

Berkeley Apparel P.L.

Productivity Commission Questionnaire:

“Issues and questions”

Recent performance and future prospects

In developing post 2005 assistance options, the Commission needs to understand how the TCF sector is performing and what its future prospects are. To augment the material contained in recent reports, the Commission is seeking information on the outlook for the various industries within the sector, the scope for further performance improvement, external factors which will influence future performance and indications of the adjustment achieved to date.

How have the TCF industries and individual firms been performing in terms, for example, of profitability, return on investment, market share, exports, improvements in productivity and product quality?

Berkeley Apparel has shown steady growth over the past 3 years but importantly this growth has encompassed strong growth in their brand business (Studio Italia and Berkeley 1907) at the expense of previous unbranded or offshore licensed brands. There has been a greater focus on both productivity and product quality as a direct result of the production process initiatives instigated in response to SIP encouragement programs. At the same time the greater focus on product innovations and technically focussed concepts has greatly improved Berkeley's market share, growth and return on investment.

What has been the contribution to performance outcomes of industry restructuring, investment in plant and equipment and R&D, emphasis on skilling, training and management performance and supply chain management?

Industry restructuring has been largely through market forces moving market shares away from the less innovative firms towards those embracing new and exciting innovations like Berkeley Apparel. This shift of market shares has a natural level of inertia involved and we would argue that there is a strong case to encourage the restructuring/rationalisation potential within the Australian suit industry by directly encouraging through more relevant SIP type 4&5 such rationalisation of current firm numbers and involvement. Berkeley Apparel supports the encouragement of product and process improvement undertaken under current SIP rules, although access to such encouragement is in part more restrictive for clothing manufacturers who necessarily have a strong visual/fashion element to their developments that is not recognised under the current arrangements. Likewise the current arrangements do not recognise the key

strategic investment concept of “brand equity” but only recognise investment in physical machinery assets that are only one part of the desired strategic investment strategy.

As noted investment in plant & equipment is directly encouraged under current SIP program and Berkeley Apparel has actively accelerated its investment programs accordingly in these physical assets.

What adjustment pressures are acting on the TCF sector (eg. technological change, increased competition from low wage or more efficient production centres overseas, changing patterns of consumer demand)?

All above examples apply to the constantly changing outerwear suit market. Technological change in both products (eg Berkeley’s fully washable suit),in processes(eg workflow systems and software developments to increase factory production efficiencies and quality),and in machinery(eg workstation attachments and workflow systems) are constantly improving. Competition from low wage cost countries overseas in particular China are in the early stages of the “acceptability” cycle. Changing patterns of consumer demand whether at the broader level of formal to casual or at the narrower level of to low maintenance natural fibre constructions etc are a never-ending part of staying market leader in a competitive domestic market.

What difficulties have occurred in adjustment to changes in the sector’s operating environment in recent years? What factors have facilitated or impeded adjustment to increased international market competition? What are the characteristics of those firms that have either succeeded or failed (eg. are brand recognition, marketing, design and/or product differentiation or some minimum scale important)?

There are many difficulties to the adjustment to changes in the suit industry’s operating environment over the past 5-10 years. Many suppliers have contracted, many have switched to full offshore sourcing and some have just exited completely. These adjustments are not unusual for any industry but have been heightened in the suit industry by the encouragement of importers (both wholesale and retail) at the expense of manufacturers as a direct consequence of the Government’s high profile policy towards garment tariffs. The tariff pause from the cuts preceding 2000 has enabled some stability in this process but the impending cuts of 2005 (plus the 25% “improvement” in exchange rate over the last 2 years) is beginning to reactivate destabilising tariff pressures for local production.

The main impediment to adjustment to increased international competitiveness is confidence: confidence to invest in machinery; confidence to invest in new product developments; confidence to invest in the key long-term aspect of “brand equity”. Similarly an associated impediment to adjustment is cash flow. To undertake the sort of strategic moves required to achieve desirable structural change, extra free cash flow is required. In both dimensions of confidence and cash flow the SIP program has been an

outstanding concept that strikes directly at these 2 key impediments to industry change. As noted elsewhere we believe the SIP program can be improved in terms of its relevance and application to the garment industry, but we also believe that it is the fundamentally correct approach to take to achieving the Government, Industry's and Consumers desired outcome.

