7 April 2003

Dr Robertson
TCF Inquiry
Productivity Commission
PO Box 80
BELCONNEN ACT 2616

Advice•Networking•Support•Advocacy

Dear Dr Robertson

Australian Business Ltd. (ABL) is an independent, broad-based business improvement organisation with a history of achievement spanning more than 115 years. A member-based organisation, ABL represents over 17,000 small to large businesses.

As one of Australia's largest business service organisations, ABL provides advice, networking, support and advocacy services for its members, as well as contributing to government policy development.

ABL aims to help businesses grow and its large membership base is some measure of its success. Consultation with ABL's TCF&L members reinforces their commitment to successfully adjusting to a more internationally competitive and commercially viable future. The sector is not seeking ongoing and indefinite forms of industry support and protection.

Given the extent of the impact that changes to current levels of industry assistance will have on the TCF&L sector and related industries, ABL appreciates the opportunity to contribute to this inquiry.

Attached is ABL's submission informing the Productivity Commission Inquiry into post-2005 Textile, Clothing and Footwear Assistance Arrangements.

ABL would be pleased to expand on the issues raised in this submission at a later date.

Yours sincerely

Paul Orton

Paul Orton
General Manager, Policy

Address: 140 Arthur Street North Sydney NSW 2060 **DX:** 10541 North Sydney Locked Bag 938 North Sydney NSW 2059
Telephone: 02 9458 7500 **Customer Services**: 13 26 96 **Fax**: 02 9923 1166
Email: member.services@australianbusiness.com.au **Internet**: www.australianbusiness.com.au
Australian Business Limited *ABN 63 000 014 504*
ABL Offices: Ballina, Canberra, Gosford, Newcastle, North Sydney, Parramatta, Port Macquarie, Murray Riverina, Tamworth, Wollongong

Australian Business Limited

YOU CALL, WE ANSWER.

Productivity Commission Inquiry

Post-2005 Textile, Clothing and Footwear Assistance Arrangements

April 2003

www.australianbusiness.com.au

TABLE OF CONTENTS

For further information contact:

Paul Orton,
General Manager Policy
Tel: (02) 9458-7544
Email: paul.orton@australianbusiness.com.au

ABL INTRODUCTION

Australian Business Limited (ABL) is a long-standing employer organisation providing broad-based business improvement support to members and clients. ABL's 17,000 members are predominately small and medium enterprises engaged in a range of business activity across NSW. This membership includes affiliation with the Illawarra and Hunter Business Chambers.

ABL Services to members include:

- Policy development and lobbying activity on behalf of our members on both Federal and State business issues.
- International Trade and Business Solutions supporting business to access international markets and capital for growth.
- Industry-specific interest groups including Textile Clothing & Footwear, Innovation, Food and Beverage, Defence and Information & Communications Technology.
- Entry level and existing worker skill development programs through ABEN (New Apprenticeships Centre) and Small Business Training Company.
- Member advice on employment and Human Resource issues, and compliance related support for Workers Compensation and Occupational Health & Safety
- Australian Business Industrial is the Industrial Relations Affiliate of ABL and is a party to a range of State awards
- Australian Business Lawyers who provide support for workplace related legal issues.

ABL is a founding member of the Australian Chamber of Commerce and Industry (ACCI), the peak council of Australian business associations. ACCI helps represent ABL members' interests on a federal and international level.

In developing its response to the Productivity Commission's Inquiry: Post 2005 Textile, Clothing and Footwear Assistance (TCF&L) Arrangements, ABL has:

- drawn on its own commissioned research over the last 12 months,
- referenced available statistics against employer perceptions, and
- consulted with TCF&L member businesses to identify the opportunities and barriers facing the industry and discuss their views on the future of the Australian TCF&L industry. The consultation identified disparate needs within the sector.

Additional to the above targeted research, the Australian Business Foundation, an independent research think tank of which ABL is the major sponsor, has recently produced a body of work focusing on innovation, new forms of business competitiveness, opportunities in a knowledge-based economy and collaborative business models.

1. EXECUTIVE SUMMARY

ABL is the major representative body of Textiles, Clothing, Footwear and Leather (TCF&L) businesses in New South Wales. These businesses will be directly and immediately affected by any change to the current structure of tariffs and industry assistance**.** The sector has the potential to successfully complete its current transformation and emerge as a longstanding and economically significant contributor in Australia as well as a powerful participant in the international market. However it requires further commitment and structured guidance from industry leaders, organisations and Government to achieve this.

If many of the current trends continue, the future of Australia's TCF&L industries as a commercially viable sector is in doubt. The exact impact of post-2005 changes to the current suite of industry assistance, including the legislated tariff reduction, is difficult to predict. This situation is further complicated because a sector that is divergent in interests and needs requires a policy response that is tailored to different needs.

RECOMMENDATIONS

Australian Business Limited:

- supports the objective of moving TCF&L tariffs towards the general tariff rate over time but only if accompanied by an appropriate structural adjustment program. The transition to this objective should take into account action by Australia's trading partners in reducing their TCF&L trade barriers.
- suggests the Government review the Strategic Investment Program (SIP) package to reflect the changing needs of the TCF&L industries through the final stages of the sector's transition. Post-2005, the TCF&L sector seeks confirmation that the Government will maintain a structural adjustment scheme to guide the sector through an environment of reducing protection.
- seeks a commitment from the Government to reduce the administrative and commercial burden of accessing the SIP. The current $200 000 threshold of eligible expenditure in relation to eligible activities needs to be reduced to $100 000 and the 5% of turnover grant cap removed.
- calls on the Federal Government to consider incorporating within the existing SIP program, a broadened selection of EMDG eligibility criteria that support TCF&L industries further developing export markets.
- recommends the immediate creation of a TCF&L Globalisation Outreach program, working within the existing SIP allocated funding to educate and guide the planning process of every TCF&L firm in Australia.
- is seeking a commitment from the Government to remove the 3% tariff on business inputs that was instituted under changes to the Tariff Concession Scheme (TCS) in 1996.

