

Submission to Issues Paper Competition Policy Review

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EXECUTIVE SUMMARY

At the time of the last major competition review in 1993, the telephone and fax were the prevalent communication technologies. The rapid growth of the Internet and technologies like mobile has had a transformative impact on modern economies. They have allowed businesses to be more competitive, global and productive; they have also irreversibly empowered consumers. This ongoing transformation is an important consideration as the Review Panel assesses Australia's competition law and policy settings.

Over the past decade, the Internet has grown to become a fundamental enabler of the Australian economy. In 2010, it generated \$50 billion in economic value and \$80 billion in societal value.¹

The Internet is an open access platform that creates a level playing field and lowers barriers to entry. These qualities have substantially contributed to the Internet's growth by facilitating uptake, and promoting new services and competition, which in turn, has contributed to the Internet's economic value.

The Internet is one of the most competition-friendly commerce platforms developed. It has changed Australia's economic landscape by driving significant competition between businesses in all sectors of the economy. It has improved how business is done: from simple productivity gains in supply management, finance, and communication, through to significant changes by expanding geographic markets and creating new channels to reach customers.

The Internet empowers consumers by putting essential information at their fingertips, which encourages businesses of all types to be more consumer-centric. Ultimately, this helps consumers make more informed choices, between a greater variety of goods and services, at lower prices.

The Internet is also rocket fuel for small business, giving them substantial low-cost opportunities to compete with bigger players. Small businesses that make the most of the Internet are two times more likely to be growing, and earn two times more revenue per employee, than those that do not.²

Policymakers face a range of complex issues and should prioritise supporting the Internet's vigorous pro-competitive benefits. This can be challenging, if competitors, who are disadvantaged by consumers choosing the services of new entrants, call for protection from that new competition.

Online, competition is only ever one click away, as consumers can easily switch between different services. To convince people to choose to keep coming back, online players must consistently offer compelling services by focusing on adding value and innovating. High consumer mobility and low barriers to entry make it easy for new players and new technologies to spring up and succeed. This online competition leads to the creation of innovative services, which contribute to the Internet fuelling competition across the rest of the economy.

Google considers there is a great opportunity for Australia to harness the pro-competitive and pro-consumer benefits that the Internet provides. It is likely that the dynamic nature of the rapidly evolving Internet enabled economy will facilitate market solutions to any issues that might emerge.

Consumers are the ultimate beneficiaries of the Internet; as businesses, both online and offline, use it to compete to offer them the best goods and services.

¹ Deloitte Access Economics, 'Connected Continent', 2011, <http://goo.gl/4IO8bV>.

² Deloitte Access Economics, 'Connected Small Business', 2013, <http://goo.gl/jOV5pc>.



1. INTRODUCTION – transformative impact of the Internet

Innovation and productivity are inextricably linked to Australia's future prosperity. Competition lies at the core of both as it drives businesses to deliver the best outcomes for consumers.

1.1 Digital enables the economy

The rise of the Internet has caused a major shift in the Australian economy and society, and going forward, its transformative impact may be equivalent to the widespread adoption of electricity.³

Digital is now completely integrated into daily business activities; whereas it was once viewed in isolation as a separate set of tools. For example, email started as a supplement to postal mail and the telephone, but today, it is the basis of communication – changing expectations of responsiveness for everyone from the consumer to the CEO.

The economic value created by this transformation is already huge. In Australia, Deloitte Access Economics estimates that the direct contribution of the Internet to the economy was worth \$50 billion in 2010, equivalent to 3.6% of GDP and greater than exports of iron ore.⁴ It is growing two times faster than the broader economy and predicted to reach \$70 billion by 2015.

The Internet also generates wider economic benefits that are not fully captured by GDP, such as \$27 billion in productivity gains to businesses and government, and a \$53 billion consumer surplus to Australian households as a result of time saved and enjoyment online.⁵

The Internet powers economic growth across the world; over the past five years, it has accounted for 21% of GDP growth and over 4.1% of total GDP in the G20 economies.⁶

This data points to one conclusion: digital is a fundamental economic enabler. In the modern economy, where the Internet underpins much of the activity, there is no separate 'digital economy'. The Internet has changed how business is done: from simple productivity gains in supply management, finance, and communication, through to significant gains by expanding geographic markets and creating new channels to reach customers.

The scale and pace of change driven by the Internet only continues to accelerate.⁷ The rise in Internet use has driven unforeseen technological innovations and has led to new generations of interconnected web services, applications, consumer devices and infrastructure.

The **annexure** to this submission summarises several economic reports that measure, often for the first time, the transformative impact of the Internet.

³ Deloitte Access Economics, 'Connected Continent', 2011, <http://goo.gl/4IO8bV>.

⁴ Deloitte Access Economics, 'Connected Continent', 2011, <http://goo.gl/4IO8bV>.

⁵ Deloitte Access Economics, 'Connected Continent', 2011, <http://goo.gl/4IO8bV>.

⁶ BCG, 'The Internet Economy in the G-20', 2012, www.bcg.com/documents/file100409.pdf.

⁷ BCG, 'The 4.2 Trillion Dollar Opportunity', 2012, <http://goo.gl/jSMoS>.



1.2 Net benefits from digital transformation

The adoption of Internet technologies has created huge productivity and national welfare gains for Australia. The Internet's economic impact is overwhelmingly realised by industries that are not often considered to be leading technology innovators.⁸ According to Deloitte Access Economics, Australia's primary industries are enthusiastic adopters of the Internet, among other things, they use it for sales, marketing, and sourcing supplies.⁹ Further, the finance and real estate industries reportedly have the highest average proportion of Internet utilisation for these activities.¹⁰

The Australian online advertising industry is a prime example of how the majority of the economic benefits of the Internet accrue to other firms. PwC estimates that the core online advertising industry is worth \$3.4 billion annually to GDP, but it supports an ecosystem that generates \$17.1 billion in broader economic activity and 162,000 jobs.¹¹

Internet technology gives firms in every sector the opportunity to transform their business processes in new ways.¹² Australian innovators are combining information and communication technologies in a variety of ways that blur old boundaries and erode old barriers.¹³

1.3 The Internet is a productivity driver

The adoption of new innovative technology practices across the economy will help to drive Australia's productivity growth and prosperity. A vital part of Australia's future fabric will be industries that can adopt technology successfully; from health to education to mining.

