



Submission to the Productivity Commission Inquiry into the Economic Structure and Performance of the Australian Retail Sector

May 2011



The Initiative for a Competitive Online Marketplace (ICOMP) welcomes the opportunity to provide a submission to the economic structure and performance of the Australian retail industry.

ICOMP, the Initiative for a Competitive Online Marketplace, is an industry initiative for organisations and businesses involved in Internet commerce, particularly online publishers, advertisers, Internet service and network providers, and agencies active in online advertising. ICOMP's mission is to promote widespread support for principles that are essential to a healthy online environment. Key goals are to encourage competition, transparency, data privacy and respect for intellectual property protection as well as the adoption of best practices to promote creativity, innovation, safety and trust. ICOMP's overall objective is the sustainable growth of the Internet consistent with the rule of law.

Recently Australia has witnessed unprecedented changes in retail practices, particularly online, which have had significant impacts on businesses, online commerce and ultimately on consumers.

Search engines

The Internet today is one of the principal ways in which people find information, share ideas, transact commerce and trade in goods and services. It is a force for economic growth and innovation, particularly in the B2C sector.

A large majority of businesses now depend upon search engines as the gateway to consumers— both to attract users to their websites for the purpose of informing them about their products, and to provide them with content that they monetize through advertising.

Therefore, in discussing the broader issues contributing to online purchasing by Australian consumers, one cannot ignore the importance of search and search engines to the online ecosystem. Search is also central to realising the Federal Government's goal of a vibrant digital environment that encourages investment and innovation.

Online Search can make or break online (and many offline) businesses. Online businesses such as newspapers, video sharing sites, and commercial blogs (to name just a few) offer content and services for free to consumers, earning revenue by selling advertising space on their sites to other businesses that want to reach those consumers. Other businesses, from bookstores and auto dealerships, to banks and fashion retailers, use the Internet to advertise and/or sell goods and services directly to online consumers, typically through their own websites. In fact many do both. In all of these business models, there is a direct correlation between revenues and the number of users visiting the site. And search is an essential means of attracting enough site visits to support an online business, particularly in the critical start-up phase.

In addition to its economic effects, search raises important questions about consumer privacy. When a consumer submits a search query, they provide private information – often sensitive in nature – to a third party. Consumers have a legitimate interest in understanding how that information is used, whether and with whom it is shared, and to what extent the consumer can control its dissemination and use.



Put simply, search matters. Anyone who cares about Australia’s digital and economic future should understand the role of search engines in the online economy and how competition in search affects Australian online businesses and consumers. To help shed some light on these issues, this submission provides an overview of the basics of search and a picture of the state of competition in search today in Australia

Despite the fact that most businesses in Australia depend upon search to be found by those consumers, the basics of *how* search works are not widely understood. Let’s start with a snapshot of the search providers here in Australia.

According to Hitwise Australia (April 2011)¹ the leading search engines in Australia by volume searches are as follows:

Leading Search Engines

The following report shows search engines for the industry 'All Categories', ranked by Volume of Searches for the 4 weeks ending 30/04/2011.

Rank	Search Engine	Searches
1.	www.google.com.au	86.58%
2.	www.google.com	5.46%
3.	www.bing.com	4.03%
4.	au.search.yahoo.com	2.34%
5.	www.ask.com	0.29%

As of September 2010, online advertising in Australia (totalling \$571.75 million) broken down as follows:

- AU\$279.6 million – 48.9% search
- AU\$151.5 million – 26.5% display
- AU\$170.7 million – 24.6% online classifieds²

In Australia, search and display advertising is worth around AU\$2 billion. This is a young industry that continues to grow at a prodigious rate. Forecast revenues may increase further as the technology used improves and as results become more relevant to end users.

¹ Hitwise Australia, volume of searches for the four weeks ending 30 April 2011, <http://www.hitwise.com/au/datacentre/main/dashboard-1706.html>.

² IAB report prepared by PriceWaterhouse Coopers, http://www.iabaustralia.com.au/index.php?/news/press/online_advertising_posts_another_record_quarter.



The industry is also characterised by high barriers to entry and significant network effects, which means that Australia's smaller market, relative to the European Union, United States and Canada, is more likely to remain highly concentrated.

