



Retailers' Christmas Survey 2018

Spending your way through Christmas

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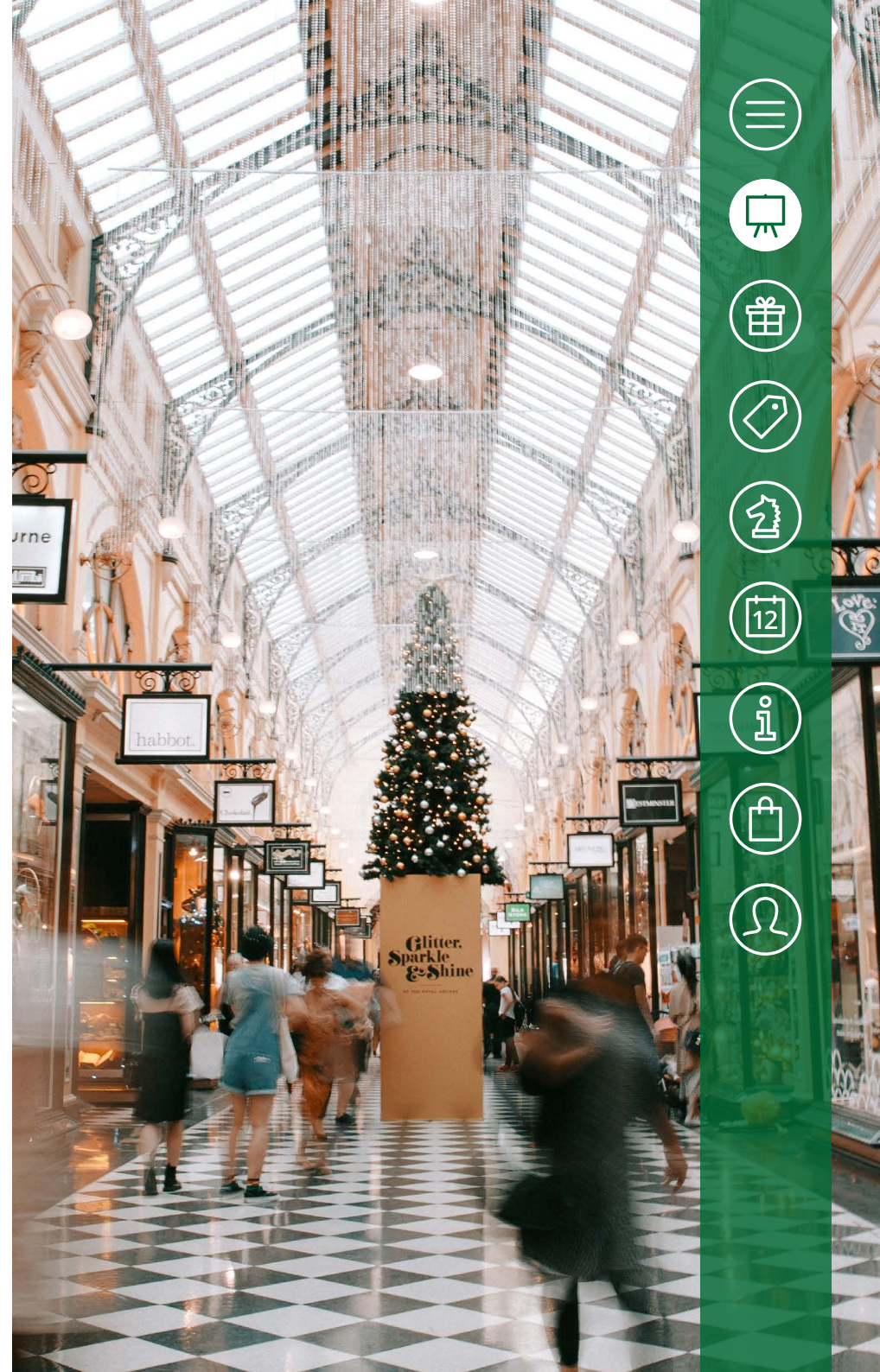
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Introduction

Executive summary

Welcome to the seventh 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 2018 Christmas period and beyond. The report analyses retailers' sentiment for the Christmas period, key trends and their expectations and priorities for 2019.



Spending your way through Christmas

As we head into the silly season, retailers have many reasons to feel optimistic. Despite a number of competitive and economic pressures, the overall retail market has performed relatively well in 2018.

While there are some dark clouds lurking on the horizon in terms of the broader economy, retailers appear to be carrying forward this optimism into the Christmas trading period, with our survey respondents expecting to increase both their sales and profit margins compared to last year. Some 80% expect to see higher sales this Christmas, compared to last year, with 41% predicting growth of 5% or more. They are slightly less bullish, but still confident, when it comes to margins, with 56% expecting some form of increase this year.

To achieve these outcomes, retailers are pinning their Christmas hopes on two key areas: a strong product mix; and an uptick in online sales through investments made in omni-channel business models.

Discounting will remain an important strategy over Christmas, with 62% of retailers already planning to discount while a further 21% are undecided.

Retailers are also looking to hold strong on pricing this side of Christmas, with most planning to discount only after 25 December. This strategy is highly dependent on customers being enticed by great products and customer service, be it in store or online, that is personalised and convenient.

However, with customers choosing to shop later and later each Christmas, aided by improvements in online offerings as well as faster and more reliable delivery services, retailers look set for a nervous first trading week in December.

Online: the new(ish) battleground

In 2017, we saw a significant increase in retailers strategically investing in their digital capabilities. In 2018, it appears that they are banking on reaping the rewards of these investments, with online set to be a key battlefield this Christmas.

Our survey shows that 79% of retailers are expecting to experience growth of 10% or more in online Christmas sales. With retailers highly focused on their e-commerce platforms, could we finally be seeing the true acceleration of online retail that other developed countries have experienced?

While retailers continue to tell us that customer experience is a key priority, this seemingly hasn't translated into any material new investments. In keeping with previous years, just 14% see customer service as the key to winning the hearts and minds of consumers this Christmas. Given that around 90% of sales are still made through bricks and mortar stores, let's hope retailers haven't forgotten the importance of great customer service this Christmas.

Can Amazon shake-up Christmas?

Amazon's operations in Australia started trading a few months before Christmas last year. Not surprisingly, their impact over that period was minimal. With a further 12 months of trading under its belt, can Amazon bring further disruption to the retail market this Christmas? Time will tell, but it would seem Australian retailers aren't too fazed at all, with 83% predicting Amazon will have no impact on their Christmas trading performance. While retailers don't expect to have their Christmas spoiled by Amazon, the real question is whether Australian consumers agree.



Shifting business models

Much of the growth for Australian retailers has historically come from expanding their bricks and mortar presence, and mainly in Australia and New Zealand. We continue to see a shift in strategic thinking, with customer and omni-channel being the key strategic priorities for two thirds of our survey respondents. The role of the store is moving away from just being a transactional space to an opportunity to build brand through an experience and service that can often only be achieved face-to-face with the customer. To this end, consumers can expect to enjoy innovative store designs and concepts this Christmas, as retailers experiment with new ways to build brand and connect with their customers.

'Responsible retailing' is becoming a key strategic focus for many retailers, and rightly so. Customers are voting with their wallets, demanding products from companies that align to their own cultural values and beliefs. Social and ethical awareness and responsibility about how products are sourced and made, as well as the impact they have on the environment and society more broadly, is becoming critical to driving customer loyalty in a customer-led market. But less than half (42%) of survey respondents believe that social, ethical and environmental responsibility is very important/critical to the perception of their brand.

Unless retailer attitudes to responsible retailing change, they risk being left behind in a world in which consumers increasingly care about the impact their actions are having on the people and the world we live in.

Outlook

Despite some warning signs for the broader economy such as falling house prices, rising energy costs and a weakening dollar, retailers remain bullish about their prospects for next year. More than 90% of survey respondents expect to see positive sales growth in 2019, with nearly a third predicting sales growth in excess of 10%.

The key growth driver appears to be online offerings – jumping from 15% to 28% – as the number one strategic priority for retailers. This marks a significant shift away from previous years, when retailers consistently said their key growth priority was centred around new store openings. Indeed, in 2017, nearly half of all respondents were primarily focused on growth through new store openings. This shift reflects both the increasing saturation of the Australian market as well as the bigger investments retailers have made in developing their omni-channel strategies. The role of the store will continue to be a critical part of retailer strategies, but it seems they are confident their investment in digital will provide the impetus needed to drive their growth aspirations in 2019.

We are entering one of the most uncertain trading periods in the history of Australian retail. The arrival of Amazon has set the cat amongst the pigeons, bringing scale and capabilities that have the potential to strike in those areas in which Australian retailers are most vulnerable.

