

WOOL SELLING SYSTEMS REVIEW (WSSR)

SUBMISSION BY:

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Our comments as woolgrowers are inserted within the questions as set out in the Issues Paper, preceded by the following general comment:

General Comment

Throughout the ages Australian wool has been treated as a commodity. Attempts in relatively recent times to regard it as, or to prepare it as, an industrial product have foundered on an inability to integrate the industry vertically from bottom up. This has been compounded by the difficulty of preparing a given source of wool from year to year, and season to season, with consistent attributes. Existing marketing systems have contributed to this, though emerging digital and on-line 'sale by description' technologies may help to overcome these earlier problems.

Previous attempts through pre-shearing mid-side sampling (TEAM formula) and local downstream top-making were frustrated through lack of industry support and labour costs, and the positioning of China as the dominant buyer and processor of Australian wools. The collapse of the Reserve Price System in the early 1990s (not to be revisited) removed many inefficiencies as well as resulting in the virtual halving of Australian wool production overall, quite apart from a severely reduced demand for wool in international markets.

This has resulted in a falling back to, or continuing reliance on, traditional well established production and selling systems, in particular the multi-centred open-cry auction. Die hard observers will say this will never change even allowing for some degree of computerised 'sale by description' as that technology develops. However a major innovation that could prove revolutionary, and thoroughly effective, would be to eliminate the 'rostrum' centered auction room wherein the auctioneer calls the shots. Instead, with well supervised 'sale by description' methods, an on-line, digitalised screen system could be developed to eliminate the need for multiple, physically-based auction centres and the

personal attendance of brokers and buyers at the one place at the same time. Sellers would indicate on screen their reserve price and those buyers wishing to compete for or beyond that price would do so electronically. This would result in significant cost efficiencies, more objectivity in the selling process, and provide instant recording and processing of sales.

However if reform could be the order of the day one might doubt whether AWEX's decision-making process would allow it to take a leading role in this regard. Its recent Christmas Eve reversal of an earlier industry decision on minimum bale weights, rejecting a consensus to give the proposed change a working trial, suggests an inability to overcome sectional interests.

Most of those remaining in the industry believe strongly in the product's qualities and have shown a moderate degree of adaptability to change which is encouraging for the future. Whatever, economies of scale for woolgrowers and others, and innovative technologies, will be the future imperative.

Selling costs could also be reduced if the Wool Levy were to be reduced from 2% to 1%. AWI technical services, including R&D support, have proved useful at times but its market promotional endeavours would seem to have been of limited value.

PHASE 1 WOOL PREPARATION

The Review Panel is seeking feedback on the farm visitation process conducted by the wool broker and wool preparation and classing practices.

Are the direct costs incurred by the wool broker in conducting these visits considered to be part of the broker service charge (BSC) incurred by woolgrowers post auction in the account sale? And, if so is there scope for a "user pays" component should the woolgrower not require this level of service?

Timing for service is not how brokers should charge. Their services are more rounded than that. Most are more than mere salespersons. The charge is a flat rate per bale. This is quite competitive. However they should be permitted to include additional identifiable and transparent charges in an overall package for service. The woolgrower should be able to opt in or opt out of some specific categories, with cost adjustments if necessary. Many brokers have a good knowledge of the properties they serve and their existing shearing schedules. Generally they visit early into the shearing to ensure that the shed is well setup, the classer is in place, and the shed handlers briefed.

They may discuss with the woolgrower and the classer selling options, changes in buyers requirements, and the market outlook. Depending on the length of shearing, one or two subsequent visits would be appropriate depending on circumstances and mutual convenience. The essential need here is for 'trust' to exist between broker and woolgrower.

Trust and certainty would be enhanced by the adoption of a standard broker's contract which would itemise and describe the basic services and list additional options (with prescribed fees). The arrangement should be fully transparent and no additional costs should be levied without consultation and agreement with the woolgrower.

During the farm visitations is the wool broker able to provide the woolgrowers and/or classer with recommendations on how best to class and prepare the wool to meet with current customer requirements? Or is the classing advice designed to meet with the AWEX "Code of Practice" for classers?

This is a matter between the broker, the classer and the woolgrower where the broker has relevant experience. Many brokers are also experienced classers and their advice and knowledge of current market conditions can be very helpful. Bale preparation and categorisation is also a key area.

To what extent are the wool brokers providing woolgrowers with information they already have? Do wool brokers have an expert understanding of market developments and implications for sheep husbandry and wool production?

