compare market offerings. This lack of transparency may also damage consumer confidence in the market.

The report also contained detailed information about why the interest rates received by consumers do not automatically follow movements in the cash rate target. Whilst average effective interest rates for term deposits and bonus interest accounts were above the cash target from 2022 until mid-2022 they were both below the cash rate target as of June 2023.

The ACCC report emphasises that the sector is concentrated with barriers to entry and expansion, and the competition for retail deposit customers is often selective and opaque. It makes seven recommendations which this report supports.

The report's principal recommendation is that there be continued monitoring of prices and competition in the retail deposits market. This recommendation is sensible and accords with this report's recommendation that there needs to be greater scrutiny of this market. Retail deposits are one critical side of the story and lending should also be more closely monitored.

Both aspects of the retail banking industry are highly important to large cohorts of the Australian community and both are equally as concentrated.

The ACCC issues further recommendations relating to conduct and transparency from banks to ensure fairer engagement with customers. Banks should be more transparent, comparable, and proactive in alerts and reports to customers and the public about deposit and bonus rates. Intermediaries play a role here too, and the ACCC notes that there are conflicted arrangements with comparison websites, and these should be transparent.

It is recommended by this report that there should be full bank account portability for consumers and small businesses. The public has been waiting too long for serious competition between the banks. It is time to make bank accounts fully portable so that customers can switch banks in the same way as they have been able to do so with their telephones ever since telephone numbers were made portable.

REMITTANCES


Remittances, a crucial financial lifeline for many, are funds sent by family members working abroad to support their loved ones in their home countries. These transfers play a pivotal role in the economies of Pacific Island countries, providing a critical source of national income and acting as social safety nets, especially where social security programs are underfunded. Remittances cover essential expenses such as schooling, food, housing, healthcare, and provide capital for business investment, especially benefiting women.

TransferWise, a fintech company now known as Wise, reports that the market for remittances in Australia is approximately \$10 billion. This sum represents money earned by Australian families and sent to relatives abroad. Despite the importance of these remittances, the cost for facilitating these transfers remains high, amounting to about 7.22 per cent of a transaction's cost, which translates to nearly \$722 million taken by banks and remittance providers.

Despite international policy efforts, fees for remitting to Pacific Island countries are among the highest globally. These high costs impact not only the individuals sending money but also the overall economic well-being of the recipient countries. The Lowy Institute notes that if remittance costs to Fiji, Tonga, and Vanuatu were reduced to the United Nations' target of less than 3 per cent per transaction, it could save more than \$79 million annually for households in these countries. The Australian government is encouraged to better support Pacific workers under its temporary labour scheme by utilizing existing financial architecture and enhancing digital capabilities in the Pacific region to alleviate these costs.

The submission to the ACTU Inquiry into Price Gouging and Unfair Pricing Practices by Wise, highlights significant issues in the market for international payments, particularly remittances. Wise points out that this market is fundamentally broken, marred by unfair pricing practices that enable the gouging of customers, especially migrant workers and other vulnerable members of society. These practices contribute to record bank profits both in Australia and globally and could be significantly mitigated by government action to increase transparency in pricing.

The submission also criticizes the current regulatory framework for international money transfers in Australia. While the ACCC's "Best Practice Guidance" requires the disclosure of the total price of an International Money Transfer (IMT) upfront, including any correspondent banking fees, it does not mandate disclosure of hidden fees in the retail exchange rate markup. This lack of transparency in pricing allows banks and remittance providers



This lack of transparency in pricing allows banks and remittance providers to continue gouging customers through these hidden fees.

to continue gouging customers through these hidden fees. The submission argues that this opaque form of pricing prevents consumers from understanding the true cost of a transaction until it is completed, thereby limiting their ability to make informed decisions and seek better deals.

It is clear that the foreign exchange market is not sufficiently competitive and there is a lack of price transparency for vulnerable users of the service. This market needs to be kept under continuous review.

EARLY CHILDHOOD EDUCATION AND CARE

One of the most significant costs facing working parents is the cost of early childhood education and care (childcare). Early childhood education and care is a unique industry and one which has pricing dynamics like no other. Despite the urgent need among parents for available and accessible childcare, the demand for the service far exceeds the availability of it. The market for childcare cannot be understood to be one national market, but a series of overlapping, highly localised markets.

One of the key findings of the Australian Competition and Consumer Commission's (ACCC) report on childcare is the highly localised nature of childcare markets. Childcare centres primarily compete within a 2-3km radius, as most parents prefer not to travel more than 15 minutes for care. The ACCC's survey indicates that location and availability are the most crucial factors in parents' decision-making processes for childcare. This localized demand significantly limits the scope of competition among centres. While affordability influences how much care parents use, once the decision to use a particular amount of care is made, price becomes a less important factor compared to other considerations. Surprisingly, the ACCC report notes that fees are higher in local markets with more childcare services, often in wealthier areas where parents can afford to pay more, indicating weak price competition in the sector.

Another factor impacting competition in the childcare market is the low rate of switching providers among parents. The ACCC found that 65 per cent of surveyed parents had not switched providers since 2020. A notable portion of these parents cited the potential disruption to their children as a primary reason for not switching, even if a better-quality or lower-priced centre was available. The transition to a new environment and the need to build new relationships with educators are significant barriers, dampening competitive dynamics. Additionally, judging the quality of childcare services poses a challenge for parents. Despite the implementation of National Quality Standards, many parents are not fully aware of these standards and find it difficult to assess key aspects of quality, such as educator standards. This difficulty in assessing quality further complicates parents' choices in the childcare market.

The interim report also highlights the issue of rising childcare fees, a significant concern for both parents and governments. Between 2018 and 2022, childcare fees increased by 20 per cent to 32 per cent across various service types. While government subsidies have mitigated some of these increases, out-of-pocket expenses for childcare have still grown at a rate surpassing wage growth over the past five years. These escalating costs disproportionately affect low-income households, as the ACCC's analysis shows that out-of-pocket expenses as a share of disposable income are higher for households in the bottom 10 per cent of income earners, despite receiving higher subsidies.

Early Childhood Education and Care in Australia is a lucrative business....

...for profit childcare providers consistently have higher margins than not for profit childcare providers...

Unsurprisingly, the operating margin and occupancy rate is positively correlated, showing that in areas with excessive demand providers are able to dominate their market.

Early Childhood Education and Care in Australia is a lucrative business, generating around \$14 billion annually. Approximately 80 per cent of this revenue is derived from government funding, primarily through ‘childcare’ subsidies. This steady flow of public money has attracted large financial interests, leading to a concentration of ownership by big companies. The five major players in the sector – G8, Affinity, Guardian, Busy Bees, and Only About Children – control about 20 per cent of long day care centre revenue. These companies collectively reported earnings of \$292 million in 2020, underscoring the profitability of private ECEC provision.

The ACCC has found that for profit childcare providers consistently have higher margins than not for profit childcare providers, 9 per cent as opposed to 6 per cent and that these margins have greatest divergence among small providers. The ACCC finds that this is consistent across all geographic and socio-economic areas, with small for-profit providers having an average profit margin of around 20 per cent in 2022, with the same cohort of not for profit providers having a negligible margin. Interestingly, the ACCC also found that large for-profit providers pay lower wages and prefer to hire less experienced teachers.

Unsurprisingly, the operating margin and occupancy rate is positively correlated, showing that in areas with excessive demand providers are able to dominate their market. Despite the ACCC finding that the sector is generally profitable, the largest early childhood education and care providers pay little to no tax.

The Albanese Government increased childcare subsidies on July 10, however the ACCC notes that they have observed “internal pricing decision documents that explicitly reference optimising the Child Care Subsidy for households to maintain or increase revenue.” Despite the policy being well intentioned, the limited effectiveness of competition in a market for a service like childcare, the non-financial costs and hurdles of both comparing childcare centres and switching means that centres – especially for-profit centres – are more able to capture the subsidy.

While the ACCC found that most childcare entities are not making excessive profits, that entities have both a privileged position, the insulation from competition, and reports from users that subsidies have been eaten in fees paints a compelling picture. While general gouging is likely not occurring, those larger for-profit centres have the ability to do so and this is concerning.

There are similar concerns about pricing in aged care, in disability services and yet other areas. There is a need for review of those. The central recommendations made by the ACCC would go a long way to fixing issues faced by parents.

OTHER AREAS OF CARE

There are also concerns about pricing of care in other sectors. A particular case in point concerns prices to provide services to persons with a disability under the auspices of the National Disability Insurance Scheme. The recent independent report on the operation of the scheme confirms what is widely known: that there is much overcharging in the provision of services.

The best-known form of overcharge is based on the ‘wedding cake’ pricing practice. That is when a vendor knows that the cake being supplied is for a wedding the price skyrockets. There is much evidence that a similar effect has been at work when the NDIS is set to pay for the provision of a service – prices rise to well above the normal levels that are charged for these services to persons with disability who are not covered by the NDIS. The Australian government has recently referred this matter to the ACCC to clamp down on these practices and has provided substantial funding for that purpose.

Attention should be given to the possibility that ‘wedding cake prices’ are being applied in other sectors – especially care sectors where government is the ultimate payer.

