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PRE-DECISION CONFERENCE SUBMISSION FOR MAGAZINE PUBLISHERS OF AUSTRALIA APPLICATION A91472

This submission has been prepared by Mark Fletcher on behalf of members of the newsXpress newsagency marketing group, representing 180 newsagencies, and with access to data and insights from Tower Systems, the newsagency software company serving in excess of 1,800 newsagents using its newsagency and magazine management software. Mark Fletcher is a Director of newsXpress Pty Ltd and a Director of Tower Systems International (Aust.) Pty Ltd.

OVERVIEW

The Association of Magazine Publishers of Australia Inc. (MPA) has applied to the ACCC for authorisation in relation to the undertaking of a Pilot to test and refine proposed changes to magazine distribution arrangements. The proposed changes only relate to the supply of magazines to newsagents.

The proposed changes do not, in our view, address the lack of competitiveness in the model of the supply of magazines to newsagents. They do not assist newsagents to reduce the labour costs associated with magazines. They do not address the retail space costs associated with magazines.

The trial seeks to test magazine supply rule changes, which impose restrictions on newsagents more onerous and anti-competitive than the current out-of-date magazine supply rules.

To be able to compete, newsagents need a magazine supply model which is fair and allows them business management levers which can be used to be competitive against supermarkets and other magazine retail channels. The proposed pilot does not address this need.

The MPA relies on support from The Australian Newsagents' Federation (ANF) for support of the trial. The ANF did not widely consult newsagents prior to endorsing the trial. Such consultation has only occurred since our objections were raised.

BACKGROUND

The model of supply of magazines to Newsagents in Australia by Gordon and Gotch and the Bauer Media owned Network Services has remained unchanged for decades. It is the model established during the time the distribution of magazines was done exclusively through newsagents in allocated territories under authorization of the ACCC.

In 1999, newsagents lost their exclusive distribution rights and magazine distributors established direct relationships with competitor retail channels: supermarkets, petrol outlets and convenience outlets.

In the years since deregulation, the supply model established with retail channels outside the newsagency channel is different to the pre-deregulation supply model use for newsagents.

Whereas retailers outside the newsagency channel have control over the magazines they receive, have significantly lower returns costs (if any at all) and, in some cases, receive financial support from magazine publishers for stocking product, newsagents have no control over the range of magazine titles they receive, the volume of each issue of these titles nor the costs associated with processing returns.

Around ten years ago, Gordon and Gotch and Network Services established XchangeIT, a data gateway through which to provide newsagents with electronic invoices and to receive sales data from newsagents. They required newsagents to install compliant computer software to receive invoices and provide sales data daily. Bauer Media, in their contract newsagents are required to sign, requires the use of an approved computer system for this purpose. In return for significant capital investment, magazine distributors advised newsagents that as a result of them providing accurate sales data, supply levels of magazines would more accurately reflect actual sales.

There is no evidence of use of supplied sales data to set reasonable magazine supply levels. In response to this, the magazine distributors say that the majority of newsagents do not provide accurate sales data. Such claims are made without supporting evidence.

Looking at data for newsagencies which magazine distributors agree do meet the XchangeIT compliance standards by providing accurate data daily, there is no evidence of the data being used to set fair and equitable supply of magazines. In my own newsagency, which complies with the XchangeIT sales data standards, almost weekly we are supplied quantities of magazines outside what ought be reasonably supplied based on the recorded sales data.

Despite falls in the sales of magazines in the order of between 6% and 9% each year for the last five years, newsagents today have monthly magazine accounts equal to or higher than five years ago. Even allowing the cover price increases over this time, the inventory investment required by newsagents in the current model has increased around 20% despite unit sales declining. The result is a considerable decline in return on investment in the magazine category.

The situation today is that in using the pre-deregulation model for the supply of magazines to newsagents and a different post-deregulation magazine distribution model for their competitors, newsagents have a higher operating costs, lower margin and less ability to act in a businesslike manner with magazines than their competitors.

An average suburban newsagency carries between 1,000 and 1,400 magazine titles. Cost analysis by Tower Systems indicates 80% of all titles supplied to newsagencies are loss making once you account for the retail space, labour and theft costs. The same analysis indicates that 20% of titles supplied are profitable. The number of profitable titles sits at around 200. Looking at newsagent competitors, the majority of the titles they carry are from this pool of profitable titles.