The characteristics that of those firms that have succeeded or failed are well summarised in your examples ("brand recognition, marketing, design and/or product differentiation or some minimum scale"). Berkeley Apparel believe they have focussed successfully on all these aspects as well as the more traditional aspects of manufacturing excellence, and attention to customer service.

Which industries in the TCF sector in Australia are most competitive (eg. in which specific products or production processes) and why? How might this change in the future? What capacity do TCF firms have to improve their productivity/cost base towards international best practice?

Berkeley Apparel cannot evaluate the competitiveness of the myriad of sectors covered by the term TCF, however it is apparent that those areas closest to the industry end product core (namely clothing production) suffer the biggest cost disabilities by virtue of their reliance on Australian costed material inputs and overhead, and Australian standard of living labour costs. To look merely at "the most competitive" without reference to significance or position in the end product "food chain" is to assume that small intermediate good elements can exist on their own independent of available supplying industries or available using industries. Likewise this sort of question has little relevance to the available potential of these "most competitive" sectors, where the answer leads not only to a "spotty" industry base, but one that has minimal scope for expansion (other than via massive export encouragement for the reduced activity base involved) and a general inability to compensate for any reduction in what is deemed to be "less competitive"

Berkeley Apparel prefers to view all current industry sectors as having potential as demonstrated by their ongoing existence in the face of the massive tariff cuts of the last 10 years, and that within those sectors are firms better focussed to achieve the Governments restructuring and performance aims.

What external forces will influence future performance and prospects (eg. exchange rates, microeconomic reform, trade barriers and overseas assistance measures)?

Key external forces will be the policy of retailers re sourcing, pricing and expansiveness towards new products and new ideas. The key to long-term survival is in the top-line and thereafter it is good management and sourcing strategy to retain sufficient margin to

survive. Retailers' reactions hold the key to this and suppliers such as ourselves then have the opportunities to develop and invent concepts/brands/strategies to work successfully with enlightened and supportive retailers. Exchange rates, micro economic reform, trade barriers and overseas assistance measures etc shape the sourcing decisions rather than overall business prospects.

Would changes in domestic policy settings (eg. to taxation, workers' compensation arrangements, etc) help the TCF sector to increase its competitiveness?

Domestic policy settings definitely assist the retention of top-line results to a viable cash positive business unit. Competitiveness naturally flows from such cost improvements; however the probability of their improvement to such a level to compensate for negative pressures from cheaper imports needs to be taken into account in any such assessment.

Is TCF activity in regional areas particularly vulnerable to changes in the sector's operating environment?

All TCF activities are vulnerable to increased import pressure whether in Bendigo or Sunshine

Impact of current assistance arrangements

The TCF sector receives government assistance through a range of measures including tariffs on competing imports, grants delivered through the Strategic Investment Program (SIP), the Expanded Overseas Assembly Program (EOAP), policy by-laws and access to generally available government programs. Analysis of the impacts of the current assistance regime will provide an important guide to the level and form of assistance that should apply to the sector after 2005.

How effective and efficient are current assistance measures in promoting desirable structural change and establishing an internationally competitive TCF sector? Which measures are the most effective?

As previously noted Berkeley Apparel strongly supports the SIP program objectives and the approach in general. Berkeley has undertaken many changes that it would not previously had the confidence or free cash-flow to otherwise undertake. We would be most pleased to take you through our new marketing and manufacturing strategies emanating directly from our experience with the SIP initiative. We believe that the

current SIP program can be further improved to more fully recognise the innovations in the key garment sector that are currently precluded under current regulations ,and to broaden the strategic encouragement to recognise the key element for long term viability in the development of “brand equity”.

Have the impacts of assistance measures varied significantly across different industries in the TCF sector? What aspects of the current package have most helped desirable change? Have there been any unintended or undesirable side effects?

As noted the key end product sector of garment production has been seriously limited in its ability to access the SIP strategy by virtue of regulated definitions for “technical only” innovative product development. This position is easily seen in the difficulties individual clothing/fashion firms have had in meeting Departmental “non-visual” definitions and their focus on technical textile aspects rather than commercially based garment considerations.

How effective has the SIP been in encouraging additional or earlier investment in process or product development and new capital equipment? Are there any deficiencies in the SIP criteria or their application?

As noted SIP has been vital to these strategic improvements undertaken by Berkeley Apparel over the last 3 years. The deficiencies relating to garment/fashion industry have been noted above as well as the need to make “industry rationalisation” encouragements genuinely operative and not just to apply to some random Non-CBD rationalisation opportunities.