Knowledge in these areas can vary widely. Advice on technical and breeding issues would probably be sought elsewhere. A wealth of informational material can be found on the internet and through direct participation in breeder groups and field trials of limitless variety.

Is there scope for the wool broker to provide additional services during the farm visitation?

In the last decade China has become the largest buyer of Australian wool taking nearly 80% of the total wool clip. This dominance has been accompanied by a more commodity based approach to wool usage as a fibre. Does this evolution present opportunities to create greater efficiencies at the point of shed preparation (for example larger lot sizes) and should the classing "Code of Practice" be reviewed to better suit this evolving processing consumer base?

Previously woolgrowers were encouraged to grow finer wools. Since the price differentiation has almost evaporated - due to changing end product requirements and advanced processing technologies, which allow greater exploitation of coarser wools - it is better to aim for cut (fleece weight) than fineness. Also broader framed sheep develop more meat potential over time.

Larger bale lots may create efficiencies down the line but but would require larger mobs of the one type to be run through the shed at the one time. Testing of a larger lot may not necessarily result in exactly the same outcomes as testing of the same wool in smaller lots. So the issue may come down to concerns about (to mix metaphors) having too many eggs in the one basket.

The AAAA to A bale classifications have limited value. The marks indicate that in the woolgrower's opinion one lot of A's is better or less in quality than another. More important is what comes through from AWTA's testing. Confidence in the testing process is critical.

The NWD and DMFR certifications have proven to be both beneficial and necessary. The AWEX 'Code of Practice' should be reviewed periodically to account for changing conditions and circumstances in the trade.

Wool handling in the shed is also critical, to ensure consistency of bale content and the avoidance of serious contamination. There has been criticism recently of falling standards in this area, even among classers. Have the recent AWI training schemes produced the improvements expected?

PHASE 2 DELIVERY AND TESTING

The Review Panel is seeking input on the process of local cartage, sampling and testing.

For a woolgrower to receive a fully certified AWTA test result on their wool they must first have delivered their product to a wool broker's store that has AWTA certified core and grab sampling facilities. Would there be any commercial benefits to the woolgrower in knowing their final test results prior to delivering their wool to a broker's store?

Only if engaged in direct selling. Most are not.

Is there a more efficient logistical process for conducting the testing compared to the current core, grab, tuft sampling, and sample movement process?

Woolgrowers cannot afford carelessness in this process. If there is a more efficient or reliable process one would like to know about it.

After the wool is sold at auction, who retains the box sample? Is there an industry standard procedure for this?

Good question. Some brokers re-bale the wool and sell it on as their own. Others may do so but give a proportionate rebate to their growers, or discount their per bale charge accordingly (but from what initial cost base?). Broker practice here warrants closer investigation.

Can AWTA testing be performed on-farm or at another regional location of the woolgrower's choice if such alternatives are preferred?

If AWTA were prepared to offer localised service well and good for those who might want it - but it may incur additional cost (which would need to be made clear).

AWTA currently tests for a multitude of measurements including micron, vegetable matter (VM), yield, length, strength, CVD, CVH, position of break, wool base etc. Are there additional characteristics AWTA should test for that would enhance the objective description process and possibly open up alternative processes for the sale of wool?

There is of course the 'comfort' factor. Additionally, if TEAM formula outcomes could be obtained from regular testing there would seem some advantage to processors from that.

PHASE 3 WOOL APPRAISAL

The Review Panel is seeking input on the item of wool appraisal and valuation.

Can any efficiencies or cost savings be achieved within the appraisal stage of the wool supply chain through some consolidation of the three forms of inspection? For example, why not just have the AWTA apply an AWEX type rather than have the wool broker and AWEX both complete this task?

Rationalisation in this area may be overdue. Duplication should be avoided as much as to reduce costs as to speed up the process. There should be one universal basic standard of testing for open selling. Additional test categories over and above the mandatory requirements could be included for direct sellers, as agreed between the woolgrower and/or the broker, the buyer, and AWEX.

Can a combination of AWTA test results and a singular, industry accepted valuation standard provide an online platform for wool to be appraised and valued? If so what efficiencies and costs savings (if any) can be achieved?

If appraisal technologies can be developed to the point where physical inspections are obviated, the existing auction system could be dispensed with and future buying and selling conducted on a common on-line digital platform (see also our general introductory comment in this regard). The cost savings and additional efficiencies would be enormous.