Opinions remain divided on the size and timing of Amazon's impact, but this Christmas will give us a better idea of just how much progress they have made. And with Australian retailers more confident than ever entering the Christmas trading period, the scene is set for another fascinating year across the Australian retail landscape.



David White

National Leader

Retail, wholesale & distribution group



Christmas expectations



Confidence reigns this Christmas

Australian retailers have traded relatively well over the past 12 months, despite a number of market challenges such as rising energy costs and a slow-down in the housing market.

Perhaps buoyed by this, they are expecting a bumper Christmas, with some 80% expecting an increase in sales and a whopping 41% expecting sales to increase by at least 5%.

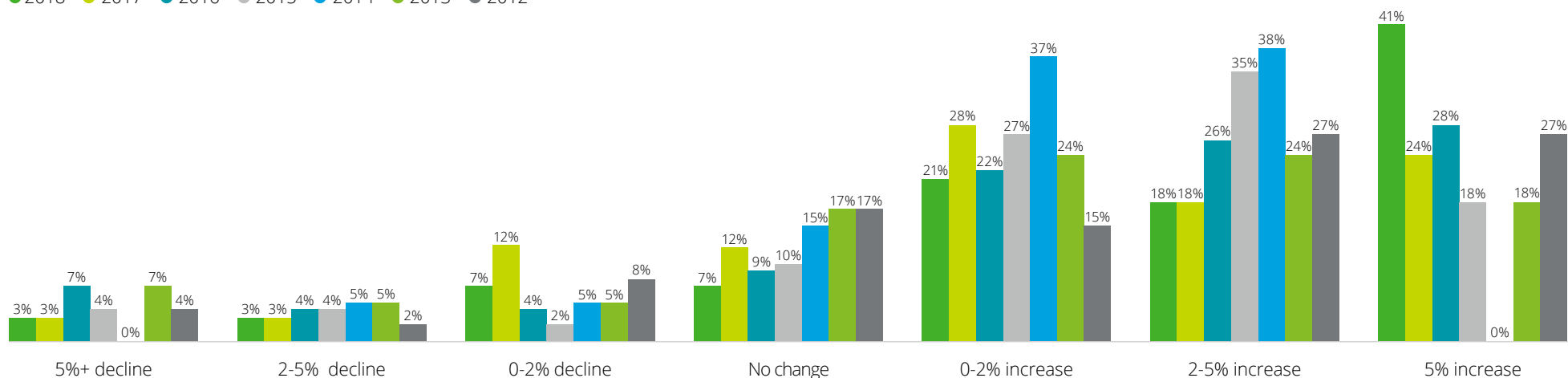
The key driver of this growth is through online, with nearly 80% anticipating their online sales this Christmas will grow by 10% or more.

“As customers look for that in-store specialised experience they cannot get through online shopping, a focus on increased staffing and training will help towards retaining and attracting customers.”

– Survey respondent

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

● 2018 ● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



This level of confidence doesn't end there. Last year was Amazon's first Australian Christmas trading period, but it barely made a blip on the market. With a further 12 months under its belt, we can expect Amazon to have a bigger impact on the Australian consumer this Christmas.

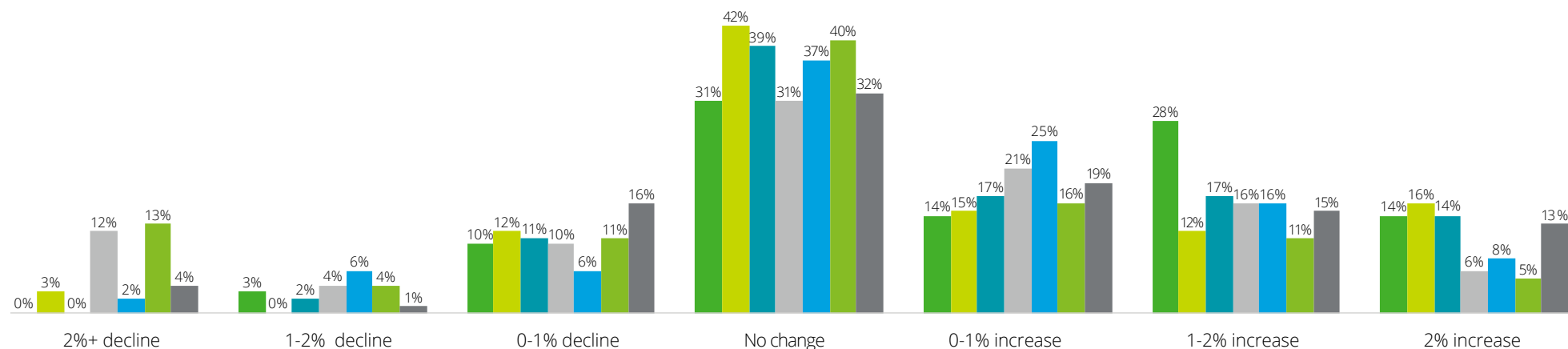
However, it appears Australian retailers don't seem to be concerned at all, with 83% predicting Amazon will have zero impact on their Christmas trading. So are Australian retailers running the risk of complacency when it comes to Amazon? All eyes will be on their trading performance this Christmas.

“Those retailers that create a new level of product and service personalisation and in-store theatre are on track to be ahead of the game.”

– Survey respondent

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

● 2018 ● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



The increasingly competitive nature of the Australian retail market has seen discounting become an addictive “drug” for many retailers that, once hooked, are seemingly unable to kick. In 2012, the first year of this survey, nearly a third of respondents told us they would not be discounting at Christmas. Fast-forward six years, and the number has nearly halved to just 17%. Increasing competition, particularly from international entrants, has made any form of price increase incredibly difficult to pass through to the consumer.

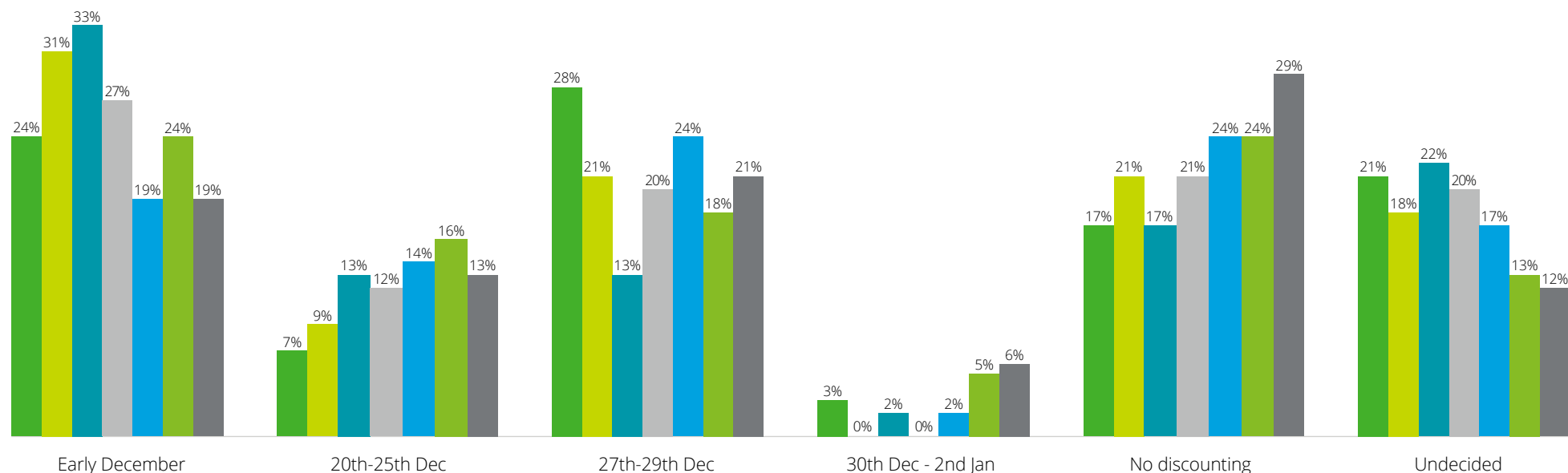
However, many retailers have managed to avoid this race to the bottom by identifying high-demand products delivered through great customer service. Around a quarter of retailers expect to discount in early December, which is slightly down on last year, while a third are looking to delay any discounting until after Christmas Day. As ever, these tactics will need to be flexible and responsive to the strength of trading across December.

“Retailers that focus on customer experience and differentiate themselves in the market will continue to be successful.”

- Survey respondent

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

● 2018 ● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



Macroeconomic outlook: a 'credit-card' Christmas

Retailers are likely to experience a slower Christmas period after a strong period through the middle of 2018.