ELECTRICITY

There have been large price increases in recent times. Some have been driven by international factors such as war, and these increases would have been greater but for government intervention in setting price caps for gas and coal.⁹

9 Much of the analysis and contribution to this chapter has been provided by Professor Lynne Chester, University of Sydney and is outlined in great detail in her 2024 paper, Australia’s National Electricity Market: Bidding rules, market power and wholesale electricity prices.

There are, however, domestic drivers of high electricity prices which this report considers below (along with some comments on gas prices).

Wholesale price increases were responsible for the rapid increase in electricity prices in the early to mid-2000s and most recently in 2022 and 2023. In 2022-2023, wholesale prices were around 33 per cent of a typical bill in 2023-2024 but increased to around 43 per cent of a typical bill.¹⁰

There is a significant degree of concentration in the industry. The wholesale (or generation) component is highly concentrated, as is retail, with the impact on market power strengthened by a high degree of vertical integration between wholesale and retail activities in 'genretailers'. As well marketing practices in retail, as discussed below, reduce competition further. And network (or transmission and distribution) supply is also delivered, across Australia, by regulated monopolies.

The components of a typical electricity bill in 2023-2024 are:³

- 43 per cent for generation costs (that is wholesale cost)
- 35 per cent is for the network charges of transmission and distribution
- 4 per cent are for environmental costs
- 18 per cent are for retail charges

Below we focus briefly on:

- a. the wholesale market and how its effect on prices is influenced by a significant degree of concentration and a price bidding system which can cause price gouging;
- b. the network or transmission component where prices have been regulated but this has not always produced the best outcomes for consumers;
- c. the retail market. This report focuses on price discrimination and on impediments to retail competition.

WHOLESALE MARKET

2022 saw record wholesale electricity prices, \$200 per MWh across the NEM in the second and third quarters compared to under \$100 per MWh in 2021. These prices flowed through to households. Estimated electricity bills increased by 9 per cent to 20 per cent in 2022-23 from the previous year¹² and the regulated price cap set by the AER (the default market offer) increased by 21 per cent for customers in NSW and Queensland.¹³ Since then, wholesale prices have more than halved and are again below \$100 MWh.¹⁴

The wholesale market has experienced volatility before. For example, in 2018 wholesale prices in Victoria and South Australia increased sharply after the Hazelwood Power Station closed.¹⁵

These high price events were triggered by changing supply conditions. In 2018 it was closure of coal plant. In 2022 it was flooding of coal mines combined with increases in gas and coal costs. It is reasonable to expect such events to have price implications. However, market power in generation combined with the current market design, resulted in excessive price increases in 2022 and 2023 and unnecessary price volatility.

Historically concentration of ownership of baseload coal plant contributed to generator market power. Market power in baseload generation is breaking down with high investment in renewable energy capacity. However, growth in renewables brings its own market power challenges. Flexible generation is required when solar and wind generation is limited, for example at night or on low wind days. In its Wholesale Electricity Market Performance Report, the Australian Energy Regulator (AER) concluded that there is a high concentration of generation ownership, particularly in flexible generation.¹⁶ Accordingly competition in this part of the market needs continuing scrutiny and design of the wholesale market needs to be reassessed.

10 Estimate by Professor Chester using AER State of the Energy Market 2022 and 2023 data

11 Estimate by Professor Chester using AER State of the Energy Market 2023 data

12 State of the Energy Market 2023, AER, page 226.

13 State of the Energy Market 2023, AER, page 222.

14 State of the Energy Market 2023, AER. See Chapter 3, pp 36-41.

15 State of the Energy Market 2023, AER, page 40.

16 Australian Energy Regulator, Wholesale Electricity Market Performance Report, December 2022.

THE BID PROCESS

The bid process in energy markets, particularly in the context of electricity markets, is a complex yet critical mechanism for determining the price of electricity and ensuring the balance between supply and demand. This process involves electricity generators submitting bids to the market operator detailing how much electricity they are willing to supply and at what price. These bids are submitted for each trading interval, which can vary in duration depending on the specific market rules.

Once bids are submitted, the market operator, the Australian Energy Market Operator (AEMO), sorts these bids in order of increasing price. This creates a 'merit order' for dispatching electricity. The market operator then matches these bids against the forecast demand for electricity in each trading interval. The aim is to find the most cost-effective combination of bids to meet the required demand.

An important aspect of this process is the determination of the market price for electricity. The price paid to all generators for a given trading interval is set by the bid of the last (or marginal) generator needed to meet demand – this is known as the 'marginal price'. Hence, even if a generator bids a lower price and is dispatched, it receives the market price, which could be higher than their bid. This price-setting mechanism is designed to encourage efficient bidding and reflect the true cost of supplying electricity at different levels of demand.

However, complexities arise in this system. For example, generators can rebid their capacity at different prices up to the time of dispatch. This flexibility is meant to account for changing conditions, like unexpected plant outages or demand surges. Yet, it can also be used strategically by generators, especially those with significant market power, to influence market prices. This has led to concerns about the potential for price manipulation or 'gaming' the system, prompting discussions around regulatory reforms to ensure market outcomes align with the broader goals of affordability, reliability, and sustainability in the electricity market.

Professor Chester¹⁷ suggests that price gouging takes place and is permitted under the National Electricity Rules. Generators may rebid right up to a few minutes before they are required to supply electricity, but the rules are weak and the incentive to gouge is enormous.

While there is a statement of reasons required by the National Electricity Rules, AER reports note that rebidding contributes to extremely high price events. These prices can be hundreds of times higher than the national quarterly average and can have a significant impact on average wholesale prices, even if the high price events are short-lived. Table 1.1 illustrates this. It shows how extreme prices in just two 5-minute trading intervals in Queensland had a large impact on the 30 minute price. This and similar events contributed to high wholesale prices in 2022 and the subsequent increase in retail prices.

Professor Chester asserts that derivatives trading subsequently informs the bidding and rebidding strategies of generators in the NEM, and the exercise of market power and this is permitted by the National Electricity Rules. The fact that the volume of derivatives trading surpasses NEM demand (and has for quite some time) is indicative of the speculative activity about future wholesale and retail electricity prices plus the role being played by non-NEM participants such as speculators and hedge funds.

Further, parties to energy market derivatives are players in the National Electricity Market.

TABLE 1.1 BREAKDOWN OF THE 30-MINUTE HIGH PRICE EVENT

Date	Time	QLD 5-minute price (\$/MWh)
31 Jan	6.35pm	1,250
	6.40pm	15,500
	6.45pm	15,500
	6.50pm	690
	6.55pm	552
	7.00pm	552
	Average 30-minute price	5,674

Professor Chester suggests that price gouging takes place and is permitted under the National Electricity Rules.

17 For an excellent analysis see Professor Lynne Chester's 2024 paper Australia's National Electricity Market: Bidding rules, market power and wholesale electricity prices

This provides an enormous incentive for companies to knowingly bid up or fail to bid up prices in order to maximise the value of their bid or minimise their downside exposure. Generation companies also have full knowledge of their derivative contract prices when they submit bids to supply capacity.

Professor Chester asserts that the exercise of market power in the wholesale market has contributed to recent prices shocks:

The AER posits that the drivers of wholesale charge increases have been much higher priced forward contracts influenced by increasingly 'peaky' demand and extreme weather events, closure of the Liddell power station, higher coal and gas costs, and reliability issues of aging coal-fired generation assets.¹⁸ The exercise of market power, however, has also contributed to these increases.

Her view is that consumers would pay lower wholesale costs if the exercise of market power - notwithstanding a highly concentrated market - was not permitted under the National Electricity Rules although she notes there is a difference between the exercise of market power and legitimate rebidding because of operational issues and changes in demand forecasts.

MARKET DESIGN

The wholesale electricity market was established with a very high price cap which has been increased over time. It is now \$15,500 per MWh. The idea was that high prices would provide signals for new generation investment allowing market forces to drive outcomes rather than government planning. Since the market started in 1998 circumstances have changed:

- carbon targets were introduced and have become more ambitious over time
- governments have established renewable targets for electricity market participants
- the Australian Government has established a capacity investment scheme to promote investment in renewable generation and storage.

Now most generation investment in the NEM is driven by government initiatives. Yet the original market design remains in place along with the price volatility inherent with high wholesale price caps. In 2022 the result was price shocks for consumers and windfall gains for generators and retailers. Origin Energy's underlying profits were up 83 per cent in 2022-23 compared to 2021-22, and AGL's were up 25 per cent.

The question is whether the current market design remains fit for purpose given the energy transition underway. Changes could involve refinements to the current market, or more fundamental changes, for example, adoption of a 'capacity market' as used in North America and in Western Australia.¹⁹

Professor Chester's paper touches on the advantages and disadvantages of adopting a capacity market. Capacity markets are the norm in North America and in many other markets including Western Australia. If well implemented, they can address the market power issues that the NEM has experienced with its 'energy only' market.

As it turns out we have inadvertently moved to a hybrid market, part capacity, part energy only. Introduction of the capacity investment scheme along with state government renewable initiatives means most generation investment is now driven by government schemes, and is not a response to price signals in the wholesale market. Arguably consumers are left with the worst of both worlds, the market power associated with energy only markets, and the cost of government schemes. This outcome adds to the urgency of a review.

