Diversity and Innovation

for Australian Wool

Report of the Wool Industry Future Directions Task Force

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The Wool Taskforce

Australian Wool Industry
Future Directions Task Force

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30 June 1999

Hon Mark Vaile MP
Minister for Agriculture, Fisheries and Forestry
Parliament House
CANBERRA ACT 2601

Dear Minister

The Wool Industry Future Directions Task Force has pleasure in presenting its report.

The difficulties facing all businesses involved in the production and processing of wool, both in Australia and overseas, are well known. For many woolgrowers, prices have been too low to keep them profitable or in business. Productivity growth of many woolgrowing businesses has been poor, and some are too small to be economic.

For some these recommendations may seem to be very tough, but the Task Force felt it was very important to spell out the options quite clearly. The first 9 recommendations address wool growers business problems in some detail.

The Task Force has no magic answers or overnight miracles, but does see many opportunities for individual woolgrowers to take initiatives which may materially improve their economic position.

The Task Force has also recommended a new innovation and implementation organisation, a commercial company, which, from 1 July 2000, would take over from AWRAP and The Woolmark Company. We have designated this company “Australian Wool Services”, although its actual name will be determined by the company itself. It would have a simple mission statement: “to commission wool innovation and to commercialise the results, for the maximum benefit of members/shareholders”. Woolgrowers would pay a declining levy and receive shares in Australian Wool Services.

They would receive these shares on the basis of 1 share per $100 of grower levy paid between the 1 July 1999 and 30 June 2000.

The board of the company would prepare a prospectus or business plan for the company’s future operation which would be the basis of a shareholder vote no later than 31 March 2001. The vote would determine whether the company continued, converted to a much smaller R&D only organisation, was completely privatised (no compulsory levies at all) or was wound up.

Because of the tight timetable proposed, it is imperative that the new board be appointed without delay – by 1 January 2000. This may precede the legislation for Australian Wool Serices itself, so the board should, as an interim arrangement, become the AWRAP board.

Two other recommendations involving the Government are:

- legislation to create a “truth in labelling” requirement for all Australian wool; and
- an allocation of funds from the textile, clothing and footwear Strategic Investment Program, to optimise future development of innovative products derived from wool, fully consistent with the objectives enunciated by the Government.

I believe there has been ample opportunity for consultation and the expression of woolgrower views during the Task Force process.

In commending the report to you, I strongly urge that early decisions be made on the report’s recommendations, and that it not languish for a further extended consultation period. The need for quick responses to the problems facing woolgrowers is obvious.

If these recommendations are carried out by Government, by the new board, but more importantly by the growers themselves, more wool businesses will have a profitable future.

Yours sincerely

Ian McLachlan AO
Chairman

Contents

There are no

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and there are

no messiahs...

Foreword

This report is essentially written for Australian woolgrowers. It came about because, in November 1998, woolgrowers passed a vote of no confidence in the organisation (the Australian Wool Research and Promotion Organisation, AWRAP) to which they pay substantial compulsory levies, and which exists to manage research and development (R&D) and promotion on their behalf. The Minister, as required under the legislation, then dismissed the board and established the Wool Industry Future Directions Task Force.

The terms of reference required the Task Force to address five questions:

- what affects the competitiveness of wool as a textile fibre?;
- how can the performance and profitability of wool businesses be improved, both at home and overseas?;
- how can the performance of Australian wool and wool products in international textile markets be improved?;
- are there better ways to fund and administer wool research and promotion?; and
- how appropriate are the existing institutional and statutory arrangements?

The Task Force saw its fundamental objective as ensuring that wool businesses – those who are or wish to become business oriented, **professional woolgrowers** – are given the best opportunity possible to be profitable on a sustainable basis.

The report is not written to let people down gently. The problems facing woolgrowers are very serious and they affect thousands of families and businesses throughout Australia. The Task Force has tried to tell the story as it sees it, so that realities can be confronted.

The Task Force comprised a group of leading professionals, mainly – and intentionally – drawn from a non-wool background. It received input from anyone willing to put pen to paper, use the Internet, come to a meeting, or pick up a telephone. Over 650 formal submissions were received. The Task Force expresses its sincere thanks to all those people – and for the goodwill with which many constructive proposals were put forward. The Task Force interviewed over 260 people in Australia and 120 people overseas.

There are no magic puddings and there are no messiahs.

But there are a number of crucial messages to be heeded, and future directions to be taken. Most require absolutely vital decisions by woolgrowers themselves. Some involve changes which Governments should make.

The central message for woolgrowers and other wool businesses is this: "there is nobody out there to save you; but there are ways you can save yourself – if you are sufficiently determined, resourceful, flexible and innovative".

The Task Force has endeavoured to put woolgrowers in charge of their businesses and of the new collective institution (via shares) which it is recommending be established. The recommendations have been written in such a way that **diversity, innovation**, the **implementation** of innovation, and **customer servicing** are the major thrusts.

The Task Force considers that if these activities are done well, then those that do them well can look forward to success, in wool as in any other field of endeavour.

There needs to be a

fundamental cultural

and

attitudinal shift

among woolgrowers...

Executive Summary

1. Which Way for Wool?

To paraphrase a well known advertisement, "wools ain't wools". There really is no such thing as "**the** wool industry" and no single solution that suits everyone. Rather, there is a wide diversity of businesses involved in producing or processing wool, with differing objectives, handling quite different products for quite different markets and end uses. Some are currently operating profitably, others are unprofitable, have been so for some time and are struggling to survive. Others again have already lost that struggle and have gone out of wool – or out of business.

So, while it does not apply to all, many wool businesses in all parts of the supply chain are facing crucial decisions about their future. They can confront the challenges and turn them to advantage, or make their minds up now to move on. The Task Force report is designed to help wool businesses in making those decisions.

The Task Force considers there are four threshold issues which underpin the specific conclusions and recommendations which follow.

First, there needs to be a fundamental cultural and attitudinal shift among woolgrowers. Woolgrowers have delegated responsibility for key activities – R&D, promotion and at times marketing/market support – to centralised agencies. These agencies have been expected to solve each and every problem and woolgrowers have tended to look for someone to blame when things have gone wrong. Many decisions have been politicised. A collective mind-set still persists in many of the submissions received by the Task Force.

It must change. Woolgrowers individually must take responsibility for their business and for their fibre. The mind-set must shift from "they or them" to "I/me "or" we/us".

Second, the diversity in wool should be celebrated, not lamented. For too long, the focus has been on "the wool industry" and what "it" should do. This "one size fits all" attitude has worked against successful outcomes. It has led to consensus decision making, politically not commercially driven agendas, lowest common denominator outcomes, interminable delays in progressing reform, and generally an FAQ (fair average quality) culture and, much of the time, an FAQ product. When the collective decisions have been wrong – as with the reserve price scheme (RPS) – the consequences have been catastrophic for everyone.

Third, wool's future success depends critically on continual innovation – and its quick implementation. Today's market place is dynamic and constantly evolving. Today's consumers face a vast array of choices, demand ever higher quality, and regularly seek new angles on products and styles. If wool businesses are to survive, they need to be responsive to these swings of fashion – quickly correcting existing deficiencies, and developing new ways of satisfying consumers. Wool's competitiveness has been declining; it must improve.

Fourth, government intervention in the commercial market place should only be in response to a demonstrated "market failure". For the most part, wool businesses, from farm to retail, operate in a competitive open market. The market place facilitates entrepreneurial activity and is clinical in rewarding success and penalising poor decisions. Sometimes markets do fail, as when individuals or groups judge they cannot capture sufficient benefits for themselves to justify an investment. Where market failure can be clearly established, some form of compulsory action may be justified. Market failure is integral to the Commonwealth Government's principles for compulsory industry taxes and levies. Even so, woolgrowers should be able to vote on what is done.

If these four threshold conclusions can be followed, the Task Force considers that professional woolgrowing and other wool businesses can have a sound future.

2. The State of Wool Demand

In recent years, weak demand has created unprofitability for a majority of wool-dependent businesses. There are still high stocks of some types of wool at various stages in the pipeline: on farm, in brokers' stores, the remaining RPS stockpile, tops, yarn and fabric. These stocks add to price pressures, but the main reason why prices are depressed is that demand is weak, in part because demand patterns have shifted. Many woolgrowers do not fully appreciate what has occurred.