Early indications from the economic modeling commissioned by the Productivity Commission are decisive in their conclusions that the removal of the Strategic Investment Program and/or the serious reduction in current tariff levels will deliver marginal benefit to the Australian economy. What is without contention is that the end of the current tariff pause after 2005, without ongoing adjustment from the Government will have a significant and deleterious impact on the TCF&L sector and related industries.

ABL wants it to be clear that the recommendations proposed in this submission are considered to be strategies for completing the final stages of adjustment for the sector. The sector is committed to successfully adjusting to a more internationally competitive and commercially viable future, and is not seeking ongoing and indefinite forms of industry support and protection.

2. INTRODUCTION

The TCF&L sector has historically had higher than average industry assistance and/or tariff rates recognising the sector's difficulty in competing with low cost producers.

The Government is reviewing post-2005 TCF&L assistance arrangements. Its current plan which freezes 2001 tariff levels until 2005, when they drop to 17.5% for clothing and 10% for fabric and footwear, is drawing to a close. Also finishing in 2005 is the Strategic Investment Program, which provides funds to assist companies restructure and increase efficiency.

ABL is the major representative body of TCF&L businesses in New South Wales, who will be directly and immediately affected by any change to the current structure of tariffs and industry assistance. The extent of the impact of changes to the current suite of industry assistance programs in conjunction with the cessation of the tariff pause will be difficult to predict. Forecasting the impact is further complicated by the diverse character of the TCF&L sector.

ABL's submission for this inquiry has been developed with the cooperation of, and in consultation with, its TCF&L members, industry associations and experts.

3. CURRENT STRUCTURE OF THE INDUSTRY

3.1 General

Australia's TCF&L sector is both extremely diverse in terms of its demography and in the nature of its constituent industries. Drawing from ANZSIC codes, the range of industries that contribute to the TCF&L sector include:

- Wool Scouring
- Synthetic Fibre Textile Manufacturing
- Cotton Textile Manufacturing
- Wool Textile Manufacturing
- Textile Finishing
- Made-Up Textile Product Manufacturing
- Textile Product Manufacturing N.E.C.**
- Hosiery Manufacturing
- Cardigan and Pullover Manufacturing
- Knitting Mill Product Manufacturing N.E.C.**
- Mens and Boys Wear Manufacturing
- Womens and Girls Wear Manufacturing
- Clothing Manufacturing N.E.C.**
- Footwear Manufacturing
- Leather Tanning and Fur Dressing
- Leather and Leather Substitute Product Manufacturing
- Textile Product Wholesaling
- Clothing Wholesaling
- Footwear Wholesaling
- Clothing Retailing
- Footwear Retailing
- Fabrics and Other Soft Good Retailing

** N.E.C. – not elsewhere classified.

The TCF&L sector is not one but a series of diverse and heterogeneous industries, within which there are also a number of distinct sub-sectors covering a wide range of design and manufacturing activities.

The TCF&L sector comprises of the following activities:

- The treatment of raw materials
  - Natural fibres
  - Man-made fibres
- The production of knitted and woven fabrics
- The manufacture of footwear
- Finishing activities, and
- The transformation of yarns and fabrics into products such as:
  - Garments, knitted or woven
  - Carpets and other textile floor coverings
  - Home textiles
  - Technical or 'industrial' textiles

The TCF&L industries can be seen as a series of supply chains in which different segments of production and distribution are integrated to form a final product, typically an article of clothing or footwear but broadening to also include industrial and customer-specified products. Collapsing these activities into four supply chains, as with the TCF&L Forum's strategy, results in these categories:

- Early stage processing
- Apparel – clothing footwear and accessories

- Textiles, leather and furnishings for domestic and commercial use
- Technical and non-woven textiles

The total value of TCF&L imports into Australia has increased markedly from $3.5 billion in 1990/91 to $7.4 billion in 2000/01. The areas most affected by the increases in imports are Australia's domestic clothing and footwear industries, where the value of imports account for 45% and 65% of market share respectively. Australia's imports of textiles, fibres, yarns and woven fabrics also increased by almost 20% between 1990/91 and 1998/99 (TFIA: September 2002).

TCF&L industries are still shrinking under the current assistance arrangements. The overall number of employees within the TCF&L sector has dropped drastically since 1985-86 from 116 400 to 72 000 in 2001-02, a drop of approximately 38%. The changing shape of the TCF&L labour force is given more definition by considering that the greatest reduction in jobs comes from the full-time positions (with part-time jobs marginally increasing) and the female workforce (a reduction of almost 45% between 1985-86 and 2001-02).

ABL has played an integral role in the development of Sectoral Action Agendas, especially for the TCF&L sector. These Action Agendas were a key plank underpinning the Government's 1997 industry policy, *Investing for Growth*. It is ABL's view that the "Action Agenda" process has produced a framework for sectoral development, based upon removal of impediments to activity and a "whole of government" approach.

In essence, the TCF&L Action Agenda has provided the opportunity for Government and industry to lift the growth prospects of the TCF&L sector, by developing a shared vision to address impediments to future growth and competitiveness.

The industry assistance packages provided by the Federal Government have made a significant contribution to assisting and guiding the transformation of some members of the TCF&L sector. In addition to the tariff pause, the programs offered by the Government include:

- $678 million (over 5 years) TCF&L Strategic Investment Program (SIP);
- the TCF&L Technology Development Fund;
- the National Framework for Excellence in Education and Training;
- the TCF&L Market Development Program; and
- the Expanded Overseas Assembly Provisions (EOAP) Scheme.

Clearly, the programs have facilitated the commitment and engagement of the TCF&L sector in meeting the challenges of their changing environment. However, feedback from ABL members indicates that smaller businesses still struggle to successfully manage the transition to a low tariff regime. The inherent characteristics of the small business; with restricted cash flow, limited resources and smaller investment and expenditure capability accounts for the poorer uptake of the Government's assistance measures.

