



Retailers' Christmas Survey 2017
Can Santa stand the heat this season?

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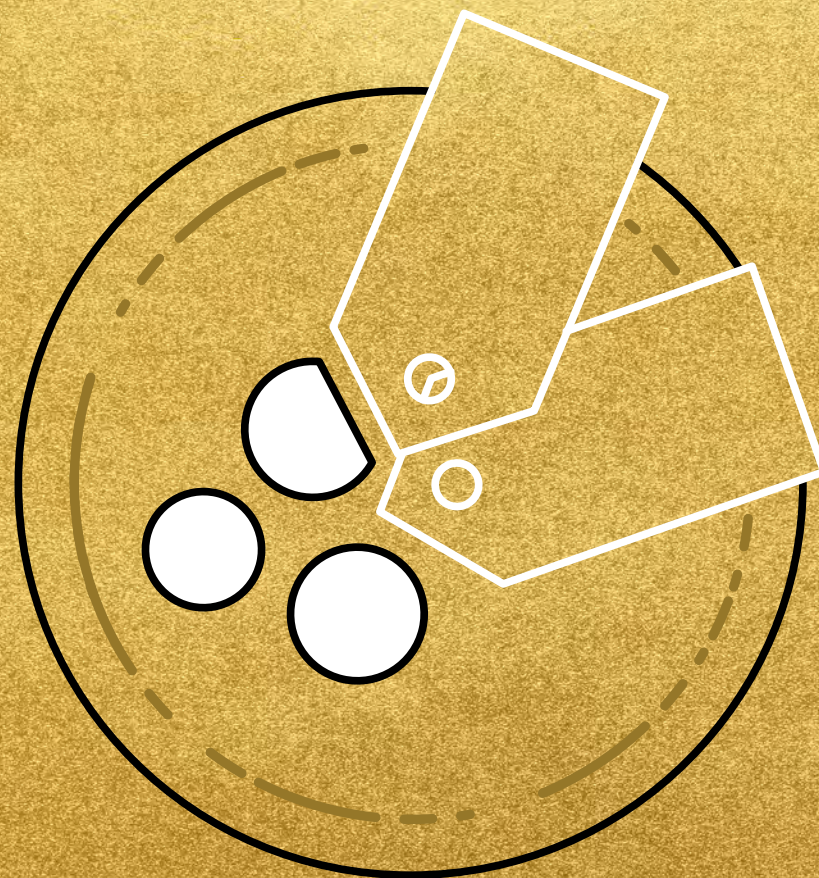
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Introduction

Introduction

Executive summary

Welcome to the sixth annual edition of the Deloitte Retailers' Christmas Survey. In the lead up to Christmas we surveyed a cross-section of executives and senior management from Australian retailers about their expectations for the 2017 Christmas period and beyond. The report analyses retailers' sentiment for the Christmas period, key trends and their expectations and priorities for 2017.



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Executive summary

Christmas caution

Overall we've seen the retail market grow and perform reasonably well so far this year. However, this hasn't necessarily translated into better results for all retailers. Whilst the overall retail pie is growing, greater competition has meant that there are more players than ever, all wanting their share.

When we look ahead to retailers' expectations this Christmas, it's no surprise that there is a strong theme of cautiousness. Whilst 69% of retailers expect Christmas 2017 sales to exceed 2016, less than half expect growth over 2%.

This is also evidence of a growing shift to focus on profitability rather than chasing top line growth. We saw many retailers pay the price for heavy Christmas discounting last year, with first quarter sales in 2017 proving to be a challenge for many. There seems to be a clear determination not to fall into the same trap this year which is evident in retailers' discounting strategies this Christmas. 85% of respondents are expecting to maintain or increase sales margins over the Christmas period compared to last year.

Whilst we continue to see nearly a third of retailers planning to mark prices down in early December, there is also a noticeable increase in the percentage of retailers seeking to push back discounting activities until after Christmas. Time will tell whether retailers stick to their guns.

Cracking open Christmas

With Christmas representing the most important sales period for most retailers, we wanted to understand what was their key focus area to increase sales this season.

New products (30%) were again the highest focus for retailers to get right. But a close second was digital and omni-channel at 27%. This marks a fundamental shift in retailers' priorities with Australia now on the edge of a digital tipping point. Investment in new technologies to make stores more appealing, shopping online more convenient and creating a seamless experience for customers, appears to be a key driver for success this Christmas. A word of caution however; the percentage of retailers focusing on customer service as a key driver for Christmas growth has fallen from 27% to 13%. Let's hope lessons have been learned from the past.

Christmas shopping online

With the continued investment in omni-channel, it's no surprise that retailers are expecting online sales to increase this Christmas. But what is surprising is the rate of growth – 69% of respondents are expecting their online sales to be at least 10% higher than last year, with 31% expecting online sales this Christmas to make up more than 10% of total sales.

Despite these results, the Australian market still has a long way to go before it reaches the level of online sales in other major retail markets. Consumers in the US expect a staggering 51% of their Christmas shopping will be done online this year. Australia is nowhere near these levels, but with the arrival of Amazon we can expect the rate of change to accelerate.

A new kid in town

As Amazon prepares to officially launch in Australia, there is both hope and trepidation for what the impact may be. With 17% of our survey respondents citing Amazon as their biggest source of new competition, they will no doubt have an immediate as well as long lasting impact on the Australian retail sector.



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But it's not all doom and gloom – far from it. Whilst 33% of respondents believe Amazon will have a negative impact on their business, 40% can see the positives that an Amazon arrival will bring. Greater channels to market created by Amazon together with opportunities for retailers to work with them, will provide a boost to some retailers.

Keeping the faith

With retailers facing ever increasing competition, we continue to see greater investment in building more meaningful relationships with customers. Shifting the mentality away from that of a transactional customer relationship to one based on a meaningful connection with the consumer is fundamental. With so much choice, customers increasingly want their purchases to mean something more to them than just a new product or service, they want to feel personally connected to the brand or the organisation.

In this year's survey, we asked retailers how they rate the loyalty of their customers to their brand and products. Some 82% of respondents believe that they have either good or strong loyalty from their customers.

Based on current market activities and trends, such a figure is surprisingly high and there may well be some aspiration rather than reality contained in these results. With the arrival of Amazon, we'll soon see.

Outlook

Despite the cautious expectations for retailers this Christmas, they remain optimistic about their growth prospects in FY18. Some 51% of retailers expect to grow their earnings by more than 5% next year which, whilst down from 60% in last year's survey, remains a lofty aspiration. With the total retail market forecast to grow at 3.6% in FY18, where will this growth come from?

Undoubtedly, the fight for market share looks set to be fiercer than ever.

Some 43% of respondents expect new bricks-and-mortar stores to be their number one strategic priority to drive sales growth in FY18. In the six years we've been running this survey this is the highest result we've seen. With many retailers experiencing flat like-for-like sales at best, there is a real risk that top line growth will only be achieved through lower profitability. Perhaps a better strategy would be to double-down on existing store networks to improve customer experience, location and create a true omni-channel experience.

And we mustn't forget about Amazon, though there's seems little chance of that. There has been so much speculation on Amazon's arrival into Australia. When will they start trading, which geographies will they focus on, what categories will they enter. The list goes on. In many ways it doesn't actually matter – what matters is having a strong brand, a meaningful relationship with the customer and a compelling reason for those customers to want to buy your products and shop with you, be that online or in-store. Amazon doesn't change these fundamentals.

What we do know, is that with so much change in the Australian retail landscape, we are set for another fascinating year.



David White
National Leader
Retail, Wholesale & Distribution Group



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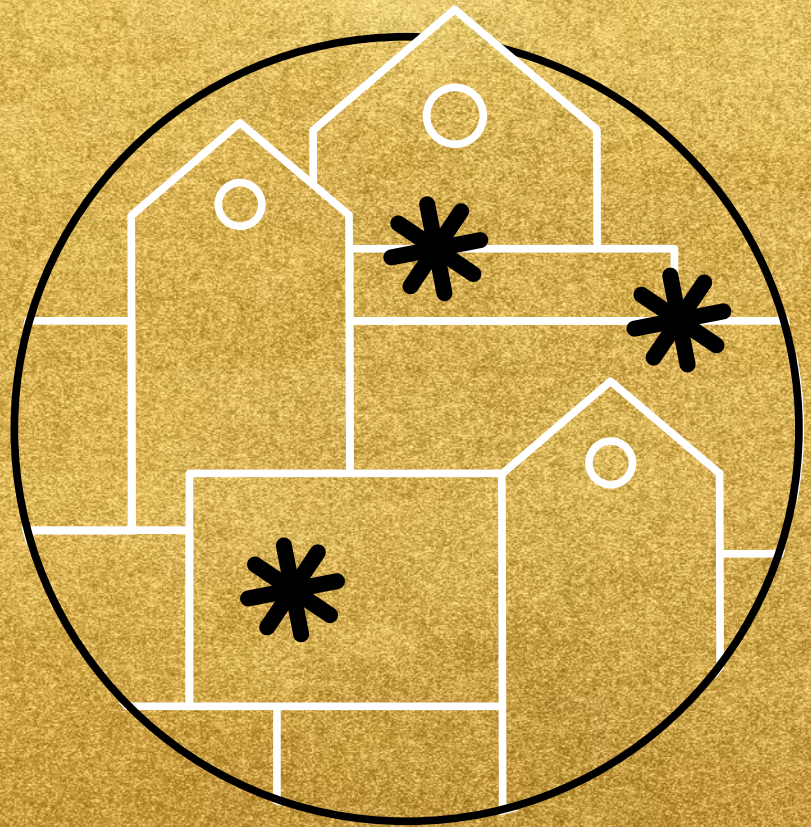
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Christmas expectations

Christmas expectations

Caution reigns this season

Despite the relatively stable economic environment and consumer spending throughout the year, competition for share of wallet has been intense. Whilst there have been some great success stories, at the same time a number of high profile retailers haven't survived. There is some concern amongst respondents that this weakness may continue throughout Christmas 2017.

This caution is reflected through our survey results, with retailers not expecting a bumper Christmas 2017. Some 69% of retailers expect sales growth compared to 76% last year and strikingly only 42% expect over 2% growth compared to 54% in 2016.

