YAKKA PTY LTD

AUSTRALIA'S TCF INDUSTRIES POST 2005 ASSISTANCE

PRESENTATION TO PUBLIC HEARINGS

June 2003

1. INTRODUCTION

The Yakka Group welcomes the opportunity to address the Productivity Commission at the Public Hearings into the Inquiry into Australia's TCF industries.

Representing Yakka at the hearings, are:

- Mr Andrew Edgar, Managing Director Yakka Pty Ltd
- Mr John Bergin, Associate Director - Operations

2. BACKGROUND

YAKKA is a wholly Australian owned, globally oriented, clothing manufacturing group. It is one of the largest clothing manufacturers in Australia – producing, sourcing and marketing a wide range of industrial and corporate apparel and footwear.

YAKKA has been in operation for over 70 years. The company has a proud record in adapting to the prevailing market and policy environment confronting it at any given point in time, and this will continue into the future. The only difference in the company's operations over time will be the extent of manufacturing maintained in this country.

The main manufacturing company in the Group is **YAKKA Pty Ltd**. which services a number of associated companies which are engaged in marketing and distribution. Other major companies within the Group, targeted at different segments of the market are:

- **Neat n' Trim Uniforms Pty Ltd (NNT)**, a market leader in the area of ready to wear corporate apparel and dedicated wardrobes for major accounts.
- **Dowd Corporation Pty Ltd.** a market leader specializing in total clothing solutions for major corporates (eg NAB, Westpac, Australia Post and most recently Qantas)
- **CTE Pty Ltd**, which manufactures and markets a wide range of specialised industrial and defence apparel
- **Icon Clothing Pty Ltd,** established to consolidate the jeanswear and fashion trouser business – now minority owned by Yakka with other members of the Laidlaw family owning the balance.

The YAKKA Group manufacturing, distribution and administration facilities are located in a number of plants in Victoria (regional and metropolitan) and in Queensland.

YAKKA is now a global sourcing company, but it will always maintain a certain extent of manufacturing capability locally, despite the higher costs associated with it, as it is a necessary component of ensuring quick response capability to service customers needs and meeting the diverse product range required in the business.

YAKKA's main strength is its very strong brand image and established market position. An efficient manufacturing operation, exceptional warehousing and distribution facilities and a skilled and stable workforce supports this. YAKKA's core business focus is ' clothing and footwear for work'.

3. YAKKA'S PRELIMINARY POSITION FOR THE TCF INQUIRY

YAKKA highlighted in its initial submission to this Review, that it plans to continue to be a strong and recognised brand in the Australian market. But, it was also flagged that the extent of manufacturing activity, employment and local value added generated by the YAKKA Group's business may well decline, depending on the Government's final decision arising from this review.

To ensure the optimum level of business activity in Australia, in the most efficient manner possible, YAKKA recommended the implementation of the following policy measures:

- Retention of clothing tariffs at the 2005 levels (of 17½ %) until at least 2010, and no further reductions after that point without a clear and irrefutable indication that the rest of the world is taking similar action
- Retention of the SIP Scheme for a further 10 years, but with modifications to ensure that it does drive change and facilitate desirable industry restructuring, across the full range of business activities inherent in the industry today (and necessary for the future)

4. REACTION TO THE COMMISSION'S TCF POSITION PAPER

Yakka fully agrees with the Productivity Commission's recommendation for a TCF package of assistance, balancing tariff reform with supportive budgetary assistance designed to help the industry adjust to, and develop in, a more open trading environment.
However, Yakka believes that the package of assistance should be applied for a 10 year period to allow the necessary time for the readjustment to occur, and enable greater certainty for investment decisions to be made. The level of assistance provided should also extend further than the Commission has recommended.

4.1. Tariffs

Yakka is fully supportive of the industry position on tariffs, as reflected in the TFIA's submissions. That is, that the clothing tariff of 17½ % be maintained beyond 2010 unless it is can be demonstrated that our major trading partners are reducing their tariffs below this point.

However, if tariff reform is being reciprocated globally then further reductions should be applied in Australia. However, the 43% cut recommended by the Commission is too severe in one hit, as is the 50% cut suggested for 2015. Yakka believes that the clothing tariff cut in 2010 should be to 14 % and then to 10 % in 2015.

