Footwear Manufacturers Association of Australia Inc

Review of Post 2005 TCF&L Assistance

Presentation to the Productivity Commission
Hearings in Sydney June 2003

Summary Overview

Background to the Footwear Manufacturers Association of Australia Inc (FMAA)

The FMAA is a national industry association which represents the collective interests of the local Australian footwear industry. Members include manufacturers of footwear, manufacturers of components (i.e. lasts, insoles, heels etc) and manufacturers of associated products such as leather care products.

The Australian industry accounts for:

- $515 million of annual manufacturing turnover
- this equates to in excess of $1.2 billion sales at retail
- approximately 3500 direct employees.
- the manufacturing industry is predominantly import replacement
- there are footwear operations in metropolitan areas and many regions, for example Ballarat, Geelong, Goulburn, Hobart, Perth and Adelaide.

The association's members account for 75% of the industry's output manufactured in Australia.

The industry's current position and future is reflective of the past.

- the history of the footwear is industry in Australia is one of continual evolution.
- it began in the first colonies as single cobblers
- by the 1920's large companies had been established with many hundreds of employees.
- during the Depression these large factories closed.
- small firms bought machinery at the auctions caused by the large firms closing - minimal import pressure.
- since the late 1990's, large firms are once again closing - due to decreasing tariffs.
- now need to keep nucleus of industry alive so that it may be re-born in a new form for the 21st century.

The industry has responded positively to needs of the community and has undertaken fundamental structural change. Since 1988 tariffs have reduced from 50% plus $10.50 per pair (estimated nominal rate of 63% compared to the manufacturing average of 10%).

The industry consolidation continues and we have achieved significant productivity gains over the 1990's. For example:

- value added per employee has increased by 93%.

- the import share of the Australian market has almost tripled to 70% of the market.
- the share of total output exported has increased to 15%.

The increase in efficiency and competitiveness has resulted from increasing specialization in specific sectors such as work wear, mid-range women's fashion & specialty footwear.

Challenges

The key drivers for a sustainable industry in the future are:

- continual rebalancing of sourcing between local manufacture and imported product.
- development of new and expansion of existing export markets.
- effective research and development including new product and process designs.
- uptake of the latest technology to ensure continuation of the current productivity and efficiency improvements.
- ongoing search for best practice protocols that assist in survival

The challenges for the industry are ongoing:

- the Australian market is comparatively small and local manufacturers produce only 12% of the footwear purchased in Australia.
- footwear imports are continually taking a larger share of the home market.
- as part of the continual adjustment process local manufacturers control 28% of the footwear imported into Australia.
- intermittent dumping occurs.

In order to develop a competitive industry the development of market control and intellectual influence is crucial:

- China's emergence as a major footwear manufacturer has been gaining strength for the last decade and is now the biggest supplier to Australia.
- 40% of the Australian market is controlled by manufacturers/importers.
- however, the same people that control the 40% carry out 90% of all design in Australia.

Comments on PC Position Paper

The Productivity Commission concluded that indefinitely “continuing special assistance” was not warranted (pxxi).

- The FMAA does not support indefinite assistance and notes that the cost of the current arrangements are lower than previous programs, that the quantitative assessments are finely balanced and there is little “allocative efficiency” gain to be had from removing special support.

- On the other hand the FMAA is certain that there would be significant losses if that support were removed.

The Productivity Commission also concluded that fairness was not an adequate basis for determining policy (pxxii)

The FMAA seeks appropriate, not fair, support to:
- achieve desirable potential outcomes
- offset costs associated with the effects of previous policies

These costs are the result of the previous Australian policy environments that led to:
- State based decentralization programs causing structural inefficiencies and fragmenting capacity
- import replacement and self sufficiency manufacturing strategies
- employment intensive operations

This Australian environment resulted in:
- lack of transferable skills for employees
- shallow labour markets
- mass manufacturing techniques
- resistance by employees, suppliers and customers to the consequences of change

The footwear industry has recognized the change in government policy but it is still restructuring and reinvesting and all the costs and benefits have not yet been realized.

The Productivity Commission also concluded that any bargaining coin attaching to Australia’s TCF tariffs is likely to be very limited (pxxii)

- The FMAA strongly opposes unilateral tariff reductions. It is notable that footwear tariffs are often at the forefront of issues to be discussed in the various trade negotiations that have been and are being undertaken in recent years. The fact that there is such interest in them demonstrates in a direct and demonstrable fashion that this arrangement is highly valuable as negotiating coin – i.e. its what the other side of the negotiating table (or more accurately, what our competitors whom the other side of the negotiating table are representing) wants.

- The FMAA considers it naïve to voluntarily incur significant costs on the basis that our competitors will do us a favour in the future

The Productivity Commission also concluded that the magnitude of the adjustment task that still lies ahead provides a reason for erring on the side of caution (pxxvi)

- The FMAA agrees with this conclusion and given the conditions outlined above would suggest the following program developments.

FMAA Recommends to the Productivity Commission

Australia should have industry policies and programs that are:
- consistent
- stable
- encourage positive adjustment

These policies can't be developed or implemented in isolation from the fact that our trading partners and competitors have programs and policies designed to produce the most beneficial outcomes for their industry, given their local circumstances.

With reference to the criteria mentioned by the Productivity Commission (p.xxix) we believe the order of importance is:

- promote certainty and transparency.
- provide sufficient support to make a difference.
- give flexibility to the firm to judge what best promotes their future competitiveness.
- provide support to firms that exhibit ongoing solvency.

