PRODUCTIVITY COMMISSION INQUIRY

INTO

AUSTRALIA'S TCFL INDUSTRIES POST 2005 ASSISTANCE

Joint Submission By

TCF Council of Fiji and Fiji Ministry of Commerce, Business Development and Investment

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1. EXECUTIVE SUMMARY

Fiji can provide a substantial and strategic adjunct to Australia's textiles, clothing, footwear and leather (TCFL) industries. It provides a base of low cost, flexible, short run clothing and footwear manufacture. It also provides a significant market for Australian produced textiles (fabrics and trims) and leather.

Historically there has been a strong relationship between the TCFL industries in both countries, especially during the 1990's due to the dual encouragement of SPARTECA enabling duty free access for Fiji product into the Australian market, and the TCF Import Credit Scheme which enabled Fiji access to competitively priced Australian fabrics and leather.

But, with the demise of the Import Credit Scheme and the further erosion of tariff preference margins into Australia through to 2000, Fiji has lost a significant share of the Australian market, principally to the benefit of Chinese imports.

While the Australian Government tried to offset this decline in trade with the introduction of the SPARTECA - TCF scheme, this arrangement does not provide sufficient advantage to encourage renewed development of Australia Fiji trade, to the extent suggested in the Scheme's objectives.

But Fiji still offers the same strategic opportunity for the Australian TCFL industry/market, that Mexico and the Caribbean do for the US and Eastern Europe and North Africa do for the European Union. But to achieve the full potential of the close relationship between the two countries, greater incentive (preferential treatment) is required at this stage, than currently accorded, to engender the collective commitment from both countries' industries.

At the very least, the Australian Government needs to extend the S-TCF Scheme beyond 2005, and introduce certain modifications to make it more attractive. But while this provides some benefit to Fiji industry, it is very limited.

Moreover, Fiji is conscious that Australian industry has some real (or perceived) concerns the Scheme could actually act against its interests. Therefore, it has proved very difficult to obtain the necessary refinements to the Scheme that would help ensure it offers the benefits originally intended.

It would be worthwhile therefore, in the context of post 2005 trade arrangements, to consider the introduction of new measures that could assist the strategic development of the collective Australia Fiji TCFL industries within the global market place.

At the time of the termination of the Import Credit Scheme, senior industry executives in both Australia and Fiji developed the concept of a Partnership Development Scheme. Under this arrangement Australian exporters of intermediate products would receive a duty rebate entitlement on the basis of their exports to Fiji, enabling more cost competitive supply of input materials to the Fiji industry. It was considered this could form part of an Australia Fiji Bilateral Agreement, but Australian officials decided upon the introduction of the S-TCF Scheme instead.

Serious consideration should be given to introducing a scheme along the lines of the previously suggested Partnership Development program, as it would benefit both Australian and Fiji industry. While it is tantamount to a subsidy, depending on the basis of application, it could be consistent with Article 27.4 of the WTO allowing a transition period for the elimination of export subsidies for developing economies.

But, if this is not possible, then in recognition of the strategic role Fiji plays as an extension to the Australian TCFL sector, consideration should be given to extending the Australian Strategic Investment Program to Fiji activities:

- ❖ Australian companies investing in productive capacity in Fiji should be able to claim this expenditure as eligible under SIP, provided they can demonstrate the investment will also be to the net benefit of the Australian industry and economy (eg enable greater pull through of Australian fabric)

- ❖ Any market development expenditure designed to help penetrate new markets for Fiji garments and footwear, utilising Australian fabrics and leather, should be eligible under SIP.

Similarly, the Fiji Government could explore the scope for providing its own SIP type funding to the Fiji industry. However, in the first instance, the Government would require an injection of aid monies from Australia to fund this, but this would be warranted to encourage further economic development and wealth creation in Fiji, to alleviate the potential poverty growth in the country. The Fiji SIP funding could be conditional (proportionate to) the use of Australian intermediate products in the applicant operations.

In conjunction with these positive development arrangements, it is essentially that Australia's tariff arrangements be held constant at the scheduled 2005 levels, to enable the collective Australia Fiji TCF industries time to restructure and consolidate their positions.

Finally, with Australia's developing negotiations for a Free Trade Agreement with the USA, scope must exist to take advantage of the opportunity of low cost, flexible manufacturing presented by Fiji. Fiji recognises that introducing this dimension to the trade negotiations at this early stage would confuse the issue, but once the Australia US FTA is finalised, consideration should be given to introducing special trade preferential levels (TPL's) under the FTA, for Fiji produced footwear and garments utilising Australian material inputs.

In summary, the Fiji TCF industry and Fiji Government recommend the following industry and trade policy measures should be introduced by the Australian Government to help foster the further development of the Australian TCF industry (and consequently the industry in and trade with Fiji):

- ❖ Freeze Australian apparel and textile and footwear tariffs at 17½ % and 10% respectively from 2005 on

- ❖ Introduce a Partnership Development Program for Australia Fiji TCF trade (or at a minimum extend a modified S-TCF Scheme beyond 2005)

- Maintain the SIP Scheme and extend eligibility to include Australian investment in Fiji productive capacity (where net benefit to Australian industry can be demonstrated)

- Provide Aid money to help initiate Fiji's own SIP type Scheme for Fiji's TCF industries

2. INTRODUCTION

This submission is a joint submission by the TCF Council of Fiji and the Fiji Ministry of Commerce, Business Development and Investment, to the Australian Productivity Commission's Inquiry into Australia's textile, clothing, footwear and leather (TCFL) industries and related assistance arrangements for the post 2005 period.

The Australian market is extremely important to the Fiji industry and given the nature of Australia Fiji trade relations, any change in Australia's future assistance arrangements for TCF will have a significant bearing on the future prospects for Fiji's TCF sector. Equally, Fiji provides both a competent source for cost efficient garment make-up for the Australian industry and a strong demand for Australian fabrics, trims and leather. Fiji provides an opportunity to enhance the future sustainability of Australia's TCFL industries, through a deliberate and forward looking relationship between supply chain partners within our collective industries.

This submission will address those aspects of the Productivity Commission's Terms of Reference of direct relevance to the Fiji TCF industry, and makes recommendations on future trade and industry policy measures which we believe are in the best interests of both, the Fiji and the Australian industries.

3. STRATEGIC SIGNIFICANCE OF FIJI TO AUSTRALIA'S TCFL SECTOR

3.1. NATURE AND SIGNIFICANCE OF FIJI TCF INDUSTRY

The Fiji TCF industry has, over the last decade developed to be a major contributor to the Fiji economy. In terms of foreign exchange earnings, it now ranks third after tourism (having by-passed sugar in 1997).