For over a decade, consumers have endured unnecessarily high electricity prices, first with high network charges, and more recently with high wholesale prices. These high prices have resulted in 'economic rents' for electricity companies. As noted by Professor Ross Garnaut the best way of dealing with economic rents arising from market power is to address the source of market power, either by promoting competition or by

18 Australian Energy Regulator. 2022. Default Market Offer Prices 2022-23: Final Determination, May 2022, p. 2.
Australian Energy Regulator. 2023. Default Market Offer Prices 2023-24: Final Determination, May 2023, p. 3.

19 In capacity markets central planners forecast generation requirements and the generation mix. Tender processes are then run to meet forecast requirements with annual payments to generators over the life of the asset. These payments are supplemented by markets which determine dispatch and provide generators with revenue to cover fuel, maintenance and other costs when they run. Since the markets only determine dispatch, wholesale price caps are set at much lower levels than in the NEM.

effective regulation. When neither is possible it can be appropriate to tax excess profits and return them to consumers²⁰. This inquiry recommends that the independent review of the wholesale energy market consider whether an excess profit tax is warranted given recent windfall gains to electricity generators.

NETWORK COSTS

The second significant component of electricity bills is network charges.

Market power in the network charges components of electricity bills arises because distribution and transmission services are natural monopolies. That is, they are uneconomic to duplicate. Prices for these network services are regulated by the AER. In the early to mid 2010s increases in network prices contributed to substantial increases in electricity prices and consumers were paying too much for network services. Regulated rates of returns were too high, some of the networks, particularly in NSW were inefficient and the regulatory framework accommodated high investment levels in distribution which were not undertaken. In response governments and institutions initiated several changes:

- The Australian Energy Market Commission amended the National Electricity Rules to give the AER additional powers to address inefficient costs.
- The AER reviewed and reduced rates of return for regulated services but as part of mandated regulatory determinations.
- The Australian government removed merits review which had contributed to high rates of return.
- The AER cut operating expenditure of distributors by up to 25 per cent as a result of mandated regulatory determinations.

Since then, network charges have fallen by over 30 per cent in real terms and are now cost reflective.²¹ However, consumers were never compensated for the price gouging that took place at the time.

Over the next few years this will be reversed with substantial new investment in transmission lines such as Marinus Link and HumeLink to support the energy transition. These investments will add to network charges. Ongoing vigilance will be required to limit the impact on electricity bills.

RETAIL MARKET

As a possible example of market power, AGL data provides evidence of price discrimination against retail customers. Table 2 is based on data from AGL's most recent annual report. It must be stressed that the data here relate only to AGL's activities in the customer markets. The first three rows of data are AGL's own figures. The other costs have been derived from AGL data by using other costs not included above and dividing by the total volume of electricity sales to customers. The result is allocated pro rata among all customers. The final row for "margins" is then simply the difference between the revenue row and the identified costs. There may of course be other costs not identified here including head office expenses, depreciation, and many other items.

Subject to the qualifications above the final row of Table 2 can be thought of as a proxy for the profitability of AGL's electricity sales in Australia. Here we find that the margin for residential and small business consumers is higher than large business by \$60.10/MWh which explains close to half the difference between consumer and business charges. From the first row first column of data, revenue per small consumers is \$292.30/MWh, this is \$128.1/MWh higher than large business customers pay. The difference in network costs is \$68.4/MWh leaving an unexplained difference of \$60.1/MWh.

TABLE 2 AGL ELECTRICITY UNIT PRICES: CONSUMERS AND LARGE BUSINESS COMPARED

	Residential & Small business consumers	Large business customers	Difference
	\$/MWh	\$/MWh	\$/MWh
Revenue	292.3	163.8	128.5
Network costs	124.0	55.6	68.4
Fuel cost	23.3	23.3	0.0
Other costs	33.0	33.0	0.0
Margins	112.0	51.9	60.1

Source: AGL (2023) Annual Report 2023.

20 Professor Ross Garnaut, Bannerman Competition Lecture 2023. The lecture is available on the ACCC's website at acc.gov.au.

21 AER review of incentives scheme: final decision April 2023

Putting all this differently, it would seem that AGL needs to explain why consumers are paying \$60.10/MWh more than seems to be justified by cost differentials. That is, for every consumer bill of \$1,000 there is an apparent excess to be explained of \$205.61 relative to prices charged to large business customers and not accounted for by genuine cost differences.

The gas customer sales and cost figures raise similar concerns with the relevant figures set out in Table 3.

As with electricity, Table 3 shows an unexplained premium paid by gas consumers which, this time amounts to 35 per cent of the total price paid. However, in this case AGL's margin appears to be slightly negative in the case of large business gas customers. Nevertheless, there remains a large differential to be explained. In this case the apparent excess to be explained is \$348.24 in every AGL consumer gas bill of \$1,000.

TABLE 3: AGL GAS UNIT PRICES: CONSUMERS AND LARGE BUSINESS COMPARED

	Residential and Small business consumer	Large Business customers	Difference
	\$/Gj	\$/Gj	\$/Gj
Revenue	31.3	11.6	19.7
Network costs	9	1.4	7.6
Other costs	1.3	0.1	1.2
Wholesale costs	10.5	10.5	0
Margin	10.5	-0.4	10.9

Source: AGL (2023) Annual Report 2023.

The discussion here may appear to single out AGL but that is simply because AGL's annual reports are more helpful with the provision of the essential information needed for the calculations. We would expect to see similar results in the other big retailers, Origin and EnergyAustralia, simply because the wholesale prices and network charges must be of similar magnitude. The retail operations involve little more than billing customers. In each case the big three retailers are multiproduct companies with other interests that include generation, gas production and distribution, LNG operations and similar businesses that are pursued by one or more of the big three. Published figures make it difficult to disentangle the contribution of electricity generation and retailing to total profit. Nevertheless, the present examination along with AER and ACCC analysis, supports Professor Chester's findings on market power.

Price discrimination unwarranted by cost differences should not occur in a competitive market because other competitors are likely to undercut the supplier which charges the high prices. The large, unexplained price differences seem to reflect a lack of competition, despite some improvements over time.

In relation to retail charges, data from the AER indicates that competition in the retail sector has improved over time:²²

In 2022–23 we have continued to see an improvement in retail competition, as reflected in the decreases in market concentration, as measured by the Herfindahl-Hirschman Index (HHI), in most jurisdictions. The total number of active retailers remains much improved when compared with 2018–19, resulting in a greater selection of retailers for customers to choose from. In residential electricity and gas markets, smaller electricity and gas retailers have gained customers and market share from Tier 1 retailers (AGL, EnergyAustralia and Origin Energy).

Notwithstanding these improvements three issues remain. The first is that the price impacts from the exercise of market power in generation is still passed onto consumers. Second, comparing retail offerings can be difficult for consumers. Third, many consumers do not, and in some cases do not have the capacity to, shop around for better alternatives. These issues have already been discussed in the section of the report discussing price practices but some further points are added here.

When plans are hard to understand it is easy to misrepresent competitor's prices and the electricity oligopoly has been pursued for just such activities. The big three electricity retailers, Origin, EnergyAustralia and AGL, as well as smaller retailers have been prosecuted for "inappropriate door-to-door marketing activities" (ACCC 2015).

22 Australian Energy Regulator, Annual retail markets report 2022–23, November 2023.

Governments have introduced initiatives to improve retail outcomes:

- Retailers in New South Wales, south-east Queensland and South Australia are required to follow a standard way of setting out their electricity prices including the ‘reference price’.
- The Default Market Offer has been introduced to cap retail prices.
- Energy retail comparison websites have been introduced to make it easier for consumers to compare offerings and switch retailers.

More recently the ACCC has called for further measures to improve retail price outcomes. The ACCC is concerned about the prevalence of conditional discounts (for example pay on time discounts) and especially the impact on hardship customers. Almost one quarter of hardship customers failed to meet their conditional discounts in the third quarter of 2022, resulting in price penalties for those customers. The ACCC recommends policy makers should investigate how best to reduce the number of customers on legacy plans with large conditional discounts, as a matter of priority. It also calls for an investigation of whether current rules around price changes reduce price certainty and contribute to the switching burden.²³ This inquiry encourages governments to act on the ACCC’s recommendations and that the regulators probe the causes and justification if any for the substantial price discrimination.

RECOMMENDATIONS

There should be a review of the design and operation of the wholesale market, as to whether it requires refinements or a fundamental change in the form of a ‘capacity market’ as in North America and in Western Australia. This review should be chaired by an independent expert with input and resources from the AER, AEMO, and ASIC. The level of electricity generation concentration should be kept under review, and there should be close scrutiny of the impact on competition, positive or negative, that could occur in the transition to a re-designed energy market. Price shocks experienced over recent years and evidence of price gouging should be considered.

ASIC should be provided with a Ministerial Direction to investigate the energy derivatives market to ensure that participants in both the National Electricity Market and the markets for derivatives are not misusing their position in either to gain an unfair advantage or influence the price of energy to meet derivative conditions.

Network prices should continue to be subject to close regulatory scrutiny with the long-term interests of consumers put first.

There should be a regulatory review of the high degree of price discrimination in the retail electricity and gas markets.

