

REVIEW OF TCF ASSISTANCE: PC POSITION PAPER

*ACCI SUBMISSION
TO THE
PRODUCTIVITY COMMISSION*

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Background

The Australian Chamber of Commerce and Industry (ACCI) is the peak council of Australian business associations. ACCI's members are employer organisations in all States and Territories and all major sectors of Australian industry.

Through our membership, ACCI represents over 350,000 businesses nation-wide, including the top 100 companies, over 55,000 enterprises employing between 20-100 people, and over 280,000 enterprises employing less than 20 people. This makes ACCI the largest and most representative business organisation in Australia.

Membership of ACCI comprises State and Territory Chambers of Commerce and national employer and industry associations. Each ACCI member is a representative body for small employers or sole traders, as well as medium and large businesses.

Inquiry Focus

The Productivity Commission has been asked by the Government to:

- evaluate the effectiveness and appropriateness of current assistance programs in meeting the Government's goal of achieving structural change and a more internationally competitive TCF sector by 2005;
- identify and analyse major impediments to the long-term viability of the TCF sector;
- identify major opportunities for the sector and its strengths and weaknesses for securing these opportunities;
- identify and analyse post 2005 policy options including tariff options, consistent with the Government's obligations, which would encourage the sector to adjust to a more viable and sustainable competitive position, with particular attention to the impact of those policy options on regions where TCF accounts for a high level of regional industry concentration;
- examine relevant workplace issues; and
- report on the likely impact on the TCF industries of international trade developments.

The Productivity Commission has released a position paper and sought comments.

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Key Points from the PC Position Paper

The key points from the Productivity Commission's position paper are as follows:

Major structural change has occurred in the Australian textile, clothing, footwear and leather (TCF) industries, mainly in response to competitive pressures faced by producers in all developed countries. More adjustment and job losses are inevitable, almost regardless of future assistance arrangements.

Contrary to the perception that these are 'sunset' industries, there are some internationally competitive Australian TCF producers. Others have the capacity to become so. Emerging strengths, including increased flexibility, responsiveness and innovative capacity, will help firms in the latter group to make this step.

Much can also be done by the TCF industries to address impediments and weaknesses that reduce viability. Improving workplace outcomes through better cooperation and communication between firms, employees and unions is a priority.

However, given large labour cost disadvantages, many firms producing standardised clothing and footwear will not survive. This in turn poses threats to some of their suppliers.

Helping those disadvantaged by change is important. Characteristics of the TCF workforce that limit alternative job opportunities for many employees and outworkers, and the continuing importance of TCF activity to some regional economies, make this a challenging task.

The current assistance package has helped some firms to improve their competitiveness and long term viability, but it is costly for others in the community.

Further reductions in tariffs after 2005 would reduce the costs of protection for consumers, reinforce incentives for performance improvement in the sector, and signal Australia's continuing commitment to the APEC trade liberalisation process.

The Commission's preferred tariff option at this stage, would maintain all TCF tariffs at the new legislated 2005 levels until 2010, then reduce most of them to 5 per cent and maintaining that rate until at least 2015. However, tariffs on clothing and certain finished textiles, which are currently much higher than those on other TCF products, would not be reduced to 5 per cent until 2015.

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To facilitate adjustment to these tariff reductions, the Commission proposes that transitional (Strategic Investment Program-style) budgetary support be extended for a further eight years, but with funding levels reducing over time. It is seeking comment on the most appropriate form of this support, including on the possibility of providing some funds to assist displaced employees and outworkers.

Balance is required in initiatives that seek to protect outworkers from exploitation. Heavy handed regulatory approaches could simply drive more production offshore to the detriment of the outworkers concerned.

Continuing government efforts to improve access to overseas markets and to advance microeconomic reform would facilitate competitiveness in the sector.

All that said, there is little that can or indeed should be done to stop further adjustment out of labour intensive standardised TCF production in Australia. Rather, the policy focus should be on facilitating and supporting the adjustment process.

ACCI's response

As pointed out by the PC, major structural change has occurred and is continuing to occur in TCF industries around the developed world. This has been driven by competition from suppliers in developing countries, changes in consumer spending patterns and technological advances.

Obviously the Australian TCF sector has not been immune from these pressures. Substantial rationalisation of production has occurred; the product mix and supply chains are changing; and both imports and exports are growing. Sectoral output and employment continue to fall.

The focus of ACCI in this inquiry is twofold: tariff reduction and the options for structural assistance after 2005.

ACCI supports the Government's expressed desire to encourage the sector to adjust into activities where it will be internationally competitive with lower levels of assistance. The PC notes that the Government has also signalled a broader commitment to improve the overall performance of the Australian economy which it says implies that any further support for TCF producers should not be detrimental to Australia's long term economic interests.

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ACCI also supports the approach of the PC in dividing the sector into three broad groups — *those that are already internationally competitive, those capable of becoming so, and those unlikely to survive even at current levels of government support*. However we do not believe that those that fall into the latter group be discarded, but rather wherever possible be assisted to structurally adjust into other segments of the market.