To what extent is physical inspection a necessary element of appraisal and valuation? Would the woolgrower be disadvantaged by relying solely on appraisal and not displaying the physical wool sample

As yet there is no clear answer to these questions. The urgent need is to develop systems that overcome the need for physical display.

Should the industry be seeking to achieve a wool selling system based entirely on sale by description? Are multiple systems needed to address diverse buyer needs?

Yes to the first part.. As for multiple systems, depends on what this implies. Wool is an international commodity the selling of which responds to common, consistent criteria, Complexity should be avoided. On-line digital systems can be adapted to meet divergent needs.

Could woolgrowers exercise more discretion in the type of tests performed on their wool in order to save costs?

See above. It is up to buyers in direct selling arrangements. If they a happy for the wool to be tested differently that is their business.

Does the information provided on the show floor meet buyer needs? What, if any, additional information would be useful? What information could be dispensed with?

Not for us to say.

PHASE 4 PRICE REALISATION

The Review Panel is seeking information and evidence on the effectiveness of the current open cry wool auction system as a mechanism for competitive and cost effective price realisation, in particular:

This boils down to confidence or otherwise in the 'system' (see below). We believe that changes need to be made to its current modus operandi and have made suggestions elsewhere in this regard.

What other selling alternatives exist for woolgrowers in the market place today and how do the selling costs to the woolgrower compare to the traditional auction method? What other methods are worthy of investigation?

Do or could other selling alternatives generate a comparable or greater level of competitive tension at the point of price realisation relative to traditional auction?

If the auction system delivers the highest level of competition for growers' wool are there more cost and time effective methods that would ultimately benefit the woolgrower (for example: online selling) and would these savings be passed down to the woolgrower?

The present auction system is dominated by exporters purchasing wool on behalf of their clients. Is there further potential to shorten the supply chain and involve downstream interests earlier in the ownership of wool with a view to removing or reducing costs?

The Panel understands that due to a reduction in weekly auction volumes a number of exporters no longer employ a full time wool buyer in each wool selling centre of Australia. This has resulted in a number of commission buyers holding multiple buying limits from a number of exporters. Against this background, is it well known whom a commission buyer is acting for in respect of individual purchases? Do commission buyers confront any conflicts of interest in their purchasing decisions when buying on behalf of clients with similar interests? What effect (if any) do such issues introduce with respect to competition for a woolgrower's wool? Is there a need to cap the number of clients one commission buyer can buy for?

Are stakeholders able to draw examples of previously attempted selling alternatives and reasons for their lack of adoption to the Review Panel's attention?

Are auction results communicated in an efficient and timely manner to market participants and thereby enhance the dynamics of the price discovery process? Why is it necessary for AWEX staff to attend auctions to record information for their market reports? Couldn't this information be automatically generated at lower cost?

Are the auctions basically the same in each of the three major selling centres, or do they differ in some respects? Are there transparent rules governing the conduct of auctions? Do auctions in the different centres generally realise similar outcomes for the sale of specific wool types?

Are there barriers to entry or other impediments impacting participation at Australian wool auctions? Could those barriers or impediments be reduced by adopting alternative processes? What are the key requirements and/or costs applied in order to participate?

Comment:

Woolgrowers are stuck here between a rock and a hard place. They are very familiar with but not altogether trusting of the auction system. However they are by and large even less trusting of any other system working better over any extended period of time, because alternatives tend to break down over time. On-line, 'sale by description' digital platforms could be the answer in due course, as the technology is refined and confidence in these systems grows.

The auction system can be seen to be somewhat arbitrary and capricious for some woolgrowers. There is a belief that it has become too formulaic and mechanistic, and that outcomes are subject to chance between the good, the bad and the indifferent. The rapidity of turnover (200 to 300 lots per hour) and unseen anomalous factors contribute to this. There have been situations where sudden market fluctuations occur within a few days or even within hours which are difficult to analyse and explain. Woolgrowers may feel that justice has not been done to their clip in a particular case. This is less of a concern for larger woolgrowers who can stagger their selling over longer periods. It is best to have a broker who can act decisively when something in

the market is amiss or suspect, and who can physically accommodate passed in wools without additional grower costs.

We repeat the comment in our general introductory observation concerning a change in the open cry auction system, as follows:

A major innovation that could prove revolutionary, and thoroughly effective, would be to eliminate the 'rostrum' centered auction room wherein the auctioneer calls the shots. Instead, with well supervised 'sale by description' methods, an on-line, digitalised screen system could be developed to eliminate the need for multiple, physically-based auction centres and the personal attendance of brokers and buyers at the one place at the same time. Sellers would indicate on screen their reserve price and those buyers wishing to compete for or beyond that price would do so electronically. This would result in significant cost efficiencies, more objectivity in the selling process, and provide instant recording and processing of sales.