The dominance of a single search provider in Australia which has more than 90 per cent market share should be a cause of concern for the Australian retail industry, which relies on search for its business.

Natural Search

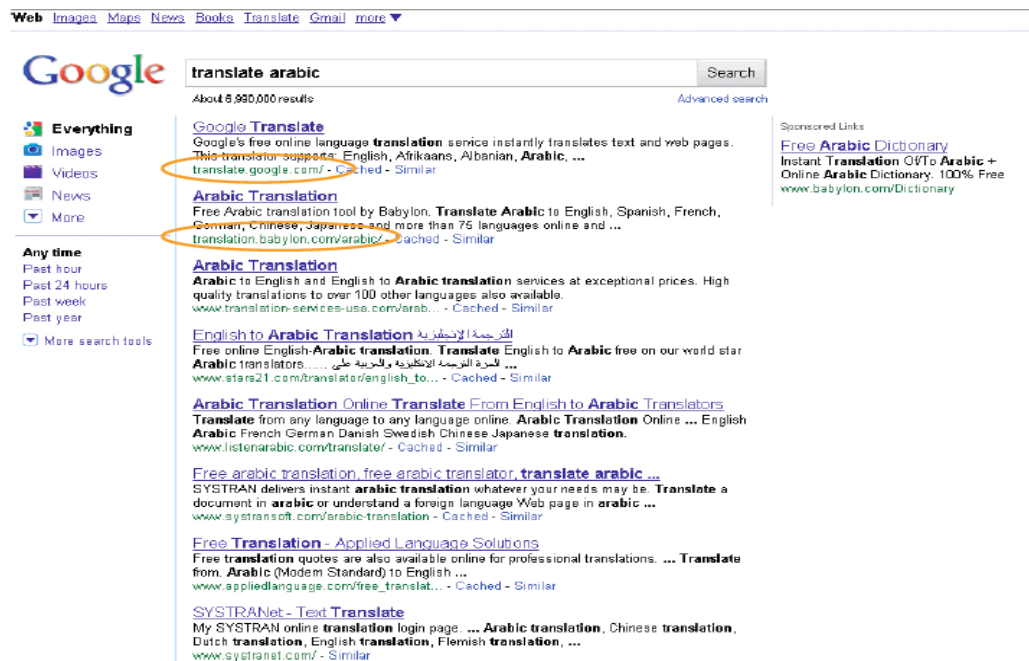
The first type of search is 'natural', 'algorithmic', or 'unpaid' search. These are the results that users expect to be ranked according to their relevance to a particular search query and that should not reflect payments (or other commercial benefits) to the search engine by the sites ranked.

Broadly speaking, there are two key functions that a natural search engine must perform to respond to a user's search query. First, before it can rank anything the search engine must 'crawl' across the web to create and regularly update a vast index of hundreds of billions (or more) web pages. Much like the index of a book, this web index is what allows the search engine to determine which websites might be relevant to a particular search term. A typical two-word search phrase will produce tens of thousands of possible results, or 'hits', with eight to ten hits listed per search results page, sometimes known as 'sponsored link'. This process is hugely resource-intensive and is one of the key ways in which search engines compete.

However, 'the trickiest part... is the *ranking* process – determining which of those pages belong at the top of the list'³ Here, search engines typically use a proprietary algorithm, which in essence sets the 'rule' by which the search engine ranks potentially relevant pages. Factors that the search engine's designers consider in writing the algorithm (*i.e.*, the human input) range from those as simple as the number of times the search term appears on a particular page to incredibly complex and nuanced factors that the search provider keeps secret. A search engine also can manipulate (manually and/or automatically) the algorithm to create exceptions to its rules to altogether exclude certain websites, put some at the top of the list, or otherwise achieve a desired result that is usually not transparent to the consumer.

³ Steven Levy, Exclusive: How Google's Algorithm Rules the Web, Wired (22 Feb. 2010) (emphasis in original), http://www.wired.com/magazine/2010/02/ff_google_algorithm/all/1.

Consider the example of a consumer searching for an Arabic translation service who enters the keywords “translate Arabic”.