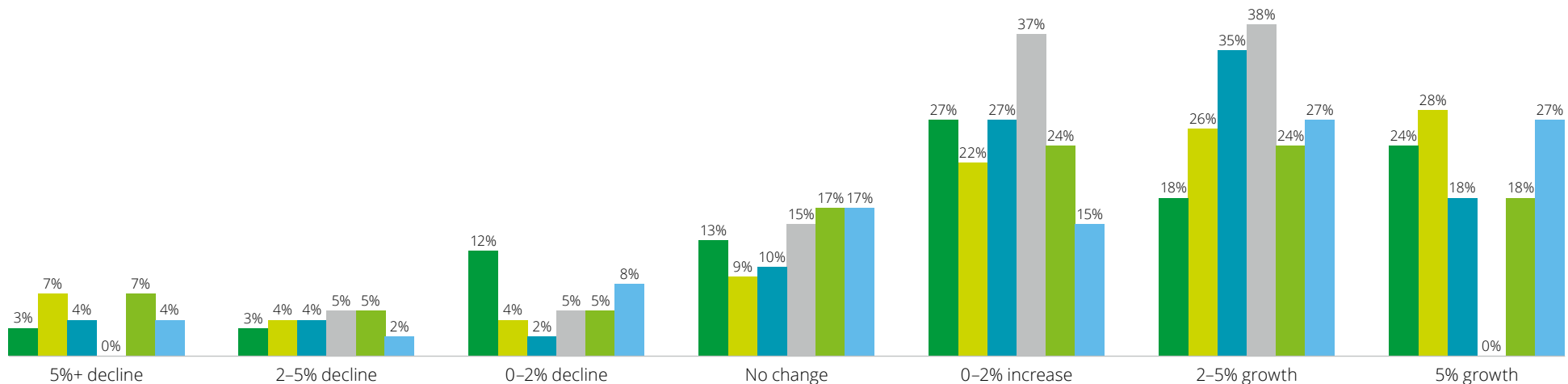
The competition is most fierce in apparel, which has faced the dual challenges of price deflation and the aggressive expansion of foreign operators into the Australian market.

Also impacting the market is the shift in spending habits of consumers. Product sales are declining as a share of consumer wallets, with catered food and entertainment picking up an increased portion.

Retailers hate uncertainty, and with Amazon's impending market entry there is certainly a high level of cautiousness around Christmas sales' performance.

Do you expect Christmas sales to exceed the previous Christmas trading period?

● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



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Christmas expectations

Caution reigns this season

Despite, or perhaps because of the nervousness around sales, retailers are seeking to hold steady on margins. Even more retailers are expecting consistent margins from last year, with 43% expecting an increase in margins compared to 48% in 2016. Retailers expecting margin declines are broadly consistent with our last survey.

With so many new and expanding competitors in the market combined with price deflation and rising electricity costs, it will be a challenge for retailers in the apparel, footwear and department store sectors to maintain margins over Christmas in the face of these headwinds.

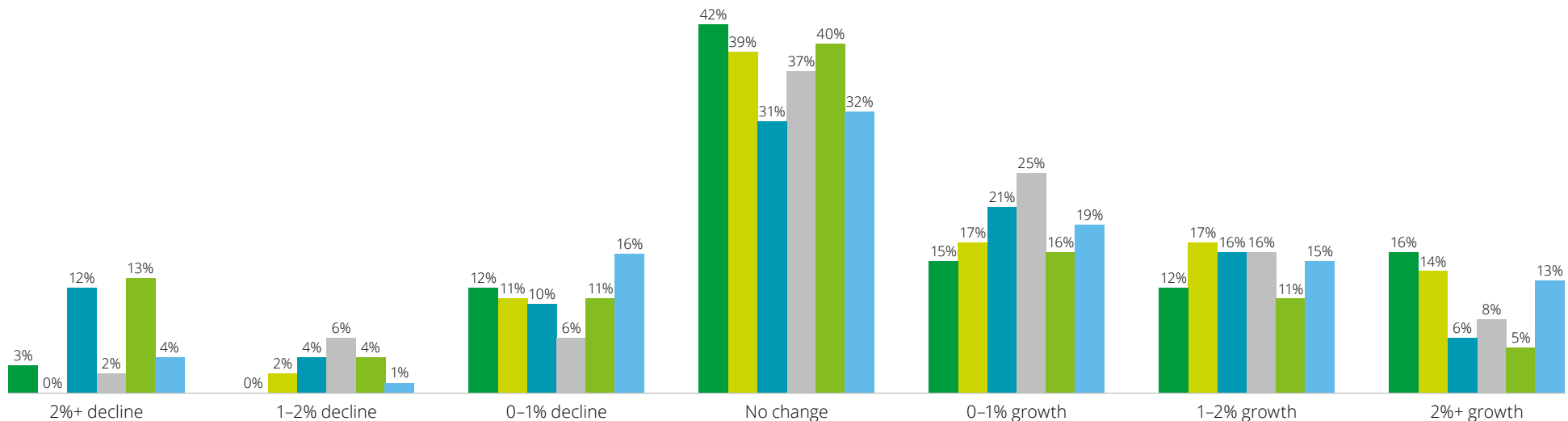
Food and grocery may find the going easier with price inflation providing a boost to margins.

“Those that have a cost structure that is lean and agile, complemented by a range, an in-store and online experience that provides a strong reason to ‘buy now’ will prosper.”

– Survey respondent

Do you expect margins for the Christmas period to exceed the previous year?

● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



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Christmas expectations

Caution reigns this season

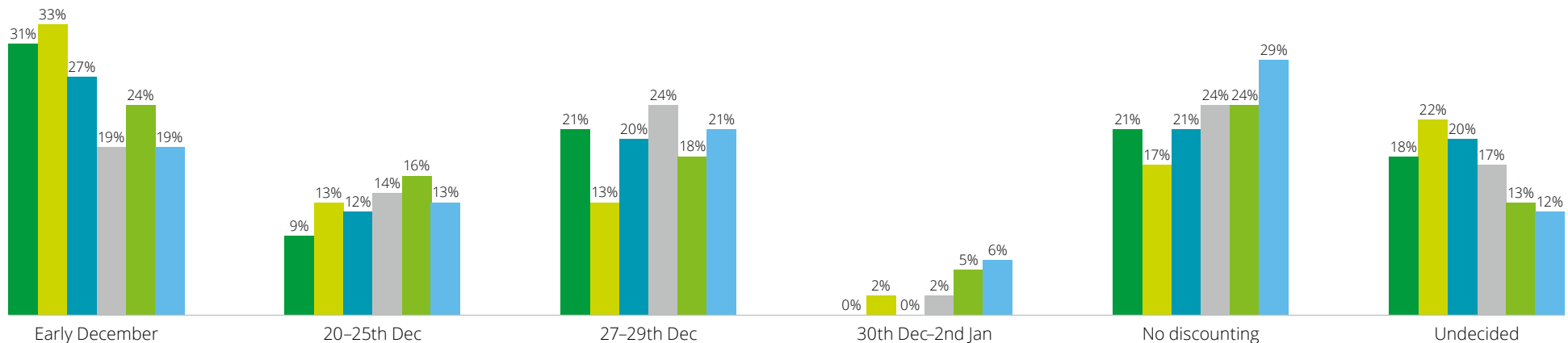
Over the past few years, there has been a consistent shift to discounting earlier and earlier in December. This year, not only has that trend reversed, but the percentage of retailers committed to no discounting has increased back to 2015 levels. For those that will discount, post-Christmas sales look to be back in vogue with 21% expecting to use this period to clear Christmas stock.

During Christmas 2016 retailers gave away significant margin during the peak sales period, which left the cupboard bare in the first few months of 2017. Traditionally, specialist retailers have taken their cues from the major department stores in marking down products, and with these department stores rebuilding after a number of difficult years perhaps the hope is that the trend of early and deep discounts will begin to reverse this year. Time will tell.

Retailers are looking for alternative ways to delight customers, and 36% of respondents highlighted customer experience and engagement as the number one strategic priority for their business. The trends overseas show that for many retailers, competing on price alone can lead to a race to the bottom, resulting in mostly losers and only a handful of winners. Our survey suggests that Australian retailers get it – they are instead focusing on engaging with customers to generate sales rather than on a purely transactional level.

At what point do you expect to begin discounting around Christmas?

● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



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Australian retail macroeconomic outlook



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This Christmas season is likely to throw up some challenges for consumers and retailers alike.

Challenges for consumers because income growth remains slow and financial risks related to stretched housing prices are a concern, which may drive some tough choices in terms of discretionary spending. Challenges for retailers because competition in the sector remains intense and additional international retailers keep clamouring on Australia's door, wanting a piece of the action in a wealthy market with a growth track record.

The first half of 2017 saw retail spending growth pick up, driven by strengthening employment outcomes including a rebound in full-time jobs growth, as well as continued wealth gains from housing. But low consumer sentiment and an array of financial risks remain key constraints, and so retail sales have declined over August and September.

The forward looking Australian Food & Grocery Council (AFGC) Retail Index suggests that retail trade growth will level out over the coming months leading into Christmas (as drawn from recent pallet activity across the country).

The continuation of double digit house price growth in Melbourne, Canberra and Sydney is adding to the wealth of home-owning consumers. This is still having some positive effect on retail spending, albeit lower than when housing market risks were less concerning to homeowners. Consumers are now more cautious about housing wealth, particularly as Australia's already high household debt faces upside risks if and when interest rates rise. Higher mortgage payments and the risk of a housing market downturn are also contributing to caution among consumers.

The best news for retailers has been that employment growth has improved significantly over the year. Jobs growth has been primarily driven by some recovery in full-time job numbers, with full-time jobs rising 3.7% over the year to October while part time jobs grew by just 1.5%. Despite this recent recovery, the proportion of part-time jobs is still high (around a third of total employment). There is also significant underemployment of 8.6%, which means that well over one million workers across Australia would prefer more hours of work than what they currently have.

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Australian retail macroeconomic outlook



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And because so many workers are looking for more work, employers have little incentive to offer much in the way of wage growth. Wage growth over 2017 has been negligible, growing only 2.0% over the year to September. This adds downward pressure to retail spending growth, since many workers are seeing no real growth in their take home pay compared to last Christmas.

Reflecting all these trends, total nominal retail spending growth came to just 3.6% in 2016-17, and is expected to stay steady at 3.6% in 2017-18.

As the wealth effects from house prices fade and employment outcomes improve, the composition of the retail budget is expected to move from wealth-driven categories to wage-driven categories. This is beneficial for non-discretionary categories such as much of food spending, but puts pressure on discretionary retail categories such as apparel and household goods, as well as Christmas spending.