Cyclical

When economies are not growing – for example, following the Asian financial crisis – consumers lack confidence to buy garments. When economic growth recovers, a pick up in wool demand can be expected, as indicated by recent consumption trends in the United States.

Structural

Deeper-seated changes affect wool demand, such as reductions in clothing expenditure, or competition for the consumer's dollar from computers or various forms of entertainment. The military's demand for wool, once important, is not currently a significant factor. Air conditioning means lighter weight clothing and thus less wool consumed per garment.

Consumer attitudes and wool fibre deficiencies

Wool's competitive position continues to weaken. Some traditional attributes are less well recognised by today's consumers – who, in any case, mainly purchase products, styles and colours or brands, rather than a specific fibre. To some consumers, wool is perceived as old fashioned – especially in an era of more casual clothing. In many of its markets, wool is no longer "special".

Wool demand has not been helped by fibre deficiencies – especially the presence of contaminating or coarse wool fibres which are "prickly" against the skin, or difficulties in machine washability and garment care.

Reserve Price Scheme legacy

The direct and indirect effects of the 1991 collapse of the RPS continue to haunt wool textile businesses and woolgrowers. Whatever the rights or wrongs of what occurred, the fact remains that the RPS caused catastrophic damage to wool businesses all along the chain.

Artificial fibre competition

Wool's competitors, especially artificial fibres, continue to make significant improvements in quality, performance and price, in part by imitating the attributes of natural fibres, making life harder for wool. The latest are Shingosen (ultrafine polyester fibres designed to mimic all of the benefits of wool) and there is also some repackaging (and sometimes renaming) of older artificial fibres.

It is one of life's paradoxes that today's consumers, environmentally sensitive as never before, continue to regard fibres derived from the oil industry with apparent equanimity.

Conclusion

The conclusion which the Task Force draws from all this is unambiguous: **the world does not need wool.** Notwithstanding this reality **the challenge is to make wool a desired and preferred fibre.** It is a daunting challenge but by no means a forlorn one.

3. Woolgrower Profitability

Australian woolgrowers are aware of these difficulties, although the severity of the shift in wool demand is not fully appreciated by everyone. Already, many have voted with their feet in response to unprofitability resulting from low prices relative to costs.

Some have adjusted into alternative enterprises which appear to offer sounder prospects. This is as it should be, and forms part of the continuing evolution of Australian agriculture as it strives for viability in the face of global competitive pressures. Others have left agricultural production altogether.

The number of sheep in Australia has declined by over 50 million – or around 30 percent – since 1991, and the number of woolgrowers by 20 percent over the same period.

The brutal reality is that too many woolgrowers have been too unproductive for too long. On-farm productivity of woolgrowing compares poorly with a number of other agricultural enterprises, such as grain, dairy, cotton and grapes, which have chalked up impressive improvements in recent years.

The reasons why woolgrower productivity has lagged are complex. However, one contributor was the RPS; it induced a false sense of security among woolgrowers. Believing that price stability had been assured, woolgrowers responded to a market message of "increase wool production" – not "become more efficient", or "increase productivity", or "improve quality", or "get closer to the customer", "or eliminate deficiencies in the fibre".

That era has passed forever, and woolgrowers must recognise they have considerable catching up to do – and not much time in which to do it.

A related factor is that many woolgrowers remain optimistic that prices will recover to profitable levels "because we have seen similar cycles before". Prices may recover or they may not. The long term trend of real wool prices is down. Some markets seem to have changed permanently. If complacent optimism was ever justified in the past, it is not now.

It is clear to the Task Force that a significant number of woolgrowers will struggle to be profitable even at wool prices somewhat higher than at present. The Task Force is not prescriptive in the sense of suggesting how many may cease woolgrowing over what time period. Circumstances differ, and people's objectives differ. Rather, the Task Force considers it should lay out the facts as it sees them, so that individual woolgrowing businesses – and the families that depend on them – can make their own decisions.

The average woolgrowing business owns less than 3000 sheep. The smallest 30 percent produce a mere 5 percent of total wool production; the smallest 63 percent, just 25 percent. These figures underscore the extent of adjustment ahead, as 3000 sheep are not sufficient for a viable enterprise in the overwhelming majority of situations.

At the other end of the scale, the largest 10 percent of woolgrowing businesses produce nearly 40 percent of the national clip. More important than sheer size is performance. **The "top" 20 percent of woolgrowers in terms of performance (which are not necessarily the largest) earn rates of return three times the average. These woolgrowers continue to be profitable even at current low prices.**

At the wool production level, this report is directed at business oriented **"professional woolgrowers"** – in other words, businesses (whether specialist wool-only enterprises or mixed farming enterprises) that are serious about long term profitability from wool, rather than businesses in which wool is a side line, where the sheep are used for weed control on cereal farms, or prime lamb production.

As the supply "factories" to the global wool textile industry, the principal role of woolgrowing businesses must be to present a consistent, quality fibre to the wool textile chain at a competitive price.

4. The Wool Pipeline

Wool is a more expensive fibre than its principal competitors, cotton and polyester, the price ratio being about 3:1. It is also more expensive to process, again about 3:1 until the yarn stage. Some of the reasons are intrinsic (for example the nature of the respective production "factories" or the need for wool scouring), others reflect the technology currently employed (for instance slower ring spinning for wool, compared with rotor or roller jet spinning for cotton or polyester), while others reflect historical practices which may no longer be appropriate (for example cleaning up uneccessary contamination, or expensive price discovery mechanisms).

At the same time, costs need not be everything. Price premiums can be sustained in the face of cost disadvantages if, and only if, quality attributes are relevant and sufficiently well recognised by consumers. But quality and price premiums are rarely permanent. In particular, the potential threat to wool posed by ultrafine fibres and fabrics must be clearly understood by woolgrowers.

There is an urgent need to eliminate unnecessary costs from the wool textile pipeline, starting with the impact of contamination which could be costing as much as $100 million annually. In addition, a more competitive and pro-innovation environment will be conducive to further cost reductions throughout the processing chain, especially involving the transport, handling and selling of greasy wool in Australia.

5. The Conduct of R&D and Promotion

For many years woolgrowers have accepted the need to raise funds via compulsory levy for the collective conduct of R&D and promotion.

Since 1936-37, when these levies commenced, woolgrowers have contributed $309 million for R&D and $2 billion for promotion – or $4.7 billion in total if measured in today's dollar values. The Commonwealth Government has contributed a further $342 million for R&D and $618 million for promotion – or $2.8 billion in today's dollars. (An additional $3.3 billion – or $5.2 billion in today's dollars – were contributed by woolgrowers for marketing support, as part of the RPS). **The total of these contributions (in today's dollars) is a staggering $12.6 billion.**

On the R&D side, the justification for compulsory levies has been "market failure": that is, in the absence of compulsory levies, insufficient voluntary R&D would have been conducted from the viewpoint of woolgrowers and processors overall. Promotion was considered essential to ensure consumer awareness of wool products and their attributes, encourage key processors and decision makers to choose wool in their product ranges, convey the results of wool fibre research to potential users, and combat the activities of huge corporate manufacturers of artificial fibres.

Government contributions have been made for several reasons – a desire to reap a general community benefit from research, a recognition of wool's disadvantages resulting from manufacturing industry protection (the so-called "tariff compensation" argument) and, in the case of promotion assistance, simply the outcome of the political process.

The centre-piece of wool promotion since the late 1960s has been the Woolmark symbol which, backed by extensive advertising, achieved widespread consumer recognition, especially in an era before the dominance of major corporate brands.

Notwithstanding these massive financial commitments, the competitiveness of the wool fibre has fallen significantly. A number of previous reports into wool promotion have queried its effectiveness, when measured against the appropriate benchmark of woolgrower benefits relative to the outlays. This particularly applies to generic consumer advertising.

Concern over the effectiveness – and even appropriateness – of compulsorily funded promotion and R&D was mainly behind the no confidence motion in November 1998.

The Task Force examined AWRAP's R&D program and the Woolmark Company's promotion activities. It also reviewed a wide range of external reports, and spoke to many people on the subject. Moreover, many of the submissions addressed these issues.

As a result, the Task Force was able to draw a number of conclusions and develop recommendations which are outlined in the following sections. The Task Force considers there are good reasons for being positive about the future if – and only if – people become more businesslike and professional in managing their woolgrowing and other wool businesses.

