AUSTRALIAN SUPERFINE WOOL GROWERS' ASSOCIATION INC

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17 March 2015 ASWGA-15-051

Mr John Roberts
Executive Officer
AWI Wool Selling Systems Review Panel

ASWGA Wool Selling System Review Submission 2015

Dear John,

ASWGA appreciates the extension time to complete our submission and the opportunity to add to the discussion. The following submission is a compilation of members' views and we trust the panel will find them beneficial. Additionally there are three attachments that are relevant to your review.

Please do not hesitate to be in touch with any queries you may have on information contained or questions that may arise.

Kind regards,

John Taylor
President

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Dear WSSR Panel,

The Australian Superfine Wool Growers' Association(ASWGA) is incorporated in Victoria and holds 'peak body' status with Austrade for the superfine (SF) and ultrafine (UF) sections of the wool industry, with national membership covering all states of Australia and Mill membership throughout the European Union, India and China with additional strong alliances across nine countries as well as Australia. ASWGA was founded in 1971 and our membership criteria is established on the quality of our members production and production systems with an annual subscription.

In Australia the Association has eight Regions, each Region has elected honorary representatives serving on our National Council and that Council elects our honorary Executive. The work of ASWGA includes representing UF & SF interests and needs across all sectors of the industry including AWI ICC, WPA, AWEX Classing Codes & Appraisal guidelines; and AWTA measurement; also ASWGA furthers the understanding of international mills on UF & SF qualities and possibilities through ongoing dialogue and liaison.

WOOL SELLING SYSTEMS REVIEW

A successful Wool Selling System for ASWGA members will have the capacity to recognise and differentiate qualities and important properties relevant to each wool category and additionally have the capacity to achieve the best market price system for each and every wool Type.

In recent times in an effort to streamline inefficiencies and increase profitability/viability, the whole wool industry has focused on reducing costs and improving productivity within that lower cost regime. We have taken our collective eye off the price makers.

Australia produces good quality wool in all categories for all uses and we have good reliable supply on offer, what we do not have is a system that differentiates 'what wool, is fit for what purpose'. A good example of successful differentiating was some years ago when Castrol Oil, in their campaign of "Oils ain't oils" introduced this concept. Today in any service station or auto shop selling oil there is a vast range with oils fit for purpose. The consumer is educated and expectations are met in performance and quality.

SF & UF high crimping Merino wool is the first sector to be suffering severely from this oversight. Good competition has fallen away as all SF & UF Merino has been lumped together under micron ranges void of focus on the properties and quality; it has been reduced to a commodity.

We must differentiate our Australian wools as fit-for-purpose to stimulate and increase competition within each sector i.e. Building trade, soft furnishings, apparel outerwear, apparel next-to-skin, medical etc, etc.

What can really make a difference to increase the potential return to woolgrowers is to review what are the price makers that are currently in the system and what additional price makers do we need to include in the system.

We thank you for the opportunity to submit our member's views on the Review Panel Issues Paper. ASWGA is more than happy to answer any queries you may have on information contained or questions that may arise.

ASWGA's priority setting for the WSSR three key objectives are:

a. evaluate whether greater efficiencies and cost savings within the exchange of ownership between the seller and the first buyer are attainable – *Efficient and cost effective systems are always important however this is a lower priority than (b).*

b. understanding the potential for increased competitive tension throughout the wool selling process and how it can be achieved, and – ***This is the highest priority for ASWGA as competitive tension is all but absent in the current wool market.***

c. determining whether there is sufficient transparency within the exchange of ownership to allow woolgrowers to make the most informed commercial decisions about their wool growing enterprise. – *The greater balanced and accurate knowledge held by the woolgrower, the better our decision making process will be.*

PHASE 1: WOOL PEPARATION

Extra Costs of Production specific to Superfine Wool

It is worth noting that while the Australian clip average Lot size is 5 bales; in high crimping SF fleece wool 18.5 – 15.6 the average Lot size is 3.4 and in UF fleece wool <15.5 the average Lot size is 2.6. If this included high crimping oddment wool in these categories the average would fall.

Depending on the enterprise ASWGA members' wool preparation can include any or all of the following points raised by members.