Its rapid development over the 1990's has largely been attributed to the preferential market entry provisions to various markets, relatively low labour costs, an attractive package of fiscal incentives and the gradual contraction of the industry in neighbouring countries, principally Australia and new Zealand.

Geographically the Fiji industry is divided into two major areas of activity. One is centred in the east of the main island, around Suva, and the other in the west around Lautoka/ Nadi.

The companies located in the west predominantly manufacture knitted garments for companies such as Australian Horizons who in turn supply to Australian retailers (although increasingly, garments of woven fabrics are being produced in this region).

It is the knit manufacturers who suffered the most from the combination of the political instability ensuing from the coup in May 2000 and the termination of the TCF Import Credit Scheme in September 2000. Knitted garments traditionally are high volume commodity products attracting lower margins and a smaller value added component than woven product.

In the East (principally in Suva), with its predominance of woven garment manufacturers, there have also been significant reductions to employment levels over the last few years; but the rate of company closures has been less. These companies also tend to make on behalf of Australian based companies, notably Pacific Brands (the former Sara Lee/King Gee labels), Yakka and Stafford Ellinson. The garments produced by this sector are more structured and many incorporate special finishes or processes such as 'wrinkle free'. A wider variety of higher cost fabrics are used, including wool and wool blends. These fabrics are sourced from Australian manufacturers including Bruck Textiles, Macquarie Textiles and Bradmill, as well as a higher incidence of third country suppliers.

The Fiji industry to date has clearly been heavily reliant upon the Australian industry for consistency and growth. The association between the Fiji garment manufacturers and the Australian industry falls into two broad classifications; independent Fiji companies producing garments on a cut, make, trim or similar basis for multiple Australian companies and Fiji companies which have a degree of Australian investment.

Fiji industry sources estimate that the major Australian based 'contractors' could be regarded as indirectly employing a third of the Fiji industry. In general, Fiji companies, which have a direct link with Australian companies through ownership or group arrangements, appear to have fared better in recent years.

In general, the garments produced by the Fiji industry are at the lower priced, high volume end, comprising basic rather than high fashion garments. Accordingly decisions regarding design, fabric sourcing and marketing have been traditionally made in Australia.

Consequently, the Fiji industry has had limited propensity, or opportunity, for product development or growth into other export markets. However, in light of the changed situation confronting the Fiji industry after 2000, with the depressed apparel market in Australia and changes to the bilateral trading arrangements, many companies have strived to develop new markets for their operations. An increasing focus is now to develop the necessary knowledge base and additional expertise, by obtaining skilled staff, through training and in developing more strategic relationships with the Australian customer base.

We believe the industry has gone through the worst, and is now settling down to a new base. Industry activity has generally been increasing in the last 12 months, albeit at a moderate rate (noting that employment in the industry in the last 2 years has fallen from 18,000 to 14,000 persons). There is a quiet optimism emerging that perhaps the major restructuring pressure has now subsided and that the remaining companies will be able to consolidate on this new base, pending of course, the Australian trade arrangements to apply post 2005.

3.2. STRATEGIC PARTNERSHIP WITH AUSTRALIA

There is no question that there are strong mutual benefits to be gained through strong trading relationships between the Australian and Fiji TCF industry. Indeed, this view has often been repeated by the Australian Government, eg the Australian Trade Minister, the Hon Mark Vaile upon his visit to Fiji in March 2002, reaffirmed the importance of the relationship and Australia's trade and investment ties with Fiji. Fiji shares the desire he expressed to explore ways to strengthen trade and investment between the two countries.

Fiji presents a viable option for garment and footwear make-up (low cost, short run, highly flexible) for the Australian market while the South Pacific Regional Trade and economic Cooperation Agreement (SPARTECA) accords a reasonable preferential margin for Fiji produced goods. In this way, Fiji can play the same important strategic role for the Australian TCFL sector, as Mexico and the Caribbean Basin do for the US and Eastern Europe and Northern Africa do for Europe.

The regional policies being pursued by the US and EU will have ongoing impact on regionalisation. The highest level and fastest growing area of trade has been within trade blocs, and not between trade blocs. Australia and Fiji are currently excluded from these major trading blocs and consequently, the huge markets they service.

Both Europe and the US are extending their "regional borders" for free trade agreements, enabling geographically close, low cost neighbours preferential access into their markets. These major trading powers see such action as being to their advantage, as their own industries have close strategic relationships (or indeed own) factories within the lower cost countries, and it favours trade between these partners in preference to other (mostly Asian) trading partners.

Under the North American Free Trade Agreement (NAFTA) and the Caribbean Islands Initiative (CBI), US imports from Mexico and the Caribbean Islands have increased significantly, at the expense of Asian exporters (notably China). The US is seeking to expand NAFTA type arrangements with other regions, and has already entered into an agreement with the African Nations (AGOA).

Imports under these agreements can enter the US market duty and quota free, thereby according them a significant advantage over other exporting nations. These arrangements help promote and sustain the US textile sector.

The EU has pursued similar policies. Preferential arrangements are in place with Mediterranean and Central and Eastern European countries, which enable these countries to obtain a larger share of the market.

It is in a similar capacity that Fiji could play an effective and strong role for Australia. However, the preferential incentive accorded Fiji for access to the Australian market is not as significant as that provided by Europe and the USA (which still apply quotas against other suppliers). For Fiji to accord the same benefit for Australian businesses as Mexico and the Caribbean Islands do for the US, or that Turkey and Eastern Europe do for Europe, greater incentive needs to be provided (along the lines identified in this submission).

Fiji garment and footwear manufacture can still offer significant advantages for Australia over Asian supply. Whilst Asia offers prices substantially below those available from Fiji, there are far greater restrictions in terms of volume and turn around. Compared to Europe and North America, Australia is a very small market and accordingly is given a low priority by Asian suppliers and consequently quality and lead times are subject to significant variability. Fiji's reliance upon the Australian market results in a higher level of service and quicker response. Whilst Fiji's manufacturing operations have been considered by some to be relatively inefficient there is a trade off in terms of the flexibility offered.

