

# Retail Therapy

## Factory Outlets – friend or foe?



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## Factory Outlets – friend or foe?

*Factory outlet retailing is now considered a ‘true’ and permanent part of the retail landscape. With consumers looking for bargains and space becoming readily available through new outlet developments, the sector is flourishing (Cummins, 2007). Already a huge success in the US and UK, the boom in Australia has definitely arrived, with factory outlet retailing now ranked as the fastest growing retail format. Retailers are increasingly integrating this format into their channels of distribution as an ideal way to move older stock and raise their profile with a fresh set of consumers (Choice Magazine, 2007). Over the next decade, the factory outlet centre market is predicted to grow from about 4 percent to as much as 6 percent of the Clothing and Soft-goods Retailing sector. However, this figure is dependant on the major developers in this space realising their expansion plans; it is possible that there could soon be over 30 outlet centres across Australia (Cummins, 2007).*

### **The ‘why’ and ‘what’ of factory outlets**

Factory outlet retailers are often classified under the category of ‘value retailers’, differing from department stores and off-price retailers. For manufacturers, factory outlets provide a profitable channel for the sale of surplus merchandise (generally last season’s excess, outdated and returned stock) direct to consumers. In essence, outlets sell a wide range of retail goods (mainly clothing, footwear and leather goods, accessories, gifts and home design products) for the ever-increasing number of bargain-hunting consumers at up to 70 percent off the full retail price (Choice Magazine, 2007). Many brands also manufacture products especially for outlet stores, though generally these products are of slightly lower quality than their standard retail lines.

Factory outlets were initially designed with minimal style, poor merchandising and basic shop fittings, being located in industrial or manufacturing areas, often near the manufacturer’s production site. Some well known districts around Australia include Bridge Rd, Richmond and Smith St, Collingwood in Melbourne; Sydney’s Redfern district and Stone’s Corner in Brisbane. These areas have now been virtually superseded by the modern day factory outlet as progressively, factory outlets changed from no-frills warehouses to well-designed buildings, with leading brands as tenants. Now, factory outlet centres provide consumers with high value and branded goods at attractive prices in a welcoming and safe environment. All these elements create a pleasurable, compelling and rewarding visit for consumers. Considering shopping as a leisure activity, factory outlet centres have also begun to include entertainment facilities mixing low price shopping with fun and entertainment.

This hybrid development is being led by Brand Smart which has expanded rapidly around the country with its Harbour Town concept centre. With sites on the Gold Coast, Perth, Adelaide and one soon to open in Melbourne Docklands in 2008, the combination of waterside frontage with outdoor cafes and shops is attracting consumers in droves. This type of hybrid type centre could very well set the standard of factory outlet retailing.

### **Consumers and their demand for 'bargains'**

Some experts suggest that factory outlet consumers are mainly women, in the 25 to 55 age group, and may drive between 30 minutes and two hours to reach their destination with a specific purchase in mind (Lombart, 2004). More broadly, there have been three overarching shopper typologies identified by Karande and Ganesh (2000); the recreational shopper, the serious economic shopper and the time-conscious deal prone shoppers.

Recreational shoppers engage in serious 'browsing' activities and will patronise the factory outlet as entertaining bargain hunting adventure. This shopper type is likely to purchase impulse items and be susceptible to in-store promotions. Time-saving shoppers are reluctant consumers who shop on major sale days to obtain the best bargain. This consumer differs from the serious bargain hunter because they value convenience over other shopping aspects and is prone to switching formats depending on the best value for money. Therefore this consumer will only patronise a factory outlet if it is offering the best value. Contrastingly, the serious economic shopper is the group most factory outlets centres attract. This group of shoppers is focused on attaining the best bargain, and will overlook quality for price.

Satisfying a range of shoppers it is not surprising that demand for outlet centres is increasing and people will travel quite a distance to get there. They have become a retail 'destination' and for many Australians, going to one of these centres has become a weekend outing for the whole family. Shoppers expect a bargain and are ready to spend time browsing and there is no doubt outlet shopping can save money, but the low prices often tempt the consumer into unplanned purchasing. And buying more items means spending more, rather than making savings.

Consequently, this bargain mentality means that all types of customers are hunting for a discount, with constant promotions offered by the major Australian retailers conditioning consumers to 'hold out' for a bargain. The lengths customers are prepared to go to obtain a discount are extraordinary, hence why the sometimes remoteness of factory outlet centres are not a hindrance to their popularity and success.

As a result, full priced retailers are being forced into price wars by fierce competition ensuing from the invasion of factory outlets (Burke and Carson, 2006). Therefore, some retailers who operate factory outlets as well as full priced stores are integrating full priced stock into their outlet store. This allows them to capitalise on the increased foot traffic and 'spending mindset' of consumers in such centres, and in some such instances, counter the cost-cutting practices that can erode profit in their full price stores. The Homebush Direct Factory Outlet (DFO) centre in Sydney has come under recent scrutiny for practicing exactly this, with retailers complaining that the centre has an unfair advantage over more established retail sites. This is largely because retailers operating in a factory outlet can yield a higher gross profit dollar against cheaper rents if they can sell full price stock in this environment (Dick, 2004).

### **The development of the factory outlet**

The factory outlet concept was traditionally utilised to clear surplus stock and faulty goods at heavily discounted prices, with the discounted price essentially achieved through eliminating the middle man (the retailer), enabling the manufacturer to pass on savings to the consumer. This discounting practice was mainly for the benefit of employees, in the form of 'sample sales', but reached consumers in the 1970s. Factory outlets offered manufacturers an attractive way to dispose of excess stock, rather than relying on department stores to clear it. Furthermore, factory outlets were a great way for manufacturers to segment their market, capturing price conscious buyers without cannibalising the higher margin sales going through department stores, and hopefully without damaging the image of their brands (Lombart, 2004).