Productivity growth contributes to incomes and to living standards. Australian productivity growth has been relatively low since the early 2000's, but Australia's national income has continued to grow due to the resources boom.¹⁴ Economists have noted that as export revenue falls, Australia will need to achieve higher productivity growth in order to maintain and improve living standards.¹⁵

Before the Internet, the development and spread of offline information and communication technologies increased productivity across industries. Investment in ICT grew significantly in the 1970's, yielding significant productivity benefits. In Australia, 20-35% of labour productivity growth in the 1990s has been attributed to ICT adoption by non-ICT producing firms.¹⁶ It is noted that these productivity benefits were slow to appear, as firms had to make changes to business

⁸ See methodology discussion in Deloitte Access Economics, 'The Connected Continent', 2011.

⁹ Deloitte Access Economics, 'Connected Continent', 2011, <http://goo.gl/4IO8bV>.

¹⁰ Deloitte Access Economics, 'Connected Continent', 2011, <http://goo.gl/4IO8bV>.

¹¹ PwC, 'Digital Dollars', 2013, <http://goo.gl/8JUARB>.

¹² For a discussion of these issues and ways to boost Australian innovation, see Jim Minifie, 'Innovation: Time for the lucky country to make its own luck', Grattan Institute, <http://goo.gl/zjVW8j>.

¹³ Ibid.

¹⁴ Over the past four decades, productivity has contributed to one-third of the growth in Australia's living standards. However, productivity has been in decline for over nine consecutive years, with negative growth of -0.8% in 2012-13. During that period, the resources boom generated high terms of trade that stimulated growth in national income. See Productivity Commission, 'Australia's Productivity Performance', 2009 and Productivity Commission, 'Productivity Update', April 2014.

¹⁵ Eslake and Walsh, 'Australia's Productivity Challenge', Grattan Institute, <http://goo.gl/zhsLv4>.

¹⁶ See Gretton et al, 'The effects of ICTs and complementary innovations on Australian productivity growth', Productivity Commission, 2003; and Parham et al, 'Information Technology and Australia's Productivity Surge', Productivity Commission, 2001.



processes to fully utilise the new technologies.¹⁷ Today, the ‘ICT revolution is not over’ as adoption continues to drive productivity growth.¹⁸

With regard to the Internet, Deloitte Access Economics estimates that the “transformations enabled by the Internet are likely to have contributed a similar magnitude to productivity growth for businesses and government as that contributed by the ICT sector over the past decade, amounting to an increase in GDP in 2011 of around \$27 billion” in Australia.

More recent research by Ai Group found that “Australia’s most innovative and ICT intensive industries (financial and insurance services, wholesale trade, and information, telecommunications and media) are also Australia’s most productive. These high-tech leaders experienced labour productivity gains of 40-45% in the last decade, compared to the average for all industry sectors of 13%.”¹⁹

While the Internet is a powerful resource, it is still in its infancy and forthcoming generations of faster broadband and more ubiquitous adoption will drive further transformation.

The transition of developed economies from dial-up Internet to the first generation of broadband over the past decade created a wave of new technology that contributed to economic growth and job creation:

- A recent study found that “a 10 percentage-point increase in broadband penetration raises annual per-capita growth by 0.9-1.5 percentage points”.²⁰ This is followed by a 1.5% increase in labor productivity over the next 5 years.²¹ Similar productivity gains have been found to coincide with investment in transportation infrastructure.²²
- Several studies focusing on the US in the 2000’s, in the early days of the shift from dial-up, found that communities with mass broadband access experienced faster growth, job creation, and higher wages.²³
- In 2006, in the US, “broadband’s deployment created approximately \$8.3 to \$10.6 billion of new GDP. In addition, between \$6.7 and \$4.8 billion constitutes new consumer surplus. In both cases, this is above and beyond what dial-up would have generated.”²⁴

The next generation of high speed broadband will likely create even greater economic benefits.

¹⁷ See Bessen, 'Technology Adoption Costs and Productivity Growth', *Review of Economic Dynamics*, 5(2), 2002; and Productivity Commission, 'ICT Use and Productivity', 2004.

¹⁸ For overviews of studies on the impact of ICT on productivity see Cardona et al, 'ICT and Productivity: Conclusions from the Empirical Literature', *Information Economics and Policy*, 25(3), 2013; and OECD 'Measuring the Internet Economy', 2013. Other studies that find ICT makes a significant contribution to productivity are Byrne et al, "Is the Information Technology Revolution Over?", *International Productivity Monitor*, 2013; Oliner et al, 'Explaining a Productive Decade', *Brookings Institute*, 2007; and Jorgenson and Vu, 'Information Technology and the World Growth Resurgence', *German Economic Review*, 8(2), 2007.

¹⁹ Australian Industry Group, 'Ready or Not?', 2013, <http://goo.gl/Xj3SXH>.

²⁰ Czernich et al, 'Broadband Infrastructure and Economic Growth', 2009, <http://goo.gl/2Ts6Ci>.

²¹ Booz and Co, 'Digital Highways: The Role of Governments in 21st Century Infrastructure', 2009.

²² John Fernald, "Roads to Prosperity?", *Federal Reserve*, 1997,

www.federalreserve.gov/pubs/ifdp/1997/592/ifdp592.pdf; Quintana-Domeque, "Street Pavement: Results from an Infrastructure Experiment in Mexico," *Princeton University, Working Paper No. 556*, 2010.