These increasing pressures in the Australian retail market aren't deterring international retailers though. Australia is considered an appealing destination for international retailers because Australia's economy is relatively strong and low risk, our population is growing quickly, and because our retail profit margins are still relatively high, compared to other nations. Our growing tourism visitation is also an incentive for retailers with international brands to locate here – further increasing competition.

More jobs across the economy are a pillar for retail success, and on that front 2017 has delivered. But low consumer sentiment and an array of financial risks are likely to still keep a lid on spending growth this Christmas.



David Rumbens

Partner

Deloitte Access Economics



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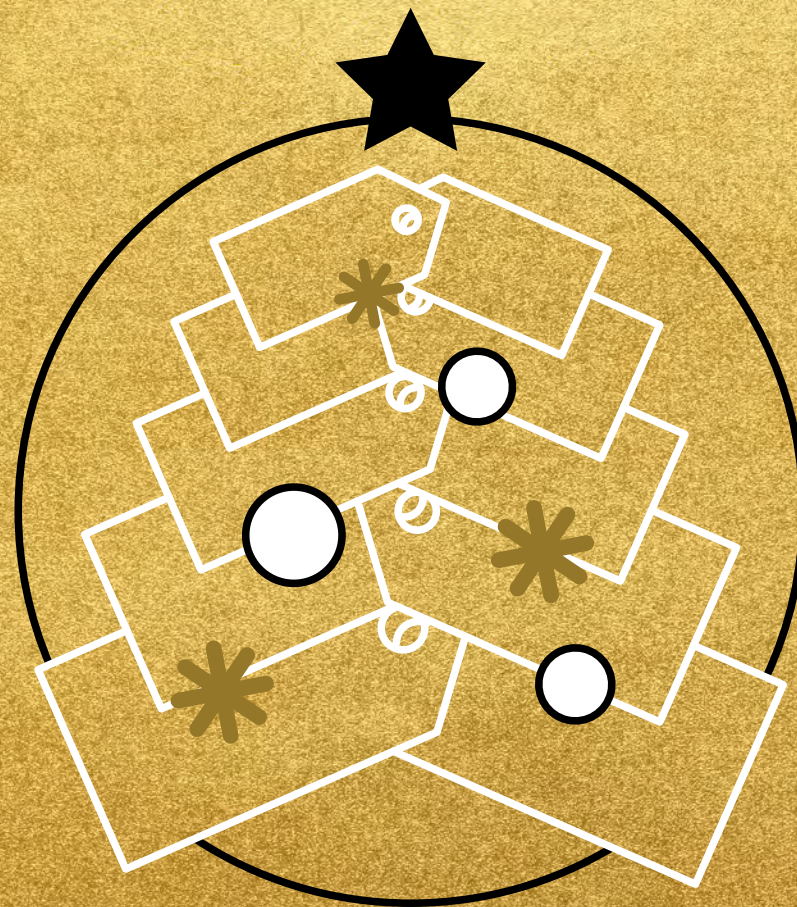
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Retail trends

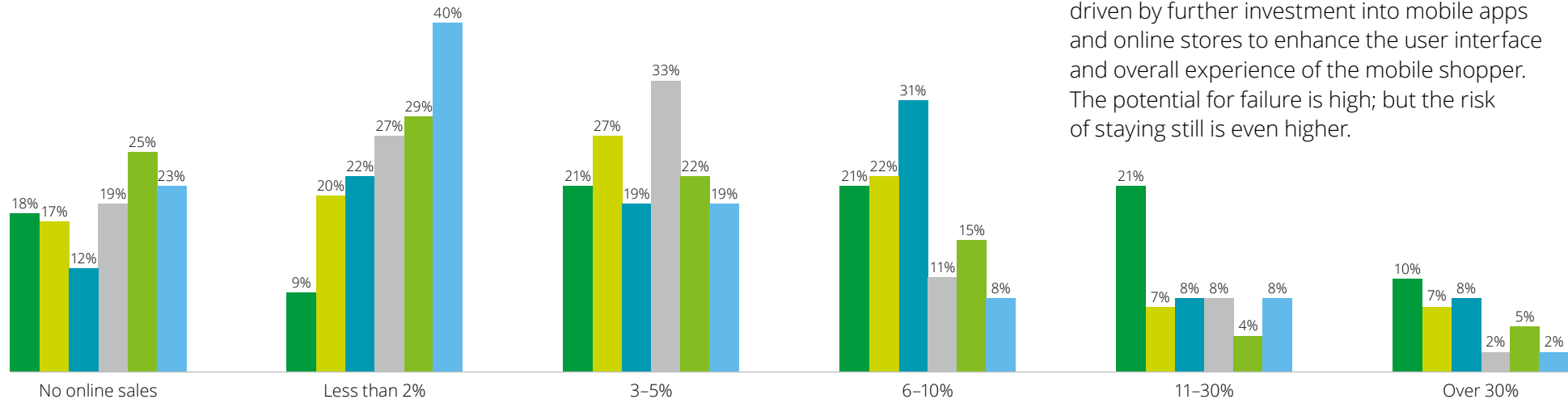
Retail trends

The digital tipping point

The online share of sales has consistently increased in every survey since 2012, and 2017 is no different. The number of retailers expecting online sales above 6% has increased from 36% to 52%. In addition, over 31% of respondents believe their online sales will be more than 10% of their total sales for the period. These results are typical for the online share of sales that we see in the market and there is an ever increasing proportion made up of online.

What percentage do you expect your online sales to be over the Christmas period?

● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



Digital influence in retail is far more than just eCommerce. The relationship between bricks-and-mortar operators and online is an ever strengthening one as the value of an effective digital strategy continues to bear fruit for traditional retailers.

Over 40% of in-store purchases in Australia are influenced by digital in some way, and we have one of the highest appetites for digital engagement in the developed world. Of those, 65% use digital tools before they ever actually walk into the store. As a result, arguably more important than the raw numbers is how online sales integrate into the broader conversation between a retailer and the consumer.

Retailers understand this, with over 80% of respondents considering an effective digital strategy to be critical or very important to the performance of their businesses.

The market is now facing a digital tipping point, where digital becomes not just a complementary sales channel but the core of the experience. Retailers are embracing true omni-channel, with the reinvention of the store experience, consolidation of store networks and shifting of large portions of sales onto digital storefronts.

Integrated offerings are being harnessed by retailers to further connect with their customers both in store or at home. This is largely being driven by further investment into mobile apps and online stores to enhance the user interface and overall experience of the mobile shopper. The potential for failure is high; but the risk of staying still is even higher.



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Retail trends

The digital tipping point

Despite the online share of wallet increasing this year, growth in online sales continues to accelerate. We see a consistent trend of growth in online sales, and despite the channel becoming more mature, the pace of change has increased this year. Local retailers are investing heavily in digital strategies, bringing a consistent and seamless experience between the in-store and online storefronts. With retailers seeing more traction in online sales, the investment in omni-channel is starting to achieve a greater return.

This growth is unlikely to slow down. Consumers in the US expect a full 51% of the holiday budget will be spent online this year. Given that the levels of digital influence in Australia continue to follow trends in the US, retailers need to consider the impact of a future landscape where consumers shop online for over half of their Christmas spending.

This is largely due to the type of shopping; gifting at Christmas lends itself to online purchases due to ease of search and a wide range of trusted products at the fingertips of the consumer.

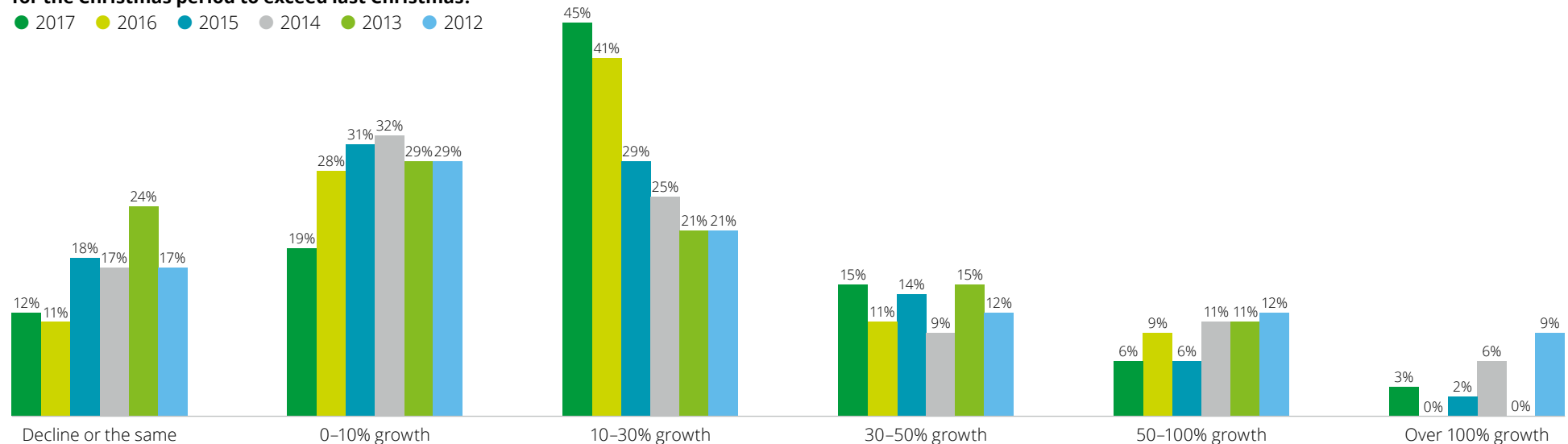
“Retailers may wish to consider assessing the maturity of their digital strategy in light of online’s increasing importance as a holiday shopping channel.

Our analysis found that 83 percent of survey respondents expect to use their desktops and/or laptops for holiday-season shopping”

– Deloitte US Retail Survey

By what percentage do you expect online sales for the Christmas period to exceed last Christmas?

● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



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Retail trends

Developing a winning strategy

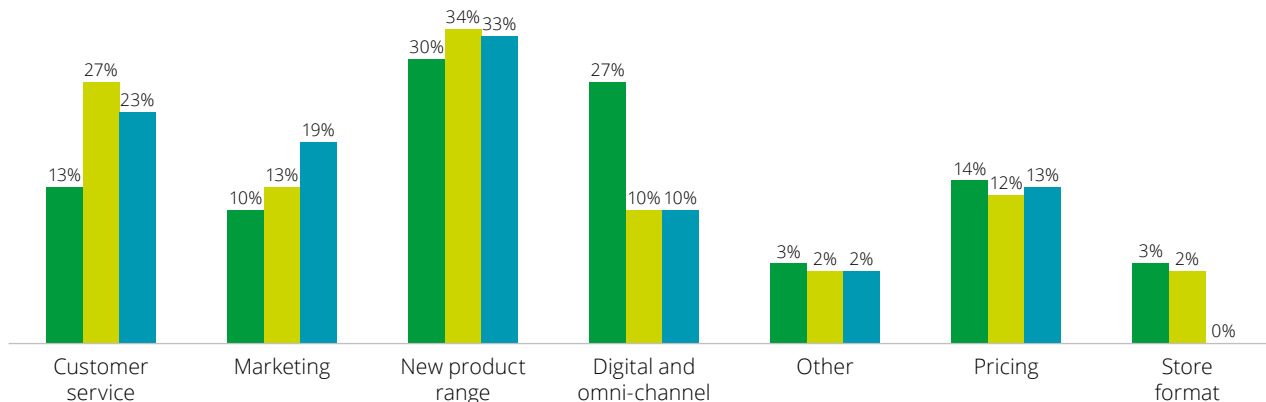
So how are retailers planning to win this Christmas? Consistent with the results of previous surveys, retailers told us that their main focus this Christmas was new product ranges, with 30% of retailers surveyed making this a priority. However, we've seen a large shift to digital and omni-channel, with 27% naming this as their key priority for sales growth at Christmas.

Retailers appear to be shifting focus away from customer service as a strategic priority over the Christmas period, but we don't see this as a zero sum game. An effective digital strategy forms an integral part of the customer experience; we think that the focus on digital strategy reflects an acknowledgement from retailers that without digital enabling both customers and in-store staff to compare, review and locate products the ability to make the sale is much more difficult.

Retailers are convinced of the loyalty of their customers with 36% rating customer loyalty as strong and 46% as good. Whilst brand loyalty still holds some cachet in the market, recent history suggests that loyalty holds only as far as the last interaction and consumers have been ruthless to retailers that have not maintained service, experience and price competitiveness. With the competition only becoming more fierce, businesses in the sector will need to stay on their game to hold on to the loyalty of their customers.

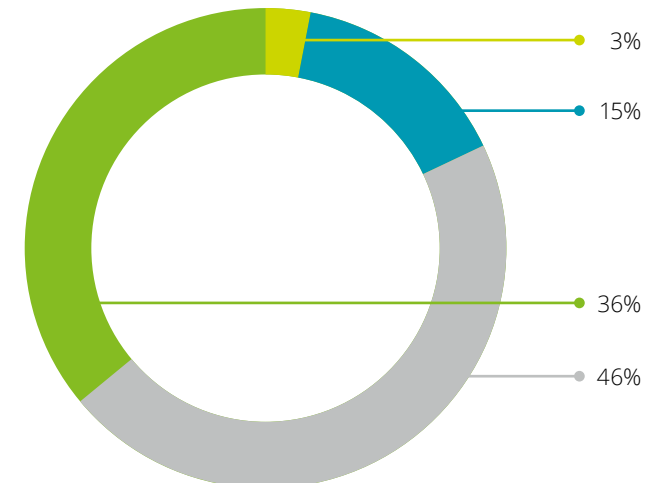
What is the single most important focus area of your business to increase sales this Christmas?

● 2017 ● 2016 ● 2015



How would you rate the loyalty of your customers to your products and brands?

● None ● Average ● Good ● Strong



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Retail trends

Relationship status: it's complicated

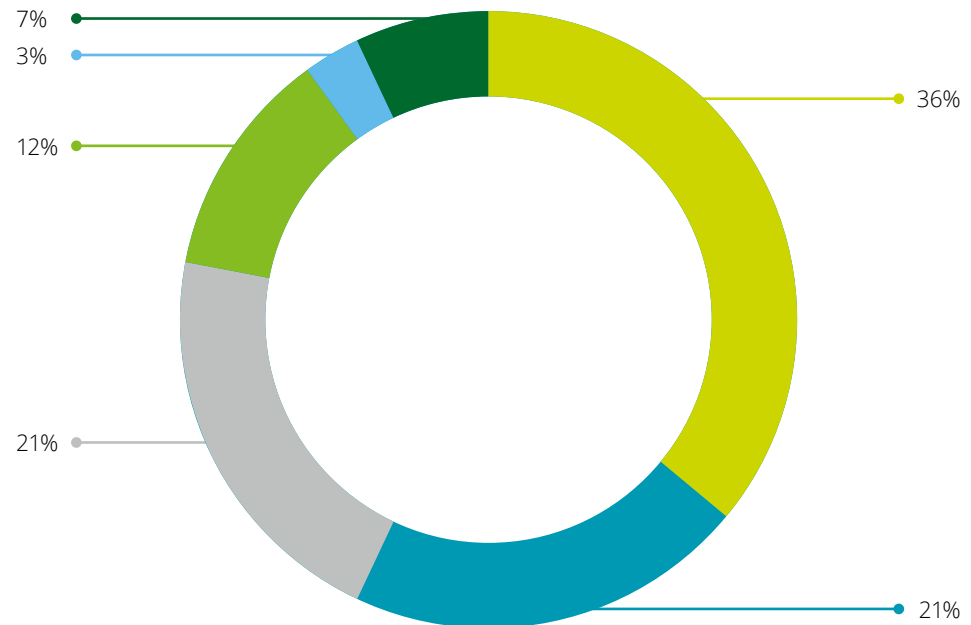
More than any other industry, retail is most exposed to economic, technological, social and demographic changes. New trends or technology can rapidly shift the relationships between brands and customers very quickly, making business models obsolete.

Retailers are listening; 36% of respondents consider customer engagement and experience as the number one focus of operators in the industry. Perhaps responding to the crowded marketplace and low consumer confidence, retailers are relentlessly focused on how to increase touch points, create a community around the brand and offer an experience beyond the shopping centre.

The focus on customer experience and engagement is a welcome change from the focus on opening stores. Retailers are thinking about how to build lasting relationships with customers which we think is the right avenue for sustainable growth.

What is the number one strategic focus of your business?

- Customer engagement and experience
- Efficiency and cost control
- Organic growth
- Omni-channel
- Acquisitive growth
- Other



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“Whilst I have a feeling the spiral of endless sales will continue for the time being, I expect we will continue to witness the encouraging improvement in retail innovation as the ‘Amazon factor’ has led more retailers to think about how they up their game.

Development of in-store experiences and service that cannot be matched by online players will hopefully see the shopping centres return to destinations that draw in customers on more than just price.”

– *Survey respondent*



Bringing it on balance

How the new leases standard will disrupt the retail industry

Changes to accounting standards are rarely barbecue stoppers; whilst accountants may get excited about changes to financial reporting frameworks, usually these don't fundamentally change how financial information is presented. This year is different; the change to the leasing standard (AASB 16 Leases) will have such a significant impact on the retail sector that companies, boards, investors and the media are sitting up and taking notice.

The new leasing standard will change the way financiers, property teams, analysts, shareholders and the general public view information in the financial statements of retailers with changes to earnings before interest, tax, depreciation and amortisation, interest expense, gearing and rental expenses.

Put simply, on signing the lease the tenant becomes obligated to pay the landlord for the value of that floor space for the duration of the lease. The obligation is, in most cases, based on the present value of the rental payments discounted at the incremental borrowing rate, which is effectively a secured lending rate. Correspondingly the entity is also entitled to an asset, known as a right-to-use asset, which represents the 'ownership' of the retail space for the duration of the lease.

During the lease, rather than recognising lease payments as rent, the lease cost is split between depreciation of the lease asset, and the payment of interest and principal of the lease liability. From a cash flow perspective, the payment be separated between the principal portion in financing activities, and interest within operating activities (or financing activities depending on the relevant accounting policy choice).

Further complicating matters, not all rent obligations are recognised on the balance sheet. Turnover/percentage rents and some exempted arrangements like casual or rolling leases are recognised in rental expense.

The devil is in the detail; with a mix of lease types, base and percentage rents, modifications, market re-sets or allowances, presenting consistent and appropriate financial information could become very complex. Incentives, options and renewals also need to be considered. With hundreds or thousands of leases, each with their own individual clauses and characteristics, this can very quickly become an overwhelming task.

In an operational sense the obvious challenges of the new standard will be capturing the data required to calculate the numbers, as well as developing leasing models which capture and calculate the appropriate balances. These models need to be able to handle modifications, revisions, changes to lease assumptions and forecasting of impacts into future periods.



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Bringing it on balance

How the new leases standard will disrupt the retail industry

Some other impacts may not be so obvious:

- Will debt finance agreements be restructured to include changes to covenant definitions?
- Will non-IFRS reporting measures be used in order to communicate to stakeholders such as shareholders, analysts and the market?
- Do these stakeholders understand the change, or will the company need to educate stakeholders on the change?
- How is the business valued and how will it value potential acquisitions?
- Finally, has the entity considered the cost of implementation, legal advisors, accounting advisors, and third party information systems to respond to all the above?

Changes in accounting standards are not unusual, although it is rare that a new accounting standard will have such wide ranging and dramatic impacts on the way entities account for and present financial information. The cost and effort in implementing this standard should not be underestimated, and will take up a significant amount of management's time and focus.

With leases arguably the most fundamental to retailers' business models compared to other major industries, companies in the sector need to start preparing for change and devoting significant effort to understand the impacts and develop the operational and financial models to meet the challenge.

The impact of this new standard will be significant for most retailers. The effective date (periods commencing on or after 1 January 2019) may sound a long way away but will be here before we know it. Businesses should start understanding how the new requirements will impact them, consider any wider implications and make any required changes to information systems, processes, incentive plans and financial covenants *now*; as well as educating stakeholders as to how they should evaluate financial results.