4. IMPLICATIONS OF AUSTRALIA'S INDUSTRY & TRADE POLICY FOR FIJI

4.1. HISTORICAL POLICY DEVELOPMENTS

The Fiji TCF sector, dominated by garment manufacturers, has developed over a period of some twenty years with the assistance of government policy in NZ, Australia, Fiji and to a lesser extent the United States. The following specific events have had the most significant impact:

- the introduction of the South Pacific Regional Trade and Economic Co-operation Agreement (SPARTECA),
- Australian and NZ government policy on the reduction of tariffs for their domestic TCF sectors;
- the Interim Fiji government's 1987 investment package incorporating 13 year tax exemption for export focussed businesses;
- the introduction by the Australian government of the Import Credit Scheme (from 1992 – 2000);
- the allocation of US quotas to Fiji; and,
- Australia's introduction of the SPARTECA – TCF Scheme in 2001.

Since tariff quotas were abolished by Australia, all TCF products exported from Fiji have enjoyed duty free and unrestricted access to the Australian market, provided they have satisfied the necessary (50%) local content requirements under the SPARTECA arrangements.

Coupled with these arrangements, Australia's Import Credit Scheme has also provided a major boost for Australia Fiji trade, over the 1990's. It provided access to the necessary intermediate product at a more competitive price and in turn, enabled the Fijian output to maintain competitive price points against third country finished products. Consequentially, it also helped generate increased interest by Australian companies in investing in Fiji, and the Fiji garment industry experienced considerable growth in that decade.

4.2. EFFECTIVENESS OF AUSTRALIA FIJI TRADE ARRANGEMENTS

4.2.1. SPARTECA

The South Pacific Regional Trade and Economic Agreement (SPARTECA) was introduced in 1982 and provides for preferential access for most South Pacific products to the Australasian market. Under the general SPARTECA arrangements, TCF goods that have at least a 50% local area content component, receive duty free import access into Australia.

It should be noted that the duty free access provided under SPARTECA is a unique concession offered to the Pacific Island countries (and Papua New Guinea), for the purpose of engendering economic and industry development in the region. That is, SPARTECA is a non reciprocal trade agreement, and Australia receives no concessions in accessing the SPARTECA countries. .

While SPARTECA enables the Pacific Island countries preferential access to the Australian market, the preference margin enjoyed by products sourced from this region has been slowly eroded as Australia's general tariff rates have been reduced. For TCF products, the rate of decline in this preference over the decade to 2005, is as highlighted in the following table:

TABLE 1: **TCF PHASING ARRANGEMENTS - AUSTRALIA**
1995 - 2005 TARIFF RATES (%)

	From 1 July						From 1 January
Sector	**1995**	**1996**	**1997**	**1998**	**1999**	**2000 - 2004**	**2005**
Apparel	40	37	34	31	28	25	17.5
Footwear	30	27	24	21	18	15	10
Fabrics	28/25	25/23	22/21	19	17	15	10

4.2.2. TCF IMPORT CREDIT SCHEME

The Australian Government introduced the TCF Import Credit Scheme in 1992 to help encourage export growth for this sector. It was recognised that major barriers (and/or subsidies) exist in key target markets for Australian TCF products and the ICS was introduced to help offset such constraints for the emerging exporters. It is now well documented that the scheme proved enormously successful in meeting both the Government's and industry objectives.

However the Scheme, coupled with the SPARTECA arrangements, has also provided a major boost for Australia Fiji trade. Not only did the ICS offset the negative effect of the eroding preference margins under SPARTECA, but actually fostered increased production and trade activity.

The benefits to the Australian textile industry of the ICS were obvious, as it provided a major incentive to seek out other markets to the domestic market on a cost competitive basis. However, it also proved to be a major benefit to the Fiji garment industry. Firstly because it provided access to the necessary intermediate product at a more competitive price (and in turn enabled the Fiji output to maintain competitive price points against third country finished products). And secondly, because it helped generate increased interest by Australian companies in supporting Fiji operations.

The resultant relationship between the Australian and Fiji industries flourished to our mutual advantage. The Fiji garment industry emerged as a major source of manufacturing growth for the country. Fiji's TCF exports became the second largest foreign exchange earner behind tourism (and now ahead of sugar). Under the SPARTECA arrangements and at the substantive tariff rates, Australia is the largest destination of TCF exports from Fiji, providing 60% of the market for Fiji made apparel and footwear.

4.2.3. S-TCF SCHEME

The Australian Government decided to introduce the S-TCF arrangements following the termination of the ICS. However, the expiry of the Credit Scheme in September 2000 (after a 3 month extension from the initial scheduled termination date of 30 June 2000) coincided with the political unrest induced in Fiji following the displacement of the former democratically elected Government.

These events conspired to place the Fiji TCF industry (and consequently the Australian industry) in an extremely tenuous position. Consequently, the Australian Government announced, in December 2000, the expansion of the application of the SPARTECA trade arrangements by introducing the S-TCF Scheme.

The introduction of the S-TCF Scheme, whilst clearly not providing the same extent of benefits as the ICS, was intended to assist the Fiji TCF sector to become self sufficient through the development of new products, markets and production capabilities.

The stated objectives of the S-TCF Scheme are to:

- encourage trade in TCF products between Australian and Forum Island Countries (FIC's) and between FIC's
- encourage increased diversity in the manufacture of TCF goods in FIC's; and
- encourage FIC's to market TCF goods and services in markets outside the confines of SPARTECA

Effective from 1 March 2001 (and with retrospective generation of benefits from 1 October 2000), the S-TCF Scheme allows defined textiles, clothing and footwear (TCF) goods manufactured in Forum Island Countries (FIC's), but not meeting all the SPARTECA requirements, to enter duty free in certain circumstances, as outlined below:

- Where a TCF good manufactured in a FIC, has more than a 70% local area content, a roll over of *latent* local area content from it to other TCF goods is allowed. However, only the value of that portion of the local area content that is above 70% of the total factory cost may be rolled over into the determination of "local content" for other TCF goods;

- And, to benefit from this 'rolled over' content, ie. the Excess Local Area Content (or ELAC), a TCF product must have a Minimum Local Area Content (MLAC) of at least 35%. In these circumstances sufficient ELAC would be allocated to enable the subject TCF product to achieve a notional 50% local area content and therefore qualify for duty free entry into the Australian market, under SPARTECA arrangements.

However, despite the Fiji industry's initial expectations, the Scheme is clearly not being fully utilised and the extent of benefits to be derived from the S-TCF Scheme is distinctly limited. The scheme does not provide anywhere near the incentive previously gained from the Import Credit Scheme, and consequently the Fiji industry's customer base has, to a large extent, moved to alternative sources of supply, notably China.