²³ Gillett et al, 'Measuring Broadband's Impact', *MIT*, 2006, <http://goo.gl/ZvhXs5>; Crandall, et al, 'The Effects of Broadband Deployment', *Brookings Institution*, 2007, <http://goo.gl/KViiQY>; Forman and Goldfarb, 'The Internet and Local Wages: A Puzzle', *American Economic Review*, <http://goo.gl/ux05IU>.

²⁴ Greenstein, 'The Broadband Bonus', *Kellogg*, 2010, <http://goo.gl/Z2nYXU>.



1.4 Continued Internet driven growth

The contribution of the Internet to the Australian economy is growing on a strong trajectory. But, just as the benefits of this digital transformation are huge, so is the opportunity cost as other countries pull ahead. Australia is currently seventh in the world in terms of the Internet's contribution to GDP, and will have to work hard to maintain that position according to BCG – with a predicted slide down the rankings to tenth place by 2016.²⁵ Further, the World Economic Forum found that Australia's relative competitiveness based on ICT use has deteriorated since 2004, slipping from a peak of 9th to just 18th in 2014.²⁶

Australia should continue to support the open and competitive dynamics that have delivered these economic returns – and encourage more. It is likely that the dynamic nature of the rapidly evolving Internet enabled economy will facilitate market solutions to any issues that might emerge.²⁷

²⁵ BCG, 'The 4.2 Trillion Dollar Opportunity', 2012, <http://goo.gl/jSMoS>.

²⁶ Ai Group, 'Australian Digital Competitiveness in 2014', <http://goo.gl/WRf4lx>.

²⁷ With regard to policy makers moving with caution where market solutions are likely to emerge, see BCG, 'The Digital Manifesto', 2012, <http://goo.gl/RgKrV>.



2. COMPETITION POLICY – competition fuelled by the Internet

The open dynamics at the heart of the Internet make it one of the most competition-friendly commerce platforms developed. It has changed Australia's economic landscape by promoting significant competition in all sectors of the economy.

The pro-competitive impact of the integration of the Internet into economic activity includes:

- Barriers to entry have been substantially reduced, facilitating opportunities for new and small players.
- Production costs have been dramatically lowered.
- Consumers are more empowered due to increased access to information, enabling more educated choices.
- These lower production costs and greater market efficiencies have led to lower prices for many goods and services and increased variety.

At the public policy level, the Australian debate about online competition in recent years has focused heavily on issues related to telecommunications and broadband infrastructure, and the local impact of increased competition from new online entrants in sectors such as retail.

Google considers there is a great opportunity for Australia to harness the pro-competitive and pro-consumer benefits that the Internet provides. While the Internet is enabling significant new competition and delivering consumer benefits in a range of industries, existing business models are undergoing some reorganisation. Policymakers face a range of complex issues and should prioritise supporting the Internet's vigorous pro-competitive benefits. This can be challenging, if competitors, who are disadvantaged by consumers choosing the services of new entrants, call for protection from that new competition.

2.1 The Internet is an open access platform

The enduring qualities of the Internet are ease of access and decentralised control. These qualities have substantially contributed to the growth of the Internet by facilitating competition and driving uptake, and in turn, they have contributed to the Internet's economic value.

The open nature of the Internet is created by the protocols and standards that underpin how its infrastructure works. In practice, this means that users can generally access any site without restriction. And, any user – be they an entrepreneur or big business – can generally create new applications, content, or services that will be accessible by all other users of the Internet.

Google is a strong supporter of the open Internet and considers that a healthy web ecosystem benefits all stakeholders.²⁸ The Internet's "openness" means that there is no need to request a gatekeeper's approval before offering a new service to the public, such as a website, ecommerce service, online search service or cloud computing. This has made the Internet an enormous

²⁸ For example, Google's Safe Browsing technology examines billions of URLs across the web, looking for dangerous websites, and notifies users and webmasters so they can protect themselves from harm. Google provides a free feed that is available to all web browsers and is used by Google Chrome, Mozilla Firefox and Apple Safari. Approximately one billion people benefit from Google Safe Browsing.



engine of economic growth, innovation and free expression. It has also driven consumer demand for broadband, benefiting Internet access providers and spurring network investment. All of this innovation has ultimately benefited consumers.

2.2 Empowering consumers

The Internet empowers consumers by putting essential information at their fingertips, which encourages businesses of all types to be more consumer-centric. Ultimately, this helps consumers make more informed choices, between a greater variety of goods and services, at lower prices.

Innovation and uptake of consumer technology

Consumers are leading the uptake of technology, which is driving a broader need for innovation across the economy. In the 1970's and 1980's, government generally led technology innovation with mainframe computers. In the 1990's, businesses became the leading adopters of technology with email and the world wide web. Since around 2007, consumers have had access to the most recent and compelling technology.²⁹

The consumer experience with technology has raised expectations of other services and products, creating a 'consumer experience gap' in other areas. For example, employees increasingly expect the same capabilities at work as they have at home, and citizens' expectations of government are increasingly set higher by their experiences with private sector online services.

The empowerment of consumers has created opportunities that some businesses have been quick to seize by filling the experience gap. Early adopters in the business world have benefited from substantial growth as consumers adopt their offerings.

Changes in consumer behaviour

Consumer technologies are enabling fundamental changes in consumer behaviour and driving positive change in many sectors. Australians are connected, with 70% of them considering the Internet to be a vital part of their lives.³⁰ 19 million Australians have mobile Internet, 14 million have fixed Internet, and each week they spend 15 hours at home and 7 hours at work using it.³¹

Australians are informed shoppers, with 84% doing online research on quality and price before heading in-store to make purchases.³² Deloitte estimates that the resulting time efficiencies save Australians around \$7 billion each year.³³ Online shoppers are even more empowered, with 95% searching the web for product information, price comparisons and reviews before purchasing.³⁴

Smartphones are Australians' best shopping companions. Once a consumer has committed to buying, mobile influences the choice of seller, based on price and availability. While in-store, 42%

²⁹ See PwC, 'Digital Pulse', 2014, <http://www.digitalpulse.pwc.com.au/pwc-digital-services/>.

