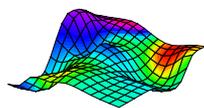


Report to

Australian Wool Innovation

Benefit Cost Analysis of AWI's Cool Wool Campaign Investment

December 2014



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BACKGROUND

BDA Group was commissioned by AWI to complete a benefit cost analysis (BCA) of their marketing investment in the Cool Wool Campaign. This investment was made under AWI's 2010-13 Strategic Plan, Marketing Strategy 2: Product Promotional Partnerships, Program 1 – Trade and Consumer Product Promotion – and will be funded until 2016 under the 2013-16 Strategic Plan as a separate program under Strategy 9 - Product Promotion. The analysis was completed with the primary purpose of providing a robust assessment of the potential returns to Australian woolgrowers from that investment and forms part of the series of AWI investment evaluation reports. These analyses are publically available from AWI¹ and apart from reporting the return on investment to shareholders supports the on-going process of investment planning and reporting across the organisation.

COOL WOOL DEVELOPMENT

Cool Wool was originally developed and launched by AWI (operating as The Woolmark Company) in the 1980's. At that time wool garments had a minimal footprint in summer and spring seasons as economically viable lightweight wool garments could not be produced. With developments in processing technologies lighter weight fabrics were able to be produced and marketed to consumers. At that time fabric weights were around 220 grams per square metre. From 1984 AWI has registered a number of trademarks around the world based on the Cool Wool name and Woolmark logo.

AWI's original Cool Wool program was deemed a success² and since then continued developments in wool processing has enabled even lighter weight fabrics to be produced. Since 2006/07 AWI has continued to invest in product development and marketing to support the market uptake of lighter weight wool fabrics outside of the traditional consumption periods over autumn and winter.

- In 2006/07 AWI supported merino "Cool" suits with high twist yarns (for product strength) with commercial partner Nippon Keori Kaisha and retailer Aoyama³.
- Development of Ultra-Light Merino with garments up to 30% lighter weight and still maintaining their durability, structure and style⁴.
- "Merino Cool" in 2008/09 where fabric weights were developed at 165 grams per square metre with 15 supply chain partners. The campaign was launched at Premiere Vision in 2008 followed by one-on-one regional retail workshops with the focus on women's wear. The Merino Cool trademark was

¹ <http://www.wool.com/en/about-AWI/how-we-consult/measuring-performance>.

² AWI Cool Wool Website

³ AWI 2006/07 Annual Report – page 11.

⁴ AWI 2007/08 Annual Report – page 50 – mainly with CSIRO investment in Trans Seasonal Cool Touch Merino.

registered in 2008 across three jurisdictions and Italian collections of lightweight woven's and knitwear produced with marketing collateral and support up to 2011⁵.

In 2011/12 AWI relaunched the original Cool Wool branding at Premiere Vision based on new Woolmark specifications for trans-seasonal wool apparel with a new consumer campaign launched in Dubai. Fabric weights were set at a maximum of 190 grams per square metre⁶. The Cool Wool brand is a sub-brand of the Woolmark and Woolmark Blend program and Cool Wool branding is available to all Woolmark licensees that are able to produce fabrics and garments to the Cool Wool specifications. Brands and retailers are also able to use the Cool Wool branding on their product if it is sourced from a licensed manufacturer⁷ (Cool Wool Guild of Manufacturers).

INVESTMENT

The AWI Cool Wool Program emphasises that wool is both cool to wear and “cool” in a social sense. Investment is made with partners from top making through to retail and supported with targeted consumer marketing campaigns that link in with a range of in-store activities, promotions and events. The broad objective of the investment is to increase the demand for Australian wool by consumers over summer and spring and warmer transitional seasonal periods.

Investment was first made in 2011/12 and is expected to continue over the current Strategic Planning period to 2016. Investment costs are provided in Table 1. Over the life of the Program AWI will invest \$17.1m (\$17.3m in current dollars).

TABLE 1: AWI COOL WOOL INVESTMENT: 2011/12 TO 2015/16: \$M

Investment	2011/12	2012/13	2013/14	2014/15	2015/16	Total
Project	\$0.7	\$1.8	\$3.2	\$2.2	\$2.2	\$10.1
Operational	\$0.5	\$1.3	\$2.2	\$1.5	\$1.5	\$7.0
Total	\$1.2	\$3.1	\$5.4	\$3.7	\$3.7	\$17.1

Source: AWI Annual Reports, AWI Program Achievement Reports and 2014/15 Cool Wool Program Plan. Note: Operational Costs were based on a multiplier of 70 cents for every dollar invested in projects.

⁵ AWI Annual Reports – 2008/09 page 12 & 15; 2009/10 page 4 & 12; 2010/11 page 20.