Despite the extensive restructuring of the sector to date, there are still more challenges to face and more change required if Australia's TCF&L sector is to have a commercially viable future. Industry must continue to build on the restructuring that has already occurred, but importantly build and enhance their sustainable competitive advantages in the face of tariff reduction, global competition and changes in technology and innovative practices.

Industry assistance for the sector has been significantly reduced in Australia, including the abolition of all quotas in 1993 and the termination of production bounties in 1995. Interestingly, a large number of Australia's trade competitors have not matched these efforts. This has resulted in Australia's TCF&L marketplace being relatively open when compared to other developed economies.

The Government has seen an active commitment by some TCF&L businesses to respond to the drivers of this change and use the SIP package to rejuvenate and recreate these older industries and better position themselves for their new future. However, this process is time consuming and not yet completed. A reviewed and recast version of the SIP package post-2005 could be effectively tailored to address the specific needs of those businesses in the final stages of their adjustment to tariff reductions.

The partnership between the Government and the sector has been the key factor in establishing and driving the transition of the TCF&L sector. The SIP scheme was developed by the Government in 1998-99 following broad consultation with the TCF&L industry, and provides the following kinds of grants:

- Type 1 grants in respect of new TCF&L plant/building expenditure
- Type 2 grants in respect of TCF&L R&D/product development expenditure
- Type 3 grants in respect of TCF&L value-adding
- Types 4 and 5 special grants in respect of TCF&L-dependent communities

Smaller TCF&L businesses report that they are unlikely to access the scheme's grants because smaller business is less able to meet the scheme's eligibility criteria. The scheme's key aspects affecting small business include:

- a minimum $200,000 investment threshold (accumulative over the life of the Scheme) for access to grants;
- a maximum grant entitlement in a program year of no more than an amount equivalent to 5 per cent of sales in the previous 12 months
- payment of grants in arrears.

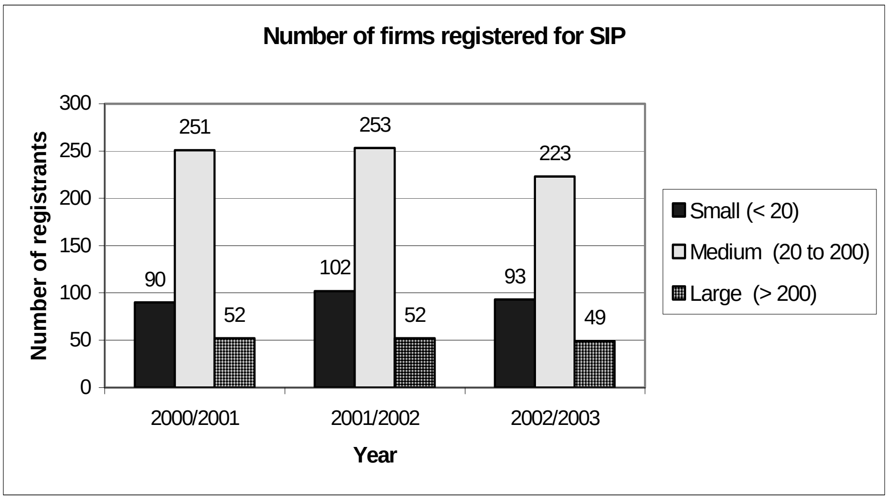
Small businesses in particular have reported barriers in taking up the SIP grants. This anecdotal evidence is supported by the figures in Graphs 2 and 3, which are derived from the Department of Industry's Review of the Textile, Clothing and Footwear Strategic Investment Program Scheme: September 2002. Further feedback from smaller TCF&L member companies suggest that the scheme is focussed at larger companies and is not friendly toward rapidly growing SMEs.

Graph 1 suggests that the majority of firms registered for SIP are medium sized. This partial data raises a number of points:

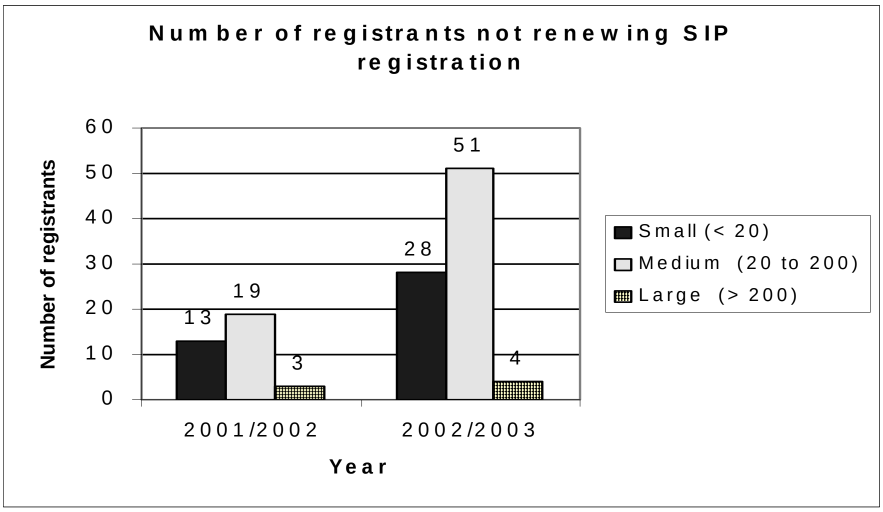
- ‘Medium’ includes firms with up to 200 employees which some would classify as ‘large’,
- The distribution of registrants within this band is not known
- Total grants to firms within each size segment may or may not mirror the distribution of registrants across the size segments
- It would be useful to compare the distribution of registrants and grants with the size distribution of all firms within TCF&L.

However, it does seem clear that small firms are under-represented as SIP registrants.

Graph 1



Graph 2



Source: Department of Industry: Review of the Textile, Clothing and Footwear Strategic Investment Program Scheme, September 2002

3.2 Political and Economic Context

Government policies, both internationally and locally, are the major strategic drivers for the development and operation of TCF&L industries around the world. Traditionally a highly protected sector, world trade in TCF&L products has been dominated for the last 40 years by restrictive import quotas in the significant importing countries (the EU and USA), and subject to strong tariff and non-tariff barriers in the major exporting countries (Asia and the Indian sub-continent).