³⁰ PwC, 'Digital Dollars', 2013, <http://goo.gl/8JUARb>.

³¹ Australian Bureau of Statistics, 'Mobile Handset Statistics, 2013', <http://goo.gl/RoGrCQ>; ACMA, 'Digital economy grows strongly', 2013, <http://goo.gl/8ANmrB>; ARC Centre of Excellence for Creative Industries and Innovation, 'The Internet in Australia', CCI Digital Futures 2012.

³² Nielsen, 'The New Retail', 2014, <http://goo.gl/SO4Eoz>.

³³ Deloitte Access Economics, 'Connected Continent', 2011, <http://goo.gl/4IO8bV>.

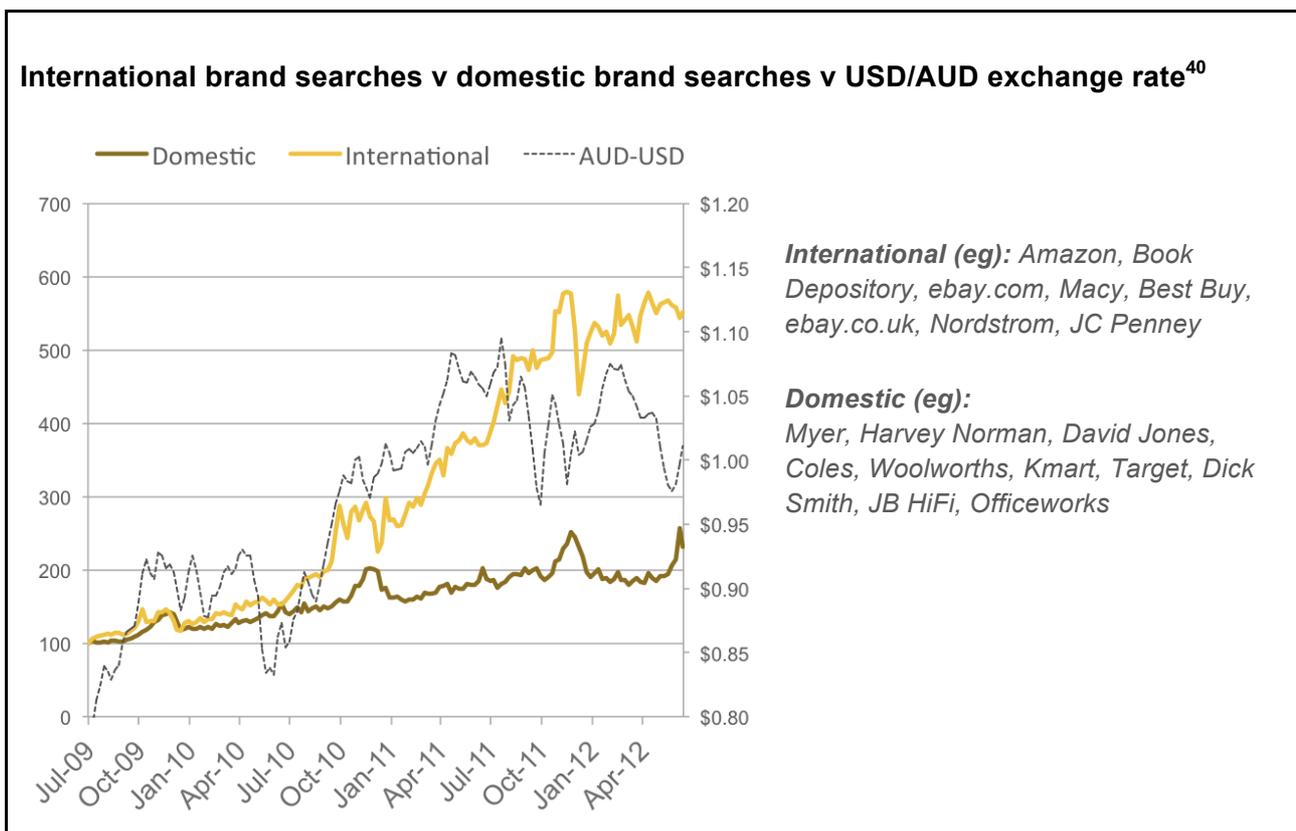
³⁴ PwC, Digital Media Research, 2011.



of smartphone owners use their devices to obtain more information about a product before purchasing, 19% use them to buy online from another store,³⁵ and 27% change their minds.³⁶ This exercise of consumer choice is leading to increased competition and a convergence of online and offline in Australian retail. Ebay estimates mobile savvy shoppers saved around \$3 billion in 2011.³⁷

Consumers also use the Internet as a two-way communication channel. There is tremendous interaction between traditional media channels like TV and radio, and online and mobile channels. Research conducted by IPSOS across 30 countries showed that nearly one in two smartphone users actively “dual-screens” by using their mobile while watching TV.³⁸

Online shoppers are extremely price sensitive and are responsive to competitive prices from overseas retailers. Google search data shows that when the Australian dollar went up against the US dollar, there was a correlated increase in search traffic to international retailers, demonstrated in the graph below from July 2010 onwards. As the Australian dollar depreciated against the US dollar from July 2011, international search traffic flattened – while domestic search traffic remained relatively constant. According to NAB, domestic online sales grew during that period.³⁹



³⁵ Nielsen, 'The New Retail', 2014, <http://goo.gl/SO4Eoz>.

³⁶ IPSOS, 'Our Mobile Planet: Australia', 2013, <http://services.google.com/fh/files/misc/omp-2013-au-en.pdf>.