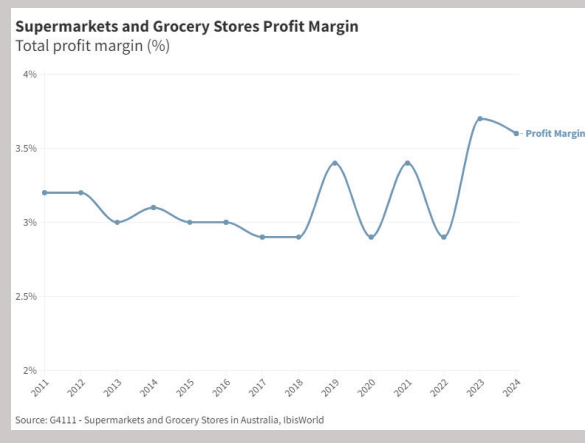
Governments and regulators should continue to introduce initiatives to improve retail outcomes brought about by current market imperfections.

FOOD AND GROCERIES

Australia’s food and grocery sector is amongst the most concentrated in the world and supermarkets and grocery related submissions led complaints to the Inquiry with 325 submissions received raising issues with major retailers. This was more than twice the next largest category of complaints received.

Most significantly, the average profit margin of the sector has remained remarkably stable despite the enormous volatility in prices throughout the domestic economy. Unlike most of the retail sector, supermarkets generally benefited from their position during and after the COVID-19 pandemic. Neither

FIGURE 10.



Coles nor Woolworths experienced declines in profit nor revenue over the pandemic as their main businesses were, rightfully, deemed essential services. This position allowed business continuity and retained their position in the market.

What has occurred since the pandemic, though, is an increase in margins in both Coles and Woolworths food and grocery segments driven by low competitive forces and an ability to not pass on immediate cost reductions. In submissions and testimony, the National Farmers Federation and the NSW Farmers both gave evidence which highlighted both the advantage enjoyed by the major retailers and the limited information available to farmers and producers.

Australia has a highly concentrated food and grocery sector and it is more concentrated than comparator countries like the UK, Germany and the United States. Despite the entry of Aldi, Woolworths and Coles still account for more than 65 per cent the market which contrasts heavily with the United Kingdom where its top four grocers rather than two account for 65 per cent of the market (Ibis World, 2023; UK CMA, 2023).

The public response to supermarkets' price setting in Australia has been more measured than comparator countries, too. Notably, United Kingdom, New Zealand and Canada each launched retail grocery inquiries where despite their relatively lower concentration and increasing competitive forces concerns around the power of price setters needed to be examined.

High prices, including coordinated high prices, are not prohibited by competition law except where there is an unlawful communication or agreement between the parties. With that exception, duopolies are free to charge high prices. The ACCC has no powers to even investigate whether the prices are excessive unless the government requires it to do so.

Duopolies have a mutual incentive not to decrease prices where possible, in particular on goods which have high price recognition. While there are concerns about major retailers unfairly exercising pressure on suppliers, there has not been a price war between the major supermarkets in some years. This contrasts with the UK experience where Tesco and Sainsbury's entered into an aggressive price war with Aldi, running an 'Aldi price-match' scheme which focused on staples (UK CMA, 2023).

While the entrance of Aldi is welcome and action since the last comprehensive inquiry to outlaw retail covenants preventing entry of competitor supermarkets into shared spaces has proven effective at removing a barrier to competition there remain high barriers to entry. It pays to be the only supermarket in the area and without a formal investigation into pricing strategies of the supermarkets it will be difficult to determine whether either major player makes decisions based on the proximity of a competitor. As raised by the ACCC, I remain concerned about the ability for established players to engage in land banking as both a deterrent to competition and to exploit some councils and planners' restrictions on retail industry development.

MARKET POWER OVER FARMERS

The disproportionate market power held by supermarkets and food processors compared to farmers is a significant concern in the agricultural sector. This imbalance manifests in several ways, profoundly impacting the dynamics of food pricing and distribution. Supermarkets and large processors, because of their size and customer reach, wield considerable influence over the pricing and marketing of agricultural products. They are often the primary, if not the sole, buyers for many farmers' produce, giving them substantial bargaining power. While both Coles and Woolworths contend they are not price setters in the market, due to Australia's ability to export its produce globally they often hold exclusive relationships with producers.

This power imbalance allows these large entities to dictate terms and prices to farmers, who, due to the perishable nature of their products and lack of alternative market avenues, often have little choice but to comply. Consequently, farmers are frequently caught in a position where they must accept prices that may not adequately cover their production costs or reflect the fair value of their labour and investment.

ASYMETRIC PRICE TRANSMISSION

When input costs for farmers have risen (such as feed, fertilizer, or labour), or when there is a supply shortage leading to increased farmgate prices, supermarkets are quick to pass these costs onto consumers. However, the reverse is not always true. When farmgate prices fall due to increased supply or reduced input costs, these reductions are not always promptly or fully reflected in retail prices. This asymmetry benefits retailers and processors, who can maintain or even increase their profit margins, while farmers and consumers see less of these benefits.

A timely example of this was evidence from Brendan O’Keeffe from NSW Farmers who noted that despite lamb prices which had been decreasing for six months, a recent announcement by Woolworths that lamb prices would be decreased as a “Christmas gift”. This announcement highlighted to Mr O’Keeffe the lack of competition in the food and grocery sector “a normal business practice in a competitive market should not be in the news ... they’re allowed to position it as a Christmas gift to consumers.”

Plainly, when those at the top of the supply chain experience an upward price shock they raise the prices like rockets, but when the reverse occurs, they fall like feathers. The upshot of this dynamic is that consumer surplus is eroded, prices stay higher for longer and the task of monetary and fiscal policy makers to control inflation is that much harder.

The review of the Food and Grocery Code

and the appointment of Dr Craig Emerson is a welcome opportunity to address this imbalance and the inquiry notes that the position of the NSW Farmers and the National Farmers Federation is that the code is both strengthened and enforceable, as it is currently voluntary and without penalties for any breaches. The evidence I have gathered undertaking this review has led me to believe that the code should be fully mandatory, i.e. membership of retailers is mandatory and the rules are mandatory.

I also note that this review of the Food and Grocery Code is not comprehensive and there is more to uncover apart from the major retailer’s treatment of farmers and other suppliers.

MARKET POWER OVER CONSUMERS

On the one hand the major players have market power to hold down market prices, to exploit farmers and other suppliers. On the other hand, if they can profit from holding down input prices a lack of competition on the product market side means that reductions are not passed onto consumers. Instead, they are able to be pocketed.

That downward price transmission is not fast is evidence of a lack of competitive forces in this sector.

PRICE TRANSPARENCY

This asymmetric price transmission issue is further exacerbated by the lack of transparency in the pricing mechanisms within the food supply chain. Farmers often have limited visibility into the end pricing of their products and the margins added by processors and retailers. Without this knowledge, they are at a

We see supermarkets increase their prices straight away when there’s a supply shortage or a cost increase but the opposite doesn’t happen when there’s say a large increase in supply or a decrease increase in farmgate prices, one of their inputs, they don’t pass that on very quickly or in full. So there’s a clear asymmetry there.”

*Brendan O’Keeffe,
NSW Farmers, Price Gouging
Inquiry Hearing, Sydney,
10 November 2023*

disadvantage in negotiations and cannot effectively advocate for fairer pricing. The lack of transparency also hinders the ability of consumers and regulatory bodies to understand and address potential unfair practices in the market.

The buyers, though, have near perfect information. Major grocers are able to see and exploit price differentials in a way farmers themselves cannot. It is nearly impossible to know if the price a farmer or primary producer is receiving is fair. Consumers, on the other hand face higher prices at the retail level, are often unaware of the cost structures and pricing dynamics that occur along the supply chain.

Addressing these issues requires a multi-faceted approach. Firstly, there needs to be increased regulatory scrutiny and potential reform to address market concentration and ensure fairer competition in the food supply chain. This could involve strengthening anti-monopoly laws and implementing policies that support smaller farmers and encourage diversification of buyers in the market.

Enhancing transparency across the supply chain is crucial. This could be achieved through initiatives like mandatory reporting of pricing structures and margins by supermarkets and processors (subject to any competition concerns) and the development of platforms that provide farmers with more information on market trends and pricing. Finally, supporting farmers in forming cooperatives or collective bargaining groups could empower them to negotiate more effectively with large buyers. Such measures would contribute to a more balanced and equitable agricultural sector, benefiting both producers and consumers.

The level of concentration in the Food and Grocery sector, as well as the relative position of producer's provider warrants closer attention from the ACCC, in particular whether supermarkets are passing on price decreases in a prompt manner.

FAIR DISCOUNTING

As prices have increased, consumers have noticed again and again that once normal prices are being advertised back to shoppers as 'special.'

Misleading price displays are illegal but despite this, there is no prescribed minimum period where a business must advertise. The extent of the obligation is that the item and a reasonable proportion of the items must have been sold at that price before businesses are able to claim it is a discount.

Up until August 2022 Coles and Woolies sold a 200 gram of Robert Timms coffee for \$8 (\$4.00 when on special). In early August Coles increased the shelf price to \$12.70 per bottle however a couple of weeks later the price was reduced to \$10.70 per bottle with a shelf tag saying was \$12.70 per bottle now “down, down!”

It is quite evident that both companies are continuing their deceptive trading practices

John, submission to inquiry

Devondale cheese has gone from \$5.00 to \$10.00 in recent months. It has been on “special” recently for \$10.00.

Kerre Ann, submission to inquiry

In a period of rapid price increases, it is many consumers' evidence that businesses have not been fairly claiming to be discounting. As prices are changing so rapidly and across so many product categories, without special resources from the ACCC to monitor price movements it is impossible for consumers to have confidence that this law is being complied with.