Since 1995, international trade in textiles and clothing has been governed by the WTO Agreement on Textiles and Clothing (ATC). The intent of the WTO Agreement is for countries to relinquish discriminatory practices between their trading partners. This principle is known as most-favoured-nation (MFN) treatment. The ATC is progressively bringing world trade in textiles and clothing within the ambit of the WTO/GATT rules. All global restrictive quotas on TCF&L products are to be eliminated by 1 January 2005.

The move to eliminate global quotas by 2005 will provide low labour cost countries such as India, China and Pakistan with improved access to markets in developed countries. China will especially benefit from the removal of global quotas, as it presently does not receive MFN from the USA.

With many aspects of clothing and footwear production unable to be automated, Australia's relatively high labour costs will continue to be a significant cost disadvantage for these domestic industries. As a consequence of the elimination of global quotas, competitive pressures will increase in most markets, many of which already experience productive over-capacity and a glut of imported products. This situation will only be further exacerbated given the Australian Prime Minister's commitment to tariff-free access for the world's 50 poorest countries as of 1 July 2003.

1 January 2005 will mark yet another significant movement in the evolution of the TCF&L international trading environment. The Government's intention to further reduce Australian TCF&L tariff levels, and the full implementation of the WTO Agreement on Textiles and Clothing requiring all WTO countries to have abolished all TCF&L restrictive import quotas will increase the global and domestic market share of products exported from low labour cost countries. In 1999 Asian countries accounted for approximately 45% of all world clothing production and that figure is expected to reach 60% by 2005.

The impact of the Asian financial crisis at the end of the last decade further highlighted the extent to which the Australian TCF&L sector has already globalised and the strong influence of international factors domestically. Affecting both the supply of inputs into the domestic industries, and the ongoing oversupply of competitively priced textiles, the economic slowdown in many of the Asian countries has had a damaging impact on Australia's textile and apparel production.

3.3 Non-tariff Barriers

The United Nations Conference on Trade & Development (UNCTAD) system for trade and control measures acknowledges that there has been a proliferation of non-tariff barriers (NTBs) as trade control measures used by countries in the face of trade liberalisation. Presently there is better information on tariffs than NTBs, both in precision and in its ability to serve as an indicator of restrictiveness.

While past trade negotiations have strengthened disciplines on the use of these types of trade barriers, concerns voiced by the private sector and disputes between governments indicate their persistence.

Analyses of NTBs tend to focus on bans, quotas and trade policy instruments taken at the border. Concerns have changed over time, with increasing application of less visible barriers resulting from technical regulation and domestic and international policies that affect international trade and investment flows.

Non-tariff barriers, such as technical regulations and industrial standards may produce the same outcome in restricting trade as tariffs.

More work by industry and the Government is needed to better identify the existence of NTB’s and their impact.

4. VISION FOR THE INDUSTRY

In recent years, the Australian TCF&L sector has been faced with the alternative of either becoming a vital and dynamic component of the world economy or dismantling as a commercially viable sector. In May 1999, the Commonwealth Government established the Textile, Clothing, Footwear, Leather Action Agenda Advisory Board to foster a partnership between government and industry, to pursue the development of an Action Agenda for the TCF&L industry and provide a basis for strategic planning and future prospects for the sector.

Since its inception, the TCF&L Action Agenda and more recently the TCF&L Forum Strategic Plan have guided the structural adjustment that continues to accompany the sector's strategic transformation. Fuelled by globalisation and underpinned by sympathetic changes in Government policy from the post war protectionist regime, the sector's future viability depends of increasing their export targets in addition to claiming a larger share of key domestic markets.

The 10-year vision developed by the TCF&L Forum in 2002 is worth repeating.

By 2012, the Australian TCF&L industry will be market led and globally focussed, with innovation expertise and world leading lifestyle niche brands driving a doubling of exports, thereby growing annual production to over $14 billion and enhancing profitability.

Area of Change	From ➨ ➨ ➨ ➨ ➨ ➨	To
Industry Image	Dying	Opportunity
Focus	Product	Consumer
Market	Domestic	Global
Segments	Survival/Commodity	Performance/Image
Competitive Driver	Cost	Innovation
Brands	Few and diffuse	Strong and niche
Sales	Decline	Growth
Route to Market	Retailers	Supply chain partnership
Product Offer	Price	Value and image
Dominant Activity	Manufacturing	Marketing
Supply Chains	Fragmented and local	Integrated and Asia/Pacific
People	Long term survivors	Young, new entrants
Skills	Simple e.g.: technical	Complex: e.g. business management
Change Agent	Reactive to government	Proactive in the market

The strategy adopted by the Action Agenda Board to achieve its vision for the sector is 'to create an environment that stimulates innovation and cultural change…'. The new market opportunities for the TCF&L sector are more about reinventing 'old' products, new approaches to 'old' markets and new competitive paradigms for 'old' businesses, than they are about entirely new products or new markets. Driven from within the sector, it will be the industry leaders who need to realise the new opportunities ahead.

Research commissioned by the Australian Business Foundation suggests that foresight, planning and innovative solutions by Australian industries in response to globalisation is changing the shape of domestic manufacturing.

One of the oldest sectors in the history of industrial development, TCF&L

industries are often referred to as 'traditional industries' and as belonging to the old economy. Typically Australian manufacturing is characterised as a declining industry of decreasing importance to Australia's future prosperity and competitiveness. The reality of course is that while manufacturing output is increasing in absolute terms, as a proportion of Australia's total output it is diminishing.

Contrary to this 'old economy' view, Professor Marceau's study *Selling Solutions: Emerging Patterns of Product Service Linkage in the Australian Economy,* conducted for the Australian Business Foundation points to an unrecognised dynamism in Australian manufacturing and a new set of competitive strategies at work.