In particular, the Task Force is excited by the development of Optim technology via CSIRO – which reduces the wool fibre diameter by 25 percent and adds new lustre. It essentially creates a totally new product from within the same sheep factory and appears to have significant commercial potential.

The viability of

Australian woolgrowing businesses

from now on should essentially be the responsibilty of

owners of those businesses...

1. Responsibilities of Woolgrowers Versus a Collective Organisation

The Task Force has concluded that past reliance by woolgrowers on collective organisations has been excessive. There have been too many of these organisations and structures, some of which have stood in the way of progress rather than facilitating it. In hindsight, they alone could never prevent a decline in the competitiveness of the wool fibre in the global textile market, nor deliver sufficient on-farm productivity growth to offset the effects of reducing wool prices in real terms. The argument that without the collective organisations, the position would have been even worse, is not compelling.

The present situation of wool's competitiveness in the global textile market is extremely serious and, above all else, requires a fundamental change in culture and attitude among woolgrowers.

Task Force Recommendation 1

The viability of Australian woolgrowing businesses from now on should essentially be the responsibility of the owners of those businesses.

That is not to deny that there are circumstances where compulsory, collective action remains desirable and justifiable. This requires an organisation, but one with a totally different structure and mind-set to that which presently operates. The Task Force's recommendations on this matter, which involve the creation of "Australian Wool Services", are set out in Section 16.

Chart 1:

Long Term Real Prices of Wool

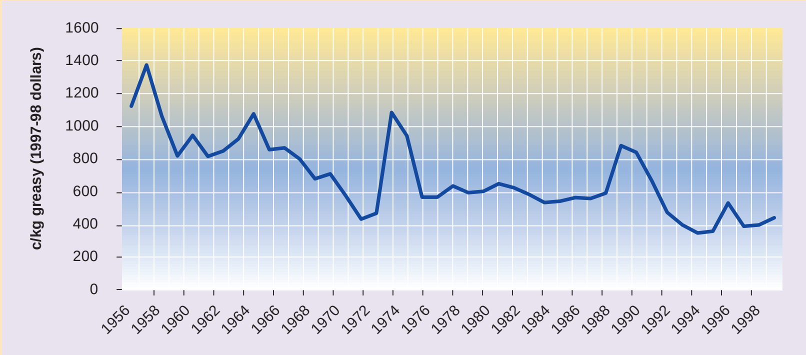


Chart 2:

Real Prices for 19 and 23 Micron Wool

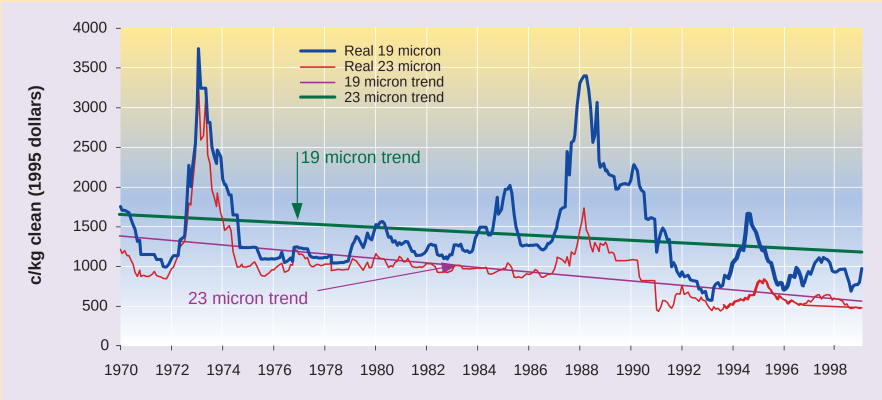


Chart 3:

Wool Prices and Costs of Production

Figure 1

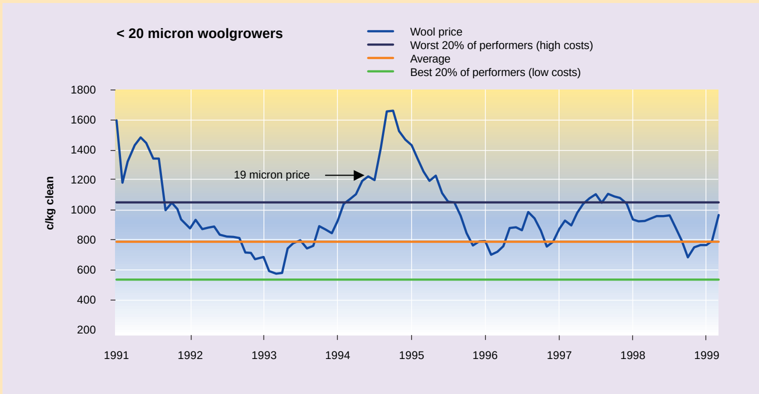


Figure 2

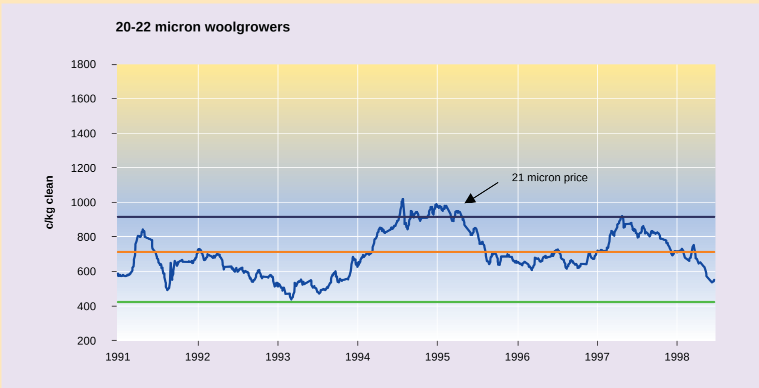
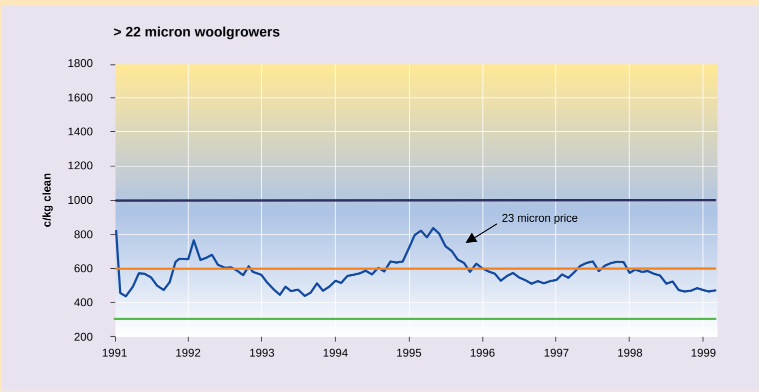


Figure 3



2. Individual Woolgrowing Businesses Must Make Crucial Decisions, and Make Them Now

The charts on the opposite page highlight the seriousness of the predicament facing woolgrowers:

- Chart 1 shows that clean wool prices have fallen steadily in real terms since 1956 – as have most raw material prices;
- Chart 2 shows that the real price of 23 micron wool has been falling twice as fast as 19 micron wool since 1970; and
- Chart 3 shows clean wool prices since 1991 for 19, 21 and 23 micron wool, each overlaid with current costs of production for three performance categories: the "best" 20 percent, the average, and the "worst" 20 percent. It shows that the best woolgrowers are profitable even at current prices, but the worst woolgrowers rarely have been profitable over the past decade.

Conclusion

Whether a woolgrowing business is large or small, wool only or mixed enterprise, the year-in year-out cost of producing a kilogram of clean wool should be at or near to, the "best" 20 percent lines in Chart 3. Chart 3 highlights that most of the responsibility for sustained profitability lies with actions by individual woolgrowers – on their own farms.

Task Force Recommendation 2

All woolgrowing businesses must take one or more of the following actions:

- **increase the revenue from their wool; and/or**
- **reduce the cost of production per kg to that currently being achieved by the best 20 percent of woolgrowing businesses; or**
- **change their enterprise mix or sell the farm.**

An obvious first requirement is that costs of production for each woolgrowing business must be clearly established, if necessary by obtaining professional assistance.

Task Force Recommendation 3

Woolgrowers should participate in benchmarking analysis or best practice groups so that the year-in year-out costs of their businesses are known, can be compared, and opportunities for improvement identified. All costs should be included, including the appropriate allocation of overheads, debt interest payments and an allowance for drought.

The next three sections expand on the three alternative decisions.