While the Fiji industry recognised that the best way to derive real benefit from the S-TCF scheme would arise through working closely with Australia under a strategic partnership approach, very few Australian companies have been prepared to devote the effort required. The only examples of where the S-TCF is generating some returns are where there is a strong partnership between the fabric supplier, the garment manufacturer and the Australian customer

Essentially, the S-TCF scheme does not provide sufficient incentive for Australian companies to put in the effort to explore the potential opportunities that may be available to them. Yet it is the Australian customers that influence production decisions and the Fiji manufacturers are, unfortunately, heavily reliant on these decision makers.

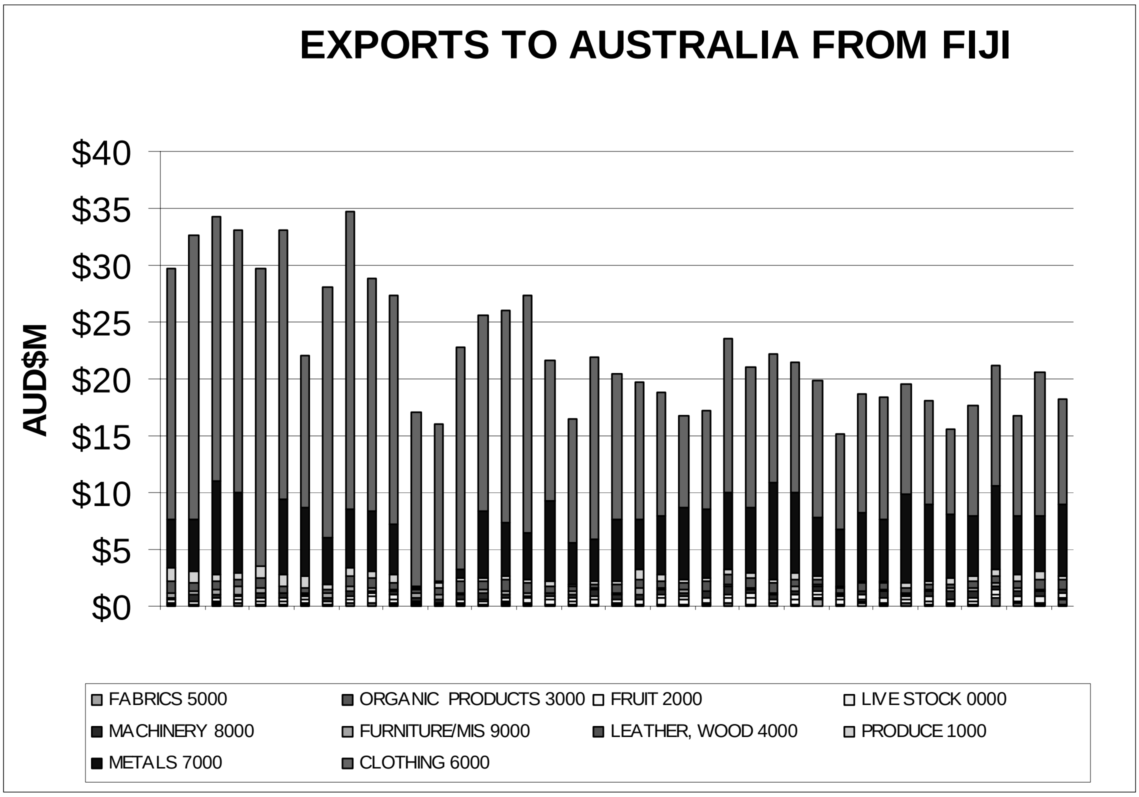
Consequently, trade in TCF products between Australia and Fiji has fallen dramatically since the demise of the ICS Scheme, despite the introduction of the S-TCF.

4.2.4. IMPACT ON TRADE FLOWS

The level of imports of garments from Fiji to Australia has continued to fall over the last two years (as highlighted in the graph below). Thus the S-TCF Scheme has had very little effect in reversing (or even holding) the decline in trade initiated by the combination of continued tariff cuts by Australia, through to 2000, and the termination of the ICS.

The longer term outlook for the TCF industry is also poor. TCF production is facing fierce competition in the Australian market from China. There has been a significant decline in both Fiji's imports from, and export to, Australian from 1999 to 2002. Furthermore, Fiji's exports have declined across all segments of the TCF production, with the knitted garment export being the hardest hit over this period.

Fiji clothing trade is now half of what it had peaked at in 1999. Yet, Chinese imports into Australia continue to keep rising, at the expense of Fiji and Australian clothing manufacturers. The situation now prevailing is considerably worse than what was promised by the Australian Foreign Affairs Minister at the time of the introduction of the S-TCF Scheme.

