

**A.I. Topper & Co. Pty Ltd - Submission to the Productivity
Commission Inquiry into the Textile Clothing and Footwear and
Leather Industries with Respect to Post 2005 Industry Assistance
Measures**

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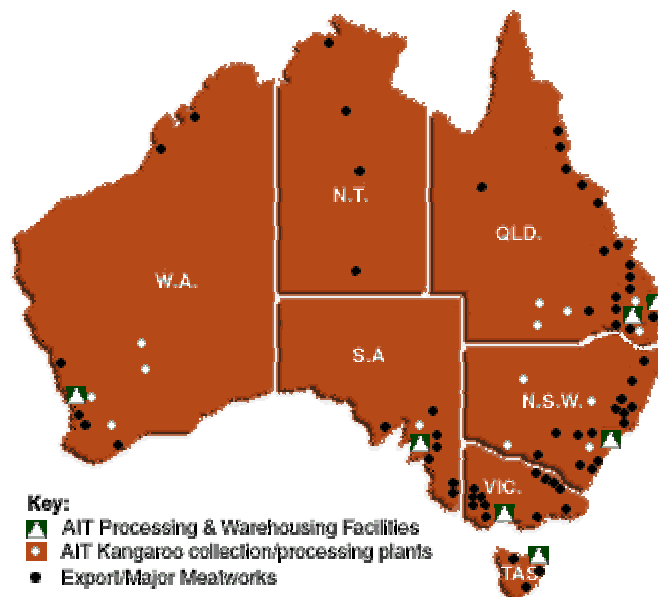
Introduction

Since its foundation in 1954 by Arnold I. Topper, A.I. Topper & Company has grown to become the largest and one of the most respected producers, processors and exporters of raw, semi-processed and finished stocks for hides and skins in Australia.

With the centre of operations located in Sydney, A.I.T. has built up a substantial network of processing divisions in all major hide and skin producing regions – Southern Queensland, Central/Northern NSW, Victoria, South Australia and Western Australia. Each of these production facilities are designed to specialise according to the hides and skins prevalent in each region so that quality across all products is of a consistently high standard. The map below highlights the main A.I.T. warehousing and processing facilities.

A focus on service and flexibility enables A.I.T. to remain highly responsive to customer needs and fluctuating demands. Stringent controls over all aspects of the production process enable A.I.T. to maintain consistently high quality levels, ensuring customer satisfaction.

As the Hide and Skin industry in Australia becomes more rationalised and advanced, there is an increasing emphasis on efficiency and quality in the production process. In line with these changes, A.I.T. devotes considerable time and investment to ensure it remains a leader, not



only in processing and exporting, but also in technological development.

Nature of Submission

This submission is made in writing to the Productivity Commission Inquiry into the Textile Clothing and Footwear and Leather Industries as a record of the views of A.I. Topper & Co Pty Ltd. However, in such a written document it is often difficult to communicate the full meaning and rationale for the views presented. Consequently, **A.I. Topper & Co Pty Ltd**

request that they be granted an audience with the Commission to verbally present the submission more fully and allow for the commission to question them on the industry and its future needs

EXISTING SIP Program Benefits

The existing SIP program has been a misdirected effort by government to stimulate the downstream processing of hides and skins into finished leather. The system aims are admirable in attempting to value add to Australia's raw material, but are founded on a misplaced notion that this development can effectively occur through the artificial financial stimulation of the finished leather making sector in capital investment. The SIP fails to go to the heart of the structural reform needed of improving the supply chain of hides and skins in Australia to the leather makers. The reforms needed are to bring the hide and skin processing sector into a closer alliance with the suppliers of the raw materials, the meatworks.

As a consequence of not having brought the supply chain into the consideration of the TCF SIP, the program has failed by not addressing the key issue of raw material supply.

Productivity Commission Terms of Reference Items

- 1. Evaluation of Current TCF Assistance Arrangements:- Comment on the effectiveness, efficiency and appropriateness of current assistance programs such as SIP in meeting the Government's goal of achieving structural change and a more internationally competitive TCF sector by 2005, including a consideration of outcomes at the company level. Comment on minimum expenditure threshold and accumulation time frame (currently \$200,000 and 5 years) program flexibility/rigidity, stimulus to innovation and investment, should leather industries be included in considerations of the TCF industries or as a meat co-product industry or as a leather and leather goods industry in its own right; has the SIP program stimulated industry structural change and enhanced companies capacity to be internationally competitive, eligible and non eligible grant activities etc.*

The Australian production of hides and skins is quite varied in size, type, and quality across the country. A tanner is usually seeking a particular size, type, quality, and volume to satisfy its own specific leather requirements. However, with the current system, where tanners purchase hides from a meatworks they are forced to accept a number of hides in their purchase that is outside their required specification. This has a depressing effect on any margins the tanners may be able to make.