Tariffs

- implement reduction in 2005 to 10%.
- hold at the 10% level for the future.
- any future reductions to be conditional upon reciprocal trade liberalization occurring globally - an industry review to establish if more than 85% of world trade in footwear is subject to a tariff 10%, as will be the case in Australia.
- any future phasing should be tops down to simplify and align finished apparel rates and thus remove tariff induced substitution exacerbating import pressures – it has been noted that apparel importers are increasingly importing complementary footwear.

Positive assistance

In order to achieve an orderly change within the industry positive assistance should remain for the next 10 years at current annual funding levels.

Strategic Investment Program

The FMAA believes the Productivity Commission is correct in its belief that further budgetary assistance is warranted to assist with the adjustment process. The Productivity Commission suggested three alternatives to budgetary assistance:

- SIP with modifications
- a bounty based on incremental value added
- a competitive entry scheme.

The FMAA believes the only option worthy of real consideration is the current Strategic Investment Program (SIP) but with some minor modifications. This is our preference as it is now well understood and the least disruptive approach. The value added approach is more suited to an industry that is expanding and also creates definitional problems and generates uncertainty. The competitive entry scheme could be workable but means picking winners. Historically this approach has always reduced the number of recipients, had a very mixed record of success and meant that application costs, time and the use of consultants increases dramatically – as evidenced by the TCFDA experience.

Our recommended changes for SIP are:

Type 1

This should continue as is but with inclusion of second hand equipment to facilitate restructuring between firms regardless of whether they are located in metropolitan or regional areas.

Type 2

To continue as is but with the addition of expenditures, appropriately apportioned, for:

- marketing and branding.
- quality of production.
- supply chain management.
- IT systems.
- payroll tax.

Type 3

Increase the maximum claim for value added from 5% to 10% of total value added.

This is more in line with the current value added characteristics of capital-intensive restructured firms. Our investigations have found that many manufacturing firms now have a value added to sales percentage of between 25 and 30%. Altering the maximum claim to 10% value added for SIP would recognize a 25% value added to sales ratio.

Type 4 and 5

The arrangements should be modified to ensure they provide a real incentive for further industry rationalization and consolidation – the current arrangement intertwines regional objectives with restructuring thus ensuring that neither objective is effectively achieved.

It is our view that restructuring assistance should apply to both regional and metropolitan areas. Perhaps the most efficient way to really achieve this goal would be to eliminate type 4 & 5 from the scheme but include second hand equipment in type 1 claims - that is allow the purchase of second hand equipment provided the purchase is not from related parties.

Other suggested alterations to SIP:

- reduce annual additional and entry level expenditure to $50,000
- impose a maximum claim entitlement equal to 5% of $300 million turnover for a group or individual firm.
- although Ausindustry's definition of innovation for SIP is working - minor clarifications would be helpful but this request appears to be less critical as experience grows - design and development work is necessarily associated with new products
- provide for quarterly payments as per automotive arrangements
- all entitlements in excess of the 5% sales cap should be carried forward to subsequent years.
- the modulation provision should be abolished
- introduce a regional uplift factor for any successful claims

Additional suggested alterations

Footwear upper components

- immediate reduction of the tariff rate on footwear upper components to zero

Tax concession for corporate apparel

- addition of footwear to the non-compulsory apparel registration scheme

Ministerial allocation

- a special ministerial allocation fund of $20 million per annum for discretionary projects, e.g. for firms that are too small to gain access to SIP or who have projects that are not otherwise eligible for support.

Restructuring & Retraining

While TCF workers have access to generally available labour programs we believe that due to the circumstances of industry restructuring that a discrete program of labour adjustment assistance could accelerate restructuring and facilitate employee adjustment.

Firms with a turnover of less than $5 million of local eligible sales who as a result of increasing import competition and restructuring are looking to reduce their level of local manufacturing could be relieved of redundancy payments thereby bringing about faster industry consolidation – the payments would come from the adjustment program

Affected employees income would be maintained for a period of say three months while they undergo retraining or alternate employment is found.

The benefit to the firm would be avoiding a cost that they otherwise would have to meet and which can inhibit the decision to restructure - the cost to the firm would be forgoing access to SIP or other government assistance. Individuals could avail themselves of this facility only once to ensure that there was no double dipping in the event of finding further employment within the TCF sector.

For firms with greater than $5 million turnover who are looking to reduce their local activities the firm would still be required to pay all appropriate redundancy entitlements. Affected employees would receive top-up payments from the fund to ensure they maintain their income levels for the three months retraining period.

The benefit to the firm would be a longer period in which to gradually wind down their operations - the cost to the firm would be forgoing access to SIP or other government assistance

Dumping

- Adjust anti dumping rules to be the same as U.S.A. rules including the Bird amendment.

Retrospectivity

- The review taking place is for assistance after 2005.
- With the exception of adjusting the duty rate on footwear upper components all adjustments should be held for beyond 2005.
- Any early changes to the positive assistance package would disrupt the current arrangements and create more confusion in the industry.

Conclusion

We applaud the Productivity Commission for recognizing that the reduction of tariffs will cause further adjustment pressures and that therefore continued positive assistance is warranted.

The FMAA recommends a further 10-year program with the key points being:

Footwear tariff held at 10% until 2015

- a full review before any changes take place.
- no further unilateral tariff cuts.

Continuation of SIP until 2015

- funding levels to be the same as is current.
- minor modifications to the current scheme as listed previously.

Federal government to actively support improved market access.

Zero duty rate on footwear upper components.

Change the anti dumping laws to those that exist in the USA.

Implement a targeted restructuring/labour adjustment program aimed at employees of small firms.

Thank you for the opportunity to participate in this review.