The wage growth challenge

Subdued wage growth and rising prices for petrol, electricity and some non-discretionary services are putting household budgets under pressure. Despite these difficult financial conditions, retail spending improved in 2017-18 as consumers dipped into their savings to support spending activity.

But this can't last forever, and a further pick up in retail spending is dependent on stronger wage growth.

Since the start of 2018 to September, 175,000 jobs have been created, with the majority of roles in full-time positions. This follows the 400,000 jobs created in 2017, indicating business continues to feel confident enough about conditions to add to their permanent staffing levels.

Strong job growth is resulting in a tighter labour market, but some spare capacity still remains, which is limiting wage growth. The underemployment rate, which measures the number of employed people wanting to work more hours as a percentage of the total labour force, remains elevated, compared to historic levels. It was 8.1% in August 2018, and has been

trending lower from the record high 8.9% reached in February 2017, driven in part by the strength of full-time employment growth over this period.

Spending squeeze v spending growth

In addition to subdued wage growth, households are experiencing a rise in the cost of living expenses. This is especially the case for non-discretionary goods and services such as electricity, education, health, and housing.

This squeeze is putting pressure on households to access savings to support spending activity. Real disposable income rose just 0.3% in the June quarter, pushing the household savings ratio down to a decade low 1%. But there's only so long households can continue to draw on savings to support spending activity, with the outlook for spending contingent on stronger income growth.

Wealth has traditionally been the strongest driver of spending, but this is changing. Australia's housing market is slowing after four years of very strong growth. House prices nationally had fallen 13 consecutive months in October 2018, now down 3.5% from a year ago. Sydney leads the pack here, following strong growth over the past couple of years.



Property prices will likely continue to either stagnate or in some markets decline, as credit conditions continue to tighten and additional supply comes onto the market.

The tightening is coming from two fronts; a focus on reducing risky lending practices and rising overseas lending costs for our banks. The financial services Royal Commission has focused attention on the lending sector, which was already facing tighter controls from the Australian Prudential Regulation Authority as it clamps down on investor lending and interest only loans.

Although the Reserve Bank of Australia will keep its official cash rate low, other central banks around the world, including in the US and UK, are raising interest rates. With investors chasing yields, this means it's becoming harder for Australian banks to find funding.

Total nominal retail spending growth came to 2.6% in 2017-18, driven by a strong June quarter of spending. Following the strong growth in the first half of 2018, spending growth is expected to moderate heading into the Christmas period.

The spending outlook across the sectors is varied as wealth effects fade and employment outcomes continue to improve. Department stores are losing out to online competitors and household goods retailers face weaker demand as the property sector slows. But stronger wage growth will provide much needed support to the sector as a whole, with supermarkets expected to benefit the most from deeper consumer pockets.

The outlook

Retail business conditions remain highly competitive in the face of these economic challenges, but in spite of this, many retailers started 2018 on a strong footing. Retail gross operating profits picked up in the opening half of the year, with June quarter profits 15.2% higher than a year ago. Cash flow, however, is a pressure point, as increased competition and weak income growth keep a lid on the ability to raise prices going forward.

With buoyant retail conditions in 2018 supported by a rundown of household savings, this threatens to be a 'credit-card' Christmas. But more likely is consumers spooked into moderating their spending as asset (make that housing) prices decline.



David Rumbens

Partner

Deloitte Access Economics



Retail trends



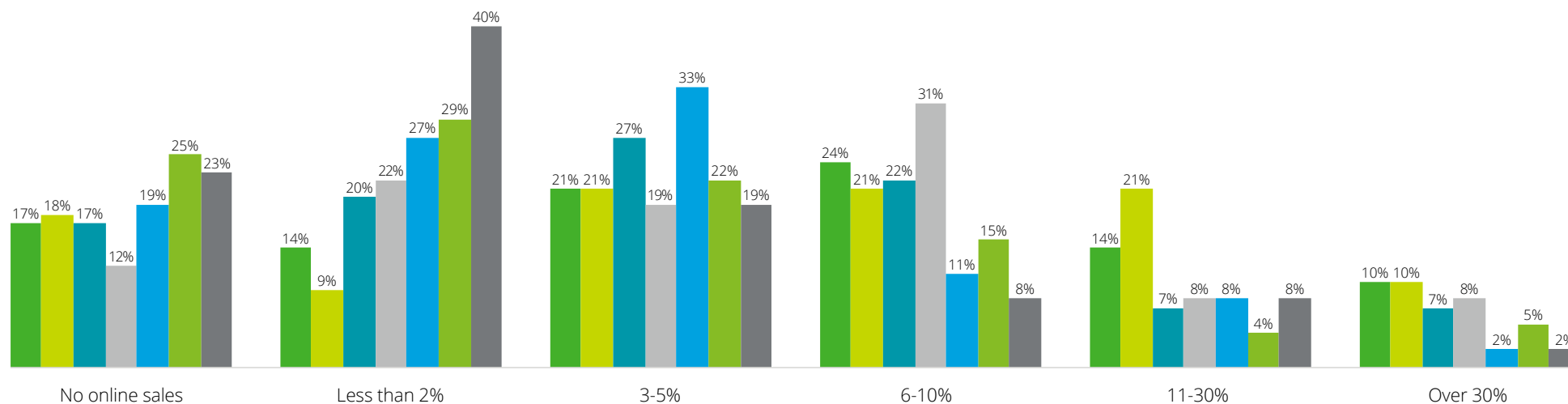
Turning the tide online

Australian retailers have made significant investments in their online business models, which are designed to both generate additional sales and complement and enhance existing services and channels.

Our survey shows that the growth in online sales will again be a significant contributing factor to retailer success this Christmas. Around half of all respondents are expecting to generate 6% or more of their sales from online this Christmas, with around a quarter anticipating online making up more than 10% of sales.

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

● 2018 ● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



Christmas has become a peak period for consumers to turn to online for gifts. Online offers speed and convenience, while consumers are more willing to browse and buy for family and friends using mobile, tablets and laptops compared to shopping for themselves.

Local retailers still expect to increase online sales over the Christmas period, with 79% expecting sales to increase by 10% or more compared to 2017. However, looking at total online sales, Australian retailers are still light-years behind many other mature markets.

Three quarters expect online sales to make up less than 10% of their total sales over Christmas. Compare this to the US, where consumers expect to spend a staggering 57% of their holiday retail budget via online this Christmas,¹ it's clear just how much potential the Australian market still has.

While Australia still has a long way to go to match the level of online sales in countries such as the US and UK in terms of sales volumes, we are undoubtedly seeing a local shift to similar business models – it's just taking more time.

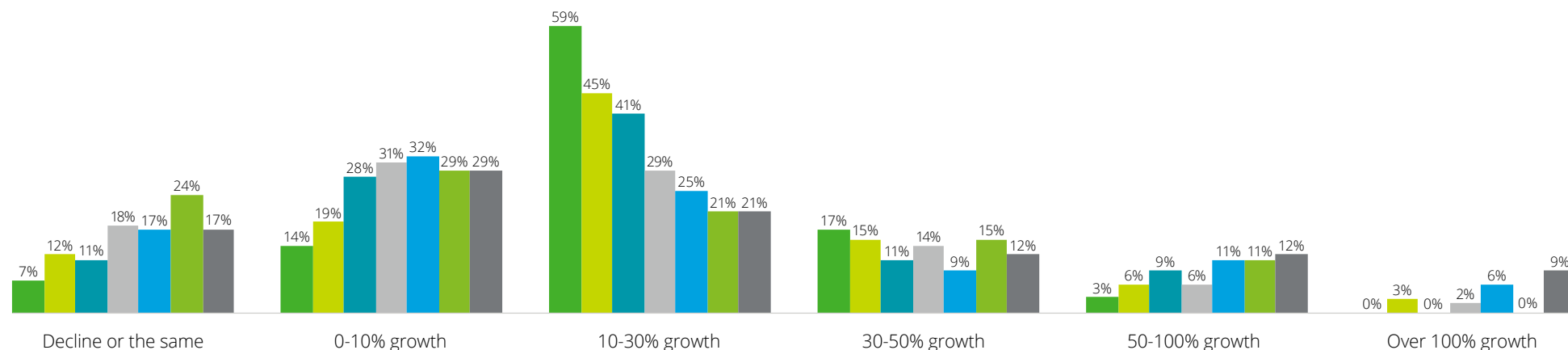
1. 2018 Deloitte holiday retail survey – Shopping cheer resounds this year

“The growth will continue to be in online retail and from the large overseas retail companies.”