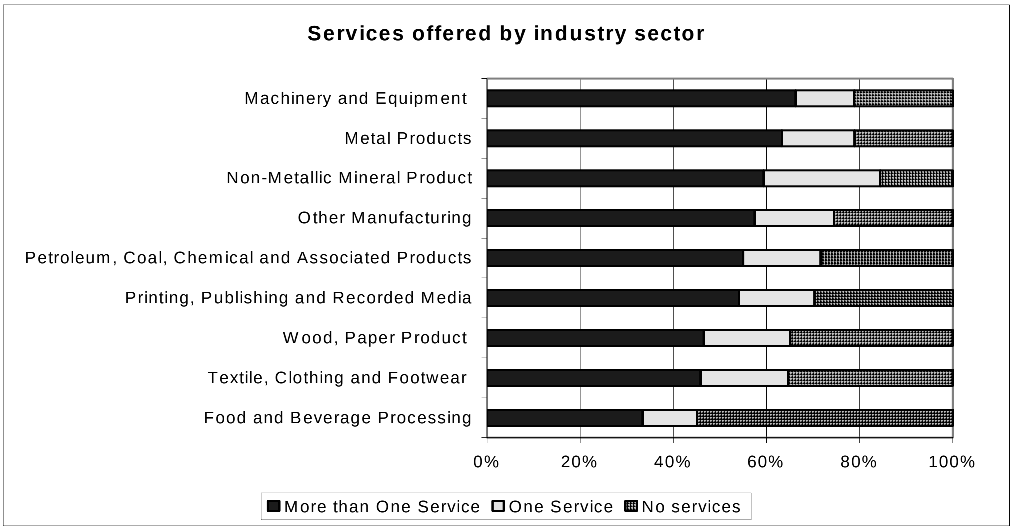
Marceau finds that Australian firms are increasingly blurring the traditional boundaries between manufacturing and services, blending and bundling products and services together in innovative ways to meet customer needs in tough and crowded markets.

This blurring of manufacturing and services affects the way enterprises structure their organisations and their relationships external to the firm. Successful product-service linkages are likely to require:

- new and unusual mixes of managerial, technical and co-ordination skills;
- stronger organisational capabilities in integrating products and services, and in redefining customer service;
- movement away from traditional functional divisions based on production, sales, marketing, finance and the like;
- increased proficiency in building and maintaining strategies for collaboration and external partnering; and
- greater cross-sectoral collaboration with the potential for more knowledge-sharing and innovation in the enterprises participating in these alliances.

The *Selling Solutions* study identifies a new dynamism in Australian manufacturing across all industry sectors. At least 65% of the TCF&L sector is identified as offering at least one additional service to their traditional product range (see Chart 3).

Chart 3



Those add-on services being offered in the TCF&L sector involve the customisation of TCF&L products and packaging for key customers such as the pricing of apparel by the manufacturer prior to packing and delivery; and bar-coding packaging to enable greater stock-control by the end-customer.

Although a large percentage of the TCF&L sector comprises SMEs, the findings from the study suggest that the size of the firm does not greatly influence the nature and extent of service provision, adoption of a product-service linkage strategy nor its likelihood to incorporate new and innovative practices.

Nonetheless, the predominance of particular services, such as the customisation of products occurring in the TCF&L industry, suggests that patterns of product-service linkage do correspond to particular characteristics of that industry sector. For example, in the TCF&L sector, the additional services offered are fewer than in other industry sectors.

One possible explanation for the narrower range of services offered in TCF&L is the dominance of the TCF&L manufacturing supply chain by non-manufacturing firms like large retailers. The power imbalance between suppliers and client retailers in demanding specific products turns TCF&L manufacturers largely into sub-contractors. This in turn limits the ability of TCF&L businesses to capitalise on new competitive strategies represented by product-service linkages.

The Australian Business Foundation's research indicates that the future of sectors such as TCF&L is dependent on fostering growth through new ways of doing business, like product-service linkages, rather than simply focusing on competing through cost reductions and production efficiencies.

A positive outcome of increased levels of globalisation and the liberalisation of world trade has seen reduced emphasis on cost as the sole determinant of competitiveness. While cost is still important, other factors such as quality, product differentiation, branding and the level of services bundled into a product are now major drivers of competitiveness.

In an evolving business climate for TCF&L the new ways of competing by developing unique business offerings through innovative combinations of products and services can provide a way forward. In particular, the findings from the *Selling Solutions* study highlight the opportunities in a mature sector like TCF&L that emerge from understanding and mobilising niche capabilities and long-term robust partnerships with end customers and others in the supply chain. These observations are echoed in both the TCF&L Forum Strategic Plan and the TCF&L Action Agenda.

5. BOOSTING INNOVATION & EXPORT PERFORMANCE

5.1 Tariff protection

The main issue for Australia in relation to protection in the next decade is in maintaining the impetus for international reductions in all of our trading partners' (tariff and non-tariff) trade barriers. With the proposed incremental removal of international tariff barriers, the Australian Government needs to ensure that Australia's trading partners do not replace tariff barriers with equally restrictive but less tangible non-tariff barriers (NTBs) to trade.

Unilateral reductions in tariffs benefit the domestic economy. However, given the world trading environment as it is, it would be missing an important opportunity to leverage lower protection levels amongst our trading partners if unilateral reductions occurred at this time. Multilateral reductions in trade barriers should be pursued instead.

ABL's broad policy objective is to achieve integrated industry reform and to promote activities which are consistent with market mechanisms and which focus on the competitiveness and innovation of the business.

Industry seeks an environment in which businesses can help themselves, in which firms can increase their investments and growth, and become more competitive, efficient, and service and export-oriented. Markets will work efficiently through the provision of a stable macroeconomic environment, an appropriate microeconomic environment based on minimising impediments to the effective operation of market forces, and the provision of an efficient and high quality economic infrastructure system.

ABL maintains a commitment to a competitive industry policy as part of a longer-term strategic view of economic and industrial development for Australian businesses and the broader community. ABL believes the greatest improvements in economic performance and efficiency will come through both removing impediments to business growth and fostering attributes within businesses that are associated with high value adding. Government has a role in facilitating adjustment processes in response to technological and policy changes or extenuating and unforeseeable external factors, and correcting underlying market failures, particularly where benefits accrue to the wider community as well as individual enterprises.