Web Images Maps News Books Translate Gmail more

Google translate arabic Search

About 8,990,000 results Advanced search

Google Translate
Google's free online language translation service instantly translates text and web pages.
This translator supports: English, Afrikaans, Albanian, Arabic, ...
translate.google.com/ - Cached - Similar

Arabic Translation
Free Arabic translation tool by Babylon. Translate Arabic to English, Spanish, French, German, Chinese, Japanese and more than 75 languages online and ...
translation.babylon.com/arabic/ - Cached - Similar

Arabic Translation
Arabic to English and English to Arabic translation services at exceptional prices. High quality translations to over 100 other languages also available.
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www.babylon.com/Dictionary

Everything
Images
Videos
News
More

Any time
Past hour
Past 24 hours
Past week
Past year
More search tools

The natural results are provided on the central part of the page, below the search box. All of the sites displayed by the search engine provide translation resources, however the site ‘translate.google.com’ has the coveted place at the top of the list of search results. Statistically, users who perform this search would be twice as likely to click on the top-ranked site than the second-ranked site, “translation.babylon.com/Arabic.”⁴ Lower rankings attract proportionally lower clicks.

Regardless of the particular means used to determine which pages appear in response to a query and in what order, the importance of this ranking decision to consumers and businesses should not be overlooked. Put simply, the order in which a site is ranked has a strong impact on whether the site will be found by a user.

As a result, the algorithms and other methods that search engines use to rank search results effectively serve as arbiters of content and quality; changes and even slight modifications to search engine rankings can have a significant impact on the ability of web publishers to reach online audiences. This is even more the case given that many users do not extend their search past the first page of results. As Pasquale puts it:

⁴ Chitika Research, *The Value of Google Result Positioning* (25 May 2010), <http://chitika.com/research/2010/the-value-of-google-result-positioning/>.

"The number of users attracted by a listed website steeply drops in correlation with its rank, beginning with the site ranked as second. By the time one reaches later pages of the search-results list, such a rank is almost as bad as not being indexed at all. In such an environment, where both commercial and noncommercial speakers place great weight on attracting users' attention, a high ranking is critical to success."⁵

Paid Search

The results that a search engine puts under the heading 'ads' or 'sponsored links' at the right side and/or top of the search page are the "paid search" results, or search ads. Sales of these ads account for virtually all of a search engine's revenues. This makes paid search the primary business model of search engines (and accounts for the vast majority of Google's revenues.)

It is no surprise that online businesses depend significantly and almost solely on search advertising to reach consumers. As noted, consumers rely intensively on search engines to find content and services amidst an estimated one trillion web pages online.

Like natural results, paid search ads are a key pathway to consumers for businesses, and they create that pathway using information that consumers provide about their interests directly through their search queries. This targeted nature of search ads greatly increases the likelihood that advertisers will reach consumers who are interested in their products and services.

Targeting is also what accounts for the power of search advertising in comparison to offline advertising, such as newspapers or billboards, and other forms of online advertising, such as display advertising; these cannot match ads to consumers with nearly the same precision.

According to a survey from search marketing firm iProspect,⁶ almost two-thirds of Australians cannot confidently differentiate between paid search engine listings and natural, or organic, results.

Only 40 percent of respondents said they could distinguish between paid listings purchased by advertisers, which appeared on the right-hand side of a page of search results or at the top of the page in a shaded box, and unpaid listings.

According to the The Australian newspaper,⁷ these findings appear to support moves by the competition regulator to launch a legal action against Google in July 2007 on the basis that Google misleads or deceives consumers by not adequately distinguishing between organic results and paid listings, in contravention of the Trade Practices Act.

⁵ *Internet Non discrimination Principles for Competition Policy Online*, Frank Pasquale, Testimony Before the Task Force on Competition Policy and Antitrust Laws of the House Committee on the Judiciary, July 15, 2008, <http://judiciary.house.gov/hearings/pdf/Pasquale080715.pdf>.

⁶ User befuddled by paid search results, The Australian, 8 November 2010 <http://www.theaustralian.com.au/business/users-befuddled-by-paid-search-results/story-e6frg8zx-1225949102430>.