FINDINGS AND RECOMMENDATIONS

There is insufficient competition in the food and grocery sector as evidenced by poor price transmission to final consumers.

Market power is exercised over farmers and many other suppliers. In addition, the gain in profits from this is not passed on, certainly not promptly or fully, to consumers because of market power and a lack of competition in the product market.

Price transparency for those down the supply chain of supermarkets is low, and this is one barrier to effective price transmission.

Supermarkets have not been transparent with customers about price histories of their displayed items and their correlated discounts.

RECOMMENDATIONS

There should be a comprehensive ACCC inquiry into competition and prices in the retail food and grocery industry.

The Food and Grocery Code should be fully mandatory i.e. membership of retailers is mandatory and the rules are mandatory.

The Food and Grocery Code should investigate creating a price register for farmers to assist them in understanding market prices across primary industries.


SUPPLY CHAIN CONCENTRATION IN NORTHERN AUSTRALIA

Far north Australia suffers some of the most acute and limited competition in the country. The extreme remoteness of communities in the far North exacerbates the pricing pressures felt by the rest of the country. In testimony to the Inquiry hearing in Cairns, Tommy Sebasio outlined just how much more expensive basic goods are on islands in the Torres Strait. Mr Sebasio gave the following examples of the prices of basic necessities:

- \$19 for a kilo of mince (\$11 on the mainland)
- \$15 head of lettuce (\$1.50 on the mainland)
- \$400 for a 45kg LPG container exchange (\$185 for an exchange on the mainland)

The cost of essentials is largely driven by the cost of transport, which in a competitive market would be expected to add more. However, shipping in the Torres Strait is performed by one private company, Sea Swift. Sea Swift is a barge operator with headquarters in Cairns and provides shipping services to the Torres Strait and Northern Peninsula. This is an essential service, which provides food and goods to more than 45,900 people.

In 2022 Sea Swift increased its prices by 14.5 per cent, which was noted by the Torres Strait Council to be such an expense as to have a meaningful impact on the Council's infrastructure program. This



The significant price increase comes after the expiry of an undertaking agreed by Sea Swift with the ACCC to limit price increases.

increase has a compounding effect on the cost of every good carried by the barge, illustrating the chain of prices that those in remote communities are subject to.

The significant price increase comes after the expiry of an undertaking agreed by Sea Swift with the ACCC to limit price increases. Sea Swift, in 2016, purchased Toll Marine Logistics Australia's (Tolls) Far North Queensland Operations, a purchase which had been opposed by the ACCC on grounds it would limit competition and potentially affect servicing in the far north.

The Australian Competition Tribunal authorised the acquisition in exchange for pricing and servicing agreements and these have now expired.

The impact of the Australian Competition Tribunal's decision has a longer tail than the five -year agreement and those who need Sea Swift's essential service will now have to endure significantly increased prices with no powers afforded to the ACCC to provide oversight or test the reasonableness.

The shipping industry in Far North Queensland and the Northern Territory is serviced by a private, for-profit, and unregulated monopoly. Such an arrangement is considerably dangerous for consumers, particularly those in remote communities with much lower incomes and abilities to pay for final products.

RECOMMENDATION

The ACCC should once again have an ability to challenge and overturn unreasonable prices charged by Sea Swift to ensure the service is not exploiting its market position.

CARTELS

A cartel exists when businesses agree to act together instead of competing with each other. Cartels cheat consumers and other businesses. They restrict healthy economic growth, drive up prices and reduce innovation and investment.

The ACCC cartel activity can be divided into 4 types. These are when 2 or more competitors agree to:

- [fix prices](#) - when competitors agree on pricing instead of competing against each other
- [market share](#) - when competitors agree to divide a market between themselves so they don't have to compete
- [control output](#) - when competitors agree to limit the amount or type of goods and services available
- [rig bids](#) - when suppliers discuss and agree among themselves who should win a tender, and at what price.

Each of these cartel types tries to emulate the sort of behaviour that might be found if there were only one monopoly supplier. Unlike in Adam Smith's time, today in Australia there are heavy penalties for cartels. Jail time for directors, and heavy fines, damages, recoveries often applies. Despite that, cartel behaviour persists because of the large profits that can be made from it.

Examples

- Earlier this year the ACCC commenced proceedings against Swift Networks Pty Ltd for alleged bid rigging and price fixing in tendering to supply technology equipment and services to five mining villages in the Pilbara (ACCC 2023).
- Sydney waste company group, Aussie Skips, pleaded guilty to increasing and fixing prices with Bingo Industries, a competitor in the supply of skip bins and services from building and demolition waste in Sydney (ACCC 2023).
- In a major case recently, BlueScope Steel was ordered to pay a penalty for attempting to fix the prices for flat steel products. Flat steel products are used as inputs in a host of industries. A record \$57.5 million penalty was imposed on BlueScope.
- In 2022 the public prosecutor decided to drop a case against Citigroup and Deutsche Bank alleged to have entered into cartel arrangements to market ANZ shares to institutional investors (ACCC 2022).

- Four individuals were sentenced and fined for price fixing the foreign exchange rate between the Australian dollar and the Vietnamese dong as well as the fees charged to customers. This price fixing was mainly at the expense of individuals remitting funds from Australia to Vietnam (ACCC 2022).
- The ACCC took action against detergent manufacturers Colgate, Cussons, Woolworths and Unilever for agreeing to cease supply of standard concentrate laundry detergents to Woolworths in early 2009 and supply only ultra concentrates to Woolworths from that time (ACCC 2016).

These examples involve illegal and potentially illegal activity. However, a good deal of cartel behaviour is tacit rather than explicit. Every month the RBA board meets and, following the meeting, announces whether or not the RBA will change the official interest rate. If there is a change in the rate the big four banks typically announce new lending rates, often within days if that is in their interest. There does not appear to be any formal agreement between the big banks but their common practice is notable. Indeed, it could almost be argued that the RBA announcements themselves serve as the price leadership signal for the banks. The common ownership of the banks also raises issues as noted earlier.

Common ownership may have worked against consumers in the case of the NAB which tried to ‘break up’ from the other big banks and set its mortgage rates below the others. The NAB said in its press release that ‘we broke up with the other banks’ (National Australia Bank, 2011) in order to offer lower interest rates to customers. Following the NAB’s “break up” it was reported that large NAB shareholders had pressured the bank to move back in line with the other big banks’ interest rates to preserve the profits associated with synchronised pricing (Kehoe and Chessel 2012). It seems that NAB had a conflict of interest with its owners who were more concerned with the combined level of profits for all of the big banks.

Despite years of strong law enforcement and rising penalties cartel price fixing continues to be prevalent. The key reason is that it is extremely profitable.

RECOMMENDATION

It is recommended that the ACCC receives further funding for strong enforcement of the cartel law. It should also apply the criminal sanctions available for unlawful price fixing and other cartel agreements.

The Assistant Minister for Competition, Charities and Treasury should conduct a public consultation to determine the need for some improvement in the drafting of the criminal elements of the cartel law in view of recent difficulties in the bank cartel case.

ELECTRIC VEHICLES (EVS)

Back when Australia had a domestic car industry, the Australian government introduced parallel import restrictions. These regulations stopped people from importing car models that were also being manufactured in Australia. The goal was to protect the car manufacturers that operated in Australia from competition from imports.

These regulations still exist today even though car manufacturers no longer make cars in Australia. New Zealand does not have a ban on the parallel imports of second-hand vehicles. Analysis from the economic consulting firm, Mandala, shows that second-hand electric and hybrid vehicles are on average 41% cheaper in New Zealand than in Australia. The price differential between Australia and New Zealand widens as the cars get older – likely driven by a larger supply of older vehicles in New Zealand. New Zealand electric and hybrid vehicles, controlling for key observable characteristics such as make type and size, are on average \$9,025 cheaper than in Australia.

Australia’s parallel import restrictions have a number of significant consequences: they make low emissions vehicles significantly more expensive in Australia, they make it harder for Australia to reduce emissions and achieve our international commitments, they reduce the private sector’s ability to help reduce emissions thus

putting more burden on the government, they worsen cost-of-living pressures given that vehicles are often one of the biggest expenses faced by households (particularly the higher running costs of internal combustion vehicles relative to EVs), and they hurt Australian mechanics, car repairers and parts suppliers who would otherwise profit from servicing these vehicles. The Australian government should remove parallel import restrictions for the importation of electric and hybrid vehicles into Australia.

Whilst the emphasis in this report is on electric vehicles, the same restrictions appear to apply to the whole of the car market and to that extent they also keep prices up higher than this report considers that it desirable to introduce the change in regulation insofar as they affect electric vehicles as soon as possible, whilst the broader change could be introduced fairly soon afterwards.

RECOMMENDATIONS

The regulations in the Road Vehicle Safety Act 2018 which block parallel imports of electric vehicles be immediately lifted.

Regulations under the Road Vehicle Safety Act 2018 which block parallel imports of cars into Australia should also be repealed in coming months.

OUT OF POCKET CHARGES BY MEDICAL SPECIALISTS

According to the Grattan Institute (2022) out of pocket charges for specialists increased by more than fifty percent in real terms from 2012-2022. Their growth far outstrips the stagnant wages growth of the same period.

Many specialists charge more than double the scheduled fee. There is no evidence that they provide a better service.