If newsagents could control their supply, our assessment is many would choose to carry these top-selling titles. They would do this to be competitive with supermarkets, petrol outlets and convenience stores. Our assessment is many newsagents would also carry unprofitable titles to position their businesses as magazine specialists.

If newsagents want a direct supply account with Network Services and Gordon and Gotch, they do not have control over what they carry and are forced to carry titles that are unprofitable.

The magazine distributors and the members of the MPA have rejected calls by newsXpress and individual newsagents to have control over titles they receive.

It is our view that engaged newsagents exerting control over the magazine titles they receive would increase magazine sales and set supply arrangements such that some magazines today that are unprofitable for them are profitable.

It is instructive to look at a couple of examples:

1. A newsagency selling quarterly magazine by a major Australian publisher achieving and net sales of six copies is regularly supplied sixteen copies. Relying on the accurate sales data provided by the newsagent, the distributor increases supply by three copies to 19 copies. This well-known title is loss making for the newsagent. As a result of the increase in supply the losses incurred by the newsagent have increased: extra labour cost to process returns and extra freight cost to ship back the returns. The new rules proposed by the MPA will not address this. Indeed, they will make it worse as the newsagent would not have the capacity to early return.

2. A newsagency selling 30 copies of the 55 copies supplied of a monthly magazine loses money on the basis that each pocket holding six copies of the title costs the newsagent $7.44 per month in retail space. Four pockets of storage space cost the business $29.76 in retail space lease costs. This cost is equal to the profit achieved from the thirty copies sold after deducting the retail space cost for the pockets from which they are sold. The only way the newsagent can make any money from this title is to early return twenty copies of what is supplied.

THE MAGAZINE SUPPLY MODEL

Magazine distributors do not know how much space newsagents have in their businesses to display stock. Nor do they know how much space is in retail businesses supplied by distribution newsagents.

This lack of knowledge of retail space availability sits at the core of the failure of the current model and is a key factor in newsagents being supplied magazines in a way that restrains their ability to compete with supermarkets and other magazine retailers.

The new rules the MPA proposes to trial focuses on a push model that remains ignorant of the retail space available. The result most likely will be that newsagents continue to be oversupplied.

On behalf of newsagents we have advised magazine distributors of the number of pockets available. Our experience is that this information if often ignored and oversupply beyond capacity to display continues.

It is not uncommon for newsagents to receive 25% more stock than they have the capacity to display in their businesses. To this the magazine distributors could be expected to say that newsagents can store the excess stock and display when able. Newsagents would respond to that noting that they often do not have the storage space and that they are not paid sufficiently to operate such a warehouse service.

THE ANTI-COMPETITIVENESS OF THE CURRENT NEWSAGENT MAGAZINE SUPPLY MODEL

The current magazine supply model to newsagents is different to the model used for competitors of newsagents. The differences make newsagents less able to compete. Here are key differences that deny newsagents the ability to be competitive:

1. Supermarkets carry only top selling magazine titles, usually to a cap of between 150 and 200 magazine titles whereas newsagents are forced to take what is allocated – usually 700 to 1,500 titles.

2. Supermarkets are not required to send back unsold magazines whereas most newsagents are – incurring for them significantly higher freight and labour costs.

3. Supermarkets are paid stocking and or other fees by magazine publishers for selected titles whereas newsagents receive no such fee.

4. Supermarkets control where they place magazines whereas the contracts newsagents must sign dictate magazine space placement and allocation.

5. Supermarkets are not required to give over prime space to promote magazines using posters and other marketing collateral whereas newsagents are required to use prime retail space to promote magazines with the threat of penalties from some if such displays are not created.

6. Some supermarkets are provided some magazine titles for sale at a cover price significantly lower than the cover price for the same title in newsagencies.

The supply model to supermarkets enables them to treat magazines as products from which they profit whereas the model to newsagents forces them to treat magazines as a business overhead.

MISUNDERSTANDING ABOUT EARLY RETURNS

At 4.b of Form A submitted by the MPA, they claim that newsagents engage in *indiscriminate early returns* . This statement is inaccurate and ought not be relied upon to justify the proposed trial of newsagent magazine supply rule changes.