Damien Cork
Director
Assurance & Advisory





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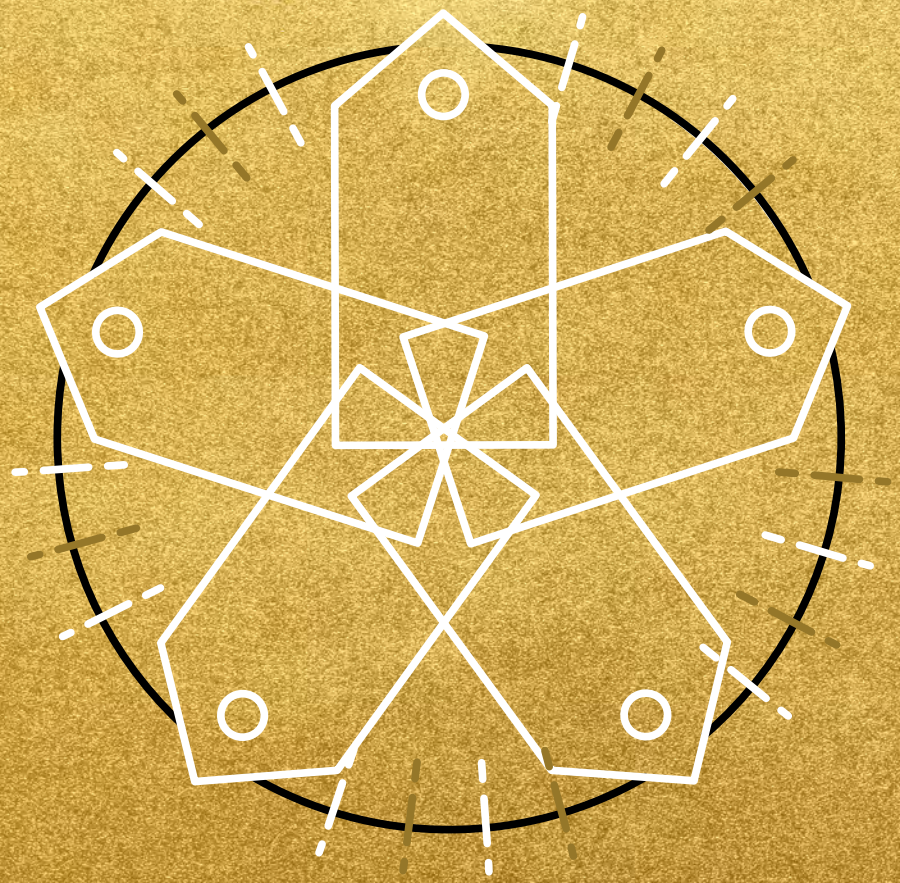
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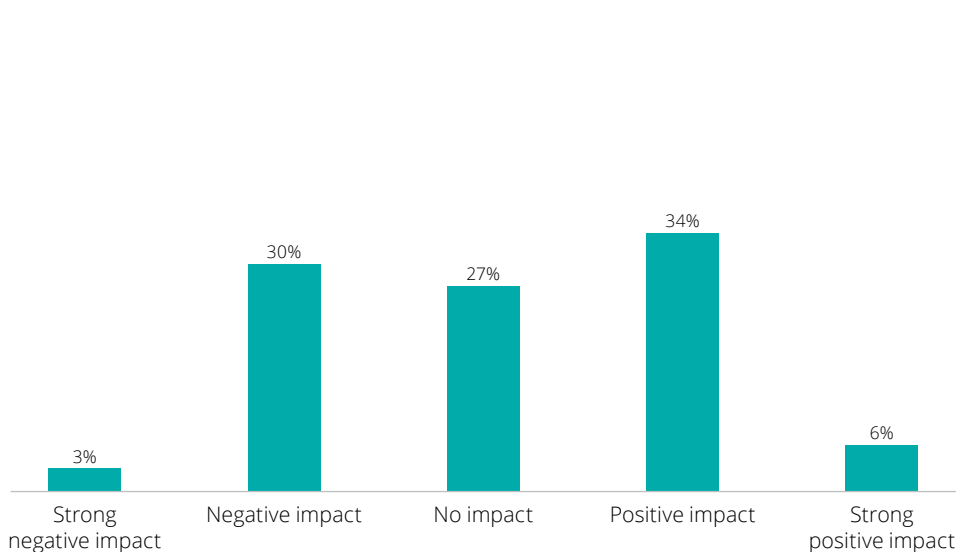
Competitive landscape

Competitive landscape

Welcome to the jungle

With a mixture of fear, trepidation and perhaps also, some quiet confidence, the Australian retail market awaits the arrival of Amazon this year. Amazon is rumoured to launch before Christmas, and is expected to offer an initial selection of products and incrementally increase range and categories throughout 2018.

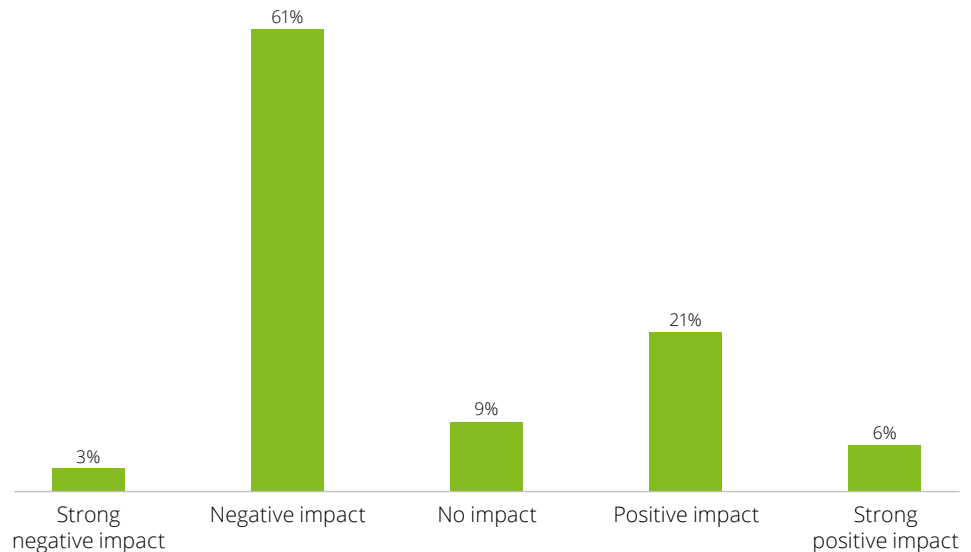
How significant do you believe Amazon's arrival in Australia will be on your business?



Retailers overwhelmingly expect Amazon to have a negative impact on the Australian retail marketplace (64%) compared to 27% who see Amazon as a positive influence.

Somewhat paradoxically over a third of retailers believe Amazon will have a positive influence on their business. This highlights that retailers might see benefits in the short term as Amazon acquires stock from local distributors and allows retailers to sell through the Amazon platform, but over the longer term lower margins and profitability across the landscape awaits.

How significant do you believe Amazon's arrival in Australia will be on the retail industry?



“Those that are agile and are able to cater and provide sound consumer options (online, in-store, click and collect, etc) will maintain or improve. Those that have not/do not streamline processes and systems will struggle to compete. Amazon will create additional pain for many retailers.”

– Survey respondent



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Competitive landscape

Welcome to the jungle

This year, we specifically asked retailers whether they expected to see the most increased competition coming from Amazon, and 17% highlighted this as a key concern. As highlighted on the previous page, Amazon presents both a challenge and an opportunity for local operators. Overseas, the domination of Amazon in online retail has forced many retailers to adapt and find innovative ways to connect and build two way communication with customers. However the Australian market is not isolated; retailers have been quietly innovating as the competition heats up locally and Amazon is already here with around \$8bn in sales through the US portal.

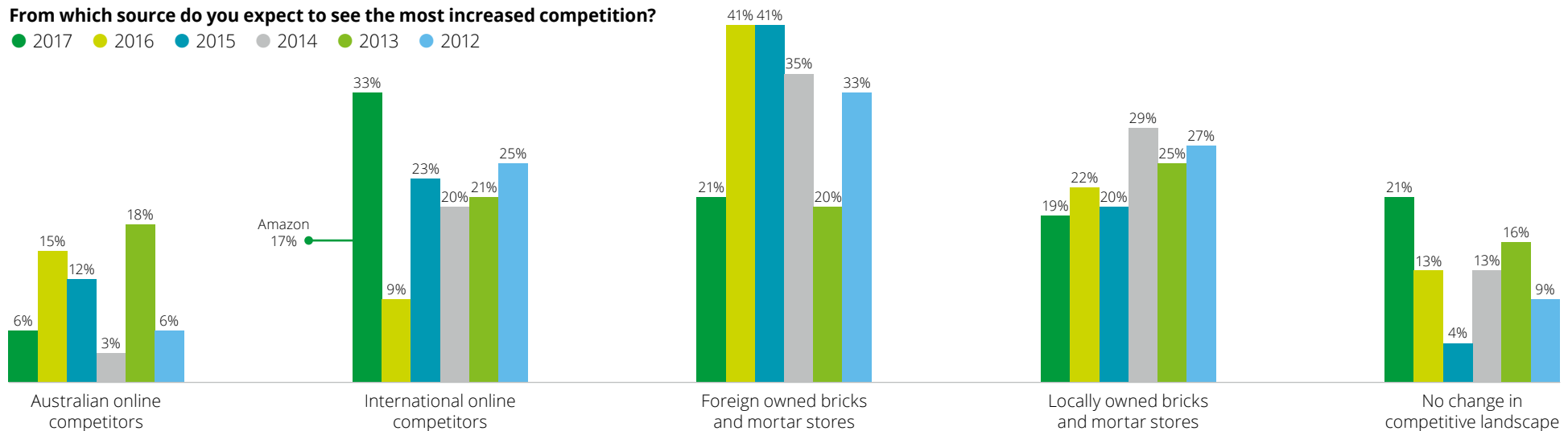
Illustrating that local retailers are starting to get to grips with the influx of foreign retailers, only 21% of respondents highlighted foreign owned bricks-and-mortar stores as the most significant source of competition.

This is down from 41% in the previous two years. And as more global retailers enter the Australian market, it's not just local retailers these new entrants are competing with.

Australia is fast becoming more and more competitive, and this is also putting pressure on these new entrants. With a number of foreign brands failing to make a significant impact on the local market, pressure on margins and some even shutting shop, Australian retailers are starting to fight back.

From which source do you expect to see the most increased competition?

● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



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“Buying the right quantity of products is going to be critical to ensure they balance the needs of customers whilst not having stock problems to have to deal with costly markdowns.

Although Amazon can't compete with retailers that stock their own brand, Amazon will generally take money away from other retailers as a whole whether a direct competitor or not.”