As outlined above, the Government has provided a suite of programs that initiated the sector's transformation partly in response to the decision to reduce tariffs in the last decade. The TCF&L sector has responded in part to these tariff reductions by contracting and also by increasing its reliance on subcontracting chains and use of outworkers.

Over the last year or so the industry code and the response to outwork by various State governments has significantly altered the economics of contracted outwork. One effect of this will be to reduce the number of outworkers in the industry. This means that there will be a significant growth of unskilled (in the sense of transferable skills) female unemployment in some areas and amongst some ethnic groups who have slim prospects of alternative employment. Sudden removal of existing assistance will compound this problem by creating a second wave of unemployed women with poor alternative prospects within TCF&L intensive locations.

The NSW Department of Industrial Relations estimates that in NSW alone, 50 000 people are employed as outworkers in the clothing and apparel sectors. Output from the TCF&L sector creates several thousand additional jobs at the retailer and service provider level and several billion dollars of additional economic activity. The sector is also a major consumer of Australia's wool and cotton crops.

The TCF&L sector *is* a willing participant in the transformation to a globally competitive environment. Reference to the 'dynamic gains' that flow from trade liberalisation, particularly the way in which heightened competition can induce increases in productivity is a generalisation that has not applied to the TCF&L sector. It is true that there are encouraging examples of business more successfully adapting to cuts in protection, but the divergent nature of the TCF&L sector requires careful consideration of the needs of each constituent industry. Severe cuts in tariffs are unlikely to automatically lead to sharp lifts in productivity, more job opportunities, higher incomes and lower prices for consumers and business. Recent experience within the sector supports this viewpoint (DFAT: Review of Australia's General Tariff Arrangements: 2000).

Early indications from the economic modeling commissioned by the Productivity Commission are decisive in their conclusions that the removal of the Strategic Investment Program and/or the serious reduction in current tariff levels will deliver marginal benefit to the Australian economy. What is without contention is that the end of the current tariff pause after 2005, without ongoing adjustment from the Government will have a significant and harmful impact on the TCF&L sector and related industries.

RECOMMENDATION: ABL supports the objective of moving TCF&L tariffs towards the general tariff rate over time but only if accompanied by an appropriate structural adjustment program. The transition to this objective should take into account action by Australia's trading partners in reducing their TCF&L trade barriers.

5.2 New Generation Strategic Investment Program

The introduction of the SIP as a part of the Government's Post-2000 package aimed to address those issues that were negatively impacting on the ability of the TCF&L industry to evolve and meet the challenges of a new competitive trading environment. The elimination of those issues would then encourage and underpin the evolution of a new, more dynamic, competitive and efficient TCF&L sector. The Government has identified the following issues blocking the sector's evolution:

- Low levels of research and development undertaken by all industries within the TCF&L sector

- Poor management and technical skill levels
- Understanding the importance of supply chain management and virtual supply chains
- The role of market access in developing Australian export markets
- Subsidised foreign industries
- The dominance of retailers in the TCF&L sector
- The importance of the business environment at each stage of the supply chain.

Although the TCF&L transition to higher value-adding activities is gradual, their trading environment changes rapidly and the industry assistance measures implemented as part of the SIP package need to be updated. The Government needs to implement realistic transitional arrangements that take into account the progress already made by TCF&L businesses in meeting the challenges of a globalising sector post-2005.

There is an inaccurate perception that only large TCF&L companies will be able to successfully navigate through the current transformation of the sector. This view fails to take into account the inherent benefits and opportunities that smaller businesses bring to the marketplace, such as flexibility, proximity to customers, ability to cater to niche markets and job creation.

The OECD Small and Medium Enterprise Outlook (2000) concludes that SMEs are at the core of future economic growth in OECD countries. Productivity growth is fuelled by competitive processes in industry which, to a large extent, build on the birth and death, entry and exit of smaller firms. Over 95% of enterprises in the OECD area are SMEs, which account for 60%-70% of jobs in most countries.

SMEs are the source of most new jobs and make significant contributions to innovation and high-technology employment. In addition, they are of considerable importance for regional development and for social cohesion. Governments need new and improved approaches for maximising the small-firm contribution to economic and social well being.

With a large proportion of the TCF&L sector comprising SMEs, it is interesting to note that findings from the Australian Business Foundation’s research suggest that the size of the firm does not greatly influence its likelihood to incorporate new and innovative practices. Supporting this view is the OECD report that smaller firms typically engage in informal R&D efforts and are innovative without formally undertaking research.

Smaller firms have traditionally focused on domestic markets and many will continue to rely heavily on local assets and markets. At the same time, SMEs are becoming increasingly globalised in response to the changing dynamics of the international trading market. SMEs are now becoming more involved in international strategic alliances and joint ventures both among themselves and together with the larger multinationals.

More generally, networking allows SMEs to combine the advantages of small scale, e.g. as regards flexibility and closeness to customers, with the economies of scale and scope provided by firm groups. This underscores that governments must reform policies and framework conditions that have a bearing on firm creation, expansion and exit.

The scheme should focus on the attributes it wants to encourage in TCF&L firms – innovation, high propensity to grow, management improvement and global market orientation.

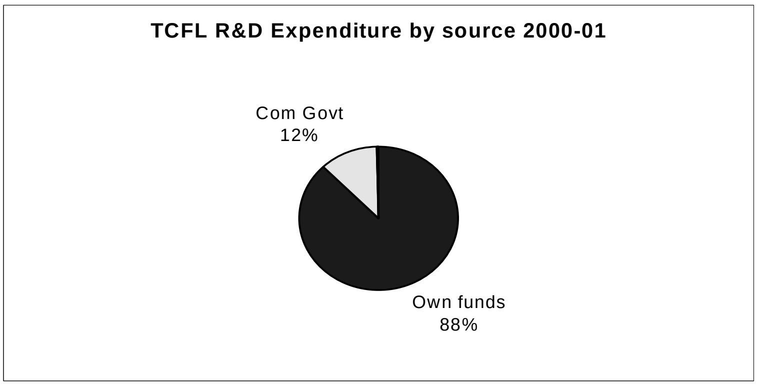
The history of Australian Government intervention means that the current state of the TCF&L sector is in large part the product of earlier Government policies. Further work is needed to ensure that firms are better prepared for the already legislated 2005 tariff reductions and any further reductions determined by Government.