⁷ User befuddled by paid search results, The Australian, 8 November 2010 <http://www.theaustralian.com.au/business/users-befuddled-by-paid-search-results/story-e6frg8zx-1225949102430>.



The iProspect survey is understood to be the first major study of search engine marketing in the Asia-Pacific region, with more than 15,000 search users surveyed.

Australian online retail industry

The Access Economics Report *Household E-Commerce Activity and Trends in Australia*, estimates that online retail sales by Australians in 2009 totalled between \$19 and \$24 billion, or around three percent of sales. Between 50 percent and 80 percent of that amount was spent with Australian online retail outlets.

The report suggests that the National Broadband Network is likely to be a catalyst for the development of e-commerce in Australia.

The Australian retail industry depends upon both natural and paid search results to reach consumers online. Advertisers are the downstream customers of search engines, and like any customer they should benefit from competition embracing:

- *Fair prices.* Competition among search platforms helps to ensure that no single search company can charge inflated fees for paid search or otherwise make it prohibitively difficult for some businesses to reach their intended audience.
- *Protection from unfair business practices.* The presence of robust competition makes small and medium enterprises and other businesses less vulnerable to harm as it lowers the risk that a dominant search engine can manipulate its results or artificially inflate advertising prices. With competition, advertisers do not have to put all of their proverbial eggs in the same basket.
- *Better outcomes.* Competition affects specific outcomes as well, such as the number of search ads displayed, return on investment (ROI) on advertising placed, and the quality of products and services that advertisers receive from search platforms.
- *Expanded reach.* Just as a brick-and-mortar store advertises in multiple newspapers to reach a wide base of potential customers in a city, businesses that advertise online benefit if they can use multiple, competing search platforms to increase the base of Internet users exposed to their goods and services. To make this work, businesses need the ability to port and re-use their data across advertising platforms. Search engines would be more likely to respect advertisers' desire for data portability if there were a competitive market in which no single search engine held a dominant share. As the Federal Government's *Digital Agenda* recognises, interoperability and user choice could help to foster a more robust digital marketplace.
- *Innovation.* Healthy competition is the key life support system for new ideas and products to come to market.



Small and Medium businesses

According to the Council of Small Business of Australia (COSBOA) the online world is no different to the offline world. Namely, large retailers can push out small businesses through scale and other advantages.

These comments were reported at the retail forum, set up by the Department of Broadband, Communications and the Digital Economy.

According to media reports in PC World, COSBOA said such moves could directly involve Google altering search algorithms to preference larger retailers, squeezing out smaller businesses attempting to circumvent traditional measures to make profits online.⁸

The same publication reported that the Minister for Small Business, Senator Nick Sherry said the issue would likely be dealt with in this inquiry.⁹

In Europe, a UK-based online shopping comparison site and ICOMP member *Foundem.co.uk* has lodged an antitrust complaint at the European Commission, arguing that they had been penalized in search after noticing a dramatic drop in their search results gravely impacting their business.¹⁰

Last year the European Commission decided to open a formal antitrust investigation into complaints lodged by online players, in particular those whose services compete with those of Google, that Google Inc. has been abusing its dominant position in online markets, in violation of European Union rules on competition (Article 102 TFEU).¹¹

The Commission's press release states:¹²

"The Commission will investigate whether Google has abused a dominant market position in online search by allegedly lowering the ranking of unpaid search results of competing services which are specialised in providing users with specific online content such as price comparisons (so-called vertical search services) and by according preferential placement to the results of its own vertical search services in order to shut out competing services. The Commission will also look into allegations that Google lowered the 'Quality Score' for sponsored links of competing vertical search services. The Quality Score is one of the factors that determine the price paid to Google by advertisers.

The Commission's probe will additionally focus on allegations that Google imposes exclusivity obligations on advertising partners, preventing them from placing certain types of competing

⁸ PC World, 18 February 2011,

http://www.pcworld.idg.com.au/article/377217/small_business_protection_required_online_world/.

⁹ PC World, 18 February 2011,

http://www.pcworld.idg.com.au/article/377217/small_business_protection_required_online_world/.

¹⁰ The Guardian, 30 November 2010, "Foundem accuses Google of using its power to favour own links",

<http://www.guardian.co.uk/technology/2010/nov/30/google-foundem-ec-competition-rules>.