– *Survey respondent*



Resolving the issue

Managing financial distress in retail

2017 saw many retailers continue to experience the financial stress of staying competitive in today's challenging retail market. With pressures of increasing overhead costs, increased competition from local and global new entrants; increasing "sale" seasons added with the need to navigate through the digital age to improve innovative, not only with their operating model but to understand and engage with their customers to increase footfall – retailers today must stay focused on assessing profitability as well as be agile enough to adjust their operations in a timely manner to mitigate losses.

Despite the ever increasing advancement of technology and limitless data, the common issues we see impacting retailers in today's challenging environment include:

Effective data analysis

Retailers are data rich, however we often see various groups spending a disproportionate time collating and analysing volumes of data, with many duplication of analysis. The key is to quickly translate available data to draw key insights in respect to trends and performance, which will enable timely operational decisions.

Today, there are numerous data visualisation tools that can assist in interpreting data to provide instant key insights enabling operational agility.

The ability to instantly view gross margin trend by location, category and product better assists the retailer become more agile in adjusting their strategy, including setting the appropriate KPIs with the appropriate rewards that will drive the right cultural behaviours.

Effective inventory management

Increasing "sale" seasons has seen the need for retailers to be smarter with their inventory management (movement) and discounting strategies. Having instant insights into what product moves best in what location, while maximising gross margin, enables strategic inventory management and drive sales volumes in the right location which will positively impact working capital. There also various innovative solutions to moving old inventory effectively, and these can be highly valuable to unlock (and improve) working capital.

Maximising the operating model

We often see opportunities for retailers to optimise their operating model, however, there is often a lack of acknowledgment of underperformance and a lack of urgency to deal with the change required to exit the non-performing channels, before it starts to impact the profitable parts of the business.

We often assist retailers quantify the true cost of doing business and identify the strategic exit options which will provide the cash to invest in the areas that will maximise profitability.

The strategies for bricks-and-mortar, factory outlets, concession stores and online must make sense and not cannibalise the profitable footprint.

Similarly, the strategy for a franchisor versus franchisee can often contradict in priorities. Product development, supplier contracts, control of online platform, marketing, brand and pricing strategies must be beneficial for the group to increase brand and product awareness. All too often we see misalignment in franchise models.



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Resolving the issue

Managing financial distress in retail

Having the right baseline to assess performance

Lastly, setting the right baseline to assess performance is critical in ensuring the correct results (and behaviour) are rewarded. For example, many retailers are also importers, and making sure that the forex conversion (whether it be budgeted, actual or hedged rates) is reported correctly to avoid management misdirection on pricing strategies and performance.

Further, with online retailers increasingly competing on “free returns”, the cost of returns must be included in channel to market reporting to ensure that profitability is not skewed.

When formal insolvency is appropriate

Whilst we have assisted many retailers with planning and executing their restructuring or planned exit strategies, for retailers with a large physical footprint who find themselves unable to fund ongoing operations, let alone fund a planned exit strategy of their underperforming stores, the formal insolvency regime can assist.

The voluntary administration process, used correctly, can ensure the survival of a retail business by providing an effective mechanism to restructure a retail business or the sale of the profitable core of the business.



Vaughan Strawbridge

Partner
Financial Advisory



Ingrid Oey

Director
Financial Advisory





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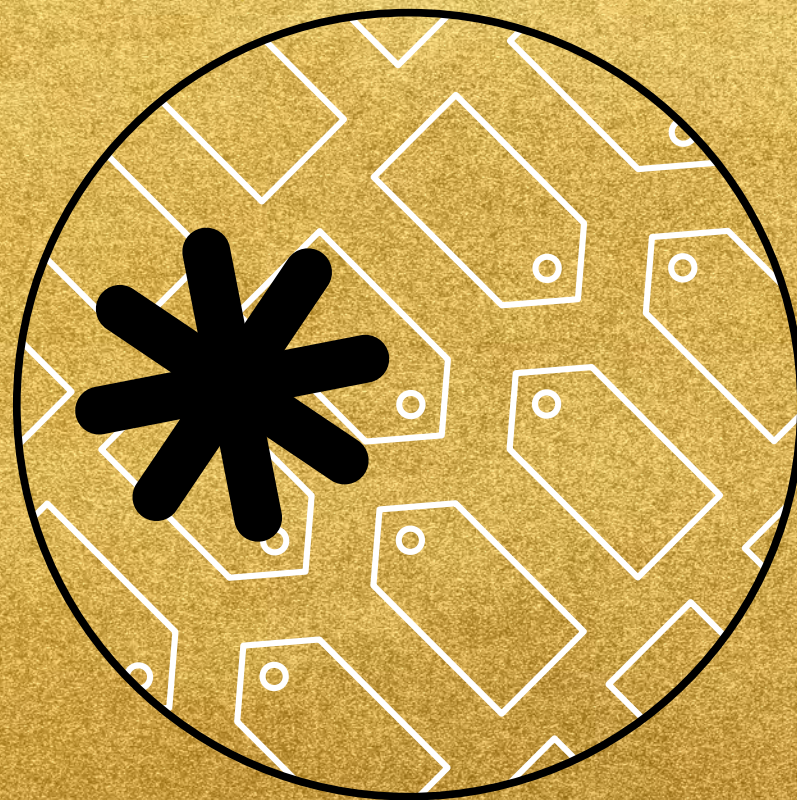
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Next 12 months

Next 12 months

Master your own destiny

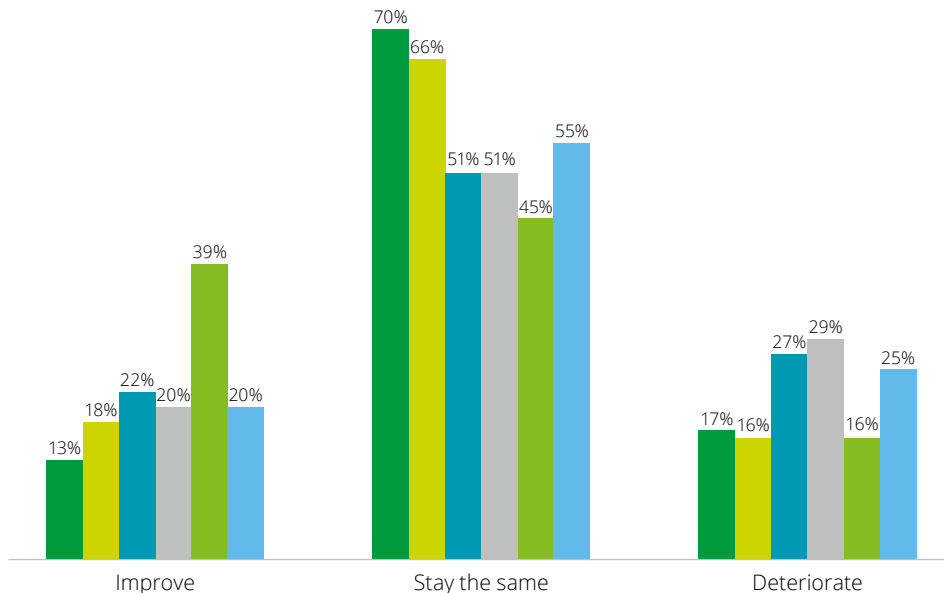
Whilst retailers are expecting modest growth in their own businesses, there is less confidence in the overall economy than we saw last year. The Australian economy is delicately poised with housing growth moderating, interest rates remaining at historic lows and wage growth stagnant.

The sector hopes to avoid an economic downturn which would spoil the party in 2018. Retailers in 2018 will need to make their own destiny; the challenge will be achieving growth in a flat market without the tailwinds of buoyant consumer confidence, a rising housing market and wage growth to provide a boost.

The process for some may be painful, and we expect to see further consolidation throughout the year, but for those retailers that get the model right there is a big prize in store.

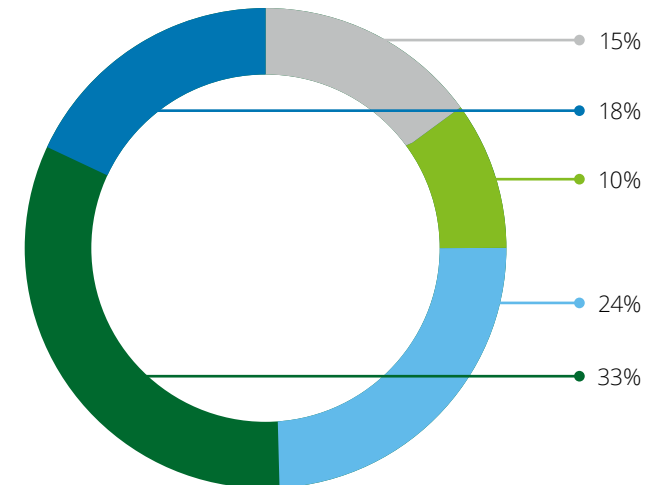
How will the broader economy perform in the next 12 months?

● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



What do you expect to be the overall earnings growth in your business in the next 12 months?

● 10%+ decline
 ● 5-10% decline
 ● 0-5% decline
 ● No change
 ● 0-5% growth
 ● 5-10% growth
 ● 10%+ growth



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“Retail food appears to be weakening with a lot of competition. Discretionary spend is under pressure. The market will be tight with marginal businesses facing closure. Energy costs remain a significant threat.”

– Survey respondent



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Next 12 months

Master your own destiny

True to form, retailers expect that new stores will again be the driving force behind sales growth in the next 12 months.