RECOMMENDATION: The SIP package needs to reflect the changing needs of the TCF&L industries through the final stages of the sector's transition. Post-2005, the TCF&L sector seeks confirmation that the Government will maintain a structural adjustment scheme to guide the sector through an environment of reducing protection.

5.3 Qualifying for SIP

SIP participants have indicated that the program has been very successful in modernising the capital equipment used by TCF&L manufacturers, and guiding a cultural shift toward R&D and new business practices. Chart 2 illustrates the positive nature of R&D expenditure by the TCF&L sector in 2000-01.

Chart 4



Source: Department of Industry: March 2003

The reported weak SME take-up of the SIP grants for Types 1-3 funding does not accurately reflect evolving SME business practices. Consistent responses from ABL members explain by example why many smaller TCF&L businesses have not participated in the SIP initiative. The two greatest hurdles for SME participation in the scheme have been:

1. incurring eligible expenditure in relation to eligible activities, with the minimum expenditure threshold of $200 000, and

2. the time and resources involved in lodging the claim for eligible expenditure.

For small businesses the $200 000 threshold for eligible expenditure is an unrealistic goal. Acknowledging that the business can accumulate investment credits over the five years of the program, the total benefits under the SIP program in any one year are capped to 5% of their total eligible revenue in the 12 months preceding the claim. The amount of work and time involved for a small business to apply and qualify for the SIP grant money is unreasonable and disproportionate when businesses must pay for consultants and contractors to assist with the formal application. ABL recommends that the threshold for SMEs' eligible expenditure be reduced. Further, the current 5% grant cap should be increased so that the financial incentives available serve to encourage greater small business participation in the SIP scheme.

SIP participants raised concerns over the nature of innovation being supported under Type 2 grants and whether this reflected the type of innovation being undertaken within the TCF&L industry. Further, administrative interpretations were seen to be unreasonably narrow, with successful SIP applications being the outcome of subjective assessment.

RECOMMENDATION: ABL seeks a commitment from the Government to reduce the administrative and commercial burden of accessing the SIP. The current $200 000 threshold of eligible expenditure in relation to eligible activities needs to be reduced to $100 000 and the 5% of turnover grant cap should be removed.

5.4 SIP and export development

Consultation with ABL TCF&L members revealed that accessing appropriate export assistance had been difficult.

Already available for a company seeking financial assistance for export activities is the Export Market Development Grant (EMDG) administered by Austrade, which encourages small and medium sized Australian businesses to develop export markets.

Where the difficulty arises for the TCF&L sector is in meeting all of the eligible expenditure criteria to qualify for the EMDG program. In particular, the conditions that require the product to either be made in Australia or, if outside Australia, to be substantially made of Australian materials create the greatest challenges for Australia's TCF&L sector.

Given Australia's relatively high labour costs and the increasing propensity to relocate labour intensive production offshore while maintaining the high value-added components in Australia, the TCF&L sector is less able to legitimately access the EMDG program.

Eligible expenditure for export development as defined under the EMDG scheme should be 'carried over' into the SIP and suitably broadened to reflect the reality of TCF&L business operation in Australia. This means that a firm carrying out low value-added manufacturing offshore should be eligible and funding should allow for international marketing, research and development, branding and business development costs.

Combining broadened EMDG and SIP eligibility criteria into the one program would minimise application burden, especially for SMEs and ensure that the SIP program was more likely to lead to the necessary export activity as identified by the Action Agenda Board.

To prevent ‘double dipping’ TCF&L firms accessing export assistance from the SIP would not be eligible for EMDG funding.

RECOMMENDATION: ABL calls on the Federal Government to consider incorporating within the existing SIP program, a broadened selection of EMDG eligibility criteria that support TCF&L industries further developing export markets.

5.5 TCF&L Globalisation Outreach program

Discussions with TCF&L stakeholders reveal that ‘broadcast’ communications to the sector have not adequately registered with a sufficient number of businesses the urgency of transforming business practices to address their changing environment.

Many businesses, particularly SMEs, have not completely thought through their future strategy with complete knowledge of likely market developments.

For example, few businesses have considered the impact of the global elimination of quotas in 2005 as set out in the WTO Agreement on Textiles and Clothing. What will low-wage exporters like China and Pakistan do? What will this mean for global supply chains and especially the Australian and US markets? How might this impact on my business?

ABL proposes the creation of a strategy assessment program that reaches as many individual TCF&L firms as possible. More than a diagnostic tool, the Globalisation Outreach program could be structured in two parts. The first component would be a group or class setting to offer specific and accurate information to TCF&L businesses about their environment and the sector’s transformation. The second component of the program would use an Outreach Adviser to work with businesses in identifying realistic scenarios that fit their individual circumstances.

The Outreach Adviser would need to work one-on-one with firms, to take them through the likely changes in the market place and forecasts for their business. At the conclusion of the program, each participating business will be sufficiently well informed of their circumstances to consult their business professionals (accountants and lawyers) in identifying a strategy that will steer the business into the future. In detail, the program would need to address:

- the imperative to be part of growing global supply chains;

- the identification of trends and opportunities in the business environment;
- an awareness of existing capabilities, skills and intellectual property assets;
- innovative management and the construction of alliances with customers and suppliers;
- bundling a total product portfolio, and
- to ask the question ‘where does this individual business fit in?’.

The objective would be to explain changed dynamics and provide the business with a realistic assessment of competitive characteristics of firms and sectors, for example the implications for the firm if China gets access to the US market, and to examine the firm’s existing business model.

The result should be some indication of whether or not the firm is in a commercially sustainable sector. If not, the Outreach Adviser would assist the business in either repositioning the firm’s strengths in a new more viable way or developing a practical exit strategy.