– Survey respondent

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

● 2018 ● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



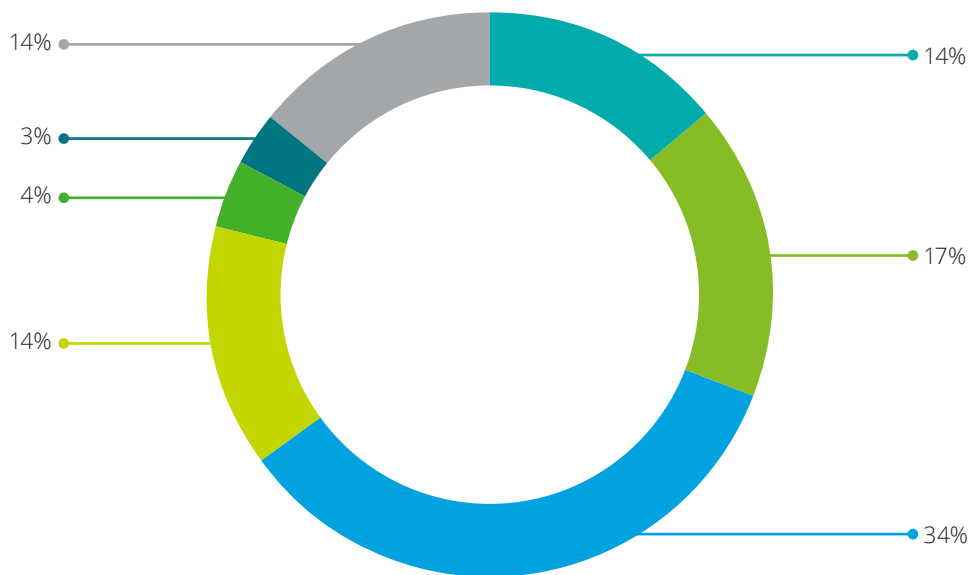
Standing out from the crowd

Given retailers' lofty expectations this Christmas, how do they expect to beat the competition? In last year's survey we saw a clear spike towards digital and omni-channel as the keys to winning share of wallet.

This year only 14% of retailers cited this as their most important focus area at Christmas compared to 27% in 2017. This would appear to reflect the confidence retailers have in their digital investments.

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

- Customer service
- Marketing
- New product range
- Digital & omni-channel
- Pricing
- Store format
- Other

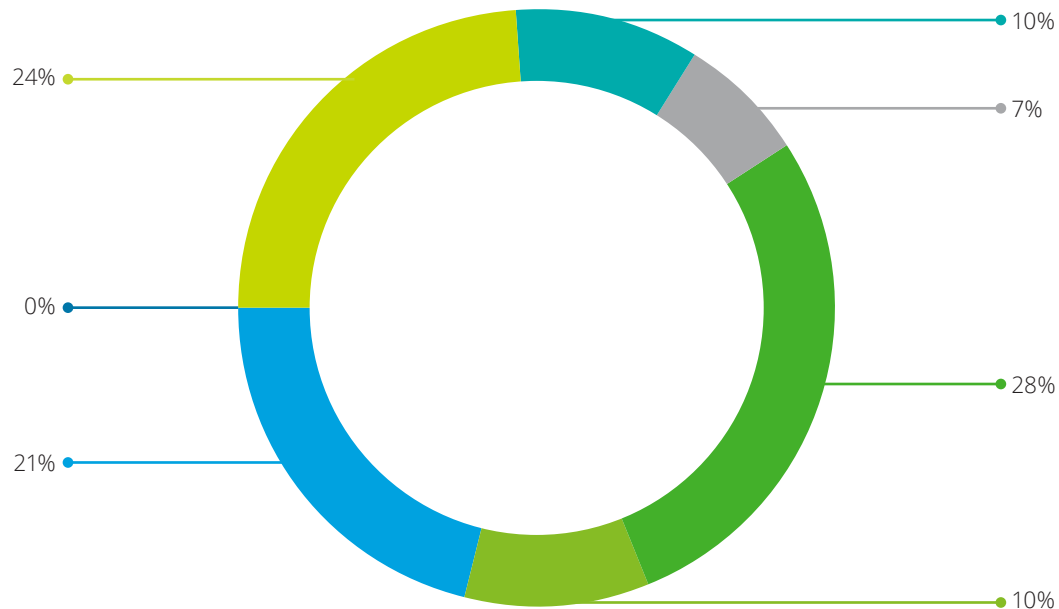


Indeed, some 55% believe their customers have a strong loyalty to their products and brands. Consequently, the majority believe their new product ranges are key to a successful Christmas trading period.

Critical to this strategy is a clear understanding of the customer, with an increasing number of retailers investing in improving their CRM systems. Those retailers with a deep understanding of their customer profile and spending patterns will enjoy most success this Christmas.

What was the most significant driver of growth in your business in the last 12 months?

- New stores
- Overseas expansion
- Acquisitions
- New products
- New sales channels
- Online offerings
- Pricing increases



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

- Average
- Good
- Strong



Engaging with the customer

In the face of increasing competition, retailers now more than ever need to be bold in investing in understanding their customer preferences, how they want to shop and when. Our survey suggests retailers are attune to this need, with 35% identifying customer engagement and experience as their number one strategic priority.

Running a close second is omni-channel at 31%, which aligns with retailers telling us they see building their sales outside their store networks as critical to their growth strategy. This is a welcome change from previous years, where as many as 40% of retailers were focused on cost control rather than seeking to grow the top line and better engage with their customers.

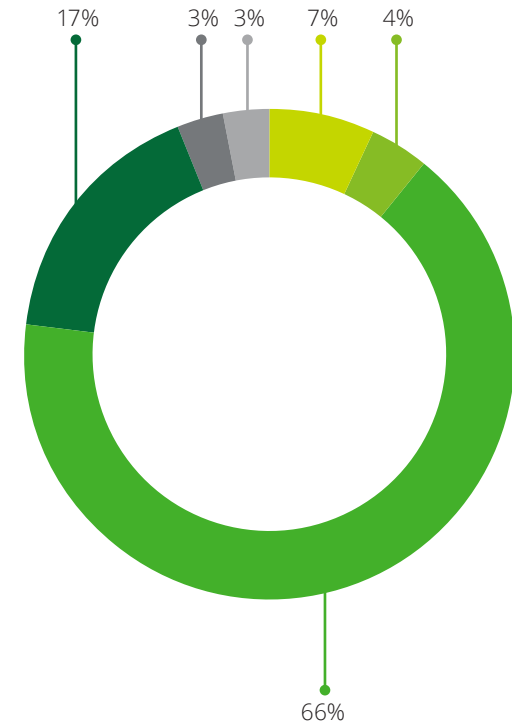
What is currently the number one strategic focus of your business?

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



Other than selling of product, what is the most important purpose of your physical store?

- Brand community engagement
- Cross-selling and up-selling other products
- In-store purchasing experience
- Knowledge/information/advice about products
- Not applicable
- Other



Embracing AI: giving customers more of what they want

Advances in Artificial Intelligence have made it possible to create personalised customer experiences – treating customers less like machines and more like people.

It seems you can't take much more than two steps these days without hearing someone, somewhere, mention AI. Artificial intelligence has, of course, been around the technology scene for a few years now, but seems to be enjoying a more recent application to the retail customer experience.

As more retailers and brands are putting the customer at the centre of everything they do, we're certainly starting to see more of them applying AI across their omni-channel user experiences (and making a serious impact as a result).

What AI means to retailers...

AI loosely encompasses three core, closely related, yet still distinctly different, technologies that can provide true customer personalisation:

- **Machine learning** – the evolution of analytics and forecasting algorithms into systems that predict and learn things in ways that closely simulate human learning

- **Natural language processing** – turning unstructured free-form text into structured, categorised information

- **Image and voice processing** – turning completely unstructured image/photographic or audio voice information into structured, categorised information.

It's possible to use any of these technologies, individually or in combination, in ways that can allow retailers to provide rich omni-channel experiences for their customers across one or more engagement channels, and not necessarily just online.

... and why it's important

Retailers equipped with AI tools can significantly improve their customers' experience, and ultimately translate this into increased revenue. AI can deliver true customer personalisation in the shopping experience, particularly when it comes to data-driven recommendations or search results and sales.



Global commerce platforms such as Salesforce Commerce Cloud have been leading this wave in embedding advances in AI technology into their core platform. In one recent instance, Salesforce, which is able to index the revenue uplift of specific customer experience features across all different brands on its single platform globally, reported statistics specifically related to AI-driven recommendations.

The numbers? Shoppers who clicked on AI-driven recommendations accounted for only 7% of visits across their whole platform, but 24% of completed orders. AI is positively impacting the end outcome of the customer experience – order completion – compared to the consumption of recommendations from a site visit perspective.