- Production and preparation of superfine wool has been a specialised activity for many years. This involves extra shed staff at shearing when the fleeces are being skirted and more attention is paid to detail by the SF & UF Wool Classer. In SF & UF wool preparation using 3 shearers would require a minimum of 2 rousabouts 2wool rollers a Classer and a presser.
- To produce the best 1PP superfine bales, sheep are coated and these coats will need replacing as the wool grows, fleeces are often double skirted, backs are taken out and only the very best sections of any fleece are included.
- In a stud operation shearers are paid 1.25 times for stud sheep and double the award rate to shear rams. Rams also have to be sedated.
- Increasing occupational health and safety regulations are payable by all growers depending on the length of the shearing process. SF & UF shearing is a longer process on a per head basis therefore this cost is greater per sheep on specialty wool enterprises.
- The rams head logo along with Growers membership number used on bales of ASWGA members wool serves as a QA indicator designating the extra care in the preparation of these wools.
- Additional classing prior to shearing is often carried out with full OFDA testing being incorporated to fine tune Lot contents.
- Wool harvesting now represents 1/3 of woolgrowers costs. (New methods of shearing still need to be seriously considered).

Is the wool broker able to provide woolgrowers and/or classers with recommendations to meet with customer requirements?

- The AWEX Classing Code and the AWEX Appraisal Guidelines both establish good independent classing standards and description codes across Australia, however these do not replace the role of our Regional Broker. The Regional broker support is still valuable as current customer requirement information is very important when preparing specialty SF & UF wool lines.

Most growers are expert on their own enterprises however few meet with the processors and manufacturers to gain insights on those customer needs and problems. Brokers see buyers on a regular basis and processors from time to time, keeping up to date with industry intelligence. The Broker is our initial liaison between grower and buyer.

AWEX Code of Practice & the AWEX Appraisal Guidelines

- AWEX worked collaboratively with ASWGA and others to establish the current AWEX Code of Practice, and in recent years AWEX and ASWGA workshopped the guidelines to update the AS Appraisal Guidelines.
- ASWGA definitely endorses the AWEX Classing Code and the AWEX Appraisal Guidelines as both establish good independent classing standards and description codes across Australia.
- ASWGA Superfine Classers ensure the strictest classing standards. Specialty SF & UF Merino classing aims to present the best quality and differentiate AS Type attributes to attract a premium price, ensuring our customers that the Merino wool purchased is fit-for-purpose.
- The wide spread practice of not classing wool and/or bulk pressing is not an option for specialty SF & UF woolgrowers. It is a one-size-fits-all commodity approach aimed at the cheapest outcome and underpins a no-premium price system.
- Chinese buyers only buy using micron, other wool characteristics needed for the production of fine quality cloth are often ignored. Therefore China taking around 80% of the Australian clip, consumes all wool into a commodity bracket with no allowance for end use. They either do not know or choose to ignore, in favour of low cost, the better product and marketing edge that can be gained through differentiating attributes throughout the Australian clip.
- The important attribute of curvature does not feature in the orders on raw wool, as micron, length, & strength make up the hauteur measurement and further dissemination.
- Streamlining the division of Lots and clip preparation for SF & UF Merion would depend on the identification of wool Type and curvature. This concept is not suitable for all wool Types.
- The commodity-based approach has been to the detriment of traditional finer crimping SF & UF Merino woolgrowers.

PHASE 2: DELIVERY & TESTING

After wool is sold at auction, who retains the box sample?

Keeping in mind this is a very small quantity of wool; most growers would be unaware what happens to the box sample after wool is sold at auction.

Would there be any commercial benefits to the woolgrower knowing their final test results prior to delivering their wool to a broker's store?