⁶ AWI 2011/12 Annual Report – page 17.

⁷ Background information was sourced from the Cool Wool Website.

PROGRAM PROGRESS

AWI's Cool Wool Program seeks to increase the demand for Australian wool by 730,000 kgs by 2016. This target is being pursued under a range of initiatives that leverages off the AWI Cool Wool brand, including:

(1) Involvement of Manufacturing partners.

AWI works with a number of manufacturing partners to support them in gaining accreditation for producing fabrics to the Cool Wool specification. Retailers purchasing Cool Wool fabrics or garments from these manufacturers are able to label their products with the Cool Wool brand. SML have been commissioned by AWI to produce Cool Wool tickets and Labels (T&L), which are available to manufacturers and retailers, and these parties are also able to produce their own tickets and labels that are consistent with their own branding requirements.

(2) Market Operation.

AWI has identified a number of markets where there are opportunities for increased consumption of Cool Wool products. Cool Wool program materials and activities were initially targeted at eight key markets – UK, France, Germany, Spain, Japan, Korea, Turkey and India – and once the program was consolidated in these markets the program was expanded to other markets where consumer growth opportunities existed.

(3) Media Activities

Consumer interest in Cool Wool products is stimulated through AWI investment in activities that communicate the benefits of lightweight merino fabrics and garments, including the fashion interest in Cool Wool by leading designers and brands. These activities seek to generate substantial media reach across consumers, including access to Cool Wool branded digital media, such as the AWI Cool Wool website.

(4) Retail Partnerships

The final area of investment made by AWI under the Cool Wool Program is in collaborative marketing partnerships with leading retailers and brands. This involves assisting retailers and brands to source appropriate Cool Wool fabrics and garments and delivering tailored marketing programs that leverage off the established Cool Wool brand and broader AWI media activities. As a result of the AWI Cool Wool program these retail and brand partnerships will increase the sale of wool garments, and hence increase the demand for Australian wool.

A number of key performance indicators have been developed and progress towards these targets is reported to the AWI Board on a regular basis. Targets set for 2013/14 to 2015/16 are articulated in the AWI Strategic Plan and are revised through time subject to changes in program budgets. By the end of 2013/14 the following progress against set targets has been achieved⁸.

- Manufacturing partners to reach 20 by 2015/16 – currently there are 23 Cool Wool licensed manufacturing partners that make up the Cool Wool Weaver's Guild.
- Increase markets from 11 in 2013/14 to 15 by 2015/16 – the Program is operational in 9 markets including India, UK, China, Middle East, Japan, Korea, Australia, Turkey and Germany. A decision was made in 2013 to withdraw resources from Spain due to continued depressed economic conditions in that market. With reduced funding planned for 2014/15 investment will be consolidated in existing markets.
- Add 6 new Woolmark licensees by 2015/16 – this target has been achieved already (Holland and Sherry Group, Dormeuil, Cerutti, Altinyildiz, Hield and Moxon).
- Increase retail partners to 16 by 2015/16 – progress to meet this target is on-track with 12 partners involved with the Cool Wool program (Raymond, Paul Smith, Richard James, Christopher Raeburn, Lou Dalton, MJ Bale, New Yorker, J Press, SARAR, Ipekis, Lotte and Parkland).
- Increase visits to Coolwool.com to 20,000 by 2015/16 – this has already been achieved with 22,067 visits in 2013/14.
- Increase media reach to 20m by 2015/16 – no data was available for 2013/14.
- Increase ticket and label sales by 5% each year – this target was exceeded in 2013/14 with an increase of 210% and ticket and label sales reaching 159,725. The reported figures only include T&L sales through SML.
- New demand to reach 730,000 kgs by 2016 – on-track to being achieved with new demand reaching 185,009 kgs in 2013/14. New demand expressed on a kg of wool basis is a derived measure based on the estimated number of Cool Wool garments that are sold using own labels and tickets rather than those available through SML, the extent to which SML T&Ls are over-ordered, clean wool weight required to make individual garments and the extent to which Cool Wool purchases would have been made anyway (without the AWI Cool Wool Program).

⁸ Based on the end of year Program Achievement Report (July 2014) and Completion Reports across AWI international offices.

For the purpose of this evaluation it was assumed that T&L sales are made on the basis of covering an excess of garment requirements by 10%, that is, the number of Cool Wool garments produced represents 90% of SML T&L sales. In addition, sales data supplied to AWI from a number of partners indicate that total Cool Wool garments sold exceeds those sold with SML T&Ls by a factor of 6. On this basis the number of Cool Wool garments sold in 2013/14 was estimated at 862,515.