Practical uses of AI in retail

Artificial Intelligence is most commonly applied as machine learning-based predictions in recommendation scenarios like cross-sell/up-sell in an online store, optimally ordered product lists or integrated customer-aware recommendations in direct marketing.

Some commerce platforms have gone as far as incorporating AI into their site search. Whether it's machine-suggested predictive search results or presenting a distinctly personalised search result to each individual customer that searches for something, even when they search with the exact same search phrase.

Natural language processing is another AI technology that has seen increasing use in recent years in the customer service space, and most powerful when employed in communications tools like live chat and messaging service agents. Companies can employ a hybrid environment of service bots and real life agents to service their customers in a personalised yet cost-efficient manner.

Advances in natural language technology have made it difficult to tell when AI is handling a service request, especially when that AI is deployed in a hybrid environment that can offload to a live person when the query gets too complicated for the AI.

A more recent customer experience driven innovation in the commerce landscape is the use of voice search and visual search to drive engagement and conversion.

The internet is awash with demonstration videos of people taking photos of everyday items (fashion, for example) on their mobile devices and then using AI driven image search on pioneering retailer sites to find and order the exact same item in no time at all.

Certainly a case of contextually driven retail at its best.

Giving customers more of what they want

Retailers can employ the customer personalisation power of rapidly evolving AI technologies in ways that are already seen to be having a measurable positive impact on omni-channel revenue.

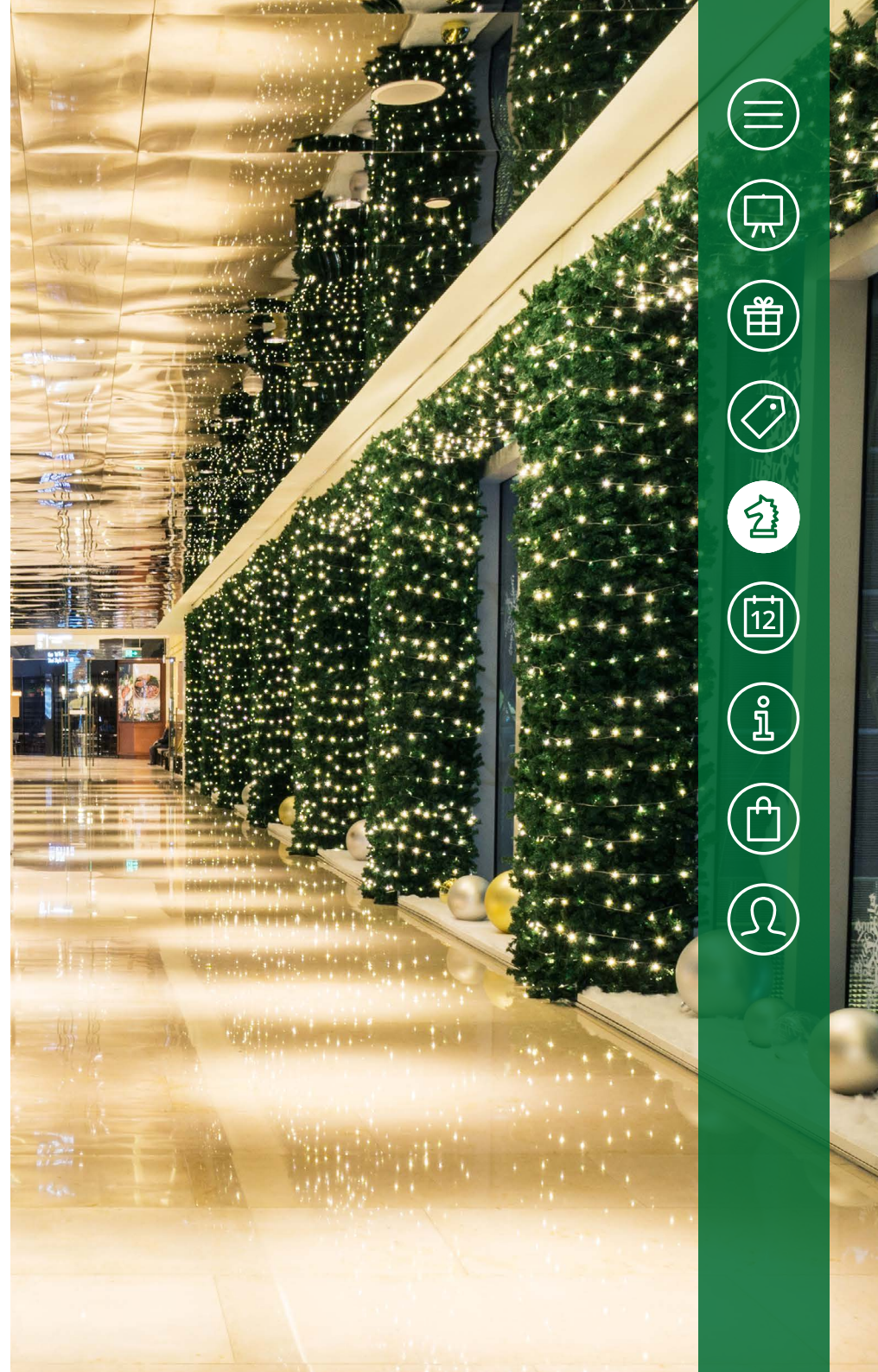
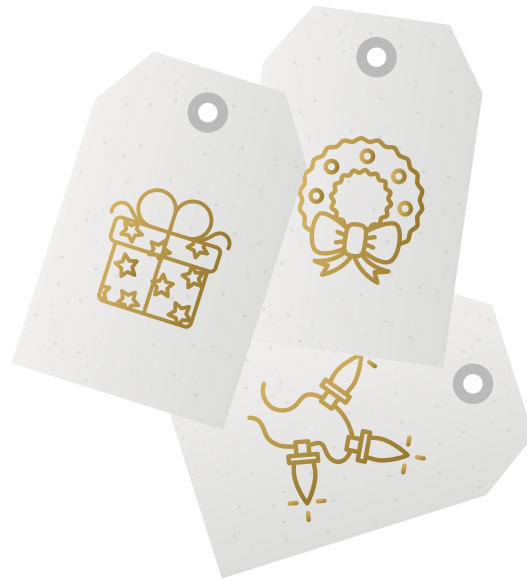
Machine learning, natural language processing and voice/image search are the key AI technology sets providing the most immediate capabilities to retailers, and employing them now doesn't have to be difficult.



John BouAntoun
Principal
Deloitte Digital



Competitive landscape



Primed for Christmas?

With Amazon's arrival onto Australian shores in 2017, many local retailers have sought to reinvent their strategies to remain competitive. This has led to greater investment in online operations – and our survey would suggest that this is proving effective.

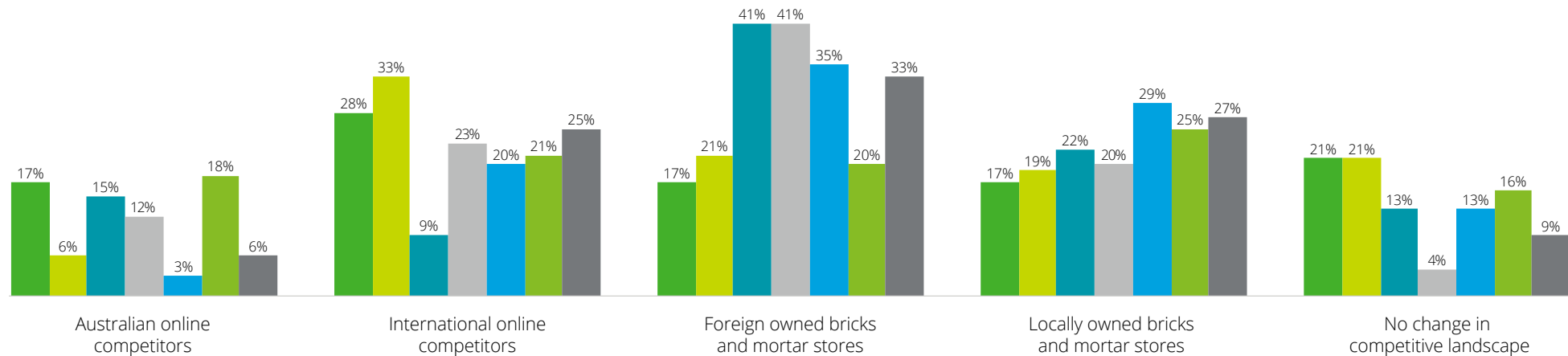
When asked where the greatest competition is expected to come from in the next 12 months, 17% of respondents cited Australian online competitors compared to just 6% in 2017. And with a third of respondents identifying existing competitors as their greatest risk to their business compared to 15% in 2017, Australian retailers are clearly focused on existing rather than new entrants.