³⁷ Ebay, 'Australians saved \$2.9 billion in 2011 by shopping smart', 2011, <http://goo.gl/qNvJul>.

³⁸ Google, 'Our Mobile Planet', 2014, <http://think.withgoogle.com/mobileplanet/en/>.

³⁹ NAB, 'Online Retail Sales Index: In depth report January 2010 – January 2012', <http://goo.gl/Zsjb0A>.

⁴⁰ Source: Google internal analysis, 2011.



Australian businesses responding

Australian retailers have a strong history of adapting to change and Google considers that the growth in Internet use presents a positive opportunity for existing and prospective Australian retailers to expand and flourish.

It is worth noting that traditional offline commerce still accounts for over 94% of domestic sales.⁴¹ Even in countries with more established online retail, like the US and UK, upwards of 90% of sales happen in-store.⁴² There is an opportunity for retailers with an existing physical presence to use the Internet to get people into their stores. The Productivity Commission Retail Inquiry noted that “the industry is still dominated by ‘bricks and mortar’ stores, although many of them are evolving into ‘bricks-and-clicks’ operators.”⁴³

Online technologies enable existing retailers with a physical presence to become multi-channel retailers that service customers in-store and online, giving the customer freedom to choose how and when they want to interact. Overseas experience suggests that it is a winning formula: 26 of the top 30 US online retailers are multi-channel retailers.⁴⁴

It is clear that Australians want to interact online with Australian retailers, demonstrated by many consumer surveys.⁴⁵ It is also demonstrated by what they search for on Google Australia, with searches for brand names around 80% for domestic and only 20% for foreign.⁴⁶

2.3 Leveling the playing field for small business

The Internet is rocket fuel for small business, with those that make the most of the Internet being two times more likely to be growing, four times more likely to be hiring, and earning two times more revenue per employee, than those that do not.⁴⁷

Deloitte Access Economics found the Internet has facilitated critical improvements in business processes from finding suppliers, finding and communicating with new customers, through to working more efficiently.⁴⁸ In short, the Internet has transformed several core business activities.

Further, when Australian small businesses use the Internet, other local small businesses benefit. Deloitte also found that small businesses are more likely to use the Internet to find additional customers and suppliers within Australia, than overseas.⁴⁹

⁴¹ Productivity Commission, Retail Inquiry, 2011, <http://www.pc.gov.au/projects/inquiry/retail-industry/report>.

⁴² Ibid.

⁴³ Ibid.

⁴⁴ The Internet Retailer, ‘Top 500 List’, <http://www.Internetretailer.com/top500/list/> (2011). For example, the US department store Macy’s has been especially clear on the benefits of multichannel. Analysis of their loyalty card data demonstrated that for every \$1.00 of transaction value through their Macys.com presence, an additional \$5.77 of in-store purchases was influenced within the following ten days. See Peter Sachse, Macy’s CEO, www.thinkwithgoogle.com/articles/time-for-change-with-peter-sachse.html.

⁴⁵ For example, see ‘Essential: why we love to shop online (and reject paying GST)’, quoted in Jason Whittaker, Crikey, 2010, www.crikey.com.au/2011/01/18/essential-why-we-love-to-shop-online-and-reject-paying-gst/.

⁴⁶ Based on internal analysis of searches for brand names in 2011. Google makes aggregate and anonymised search data publicly available at <http://www.google.com/trends>.

⁴⁷ Deloitte Access Economics, ‘Connected Small Business’, 2013, <http://goo.gl/jOV5pc>.

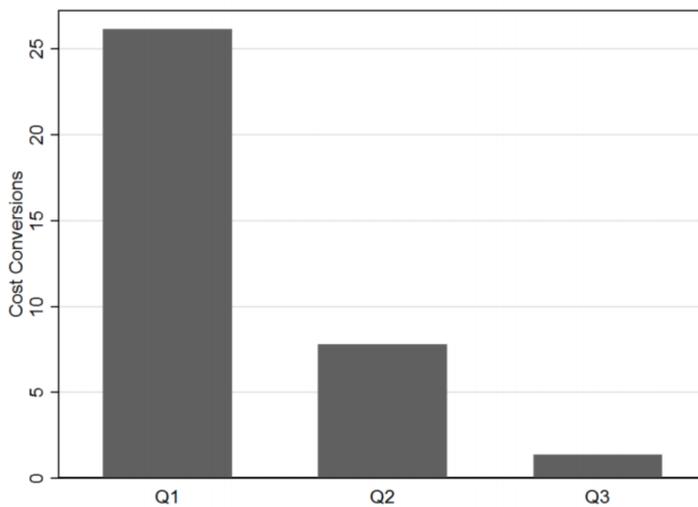
⁴⁸ Deloitte Access Economics, ‘Connected Continent’, 2011, <http://goo.gl/4IO8bV>.

Low barriers to competing on the Internet allow smaller players to compete with larger companies.

Reaching new customers to drive growth

The Internet has transformed the simple but important activity of reaching new customers to drive growth. Determining advertising efficiency is an age-old problem, summed up by the statement credited to US retail pioneer John Wanamaker that “half the money I spend on advertising is wasted; the trouble is I don’t know which half.”

Online advertising data allows advertisers to dramatically lower the cost of sales over the course of a campaign, based on econometric analysis.⁵⁰ This delivers cheaper prices for advertisers, and ultimately for consumers too. The graph below shows a dramatic reduction in costs per conversion or sale, over three quarters, as advertisers use data to show ads to consumers that are more interested, thus saving money by needing to show less ads to achieve the same number of sales.



Source: Catherine Tucker, Figure 19⁵¹

Increasing geographic markets and channels to market

The Internet potentially expands geographical markets beyond local to national and international markets, through online marketing and increasing access to information. It also opens up new sales channels to reach consumers, which reduce costs while improving the effectiveness of serving customers, for example, eCommerce sales or online lead generation.