In making recommendations about the future arrangements for the sector, it is important to understand its importance to the manufacturing industry and the economy broadly. The TCF manufacturing sector in Australia covers all stages of production of textile, clothing, footwear and leather products. In 2000-01, Australia's 5000 TCF firms generated turnover of \$9 billion, and provided 'factory-based' employment for at least 58 000 people, with some data sources suggesting a figure of more than 70 000.

We note like the PC that:

- TCF production is more significant for some States and regions (accounting for 6 per cent of value added and 9 per cent of employment in Victoria's manufacturing sector.
- production is mainly based in Melbourne and Sydney, but TCF firms are important in regional centres such as Geelong, Bendigo, Wangaratta, Albury-Wodonga and Devonport.
- There are mainly small to medium sized privately-owned firms, particularly in the clothing industry

There are linkages between the TCF manufacturing sector and other parts of the economy by way of upstream links to producers of raw materials and downstream links to wholesalers and retailers of TCF products and industries such as furniture manufacturing, hospitality and health services that are major users of TCF products — many of which are members of ACCI's member organisations.

TCF products imported into Australia are subject to the following tariff rates:

- 25% for clothing and finished textiles
- 15% for cotton sheeting, fabric, carpet and footwear
- 10% for sleeping bags, table linen and footwear parts

Legislation has been passed to reduce these tariffs from January 2005. Items at 25% will fall to 17.5%, those at 15% to 10% and those at 10% to 7.5%. However, even after the 2005 tariff reductions, the TCF sector will continue to receive a level of tariff

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assistance above that afforded general manufacturing activity. The sector also benefits from a range of other assistance measures implemented as part of the Government's post 2000 assistance package, including the Textile, Clothing and Footwear Strategic Investment Program (SIP) and the Expanded Overseas Assembly Provisions Scheme.

Issues

Our comments are primarily directed to these two issues - tariff reduction and the operation of the Strategic Investment Program.

Tariffs

ACCI's policy in relation to general rates of tariffs is essentially that while there are benefits to the Australian economy from unilateral reductions in tariffs, there are greater benefits from multilateral tariff reductions. This policy also guided ACCI's comments in relation to the TCF industry.

Government policy announced in 1998, which was subsequently legislated, saw tariffs reduced until 1 January 2005. On balance, ACCI supported the Government's approach.

ACCI's approach to the previous Productivity Commission TCF review was developed after lengthy debate. On 12 March 1997, in the context of the draft Productivity Commission report on the review of automotive arrangements and the review of TCF arrangements, ACCI resolved:

The ACCI supports continuing removal of international trading barriers, but believes that any further reductions in Australian tariffs (outside those already announced) must be considered in the context of a whole of government industry policy.

The scheduling of any further cuts in the level of protection must be part of a wider package of comprehensive, domestic reform to taxation, workplace relations, waterfront, other regulatory compliance and microeconomic reform, implementation of national competition policy, and, in terms of external trade, improved market access.

The revenue implications of any measures that may be implemented need to be accounted for, and alternate revenue sources or expenditure cuts be identified.

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In assessing the possible outcomes of any further reductions in assistance to the textiles, clothing and footwear, and passenger motor vehicle industries, full account should be taken of the economic, strategic and social impacts.

Since the 1997/1998 TCF Review, there has also been a review of general tariffs. In the Government's response on 19 December 2000 to the Productivity Commission's Review of General Tariffs, the Government decided to retain the general tariff rate at 5 per cent. The Government stated that:

...it believed that the general tariff could be removed when there are clear and substantive benefits including trade benefits in doing so... we consider there would be benefit in holding these current arrangements for the present and moving to withdraw them at a time consistent with trade and fiscal objectives.

ACCI supported the removal of the general rate of tariff in the context of multilateral negotiations, or by 1 January 2005 at the latest.

Tariffs are no longer the major issue in Australian industry policy. With the tariff applied to all items other than TCF and PMV at 5 or less per cent, there remains little in the way of tariff barriers into Australian markets.

The lesser importance of tariffs as an issue in Australian industry policy should not impede the momentum for further tariff reductions. The benefits that have accrued over the past decade are evidence of the need for further reductions in tariffs.

While ACCI recognises that there are benefits to the Australian economy from unilateral reductions in tariffs and believes that Australia should continue to reduce tariff duties, such benefits would be vastly increased if there were simultaneous reductions in protection levels by our trading partners. It would therefore appear to us that unilateral tariff reductions should not be pursued, but that bilateral and multilateral tariff reductions be pursued instead.

A major issue for Australia in relation to tariffs in the next decade is not only ensuring that Australia's remaining tariff barriers are removed, but rather maintaining the impetus for international reductions in our trading partners (tariff and non-tariff) trade barriers.

Additionally, with the progressive removal of international tariff barriers the Australian Government must ensure that Australia's

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trading partners do not seek to replace tariff barriers with equally restrictive non-tariff barriers to trade. Non-tariff barriers do in effect present the same restriction to trade as tariffs and have the potential to reduce or remove potential benefits from multilateral tariff reductions.