To derive the corresponding wool weight of Cool Wool garments sold standard conversion factors have been used⁹. Using an average conversion factor of 650 grams of clean wool per garment the total volume of Cool Wool product sold in 2013/14 is estimated at 560,635 kgs.

The final piece of data required to estimate the extent of new demand is the extent of substitution of non-Cool Wool branded garments for Cool Wool branded garments. This is relevant because consumers have had access to lightweight garments for warmer months for many years and product has been developed and marketed accordingly without AWI involvement or as a result of past investment by AWI in this area. During the Australian 2013/14 summer AWI ran a consumer survey to determine the extent of garment substitution¹⁰. It was found that only 33% of Cool Wool garments sold represented new demand, where these consumers changed their purchasing behaviour in favour of wool garments for wearing in warmer months. On this basis, the volume of new demand generated by the AWI Cool Wool investment for 2013/14 was estimated at 185,009 kgs.

TABLE 2: PROGRESS TOWARDS SET INVESTMENT TARGETS

Measure	2011/12	2012/13	2013/14	2014/15	2015/16
Manufacturing Partners	0	17	23	23	23
Markets	8	9	10	13	14
Media Reach	5.6m	Na	Na	20m	20m
Website Visits	0	10,000	22,067	20,000	20,000
Retail Partners	0	10	12	14	16
T&L Sales (SML)	0	47,950	159,725	167,711	630,234
Total Garment Sales		258,930	862,515	905,641	3,403,263
New demand (kgs)		55,540	185,009	194,260	730,000

⁹ Provided by AWI General Manager Off-Farm.

¹⁰ BDA Group report to AWI, Cool Wool Survey results, 4 March 2014.

Estimated sales and new demand for 2014/15 was based on an assumed increase in SML T&L sales of 5% and the estimated sales and new demand for 2015/16 was based on the assumption that the AWI investment would reach the new demand target. Clearly, there needs to be a far greater increase in SML T&L sales than 5% to achieve the new demand target.

Results from the AWI Summer 2014 Global Fabric Tracker Survey¹¹ identified a number of factors which will affect the extent to which new demand can be generated in the future. Overall it was concluded that the images and benefits from the Cool Wool program convey to consumers that Cool Wool garments are fashionable and comfortable to wear, but that this is not necessarily building new demand (conversion to purchases). Consequently the required increase in new demand by 2015/16 might be difficult to achieve under the current program structure and operation.

- While consumers prefer natural fabrics for wearing in warmer season, merino wool was not strongly associated with being a fabric for all season.
- Although one in three consumers had purchased wool to wear in warmer seasons awareness of Cool Wool and the associated imagery was relatively low.
- There was generally a weaker understanding of the benefits of Cool Wool in the UK, Japan and Italy.
- Cool Wool imagery is seen to depict current fashions.
- After seeing Cool Wool images and benefits two in three consumers agreed that Cool Wool garments are fashionable and comfortable to wear in warmer seasons.

BENEFITS

Benefits are expected to flow to Australian woolgrowers through higher prices for greasy wool as a result of new demand for Australian wool generated through the AWI investment in the Cool Wool Program. The target growth in new demand is 730,000 kgs by 2016 which would be sustained into the future once AWI investment is withdrawn. This level of benefit represents a minimum as no consideration of increased demand past 2016 is made, yet it is envisaged that the retail sector would continue to leverage off the Cool Wool brand to develop further business growth opportunities. Cool Wool branded products would still be expected to be produced by licensed manufacturers.

As many factors influence the price of greasy wool over which the Cool Wool program investment will not impact, including supply conditions through time, consumer incomes, relative prices of competing

¹¹ Nielsen 2014, Global Fabric Tracker Study: Summer 2014, Report to AWI, August.

apparel fibres, market access conditions and global population growth¹², the success or otherwise of the Cool Wool program investment cannot be determined from an analysis of wool price. Instead, the impact on Australian wool grower profitability is derived from the increase in new demand measured on a kilogram basis. This approach enables an “equivalent” price impact to be derived based on demand growth generated as a result of the AWI investment and hence the increase in farm level profits across the industry that can be attributed to the investment. This incremental increase (all other things being equal) will depend on the price and volume effect.

- (1) **Price effect** -responsiveness of demand at the consumer level and the extent to which this demand growth is “passed back” to Australian woolgrowers in the form of higher prices; and
- (2) **Volume effect** - increase in demand that is generated by the Cool Wool Program.

Price Effect

Various economic agencies have tried to model the returns to Australian woolgrowers from increased consumer demand for wool products¹³. The problems with these models include: they require regular updating; can be difficult to understand; and are typically aggregated to a level where it is hard to separate out price effects across different market segments.