⁴⁹ Deloitte Access Economics, ‘Connected Continent’, 2011, <http://goo.gl/4lO8bV>.

⁵⁰ Catherine Tucker, MIT Sloan School of Management, ‘The Implications of Improved Attribution and Measurability for Antitrust and Privacy in Online Advertising Markets’, *George Mason Law Review*, Vol. 2, No. 2, pp. 1025-1054 (2013), http://www.georgemasonlawreview.org/doc/Tucker_Website.pdf.

⁵¹ Ibid.

Birdsnest, from country retailer to national online success

One example of a business using online channels to grow is Birdsnest, a retailer of women's apparel based in Cooma NSW. The business started as a classic country town retailer, and in 2004 it employed 5 people. In 2006, the business reached the limits of its growth in the small geographic market around Cooma. Historically, the only expansion option would have been to open new stores in other locations, with all the attendant risks associated with managing multiple shopfronts.

The Internet provided an alternative that allowed Birdsnest to expand its geographic markets from local to national, and even international. Birdsnest now employs about 100 people in Cooma and is experiencing 30-40% year-on-year growth.

Efficient supply chains

The Internet can create efficient supply chains and cost structures for key production activities. It can reduce the transaction costs of locating and purchasing supplies,⁵² and increase the efficiency of producing and delivering goods and services through, for example, enabling lower inventories or better cooperation among designers of new products.⁵³

The Internet can also change the structure and scale of enterprises. It is a powerful export tool that enables small businesses to go global, regardless of their size and geographic origin, by using technology to supervise, communicate and coordinate. Even the smallest company can equip itself with technology that would have been the envy of a Fortune 500 company a decade ago. This gives small players the ability to access international sales and labour markets.

Australian manufacturing micro-multinational

Shoes of Prey, headquartered in Sydney's Surry Hills, is a rapidly-growing small business with a regional supply chain, that exports more than 60% of its sales. This online women's shoe retailer allows customers to design bespoke shoes via a web application, with the shoes then manufactured on-demand in China and shipped anywhere in the world.

Since Shoes of Prey was founded in 2009, it has grown from a workforce of 3 people, to 50 Sydney-based employees. Its customers have designed over 10 million shoes on its website and in 2012 Shoes of Prey's revenue grew by 300%. Shoes of Prey has recently moved offline, with a boutique in the David Jones' Elizabeth Street flagship store.

⁵² Varian H, Litan R, Elder A, Shutter J, 'The Net Impact Study', 2002, www.netimpactstudy.com/NetImpact_Study_Report.pdf.

⁵³ Ibid.



3. COMPETITION LAW – competition between online players

3.1 Competitive dynamics in online markets

Over the past few decades, Australians have experienced an unprecedented and rapidly accelerating pace of innovation, especially in communications and information technologies. As discussed above, the Internet is fueling significant competition across the economy, driven in part by competition between online players.

As more and more services and products “go online”, it becomes increasingly important to understand the competitive dynamics of the Internet. The key online dynamic is that competition is only ever one click away. On the Internet, people can – and do – easily switch between different services.

In a 2012 paper, regulatory economist Bob Harris, from the Haas School of Business at University of California, Berkeley, considers the interplay of switching costs in online markets.⁵⁴ Switching costs are important to competition as they indicate the level of barriers to consumers from changing suppliers of a product or service.

Harris assesses switching costs for online search and finds they are “essentially zero”:

Not only can search users readily and costlessly switch among the leading generalized search engines—Google, Bing or Yahoo—they can and do use a host of other, more specialized search engines to find information on the Web. They also use bookmarks to speed up direct navigation to the “favorite” websites, shopping sites such as Amazon, and mobile apps to search for information. Indeed, most consumers use a combination of these search methods.

Overall, Harris concludes that widespread use of free Internet search has empowered consumers to search for alternate products and suppliers, comparing service offerings and pricing.

3.2 Market definition

The definitions of ‘market’ in the Competition and Consumer Act continue to operate effectively, even in light of recent structural changes in the economy.

⁵⁴ Robert Harris, *Yale Journal of Law and Technology*: Vol. 15: Iss. 2, Article 4, <http://digitalcommons.law.yale.edu/yjolt/vol15/iss2/4/>. Independent academic paper, with financial support provided by Google. Quote from page 4 of Australian version presented at the “Competition in the Online Environment” at Melbourne Business School in November 2012 available here: http://www.ipria.org/events/conf/Competition_Conference/Switching_Costs.pdf.



Google draws the Review Panel's attention to a 2013 paper by Professor Stephen King of Monash University, and former Commissioner of the ACCC, *Market definition and market power in two-sided markets*.⁵⁵

Market definition can still follow traditional Australian methods but inferences about market power cannot be made from market shares ... competition authorities need to carefully analyse the nuances of any particular market and be aware that small changes in market behaviour, or changes in factors that are external to platform owners, can lead to significant changes in market outcomes.

3.3 Time needed for previous amendments to be tested

Over the past 35 years, Australia's competition law has been regularly reviewed and improved; including *Swanson* 1976, *Blunt* 1979, *Griffiths* 1989, *Cooney* 1991, *Hilmer* 1993, *Dawson* 2003 and numerous reviews by the Senate Economics Committee, Productivity Commission and National Competition Council. Those reviews have resulted in a range of amendments to the competition law, some of which have been significant and others that have been more procedural in nature.

The interpretation of Australia's competition law is ultimately a matter for the courts and it typically takes some years for that interpretation to be settled. The first step is a Federal Court decision on conduct that is the subject of enforcement action by the ACCC and/or civil litigation. It can often take a further two years to reach final resolution if that Federal Court judgement is appealed to the High Court.