Are there any particular problems or anomalies in other assistance arrangements (eg. the EOAP and policy by-laws)? How might they be avoided/alleviated?

There is always concern as to how NZ Customs administers its policies in favour of its own, however this aspect has diminished in recent years as has the extent of price distortion from the Fiji trade. These aspects should be assessed in more detail at the industry level to allow informed judgement utilising industry based and independent statistics.

To what extent are TCF firms taking advantage of the current tariff pause to prepare for the legislated tariff reductions in 2005?

Berkeley Apparel is taking maximum advantage of the current pause aided by the confidence provided by the SIP program and our active interest in adjusting as required. This may not be true of all firms but the firms that are increasing their market position are definitely using the current tariff pause to put in place strategies to adjust and improve

How significant are the costs imposed on consumers, taxpayers and other industries by the assistance package for the TCF sector? To what extent have these imposts hindered the performance of local downstream industries such as furniture manufacturing?

Berkeley Apparel does not believe the costs on consumers are significant. By world standards men's suits in Australia are extremely accessible to the general consumer, and the assistance program to date has been handled in a manner that ensures critical firms like Berkeley have the opportunity to stay and adjust to the changing circumstances in an orderly and digestible way.

Workplace issues – Confidential – Commercial In Confidence

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Market access issues

In accordance with the terms of reference, the Commission is seeking to assess the effects of other countries' trade barriers on future prospects for the local TCF sector and the influence of institutional arrangements (eg. the WTO, APEC and Australia's current and prospective free trade agreements) on these barriers?

In what ways, and to what extent, do overseas tariffs and non-tariff barriers restrict access to markets? Are there examples of current barriers creating, rather than hindering, opportunities for Australian firms?

Berkeley Apparel has attempted export programs to Ireland and Europe under previous ICS program with some level of success. However export programs require a strong home base and in the absence of the ICS program this has not been a priority in the current Berkeley Business Program. There are numerous barriers to offshore expansion not the least of which is distance given the relatively high production cost and hence inability to airfreight or discount on price to kick-start interest in the product.

Have local TCF firms been able to circumvent the trade barriers of other countries (eg. by establishing production facilities in other countries/regions, through brand recognition, concentrating on high value niche products etc)?

All of the above are possible but Australian suit manufacturers are small in the world market and domestic market is the key to their long term viability

What new opportunities or threats are likely to arise from current efforts to liberalise TCF trade through the Doha round of WTO negotiations and the APEC commitment to free and open trade in the region by 2010 for developed countries and 2020 for developing countries? What will be the impact of developed countries removing their quotas on imports from developing countries under the WTO Agreement on Textiles and Clothing?

Analysis of trade figures shows that China does not yet have the dominance of the branded suit market experienced in other garment sectors. The freeing up of US and European markets will have less trade distortion impacts than in many other garment areas.

Are imports from least developed countries (eg. Bangladesh) likely to increase significantly as a result of the recently announced removal of Australian tariffs on products from these countries?

No

How helpful has export assistance provided through Austrade (eg. export market development grants), EFIC (eg. export finance guarantees) and the DFAT market access initiative been in assisting TCF exporters?

N.A.

Is dumping in the Australian market a significant problem? Are current anti-dumping measures effective?

Dumping is significant but perhaps more so in those areas dominated by the non-cost based pricing of Mainland China

Quotas are the only known means of controlling import growth from dumping

Post 2005 assistance arrangements

The Commission is seeking to identify post 2005 options that benefit consumers, taxpayers and the wider community, and encourage the TCF sector to adjust to a more viable and sustainable competitive position without undue disruption.

What rationale, if any, is there for maintaining tariff assistance to the TCF sector indefinitely? If not, over what time frame would it be reasonable to remove the sector's preferential tariff treatment? What are the key considerations in determining that time path?

Berkeley Apparel believes that a 3 step program through to 2015 would enable adjustment of end product tariffs from their current 25% to an end point of 10% to be achievable with minimum disruption provided an adequate SIP program was simultaneously in place.

The key considerations in determining the time path is to minimise adjustments so that they can be absorbed in digestible amounts without destroying confidence of both manufacturers and retailer in the industry's ability to accept the challenge and invest in long term strategies with SIP encouragement.

What, if any, of the other components of the sector's current assistance package should be retained? What modifications to programs such as SIP and the EOAP should be made if they were extended? What role would they play in facilitating structural change in the TCF sector?