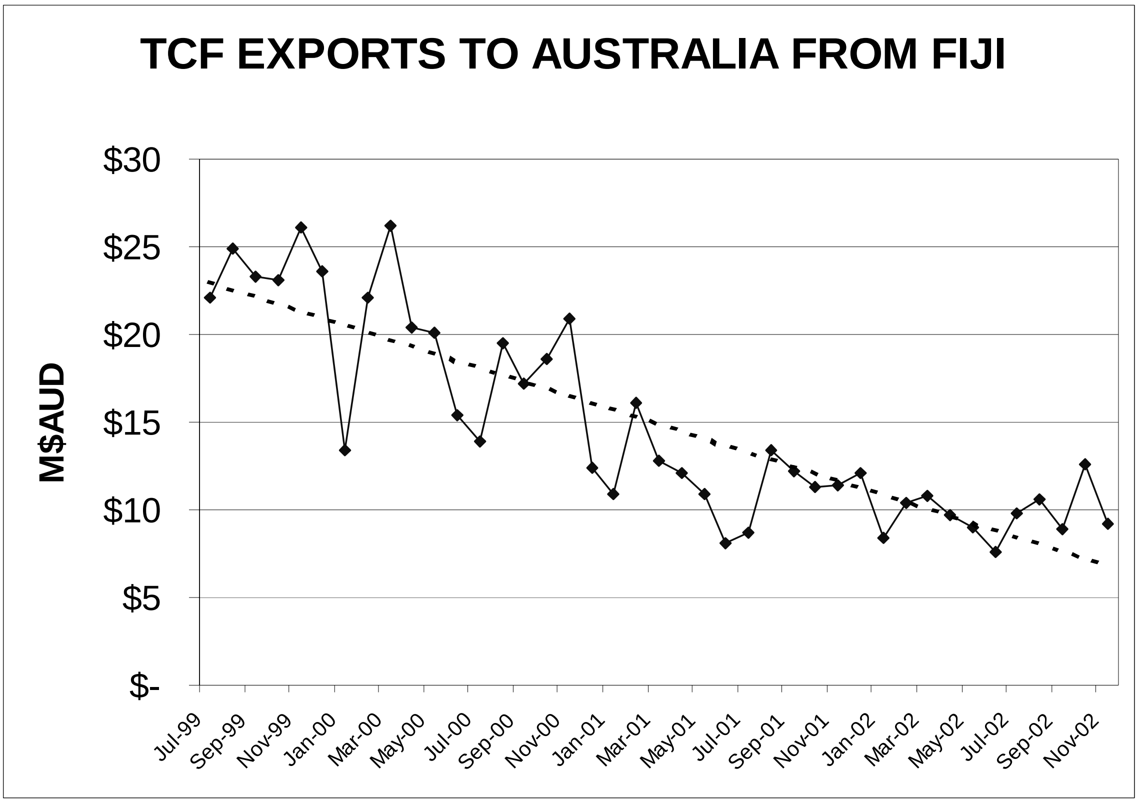


Source: Australian Department of Foreign Affairs and Trade

The Fiji TCF industry continues to feels the negative economic impact of the global environment and of an ineffective S-TCF Scheme. While ratings agency Moody's has changed its sovereign rating of Fiji to stable from negative, indicating an improvement in Fiji's economic and financial situation, the recovery has been patchy. While some industries have recovered, the textile/garment industry has continued to struggle. The industry continues to suffer from short order books and factories are still either closing down, laying off staff or putting expansion plans on hold.

Fiji's exports have declined across all segments of the TCF production, and this trend in trade has continued over the last year (as clearly demonstrated in the following graph).

A further detailed breakdown of trends in trade, between Australia and Fiji, are provided by key product category in the Appendix to this submission *(this data is currently being derived and analysed and will be forwarded shortly).*



Source: Australian Department of Foreign Affairs and Trade

To alleviate this downward trend in exports to Australia, the Fiji Government and industry have tried to break into other markets notably the US market, but the chances of success are slim. The US Government has already entered into an Agreement according African nations preferential access to the US market and in February last year, gave Pakistan permission to increase textile exports to the US by 11-13% over the next three years (as a reward for its support of Washington in the war in Afghanistan). Vietnam is also shaping up as a major competitor within the US market, given the bilateral trade accord signed by the two countries late last year (although the US is now negotiating clothing quota arrangements with Vietnam).

With all of the changes in trade and industry policy, employment in the Fiji TCF industry has fallen from 18,000 persons to 14,000 persons over the last 2 to 3 years. In the main, this has occurred as a direct result of the reduction in trade with Australia.

5. FIJI INDUSTRIES' FUTURE STRATEGIC DIRECTIONS

5.1. ROLE OF FIJI GOVERNMENT

The Fiji Government has been an active participant with its domestic TCF industry, in developing plans and actions that will help the ongoing industrial development of the sector, as was evidenced by the initial introduction of Fiji's Tax Free Factory/Zone (TFF/TFZ) Scheme in 1988. This was a major factor, along with the SPARTECA and Import Credit Scheme, which led to the upsurge of TCF manufacturing ventures being established in Fiji.

Since then, the Fiji Government has continued to provide assistance to the TCF industry (specific and with other industries) through the following means:

I. **TCF industry specific assistance:**

(i) provided grants to the TCF Institute to upgrade human resource development of the Fiji TCF Industry Plan and also addressing the market situation;

(ii) funded a feasibility study to explore the possibility of enhancing trade between Forum Island Countries (FIC) and the USA;

(iii) funded the development of the S-TCF software package to assist the manufacturers in calculating the costs involved in the Scheme;

II. **All Sectors/Industries assistance:**

(i) implemented a new Investment Incentive Package that is appropriate for every investment and provides relief to investors and a stable framework for lone-term investment;

(ii) implemented an Economic Rehabilitation Package for the sectors affected by the May 2000 coup in Fiji which included the manufacturing sector;

(iii) implemented a Duty Suspension Scheme (DSS) in July 2002 to support exporters gain duty free based on certain percentage of exports of eligible items.

However, the major policy that the government implemented, in 1999, for the TCF industry was the TCF Industry Plan. The 5-10 year plan formulated a set of strategies and an action plan to ensure its continued sustainability beyond 2005 when open global competition is due to begin for the textiles sector.

The four main components of the Plan are:

(i) efficiency, productivity and international competitiveness in the TCF industry;

(ii) business environment – domestically and internationally;

(iii) human resource development; and

(iv) the market situation.

Business environment – domestically and internationally

This component required industry to address issues on low productivity, high staff turnover and absenteeism, and declining international competitiveness. The manufacturers are currently addressing these issues on a day- to-day basis.

Efficiency, productivity and international competitiveness in the TCF industry

This component required various government departments to address issues on rising labour costs, high cost of utilities, insufficient supporting infrastructure and eroding levels of preferential access into Fiji's major markets for TCF products.

Due to factors beyond government control, we have not been able to work on this issues. For instance, high internet costs is attributed to a highly regulated telecommunications industry which is protected until 2004.

Human Resource Development

The Government provided grants to Garment Fiji Ltd, later changed to TCF Institute, for human resource development in the TCF sector to increase the skills level of trained personnel thereby improving productivity in the TCF industry.

A grant of $1,025,413 was provided to cover the operating costs and capital costs of the Institute in the past three years. In terms of training, 8,631 people have been trained in the following areas: machinist, mechanical; sewing machine, service & maintenance; Supervisory development; quality; design; technical; business planning; award courses; and consultancies.

Market Situation

The Government, in its efforts to address the market situation undertook various efforts to address eroding levels of margin preference under SPARTECA. In this regard, government made submissions to the Australian government seeking improvements to the Rules of Origin (ROO).

The Fiji government was also granted three derogations to the ROO prior to the expiry of the Import Credit Scheme arrangement.

On the exploration of other markets, Government funded a consultancy to explore the prospects of an enhanced trade agreement between the Forum Island Countries and the USA. Since the proposal require the participation of the Forum Island Countries, Fiji raised the issue at the recent 43rd Forum Island Leaders Meeting that was held recently in Fiji.

Proposed trade agreement between FIC and the USA

The Government funded a feasibility study to explore the possibility of enhancing trade between Forum Island Countries and the USA under a similar agreement as the AGOA agreement for sub-saharan countries. Since the initiative will involve FIC, the topic was introduced at the 43rd Forum Island Leaders meeting that was held in Fiji. The Forum Secretariat will conduct a feasibility study on the issue.

