



BRUCK TEXTILES

**PRODUCTIVITY COMMISSION INQUIRY
INTO
POST 2005 TCFL INDUSTRIES
ASSISTANCE**

SUBMISSION – MARCH 2003

INTRODUCTION

Bruck Textiles is a Australia's leading manufacturer of woven cotton and man made fibre fabrics for apparel, furnishing and industrial end use. The company has been established in Australia for more than 50 years, with annual turnover of over \$120 million, and we have strong plans for the future.

However, our business structure has changed dramatically over the life of the company due to a wide range of factors. But of all these factors, government policy continues to play a significant role and future assistance arrangements will have a real bearing on our future plans.

In this context, we see the current review of future TCF assistance arrangements as extremely important and have prepared this submission with the view of highlighting the implications of various options, for our business.

COMPANY BACKGROUND

Bruck Textiles Pty Ltd is a privately owned company, which commenced operations in 1946. The manufacturing plant is located in Wangaratta (in north-east Victoria), and employs 482 people engaged in fabric weaving, dyeing, printing and coating.

Bruck also owns Wilson Fabrics and Wallcoverings, a fabric wholesaling business which employs 60 people, and a further 60 persons are employed at our corporate headquarters and sales office in Surry Hills, Sydney.

Bruck Textiles is the pre-eminent Australian manufacturer and supplier of woven fabric for industrial and corporate wear, defence and institutional fabrics, and targeted women's and men's wear, including specialty fabrics such as moleskins and firefighting materials.

Further, via its internal and external markets, Bruck leads in the development of furnishing fabrics, of varying widths and product base.

The major market segments which Bruck services are:

(i) Corporate Apparel

Bruck competes in the corporate/workwear segment of the apparel market. The company has steadily moved away from the fashion apparel market, which is now predominantly supplied by imports. However, Bruck's ability to undertake the whole weaving, dyeing, printing and finishing process, enables the company to more readily meet the requirement for quick response and enhanced service necessary to properly service the corporate apparel market.

Bruck has been successfully exporting apparel fabrics into the U.K. for the past six years and is pursuing opportunities for a stronger presence in the U.K. and the U.S. The product mix being developed will allow for increased market penetration by co-ordinating prints, plain dye and colour woven apparel products.

However, Bruck is very conscious of the ever-contracting Australian apparel market and the instability of the Fiji garment industry, which has long been a major

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destination for Bruck's output. For this reason, the company's focus is increasingly on broadening the end use focus of our products.



(ii) Furnishings

Furnishings, including plains, prints, jacquard and upholstery fabrics, represent a strong business segment for Bruck and these are distributed through our own Wilson label and also through other manufacturers/wholesalers. This is a mature and successful business, focused primarily around prints.

Bruck and Wilson produce ranges of ready made (and ready to make) drapery. These products are sold directly to retail. The inclusion of commercial sheeting into the Bruck range has provided excellent opportunities to service domestic, institutional and hospitality markets throughout the Asia-Pacific region.

With the acquisition of Bartex a few years ago, Bruck now also services the printed apparel and bed linen markets. In addition, the ability to print in-house has enabled improved quality, control, shorter lead times and reduced costs.

Bruck is the pre-eminent supplier of back coated drapery and linings in Australia. The polymer coating of drapes prevents light penetrating fabric and acts as insulation for cooling in summer and heating in winter. Bruck has two narrow and one wide coating machine installed. The wide machine is the only one of its type in Australia.

Currently Bruck exports furnishing fabrics to 17 countries around the world. The established distribution system is quite effective in channelling Australian product into Asia, Europe and the Americas.

Furnishing as a segment is a growth market that is less sensitive to imports and offers higher margins.

(iii) Specialty Fabrics (Niche Markets)

Bruck is increasingly forging new markets of strategic significance, with innovative fabric styles and high tech, high value applications. Prime target markets for this focus are the Defence Forces, fire fighting services and hospital suppliers.

Bruck has negotiated a Licence with Rhodia International to ensure the continuation of its flame retardant fabric business, for use in protective apparel for the emergency services.