“Of most concern is the ongoing adoption of online, and especially Amazon Prime, that is not widely understood in the Australian market to date.”

- Survey respondent

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

● 2018 ● 2017 ● 2016 ● 2015 ● 2014 ● 2013 ● 2012



We have yet to see the full force of Amazon in Australia, with the business still very much in start-up phase. While Amazon Prime, a critical component in winning loyal customers, has been launched locally, services offered have still yet to match those in other countries. For Amazon Prime customers in the US and UK, for example, free next day delivery has driven huge volumes of impulse buying and loyalty to the platform.

In Australia, Amazon Prime currently only offers free two-day delivery, some way off many other local online retailers. This may help explain why 90% of our respondents said Amazon hasn't affected their business since its local launch. However, it is important to learn the lessons from other countries where Amazon has been so successful.

Amazon Australia continues to invest heavily in its infrastructure and people but it is not realistic to expect the creation of a multi-billion dollar business overnight. So it's a word of warning – under-estimate Amazon at your peril.

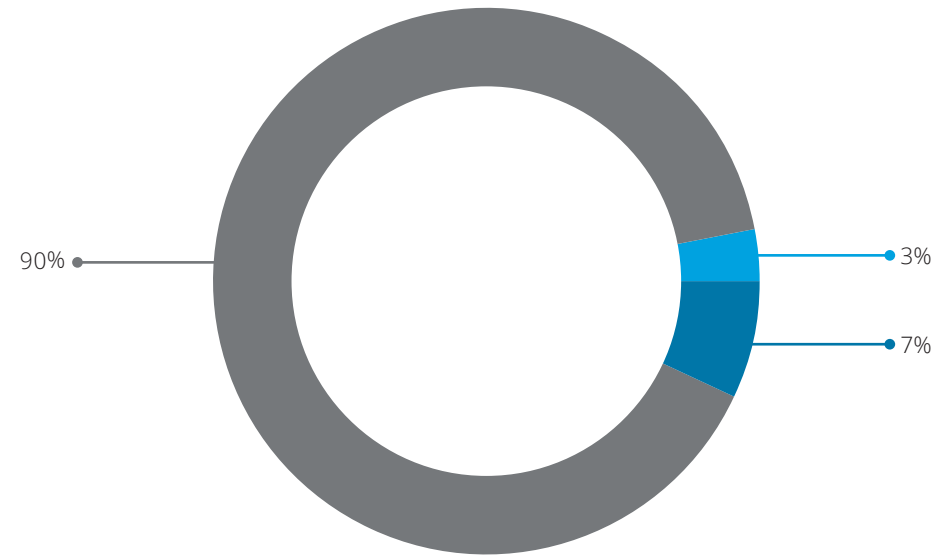
How significant do you believe the impact of Amazon will be over this Christmas period on your business?

● Negative impact ● No impact ● Positive impact



How much of an impact has Amazon had on your business since launching?

● Negative impact ● No impact ● Positive impact



A new GST landscape: offshore, low value sales

While it may be some time before the full impact of GST on offshore sales of low value goods is apparent, Australian retailers should focus on strategies to improve their share of online sales to local and global consumers.

Since 1 July this year, GST has applied to 'low value' goods sold by offshore retailers to Australian consumers – a change over eight years in the making, when the push from Australian retailers to review/remove the GST concession for imports of low value goods began to grow.

In pushing for change, Australian retailers were primarily concerned with levelling the playing field between themselves and overseas retailers. Their objective also aligned with a broader government aim of collecting the appropriate amount of tax revenue for offshore sales. Canberra opted for a 'vendor registration' model as the most practical (and achievable) GST collection option.

In December 2017, the Federal Government estimated a gain to GST revenue from the change

of \$300 million over the four-year forward estimates period starting 1 July 2018, including a gain for 2018-19 of \$70 million. While the actual revenue collection figures for offshore sales of low value goods since 1 July are not yet available, it's worth noting that the initial GST revenue collections on inbound supplies of intangible/digital services (i.e. estimated at \$150 million for 2017-18) was trending towards double this amount after the first quarter.

Additionally, the ATO estimated that approximately 3,000 entities could have a GST registration obligation because of the offshore sales of low value goods measure. As at early July, more than 700 offshore businesses had registered under the simplified system (not counting entities that had registered under the full GST registration system).

The new rules (in brief)

Subject to suppliers meeting the \$75,000 GST registration threshold, the 1 July changes generally:

- Apply 10% GST to offshore supplies of goods worth \$1,000 or less, that are purchased by Australian consumers

- Treat the operator of an online marketplace (an 'electronic distribution platform') as the supplier of low value goods if the goods are sold via the platform
- Treat re-deliverers as the supplier of low value goods if the goods are delivered outside of Australia as part of the supply, and the

- re-deliverer assists with the delivery into Australia as part of a shopping or mailbox service provided to the consumer
- Allow non-resident suppliers of low value goods to elect to use the simplified GST registration and reporting system.



Impact on initial sales

It's certainly too early to say if the change has altered consumer behaviour regarding domestic versus international online purchasing. Initial assessments suggested there hasn't been a discernible impact. Retailer associations told a parliamentary committee in mid-August that the GST change did not appear to have produced a sudden fall in offshore purchases, nor a spike in domestic sales.

On the other hand, one of Australia's major online retailers recently reported a 27% fall in its low value, direct import sales during the first three months of the financial year, coinciding with the retailer adding GST into its pricing.

More will inevitably be revealed when harder data over a longer period becomes available, but it should be remembered that past consumer surveys have consistently indicated that factors other than GST are more important when deciding whether to purchase online from offshore retailers.

Going forward

Given the geographic spread of online suppliers, how will the ATO enforce the application of the new rules, to both maintain a level playing field and collect the proper amount of GST revenue? In practice, the majority of offshore sales are made by a relatively small percentage of suppliers that, due to their internal governance and risk

management procedures, have likely already registered for GST.

The ATO is continuing to engage with offshore businesses that it considers should be registered. For businesses that fail to comply, the ATO has outlined some of the action it can take, including:

- Registering the supplier for GST
- Imposing an additional 75% administrative, legally payable, penalty
- Intercepting funds from Australia that are destined for the supplier
- Registering the debt in a court in the supplier's country
- Requesting the taxation authority in the supplier's country to recover the debt on behalf of the ATO.

The effect of the ATO's firm stance to enforcing the new rules will take some time to become apparent. It will be important to wait for that to occur before trying to assess the full impact of the new rules on domestic versus international online sales, and determining whether they have succeeded in fully levelling the playing field.

That being the case, Australian retailers can now, and certainly should, fully focus on strategies to maintain or improve their share of online sales to Australian consumers, as well as using online sales channels to reach and attract customers outside Australia.

It won't be too long before Australian retailers using e-commerce channels to expand into offshore markets begin facing the potential imposition of foreign GST (or equivalent) on low value goods sold to foreign consumers, as other countries follow Australia's lead. Changes to GST on low value goods in New Zealand will come into effect from 1 October 2019, while similar arrangements are being progressed in Singapore and other jurisdictions. Moreover, a recent decision of the US Supreme Court has potentially opened the way for many US states to begin requiring remote sellers to collect and remit sales taxes.

These potential foreign tax obligations will throw up a range of compliance and pricing related challenges for affected Australian retailers – and careful monitoring of international GST/VAT developments will be essential.



Jonathan Paul
Partner
Tax



The next 12 months



Maintaining the momentum

Looking forward to trading conditions over the next 12 months a number of macro-economic threats could de-stabilise consumer confidence. This appears to be of concern to retailers, with 41% of survey respondents expecting consumer confidence to decline in the next 12 months.

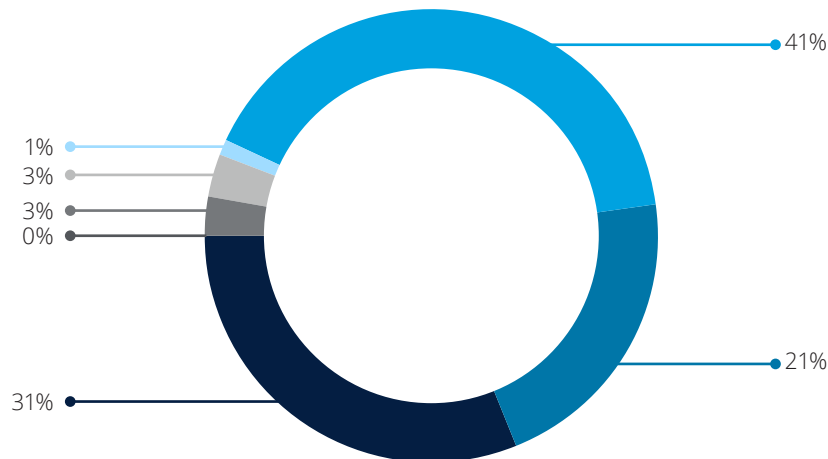
Falling house prices, together with the likelihood of higher interest rates, threatens to slow discretionary consumer spend heading into 2019. However other factors, such as stronger

wage growth, may help compensate for some of this impact.