Chart 4:
Increasing Wool Value

OBJECTIVE	STRATEGIES	OUTCOME
Join grower marketing groups	• Regional or bloodline based • Investigate marketing initiatives, eg Fibre Direct, SRS, Pooginook, Egelabra etc. • Obtain clearer feedback from processors and the market place	Improve knowledge of wool's intrinsic performance Long term supply contracts
Eliminate contamination of wool	• Wool pack material • Other wool-shed contaminants • Baling twine etc • Stained or dark fibres (wool classing, pre shearing treatment, sheep classing)	Provide a quality guarantee or join a QA scheme that works
Higher processing value or (finer micron) Breed for more wool	• Bloodline/sire selection: use sire reference and Merino Benchmark data • Objective measurement of other known characteristics • Sheep classing on-farm (wool sampling, OFDA, Laserscan measurement etc)	Increase wool value without sacrificing wool cuts or increasing costs of production
Eliminate coarse fibres (initially over 30 microns tender wool)	• Sheep selection (average FD; CV of FD) • Coincide shearing with seasonal break • Investigate new harvesting systems (such as Bioclip)	Test for/display distribution of FD or any other objective measurements at time of sale, to enhance value
Improve risk management	• Understand the use of futures, forward selling, alternative selling systems • Seek appropriate professional advice	Lock in acceptable prices relative to cost of production
Keep on top of research and market data	• Employ farm consultant for benchmarking analysis - adopt "best 20 percent" practices • Read and adopt past research findings where appropriate • Understand market data	Achieve superior performance at all levels

3. Enhancing Woolgrower Profitability: Increasing Revenue

There are many ways individual woolgrowers – or groups of woolgrowers – can enhance profitability by increasing revenue, whether by producing wool more efficiently (per sheep, per hectare or with more sheep) or obtaining higher prices for better prepared or better quality wool. Several options appear in Chart 4 on the opposite page; the list is not exhaustive.

Demand trends are indicating a progressive shift to finer, lighter fabrics, therefore an increasing preference for finer wool. Between 1950 and 1981 there was an average premium of 12 percent for 19 micron wool over 23 micron wool. Between 1981 and 1999 that premium had widened to 36 percent, despite a significant increase in the proportion of the clip 19.5 microns and finer.

Conclusion

Maximising woolgrower revenue requires a professional management and business approach to the entire woolgrowing and farming enterprise. Woolgrowers should utilise competent professional advice, and the array of objective systems now available for breeding **higher value wool** and/or **more wool.**

Task Force Recommendation 4

Woolgrowers must take individual responsibility for the quality and performance of the fibre they produce. They should eliminate all possible fibre deficiencies (especially contamination, certainly black, stained and coarse, and preferably tender, fibres) and give customers confidence that they are delivering a consistent, price competitive, quality textile raw material. They should provide a quality guarantee or join a QA scheme that works.

At present, very few woolgrowers understand what happens to their wool after it is sold, let alone their customer's requirements. Consequently, they are not in a position to service that customer's needs. This needs to change.

Task Force Recommendation 5

Woolgrowers should:

- **adopt commercial business risk management strategies and consider long term supply agreements for at least part of their clip;**
- **communicate effectively with their processor customers, obtaining and responding to feedback; and**
- **seek critical market mass by combining with woolgrowers producing similar wools.**

Chart 5:

Farm Leasing Case Studies:
A Benefit to Lessor and Lessee

Syndicated leasing (WA)

- 11 woolgrowers offered lease of 3100ha, early 1998
- 10 accepted, formed unit trust
- runs 30000 wethers for live export
- participants run more ewes on their farms
- current low wool prices not a detraction

Lessor perspective

- farmer had the opportunity to lease neighbouring farm
- little spare labour and a young family
- so he let another neighbour lease both farms and became the manager of both
- less risk, less stress, higher net return, better lifestyle, more family time

Group farming

- 3 farms combined to optimise cereal machinery purchase, 1979
- now also incorporates merino enterprises
- professional advice established appropriate returns for land, labour and risk capital
- all employees paid commercial rates plus bonuses
- economies of scale, new technology, sound structures, good management and communications

Intergenerational challenge

- farm not large enough for parents plus two sons
- leasing extra land started small, progressively expanded to several farms
- forced sharper management of costs and livestock
- lessors have included a widow, non farming descendants, and urban professionals

Alternative career

- farmer wanted to pursue alternative career
- negotiated a 9 year lease with 2 competent farmers
- lessor has contributed some livestock and new investment for water and fences
- lessees contribute labour for fencing etc
- both parties committed to long term
- now in the fourth year and working well
- lessor will obtain livestock back at the end of the lease

Woolgrower expansion (Eastern States)

- efficient woolgrower wanted to expand
- advertised for suitable properties
- the further afield, the larger the unit would need to be
- 8000-16000 dse's per unit
- no appropriate takers yet!

Leasing common in one WA Shire

- over 30 percent of cleared land in West Arthur Shire leased
- conventional leasing or lease back or share farming
- profitable if lessor has spare labour and plant capacity
- nearly half the 80 members of the Darkan Farm Management Advisory Service lease at least one property

Temporary sheep loan

- woolgrower wanted to crop more land
- so he loaned his young sheep to a neighbour free of charge, to be returned off-shears 12 months later
- lessee derived the wool proceeds, lessor increased crop revenue and obtained adult sheep at the end of the period

4. Enhancing Woolgrower Profitability: Reducing Costs

Woolgrowers need to examine clinically all facets of their cost structures, especially in light of wool's fibre competitiveness and the adverse impact of increasing soil salinity and acidity on much of the land base. The best 20 percent of woolgrowers earn net returns three times the average. Woolgrower average productivity growth in recent years has averaged around 0.5 percent per year, well below the 1.6 percent achieved by beef producers and the 3-4 percent by wheat and cotton farmers.

Task Force Recommendation 6

Woolgrowers should:

- **aim to achieve annual productivity improvements of 3-5 percent, even after they have reached "best 20 percent" cost levels;**
- **assess their overall farming structure and the feasibility of improving land, labour and risk capital productivity via increased purchases or leasing;**
- **improve pasture productivity and pasture management practices; align key sheep events (lambing, shearing) with the annual pattern of pasture production; and**
- **accelerate the rate of genetic improvement, utilising the results of comprehensive analysis now available (for example, Merino benchmark).**

Leasing of land has not been common in Australia (especially Eastern Australia) but it represents an option of potential benefit to both lessor and lessee. The Task Force has found a wide range of leasing situations operating satisfactorily, as Chart 5 on the opposite page describes.

Task Force Recommendation 7

Woolgrowers contemplating expansion of their business, or those wanting to cease woolgrowing, should carefully consider the merits of leasing land (lessor or lessee). In doing so they should seek professional advice on structures and mutual obligations.

The Task Force considers it is not reasonable that the next generation of wool harvesters will want to drag the equivalent of 15 tonnes of sheep each day. New handling and harvesting systems are either here or just around the corner – for example, Bioclip, the SLAMP machine, or others.

Task Force Recommendation 8

Woolgrowers should seek the introduction of new competition into wool harvesting systems so that increased labour flexibility outside the rigidities of the pastoral industry award can deliver cost savings to woolgrowing businesses and improved health to those doing the harvesting.

The maximum bale weight limit of 204 kg – which relates to a now obsolete system of handling bales by trollies in brokers' stores – should be abolished.

5. Facilitating Adjustment

A significant number of woolgrowers are unlikely to make changes sufficiently quickly to ensure adequate profitability from their woolgrowing enterprises.

From every perspective – from a business and economic point of view, from a landcare and animal welfare point of view, but above all from a family point of view – it is desirable that realistic assessments be made promptly by these woolgrowers and their families. Their options are:

- shifting into alternative enterprises – such as other grazing enterprises, cropping, horticulture or growing trees;
- leasing the farm – with alternative employment or retirement; or
- selling the farm.

Selling up involves family structures and questions of location, pride, self-esteem, fear of not finding alternative employment, and the loss of a livelihood and assets which may have been in the family for generations. But delaying the inevitable usually makes the final outcome even more painful.

Task Force Recommendation 9

Woolgrowers facing major adjustment should re-examine Chart 3 and confirm their chances of reaching "best 20 percent" cost levels. Especially where the sale of their farm is in prospect, woolgrowers should seek professional advice promptly, and/or the help of local support groups.