Bruck has also sought to build a competitive advantage through the purchase of certain specialised equipment, for producing wrinkle free cottons, application of fire retardant finishes, specialised infra-red special capabilities for defence applications, etc.



REGIONAL CONSIDERATIONS

Bruck Textiles is a significant employer in the regional centre of Wangaratta, Victoria. Apart from the direct employment provided for almost 500 workers, we also generate flow on employment (conservatively estimated at some 1,000 – 1,200 people) for other service providers and suppliers in the community. If Bruck's market was to decline, this would put at serious risk, not just this employment, but the regional infrastructure developed to support the company's productive capacity in Wangaratta.

Yet, despite the benefits Bruck's operations provide the local community, the cost of conducting manufacturing activities in regional areas is becoming prohibitively high. Apart from the additional transport/freight costs for both input and finished products, the company is now confronting additional regulatory imposts, with higher insurance, environmental and utilities costs, than imposed on our metropolitan based counterparts.

IMPACT OF EXISTING ASSISTANCE ARRANGEMENTS

Tariff Arrangements

The freeze in fabric tariff reductions in the period 2000 to 2005 was most welcome from Bruck's point of view, as this was a period in which the company was part of a major industry restructuring exercise, and from which we consequently had to consolidate our operations and reposition ourselves in the market (especially new markets). This would not have been possible without the tariff freeze, as it ensured a period of stability and gave the company's principals the confidence to embark on the change that was necessary.

Unfortunately, we do not believe the same could be said for our major market – ie the apparel industry. While it was hoped the freeze would also help the apparel sector consolidate its position, the reality was that the decline in tariffs through to 2000 had a much greater debilitating effect than anyone had thought possible. The continued surge of imports immediately following the last review (due to the further scheduled tariff cuts) coupled with retailer attitude towards price points, meant that the apparel sector overall was already weakened by the start of the current program. This was further compounded by the retail pressure on apparel manufacturers to absorb the impact of the introduction of the GST. To maintain competitiveness, companies have focussed on continued cost cutting often at the expense of quality and product development.

This has had obvious adverse flow on effects for Bruck. Our domestic apparel market continues to decline, and while we are seeking to improve and differentiate our own product, the basic fashion industry is not in a position to afford a specialist differentiated fabric given the price points it is forced to meet. Thus more and more, we are moving into other market segments.



Termination of Import Credit Scheme

The termination of the Import Credit Scheme had a significantly detrimental effect on our business. The ICS had enabled us to seek to establish new markets overseas, with the credits helping offset the costs involved in overcoming other countries' barriers to imports and in establishing appropriate distribution networks and undertaking necessary market research. While we still export to the UK and US, overall exports have dropped since 2000 as the cost of maintaining a presence in these markets cannot be redeemed in the price we can solicit. The exports that we still retain are essentially in those product lines where we were able to generate a sufficient market presence through the support of the ICS, but this is proving much more difficult now with new products and in new markets.

However, the greatest impact arising from the termination of the ICS has been our Fiji business. Fiji is still a major market for Bruck as a number of our key customers maintain make-up operations in Fiji. But the ICS was a significant factor in ensuring a strong viable garment business in Fiji, and the level of activity in Fiji has declined considerably with the end of the Credit Scheme.

In an effort to offset this, the Australian Government introduced the S-TCF Scheme to help retain a reasonable level of industrial activity in Fiji. To some extent this has helped companies in Fiji and thus retained a demand for our fabrics. But in truth this is a double edged sword as it enables Fiji to utilise third country fabrics more readily and this threatens our own activities. There is no doubt that without the introduction of the S-TCF investor confidence would have fallen even more in Fiji and we may well have lost more, if not all of our business there. But the S-TCF does little to encourage Australian inputs into Fiji manufacture, and the retention of a bilateral ICS scheme for Australia Fiji trade would have provided much greater support and encouragement for Australia Fiji joint strategic activity.

It should be recognised that the build up in the Fiji industry activity following the introduction of the ICS was not immediate, but gradual over time. Similarly, the decline in industry activity following the termination of the Credit Scheme has been steady and is still ongoing. The new S-TCF Scheme offers insufficient encouragement to stop this, and this is a major concern for Bruck, as it threatens to destroy our one remaining volume market for apparel fabric

Strategic Investment Program

The TCF Strategic Investment Program (SIP) has worked well for Bruck. It has provided the necessary encouragement to enable us to undertake necessary operational restructuring, new capital investment and product development to help us reposition our business.