Early returning magazines is the only mechanism newsagents have to manage cash flow. The magazine distributors will dispute this. They will say newsagents can request supply adjustments and or the elimination of titles. Such a statement would be inaccurate. While some requests by newsagents to distributors to reduce to cut altogether supply of titles are attended to, such action is only ever short term. The distributors often immediately replace cut titles with new titles and, often after three months, the cut titles reappear.

Early returning by newsagents is the only means available to manage their level of indebtedness.

There are three types of early return of magazines by newsagents:

1. **Return of all stock of a title on the day it arrives in the business,** denying the title any opportunity of achieving sales. NOTE: This could be done because there is no room in the newsagency for the magazine, to manage cash or to hit back at a distributor because of other behavior. It is our view that returning all stock of a title on the day it arrives is most likely not indiscriminate early returning.

2. **The return of some stock the day a title arrives in the business** in response to the oversupply by the distributor. NOTE: Some of the newsagency magazine management software used by newsagents tracks net sales and suggests an early return quantity based on this and allowing a reasonable gap for over average performance. The most common gap over average sales we have seen is 25%.

3. **The return of some or all stock ahead of the distributor set return date but some days or weeks after the title first arrived in the business.** NOTE: This type of return is usually done on the basis of sales so far and an assessment by the newsagent of the prospects of sales through the remainder of the on-sale period. Space availability is also a factor in this type of early return decision.

The MPA application makes no mention of early return types two and three yet it is our assessment that they make up the bulk of early returns.

PUBLIC BENEFIT

The best way to serve the public benefit in the availability of magazines is to provide newsagents with the ability to control magazine supply as it is only this which allows them the ability to come close to competing with their competitors.

The current situation favors supermarkets and other retail channels over newsagents. It gives those retail channels a competitive advantage over newsagents. These other channels do not have the same high labour cost nor are they forced to carry and process the same volume of unprofitable titles as newsagents.

Whereas we understand supermarkets are provided electronic invoices at no additional cost, newsagents have been forced to pay an annual fee of between $400 and $800 per year for the privilege of receiving electronic invoices. This is a financial burden not imposed on channels competing with newsagents.

One argument put forward for a difference in approach is that magazines are a key traffic generator for newsagencies. This is less the case now than in the time of regulation, prior to 1999. With under 50% of all magazines sold in Australia sold through newsagencies, our channel relies on other products for traffic with magazines often the add-on purchase.

Newsagents struggle to evolve their businesses in the face of changing circumstances because of the lack of control they have over the supply of magazines. Many newsagents maintain more magazine retail space than is commercially viable simply because of the volume of stock sent to them. Supermarkets do not have this problem.

THE MPA APPLICATION

At 4.a of Form A, the MPA states: *The MPA submits that the proposed Code of Conduct will result in an improvement in the commercial viability of newsagencies by reducing their business costs while increasing magazine sales.*

No evidence has been provided to support this claim. All tasks involved in the receipt of magazine goods for sale, pricing them, managing them in-store, selling them, removing them at the end of the on-sale, counting returns and removing covers from returns will still need to be done. The only saving will be the elimination of some of the freight component of returns. This is a small part of the cost of magazines.

As indicated at point 4 of the new rules to be trialed as documented in Annexure B: *A Distributor will not be required to accept Early Returns from Retailers, except where such Early Return is made by a Retailer to correct an error in allocations quantity.* This will require newsagents to carry some stock for longer than is the case today, increasing their costs.

At 4.b of Form A, the MPA states: *In order to limit the cash flow issues associated with the 'sale or return' model many newsagents are engaging in indiscriminate early returns sometimes without even offering the product for sale.* The MPA offers no evidence to support this claim. As stated elsewhere is this submission, some early returns are considered and appropriate. Early returns are the only lever currently available to newsagents through which they can manage their level of indebtedness to magazine distributors.

At 4.b of Form A, the MPA states: *More efficient distribution (where supply more closely matches demand) will improve the effectiveness of the supply chain, the retail experience for consumers and improve magazine sales.* The magazine distributors have the capacity to achieve this without a trial or rule changes. All they need to is act according to the claims they have made to newsagents in the past – that supply is based on the sales achieved in newsagencies as reported back through the provision of accurate sales data.

Our position is that if newsagents were supplied on the basis of reported sales with a small oversupply to allow for reasonable growth, there would be fewer early returns and more newsagencies in business today.

This position has been put to Gordon and Gotch and Network Services on many occasions over many years including to some directly involved in developing the proposed new rules for this MPA trial.