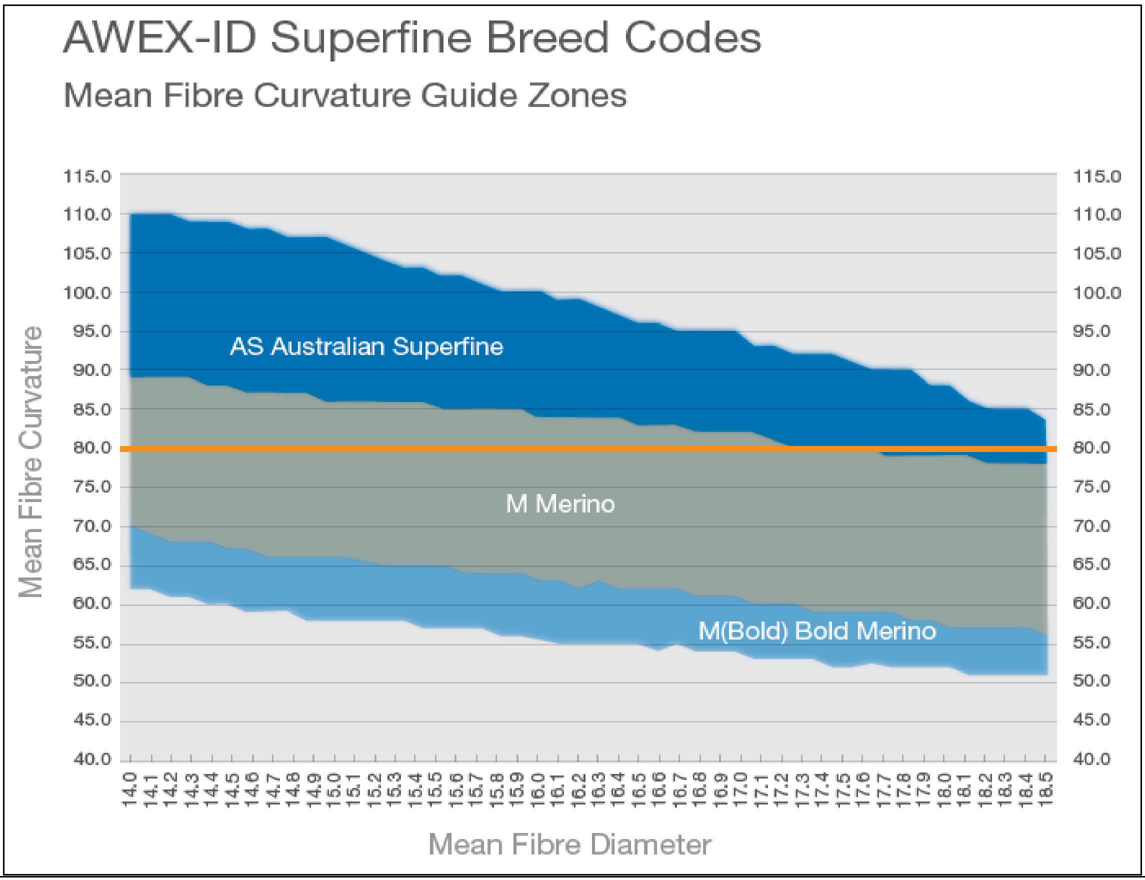
- There are a number of methods used to establish on farm measurement data. Pre shearing or during shearing some growers have in shed testing using either laser scan or OFDA. This requires employment of extra staff and unless the grower owns the equipment a grower is charged per fleece. The cost benefit ratio has meant that some growers collect data yearly others less frequently.
- Knowing the results before sending to store gives the option to store on farm. Many SF & UF growers do test all sheep and micron tag them therefore there is greater certainty on what is included in each Lot and certain markets can be targeted when classing their clip. However for final sale Lot lines or individual bales would still need to be tested. Some superfine growers identify their bales on micron with their own branding code.

Are there additional characteristics that AWTA should test for to enhance the objective description process and possibly open up alternative processes for the sale of wool?

- Curvature affects the processing performance of SF & UF Merino. AWTA currently test for curvature however the test is not as reliable as other tests conducted by AWTA. Yet the survival of the high crimping wool fibre, preferred by the Italians and suiting industry in general depends on being able to identify curvature and report on it accurately.

If curvature testing were reliable more buyers would be referencing curvature in their assessment of Lots to bid on. The SF & UF industry needs a reliable and agreed test for curvature (OFDA or laser scan) to maximise competition.

- SF & UF Merino must always have the opportunity to identify attributes that attract a premium to enable continued production of a fibre used and preferred in the high-end fashion industry, despite the pull by the bulk of the wool industry to target commodity-based practices.