With the rapid decline in the apparel market, it was vital that Bruck take such action. However, without the support offered by the SIP, we would not have had sufficient confidence in the payback on our investments, to have committed to the extent that we have.



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Now that we have embarked in these directions, and with the continuing support of SIP, we are finding that we are able to develop new highly specialised product (eg for defence/protective purposes) that is taking us into higher value added, and more sustainable areas. But the cost of such development is extremely high, and the chances of success low, and it is unlikely that we would engage as extensively in experimentation into new products and applications without the SIP type assistance.

While the scheme has been very positive for Bruck, there are of course areas where we believe it could have provided greater benefit. These are addressed later in this submission.

Enhanced Overseas Assembly Provisions

As mentioned earlier, as Bruck's apparel customers increasingly move offshore, there is the very real risk that they will not continue to pull through Bruck's product. Bruck sought to counter this to some extent by accessing the Government's Expanded Overseas Assembly Provisions (EOAP) scheme, arranging for clothing products to be made offshore utilising Bruck fabric produced in Australia.

It was expected that the EOAP would help Bruck retain, if not grow, the overall demand for its product in the changing apparel market environment. The EOAP activity was intended to enable Bruck to extend our market possibilities, both domestically and for export, either in the traditional piece good form or as finished garments.

While we are still engaged in EOAP activities, it has proved more costly and difficult than we had envisaged. For major offshore producers of apparel, the Australian market is only a small consideration, and the volume of product demanded does not warrant disrupting production runs to incorporate a relatively small amount of Australian produced fabric. That is, they would rather provide a finished product from their existing production (utilising locally sourced fabrics), or charge a premium for the special runs.

In this context, the assistance accorded by the EOAP (through the concessional duty on the re-imported finished product) is often insufficient to offset the cost involved (both of the actual product and the management/orchestration of the process). The benefit will become even more marginal once the apparel tariff reduces to 17½ %.

SPARTECA, S-TCF Scheme

As mentioned above, Fiji has been a major market for Bruck's fabrics. Through the 1990's it proved to be a major source of make-up as the Australian clothing industry was finding itself being forced offshore.

However, Fiji's competitiveness was seriously hindered as a result of the conclusion of the former TCF plan in Australia - through the further erosion of Fiji's preferential access to the Australian market (as Australia's clothing tariffs against third countries came down to 25%), and the impact of the termination of the ICS which resulted in Fiji's garment producers being confronted with higher fabric prices.

This put serious strains on the Fiji industry's future sustainability, and this in turn had serious ramifications for Bruck's own viability. Thus, we welcomed the decision of the Australian Government to introduce the SPARTECA – TCF scheme in early 2001, which was intended to help sustain a reasonable level of Australia Fiji bilateral

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trade in TCF products, whilst expressing serious concerns as to the Scheme's mechanistic ability to deliver the desired outcome.



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Under the scheme, Fiji manufacturers are able to accrue Excess Local Area Content (ELAC) points, where the local content in their finished garments (or other eligible TCF products) is greater than 70% (of total factory cost). They can then apply these points against products that would not normally qualify under SPARTECA for duty free entry into Australia (because they have a local content less than 50%), to notionally meet the 50% content requirement.

To an initial extent, this had a positive impact for Bruck, as it gave renewed confidence to sectors of the Fiji industry, which in turn ensured continued demand for our fabric. Moreover, to benefit under the scheme, the Fiji manufacturers must be using Australian inputs to generate the necessary excess content.

But, we are increasingly finding that there are also downsides under the scheme for Bruck. As the ELAC generated is not being utilised in other new product lines that do not require Bruck fabrics, there is increasing pressure for the Fiji makers to average down their use of Bruck fabric and utilise the points generated for substituted fabrics from 3rd countries.