Despite these potential challenges, retailers remain confident of achieving growth in 2019, with over half of respondents expecting earnings to grow by more than 5%. Over the past 12 months, we have seen a number of retail business failures but we have also seen some very positive trading results. So while trading conditions may be challenging, the stronger performers have been able to achieve growth – and they are confident this will continue.

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



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

- New stores
- Overseas expansion
- Acquisitions
- New products
- New sales channels
- Online offerings
- Pricing increases



Outgrowing stores

While 42% of retailers still expect to open new stores next year, new shop fronts are no longer expected to be the key driver of growth. This marks a significant shift away from traditional retailing in Australia, where a growing market has seen retailers rush to open new stores across Australia and New Zealand. Tellingly, our survey shows that Australian retailers now see online offerings as their key growth driver.

They are shifting away from traditional models, with stores acting merely as transactional centres, and instead investing in online and creating better customer experiences both in-store and on the purchase journey. Excluding product sales, some two thirds of retailers see the most important role of their physical stores as creating a better customer experience.

Two thirds also cited omni-channel and customer experience as their number one strategic priority, suggesting that Australian retailers appear to be

on the right track to success. As a result, executing on this strategy in the face of fierce competition will be critical in the next 12 months.

Overseas expansion

Australian retailers have traditionally been reluctant to expand overseas, despite opportunities in growing markets such as South East Asia and China.

With over 50% of respondents generating no revenue from overseas, future growth opportunities outside Australia clearly exist.

However, it appears local retailers are still reluctant with just over a third currently considering building overseas operations next year.

With the Australian market becoming more saturated, it is only a matter of time before local retailers shift their attention to opportunities overseas, but based on our survey results, for most this won't be in 2019.

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

● Increase ● Decrease ● No change/not applicable



“Retail stores who provide customers with in-store technology experiences are innovative as this will catch the attention of younger shoppers. By using apps they will build loyalty and make their consumers feel like they are part of the ‘in group’.”

– Survey respondent



Paying your employees... right and smart

A happy workforce is a productive workforce, which in turn, brings a positive return on investment for organisations and individuals.

In recent years, too many Australian businesses have attracted media and regulatory spotlights for not paying their employees correctly. Over the past year, reported underpayments have averaged \$9.4 million, and reported penalties handed down by the Fair Work Commission were up to \$660,000. Certainly, under and over payment of wages is both a risk and reality across the sector.

Just as the Christmas season has arrived, and retailers are taking on more casuals, a layperson might ask: how it could be it so hard for businesses to just pay their employees correctly?

The complexity surrounding Australia's industrial relations environment, and specifically for retailers, combined with significant changes to the General Retail Industry Award (the Award) mean there are multiple triggers that can result in non-compliance and sub-optimal deployment of resources.

In addition to the risk factors, Fair Work's Better Off Overall Test (BOOT) also imposes particularly complex requirements for employers.

So employer obligations to their employees are more than wide-ranging. From legislative requirements and Enterprise Agreements (EAs) to common law contracts, if your workforce is covered by more than one of these, every time rates or terms change, ensuring all your employees are paid in a way that ensures they are BOOT compliant can be a real challenge.

With the increasing public scrutiny around wage-related issues, a number of other issues are also in play for those needing to effectively manage wage-related risk:

- Proposals by Labor in Victoria and New South Wales to criminalise underpayment of wages
- The introduction of Single Touch Payroll (STP) designed to improve the Australian Taxation Office's visibility of superannuation contributions means it has never been more important for organisations to proactively identify and address superannuation and tax risks and issues
- Potential relief via the 12-month superannuation amnesty, which is designed to incentivise the voluntary disclosure and prompt remediation of any historic underpaid superannuation obligations.



Risk factors to be aware of

If your industrial relations environment presents any of the following risk factors, there is a strong chance that someone in your organisation is not being paid correctly:

- A large workforce, including both salaried and wages staff
- A multi-state presence and therefore governing legislation
- Disparate and legacy payroll and other systems
- Misinterpretation or a lack of understanding of the Award
- Divergence from Enterprise Agreement (EA) principles
- Change forces such as M&A activities, new systems, agreement negotiation and customer demands.

Navigating the challenges

Some questions, and actions, can certainly help retailers navigate the challenges:

- Do you understand the financial impact of recent regulatory changes, for example, in relation to overtime for casuals? Many retailers will hire casual employees to cater for the busy Christmas period, so it is imperative that they understand the impact of the changes in the rates and

overtime clauses applicable for casuals under the Award and implement controls to ensure their business is BOOT compliant and has adjusted its financial forecasts.

- Has your payroll system been re-configured to satisfy changes to regulatory requirements?
- Changes such as M&A activity, implementation of new systems and renegotiation of EAs represent the perfect opportunity to re-design an EA and re-configure systems for wage compliance while also optimising business benefits. Seize the opportunity to perform a compliance review to understand the current state and roadmap any changes required.
- Take stock of what relevant legal advice has been obtained in the past about various wage components of the Award or your EA, including ordinary time earnings (OTE), allowances, superannuation, leave, leave loading and severances.
- Seek advice and review pay code superannuation classifications for OTE and relevant contractual requirements to mitigate risk of incorrect payment of superannuation and tax.

A useful starting point to understand potential wage payment risks is via a data-driven approach that will help the business make informed decisions and prepare for changes on the horizon through scenario planning based on actual rosters, time and attendance and payroll data.

Truly understanding the drivers of over and under payments, and how well systems and processes support business operations, people and culture is key.

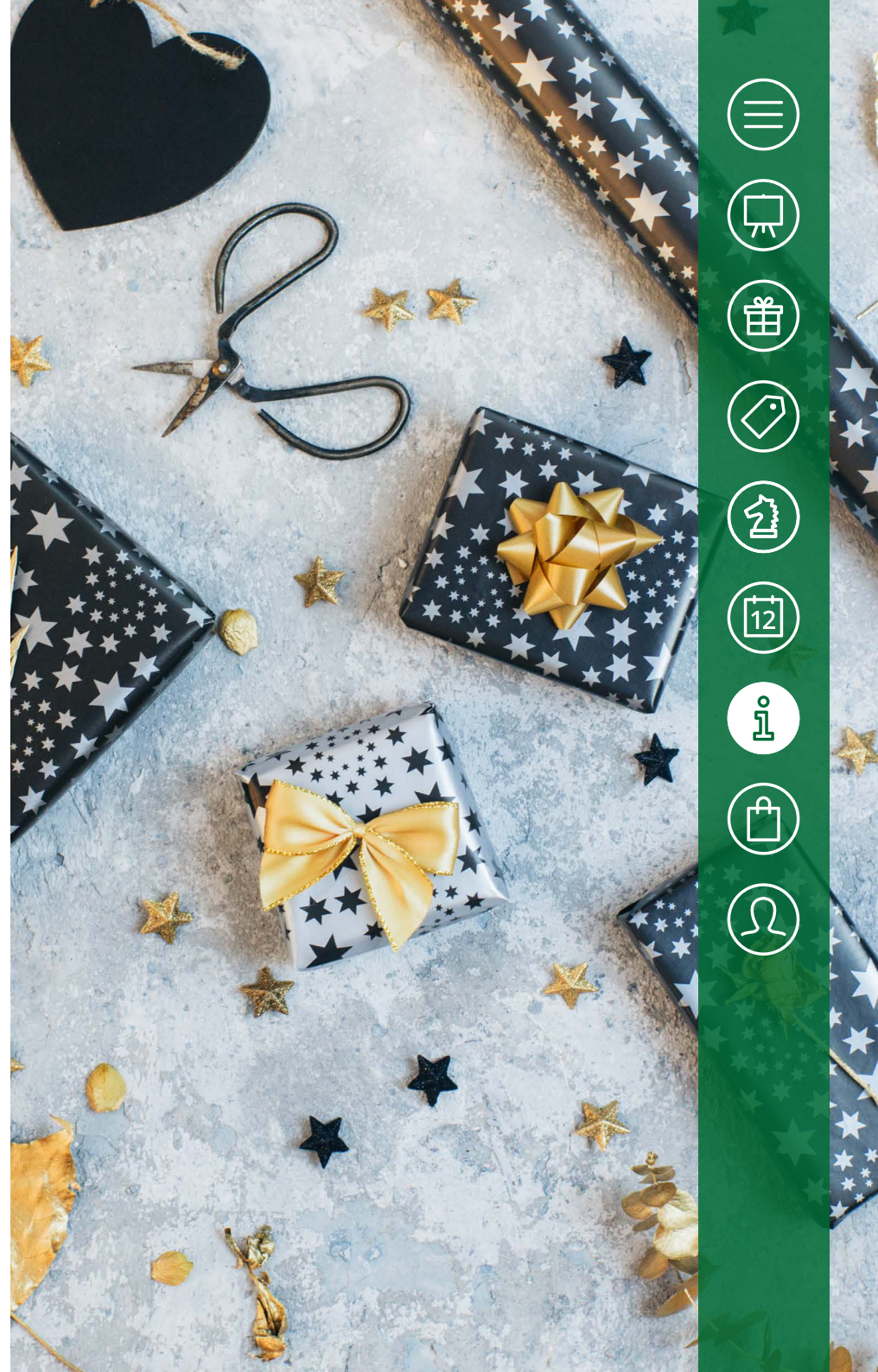
By identifying opportunities for systems and process improvement and compliance issues, your business can look to automate the monitoring of payroll changes and controls. Automation in turn will equip your business to better adapt to the changing industrial relations environment, de-risk what can quickly become a major reputational, regulatory and legal issue, and optimise business performance.