Consistent with our earlier policy approach to both general tariff reduction and automotive tariff arrangements, ACCI:

- Supports the TCF tariff phasing to 17.5 per cent for clothing and finished textiles; 10 per cent for cotton sheeting, fabric, carpet and footwear, and 7.5 per cent for sleeping bags, table linen and footwear parts on 1 January 2005; and
- Argues that further reduction in the TCF tariffs should be in the context of multilateral negotiations, but that the tariff should over time be removed.

It is also relevant to again call for the removal of the 3 per cent impost imposed on TCF manufacturers via the Tariff Concession Scheme. ACCI has been calling for the removal of the 3 per cent tariff since it was first introduced in 1996.

During the 2001 election campaign the Government committed to “the removal of the 3 per cent duty under the Tariff Concession Scheme (TCS). However, this will not occur until there are clear benefits, including industry benefits, and when it is fiscally responsible to do so”.

ACCI welcomed the commitment by the Government to the removal of the 3 per cent duty on domestic manufacture and urged the Government to immediately review the costs of this policy on Australian industry.

The TCS is in essence a tax on imported inputs to domestic manufacturing, particularly where imported finished goods come into the country tariff-free. The TCS was introduced to exempt from tariffs those goods for which there is no locally produced substitute. This policy recognised the fact that no competitive advantage arises for domestic industry applying tariffs to goods it does not produce. The TCS as now operating disadvantages business using imported inputs by increasing cost and reducing competitiveness.

Amendments made to the TCS in 1996 were a one off decision and explained as a way of business sharing the burden of the deficit reduction process. Instead of abolishing the TCS for both business

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and consumer goods, the Government made amendments to make business inputs entering under Tariff Concession Order (TCO) subject to a three per cent tariff while consumer goods imported under a TCO would enter tariff free.

As the Budget has been in surplus, the removal of the TCS should have been and must remain a high priority for Government. Australian manufacturers do not need Government imposed incentives to relocate production overseas, or to compete with imported goods burdened by taxes that only apply to domestic manufacture.

Structural Adjustment

The TCF industry has been the subject of substantial government involvement in its affairs for some time with industry specific arrangements evolving over time into industry wide plans covering a number of manufacturers.

The arrangements applying in the industry have been periodically reviewed by the Productivity Commission, the Industry Commission and its predecessors. Since 1985 the arrangements have included three main components:

- Steadily declining tariffs;
- An arrangement which gives manufacturers duty free entry of to a level of their value of production; and
- An export facilitation scheme / Competitiveness and Investment Scheme.

It is clear that reductions in assistance since the mid 1980s have led to increased productivity and performance by the TCF. While the competitiveness of the industry has increased as evidenced by growth in exports in the last few years, there are still significant investment and technology issues to address.

For that reason we support the continuation of the Strategic Investment Program to maximise the benefits of the program to date and to give the sector some continuity and certainty. There were teething problems with the introduction of the scheme and in essence it has only been fully operational for two years.

Our members have advised that there have been administrative and commercial burdens of accessing the SIP, and have suggested that the current \$200,000 threshold of eligible expenditure in relation to eligible activities should be reduced to \$1000,00 and the 5 per cent of turnover grant cap removed.

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For the industry, critical issues include re-investment in plant and equipment given the global nature of the industry, innovation, an appropriately skilled workforce, and environmental regulations will affect the competitiveness of the Australian industry in the world market. ACCI supports further structural adjustment assistance to the sector to help it become internationally competitive.

The PC has recommended the following approach to SIP:

- *Following expiry of the current SIP in mid 2005, a new transitional support program would operate for eight years.*
- *Total funding for an initial four year period would be set at \$560 million – equivalent to notional annual funding levels under the current SIP (in nominal terms).*
- *Funding for the subsequent four year period would be halved to \$280 million.*
- *Transitional support would then terminate.*

ACCI supports this approach.

We also note that the PC has proposed three options for addressing the design deficiencies in SIP:

- A: a modified version of the current SIP with least disturbance to the current framework
- B: a value added bounty
- C: a competitive bidding scheme.

ACCI's preference would be for option A as on balance it will improve the existing scheme without changing the nature of it, and is more likely to deliver outcomes. Option B & C also appear to be more complex, and administrative simplicity is preferable.

Recommendation

ACCI recommends that:

- the TCF tariffs remain at their legislated level from 2005, and be traded away in the context of multilateral negotiation – either through WTO negotiations in the Doha Round, or through the APEC commitment of zero tariffs;
- SIP be extended to 2013 along the lines as proposed by the Commission with a phase out, and that the scheme be

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maintained in its current form with minor modifications rather than changing it to a value added bounty or a competitive bidding scheme; and

- the PC advises the Government to remove the 3 per cent tariff impost imposed on TCF manufacturers under the Tariff Concession, and to remove it for manufacturers in all sectors.