There is also great variation in out of pocket charges for the same services by different specialists.

High out of pocket charges lead to many potential patients being unable to afford specialist care. According to the Grattan Institute around 500,000 Australians missed out on or delayed needed specialist care because of charges being prohibitively high.

Out of pocket costs are a key barrier to access healthcare in Australia, with ample evidence from many countries that out of pocket costs reduce access to and utilisation of healthcare, and that this more strongly affects populations with higher needs for healthcare. Australia has one of the highest rates of out of pocket costs in Organisation for Economic Co-operation and Development (OECD) countries and is unusual as general practitioners (GPs) and specialists in private practice are paid by fee-for-service (FFS). The level of fees and decisions to bulk bill, or use gap cover in private inpatient settings, are entirely at the discretion of doctors.

A seminal article by Nobel laureate Kenneth Arrow (1963)²⁴ first highlighted that consumers have much less information than healthcare providers, creating potential for excessive market power, inefficiency and inequity in healthcare.

For services provided by private non-GP specialists, either in their offices or in private hospitals, information on fees charged by doctors and out of pocket costs is not easily accessible by patients before they use healthcare, and neither is information on the quality of providers. Patients face considerable uncertainty before they visit a doctor about whether they will have to pay an out of pocket cost, and if so, how much it will be. They have little information on which to make choices. As a result, patients are often left to navigate a very complex healthcare system and bear much of the burden of seeking out information and financial risk that public and private health insurance is supposed to remove. A lack of informed choice means there is little competition between providers and excessive market power such that patients are worse off. There is evidence of considerable fee variation and that specialists and GPs in more affluent areas tend to charge higher prices.

Prices that are 'too high' are a source of waste as those resources could have had more beneficial uses

elsewhere, and provide skewed incentives and price signals that lead to inefficient decisions being made by patients (e.g. discouraging health care utilisation and assuming that higher prices represent higher quality) and doctors (e.g. choosing high earning specialties instead of those most in need) leading to a misallocation of resources and inefficiency.

The Australian Government's response to concerns about specialists was to introduce a price transparency website in 2019 (Medical Cost Finder), following similar websites introduced by some private health insurers. However, reviews of evidence on the effectiveness of these online platforms in healthcare and in other industries, mainly from the United States, provide mixed verdicts. More generally, the effectiveness of consumer- focussed interventions to improve the allocation of resources in healthcare markets and increase competition remains uncertain with policy responses dominated by ideology rather than evidence, and no evaluations in Australia.

Both the Productivity Commission in its Human Services Report and the Harper Competition Policy Review in Human Services have made recommendations about the role of competition in healthcare including the role of improved consumer information and choice.

RECOMMENDATIONS

The National Competition policy review should conduct or commission a contemporary study of specialist fees backed by an analysis of restrictions on competition and of the role of information imbalances between patients and specialists.

As mentioned earlier in this report a feature of the NCP from 1995 to around 2007 was that the Commonwealth itself failed to conduct review in many areas within its jurisdiction. It would be a good test of the Commonwealth's own commitment to a renewed NCP if it authorizes a review of competition in relation to specialists, as well as of specialist fees.

The Australian Health Practitioner Regulation Agency should, separately, review of specialist fees and the policy steps that could be taken to reduce them.

PHARMACEUTICALS

In 2015, the Government directed the Productivity Commission (PC) to undertake an inquiry into Australia's intellectual property arrangements. This included consideration of the pharmaceutical sector. The resulting report identified two strategies common to the pharmaceutical sector that can have adverse consequences for markets and consumers:

- *Evergreening* is a strategy of obtaining multiple patents that cover different aspects of the same product, typically on improved versions of existing products. Some of these may be genuine innovations that improve consumer wellbeing, while others may be technical changes that have unclear consumer impact. The ability to obtain multiple patents on a product over a period of many years effectively extends the term of exclusivity that the patent holder obtains.
- *Pay-for-delay agreements* refer to patent holders (originators) paying generic manufacturers to keep the generic product off the market beyond the scope of a patent (both in terms of a generic that may not breach the original patent or preventing entry after the expiry date) as part of a settlement agreement to resolve a court action.

The PC's report noted that pharmaceutical companies have strong incentives to extend the exclusive commercial life of their products and can use a variety of strategies to do so. These strategies limit pharmaceutical products available in the market, impacting consumer choice and price reductions that may come with competition. Delayed entry also has the effect of postponing any regulatory price drops, such as the automatic price reductions under the PBS.

Government spending on the PBS is significant. The most recent budget papers put at over \$18 billion per year. Pharmaceutical wholesaling is also a largely concentrated sector.

Amongst a range of recommendations, the PC recommended (and the ACCC supported) the introduction of a mandatory reporting scheme in relation to originator-and-generic agreements to improve the detectability of pay-for-delay agreements, similar to the reporting arrangements in the United States (recommendation 10.2).

Government response in 2017 supported this recommendation in principle. Work by a range of agencies to implement this recommendation was progressed through the Government's Intellectual Property Policy Group throughout 2017-19. However, following the onset of the COVID-19 pandemic, the work appears not to have proceeded with or deprioritised. The recommendation needs to be given effect to.

RECOMMENDATION

A mandatory reporting scheme should be implemented in relation to originator and generic agreements to improve the detectability of pay for delay agreements similar to the reporting arrangements in the United States.

8. FINDING AND RECOMMENDATIONS

After considering the submissions received, having heard evidence from organisations and individuals and on the balance of evidence provided, this report makes the following findings and recommendations to improve competition and pricing regulation in Australia.

The often-weak state of competition in many sectors of the Australian economy provides a platform which enables many businesses to charge higher prices to consumers than they would if there were effective competition. Businesses seek to capture as many consumer dollars (or 'consumer surplus') as they can whether by charging high prices uniformly to all consumers or by charging different consumers different prices according to their willingness to pay – that is price discrimination.

CONCLUSIONS AND RECOMMENDATIONS

The various business pricing practices analysed above are mainly designed to enable producers or suppliers to capture as much consumer surplus as possible.

This review has identified business pricing as a contributor to inflation. It has also concluded at the micro economic level there is a range of business pricing practices which do or may often operate against the interests of consumers. These include: loyalty taxes, loyalty programs, rack pricing, complex confuse pricing, excuse-flation, algorithmic pricing, asymmetric rockets and feathers approaches to pricing and price discrimination.

Typically, the ability of producers to capture consumer surplus stems from imperfections in the state of competition or from a lack of consumer knowledge of what is on offer, or costs and difficulties in switching to another supplier.

In Australia's less than fully competitive economy the consumer often comes out second best in the battle between producer and consumer surplus. Too often the producer captures an unjustifiably high proportion of consumer surplus and converts it into consumer surplus.

In general, these practices are not unlawful nor there should be direct controls on such practices.

But there is a case for exposure of these prices by regulators such as the ACCC.

The report has also identified a number of prices where there has been or may appear to be excessive, exploitative pricing that is price gouging in the sense that prices greatly exceed the costs of supply and a reasonable profit.

What are the policy implications?

A useful starting point is to recognise the strengths but also the limitations of the application of competition law to resolve problems about high prices. Competition law plays a valuable role – prohibits anticompetitive agreements that may take forms such as price fixing, market sharing, big rigging, active boycotts, as well as concerted active practices by business that give rise to these effects. It also prohibits anticompetitive mergers and anticompetitive abuse of market power.

Consumer law also has a number of important attributes which also help competition particularly its prohibitions on misleading and deceptive conduct as well as prohibitions on unconscionable conduct and unfair contract term pricing.

There are, however, many manifestations of anticompetitive behaviour that are not addressed by competition law, including lawful price cooperation between competitors. In some very concentrated markets competitors are able to raise prices in parallel without having an unlawful price fixing agreement. Those prices can be high as or higher than a cartel may charge. Another example is pricing by a dominant or monopoly firm: this is not addressed by competition law.

Despite the fact that the greatest concern of economists with monopoly or market power is harmful high prices, high and unfair prices are not prohibited by competition law. There has been an ideologically-driven resistance to competition law addressing this feature of monopoly behaviour in Australia and in North America.

The European Union is an exception and prohibits excessive pricing by monopolists. Although limited use is made of this in Europe, the same provision should be incorporated into Australian law. This power has recently been used with considerable effect on pharmaceutical industry overcharging.

As the discussion in foregoing chapters indicates, there are a number of issues where there is a case for consumer protection, like the provision of more information, steps to facilitate consumers switching from one business to another which are not present in consumer protection law.

Where governments take steps that directly or indirectly raise prices, there is no recourse under competition law. As a consequence, there is a need to consider whether greater steps should be taken to address concerns about high prices. We set out a number of steps below. These do not include proposals for price control or regulation.

PRICES

The Australian government needs to take more action and pay more attention to prices and pricing behaviour. Pricing behaviour by business (in some cases aided by Government) is adding to inflation in an unwarranted way. There is evidence, post pandemic, of ongoing overcharging which requires investigation and there is widespread public concern about the legitimacy of many price increases.

Pricing behaviour across a number of industries should be fully investigated by the ACCC, armed with appropriate powers of investigation. But the governments generally only use their power to require the ACCC to conduct price investigations. It does this most often when there is a short-term problem of political concern.