Investment Package

The Investment Incentives Package became effective from January 2001. The intention of the new package is to make incentives transparent, easily available, automatic and non-discretionary with the aim of increasing investment in Fiji.

The incentives package encompasses eight principles as follows:

- low tax rates;
- income taxed only once;
- low duty rate on production inputs, construction; and capital materials;
- accelerated depreciation allowance;
- investment allowances;
- loss carry forward;
- duty free input for exports;
- export income tax deductible.

Duty Suspension Scheme (DSS)

The DSS is a government initiative introduced as part of the Investment Package (2001) to enable Fiji exporters to use world priced inputs into their products to make them more competitive. Firms that have been, or would have been entitled to concessions under the TFF/TFZ Scheme can participate in this Scheme.

Under the DSS, a member would be provided credits to import duty and VAT free based on a proportion of dollar of imports of raw materials required to produce exports. This scheme is available to those companies that would have been entitled to concessions under the TFF/TFZ Scheme or the Fifth Schedule Exports Incentive Scheme. To participate in the Scheme, interested companies are required to join the Exporters Club.

5.2. INDUSTRY FOCUS

Key drivers for the industry, and the reason for Australia's interest in the Fiji industry as an integral adjunct to its own operations, are:

- Close to Australian market
- Quick response capacity
- English speaking
- Cost competitiveness
- Strength of strategic relationship between Australian and Fiji companies

The Fiji industry has vigorously been pursuing activities that will improve its future competitiveness. These include:

- Actively seeking new export markets, beyond Australia
- Improving skill levels in the workforce
- Increased focus on workplace practices to improve overall productivity levels and business efficiencies
- Addressing workplace relations to instill a greater loyalty within the workforce to reduce staff turnover and absenteeism
- Exploring scope for increased investment to strengthen supply chain relationships within the industry
- Improved dialogue between Australian and Fiji industry to collectively address, in a strategic manner, their future growth and development opportunities.
- Rewarding local supply and labour performance, which has and will continue to raise local cost structures
- Increasingly looking to add higher value to Fiji production; eg with the possible advent of new and improved facilities to undertake embroidery, screen printing, washing and dyeing locally
- Increasing the work content of local garment production, through the provision of extra features such as extra pockets, finer detail on stitching and elaborate packaging (which also add value to the finished product)
- Exploring avenues to target markets beyond Australia (eg ongoing exploration of US market prospects over the last 2 to 3 years).

The industry was, and in certain important industry segments still is, engaged in meaningful dialogue with sectors of the Australian industry to develop longer term, strategic partnerships that will be of mutual and collective benefit. Under this partnership approach, the industry was becoming increasingly focussed on developing and enhancing the local support infrastructure, on improving training and skills development and on targeting external markets beyond the immediate Australia Fiji region (as highlighted above). This latter aspect mirrored the Fiji Government's own recognition that Fiji needs to reorient outwardly to the large global markets for the income derived from the export of goods and services.

The Fiji industry recognises that the implementation of trade liberalisation arrangements under the auspices of the WTO and APEC will significantly erode, and to some extent make redundant, the preferential access currently available under SPARTECA, Lome (Europe) and GSP schemes. There has been an increased focus on the need to develop niche markets to break free from the current over dependence on preferential access entry provisions. To be successful in this endeavour, the industry will have to strive to create higher efficiency, productivity and quality.

But to date the industry has been responding to customer requirements which generally have been to produce basic merchandise at low cost. This means Fiji manufacturers are essentially being geared by their customers to remain producers of low, cheap and poor quality garments, competing directly with low cost producers from countries such as China, Korea, Thailand, Indonesia, Vietnam, Sri Lanka and Bangladesh.

To break out of this vicious circle, the industry will need to focus more on developing new products and be prepared to market these, itself.

Priority will need to be given to phasing in the full spectrum of technical and management training that is needed to sustain the industry over the medium to long term. This must be premised on the learning of product design and production processes and procedures, that are characteristic of advanced garment manufacturing industries. Only by investing in human and managerial capital will the industry be able to create competitive advantage and keep pace with technological progress.

There is also potential for the industry to substantially improve productivity. This could be achieved through introducing better in work handling and transport systems, re-designing production lines, and introducing low cost attachments and other modern aids and piece work systems. This will however adversely affect the ability of manufacturers to fulfil the rules of origin requirements under SPARTECA.

6. AUSTRALIA'S FUTURE TRADE & INDUSTRY POLICY

The Fiji economy is still developing. After a number of setbacks in recent years, there is still a long way to go and the nation continues to need a supporting hand from countries like Australia. But that support need not be through general Aid programs, but should be geared towards ongoing industry development.

The TCF industry in Fiji offers the greatest opportunity to accelerate economic and industrial development for Fiji, and Australia can help this development through a combination of trade policies and targeted assistance. This can be done strategically, so that it in turn helps Australian industry and allows the two industries to develop in strategic partnership.

6.1. GLOBAL TARIFF ARRANGEMENTS

As highlighted above, SPARTECA's margin of preference has been progressively eroded as part of the Australian Government's drive to open up the domestic economy by continually reducing tariffs on TCF imports from other countries. While the tariff pause accorded to the industry for the 5 years 2000 to 2005 has provided some relief for this, Fiji's competitive position was already seriously eroded by then.

By 2005, the tariffs on imports would reduce to 17.5%, meaning an erosion of preference by one third from existing levels. Fiji will find it increasingly difficult to compete in the Australian market against other (Asian) low cost producers whose costs of labour and utilities are 5 to 10 times lower than Fiji's.

However, the Fiji industry will continue to strive to improve its production efficiencies and cost structures, as per its industry plan identified earlier in this paper, to compete in this environment.

But the new tariff structure will impose considerable further pressure on both Fiji and Australian industry, and further restructuring will be essential. It is vital that Australia's tariffs be maintained at the scheduled 2005 levels for at least a further 5 years, if not longer.

6.2. S-TCF SCHEME

As stated earlier, the S-TCF Scheme has not proved as beneficial for the industry as had been hoped (and promised). In large part this is because it offers limited incentive for Australian industry, who are key partners in the ongoing development of the Fiji industry.