Government adjustment assistance only scratches the surface of the problem and may give false hopes that farming families can tough it out. Although it might not be politically correct to say so, every woolgrowing business encouraged to remain a little longer when its ultimate viability prospects are bleak, represents an expansion opportunity blocked for another business.

Task Force Recommendation 10

Rural adjustment assistance should focus on helping non viable woolgrowers exit their businesses as quickly and painlessly as possible and should not block the adjustment process by providing false hopes, such as interest rate subsidies.

In leasehold title regions, landholder flexibility can be curtailed by legislative restrictions. For example, in the western division of NSW, formal approval is required before a woolgrower can sub-let a property to another woolgrower. A preferable solution would be the freeholding of much of the pastoral leasehold land, subject to certain land use covenants (especially stocking rate limits).

Task Force Recommendation 11

State Governments should remove any remaining obstacles to viable operating structures for woolgrowing businesses on leasehold land, or expedite the conversion of leasehold title to freehold.

6. Truth in Labelling for Australian Wool

It became clear to the Task Force during its consultations that some Australian exporters of greasy wool or tops do not always deliver what the buying order stipulates. Some overseas trading houses do the same. This practice, while obviously not widespread, damages trust and potentially the reputation of all Australian wool. Problems have mainly involved China but have also arisen elsewhere. Use of the new China "model wool contract" should assist to restore trade confidence and trust.

Wine exporters operate an effective "Label Integrity Program" under the auspices of the Wine and Brandy Corporation, ensuring truth in labelling. The scheme provides an associated audit trail. Prosecutions for fraud have been extremely effective.

Conclusion

The practice of not delivering to specification should cease immediately and a simple system that prevents it, or allows complaints to be dealt with effectively, should be put in place.

Task Force Recommendation 12

A truth in labelling scheme should immediately be established by Commonwealth legislation for all Australian wool requiring that:

- **all wool be accurately described as to its known content at the point of export;**
- **relevant test certificates be held by the test house concerned;**
- **a truth in labelling unit within the test house handle complaints; and**
- **the confidentiality of processor intellectual property be safeguarded.**

(Light-weight OPTIM woven fabric)

Chart 6:

Manufacturing Supply Chain Relationships

Defence

"Success in defence contracting depends on the strength of your partnerships. We don't think of ourselves any more as prime contractors but as team leaders. The other members of the team will be large, international, high technology companies or, perhaps, smaller companies with desirable intellectual property or knowledge of particular markets or products. The successful team will be one that is open with each other and shares knowledge and experience as well as having a good understanding of how risk is shared."

Construction

"The construction industry is very competitive. Contractors rely on subcontractors and suppliers to quote them the most competitive price. Contractors still call bids for work or supplies but more often they form long term relationships where prices are set by negotiation and both sides rely on the mutual dependency of the relationship to ensure that each is fair and reasonable. We believe by this means the highest possible standards and quality are achieved."

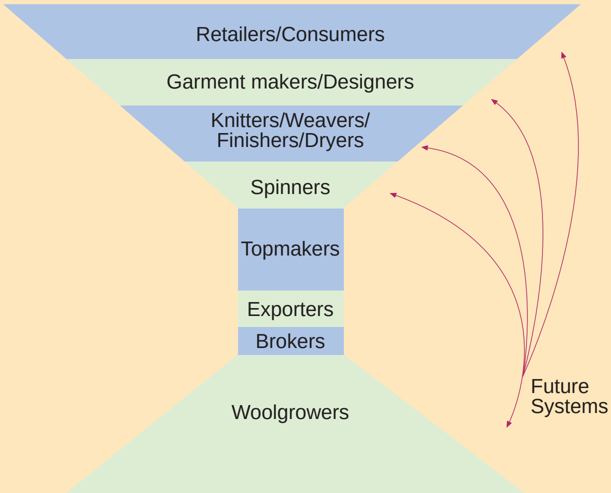
Wine

"In 15 years the Australian wine industry has been transformed from a relatively unsophisticated wine grape supply situation to one where nearly every grapegrower has a contract with a winemaker. The contract may actually specify which label of wine is subsequently produced and from which vineyard block the grapes must be picked. As part of the contract there is a free flow of information between grapegrower and winemaker, for their mutual commercial benefit. The focus is always on achieving greater predictability, quality and consistency, so that new markets can be captured."

Source: Leading CEOs in the respective industries, personal communication.

Chart 7:

The Wool Textile Chain "Wineglass"



7. Improving Woolgrower/Customer Communication

The Task Force has concluded that communication between woolgrowers and their customers is inadequate. The impersonal nature of the auction system is a major impediment although prices, of course, constitute the single most important purchaser feedback – even if the messages they convey are not always palatable.

Most successful manufacturing industries have developed strong supply chain relationships, as Chart 6 describes. Previous buyer/seller conflict and opportunistic trading have given way to mutually dependent long term partnerships. Many woolgrowers are keen to do the same – either individually or, given the realities of size, in groups. Some have started the process. It is made more difficult by the "wineglass" structure of the processing chain, depicted in Chart 7, and will not be achieved without considerable woolgrower effort.

Conclusion

Many topmakers blend "down to a price" – not "up to a quality" – involving batches of up to 1000 farm bales and some cheaper inferior wools. Obviously blending increases the risk of contamination unless great care is taken. Some topmakers seem unwilling or unable to prevent contamination or precisely identify its source. They tend to offset their risks by discounting all wool purchased. Some topmakers, and some spinners, are an obstacle to feedback passing down the chain to woolgrowers from later stage processors, where diversity reappears.

Task Force Recommendation 13

Woolgrowers should consider participating in regional or bloodline marketing groups, or dealing with merchants as in the cotton industry, for the purpose of achieving larger consignments, supply chain relationships, more effective customer feedback and price premiums, assisted by a recognised QA scheme or quality guarantee.

Topmakers should insist on only purchasing quality assured wool to minimise the risk of contamination.

Conclusion

The Woolmark Company has also been a blockage to more effective communication between processors and woolgrowers. It is not geared to service professional woolgrowers effectively. In the past there have been numerous cases, in the Task Force's judgement, where unpalatable messages from processors have not been relayed to woolgrowers for fear of offending them (political versus commercial accountability).

Task Force Recommendation 14

A biennial wool conference should be instituted, to be held in Australia, to give professional woolgrowers, leading wool processors, service providers and researchers around the world the opportunity to exchange views in a way which has never happened before.

8. New Systems of Wool Selling

While the traditional auction system assembles buyers and sellers in one place and time, and arguably produces the best price on the day, it is an impersonal and costly method of price discovery which has been supplanted in many other markets (for example, cotton).

Electronic selling is at the point of being implemented and at last appears to enjoy strong support from woolgrowers, brokers, buyers and processors.

Task Force Recommendation 15

Electronic auction selling should be commenced within the next 2 to 3 months. It should be available to be used by anyone, anywhere in the world, who is able to connect to the system.

Electronic selling would mean completely decentralised selling – and buying. Samples can be displayed and paid for by sellers. Sellers would have the opportunity to display all available data on their wool – again at their cost – which would help to break down the FAQ mentality of the past.

The market place should determine which systems of wool selling – traditional auction, electronic auction, electronic offer boards, private treaty, tendering, direct consignment, or long term supply agreements – should prosper. What is required is a fully competitive environment where new ideas can be trialled commercially – and promptly.

Task Force Recommendation 16

Associated electronic offer boards – where tested wools are available for sale to the world on a 24 hour a day 7 day a week basis to any purchaser, subject to woolgrower reserves – should be implemented without delay.

The Australian Wool Exchange (AWEX) was established after the demise of the Australian Wool Corporation (AWC) to supervise the orderly operation of auctions, provision of market information and development of QA standards. It has come to see itself as a "business" in its own right, rather than just as a facilitator. Its desire to control the introduction of electronic selling – and receive a revenue stream in the process – is an example.

Conclusion

Instead of being a catalyst for reform, AWEX has become an inhibitor. Its centralised role is superfluous, especially with electronic trading.

Task Force Recommendation 17

AWEX should be disbanded and its functions assumed by whatever voluntary groupings of market participants emerge.

If this does not happen quickly, the Australian Competition and Consumer Commission (ACCC) should rescind the authorisation which exempts AWEX from the normal provisions of the Trade Practices Act, and/or the Competition Tribunal should uphold the appeal to the decision which is pending.