The Government only has power to refer price related matters about a firm or industry to the ACCC. Currently, the Government cannot require the ACCC to conduct more general 'market studies', as in many other countries. Often, an industry or market study reveals the heart of the problem whether high prices or other exploitative or anticompetitive behaviour. The power by competition regulators to conduct market studies is becoming more common around the world.

The ACCC cannot self-initiate price or market studies and if it tried to do so it would lack legal powers and legitimacy. If its work depends on ministerial reference, there can be serious delays in urgent situations and political and government factors and processes can also inhibit or slow down referrals.

Self-initiated ACCC inquiries would speed up and improve dealing with situations of rising prices.

There is a need for greater investigation, transparency, and exposure of many prices.

Benefits include:

- a. public understanding and education which may prompt consumers to act in their own interests.
- b. sometimes businesses may be 'nudged' or 'shamed' into changing their pricing practices.

- c. sometimes governments or regulators may impose requirements on business for better disclosure of their practices to consumers e.g. the provision of more information including upfront information about the prices, their components and their future evolution.
- d. revelation of the limited role of competition in enabling these practices. Occasionally this may prompt more competition, or more informative behaviour of business or some ways of reducing the costs of switching, with the net result that there is a better outcome for customers.

Governments have previously used the power of naming and publicising overcharging to help regulate prices. When the Coalition Government introduced the GST in 2000, it enacted legislation giving power to the ACCC to declare that particular prices of industries were overcharging in relation to GST related prices that existed for three years.

A similar power has applied under legislation both by the Victorian and NSW Coalition Governments in recent times in relation to ensuring that insurance prices were lowered in line with reduced taxes on insurance.

The ACCC does not currently have this power and it prevented from naming the kind of overcharging this report has found concerning including in early childhood education and care and by NDIS providers.

This power should be reinstated with appropriate procedures and safeguards to govern the exercise of this power.

ABUSES OF MARKET POWER

Section 46 of the Australian Competition and Consumer Act is intended to cover the abuses of market power, however, it omits any action in regard to the most obvious abuse of market power which is the charging of excessive prices.

Such a power is included in the European Competition Law.

The Australian law should be brought into line with European law by inserting a provision into Section 46 that prohibits the charging of excessive prices and makes it an offence under the Australian Competition and Consumer Act.

Such a finding and any sanctions would have to be endorsed by the Federal Court of Australia. As an alternative more integrated approach the government could establish a Commission on Competition and Prices which would review government and other anticompetitive restrictions, and high prices caused by a lack of competition. The ACCC would continue to enforce the law and where appropriate undertake pricing and market studies.

RECOMMENDATIONS

Recommendation 1.1: The Australian Government should use its power to require the ACCC to conduct more price and market investigations.

Recommendation 1.2: The Australian Government should have power to require the ACCC to undertake market studies as well as price studies.

Recommendation 1.3: The ACCC should have power of its own to initiate price and market studies.

Recommendation 1.4: The GST pricing legislation of 2000-2003 provisions regarding the naming of businesses and industries that overcharge should be reinstated.

Recommendation 1.5: Section 46 of the Australian Competition and Consumer Act should be amended to make it an offence to charge excessive prices in terms similar to the European Union provisions.

Recommendation 1.6: The Government could establish a Commission on Competition and Prices to review Government and other restrictions on competition and high prices caused by a lack of competition.

MERGERS AND DIVESTITURE

FINDINGS

This report has found a significant weakening of competition in the Australian economy and there is strong reason to believe that this is partly the result of inadequate competition law.

MERGERS

Australia is one of the few OECD countries with no compulsory pre-merger notification law.

The disadvantages of this include that there is tactical behaviour by businesses in terms of non-notification, late or no provision of relevant information required by the ACCC and other forms of game playing.

This makes the task of the ACCC in applying merger law more difficult. Moreover, it can lead to the exclusion of the ACCC from coordinated international consideration of mergers, which occurs in the USA and the European Union which receive early merger notification.

MERGER ONUS OF PROOF

Under the Australian system, an anticompetitive merger can only be blocked by the ACCC if it can prove in a court of law that the merger would be likely to substantially lessen competition. The current system often makes this difficult to do.

The merger law differs from many other laws in that the test is not about proving that a particular event e.g. an offence against the law such as a price fixing agreement between competitors occurred. Rather it is about a future unknown outcome, and this makes it difficult to prove on the balance of probability that an anticompetitive merger will occur. Whilst the likely outcome of many mergers is fairly clear there is a significant number where it is unclear or totally unknown as to what the effect of the merger on competition will be.

As a result, anti-competitive mergers can be permitted when they should not be allowed.

Added to this, there are considerable resources devoted to defending mergers by big business, big law firms, consulting firms and others. This is a new challenge faced by Australian regulators and courts, making the protection of competition especially difficult compared with anything in the past.

It is better that the precautionary principle of regulation should apply – the onus should be on the applicant seeking a merger to satisfy the ACCC (and the Australian Competition Tribunal) that there is not likely to be an anticompetitive effect.

SUBSTANTIAL LESSENING OF COMPETITION

The wording introduced into the merger law in 1993 has proved to be problematic in the courts. It replaced the former test which prohibited mergers that gave rise to dominance or increased dominance. That former test had the disadvantage that it only blocked mergers that led to single firm dominance or pure monopoly and did not catch mergers that for example reduced the number of players in the industry from say four to two because no one firm was dominant even though it was obvious that the merger would harm competition.

Despite its shortcomings the older dominance test had two advantages. First, it focused explicitly on the structure of the industry and in particular whether the number of important firms in the market would be reduced. Second, it implicitly emphasised the immediate impact of the merger rather than immediately proceeding to take a view of the somewhat distant future.

The term 'substantial lessening of competition', although having wider coverage of mergers, has two consequent disadvantages. First, there is a failure to emphasise the structure of the industry. Instead, the term 'substantial lessening of competition' tends to focus on possible future conduct which is much more difficult to assess. Second, it tends to focus on long term outcomes. This creates a situation where the defence can readily argue that many possible behavioural outcomes might occur over a period of time and again this makes the task of proving that a merger would substantially lessen competition very difficult.

The solution is to bring back appropriate structural language into the law.

At the same time the law should address another problem – small acquisitions which on their own do not necessarily amount to a ‘substantial lessening of competition’ can nevertheless be anticompetitive in the long run.

There has been a wave of takeovers of newly emergent potential competitors (‘killer acquisitions’) by digital platforms which look to be anticompetitive in the long run. Accordingly, the law should be changed to enable prohibition of mergers which simply add to existing market power.

DIVESTITURE

Australia appears to lack power to break up big businesses that break the competition law. There is a strong case in principle for such a law because the structure of an industry can have a powerful effect on competition. The USA has successfully applied its divestiture law to break up the oil industry, the tobacco industry, the chemical industry and in recent times the telecommunications industry. These break ups have powerful effects on promoting competition. Other countries such as Germany and the UK have a successful experience of divestiture and Australia itself has engaged in heavy divestiture activities in areas previously owned by governments e.g. electricity and gas.

There is a strong case, therefore, for applying divestiture law where there are breaches of the law proven in the courts and where the court on recommendation from the ACCC considered that the best answer to the problem is the breakup of the firm.

The introduction of such a provision would also have a powerful effect on achieving compliance on the notoriously weak Section 46 of the Australian Competition and Consumer Law. The general provisions of Section 46 have been altered in a sensible manner recently, but that section still lacks strong teeth and there has been a history of few fines or other strong sanctions. If there were the possibility of a divestiture order from a court following breaches of Section 46 there would be far more compliance.

Recommendation 2.1: The Australian government should establish a pre-merger notification system along similar lines to most OECD countries.

Recommendation 2.2: That in merger matters the onus should be on applicants to satisfy the ACCC and on appeal the Australian Competition Tribunal that the merger is not anticompetitive and is in the public interest.

Recommendation 2.3: The merger test should be augmented to continue to prohibit mergers which substantially lessen competition but there should be an additional provision prohibiting mergers that give rise to substantial market power (a more structural and immediate test) and/or which entrench, create, or add to market power.

Recommendation 2.4: A divestiture power should be introduced into the competition law.

COMPETITION AND CONSUMER LEGISLATION.

The competition provisions of the Australian Competition and Consumer Act are by far the longest in the whole world. They make up about 20,000 words compared with a simple couple of sentences in the USA Sherman Act and a half page in the European competition law. The Act needs to be shortened.

RELATED LEGISLATIVE AND GOVERNMENT ACTION

SECONDARY BOYCOTTS

There are arguments for and against the inclusion of secondary boycotts in the competition law. Some argue this is a matter for the industrial relations authorities. Others argue that because secondary boycotts are not typical of the relationship between employer and employee but involve a third party there is a case for the matter being dealt with under the Australian Competition and Consumer Act.

Without taking sides on this issue, it should be noted that the secondary boycott provisions differ from nearly all other provisions in the competition part of the Australian Competition and Consumer Law insofar as they do not require harm to competition in order for there to be a breach. If the secondary boycotts law is retained a competition test should be included.

NON-COMPLETE CAUSES

Australia should ban non-compete clauses in employment contracts in line with emerging American practice. These clauses cause a chilling effect on employees moving between employers and inhibit the transfer of talent to more efficient firms. These clauses are also used to prevent part-time and casual employees from finding employment elsewhere, stifling employment growth.