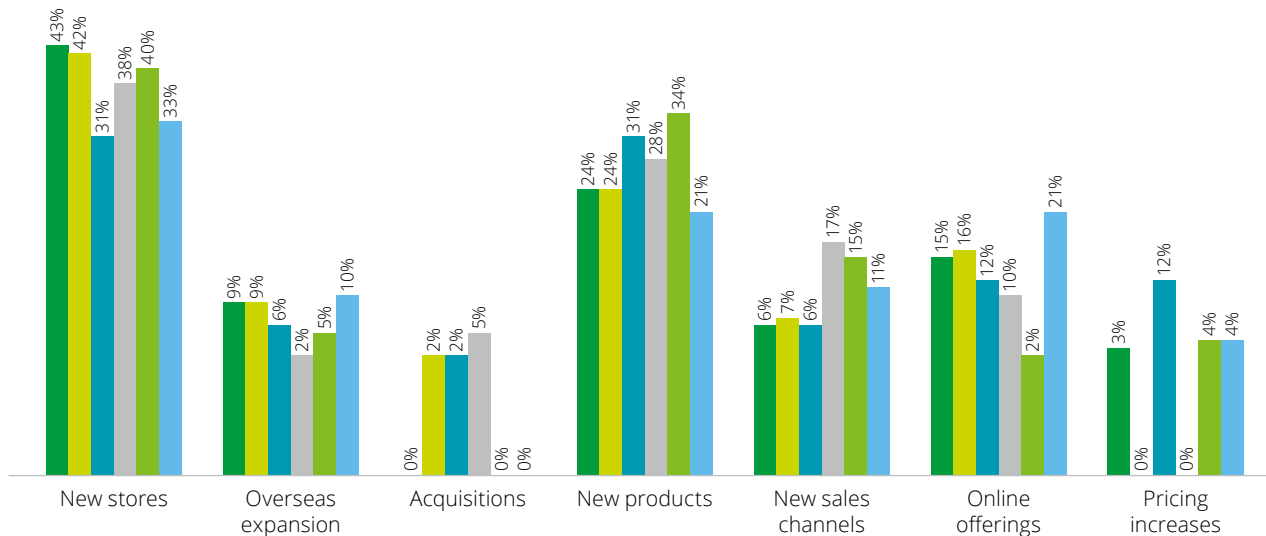
But with many retailers experiencing flat comparable store sales, new store growth may be at ever diminishing returns on investment. We've seen in markets such as the US and UK the impact of retailers investing too heavily in bricks-and-mortar, and Australian retailers need to take heed. Whilst Australia isn't at the same saturation levels as these markets, we need to learn from their mistakes.

Reinvention and re-purposing of stores which work harmoniously with the growing online sales channels perhaps offer a better long term strategy than simply growing the size of the store network.

Consistent with our expectations of price inflation in 2018, few retailers are expecting price increases to drive sales growth. The recent increase in the Australian dollar will flow through into price deflation if levels remain elevated, requiring volume growth and new stores to drive sales.

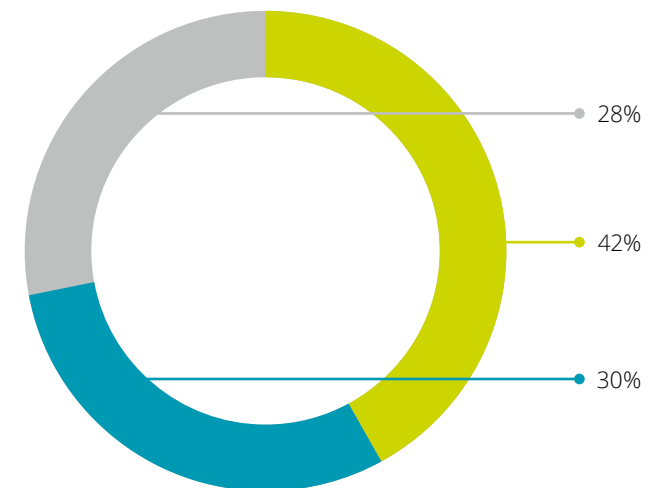
What do you expect will be the most significant driver of sales growth in your business in the next 12 months?

● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



Do you expect to increase net stores/outlets in the next 12 months?

● Increase ● Decrease ● No change/NA



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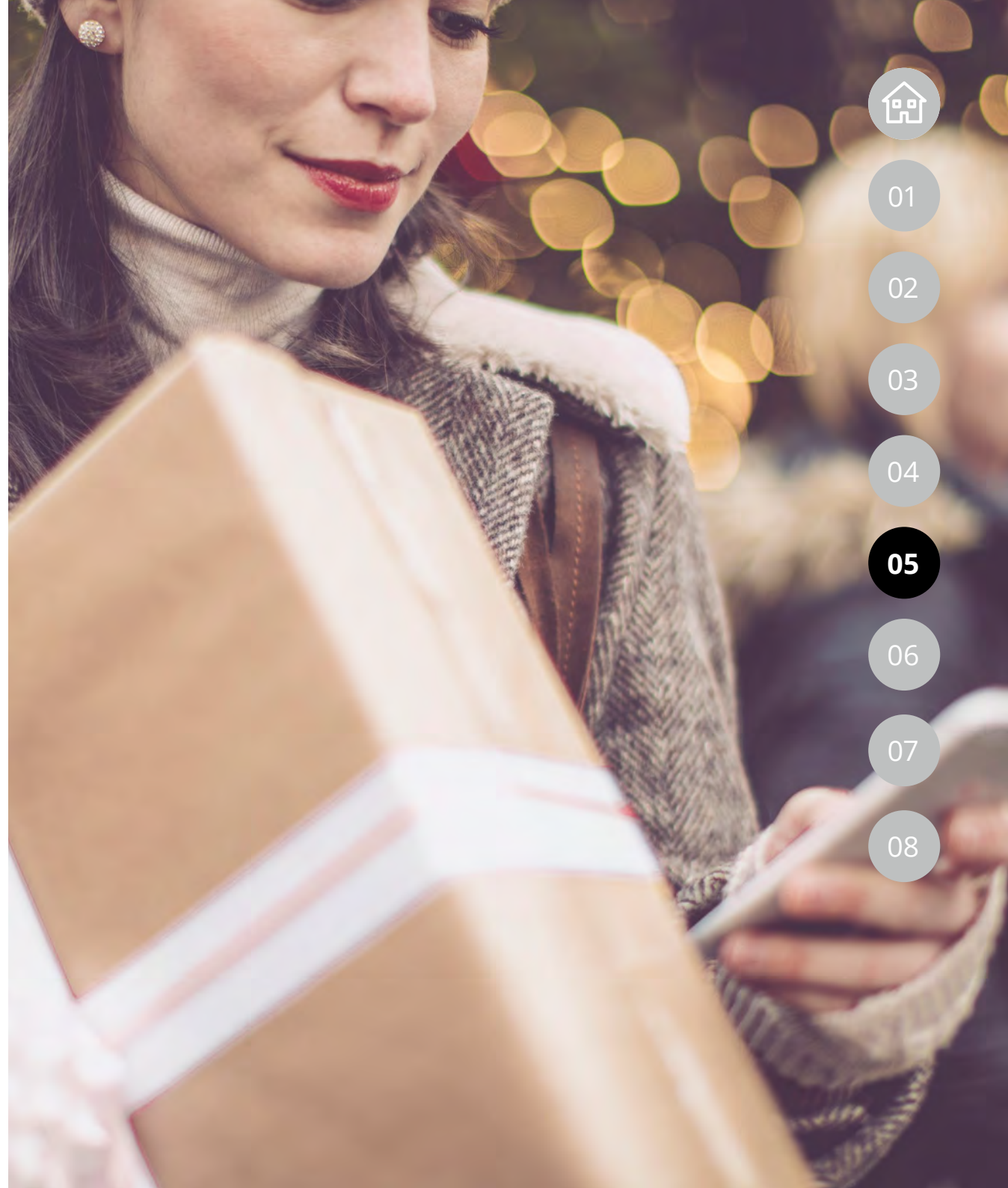
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“Physical retail store formats will not disappear. However, they may need to adapt and transform in order to realise profitable growth in a highly competitive blended environment where digital has the potential to not only influence but also capture market share.

For many retailers too, maintaining a dual in-store and online presence will remain important.”

– *Survey respondent*



Next 12 months

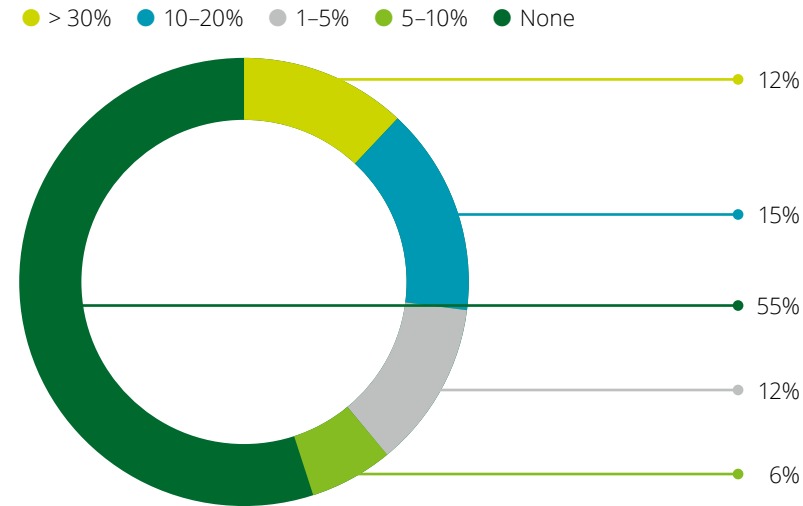
Master your own destiny

Overseas expansion has tended not to be a major focus of local retailers over the past few years, and again this year 58% of retailers do not consider a foray overseas as an opportunity in 2018.

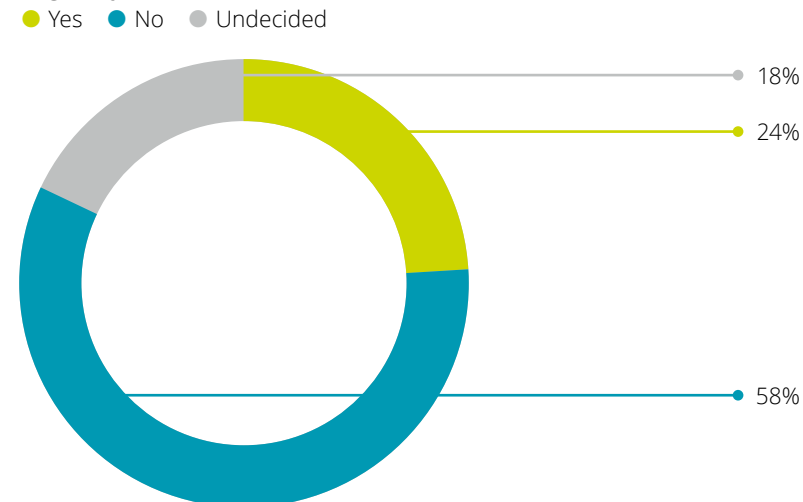
Retailers are facing a battle on the home front and have chosen to prioritise this first rather than risk losing focus by going into new markets.