¹¹ European Commission press release, 30 November 2010, "Antitrust: Commission probes allegations of antitrust violations by Google."

¹² European Commission press release, 30 November 2010, "Antitrust: Commission probes allegations of antitrust violations by Google."

ads on their web sites, as well as on computer and software vendors, with the aim of shutting out competing search tools. Finally, it will investigate suspected restrictions on the portability of online advertising campaign data to competing online advertising platforms”

The formal proceedings follow complaints by a number of online search service providers including [Foundem](#), the French legal search engine eJustice and *Ciao!*, a price comparison search engine. Complaints have also been made by the German publisher groups, Bundesverband Deutscher Zeitungsverleger and the Verband Deutscher Zeitschriftenverleger, the German mapping company, Eurocities and the French website publisher, 1plusV.

Other organisations and online businesses have expressed similar concerns . One such organisation is One News Page, a global news navigator website, which has developed a site called “Have I been penalized?”.¹³ This site has been established, following what is claimed by the owner to be a lengthy Google ‘penalty’ which despite repeated efforts remains unexplained. One News Page claims the Google penalty decreased its website traffic by 95 percent almost overnight.¹⁴ The “Have I been penalized?” is an initiative which is supported by ICOMP.

Regulatory challenges

E-commerce is the vital force of the Internet and policy makers and regulators should take into account the borderless nature of e-commerce and be able to adapt to the developments of technologies, their use by business and consumers and the potential for abuse. While industry self-regulation, good corporate practices and empowerment of consumers play a large and relatively successful role in managing risks and abuse online, there is sometimes the need for regulation and intervention.

A healthy and competitive environment for online commerce relies on the ability of businesses to respond swiftly to consumers’ needs. It also relies on the development of best practices and cross-industry support for high standards in Internet behaviour. The best way to achieve high standards and best practices is by finding the right balance between self-regulation on the one hand and public regulation on the other. Getting this balance right depends on dialogue, on industry commitment to responsible behaviour and on informed regulators working for flexible solutions that encourage innovation and robust competition.

The Department of Broadband, Communications and the Digital Economy in 2009 released its report *Australia’s Digital Economy: Future Directions*. The paper states:¹⁵

“Governments must continue to review regulatory structures as technology and markets evolve. Ongoing review allows these frameworks to continue to provide an environment in which businesses can grow and consumers can act with confidence.

¹³ www.havebeenpenalized.com

¹⁴ PRmoment.com, 6 May 2010, <http://www.prmoment.com/neil-boom-pr-director-at-onenewspage-com-explains-the-pr-strategy-his-business-took-when-google-turned-off-the-tap-.aspx>.

¹⁵ Australia’s Digital Economy: Future Directions, Department of Broadband, Communications and the Digital Economy, 2009, pp 20.



The Government will continue to consider those aspects of Australia’s regulatory framework that are most pertinent to the digital economy to identify whether reforms are necessary to promote and enable Australia’s development as a knowledge economy.”

It is ICOMP’s view that where there is a single dominant search engine the current framework in the digital economy requires scrutiny, especially given the dependency of so many businesses on the services of a single search provider and online advertising network

ICOMP believes that in light of the growing importance of online platforms in Australia, the existing legal and regulatory framework should be applied with the aim of maintaining and restoring the balance in the system and providing online retailers and consumers with greater choice. Where the pre-existing framework proves to be inadequate, it will be necessary for the legislator to step in and make the necessary changes.

ICOMP encourages the Productivity Commission to consider the following as part of its inquiry:

- The recognition of the increasing reliance of online retailers on a single search engine and search rankings.
- The need to foster an Australian regulatory framework which promotes greater choice, transparency, fair prices, and protection from unfair practices from search engines with significant market power.
- A recommendation that the Department of Broadband, Communications and the Digital Economy (DBCDE) be responsible for the fostering of a fair digital economy regulatory framework, in line with its Australia Future Directions paper.
- The commissioning of a formal survey by the Productivity Commission with online retailers concerning their reliance on search.
- A recommendation to the Australian Competition and Consumer Commission (ACCC) to open a formal inquiry into Google’s practices and market dominance.

Contact

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