This means that it can take at least five years after an amendment to the competition law before the High Court has an opportunity to provide an interpretation. This time period can extend significantly longer in the absence of an appropriate case. For example, amendments made to the prohibition on the misuse of market power in 2008 have yet to be considered by the High Court. Similarly, amendments to prohibitions on cartel arrangements made in 2009 received their first Federal Court judgement following a contested hearing in *Bradken* in 2013.⁵⁶

Google submits that the Review Panel should take a cautious approach to amending sections of the Competition and Consumer Act. The current cycle of review and legislative amendment makes it difficult to assess whether earlier amendments have been effective in addressing perceived deficiencies in the competition law. For this reason, competition law should only be amended if there are clearly demonstrated substantive or procedural deficiencies.

⁵⁵ Stephen P King, 'Two-sided markets', *Australian Economic Review*, Volume 46, Issue 2, pages 247–258, June 2013. Independent academic paper, with financial support provided by Google. Available at: http://www.ipria.org/events/conf/Competition_Conference/Market_definition_&_power.pdf.

⁵⁶ *Norcast S.ár.L v Bradken Limited (No 2)* [2013] FCA 235 (19 March 2013); regarding the section 44ZZRD(3)(c) of the Competition and Consumer Act prohibition on bid-rigging.



4. REGULATORY IMPEDIMENTS

4.1 Copyright and fair use in the digital age

A modern, flexible copyright regime will become an increasingly crucial element of economic policy as Australia transitions to an economy that relies heavily on knowledge, innovation and creativity.

The lack of a flexible copyright regime in Australian acts as a significant impediment on local businesses competing on the global stage. Innovation often occurs in rapid response to consumer demand and can be held back by laws that only permit narrow categories of activities.

Copyright should be “future-proofed” to make it more flexible and technology-neutral. An economic study has shown that this will generate an economic benefit of \$600 million per annum in Australia, within 10 years.⁵⁷

Reform would help local creators reach global audiences, make Australia more attractive to technology investment, attract a digitally skilled workforce, allow Australian technology and content creators to be competitive globally, and permit Australian consumers to enjoy the content that they own in innovative ways.

The digital world has moved forward and left Australia’s copyright regime outdated. Australia’s copyright law is too static, narrow and technology-specific, which is holding back innovation, creativity, investment and the enjoyment of content. It means that new and innovative uses of copyright materials are frequently not permitted, as they are not specifically covered by an existing exception, no matter how strong the public interest may be. Australian businesses are not as free to innovate, putting them at a competitive disadvantage to counterparts in countries like the US.

The ALRC’s *Copyright and the Digital Economy* report recommends the implementation of a ‘fair use’ flexible exception. The government is considering its response. Google supports such a ‘fair use’ exception,⁵⁸ and encourages the Review Panel to consider it as an opportunity to remove a regulatory impediment to competition.⁵⁹ Doing so will help Australian businesses capitalise on the next wave of innovation, unlocking new investments and economic growth.

⁵⁷ Nick Gruen, ‘Excepting the Future’, Lateral Economics, 2012, prepared for the Australian Digital Alliance: <http://digital.org.au/our-work/publication/exceptional-industries-and-excepting-future>.

⁵⁸ See Google’s submissions to the ALRC:
http://www.alrc.gov.au/sites/default/files/subs/217._org_google.pdf and
http://www.alrc.gov.au/sites/default/files/subs/600._org_google.pdf.

⁵⁹ Regarding the relevance of copyright to competition in markets for copyright material, Google notes the ACCC’s submission to the ALRC review, which states that:

The ACCC broadly supports the introduction of a fair use exception, as proposed by the ALRC, and considers that such an exception is likely to promote an appropriate balance between socially beneficial incentives to create and incentives to disseminate and use copyright material.

... introducing more flexible copyright laws should be able to accommodate and foster technological advances and innovations that might otherwise be curtailed by prescriptive and/or narrow exceptions.

ACCC, ‘Submission to the ALRC Copyright and the Digital Economy Discussion Paper’, 31 July 2013, pp 2 & 7, www.alrc.gov.au/sites/default/files/subs/658._org_acc_.pdf.



ANNEXURE – economic studies

The Internet in Australia is as valuable as iron-ore exports

Deloitte's 2011 *Connected Continent* report examined the importance of the Internet to Australia's economic outlook.⁶⁰

- **The Internet contributes \$50 billion to the economy** – or 3.6% of gross domestic product, in 2010, equivalent to the value of iron ore exports. It is expected to grow at 7%, more than twice the speed of the rest of the economy, reaching \$70 billion by 2015.
- **The average Australian is online** – households benefit from greater choice, convenience, and easy access to information, which they value at \$53 billion.
- **The Internet creates jobs** – 190,000 people are in jobs directly related to the Internet, including IT software firms, Internet Service Providers, and companies providing e-commerce and online advertising services. Those 190,000 jobs alone generated \$22 billion for the Australian economy in 2010.
- **The typical Australian business is an Internet business** – the Internet's economic impact is overwhelmingly realised by industries that are not often considered to be leading technology innovators. For example, Australia's primary industries are enthusiastic adopters of the Internet: highlighting the benefits from using the Internet for sales, marketing and sourcing supplies. Businesses, particularly small businesses, have seen their productivity rise dramatically, with gains worth \$27 billion each year.

Digital media are invigorating content in Australia

BCG's 2013 *Culture Boom* report assessed the economic and social impact of the Internet on Australian viewers, artists and the media and content industry.⁶¹

- **The media industry is healthy, with the Internet providing a "shot in the arm"**—by 2015, total annual revenues of the sector are expected to grow by \$4.3 billion to \$29.1 billion and jobs are expected to grow by 15,000 to 120,000. Online media is driving over 50% of the growth in revenue and jobs.
- **Australian viewers, readers and listeners derive a \$24 billion surplus from online media and content**—Australians like the new media world, where their access to, and choice of, media has never been greater.
- **Australia has a trade surplus in online content as the Internet has helped local creators reach a global audience**—Americans alone watch two times as many hours of Australian videos as Australians. 35% of newspaper reading is done online with Australian readers overwhelmingly (91% of the time) choosing Australian newspaper websites.