Australia needs to follow laws which are emerging in the United States and elsewhere which ban no compete clauses in employment contracts.

GOVERNMENT ACTIONS

Many government actions have the effect of substantially lessening competition.

Such matters were the subject of the National Competition Review (the Hilmer Report in the 1990s).

There is a special need for the current National Competition Review to look into ways of reviving policies and laws that prevent governments from needlessly restricting competition.

Recommendation 3.1: The Australian Consumer and Competition Act needs to be shortened.

Recommendation 3.2: If the secondary boycott law is retained in the Competition Law there should be a provision that secondary boycotts are only unlawful if they substantially lessen competition.

Recommendation 3.3: Australia should ban non-compete clauses in employment contracts affecting both employees during and post-employment.

Recommendation 3.4: The current National Competition Review should examine policies and laws that prevent Governments from needlessly restricting competition.

Recommendation 3.5: The ACCC receives further funding for strong enforcement of the cartel law. It should also apply the criminal sanctions available for unlawful price fixing and other cartel agreements.

INDUSTRY SPECIFIC

Through the public hearings and submissions, I have found evidence of price gouging or uncompetitive behaviour in specific industries and make the following findings and recommendations:

AVIATION

This report does not in general recommend the introduction of price regulation.

However, it supports present areas where there is price regulation such as in the fields of energy and telecommunications.

There is also a very strong case for the introduction of price regulation in relation to airports, which hold a very clear monopoly.

In the area of airport charges, the power of regulation should be applied.

This report also found the need for reviews of international and domestic restrictions on competition.

Recommendation 4.1: Airport prices should be regulated in the same way as other utility prices.

Recommendation 4.2: The Australian Government should use the opportunity of its current aviation review to remove international and domestic restrictions on competition. Any remaining restrictions should be reviewed by the Treasury led Competition Policy Review.

EARLY CHILDHOOD EDUCATION AND CARE

Childcare is a profitable industry. It is not one national market, but operates as a highly localised market. The ACCC has found that fees are higher in local markets with more childcare services, often in wealthier areas where parents can afford to pay more, indicating weak price competition in the sector. There is enough evidence of for-profit centres not being subject to competition, and potentially of price gouging occurring.

HEALTH, AGED AND DISABILITY CARE

Similarly in the broader care sector, users are often overcharged due to both the design of the market, the disconnect between user and payer, and the power differential between provider and client. This has resulted in massive premia being charged to users that would not occur in an efficient market.

Recommendation 4.3: The ACCC should be empowered to investigate pricing decisions made by for-profit providers to ensure gaming is not occurring.

Recommendation 4.4: Prices in relation to disability, care and support and aged care should be kept under continuous review by the ACCC.

BANKING AND FINANCIAL SERVICES

Due to the ability for the banks to maintain stable margins in a dynamic pricing environment, the ability for banks to increase their cash margins warrants further investigation from the ACCC to determine if the banks are failing to pass on deposit rate increases to depositors.

Policies to entice competition in the Banking sector should be encouraged.

REMITTANCES – FOREIGN EXCHANGE MARKET

It is clear that the foreign exchange market is not sufficiently competitive and there is a lack of price transparency for vulnerable users of the service, specifically in the area of remittances.

Recommendation 4.5: The ACCC should be provided with a standing Ministerial Direction to monitor prices and competitiveness in the retail banking sector.

Recommendation 4.6: The ACCC should be issued with a Ministerial Direction to undertake a further inquiry into pricing practices in foreign exchange markets to develop mechanisms for a fairer transmission of cost information to consumers as well as to provide specific assistance to prevent exploitation of those with low English language proficiency.

ENERGY PRICES

This report has found substantial price gouging taking place in the energy sector which needs urgent reform. Both the significant vertical integration of the industry and the concentration of market participants have provided ample opportunity for generators, network operators and retailers to extract extraordinary profits and in some cases unfair prices.

In particular, the wholesale market needs most urgent reform given the enormous downstream effects of gouging in this market on the broader economy.

Recommendation 4.7: There should be a review of the design and operation of the wholesale market, as to whether it requires refinements or a fundamental change in the form of a 'capacity market' as in North America and in Western Australia. This review should be chaired by an independent expert with input and resources from the AER, AEMO, and ASIC. The level of electricity generation concentration should be kept under review, and there should be close scrutiny of the impact on competition, positive or negative, that could occur in the transition to a re-designed energy market.

Recommendation 4.8: ASIC should be provided with a Ministerial Direction to investigate the energy derivatives market to ensure that participants in both the National Electricity Market and the markets for derivatives are not misusing their position in either to gain an unfair advantage or influence the price of energy to meet derivatives conditions.

Recommendation 4.9: Network prices should continue to require close regulatory scrutiny with the long-term interests of consumers put first.

Recommendation 4.10: There should be a regulatory review of the high degree of price discrimination in the retail electricity and gas markets.

Recommendation 4.11: State Governments and regulators should continue to introduce initiatives to improve retail outcomes brought about by current market imperfections.

FOOD AND GROCERIES

The level of concentration in the Food and Grocery sector, as well as the relative position of producers provider warrants closer attention from the ACCC, in particular whether supermarkets are passing on price decreases in a prompt manner.

Enhancing transparency across the supply chain is crucial.

Recommendation 4.12: It is recommended that there should be a comprehensive ACCC inquiry into competition and prices in the retail food and grocery industry.

Recommendation 4.13: The Food and Grocery Code should be fully mandatory i.e. membership of retailers is mandatory and the rules are mandatory.

Recommendation 4.14: The Food and Grocery Code should investigate creating a price register for farmers to assist them in understanding market prices across primary industries.

SHIPPING COSTS IMPACTING FNQ AND NT

The shipping industry in Far North Queensland and the Northern Territory is serviced by a private, for-profit and unregulated monopoly. Such an arrangement is considerably dangerous for consumers, particularly those in remote communities with much lower incomes and abilities to pay for final products.

Recommendation 4.15: The ACCC should once again have an ability to challenge and overturn unreasonable prices charged by Sea Swift to ensure the service is not exploiting its market position.

ELECTRIC VEHICLES

Tariffs and restrictions on the import of electric vehicles is no longer sensible since the exit of car manufacturers from Australia in the preceding decade. Unless this changes, restrictions on imports create unnecessarily high prices for consumers.

Recommendation 4.16: Regulations in the Road Vehicle Safety Act 2018 which block parallel imports of electric vehicles be immediately lifted.

Recommendation 4.17: Regulations under the Road Vehicle Safety Act 2018 which block parallel imports of cars into Australia should also be repealed in coming months.

OUT OF POCKET CHARGES BY MEDICAL SPECIALISTS

Recommendation 4.18: The National Competition policy review should conduct or commission a contemporary study of specialist fees backed by an analysis of restrictions on competition and of the role of information imbalances between patients and specialists.

Recommendation 4.19: The ACCC or the Productivity Commission or another appropriate body should, separately, review specialist fees and the policy steps that could be taken to make them more transparent or to reduce them.

PHARMACEUTICALS

Higher medicine prices exploit the most vulnerable and while our pharmaceuticals price regulation is normally robust, the gaps that exist undermine the policy goals of encouraging generic manufacture and distribution of medicines.

Recommendation 4.20: A mandatory reporting scheme should be implemented in relation to originator and generic agreements to improve the detectability of pay for delay agreements similar to the reporting arrangements in the United States.

3. WITNESSES AND SUBMISSIONS

WITNESSES

Ann Kreger (community member)
Associate Professor Lynne Chester (University of Sydney)
Brendan O’Keeffe (NSW Farmers)
Corey Irlam (Council on the Ageing)
Dale Beasley (SA Unions)
Danielle Jaeger (community member and healthcare professional)
David Caig (community member)
Dr John Falzon
Dr Mark Giancaspro (University of Adelaide)
Dr. Evan Jones (University of Sydney)
Dr. Jim Stanford (Centre for Future Work)
Elida Faith (community member)
Grace Taylor (community member)
Greg Jericho (Australia Institute)
Jacqueline King (QCU)
James Pawluk (Concordia Vox)
Josephine Buckhorn (community member)
Kade Denton (National Farmers Federation)
Kelly-Ann Tansley (Zahra Foundation)
Leticia Choppy (community member)
Matt Grudnoff (Australia Institute)
Mike McNess (Transport Workers’ Union)
Peter Davidson (ACOSS)
Professor Lisa Magnani (Macquarie University)
Professor Philip Clarke (Melbourne Law School)
Rebecca Thistleton (McKell Institute)
Robert Hill (ETU)
Sarah McKenzie and Matthew Lloyd Cape (Per Capita).
Tommy Sebasio (community member)

PRICE GOUGING INQUIRY SUBMISSIONS

Anglican Diocese of Melbourne

Associate Professor Lynne Chester, University of Sydney

Australian Council of Social Services

Carly Dober

Catholic Religious Australia

Concordia Vox

COTA Australia

Dr. Evan Jones,
University of Sydney

Elisabetta Magnani, Professor of Economics, Macquarie University

Flavio Menezes, Professor of Economics Director, Australian Institute for Business and Economics,
The University of Queensland &

John Quiggin, Professor of Economics, The University of Queensland

McKell Institute

Per Capita

Professor Philip Clarke, University of Melbourne

Professor Anthony Scott, Monash Business School

The Australia Institute Centre for Future Work

TransferWise

Victoria Trades Hall Council

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