

Why Market Domination Is Elusive

A new study confirms what most of us have known for a long time: not collecting sales tax gives mail order retailers an important competitive advantage. A team of researchers at Ohio State University tracked the spending of 245,000 households that had spent at least \$100 at Amazon.com in the first six months of 2012 and then kept tabs on them through the end of 2013. Their findings? In the 20 states where Amazon is now collecting sales tax, households trimmed their spending at the retailer by 10%, compared to households in states where sales tax was not collected. For purchases of over \$300, the spending pullback was a more precipitous 24% in sales tax jurisdictions.

That a 4% to 10% sales tax levy would influence consumer behavior is hardly surprising. But before brick-and-mortar retailers conclude that a uniformly applied sales tax will “level the playing field,” they should take note of some of the other findings. The survey showed that brick-and-mortar retailers received a 2% revenue increase in states that had an online sales tax. However, the biggest beneficiaries of the online tax were the online merchants that weren’t required to collect sales tax, typically independent businesses operating on the Amazon marketplace or eBay. In states where Amazon collected sales tax, these companies experienced a 61% revenue gain.

Some may quibble about the survey methodology or the precision of its findings, but the Ohio State research highlights two irrefutable truths. One is that sales tax avoidance confers a tremendous benefit to online sellers. The other is that lower price is not the sole reason consumers gravitate toward internet retailers. Showing that changes in tax policy may slow or even stop Amazon’s growth, the research also highlights that the online giant, like every other retail format, has its limits. Amazon management is apparently aware of the challenge, as evidenced by their shifting positions on collecting sales tax. At first, they were staunchly against it. But as it became harder to resist, they made an about-face, advocating that all online merchants should collect sales tax. (If you can’t beat ‘em, join ‘em.)

In each decade of the past century, there have been predictions that some fast-growing retailer was on the verge of complete and unchallenged domination. In the 1920s, it was the Atlantic & Pacific Tea Company, which was seen as such an overwhelming threat, Congress wrote laws specifically designed to limit its expansion. A decade later, it was Sears & Roebuck, which had begun buying controlling interests in key suppliers like Whirlpool appliances and even Harmony guitars. In the 1960s, when K-Mart introduced deep discounts and the famed “Blue Light Special,” conventional wisdom held that all other retailers were in peril. More recently, candidates for domination have included Wal-Mart, a variety of

big box retailers including Guitar Center, and Amazon of course.

Ironically, when pundits start referring to a retailer as an “unstoppable juggernaut,” its best days are usually behind it. Just consider the status of the powerhouses listed above. A&P has made several trips to bankruptcy court and is now a marginal regional grocery chain; Sears and K-Mart are hemorrhaging red ink and their continued survival is in doubt;



growth at Wal-Mart has ground to a halt; and many of the big box specialists, like Best Buy, Toys R Us, and Office Depot, are in retrenchment mode. Exactly when Amazon peaks is an open question, but if history is any guide, it will happen.

As more online purchases are subject to sales tax, online sales growth will slow and the relative competitive positions of brick-and-mortar and online retailers will

shift. However, don’t expect a return to the retail landscape that existed prior to chains and online selling. Retail evolution has consistently taken unanticipated turns. Three decades ago, mall-based home organ retailers were the industry’s most profitable operators. Two decades ago, high-end guitar specialists were a rarity. A decade ago, no one expected Amazon to be an important factor in the m.i. market. A decade from now, who knows what retail will look like.

Here’s one safe prediction though: Consumer expectations of price, selection, and service will continue to rise. And the market will continue to fragment, driven by 300 million citizens who demand that goods and services be tailored to their specific needs, no matter how quirky. This irrefutable dynamic suggests a continued place for nimble retailers who can identify and service a niche. The internet, by breaking down geographic barriers and creating more transparent pricing, has made the market more competitive than ever. That said, the diversity of consumer needs and wants makes it unlikely that any single player is destined to completely dominate. And remember, anyone who says they’re on the verge of taking over has probably already peaked.

Brian T. Majeski
Editor

brian@musictrades.com