It is important that the tariff reform is implemented with care, to ensure that potentially viable business in Australia is not lost in the process.

For instance, in Yakka's case it must be recognised that the company produces a basket of core industrial products – ie shorts, coveralls, bib and brace, etc – at two principal production facilities (Wodonga and Brunswick). These are products that can be sourced more cost effectively offshore, but at current tariff and exchange rates, the benefits derived from local production (ie quick response, inventory costs, customer service) offset the price premium to be derived.

Yakka would like to believe that this will still be the case at a duty of 17½ % on clothing, and indeed the restructuring the company has undertaken, and plans to undertake through to 2005, has been with an eye to ensuring that this is the case.

However, at a duty of 10% for clothing, the price disability of Yakka's Australian produced garments will be double that under a 17½ % tariff, unless Yakka can introduce some major change to its domestic production. *(Yakka is happy to share hard data on this issue with the Commission, on a Confidential basis)*.
In order to adjust to this extent of tariff reduction, Yakka will need - at the very least – to undertake further restructuring and consolidation, as the duty arrangements will signal a threshold at which it will be very difficult to sustain the premium associated with retaining production in Australia.

With the stability of a constant tariff of 17½ %, Yakka will continue manufacturing in Australia. However, in anticipation of further tariff reductions, the company will embark on the systematic rationalisation of domestic manufacturing.

At the time of the last Industry Review, Yakka advised that its local to import product mix would shift from 70/30 to 30/70. The company is now well down that path and this will be the situation by 2005. But with further reductions in assistance, further restructuring is not only inevitable - it is essential.

If the tariff reductions are stepped down over a manageable timeframe, and each reduction is not unduly severe, Yakka will be able to take a reasonable and structured approach to rationalisation. In all likelihood however, the optimal position will be to shift to a one factory operation, capable of significant production output, but of a highly diversified product range.

This would mean further reductions in manufacturing employment which will impact adversely on the opportunities for those category of workers previously identified as having the greatest difficulty in obtaining new employment – ie females, migrants, non English speaking workers.
Regional impacts are also significant and would cause knock on effects to other suppliers in the regional areas (including Macquarie Textiles in Albury and Bruck at Wangaratta). Large volumes of product are involved and impacts would be felt across a wide cross section of businesses.

If this restructuring is undertaken over a period of time, in a well managed manner, the Yakka Group envisages its employment would drop by 250 people, retaining employment of 1200 people. The company would continue to manufacture but with further value added in processing, marketing, design, product development, distribution and customer service.

However, if the tariff adjustments occur at a faster rate, the necessary restructuring will also need to be accelerated. However, doing this quickly will create substantial disruption to the Yakka business and will inevitably lead to a greater rationalisation than would otherwise need to be the case – simply because it takes time and money to manage the transition appropriately.

It is what happens to the tariff that will determine the speed and extent to which Yakka reacts. It must be recognised that when tariffs change there is a very direct relationship in the market with the wholesale price. A price change gets forced immediately in response to tariff change, whereas it is possible for example, to negotiate around foreign exchange rate movements (as these regularly move up and down). Customers are immediately aware of impending tariff movements and already factor in price reductions on this basis.

For this reason, Yakka favours a stepped down approach to tariff reductions rather than an annual phase down approach. Yakka's major competition now is clearly import based, and annual tariff reductions would impose regular price pressure each year. A 5-year period of stability and then a stepped down approach is much more manageable for the industry.

4.2.Budgetary Assistance

Yakka supports the Commission's contention that budgetary assistance is warranted to ease the adjustment pressure on the TCF industries during the period of transition as tariffs are reduced. However, this pressure and the need for the industries to restructure in response to that pressure will be significant, and it will apply throughout the decade to 2015.

To provide the necessary support over this period, the Budgetary assistance should be accorded for the full 10 years (not just 8 years as suggested by the Commission) and it should be applied at the current annual rate (of TCF funding assistance) for the full 10 years.

4.2.1. Nature of Budgetary Support

In determining the nature of the support mechanism used, Government must review the effectiveness of the SIP program. While Yakka believes that of the 3 options suggested by the Commission, the continuation of a SIP type scheme is the most appropriate, it will need to be modified.