The Meatworks, virtually by definition are the primary providers of the raw materials to the Australian hide and skin industry. The price they receive is determined by a number of factors including:

- world market prices for hides and skins,
- exchange rates,
- extent of competition between domestic hide and skin processors,
- Availability of hides and skins to domestic processors
- mix of hide and skin types, size, quality, and volume in the offering,

- processing capacity of domestic hide and skin processors,
- sale mix to domestic or export
- geographic locations of the meatworks to the hide and skin processors,
- cost of freight, and
- cost of processing as short term preservation, brine curing, and tanning.

Traditionally prices for meatworks have always been strong due to large number of domestic processors and processing capacity.

The result is that whilst the extent of competition in the industry is fierce, it places on-costs at the meatworks gate of between \$10 –\$15 per hide depending on how the hide is to be processed.

Hide and skin processors, including tanners and finished leather producers have to contend with the above unnecessary on-costs which render the Australian tanning and finished leather producers uncompetitive. The SIP scheme at this point in time has not addressed the removal of these on-costs and should be altered in order to do so.

The state of the industry has not further developed to significantly change the degree of value adding to Australia's raw materials of hide and skins through the SIP. The same players still exist, assisted by financial government stimulus, and those that have not been assisted by the SIP continue to exist and outperform those obtaining the current SIP benefits. Surely this illustrates to government that a portion of SIP funds are being misdirected.

The hide and skin processing industry needs to be seen as part of the supply chain from the meatworks through to finished leather goods - an integral link in the supply chain.

2. Assess Leather Industry Long term Viability and Outcomes of TCF Policy and its Implementation on the Future Leather industry in Australia

The mere use of the term “leather industry” tends to ignore the fact that not all hides and skins produced in Australia are suited for processing into leather within Australia in market terms. The use of the term “leather industry” is a structural impediment in its own right because it can create a mindset of leather being the only hide and skin product that is exported from Australia, which is contrary to the reality in the marketplace. Figures of export volumes of hides, skins, and leather show this.

Use of the term hide and skin processors to include all potential stages in the supply chain is more appropriate as it includes brine curers, tanners, and finished leather producers.

2a) Identify and analyse major impediments to long-term viability of the leather industries. These would include factors such as cost structures, and market and firm characteristics such as import competition, corporate structure, existence of critical mass, management and workforce skills, the purchasing strategies of major retailers, the ability of the sector to attract investment, and international trading arrangements including market access issues.

The cost structures of the existing supply chain to the hide and skin processors demonstrate a sub optimal supply chain structure. It means that firms pay for some material that they don't want, depressing the average price paid and incurring significant on-costs in transporting and processing hides and skins that were not required.

One of the major impediments in the long-term market development of finished leather is the lack of trust between the players, meatworks, hide and skin processors, tanners and finished leather suppliers. This stems from years gone by where there was a lack of trust and cooperation between the meat operators and the hide processors / tanners as the meat operators speculated with their hides in the hide processors/tanner sector in a cavalier manner creating instability in this sector. In recent years the hide processors/tanners have been more successful in forging alliances with the major meat operators, educating them as to what is required to stabilise raw material supply and give them better returns

The nature of the ownership structures of hide and skin processors in Australia is largely through private family companies. Whilst the industry has consolidated over the last decade, it still does not directly have access to the significant capital requirements to create an operation that can remove the supply chain inefficiencies and give the hide and skin processors precisely what they need to suit their particular market's needs.

2b) Identify major opportunities for the leather sector and its strengths and weaknesses for securing these opportunities

STRENGTHS

- Significant supply of raw material
- Significant labour supply with high general education standards compared to many overseas competitors
- Alliances are developing with meatworks to provide better and more consistent supply of product
- Proximity to SE Asia to sell raw and processed materials

WEAKNESSES

- Fragmented supply chain
- Comparatively high costs of labour and environmental compliance to our competitors
- Expanding SE Asian hide and skin processing sectors competing for raw material with raw material downstream processors
- Mistrust in the supply chain
- Too many small companies
- Oversupply of wet blue tanners compared to supply of suitable hides and skins for the wet blue processing markets bidding for product to stay in business but not provide returns on capital
- Remnants of a hide tender system that can distort the real value of a hide and skin to a processor up or down
- Significant geographical distances to be travelled in freighting product from supplier to processor