In this evaluation a different approach has been used, which is broadly consistent with previous evaluations of AWI investments, and is easier to update and to understand¹⁴. The basic principle underlying the approach is that an increase in wool demand at the consumer level will stimulate a similar quantity of supply at the farm level. The value of this extra supply can be quantified in terms of the additional gross margin that would be earned. This value is then adjusted to reflect Australia's share of total fibres in the extra fibre (garments / units) demanded at the consumer level. For the purpose of this evaluation it was assumed that the extra demand would largely occur for worsted mainly wool garments across fine wools (merino). On this basis the return to Australian wool growers from the price effect associated with a 1 mkg of wool increase in consumer demand was estimated at \$3.9m. This estimate was based on:

- 145m kgs of final product with Australian wool contributing 125 m kgs¹⁵; and
- The gross margin for fine wool and medium wool expressed on a kg clean basis for fine wool of \$4.49.

Volume Effect

¹² See the AWI Strategic Plan 2013/14 to 2015/16, page 19.

¹³ These include ABARE, BDA Group and WA DPI.

¹⁴ This approach was detailed in a BDA Group report to AWI in February 2012. Estimates will provide a minimum value.

¹⁵ Other fibres account for the remainder.

The volume effect relates to the increase in wool (by weight) demand - the target for the AWI investment is 730,000 kgs by 2016. There are three components to this increase for which data is required to measure the increase in new demand.

- (1) Increased Cool Wool garment sales made by participating partners (manufacturing, brands and retail).
- (2) Corresponding clean wool weight based on type of Cool Wool garments sold.
- (3) The extent to which recorded consumer purchases represent substitution from non-Cool Wool branded wool garments that would have otherwise been purchased for wearing in warmer months.

Considering both the price and volume effect total benefits expected to be generated as a result of the AWI Cool Wool investment by 2016 is estimated at \$2.8m a year. Annual benefits to 2016 are provided in Table 3. Two scenarios for the future success of the program are considered. The first is the achievement of the target new demand by 2016 and the second is based on a 5% growth in SML T&L sales. In terms of new demand, the program has so far delivered around 25% of the benefits sought by 2016. It was also assumed that these benefits would be sustained into the future (15 years) as AWI Cool Wool partners continue to enjoy sales opportunities generated from the increased demand (changed consumer preferences is sustained).

TABLE 3: ESTIMATED PROGRAM BENEFITS

Measure	2011/12	2012/13	2013/14	2014/15	2015/16
Target New demand (kgs)	0	61,712	185,009	197,260	730,000
Benefits (\$m)	0	\$0.24	\$0.72	\$0.77	\$2.85
5% T&L Growth New Demand (kgs)	0	61,712	185,009	194,259	203,972
Benefits (\$m)	0	\$0.24	\$0.72	\$0.76	\$0.80

PAYOFF

In this section the estimated pay off on the AWI investment is reported. Measures are reported in Table 4. It was estimated that the AWI investment will generate benefits to Australian wool growers of \$47m in present value terms ¹⁶ if the program is successful in reaching the new demand target. This represents a return of \$3.10 on every dollar invested by AWI in the Cool Wool program over the years 2011 to

¹⁶ A discount rate of 5% was used.

2016. If the new demand target is not reached and only a 5% growth in SML T&L sales is achieved in 2014/15 and 2015/16 then the investment would nearly break-even with investment benefits to Australian wool growers estimated to be slighter lower then AWI investment costs.

TABLE 4: INVESTMENT PERFORMANCE MEASURES

Measure	Target	5% T&L Growth
Present Value of Benefits (\$m)	\$47.28	\$15.24
Present Value of Costs (\$m)	\$15.43	\$15.43
Net Present Value (\$m)	\$31.85	(\$0.19)
Benefit Cost Ratio	3.1	1.0

CONCLUSION

AWI investment in the Cool Wool Program seeks to build new demand as wool is positioned as a fashionable and appropriate fibre for wearing in warmer seasons. To date the program has successfully built new demand across nine markets worldwide. If the AWI target of 730,000 kgs of new demand is reached in 2016 Australian woolgrowers will be delivered a benefit of \$47m in present value terms, which represents a solid return on the AWI investment. On current progress the investment is estimated to nearly break-even with benefits to Australian woolgrowers almost offsetting actual and planned investment costs by AWI.

If Australian woolgrowers are to achieve a solid return on the AWI investment in the Cool Wool Program then the increase in SML T&L sales (and associated non SML T&L sales) will need to be substantially more than the planned 5% each year. While the increase from 2012/13 to 2013/14 far exceeded 5%, demonstrating that such gains might be achievable in the future, the program will need to address the relatively low awareness among consumers of Cool Wool benefits and imagery.