On the basis of analysis we have undertaken on the nature of our fabric sales to Fiji since the scheme was introduced, we believe there is enough ELAC generated such that Fiji could readily and immediately displace more than 50% of Bruck fabric with 3rd country purchases, under the scheme. This places us in a severely vulnerable position and undermines our ability to plan confidently for the future. All it needs is for one of our major customers to decide to manipulate the S-TCF scheme in this way, and it will seriously erode (if not destroy) the critical mass needed for our continued economic production in Australia.

Accordingly, we believe an alternative scheme should be introduced, which still provides the necessary incentive for the Fiji manufacturers, but not at the potential cost of the Australian industry.

BRUCK'S FUTURE STRATEGIC DIRECTIONS

Bruck has, of necessity needed to rationalise the manufacturing operations based in Wangaratta. But we are already seeing the benefits of this action through improved efficiency and productivity and reduced costs. We are also streamlining our management and marketing infrastructure.

Bruck is also repositioning its business to ensure we fully service key clients, but reduce dependence on other customers where the returns are limited or the market is more volatile. In this context, we are increasingly strengthening our relationship with the Australian Defence Forces, forging a mutually beneficial partnership that is a real strength for both parties. This has given us an opportunity to develop new specialised product with a significant degree of innovation and value added.

However, while we are striving to maintain our international competitiveness, we remain concerned about the ability of our core customer base in Australia to retain the necessary critical mass to ensure its own sustainability. And while we continue to explore numerous avenues to expand into export markets, we are continually confronted with market access difficulties into other countries.



FUTURE ASSISTANCE ARRANGEMENTS

While we will be doing everything in our power to achieve our future goals, there is a significant role the Government can play to help us achieve the desired outcomes more quickly than would otherwise be the case. The areas in which the Government can help, and the reasons for this, are outlined below.

(i) Tariff Duty Rates

Bruck's ability to remain fully competitive depends on maintaining a strong domestic presence. But, if Australia reduces its tariffs further while the rest of the world maintains more extensive (and in the majority of cases significantly higher) barriers to trade than we do, then this will seriously undermine the future viability of our key customers. In turn of course, this will impact adversely on Bruck with obviously detrimental connotations for our employment base in Wangaratta.

It would seem that other countries' focus with the Doha Round of Multilateral Trade Negotiations is primarily on trade barrier issues, and the preliminary positions being mooted suggest that their end targets will barely bring them to the levels we already have scheduled by 2005. We should not be accelerating our trade liberalisation until it is clearly evident what our major trading partners have in mind. And we certainly should not be rushing "ahead of the pack".

Bruck recognises that tariffs are legislated to come down again on 1 January 2005, to 17.5% and 10% respectively for clothing and fabrics. The company understands and accepts this, but this does not change the fact that it means Australia is out of step with all our trading partners. It is imperative therefore, that these duty rates be not reduced further before 2010, at least.

Moreover, any further reductions in the post 2010 environment should be subject to a review of other countries' trade liberalisation progress, and only implemented if there is demonstrable evidence that our major trading partners in these product areas have, or are clearly implementing, similar action.

However, given that Australia's tariffs on fabrics are being reduced in 2005, it is not appropriate to leave tariff on yarns untouched, where there is no local manufacture of such yarns. In Bruck's case, many man made fibre yarns and the ring spun cotton yarns consumed in our manufacturing processes are only available from offshore sourcing, and the tariff on these should be abolished (ie they should be duty free). However, we have no objection, and support, continued tariffs of 5% on those yarns that are produced locally.

(ii) Positive Assistance – Strategic Investment Program

As stated above, the program funding currently provided by the Government to assist the TCFL industry has provided a positive impetus for companies like ours. We believe similar schemes will still be warranted beyond 2005, as there will continue to be significant restructuring pressure on the industry, especially given the major transitions that will be occurring globally as the WTO Agreement on Textiles and Clothing concludes. At the very least some sort of recognition and support will need to be provided to regional based operators, where costs of servicing customers are higher (and alternative employment opportunities are limited).

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The Strategic Investment Program in particular has provided significant encouragement to Bruck in introducing new technologies and implementing innovative activities and must be retained beyond 2005. However, the industry will continue to change and there are various improvements that could be made to the scheme to ensure the most desirable development of the industry in the future.