9. Australian Wool Testing Authority

AWTA has been a valuable organisation serving woolgrowers and wool processors in Australia and overseas. Its professionalism and the consistency of its test results enjoy a wide international reputation. It has done a commendable job in promoting testing of length and strength and developing a practical, workable electronic selling system. It has now also pledged explicit technical support to the developers of the OFDA 2000 machine.

However, its status as a tax exempt, non profit company, limited by guarantee and without a permanent share capital, has helped it see off several would-be competitors. In practice, if not in theory, it is a monopoly service provider. The Task Force has concluded that AWTA has:

- been reliant on the Airflow fibre diameter testing technology for too long;
- been slow in encouraging new testing machines (such as Laserscan) or the testing of new fibre characteristics (such as percentage of fibres over 30 microns, or curvature); and
- built up excessive reserves (over $61 million as at June 1998) which ensures that competitors will be defeated and which the Task Force considers could be better used for the benefit of woolgrowers (who paid most but not all of the charges creating these reserves).

Task Force Recommendation 18

The new ATWA should become a conventional company with its shares owned by woolgrowers via Australian Wool Services

This may be acheived in two ways. The directors of AWTA should approve the transfer of the assets and undertaking of the business to Australian Wool Services (Section 16) for a nominal consideration, subject to appropriate legal and taxation advice. Alternatively, AWTA should be demutualised by the issue of permanent share capital to members; following demutualisation, there should be a placement of ordinary shares to Australian Wool Services for a nominal consideration, the purpose of which would be effectively to transfer ownership of the restructured AWTA to Australian Wool Services. These changes should take effect from 1 July 2000.

Task Force Recommendation 19

AWTA should play a more explicit catalytic role, encouraging the adoption of new technology in testing and related areas. This may include electronic selling and the introduction of on-farm testing, first via the issuing of guidance certificates and ultimately an effective and practical on-farm certification scheme. This should facilitate the electronic sale of wool while it is still in the shed, a logical and desirable development which would enhance woolgrower selling strength and in turn enable more efficient transport at the buyer’s direction.

AWTA should also be involved in operating the truth in labelling scheme (Recommendation 12).

10. Reserve Price Schemes

The Task Force was surprised that a number of woolgrower submissions – though a small minority overall – advocated the return of some form of RPS. To most of these woolgrowers, the concept was not wrong, merely its execution during the late 1980s. With clearer safeguards, they felt a revised RPS scheme could work effectively in future.

The main argument advanced in support of an RPS was its capacity to deliver relative price stability, of benefit to both woolgrowers and processors. To the extent that they think this is a desired objective, it should be pursued by woolgrowers themselves through normal market mechanisms, principally the use of risk management tools or long term supply contracting.

In case there is any doubt on the matter, the Task Force wishes to be absolutely clear:

Task Force Recommendation 20

Under no circumstances whatsoever should any form of RPS for wool ever be reintroduced in Australia.

11. Trade Policy and Wool

Successive Commonwealth Governments have been at the vanguard of efforts to liberalise world trade, including liberalisation of textile trade barriers. These efforts have been strongly advocated by woolgrowers and are fully endorsed by the Task Force. Bilateral trading initiatives should also be pursued, for example, with China and India.

Unfortunately, the Government itself succumbed to sectional pressures when it opted for a five year tariff pause for local textile, clothing and footwear (TCF) manufacturers. Current Australian tariffs on imported wool products (up to 31 percent) provide powerful ammunition for other countries (such as India) to maintain their own high tariffs, and fend off pressure for reform from Australia's Trade Minister. These overseas tariff barriers disadvantage Australian woolgrowers enormously.

Task Force Recommendation 21

The Commonwealth Government should continue its consistent advocacy of liberalised trade in textile products, and should ensure that domestic TCF tariffs resume their downward path at the end of the five year tariff pause.

China's complex quota system for imported wool deserves particular mention, if only because China is such an important wool customer. The quota scheme creates major uncertainty for Chinese buyers and processors, and Australian woolgrowers and exporters alike. Worse, it prevents some buyers from being knowledgeable about what they should be purchasing. Some Chinese trading houses which receive quota allocations do not help Chinese processors in the pursuit of this knowledge. Electronic trading will provide a wider spread of knowledge.

Ideally, the whole quota scheme should be scrapped, but as a minimum it needs to become more predictable, transparent and less intrusive. Current regulations also make it more difficult for Chinese mills to obtain foreign exchange approval, once import wool quotas have been allocated.

Task Force Recommendation 22

The Commonwealth Government should strongly encourage Chinese authorities to liberalise China's wool quota regime, initially by increasing the proportion of quota allocated directly to mills rather than traders, abolishing quota on re-export wools, providing a full value added tax (VAT) rebate on wool product exports, and accelerating the privatisation of State Owned Enterprises.

12. The Role of Government

Commonwealth and State Governments have been heavily involved in various facets of woolgrowing and marketing over many years. Unfortunately, this heavy involvement has led to politicised decision making, in stark contrast with cotton, for example. Areas of government involvement have included:

- State Governments pursued well intentioned, but ultimately damaging, closer settlement schemes; Commonwealth and State Governments have offered adjustment and drought assistance – with mixed results;
- successive Commonwealth Governments established the RPS, later gave woolgrowers more control in setting the floor price, then abolished the scheme after the stockpile had reached over 4 million bales, and finally made a sequence of major policy changes affecting the manner of the stockpile disposal;
- the Commonwealth Government continues a long-standing policy of matching rural R&D levy expenditure, up to 0.5 percent of gross proceeds, and a wider 125 percent R&D tax deduction to business in general; the Government argues that the whole community benefits from a strong R&D focus and that the support encourages "public good" research which otherwise would not take place to the same degree; and
- for a number of years the Commonwealth Government made significant taxpayer payments for wool promotion.

Task Force Recommendation 23

The Commonwealth Government should continue its matching 0.5 percent contribution for wool R&D.

The Commonwealth Government's $772 million assistance package to coincide with a tariff pause to TCF manufacturers between 2000 and 2005, includes $700 million for a Strategic Investment Program. It is "designed to encourage new investment, R&D, innovative product development and value adding in Australia's TCF manufacturing industries, particularly in those sectors utilising Australia's wool, cotton and leather where we have a significant natural advantage over many of our international competitors". **These objectives are precisely the focus of this report on wool.** However, the Task Force is concerned that excessively detailed rules for the expenditure of the funds might prevent the effective commercialisation of new innovative wool products and development of clusters of wool processing businesses.

Task Force Recommendation 24

To ensure that the Government's TCF assistance objectives of encouraging new investment, innovation and value adding of wool-based processing in Australia are met, a significant portion of funds from the Strategic Investment Program should be allocated to Australian Wool Services. Subject to the appropriate safeguards, the board of the new organisation should be responsible for spending these funds and obtaining the appropriate returns.

13. Value Adding

Despite its wool production advantages, Australia has not developed a competitive wool processing tradition beyond the topmaking stage. The proportion of greasy wool combed in Australia has risen steadily to over 30 percent. However, in the spinning, weaving and knitting sectors, there has been a decline in domestic activity.

The Task Force considers that these later stage processing trends may be about to change:

- Australia's recent low inflation, strong growth performance, and a more cooperative and flexible industrial relations environment, have improved its attractiveness as an investment location;
- Australian business flair is being demonstrated in a growing range of activities – such as software, film making, advertising, wine making, cheese making, and so on;
- there have been a number of niche investments in wool garment-making, some of which are now exporting successfully; several leading Australian fashion designers are winning growing international reputations;
- new machinery and technology have enabled further automation in knitting and garment-making;
- CSIRO has concentrated all its wool processing research facilities in Geelong; and
- the recently opened International Fibre Centre in Geelong is seeking to build on an established cluster of expertise in the region, and enhance a commitment to education and training.

The Task Force has also been made aware of some new commercial interest in value adding investments, including joint ventures between Australian firms and established overseas wool processing expertise. The Task Force is encouraged by this renewed interest because its judgement is that unless a significant proportion of wool can be processed through to the fabric stage in Australia, it will be difficult for woolgrowers to know enough about their product to be other than raw material price takers.

While not drawing too close a parallel, it is worth highlighting the enormous strides taken by winemakers over the past decade or so, reflecting not only Australia's suitable climate for growing grapes, but the application of superior viticultural and wine making technology compared with some of the traditional overseas centres of excellence.