Sunjae Choi
Director
Risk Advisory



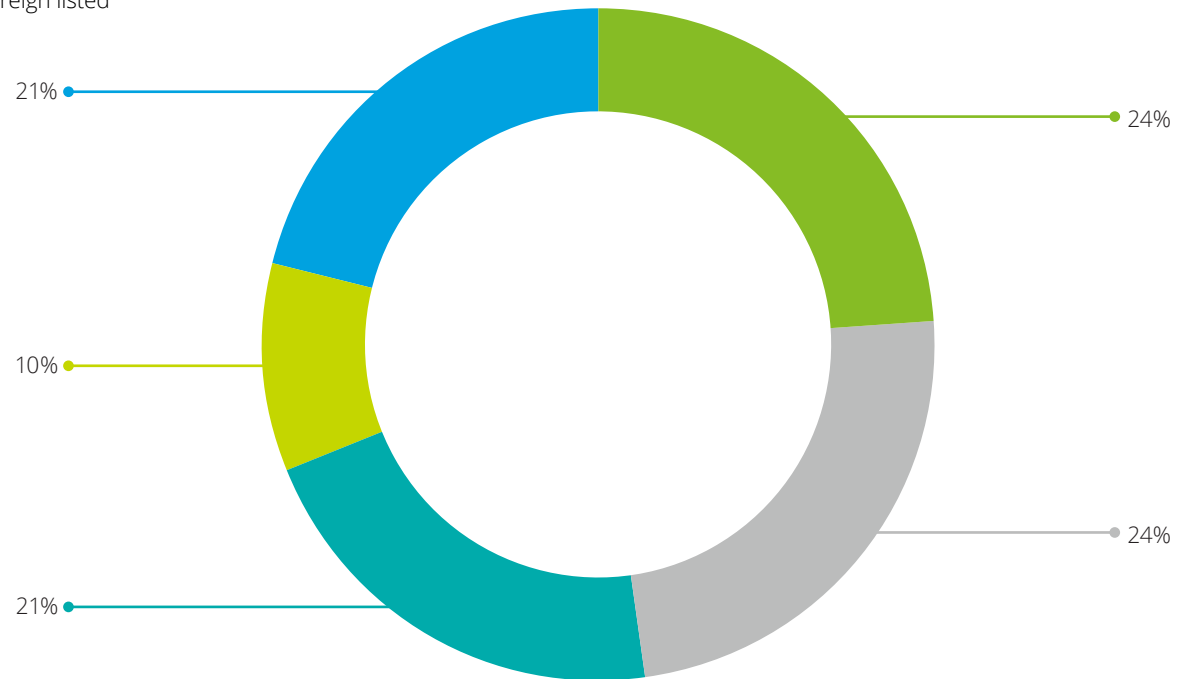
About the survey



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

Ownership structure of respondents

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



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.

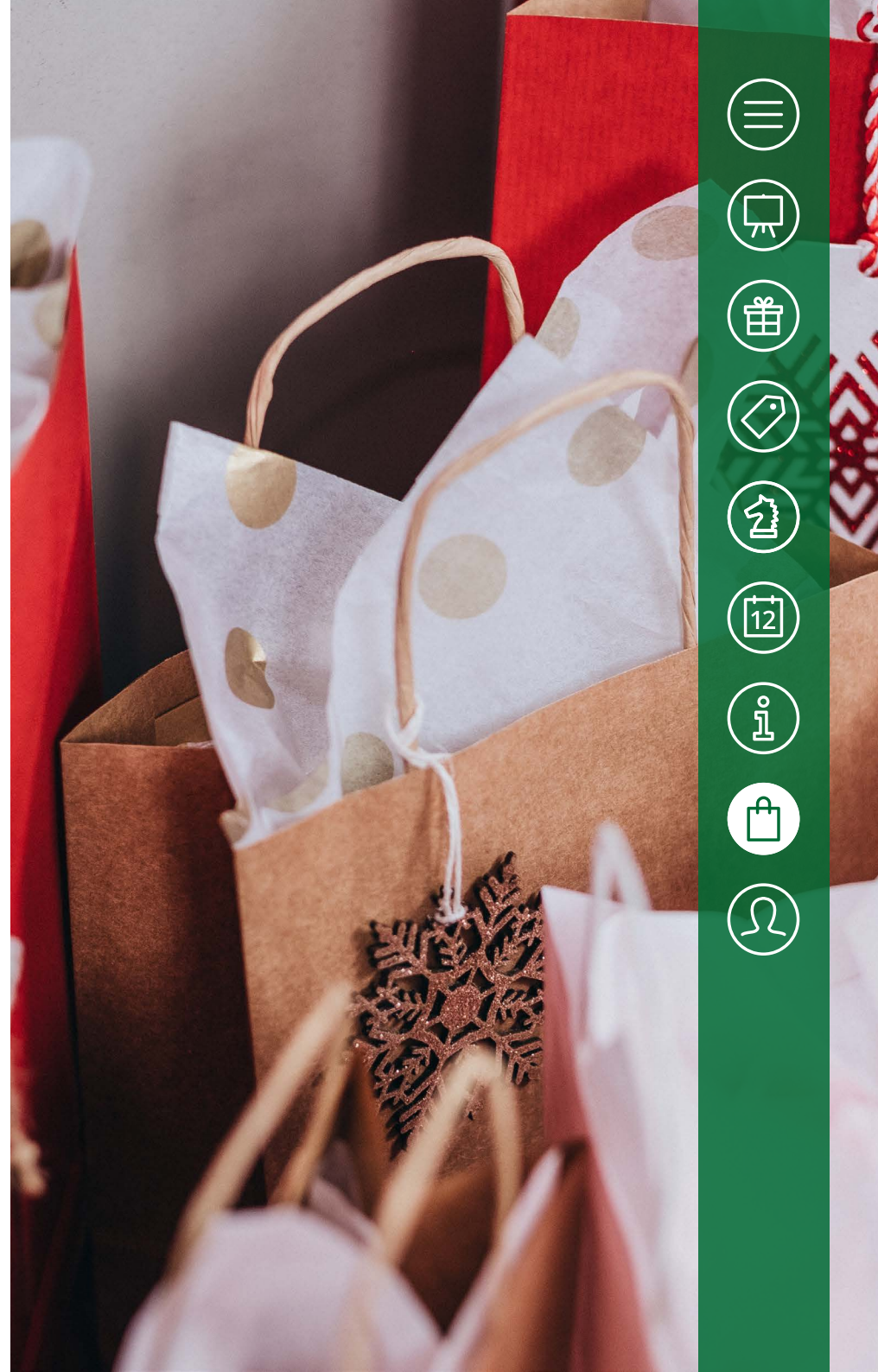
The geographic reach of participants is evenly distributed between Australia, New Zealand and global retailers.

Number of employees

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



Retail, wholesale & distribution group



Deloitte's retail specialists work across every segment of your industry, helping local and global retailers, wholesalers and distributors to meet their biggest challenges: from supply, customer loyalty and franchising trends to changes in consumer taste.

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



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