A continued SIP program through to 2015 is central to this tariff wind down strategy .As noted the SIP program needs to be modified in its administration to:

(a)Better reflect the strategic activities of the more visually based garment and fashion industries and their innovative strategies. There is a need to better reflect the role of these key industries by de-linking the current value added arrangements of Type 3 under current SIP so that this dimension is not restricted from those areas focussed on visual fashion innovations for their long-term viability;

(b)More direct encouragement of industry rationalisation could be achieved by removal of the "non-CBD" requirement of the current type 4&5 provisions directed at industry restructuring

Would further reductions in assistance post 2005 be likely to cause significant economic or social disruption? If so, how could the sector be best helped (eg. special adjustment or regional assistance)? Are there any case studies of previous adjustment experience (both positive and negative) which the Commission should consider?

Berkeley Apparel believes a double policy approach of adequate SIP encouragement conjointly with the stepped tariff reduction program to 10% in 2015 is manageable without significant economic and social disruption.

If a tariff only approach(without an adequate SIP Program) is taken Berkeley Apparel believes the disruption for its own local operations ,and for the industry in general will be virtually total, with minimal confidence and any positive basis for forward long-term planning of local activities

Berkeley Apparel P.L

Submission to Productivity Commission Textile Clothing &Footwear Inquiry

Berkeley Apparel Pl is the largest suit manufacturer in Australia with approx 150 manufacturing employees. It makes this submission to the TCF Inquiry as a member of the TFIA and fully supports the position and proposals put forward by the TFIA for post 2005 policy arrangements.

The bulk of Berkeley's detail position is included in attached individual responses to the Commissions list of "Issues and Questions" previously circulated as a guide to the Commission's key areas of interest. Additional background aspects underpinning the company's view and then a Summary of our position are noted below.

Background to Berkeley Apparel's Policy Position

*Berkeley operates in a highly import competitive sector of the TCF market. Over the last 10 years the overall volume of suits has remained relatively stable around 900,000 suit equivalents, but the import volumes within this total market size have grown from approx 25% to 65%. At the same time many of the established local players have either exited the industry(Rundles, Friedman etc) or moved to primarily import distribution (Flair, Boss, Rodmill etc) or moved to primary retailer focus (Fletcher Jones, Stafford's) .

*Berkeley has positioned itself in the middle –to-upper price segment of the market to maximise its focus on customer service through local manufacturing, and to utilise its design innovations under its own brand equity developments in particular the brands "Studio Italia" and "Berkeley 1907".

*Berkeley has a strong focus on innovative product development over the years and this has been heightened by the encouragement and resourcing provided by this element of the Federal Government's SIP Program.

Some of the initiatives over the years include:

- Development of the poly/wool suit with Aweave in the 80's
- Development of high twist fabrics (to provide lighter but similar resilience to gaberdine) into "High Comfort" concept in 2000
- Development of the "High Movement" concept in 2001
- Development of exceptional shape retention and recovery suits in 2002
- Development of Fully Washable Conventional Suits in 2003

*Berkeley Apparel is responsive to Government policy initiatives and seeks to build on its innovative potential, and brand development strategies to achieve Government objectives of long term viable enterprise at low tariff levels. As such has sought to constructively assess policy options in this positive light as they relate to the Australian suit industry

Summary of Berkeley Apparel's Position re Post 2005 TCF Policy.

*Believe that a 3 step reduction program from current garment rates of 25% down to 10% in 2015 is achievable with minimum economic and social disruption if accompanied by and adequate SIP program extending the current program in place.

*Berkeley Apparel only supports such tariff reductions in this form with the complimentary operation of an ongoing adequate SIP program.

*The adequacy of the ongoing SIP program would involve at least funding of current annual levels and would involve modifications of current regulations to better address other key triggers for viability in the clothing industry namely:

- de-linking of Type 3 Value Added Dimension to recognise the difficulties for garment manufacturers to access this dimension when the Type 2 requirement is restricted from them by the “non-visual” only requirement for both Type 2 and hence Type 3 under the linking requirement; and their greater emphasis on investment in brand equity rather than capital equipment for long-term viability being also precluded from Type 1 investments and hence restricting the only other available route to Type 3 access for clothing under these current linking provisions.

- removal of the “non-CBD” provisions applying to industry rationalisation objectives of Type 4&5 under current SIP regulations

*Berkeley Apparel Ltd fully supports the position presented by the peak industry body TFIA and has been actively involved with the many other industry personnel developing that position