If there is to be a resurgence of commercial wool processing investment in Australia, it will need innovative wool fibre technology, mostly developed by Australian researchers. This underscores the importance of a sufficient allocation of funds from the TCF Strategic Industry Program for wool fibre innovation.

Task Force Recommendation 25

International and domestic investors in wool processing should carefully assess the potential for new value adding investment in Australia which would capitalise on both more commercially focused wool fibre innovation, and an improved overall investment climate.

14. Promotion

Expenditure on promotion has far exceeded expenditure on R&D as far as both woolgrower levies and Government funds are concerned. **Since 1936-37, wool promotion expenditure has amounted to around $6 billion in today's dollar terms.** Having spoken literally to hundreds of people, looked realistically at the options available, and thought hard about the issues, the Task Force has come to a number of conclusions:

- the word "promotion" is confusing in that it covers too many activities and is misinterpreted, especially by woolgrowers; the Task Force prefers the terms "consumer marketing" and "product marketing";
- consumer marketing, especially in mature developed markets, is principally the responsibility of retailers and brand owners; generic symbols like the Woolmark symbol have less relevance than they once had, and the identification of measurable benefits to woolgrowers is difficult to establish; some respected marketers told the Task Force that generic advertising no longer works;
- in any case, Australian woolgrowers these days have nowhere near the financial resources to fund meaningful generic advertising programs throughout the **developed** textile markets of the world; the development of carefully tailored and commercially funded symbols may have applicability in some markets or market segments;
- commercial firms may be able to leverage the existing recognition of the Woolmark symbol – two examples being the Woolmark endorsement given to Procter and Gamble's new home dry cleaning product, Dryel, and the use of the Woolmark by the large Japanese retailer Aoyama on 70 million advertising leaflets distributed to Japanese homes each week;
- in some countries (such as China and, interestingly, the United States where wool consumption has always been low) the Woolmark symbol still makes a positive contribution in denoting quality products; if practical, its use should be confined to products made from Australian wool, now that other countries no longer contribute to its funding; and
- product marketing – that is, among businesses within the wool textile chain – is vital, especially at the designer/garment maker level where fibre choice decisions are made.

Task Force Recommendation 26

Levy-funded generic advertising at woolgrower expense should cease forthwith.

Product marketing is by far the most important marketing responsibility that a new collective organisation should have; "its task is to influence decision makers to use wool", in other words, to commercialise and implement the innovation brought about by R&D.

The word "promotion" should disappear from the lexicon of the new organisation.

15. Research and Development

Innovation into the wool fibre and its processing is **essential** if wool businesses are to catch up and then keep pace with innovation in other textile chains. While it is undoubtedly true that many wool processors conduct their own research and product development, some activities are beyond the scope of individual firms. Moreover, Australian woolgrowers are generally not able to "free-ride" on research conducted in other countries – as Australian cotton growers, for example, can free-ride on United States cotton research.

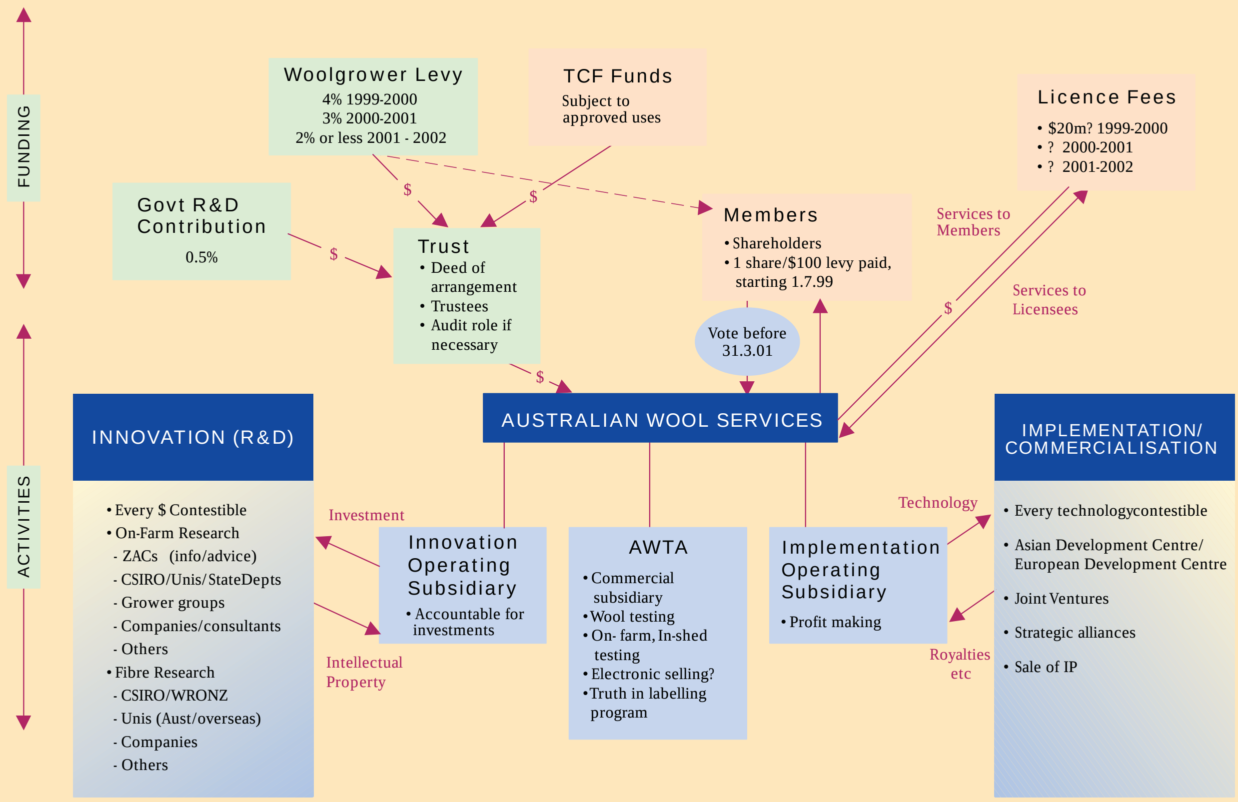
Thus, the Task Force has reached the following conclusions:

- collective R&D continues to be of vital importance, for which a market failure justification remains valid in many, but not all, circumstances;
- it is more likely that the benefits of on-farm R&D can be captured by woolgrowers; the further away from the farm, the more likely it is that the benefits will be shared between other market participants, with obvious implications for funding responsibility;
- on-farm R&D should be focused in areas which have whole of industry benefits rather than geographical single issue solutions;
- a range of off-farm R&D activities, especially those directed at correcting existing deficiencies and enhancing the properties of the wool fibre, is absolutely essential if wool's competitiveness in the textile market is to be enhanced;
- it is not realistic for such projects to be funded only by wool processors, given historical relationships and the current state of wool demand;
- in the past, many collectively-funded R&D projects have been poorly conceived and conducted; some have continued well after the prospects for success have been recognised as low; the ownership of intellectual property resulting from the research has not always been clearly established – it should reside with the research funder;
- the implementation / commercialisation of research results has in most cases been poor, lacking commercial acumen, and thus taking far too long;
- the administration costs of AWRAP / The Woolmark Company are excessive; and
- it will be inappropriate for a new shareholder-owned wool organisation, Australian Wool Services, to part fund industry bodies (AWRAP's 1997-98 funding of the Wool Council was $290,000).

Task Force Recommendation 27

The primary focus of a new collective organisation Australian Wool Services should be on innovation and its implementation.

Chart 8:
Australian Wool Services



16. Australian Wool Services

The Task Force has made important recommendations about woolgrowers' responsibilities for the future of their businesses. However, as noted earlier, there are circumstances where compulsory collective action remains desirable and justifiable. This requires an organisation, but one with a totally different structure and mind-set to that which has operated in the past.

The Task Force has concluded that the Minister should appoint a new board of AWRAP, no later than 1 January 2000, which would have the responsibility of preparing a new organisation – a conventional company which the Task Force is calling "Australian Wool Services Ltd" (the actual name to be determined by the company itself) – and a business plan / prospectus on which woolgrower shareholders would vote, no later than 31 March 2001.