PHASE 5 INVOICING AND PAYMENT

The Review Panel is seeking information on the post sale invoicing process and the various charges.

In what proportions is the Post Sale Charge (PSC) borne by the various participants in the supply chain? For example, is the cost incurred by the exporter reflected in the price paid by the overseas customer? Or is it taken out of the initial price they bid at auction for the woolgrower's wool?

One cannot comment much on this except that where clearly excessive charges and duplication could be avoided the ability of buyers to pay higher prices might be increased.

What services are provided by the wool broker to the woolgrower that are covered by the Broker Service Charge (BSC)?

See also above. This can be a mystery for some. The essential requirement is that there should be detailed itemisation and transparency in all aspects of the arrangement and of the respective charges and costs.

What services are provided by the wool broker to the buyer that are covered by the Post Sale Charge (PSC)?

Are all costs incurred by the woolgrower sufficiently transparent (ie. are they generally known and publicised prior to the sale of wool?)

Is there potential for a more detailed breakdown of the individual selling and buying costs of wool to be made available to woolgrowers to facilitate more informed commercial decisions regarding the sale of their wool? Is there a need for an industry standard invoice or account sale format?

See above.

Given a move to a more transparent invoicing standard, would there be a demand for the broad introduction of a tiered wool broker service/price offering, such as: Premium, Standard and Basic?

See above. This may remove some misunderstandings and induce more confidence in the relationship.

Could there be any material benefits to woolgrowers by extending the exporter's payment period for wool from the existing 7 days prompt period? (ie. would this free up additional working capital that could be applied to create increased competition at the point of price realisation?)

No.

PHASE 6 EXPORT PROCESS

The Review Panel is seeking information on the export process and the scope to reduce costs and create further logistical efficiency. The Panel has a particular interest in:

whether there is scope for the exporter and processor sector of the industry to leverage its combined scale to negotiate more competitive freight rates from shipping companies and freight forwarders.

whether the exporter sector of the industry can leverage its combined scale to negotiate more competitive rates from wool dumps and whether there is scope for an industry owned and/or managed facility.

the exporter's ability to achieve consistent and competitive funding lines from banking institutions, particularly considering a high percentage of wool is shipped prior to receiving payment for the goods.

No specific comments on the above. Securing larger bale lots may achieve economies of scale but is unlikely to directly benefit the woolgrower (see comment above).

PHASE GENERAL

The Review Panel is seeking information on the following areas that do not fall within the 6 phases of the selling process referenced in this paper but relate directly to the overall scope of the Review.

Wool industry institutions

AWEX undertakes a variety of tasks, including market reporting and ensuring accuracy in wool description, that help the wool market to perform efficiently. In a similar vein, AWTA supports market efficiency by providing critical data describing the range of wool characteristics. Would there be advantage in combining the activities of AWEX and AWTA?

AWEX and AWTA have different functions which by being kept separate protects and strengthens the integrity of the overall system. However, as noted in our introductory comment, if reform of the system is what the industry requires one might have doubts as to AWEX's capacity for leadership following its inexplicable Christmas Eve reversal of an earlier industry decision on minimum bale weights. In doing so they even rejected a modest industry proposal to give the agreed change a year-long working trial. Such inconsistent unilateralism does not engender confidence.

Is there an opportunity to increase competition in wool testing services currently provided by AWTA? Should woolgrowers be able to nominate what tests they would like performed on their product and pay accordingly for the services provided?

AWTA testing (whether central or regional) should and must remain the mandated standard. As for non-regulated testing, if direct sellers see an advantage in seeking alternative services and are prepared to meet additional costs, the option should be available.

Talman Solutions provide the majority of wool exporters and a large number of wool brokers with inventory management IT systems. Do the systems provided by Talman Solutions generally meet the requirements of their customers? Is there potential for greater competition for this service offering within the wool industry?

AWEX market reporting

Does the AWEX market report meet the needs of both the buying and selling sides of the market and if it is deficient in any way, how should it be amended?

Is there sufficient access to AWEX market information?

What influence (if any) does the AWEX market report have on purchasing decisions made by overseas wool processors when negotiating with Australian wool exporters?