- Cluster of small tanners and brine/salting processors in Victoria that compose a small part of the industry but represent their needs as the needs of the broader industry directly through their own lobbying and control of so-called industry bodies.
- View of small tanners is often archaic to a historical perspective of how things used to be rather than working within the new competitive and alliance based environment. Wanting, hoping, and attempting to keep the system as it was but slowly succumbing to the new market pressures
- Lack of capital and concern about market risk to undertake a significant expansion in upstream processing
- Cost of better chemicals for tanning and finished leather making is high due to compliance costs in gaining approval under NICNAS, even though testing and compliance may have been achieved in an overseas country that have just as stringent health, safety, and environmental standards as Australia
- Large distances from high end fashion markets in Europe
- Low quality of hides and skins by world standards

OPPORTUNITIES

- Invest at the meatworks gate, or nearby, to allow hides to be sorted, preserved, and directed to the appropriate market of domestic processors in the type, size, quality, and volume they require.
- Obtain commitment from meatworks and processors to funnel raw material hides and skins into a location, or number of locations
- Add more value adding to Australian hides and skins
- Increase returns to meatworks
- Potential increased returns to producers as market price of hides improves
- Further downstream investment in finished leather production because raw material is available at a lower cost to the tanner

2c) *Identify policy options including tariff options consistent with the Government's international obligations such as those under WTO and APEC, which would encourage the leather sector to adjust to a more viable and sustainable competitive position*

The problem has less to do with restricting access for overseas suppliers into the Australian market through tariffs, as the need to provide a domestic environment where tanners/finished leather producers have access to the type, size, quality, and volume of raw materials at a competitive price most suited to their leather requirements

2d) *Analyse the short and long term implications of each policy option for the structure, performance and competitiveness of the leather sector, investment, employment, consumers, resource allocation, flow on effects for other industries, general growth prospects and appropriate role for government. Particular attention should be given to the impact of policy options on those regions where the TCF accounts for a high level of regional industry concentration;*

The stimulation of the hide and skin processing industry through the creation of plants that are able to work with meatworks through the supply chain to receive hides and skins, and then direct them to their best ends will have the effect of providing a steady supply of the required product. This will lead to a bigger and more internationally competitive hide and skin processing and finished leather industry. As a result of this expansion the number of people employed will increase, and resources are more effectively allocated to value adding activities.

The role for government is to provide a framework for this upstream investment to be implemented and stimulate the investment in such activities.

2e) Examine relevant workplace issues including the more effective use of flexible modes of employment, labour mobility in and out of the sector, especially in regional Australia, and the scope of innovative workplace reform including policy options to improve the competitiveness of the sector;

As mentioned previously, the current TCF – SIP has not led to any significant change in the supply chain management. Consequently, high labour turnover results from the boom and bust production within the individual firms in the industry as they hire and then trim labour in line with production. This has a consequence that new labour is frequently being trained and then let go a cost to the businesses. This has to be resolved to “guarantee” supply to those downstream processors who must invest heavily in capital both human and plant. Unless the stability and cost of supply can be maintained relative to international benchmark prices, the industry will not be able to expand into downstream processing.

2f) Report on the likely impact on the leather industries of international trade developments, including, but not limited to, the DOHA round of trade negotiations and proposed Free Trade Agreements.

As previously mentioned, it is not so much a problem of international competition coming on shore and competing in supply, as rationalising the supply chain to provide the most appropriate product to the downstream processors at a competitive price.

2g) Any other comments pertinent to the review or the leather industry submission not covered above.

So far the focus of the government has been at the wrong end of the supply chain. Any financial stimulus to the industry has to address and influence the beginning of the supply chain at the meatworks door and raw material processing, otherwise any government funds allocated to the downstream sector will continue to be completely wasted.

As one of Australia’s largest and most reputable hide and skin processors, A.I. Topper & Co Pty Ltd believes it is well placed to give insight into the hide and skin industry’s needs. It hopes that this submission creates the opportunity for the TFC – SIP to review its approach

and modify it to direct its efforts into supply chain development with meatworks to enable the appropriate product to be available for hide and skin processors for tanning and finished leather making.

3. *What Should the Nature and Extent of TCF Industry Support Measures for the Leather Industries Post 2005?*

The support to the hide and skin processing industry should be through direct financial stimulation of up stream processing and creating an environment for the further development of supply chains with meatworks to pool hide and skin production to provide the industry with the raw material size, type, quality, and volume that it requires to meet customer demands.