At 6.a, of Form A, the MPA states: *The pilot will be limited in scope and time and will not result in any detriment to the public.* We say this is inaccurate as the trial will not test changes to magazine supply arrangements to enable newsagents to operate competitively. We say the rule changes continue to restrict the ability of newsagents to be competitive with supermarkets and other outlets in the sale of magazines and that this will likely result in more newsagency business closures.

Annexure A notes that variables sought for the Pilot Group include *magazine pocket count*. There is no indication in the submission as to how this would be used.

At Annexure A Pages 9 through 12, the MPA outlines data to be assessed to determine performance and to guide advice to newsagents to help improve process management and understand the value of magazines.

Newsagents today have access to such reporting from their newsagency magazine management software. They can report on return on investment, return on floor space, return on shelf space, stock turn, magazine sell-through rates and other key performance indicators by distributor and often by magazine category. It is this data many newsagents use to engage in early returns.

Magazine distributors themselves have access to sell through data and this data sitting their own computer systems indicates the extent to which sell through in the newsagency channel is lower than in other channels – because newsagents are supplied by the distributors on a different model to other channels, because newsagents are more likely to be oversupplied.

At Annexure B, Part 2, Point 1 – Minimum Sales Efficiency, the MPA proposes a Minimum Sales Efficiency that is based on the distribution quantity per issue of a magazine title. This approach serves the publisher and distributor but not the newsagent. The Minimum Sales Efficiency does not reflect the retail lease and labour costs associated with the magazine space in a newsagency.

For the record, our estimate of Minimum Sales Efficiency necessary to break even by type of newsagency is as follows:

1. Capital city shopping centre newsagency: 65%
2. Capital city high street newsagency: 50%
3. Regional shopping centre newsagency: 60%
4. Regional high street newsagency: 45%.
5. Rural high street newsagency: 40%.

These numbers are based on years of working with newsagents and analyzing lease, labour and other costs for magazines.

We suggest that any trial using Minimum Sales Efficiency as a measurement point ought to require prior to the commencement of a trial the appropriateness of the proposed Minimum Sales Efficiency for the participating newsagents.

It appears to us that the MPA has set arbitrary Minimum Sales Efficiency percentages to serve magazine publishers and distributors and not newsagents.

At Annexure B , Part 2 Point 2 – Consecutive Nil Sales, the MPA sets points at which certain types will cease to be distributed for twelve months based on a documented number of consecutive nil sales. Our view is that for 2.a the number should be four consecutive weeks; for 2.b three consecutive issues and for 2.c two consecutive issues as noted.

Our bigger concern is that a title is only stopped for twelve months. Based on past experience, the magazine distributors will re-start the title. Newsagents ought to have the capacity to permanently stop a title.

An even bigger concern is what magazine distributors may do as a result of stopping a title. There is evidence today to indicate that the magazine distributors start other titles in response to currently supplied titles being stopped. This has the effect of delivering the same volume of product and maintaining the same level of inventory investment by newsagents.

We think an additional rule related to point 3 of Part 2 of the MPA submission committing distributors to actively ensuring their allocations software does not allocate any new titles at the same time or shortly after the cancellation of supply of any title.

At Annexure B, Part 2 Point 4 – Early Returns. Our view is that newsagents ought to have the ability to early return any title based on agreed criteria that is negotiated with a panel of newsagents and not their industry association representatives.

At Annexure B, Part 2 Point 5 – Redistributions – Packs & Singles. Our view is that there should be no redistributions. That said, if they are to be permitted under any rules, magazine distributors must be required to ensure that all copies redistributed are in merchantable condition with old price labels removed and with the pages not bent or damaged in any way. Network Services is guilty of redistributing titles that are un-merchantable.

At Annexure B, Part 2 Point 6 – New Titles. While we note that the proposed rules allow for newsagents being advised quantities to be distributed, there is no allowance for newsagents to be able to set their desired quantity. This is an extraordinary oversight. Indeed at 6.b, the MPA notes: *the number of copies of the Launch Issue distributed to each Retailer is determined reasonably having regard to the total print run of the Launch Issue and the average sales of 1 or more equivalent Titles (provided that a Distributor may distribute at least 2 copies of the Launch Issue to each Retailer).* There is no consideration in this rule of newsagents and their businesses. What if they do not have the space for a new title? What if the area of interest covered by the new title is satisfied by magazines from another distributor? What if the newsagent does not want to stock the title? Basing allocation on the print run continues the current distribution model that sees newsagents competitively disadvantaged compared to supermarkets and other retail channels.