It is important though not to forget the longer term opportunities that establishing a beachhead overseas can provide. The Australian market is competitive and becoming more saturated. Local brands will need to look offshore at some point in order to continue growing and building global brand recognition.

What percentage of your sales are generated from operations overseas?



Do you see expanding your operations overseas as an opportunity to grow your business in the next 12 months?



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Tax transparency

Not black and white

You may think it is a reasonable assumption that the focus on multinationals and their tax affairs is not something that impacts the retail industry. It is easy to dismiss this issue as just something relevant for technology and pharmaceutical companies. The reality is that tax transparency is here to stay, and businesses in *all industries* will face increasing pressure to be more transparent about their tax affairs. Retailers are firmly included in this group as their relationship and direct connection with the public creates increased public interest in their tax affairs.

A number of factors have contributed to the current state including an environment where public perception, at times fuelled by the media, is that large companies are shifting their profits out of Australia to lower tax jurisdictions – especially where these companies are selling to Australian customers and are perceived not to be making sufficient profits and consequently paying enough tax in Australia.

The Australian government, through the ATO, is also driving the focus on transparency and how much tax is paid in Australia by large multinationals. The ATO has just published their Tax and Corporate Australia report, and for the first time have formally estimated the large businesses corporate tax gap at \$2.5 billion. This “gap” represents the difference between the ATO and taxpayers’ interpretations of “grey areas” of the tax law such as transfer pricing and the borderline between acceptable tax planning and tax avoidance. The ATO is focused on reducing this gap and the ATO has indicated that key areas of activity will focus on, amongst other things, international profit shifting, related party debt, offshore service hubs, inbound supply chains, group structuring and business events.

We have seen many multinational retailers singled out in the press about their tax affairs. We have also seen early adoption of the Voluntary Tax Transparency Code by retailers such as Wesfarmers and Woolworths and more recently, Aldi. New entrants to the Australian market, especially foreign owned multinational groups can expect increased media scrutiny and a wider public focus on their activities in Australia including their tax affairs.

Against this background, many new retailers entering the Australia market may wish to consider whether they should sign up to the Voluntary Tax Transparency Code or otherwise provide greater transparency to the public about their tax affairs. No doubt there will be calls for them to do so. Transparency and the tax contribution that a business makes is a real issue that businesses, including retailers, will need to consider at some point in time.

Some elements of tax transparency will not be able to be controlled by a business, for example the ATO reporting of tax paid data, and other elements, such as disclosure in financial statements will only provide a snapshot of information to the public. The Voluntary Tax Transparency Code referred to above provides a framework for businesses to publicly disclose more information about their tax affairs at a greater level of detail than that already published by the ATO or what is otherwise publicly available. The Code represents an opportunity for retailers to proactively present the facts associated with the tax contribution their business makes.



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Tax transparency

Not black and white

This represents a significant shift in transparency especially for those companies that are not listed on the ASX or are not otherwise required to submit accounts to ASIC. However, at the time of writing only 113 corporations have signed up to the Voluntary Tax Transparency Code and out of these 113 corporations only a handful are retailers. The low uptake of the Code has resulted in calls for the Code to become compulsory.

The crucial challenge for businesses will be to ensure that any tax information is correctly presented and that it can easily be understood by the public in the context of one of the world's most complex tax systems. This means that regardless of whether the decision is made to formally sign up to the Code or otherwise provide additional information to the public there are a number of considerations relevant in deciding whether to provide greater tax disclosure. These factors include cost considerations, resource requirements to collate and interpret the data, the appropriate level of additional disclosure and information accuracy. A sound and effective tax risk control framework should contribute toward increased accuracy and relevance of data produced.

Whilst it might appear that providing these increased levels of disclosure is burdensome especially to new entrants who are focused on establishing themselves in a new market, the opportunity for the retail industry is to show the public the contribution made to the Australian economy. The contribution is broader than simply the income tax paid, it includes the payment of payroll tax and collection of PAYG for the numerous people employed in this industry as well as the collection and remittance of Goods and Services Tax. This is a valuable contribution to the Australian economy which should be articulated as part of the wider contribution that retailers make.



Kamlee Coorey
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Corporate Tax



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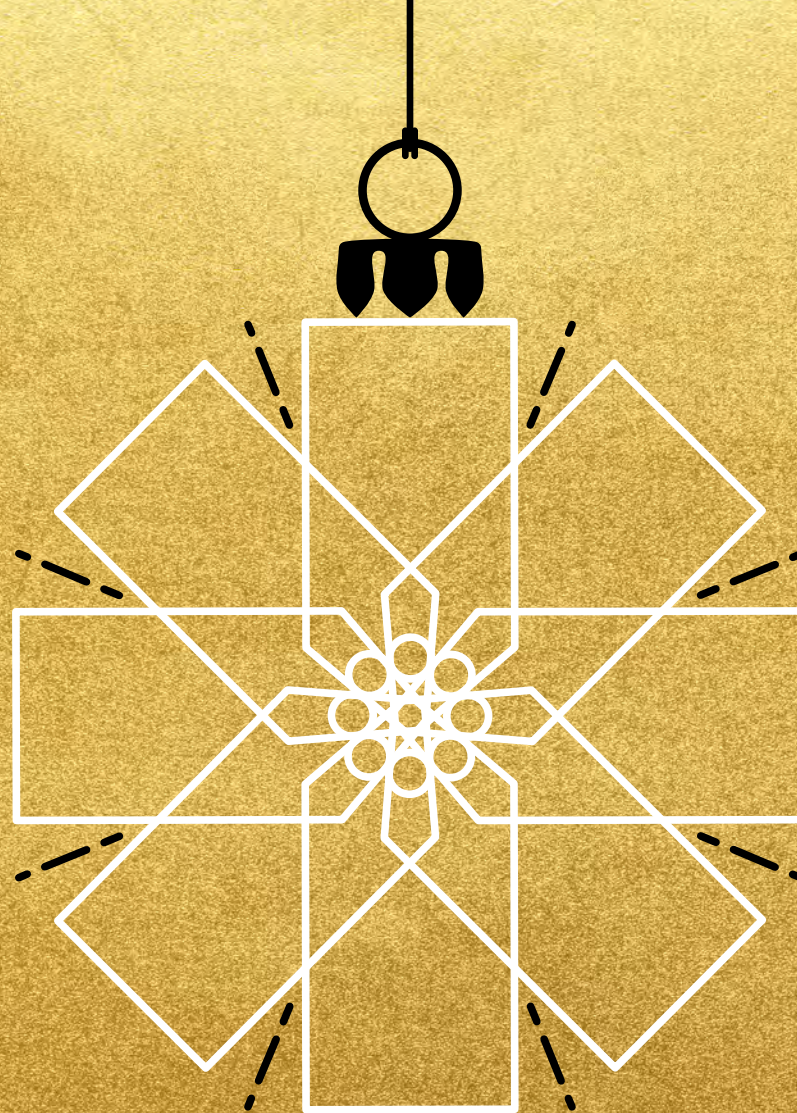
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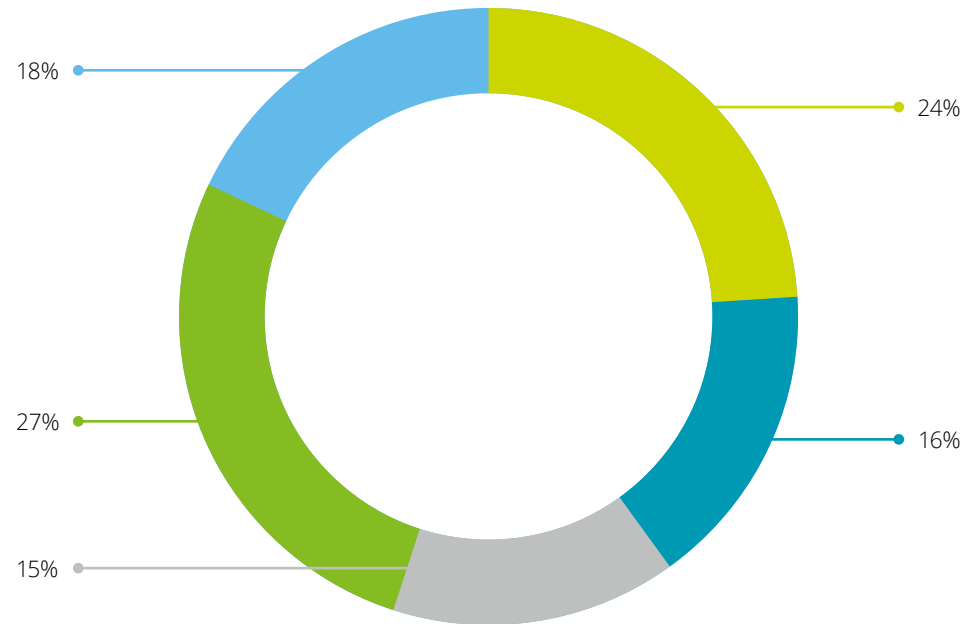
About the survey

About the survey

The Deloitte Retailers' Christmas Survey is based on a survey of 52 senior executives of leading retailers in the Australian market. The respondents are executive and senior management from a cross section of retailers inclusive of listed, private and foreign owned businesses.

Ownership structure of respondents

- Australian owner-managed
- Australian private/other
- Australian listed
- Foreign private
- Foreign listed



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About the survey

The selection of participants is intended to provide a representative sample of large and small businesses, with most participants made up of the sub-1,000 employee segment.

The geographic reach of participants is evenly distributed between Australia, New Zealand and global retailers.

Number of employees

- 1-500
- 501-1000
- 1001-5000
- 5001-10000



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Retail, wholesale and distribution group

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Operationally, we can help you better manage your supply chain, improve processes and implement new technology – delivering practical solutions that rapidly build your efficiency and productivity.

Our services for retailers, wholesalers and distributors include:

- Mergers and acquisitions
- Restructurings and turnarounds
- Growth and channel strategy
- Trade promotion management and control
- Customer relationship management
- Supply chain planning and optimisation
- Store operations and locations
- Logistics and warehousing management
- Store redesign and strategy
- Integrated cost reduction
- Sourcing and procurement
- Corporate performance management
- Security and fraud protection
- Information technology integration
- ERP and software implementation
- Tax structuring and advice
- Financial process improvements and advice
- Accounting advisory
- Outsourcing advisory



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Deloitte specialists in the retail sector

If you would like further information about any of the topics in this report, or our advisory capability to the retail industry, please contact us.



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