From a woolgrower perspective AWEX market reports meet routine needs. Australian Wool Industries Secretariat (AWIS) is a valuable information resource and service to the industry. Other institutional and private groups also provide useful and timely information for woolgrowers. AWI would of course be included among these.

Centralisation

What are the benefits and costs of any move to centralise the sale of wool?

Would centralisation provide increased opportunity to conduct alternative processes for the selling of wool?

What impact would centralisation of wool selling centres (Sydney, Melbourne and Fremantle) have in relation to cost reduction and competitive tension for woolgrower's wool?

What financial impact would centralisation of wool storage centres have on the exchange of ownership process?

Did previous studies on centralisation identify tangible financial benefits within the exchange of ownership process? And if so what were the barriers to progressing with centralisation?

Once online platform selling becomes the 'system' there will be a 'virtual' centre and that will deal with the centralisation issue. However brokers may wish to establish locations where wools might be inspected if requested by a buyer(s). Meanwhile the three existing selling centres should be maintained.

Digitalisation

Can Australian wool be appraised without physically handling a wool box sample? And if so would that appraisal be accurate enough to allow an exporter or processor to deliver wool in accordance with a specific mill or customer's requirement?

Can price realisation between the seller and the buyer be achieved via an online platform whilst still maintaining a comparable or improved level of competition for woolgrower's wool?

What cost saving benefits can be achieved by online appraisal and or selling? And who would benefit from it?

Why have previous attempts at the online selling of wool failed?

See comments above. In short this is an area that warrants extended development. The nature and costing of broker services would have to adapt

of course, but there would still be a central role for brokers in relation to market advice, clip preparation and promotion, and bale handling.

Transparency

What scope is there to allow woolgrowers to make better informed decisions in relation to what it is costing them to sell their wool? More specifically would greater understanding of the costs and returns reflected in their final price received facilitate improved commercial decisions concerning their own wool growing enterprise?

To what extent does the woolgrower understand their own cost of production before their wool leaves the farm gate? Is there scope for a greater understanding of both production and selling costs to facilitate more informed commercial decisions for woolgrowers?

See comments above. Woolgrowers would be better informed as to all aspects of production and selling if there were greater transparency in relation to all stages in the process from farm gate to sale, and beyond.

Woolgrowers should also be provided with meaningful feedback from downstream operations concerning the reception and performance of wools in their category, end-user appreciation, and outcomes (problems or otherwise). There would be an enhanced role for IWTO in these areas.

Selling alternatives

Whilst there are numerous selling alternatives to traditional auction that are made available to woolgrowers they can generally be grouped into five categories – Direct selling, Private buying, Physical forwards, Forward Basis contracts (cash settled against micron indicators) and online selling (currently performed by Auctions-Plus). The table below illustrates the process flow and relevant costs of each selling avenue.

TABLE 3. SELLING METHODS IN WOOL

The table suggests that in all cases the alternatives to traditional auction present fewer stages and more potential cost savings compared to traditional auction. Yet more than 90% of Australian wool still sells by traditional option.

Why has there been minimal woolgrower adoption of these alternatives?

Are there up front cost savings offered to the woolgrower by the wool-selling broker to use these selling alternatives?

Does the industry have the necessary skills, knowledge and expertise to utilise these options?

Are there training initiatives the industry should examine to enhance the skill base necessary for uptake of alternative marketing options?

Do the above selling alternatives provide the same level of competition for woolgrowers' wool as traditional auction?

TABLE 3. SELLING METHODS IN WOOL SUPPLY CHAIN FROM AUSTRALIAN GROWERS TO FIRST BUYER

What forward selling mechanisms currently exist in the market place for wool producers? What systems might be introduced and are worthy of further investigation?

The Panel understands that there have been a number of forward selling platforms within the wool industry that are no longer available. Why were they discontinued? And are there aspects of these platforms that could be retained if developing future forward selling mechanisms?

In other markets, automation and connectivity has made it easier for the development of derivatives products such as futures and options. Would such products create new hedging opportunities for woolgrowers and other market stakeholders?

The reason that forward selling platforms (Futures and Hedging) have failed or are under-utilised is because there is not enough market depth and volume in the product. Cotton, being a more uniform product and because of the size

and scale of its markets, has developed viable forward selling platforms. There is also a suspicion of a lack of sufficient integrity in existing wool selling systems to warrant confidence in this respect. This too warrants closer inquiry.

Would there be benefits to the woolgrower by unbundling and making transparent the existing costs within the supply chain to allow them to be more selective in the services they adopt?

Our comments on this cluster of issues can be inferred from the comments above.

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