At Annexure B, Part 2 Point 7 – Maximum shelf life. For reasons outlined already, the proposed maximum twelve-week shelf life only works if reasonable sales are achieved right through the proposed self life. One reason newsagents early return a title is because of a long shelf life. In their newsagency magazine management software newsagents can easily see sales and sales decay graphs. They can see for some long on-sale titles that as much as 80% of sales are achieved in the first four weeks, making the next eight weeks loss-making unless they early return.

This Maximum shelf life rule coupled with the early returns rule denies newsagents the opportunity to be commercially competitive with supermarkets and others. To this some publishers and distributors will say that they supply some long shelf life titles to supermarkets. Responding to that we would want to know what stocking and or other fees and inducements are offered to supermarkets to make the allocation of the space viable. Further, we would note there is a significant difference in the mix of magazine titles purchased in newsagencies versus supermarkets, making some long shelf life titles, such as food titles, viable for supermarkets.

OUR PROPOSED MAGAZINE SUPPLY TRIAL ALTERNATIVE

Our view is that the magazine distributors, magazine publishers and newsagents do need to work collectively on a new magazine supply model and that it is appropriate that such a model is trialed for an appropriate period of time to determine effectiveness.

The goal of our proposed trial is to test supply rule changes that would enable newsagents to be competitive with supermarkets. The MPA proposed trial does not test such magazine supply changes, Indeed, it seeks to further restrict newsagents thereby making them less competitive.

newsXpress proposes it works with the MPA and magazine distributors on behalf of its members on an alternative trial.

The goal of the proposed trial is to test magazine supply rules that focus on making newsagents competitive with supermarkets and other retail channels.

We propose this as we consider this approach is what is needed to encourage newsagent engagement with magazines and to guide the increase of sales of magazines in newsagencies.

Rules we propose for trial in a selected group of newsXpress outlets are as follows:

1. newsXpress to centrally set magazine titles to be ranged by participating newsXpress outlets.
2. newsXpress to set supply volume for each issue of an approved title for each participating newsXpress outlet.
3. Magazine distributors to advise newsXpress of new titles and suggested allocations for approval.
4. Magazine distributors to facilitate engagement with newsXpress on discovering new titles which could be added to supply based on existing sales.
5. No early returns by participating newsagents for the first thirty days of on-sale unless by prior agreement with the magazine distributor.
6. No allocation of a previously cancelled title by a magazine distributor without newsXpress permission.
7. Re-issues to be circulated to participating newsagents only with newsXpress permission.
8. No full copy returns of unsold magazines required.
9. The option for a publisher to pay participating newsagents a stocking fee to carry a title for an agreed period of time – to enable a publisher to use the newsagency channel to get a new or low volume title in front of consumers without the newsagent having to donate space and labour for no return.

NOTE: These are not the only supply rules to apply. The above list reflects rules that are different to how magazines are allocated today.

As part of the trial newsXpress would engage with each newsagent in the following ways:

1. Undertaking a relay of magazines in-store to create a fresh shopper experience and ensure optimum placement based on known successful magazine title adjacencies.
2. Training those involved in putting out magazines on how to undertake this important task to drive magazine sales.
3. Reviewing magazine management practices to ensure a current best practice approach.
4. Training all retail staff to better engage with shoppers about magazines.

newsXpress has proposed its alternative trial to the magazine distributors and key magazine publishers several times over the last three years as they considered the development of the new rules proposed to be trialed under the application before the ACCC.

newsXpress has proposed providing its services at no cost to any participant in the trial.

COMMENTS ABOUT THE ANF

We are disappointed Australian Newsagents' Federation claims to represent newsagents on this issue without canvassing the opinions of newsagents. We are not aware of any consultation with newsagents or other parties who could provide access to facts that could facilitate the ANF developing a more informed view.

CONCLUSION

The proposed trial before the ACCC for authorization does not address the goals of the trial. Further, it does not address the anti-competitive business rules and processes of magazine supply to newsagents versus those for competitors of newsagents.

For newsagents to be viable with magazines, they need the access to business management levers that enable them to act in the interests of their businesses. The current model applies what is effectively a tax that is a major factor in the closure of many newsagencies in recent years.

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