Some of these are technical administrative/definitional issues and can be taken up with program administrators at a later time (eg definition of eligible capital expenditure, definition of innovative processes). But others are of fundamental importance to the industries' ongoing development and need to be specifically reflected in the Program objectives/guidelines, for example:

- ❑ A large measure of a company's future competitiveness and sustainability will rest with its ability to manage and fully integrate with the rest of its supply chain. Any endeavours to improve a company's understanding, communication and interaction with its supply chain partners (both suppliers and customers through to final consumer) must be supported
- ❑ The 5% cap on sales act as a deterrent for companies to introduce major capital works projects, at this late stage in the program. This a disincentive to wholesale re-equip. Bruck is looking at a \$20 million re-investment, but the way the program is structured, it is not in our interests to do this all at once. We certainly will not be in a position to commit to a major re-investment of this sort unless the SIP scheme is extended beyond 2005, as we will not be able to roll over the funding generated into subsequent years. But even if there is the prospect to roll over funding entitlements (that exceed the yearly cap), there will be no incentive to also engage in additional R&D/product development projects as funding entitlements will be exhausted. Consideration should be given to allowing special one-off grants for major works projects.
- ❑ Indeed, it would be of considerable benefit if firms could apply for one off grants on the basis of any major capital expenditure (say of \$100,000 and more). There is no question that there can be a considerable lapse of time between the investment and consequent funding. It is not inconceivable that a lag of 18 months can occur between undertaking a major capital investment (ie in July/August of a given year) and obtaining the SIP grant for this expenditure (need to wait until the financial year is completed, audited and assessed). It should be possible for claims to be project based and immediate, and not just program year based.
- ❑ Consideration could also be given to allowing more regular and frequent payments on R&D/Product development activities, where firms have a proven historical, and demonstrable current, performance record in the conduct of such activities. This would enable companies to keep re-injecting the funds in the business, embarking more immediately on new projects rather than waiting (up to 18 months) for the grant payments before starting on major new projects.
- ❑ Expenditure on environmental projects should receive additional encouragement. That is, if a project can be deemed to have clear and demonstrable environmental benefits, it should be able to generate a bonus payment. For example, Bruck has been considering undertaking a project to help reduce water consumption in our mill, given the severe water restrictions currently confronting our region. This project will have significant flow on benefits for the local community, and this type of expenditure (which is for the "greater good") should be specifically encouraged through the application of some sort of multiplier to the

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normal grant rate. Note: Bruck at present consumes approximately 87% of the water consumption of the region.

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Similarly, additional support should be accorded to regionally based TCF companies that can demonstrate their significance to the area (either as specific grants or once again, perhaps the application of a “regional multiplier” could be applied to funding generated under SIP). Bruck is a major contributor to the Wangaratta community, but being regionally based is not without its costs and it is often difficult to compete with metropolitan based companies.

- ❑ Indeed, perhaps it is in these areas that the application of the sales cap on total grants generated, could be relaxed – that is on expenditures relating to regional and environmental developments. Given the nature of industry grants in Europe, which are often ostensibly paid for these purposes, it would seem that these are acceptable reasons under WTO for Government grants to be forthcoming.
- ❑ The industry increasingly must see itself as being part of the global supply chain. Certainly Bruck has recognised this for some time, but it is extremely difficult to generate the right contacts, access the necessary information, or forge the appropriate presence within the international market. All efforts to research supply/market opportunities globally and to develop the necessary market presence/contacts should be supported under the programs (at the very least EMDG type support should be provided under SIP for all such activity)
- ❑ TCF is essentially a labour intensive sector (although textiles is more capital intensive than the rest). But predominantly assistance over the last decade has focussed on improving capital productivity within the industry when labour is a major cost element. SIP (or the appropriate subsequent program) must recognise this and provide specific assistance for skills development within a company.

To aid certainty and predictability within the industry, and to ensure a true long term focus is developed, the positive assistance measures should be implemented for a further 10 year period – ie 2005 to 2015. The industry appears to have stabilised, but it needs confidence that it has a predictable environment to work in, in order to undertake further, necessary restructuring decisions.