The Outreach Adviser, who would need to be a TCF&L expert with industry credibility, should be able to navigate the firm to an appropriate program within SIP or elsewhere to develop a complete business strategy. The Outreach Adviser may need from a few hours up to 2 days with each company depending upon the complexity of its business.

The need for this scheme exists now to better prepare firms for the 2005 tariff reductions. Whether it is needed post-2005 would depend on how close the scheme had got to contacting every TCF&L business in Australia and ‘holding up the mirror’ to all those who want it.

RECOMMENDATION: ABL recommends the immediate creation of a TCF&L Globalisation Outreach program, working within the existing SIP funding to educate and guide the planning process of every willing TCF&L firm in Australia.

5.6 Tariff Concession Scheme

Prior to 1996, tariffs were not imposed on inputs if there was not a domestic supplier for the same product. This policy reduced the cost of Australian production, making Australian output more competitive not only overseas but also in our own domestic market.

Amendments made to the Tariff Concession Scheme in 1996 were explained as a way of business sharing in the burden of the deficit reduction process. Introduced as a revenue measure in 1996 when the budget was deeply in the red, this imposition on Australian trade can no longer be justified. The changes resulted in a 3% tariff on many business inputs as a means to raise revenue. The Government needs to reverse this highly distortionary and anti-competitive measure.

As a result of this tax on business inputs, Australia's TCF&L sector has effectively been asked to compete internationally and domestically against imports, with unnecessary and artificially high input costs. This impost has adversely impacted on the investment and employment opportunities in the TCF&L sector. This is not conducive to creating a healthy, innovative and forward looking sector.

In its Review of Australia's General Tariff Arrangements, the Productivity Commission concluded that the 3% tariff:

> "imposes a competitive disadvantage on Australian manufacturers who use those inputs, as well as raising costs by their customers. Reduction of the concessional rate to Free…is estimated to bring net efficiency benefits to the economy…"

The Productivity Commission has calculated that there would be net benefits to the economy from the removal of the 3% cost impost. Such an initiative would be widely welcomed by industry and would make a significant impact to the competitiveness of a wide range of Australian industries, especially the manufacturers within the TCF&L sector.

RECOMMENDATION: ABL is seeking a commitment from the Government to remove the 3% tariff on business inputs that was instituted under changes to the Tariff Concession Scheme (TCS) in 1996.

6. CONCLUSION

The Howard Government made a commitment in 1996 to develop partnerships with the TCF&L sector to ensure that they can meet the challenges associated with a changing and volatile environment. Aggressive competition, volatile markets, environmental concerns and demanding consumers are just some of the issues facing Australia's TCF&L sector. Australia's TCF&L sector, now more than ever before, needs the Government to honour its commitment of assisting the sector through this period of transition to ensure their future commercial viability.

The announcement by the Government in 1997 of a five year $700 million SIP package to encourage dynamic investment in Australia's TCF&L sector was a powerful project. Together the TCF&L Action Agenda and the SIP package provided the foundations for systematic long term strategic planning for the sector beyond 2005. These commitments established solid infrastructure for *guiding* the sector to the next stage of its development. However a decision now to drastically reduce tariffs without maintaining a new generation of the SIP will not deliver the outcomes desired by the Government.

From ongoing consultation with TCF&L members, and research led by the Australian Business Foundation, the findings indicate that the benefits provided by the TCF&L Action Agenda to consider and clarify opportunities, impediments and strategies for the sector require more time to be realised. Business is seeking a further and final commitment from the Federal Government to guide the last stages of the sector's transformation beyond 2005. The Government's assistance packages to date have established a strong framework within which many of the TCF&L businesses have been able to commit to structural adjustment. With these practices well entrenched in the sector, a decision by the Government to significantly cut tariffs without the support of a refined SIP package post-2005 would be seen by business as abandonment before the process has been completed.

The transformation of the TCF&L sector is a gradual process already underway. It is critical for the successful completion of the process that the Government maintains its guidance of the sector using a combination of tariffs and assistance measures.

A key finding from the research is that fundamentally different competitive strategies, based on innovation and knowledge are vital in the face of an increasingly volatile and globalised business environment. Businesses are therefore required to be more productive, nimble, globally connected and capable of continually creating new products and services that are valued highly by customers because they are customer led innovations.

Understanding and mobilising niche capabilities and long-term robust partnerships with end customers and others in the supply chain present a way forward for the sector, allowing TCF&L to compete effectively as well as anticipate and fulfil the needs of its customers.

Ultimately, an effective and productive regulatory environment involves an outcome-oriented approach integrated with other policy areas to avoid unnecessary hindrances to competitive business practices.

Australia's domestic market is small by world standards, and absorbing increasingly high levels of imported TCF&L goods. Australian TCF&L businesses need to reduce their reliance on the domestic market through increasing the current levels of exports, creating strategic alliances and linking with international supply chains. Special attention must be paid to developing global alliances. The ability to forge relationships with international supply chains is a key strategy for developing growth and a strong foot-hold in export markets.

7. REFERENCES

Commonwealth of Australia: Textile, Clothing and Footwear Strategic Investment Program Scheme 1999: December 2002.

Department of Industry, Sciences and Resources, Textiles, Clothing Footwear and Leather Industries: Action Agendas: A Discussion Paper: March 1999.

Prime Minister's Press Release: Tariff-Free Access For The World's Poorest Countries: 25 October 2002.

Professor J. Marceau *et al*. of the Australian Expert Group in Industry Studies: Selling Solutions: Emerging Patterns of Product-Service Linkage in the Australian Economy: February 2002.

TCF&L Forum: TCFL Forum Strategic Plan: Australian Textile, Clothing, Footwear, Leather Industry>>2012: Global and Growing Blueprint for a Positive Future: June 2002.

TCF&L Forum: Market Access Industry Participation Program Report: July 2002.

Victorian Government: TCF&L Industry Plan: June 2002.

World Trade Organisation: Non tariff Barriers, technicalities, red tape etc.: http://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm8_e.htm: March 2003