To the extent that Australian customers are interested in sourcing 3rd country fabrics, their prime concern is price, and it is cheaper and less involved to source the finished (rather than intermediate) product from these other sources. The prevailing attitude from the Australian customer is that it is all too hard to try to utilise the S-TCF scheme; ie that there is no point in getting fabric in China for example, freighting it to Fiji, struggling with points determination and allocation, and then trying to convert to garments in a relatively high infrastructure cost country. From their perspective, It is simpler and cheaper to make up in China and pay the 25% duty on entry into Australia. This attitude will be even more pronounced at a duty of 17.5%.

Compounding this attitude and perception is the fact that the Australian retail market has experienced a significant downturn in the very period in which we were hoping that the scheme's introduction would provide some impetus to our bilateral trade.

Fiji recognises that the S-TCF Scheme was not intended to provide the same extent of benefits as the ICS, but it was expected that it would provide sufficient support to assist the Fiji TCF sector to become self sufficient through the development of new products, markets and production capabilities. It was also expected, indeed it was a key pre-requisite of the early considerations on alternative support arrangements, that it would contain the fall off in trade, expected as a result of the ensuing disruption caused by the termination of the ICS.

None of the stated objectives for the Scheme (highlighted earlier) have eventuated to date, and are extremely unlikely to eventuate in the absence of any modifications to the Scheme. If the Scheme is to continue beyond 2005, it is vital that the Australian Government be more receptive to making immediate modifications to the Scheme when a need is demonstrated.

The Fiji industry has been seeking the following modifications to the Scheme for the past 2 years, since the Scheme's implementation, but despite the steady fall off in trade, it has not been accommodated:

1. Reduce MLAC thresholds to 25% for all products

2. Remove the deeming provision

3. Extend coverage of the scheme to include wool products

6.3. AUSTRALIA'S POSITIVE ASSISTANCE

Fiji notes Australia's positive assistance schemes, designed to encourage further development of Australia's TCFL industries, and the fact that they appear to be working well.

TCF Strategic Investment Program

SIP in particular appears to be offering the necessary incentive to help drive desirable change within the industry. Indeed, Fiji industry is conscious that the concept of support to encourage investment in new capital equipment, latest technologies and innovative product development and process improvement, would also prove a major and positive driver for Fiji's industrial development.

Market Development is also important to Fiji. Similar activity should be funded in Fiji, as there is no reason why Australian firms should not be encouraged to develop new markets utilising Fiji make up.

If Fiji industry is recognised as a viable, strategic partner for Australian industry, then it should be possible to extend SIP funding to investment in Fiji. This could be accommodated, either by allowing Australian companies' expenditure in Fiji to be eligible for SIP, and/or providing aid money to Fiji government to provide similar level/type of support for Fiji industry. This would be in Australian industry's interest as Fiji provides a source of low cost labour and pull through demand for Australian fabrics, trims and leathers.

Overseas Assembly Provisions

The Australian Government has recognised that with the continued annual reduction in tariffs that a large part of the domestic clothing industry will be forced offshore. In turn, this will reduce demand for local textile output unless measures are put in place to help maintain a "pull through" of Australian textiles with the newly established offshore arrangements. Fiji understands that it is for this reason, the Government decided to modify, and extend the previous OAP arrangements until 2005.

Consequently, under the Scheme, registered firms have been able to import garments produced in third countries, utilising Australian fabric, with duty payable only on the overseas value added. This has further diminished the margin of preference gained under SPARTECA and instills greater urgency for the need to offer targeted assistance to encourage the collective development of an Australian/Fiji textiles/clothing supply chain that can draw on combined advantages/attributes to compete more effectively in world markets

The EOAP has encouraged the focus of Australian companies to shift from Fiji to lower cost sources of garments, utilising the scheme. However, the EOAP is not really a practical option for more complicated or tailored garments and is more attractive in the manufacture of simple garments (eg. T-shirts and skirts). In the latter case, the overseas value added is low and thus the duty cost, on "re-entry" of the finished product into Australia, is minimal as it is only applied to a small proportion of the overall value of that product. However, as Australia's tariff reduces, we would envisage that the attraction of the EOAP scheme will also commensurately diminish.

6.4. ALTERNATIVE MEASURES OF SUPPORT

In his speech to the Fiji Australia Business Council at its Annual Conference in 2000, Australia's Minister for Foreign Affairs, the Hon Alexander Downer, identified many challenges ahead for Fiji and its industry. Indeed, some of the specific difficulties confronting the Pacific Island countries that he highlighted were:

- Declining trade competitiveness, particularly due to the declining margins of preference compared to third country imports *(as noted above)*

- Paucity of good and comparable data to support policy advice and development

- Falling levels of investment.

The Minister did though go on to say that Australia stands ready to assist Fiji (and other Island nations) in areas which will help to create sustainable economic growth and improve employment opportunities **and that he would be open to ideas from Fiji**. He stated that the Pacific Island region and the regional agenda is one of Australia's major foreign policy priorities. This supposedly provided the opening for Fiji to pursue innovative and resourceful proposals with the Australian Government to help drive the quantum change that is needed to position its industry in such a way that ensures its long term future and sustainability.

Fiji industry is strongly of the view that Australia and Fiji both need to develop programs that will help strengthen the strategic relationships between the Australian and Fiji industries, for the mutual benefit of both industries. This is not only in the Fijian industry's interest, but also in the Australian textile sector's interest. Australian industry is vitally concerned to see the Fiji garment sector remain viable, as this provides an obvious opportunity to maintain a significant market for its fabric output. But if the competitive advantage is not there, Australian textilers will be forced to look for linkages beyond Fiji (especially given likely prospects utilising the EOAP's). While the preference, and arguably significant potential, would be in collectively marketing Fijian garments, made from Australian fabric, in all world markets, this will not be possible unless some major bilateral mechanisms are introduced to facilitate such an outcome.

We note that the US industry has a close relationship with the clothing industry in Mexico and the Caribbean, as does the European industry with the garment manufacturers in Eastern Europe. It is in a similar capacity that Fiji could have played (and still can play) an effective and strong role for Australia. However, the preferential incentive accorded Fiji for access to the Australian market is not as significant as that provided by Europe and the USA (which still apply quotas against other suppliers). For Fiji to accord the same benefit for Australian businesses as Mexico and the Caribbean Islands do for the US, or that Turkey and Eastern Europe do for Europe, greater incentive needs to be provided. The S-TCF as it currently stands is not enough and clearly further modification to this scheme is warranted.

It was hoped that the S-TCF scheme would help minimise this negative impact on the industry, but it is clear that the scheme is not being fully utilised and indeed, that the industry seriously misjudged the expected benefits of the S-TCF.