Yakka is a major player in the Australian TCF sector and the company has invested heavily to reposition itself for the future. Yet the pro-rata share that companies like Yakka have received under the SIP scheme is very low. While the SIP funding received by the Yakka Group of companies has been put to good use (eg latest cutting equipment in Yakka, reconfiguration and streamlining of manufacturing and distribution processes at NNT, new strategic defence apparel at CTE), there is considerable investment that Yakka has undertaken to improve its supply chain management, interaction with its customer base and strengthening of the brand profile that simply has not qualified for budgetary assistance.

Any replacement program for SIP post 2005 should include funding support for further rationalisation and consolidation within companies. Restructuring by individual companies will be essential to ensure they can strengthen their underlying base, and this activity should be encouraged under the SIP replacement program. The program should also recognise the changing face of the industry, and support the overall business activity of firms engaged in TCF manufacturing in Australia.

The industry's focus now is to service the customer to the fullest extent possible. To do this effectively, the industry needs to continually update its information technologies to ensure regular and timely communication with its customers and our suppliers, and needs to ensure it retains speedy and reliable distribution channels. In short, the Australian clothing industry needs to effectively manage its supply chain to ensure the necessary value add to its domestic manufacturing processes, to underscore continued demand for these activities. SIP must more effectively encourage such investment in future.

For Yakka's part, it will manage the overall supply chain, providing the customer with the ultimate apparel solution. The company will be a significant sourcer, warehouser, distributor and manufacturer of corporate apparel and work wear. But if it did not engage in the design, sourcing and distribution activities, it would no longer be able to justify and support any of its manufacturing activity in Australia.

The innovation aspect of the Scheme also needs to be modified to reflect the true nature of research and development in the clothing industry. There is no question that Product Development remains an important aspect of both industrial and corporate markets. (and the YAKKA Group has effectively utilised the SIP where development relates to sophisticated protective clothing and Defence markets). But R&D as defined in the Government Programs does not truly account for the fashion and commercial risk involved in most garment development. The focus is on technical risk, which is not really the issue for the bulk of consumer clothing development.

Similarly, SIP does not give sufficient encouragement to expand existing or develop new markets. The market access/market development component of the scheme has not been effective due to the administrative interpretations applied. This is unfortunate as there are now new market opportunities (beyond those explored in the past) but there is no access to any support to explore these.

5. Other issues

Yakka notes that imports from the Lesser Developed Countries (LDC's) are to be granted duty free access to the Australian market from 1 July 2003.

Yakka has no objection to this and recognises that basic clothing manufacture provides a real opportunity for industrial development in such countries. However, the company is concerned about the intended rules of origin for products imported from LDC's, which purportedly will be:

- 50% local content and last process of manufacturing (as per ANZCERTA & SPARTECA)
- But, the local content can comprise up to 25% other LDC <u>or even DC</u> content

Thus, theoretically a garment imported from say Cambodia could have 25% Chinese content. Apart from the obvious implications this has for transhipment and consequent erosion of the impact of Australia's global tariffs, this eliminates any incentive for Australian textiles to be incorporated in LDC garment manufacture.

This development is seriously counterproductive to any ongoing and managed approach for the repositioning of the Australian industry, and the Rules of Origin for LDC's must be modified immediately to exclude any prospect of allowing DC produced TCF goods to circumvent Australia's existing tariff structure.

6. Conclusion

Yakka is prepared to do whatever is necessary to secure the future position of its business. The action taken by the company will inevitably reflect the nature of government policy decisions. The bleaker the policy environment, the more radical the company's restructuring decisions will need to be.

To ensure the appropriate and ongoing re-positioning of Australia's TCF industries in the global environment, Yakka recommends the following assistance package be applied after 2005:

- Clothing tariffs held constant at 17½ % until 2010
- No further tariff reductions beyond 2010 unless they are reciprocated globally
- If tariff reform is being reciprocated, implement stepped down clothing tariff reductions to 14% in 2010 and 10% in 2015
- Extend SIP type budgetary assistance for the10 years to 2015, at current annual funding levels for the full period
- But introduce necessary modifications to the SIP type arrangements to provide sufficient incentive to encourage:
    - Further industry restructuring
    - Enhanced supply chain management and customer responsiveness
    - Commercially relevant product development
    - New market development

And immediate action needs to be taken to ensure that the new arrangements for LDC's do not allow for any circumvention of Australia's overall trade arrangements.

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