The factory outlet had its origins in the US, however after increasing competition from a variety of retail formats and the maturity of the factory outlet centre concept, developers were forced to seek opportunities to apply this successful format in foreign markets earlier than originally intended. The UK was considered an attractive initial target market by developers and now boasts the most factory outlet centres in Europe. The third wave of development was in Europe, mainly in Germany, Italy, Spain, Switzerland, France and Belgium (Lombart, 2004).

Compared to the US and Europe, the factory outlet format is relatively new to the Australian environment. The first outlet to open was the DFO in Moorabbin in 1997, attracting over 2.5 million customers and turning over in excess of \$100 million in its first year. Since that time,

the outlet scene has developed quickly with Austexx and Brand Smart opening centres in nearly every state across the country.

### **The debate against factory outlets**

Many major factory outlets are located on airport land, leading competing retailers to object over its lax zoning restrictions. Federal government land such as this is exempt from council zoning laws and once the factory outlet has been established in this space, it can charge tenants reduced rental rates, again savings that can be passed onto the customer via discounted merchandise. Some recent reports are also questioning the discounting at outlet stores; one recent study found that almost 75 percent of one outlet was stocked with full-priced garments and those items that were discounted were found to be several seasons out of date (Stensholt, 2004; Craig, 2007; Wright, 2007).

Whilst continual growth in the retail sector is positive for the economy in general, many shopping centres and retailers are opposing the increased presence of factory outlets. The battle between the factory outlet and the shopping centre has led to court action over zoning permits. For instance, Westfield lodged several appeals against DFO developer, Austexx, and in 2004 the group successfully contributed to the closure of the Orange Grove centre. The centre was closed after government intervention into zoning allowances found that the centre was not built on correctly zoned land. A spokesperson for Westfield claims that they will continue to take action against factory outlet centre developers given the uneven playing field.

Many centres are siding with Westfield claiming the factory outlet is diluting the shopping dollar and re-establishing the need for a bargain in the eyes of consumers. Figures from 2004 estimate that about 10 percent of shopping centre turnover is leached out by factory outlets (Chong 2004), and with the growth in the number of outlets since 2004 this figure may in fact be much higher today.

Austexx' Homebush factory outlet has suffered a recent dismissal of an extension application after it was feared further redevelopment would be a blight on the retail environment. Austexx argued that factory outlet retailing is a different type of retailing altogether and should be allowed to operate and expand accordingly, in industrial areas to minimise any adverse affects on mainstream retailers. The judge ruled that the proliferation of the factory outlet gives rise to further investigation into zoning allowances as current outlet centres are very similar to mainstream shopping centres (investing in eatery and entertainment precincts) and

should be located in retail districts with public transport access. This court battle came soon after the Strathpine City Council, in conjunction with lobbying from Westfield, AMP and Centro – all of whom run shopping centres in the surrounding areas – successfully opposed the development of a DFO site in their area (Nixon, 2006).

In another hotly contested debate, Austexx abandoned plans to develop a DFO site at the Hobart Airport. The plans for the \$100 million development had been altered by the Government and Austexx could not accept the 44 percent reduction in size recommended. Austexx planned to develop a 18,000 sqm 100 store DFO centre, a homemaker centre and hardware centre, along with a 2000 spot car park. With the proposed smaller space of a net lettable area of 10,000 sqm, Austexx maintained that this was not sufficient to provide for a successful format for DFO and, as such, chose to abandon the project.

### **The future....**

Despite continual opposition from traditional retail developers, expansion of the factory outlet format is not likely to stop. In fact, Austexx has many more outlets planned, while rival developer, Brand Smart, currently has three Harbour Town complexes with one more planned for the Melbourne Docklands precinct in 2008. The implications for retailers within traditional centres is that a reliance on entertainment and food precincts, service and atmospherics can no longer be the differentiating factor, as factory outlet's have their own hybrid format that includes many of these facilities, and the distinction between the two formats is becoming less apparent.

Despite fears of oversupply, there remains a strong investor interest in developing factory outlet centres. Airports, existing retail sites that offer further development potential or are under-utilised, and tourist destinations are the most sought after spaces. Unfortunately developers will always have to contend with the possibility that a new outlet centre is likely to impact on other shopping centres within the same trading zone, including both conventional retail centres and competing outlet centres. And while retailers are fiercely fighting for the precious retail dollar, there will be no resolution between the two parties. Although there is competitive resistance to factory outlets, the international spread of the format indicates that consumer demand will continue to drive their production.

Factory outlets will not be without challenge, as product sectors blur and consumers increasingly value convenience, all retailers will be forced to adapt their offering to meet the ever-changing consumer needs.

### About the author

Alana Jones is a recent Monash Retail Management graduate who works at the Centre as a Research Analyst. She brings with her over three years of shopfloor retail experience where she was exposed to a broad range of issues faced by Australian retailers. She has also worked as a Stock Analyst within one of Australia's largest retail organisations. New retail formats and consumers' adoption of them is of particular interest to her.



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The Australian Centre for Retail Studies provides research driven education to those involved in the retail sector through broad based research and information generation, management education programs and the promotion of retailing as a career.

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## Enquiries

Please contact us if you have any enquiries about Retail Therapy or the centre itself. Also if you would like further information about this paper or contributing please feel free to contact **Jeff Rogut**.

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