Principally, the scheme does not provide the edge that ICS gave, and the Fiji industry's customer base has, to a large extent, simply decided to move to alternative sources of supply, notably China.

It was always recognised, by the Fiji industry at least, that the relationship between Australia and Fiji needed to be on a strategic partnership basis, and that any benefits under the new scheme would not materialise unless future strategies were developed on this basis. That is, with Australia supplying the design and marketing expertise, and Fiji the efficient, quality make up.

But this has not eventuated, as the S-TCF scheme does not provide sufficient incentive for Australian companies to put in the effort to explore the potential opportunities that may be available to them. Yet it is the Australian customers that influence production decisions and the Fiji manufacturers are, unfortunately, heavily reliant on these decision makers. The only examples of where the S-TCF is generating some returns is where there is a strong partnership between the fabric supplier, the garment manufacturer and the ultimate manufacturer.

However, a definitive program is warranted to bring the industries together, to work closely for mutual and strategic benefit. Minister (Downer) has stated that his preference is for enhanced links to be developed between business people, which can then contribute to "the development of private sector linkages and to economic growth". That is, he would like to see the stimulation and growth of the Fijian economy driven by private sector. By joining forces, the Australian and Fijian textile and clothing industry can help deliver this, provided a conducive (trade and industry) policy framework is provided to help facilitate such a focus.

Certainly, there would appear to be significant scope to expand into the US and European markets utilising the added advantage of quota free entry for Fijian exports coupled with the market knowledge and expertise of Australian firms.

Prior to the introduction of the S-TCF, certain companies from both countries' industries were exploring this issue together and came up with the idea of a Partnership Development Scheme to provide a sound base for the collective Australia Fiji TCF industries to consolidate their operations, to strengthen their commercial and strategic relationships and to develop the industries' overall international competitiveness. The major objectives of the Partnership Program would be to:

- improve the free flow of trade and investment within the region
- encourage further product promotion and international market access of product utilising the collective skills and knowledge of the Australian/Fiji interests
- foster increased investment in the industries, and
- promote training and skills development within the industry in Fiji

The introduction of the Scheme would ensure Australian fabric and other intermediate products can be landed competitively in Fiji:

Under the Partnership Development Scheme, A "Partnership Entitlement" would be accredited, by the Australian Government to Australian manufactured intermediate goods exported to Fiji, for use by the latter's TCF sector. The Entitlement would be provided on the basis of up to ,say, 30% of the Australian value added of the exported product. The "Entitlement" would be provided by the Australian Customs Service upon application (including proof of export) by the Australian manufacturer of the exported product, and the value of the "Entitlement" can be offset against tariff duties on third country TCF imports into Australia, and would only be applied as part of the bilateral agreement between Australia and Fiji:

- to considerably reduce the cost base for the Fijian garment and footwear industry, and
- to maintain strong demand for Australian produced fabrics and other inputs

Alternatively, given that Australia's current TCF programs seem to offer the necessary encouragement, consideration should be given to extending those schemes to Fiji activities.

Could extend SIP to include expenditure by Australian companies in Fiji provided it can be demonstrated that this is having net flow on benefits to Australian economy and industry – eg investment in new plant and equipment, extending industrial infrastructure to textiles/dyeing and finishing, market development focussed on Fiji make up of Australian textiles.

Similarly, Fiji government could provide similar schemes, but in first instance may need aid monies from Australian government to help fund it. Would only provide assistance to those firms utilising Australian fabrics (on a pro rata basis).

Australia is paying $25 million to help law and order. This is a valuable contribution to Fiji and is clearly directed to a specific need within the country. However, a similar concept could be used to encourage industrial development to generate employment (and thus relieve pressure on social disorders).

Australia US Free Trade Agreement

Market access can clearly be further enhanced by the Australian/Fiji industries jointly, focussing on opportunities beyond the Australia Fiji region. The industries:

- Recognise significant scope to expand into the US and European markets utilising the added advantage of quota free entry for Fijian exports coupled with the market knowledge and expertise of Australian firms

- Recognise need to reorient outward to the large global markets

In light of this, the Fiji garment sector is increasingly looking to the United States to sustain operations and for new market opportunities. Existing arrangements with the US are sustaining the Fiji industry with many knit based factories doing subcontract work for this market. The US market, being in the Northern Hemisphere is regarded as being complementary to the Australian market, however it is a much tougher market requiring good quality and extremely lean prices. The gestation period for orders is also much longer with reported lead times of up to 12 months from initial interest to order placement.

As mentioned in Section 5 of this submission, on future industry directions, the Forum Island Countries are seeking to develop enhanced trade between the FICS and the USA, and further research is being undertaken to help facilitate this.

However, Fiji notes that Australia's negotiations with the US on a free trade agreement are gaining momentum. There would appear to be good prospects to introduce Fiji activities into the parameters of that trade agreement once it is finalised (Fiji recognises that this concept should not be introduced too early in the negotiations, as it will confuse the situation). But once an Australia US Trade Agreement is finalised, it would be of benefit for both Australia and Fiji for Fiji make up activity to be introduced through special Trade Preference Level Agreements with the US. Once again this provides the advantage of a lower cost source of make up for Australian customers wishing to target the major US market, and provides more extensive scope for pull through demand for Australian fabrics.

7. CONCLUSION

The TCF industry is crucial for Fiji's economy in terms of employment provision and foreign exchange earnings. The Government has acted for the recovery for the industry in times of crisis and need as it sees it as a significant industry for the people of Fiji.

With the changes in Australia's industry policy arrangements, Australia Fiji trade is clearly at the cross-roads. Under current scheduled arrangements, the future prospects are not encouraging.

A partnership approach to future trade and industry development by Australia and Fiji is strongly advocated to ensure the long term sustainability and international competitiveness of the collective TCFL industries. The implementation of more meaningful trade and industry policy measures, targeted at building the strategic relationship between Australian and Fiji TCF, will provide:

- A bilateral benefit to the TCF industries of both countries
- The most effective means of support to the Fijian TCF industries, which will continue to enjoy more cost effective inputs as well as the flexibility of short lead times
- A means for continued investment and export by Australian textile companies and security for their employees and Fijian garment manufacturers and their workforce
- A sound base for the joint Australia Fiji textiles and clothing industry to consolidate their operations and build for the future
- An opportunity to support these industries without contravening World Trade Organisation obligations, as Fiji is an emerging economy and can rightly adopt measures to help accelerate this process.