> **Task Force Recommendation 28**
>
> **A new company, Australian Wool Services, should be established to conduct activities appropriately performed by compulsory collective action. It should be structured as a conventional company limited by shares.**
>
> **Members (shareholders) should receive shares reflecting their compulsory levy contributions, commencing from 1 July 1999.**
>
> **During calendar year 2000, the board of the newly formed company – which should be in place by 1 January 2000, initially as the board of AWRAP – should prepare a business plan or prospectus, to be put to a meeting of shareholders (based on shares allocated during the 1999-2000 financial year) no later than 31 March 2001.**
>
> **At that meeting, shareholders will vote on whether to adopt the plan – and thus continue the company in its existing form – or not.**

Chart 8 on the opposite page gives a schematic representation of how Australian Wool Services will be structured and operate.

The company

> **Task Force Recommendation 29**
>
> **While it will be up to the company itself to determine, the Task Force recommends that Australian Wool Services' mission statement should be as follows:**
>
> **"To commission wool innovation and to commercialise the results, for the maximum benefit of members / shareholders.**
>
> **"This will be achieved by:**
>
> - **maximising the value of existing wool intellectual property (IP), including the Woolmark symbol;**
> - **facilitating wool innovation, on a contestible basis, to meet the requirements of the market place; and**
> - **commercialising the intellectual property and innovation via industrial marketing of wool".**

Shares and levy rates

Because of the innovation focus of Australian Wool Services, the Task Force has concluded that no distinction should be made in the levy between R&D and what was previously designated as "promotion". However, the matching 0.5 percent Government contribution must be designated entirely for R&D purposes.

> **Task Force Recommendation 30**
>
> **Shares in Australian Wool Services will be allocated to woolgrowing businesses on the basis of one share per $100 of levy paid. The compulsory levy will remain at 4 percent for 1999-2000 and will drop to 3 percent for 2000-01. The Task Force considers it could drop to 2 percent for 2001-2, but this will depend on the outcome of the shareholder vote.**

Other capital or income

In addition to the woolgrower levy and matching Government R&D levy, Australian Wool Services would derive capital or income from the following sources:

- a significant allocation from the TCF Strategic Industry Program, as set out in Section 12 above;
- licence fee income, relating to the use of a revamped Woolmark and more clearly defined fee-based services, possibly increasing in total amount;
- any assets of AWRAP/The Woolmark Company remaining after it meets contractual obligations, staff redundancy payments, and so on;
- investment income – royalty payments etc – from the implementation of research and innovation;
- other income (interest etc); and
- the net equity residing on the balance sheet of AWTA.

The Trust

Task Force Recommendation 31

In order to cover the situation of a conventional company receiving taxpayer funds and woolgrower levies collected under legislation, a trust will be interposed between the Government source of those funds and Australian Wool Services as the recipient. The trust will operate pursuant to a deed of arrangement with the Government, along similar lines to that of Meat and Livestock Australia Limited.

Importantly, the Trustees of the Trust (who might comprise two or three respected identities from woolgrowing and business circles) will be required to confirm that the funds are expended for approved purposes. Should they have any doubts, future levy or taxpayer funds could be withheld pending a formal audit.

Board tasks

Task Force Recommendation 32

The main tasks of the board will be to:

- **establish the structure, operations and culture of Australian Wool Services as an innovation and implementation company; and**
- **prepare a prospectus or business plan to be put to a vote of shareholders/members not later than 31 March 2001 and on which the future operations of the company would depend.**

Board composition

Task Force Recommendation 33

The board will comprise 10 members – including the Chairman – 3 of whom should have woolgrowing experience with appropriate board level/international experience, 3 having international experience of the wool textile industry, 3 with broad business experience, plus the chief executive. The calibre of board members should be at the highest level, with remuneration recognising their expertise and time commitments. The Board should thus have a cross-section of experience, and a demonstrated track record of commercial success and sound judgement, in areas relating to the company's mission statement, in particular:

- **an understanding of the corporate performance of R&D and innovation;**
- **industrial marketing;**
- **the ability to commercialise the results of innovation;**
- **the changes necessary to produce an appropriate commercial culture within the company; and**
- **international experience.**

Board members would initially be appointed by the Minister, with the assistance of professional advice. Thereafter, election of board members would be a matter for shareholders – like any company – with a proportion coming up for re-election every 12 months in accordance with the Corporations Law. At the first annual meeting (March 2001) the confirmation of all board appointments would be an agenda item.

Transition issues

Considerable changes will be required in the transition from AWRAP and The Woolmark Company to Australian Wool Services. Depending on a full assessment of relevant statutory and commercial obligations, together with legal and taxation issues, AWRAP and the Woolmark Company may become subsidiaries of Australian Wool Services, or have their activities and net assets transerred to it. One vital requirement – to ensure the necessary cultural change occurs – is that there be a spill of all staff positions. A number of existing employees would be likely to be offered employment in Australian Wool Services – indeed, much of the value of the new company will reflect the human capital of key staff. However, nothing should be automatic or guaranteed, and the terms and conditions of employment may be different.

Australian Wool Services will be a considerably leaner organisation than AWRAP / The Woolmark Company. Where it is cost effective to do so, overhead functions (such as finance, human resources, legal etc) should be outsourced, although specific decisions would be made by the new board.

The board should choose the company's name. The Task Force puts forward two names for consideration: Australian Wool Services Ltd and Australian Wool International Ltd.

Innovation operating subsidiary

The subsidiary company responsible for commissioning innovation projects would be accountable for the performance of its contractors. All funds would be fully contestible and information and advice obtained from groups such as Zone Advisory Committees (ZAC) would form a key input to the decision making process. A key requirement would be the need for clear contractual obligations, especially the ownership of intellectual property resulting from the innovation projects – it should reside with Australian Wool Services – and the need for projects to be completed on contract and in a timely manner.

Implementation / commercialisation operating subsidiary

This company would be responsible for the commercialisation of intellectual property generated by innovation investments. Its performance would be assessed in a conventional commercial manner. In commercialising innovations and technology, it may use intermediary organisations in particular countries; these could, for example, comprise former Woolmark Company employees who had a particular knowledge of regional markets and wool processing businesses.

The company would also be responsible for licensee negotiations and servicing. The Task Force sees considerable potential for increased licensee income, provided there is a clearer spelling out of the nature of the services being offered in return for the licence fee. In other words, the licence fee would more closely resemble a commercial fee-for-service activity, in which the Woolmark symbol (appropriately revamped to denote unique quality products derived from Australian wool) and employee or contracted professional expertise (as consultancy advice) would be the main services being provided.

AWTA

As discussed in Section 9 above, AWTA would become a fully owned subsidiary of Australian Wool Services. As well as its traditional wool testing activities, AWTA would have a role in developing an effective system for on-farm or in-shed testing, possibly managing electronic wool selling and handling the truth in labelling program. However, it would not be a monopoly provider of these services.

The prospectus/business plan and vote

The development of the prospectus or business plan would be the principal task to be performed by Australian Wool Services during 2000. It would set out a number of possible scenarios for the future development of the company and these would be voted on by shareholders at the first meeting, to be held no later than 31 March 2001. In particular, the business plan would describe how Australian Wool Services would continue in operation along the lines of the structure set out in Chart 8. An important part of the business plan would be an assessment of the future role and value of the Woolmark symbol in various markets of the world, and its contribution to product marketing in general, and licensees in particular.

Task Force Recommendation 34

There should be sequential questions along the following lines put to shareholders at the March 2001 meeting of Australian Wool Services. Proxies could and would be used by shareholders unable to attend the meeting:

1. **Should there be a compulsory levy of 1 percent for the purpose of conducting R&D, innovation and product marketing.**
   - **only if greater than 50 percent of the total shareholding of Australian Wool Services voted in favour (yes), would the 1 percent levy continue. Otherwise compulsory levies would cease on 30.6.01; the matching Government 0.5 percent levy would also cease; and Australian Wool Services would either continue as a fully privatised company, with tradeable shares (and possible stock exchange listing), able to seek capital from existing or new shareholders as and when it saw fit and eligible for the general 125 percent tax deduction for R&D); or it would be wound up, with any net assets returned to shareholders.**
2. **If the first question has been answered in the affirmative, then Australian Wool Services shareholders would be asked whether there should be an additional compulsory levy of 1 percent (or such other amount as specified in the business plan) to provide funds for the commercialisation of R&D, innovation and product marketing.**
3. **Any other questions put by the Board.**

In practical terms the two questions would be voted on at the same time with shareholders only being required to vote on the second question if they had voted yes to the first question, and so on.