(iii) EOAP

The EOAP arrangements should be continued, but they need to be extended beyond garments to encompass make up of the full range of textile products. Garments are only one end use of fabrics, and the textiles industry is increasingly making fabrics for other end purposes, eg furnishings, industrials, etc. The EOAP should extend to offshore make up of these products, as long as the input materials are clearly Australian made fabrics.

This is vital for the industry, as the EOAP provides the last bastion for the industry to forge a role as a supplier of intermediate products if Fiji activity continues to decline, given that the make up industry has contracted extensively in Australia.

Consideration should also be given to introducing fully duty free access of EOAP products, where the fabric is entirely of Australian make up, to maintain the effectiveness of the scheme, once tariffs are further reduced on 1 January 2005.



(iv) Fiji

Fiji is very important to Bruck. If the Fiji industry is not seen as an attractive source of make up by the Australian industry, they will move to China – in which event, they will become straight importers, and there will be limited market opportunities for Bruck's textiles.

The S-TCF Scheme clearly is not working as well as originally intended, or expected. And the only way to improve would appear to be by minor "tinkering around the edges" which will have marginal benefit and potentially serious ramifications for Australian order, or attempt and give the points some currency whereby they are redeemable for cash and have some value.

There is no question that if the Government is serious about encouraging Fiji's ongoing economic development, it must be prepared to find a better way of using the S-TCF points, or ideally, come up with a better scheme – something that works. But, the solution must be a program that encompasses, and has benefit for, both Australian and Fiji industry.

However, there are many and varied parameters for introducing support packages for Fiji. Ultimately though, there will need to be hard financial incentives to entice Australian businesses to recommit to Fiji production. But this is very important for Bruck, and no doubt other fabric producers in Australia.

Bruck is prepared to work with the Government, and with Fiji industry, on the development of a new, comprehensive scheme, that will help foster the development of a strong Australia Fiji textile and apparel supply chain. We strongly encourage the Australian Government to devote serious resources to this exercise.

(v) Free Trade Agreements

Overall, we are wary of potential Free Trade Agreements with other countries, as it would be easy to be completely swamped in a small market as Australia by low cost duty free imports. Equally, we recognise that most countries with which a Free Trade Agreement may be considered, would have a significantly larger market than Australia and that this could present some real opportunities for an efficient Australian manufacturer, such as Bruck.

Certainly, we believe that an FTA between Australia and the US can offer some significant opportunities for us to expand our exports into that market. It is a significant market, and has similar cost structures to our own. If we could penetrate this market in a meaningful way, it would enable some real scale economies which would help our existing operations.

But for an FTA to be of any benefit to industry in either member state, it clearly must offer some sort of advantage that is not otherwise available. Essentially, this will normally stem from preferential access to a market, according a competitive advantage over 3rd country imports. If Australia is embarking on a series of FTA negotiations, then surely it is in our interests to retain our global tariffs as high as possible, so that we have some negotiating leverage. This applies equally to the Doha Round negotiations as it does to individual bilaterals.



CONCLUSION

The future for Bruck is no longer inextricably linked solely to clothing. The company is no longer providing any fabric to retail oriented clothing manufacture. Bruck's strength is in maintaining an efficient highly capable manufacturing site focussed on servicing an increasing range of end uses. While there is still a focus on apparel fabrics, this is principally for offshore make up in low cost sources (ie Fiji), and we are increasingly moving to industrial fabrics and defence oriented fabrics, and other non-clothing related applications.

The company has reinvented itself, away from this traditional reliance on the clothing market, into areas where we were not competing before. This has not been an easy task and we still have a long way to go.

But, the company has a future. However, there is a role for Government to play as well, to help get us through the transition period, as we continue to restructure. This does not mean that Bruck believes the Government needs to, or should, provide blanket support across the whole TCFL sector, when some sectors of the industry either are not making any efforts to change or are clearly unsustainable into the longer term.

Government resources should be focussed in those areas where companies are clearly striving to make change and can demonstrate that they are continuing to change, as these are the areas where the Government support will make the real difference, and ensure a positive return to the community at large.