⁶⁰ Deloitte Access Economics, 'Connected Continent', 2011, <http://goo.gl/4IO8bV>.

⁶¹ BCG, 'Culture Boom', 2012, www.bcg.com/documents/file101187.pdf.



The Internet is rocket fuel for small business

The 2013 *Connected Small Business* report from Deloitte Access Economics provides insight into the use of the Internet by Australia's small and medium-sized businesses, which employ more than seven million people and are responsible for half of private sector economic activity.⁶²

Deloitte gives a report-card on the level of 'digital engagement' of small businesses based on a national survey of 500. It ranks businesses in four levels of digital engagement from high (making the most of the web of by using tools like online marketing), through to medium, low, and very low (essentially not using the web at all to reach customers).

Small businesses making the most of the web with high digital engagement are:

- Two times more likely to be growing, and earn two times more revenue per employee
- Job creators, being four times more likely to be hiring
- Enjoy better business outcomes – on average, moving up a level of engagement equates to an average \$350,000 or 20% increase in annual revenue
- Three times more likely to have growth as a business objective
- Three times more likely to be increasing investment in digital over the next year
- More resilient with better growth prospects, more diversified sources of revenue, and a larger customer base

Yet, Deloitte found that only 16% of Australian small businesses have high digital engagement and are enjoying those benefits. 25% have medium digital engagement, 24% have low engagement and are barely using the Internet, while 35%, the largest group, have very low digital engagement and are not using the Internet at all to reach customers.

For small businesses with very low engagement, this is significant low hanging fruit that can increase growth expectations. Establishing a digital presence with a website creates the biggest and easiest payoff, a good first step for the 40% of business that do not have one.

⁶² Deloitte Access Economics, 'Connected Small Business', 2013, <http://goo.gl/jOV5pc>.

Internet advertising drives substantial economic activity in Australia

PwC's 2013 *Digital Dollars* report for IAB Australia on the impact of Internet advertising estimates that:⁶³

- **Online ads are worth \$17.1 billion to the economy**—ads are an important part of a highly dynamic economic ecosystem that enables the creation and delivery of a huge range of content and services to millions of Australians, and contributes \$17.1 billion in economic activity and 162,000 jobs. The value of the ecosystem is forecast to reach \$26.5 billion by 2017, growing at more than two times the pace of other sectors.
- **People value ad-supported services and content at \$70 billion**—the ad-supported ecosystem generates additional consumer welfare benefits worth approximately \$70 billion in value above the price paid for access to services. Ads are the primary funding model that supports many things Australians use the Internet for on a daily basis, and access at either no cost (free) or low cost.

Tech startups could unlock a \$109 billion economic lift and 540,000 jobs

Entrepreneurs working more closely with educators, government and corporate Australia is the key to unlocking the potential of the tech startup sector and delivering an additional \$109 billion to the economy, according to PwC's 2013 *The Startup Economy* report.⁶⁴

The startup sector is a rapidly growing part of the economy which has the capacity to contribute four per cent of GDP and create 540,000 new jobs by 2033. The four key ways to unlock the potential of the sector are:

- **Attract more entrepreneurs with the right skills:** in the short term Australia needs 2,000 more tech entrepreneurs each year, from the existing workforce. In the long term, Australia's education sector must produce more skilled tech entrepreneurs.
- **Encourage more early stage funding:** funding for tech startups will need to increase. Australia invests approximately \$7.50 per capita in venture capital per annum, compared to \$75 for the United States and \$150 for Israel (all quoted in US dollar figures).
- **Open up local markets to tech startups:** Governments are major consumers with spending totaling \$41 billion in 2012. They can be more startup friendly with procurement reform.
- **Foster a stronger culture of entrepreneurship:** Australia has a considerably higher 'fear of failure' rate than nations like the US and Canada, constraining the sector. The tech community is key to changing this by celebrating its own success and becoming more inclusive.

⁶³ PwC, 'Digital Dollars', 2013, <http://goo.gl/8JUARb>.

⁶⁴ PwC, 'The Startup Economy', 2013, <http://goo.gl/srSqaj>.



Copyright reform potentially worth \$600 million to Australia

Australia's copyright regime is currently holding back innovation, making copyright more flexible and technology-neutral will, over time, add \$600 million in annual productivity gains.

The 2012 Lateral Economics reports, *Exceptional Industries* and *Excepting the Future*, value the 'copyright exceptions sector' at \$182 billion dollars per annum, or 14% of Australia's GDP.⁶⁵

The 'copyright exceptions sector' includes sectors that rely on using copyright material, such as education and research institutions, libraries and cultural institutions, digital, Internet and web hosting providers. Copyright 'exceptions' are vital to Australia's cultural, technological and economic activity. Exceptions allow people to, for example, shift their music from CD to MP3 so that they can use an iPod.

Australia's outdated copyright laws create a legal environment that is less conducive to innovation and investment than comparable countries for services such as web hosts, search engines and social media.

Australia's current copyright regime fosters risk and uncertainty and has a negative impact on investment and innovation.

- Negative impact on investment: the reports found that investors would value the reduced risk and uncertainty from more flexible copyright at around \$2 billion a year.
- Negative impact on innovation: with inadequate and inflexible copyright 'exceptions', there is far more copyright risk to online services in Australia than in comparable countries with more flexible copyright laws.

More flexible, technology-neutral copyright laws would make a substantial contribution to Australia's economic growth and innovation with negligible downsides for content owners.

⁶⁵ Nick Gruen, 'Excepting the Future', Lateral Economics, 2012, prepared for the Australian Digital Alliance: <http://digital.org.au/our-work/publication/exceptional-industries-and-excepting-future>.