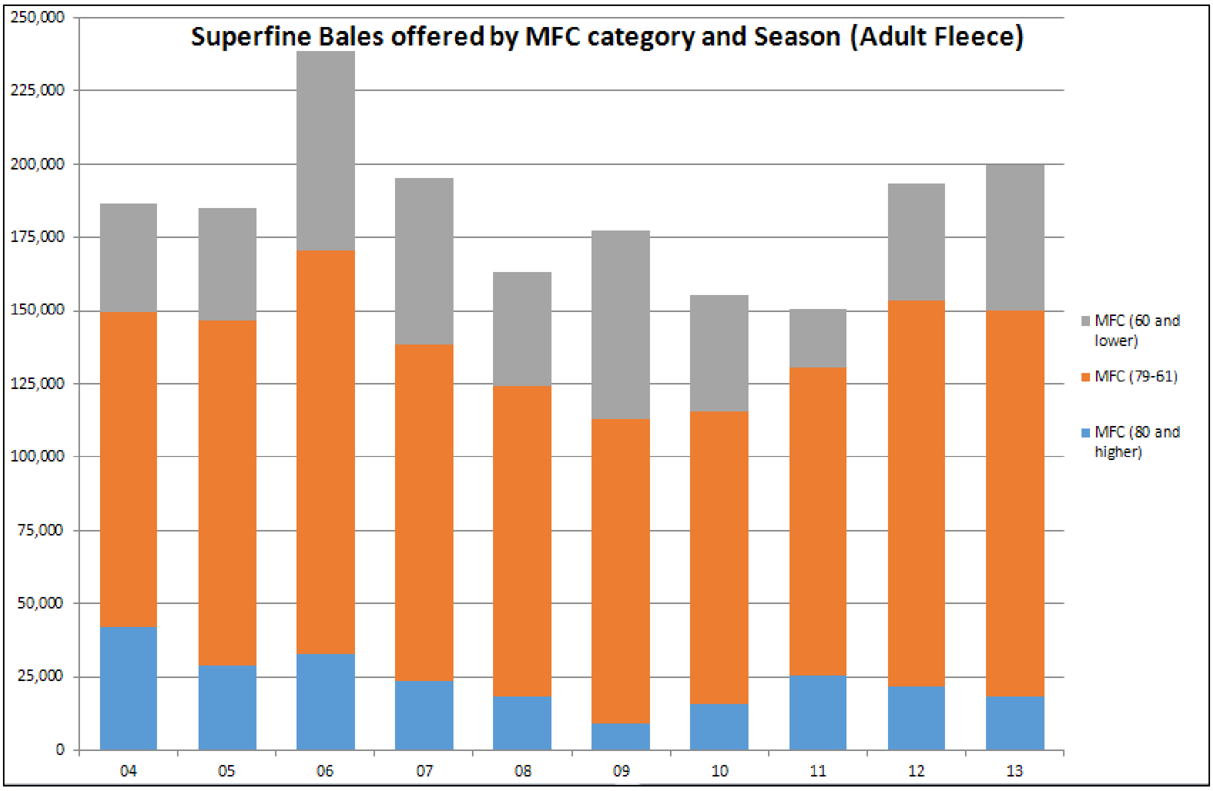


Notes about Mean Fibre Curvature (MFC) and use in AWEX-ID Breed Group Appraisal

- Precision of MFC is not high. It is typically around +/- 7 degrees/mm. Due to its relatively low precision MFC is used as a guidance measure only. Each appraiser/auditor can apply the AWEX-ID breed they feel best suits the visual presentation of wool.
- Wool that has indistinct crimp characteristic can also record high readings (e.g. Comebacks, Downs).
- However, within the Superfine fleece sector the MFC can be used as a tool to assist the appraiser identifying AS and M - Bold types. (The balance are typed as Merino which may display influences of both Saxon or Bold breeding or neither).
- Why use MFC? Appraisers historically have under appraised the presence of AS bred wool. Using MFC it provokes the appraiser/auditor to make a decision.
- Not all appraisers have measured results when appraising the wool.
- The above MFD/MFC profile is indicative of the general bands of each AWEX-ID breed group. In practice the boundaries between each group is more blurred than illustrated on this chart.

Superfine Fleece wool (18.5 and finer) by appraised Breed Group 2013/14 ytd
AS 8.1% M 74.7% M (BOLD) 17.2%

Indicative volumes of Superfine Fleece wool since 2004 using MFC as a proxy for Breed Group.



PHASE 3: WOOL APPRAISALS

Can any efficiencies or cost savings be gained through appraisal inspection consolidation?

All three inspections/appraisals are driven by a different purpose; these three purposes cannot be consumed into one common driver.

Additionally the Brokers, AWEX Appraisers or Buyers already transpose AWTA Test Certificate Results to create the base data for their reports, the work is not done a second time.

As the selling agent, the Brokers appraisal provides an assessment on the potential sale price for the grower to decide how and when they will sell their wool.

The AWEX Appraiser establishes an independent assessment of each Lot based on the uniform standard across all Australian wool, this in turn establishes international product confidence that consistent quality will be supplied regardless of what wool Type is being purchased.

The Buyer will always appraise their prospective purchase to ensure it meets the specific needs of their client and thus protecting their reputation and business.

Can a combination of AWTA results and a singular industry accepted valuation standard provide an online platform for wool to be appraised and valued?

- The Australian wool clip comprises many breeds of sheep and wool varieties fit for different end purposes, “a singular industry accepted valuation standard” would be a particularly complex matrix if it were to accurately reward quality. We already have a very good appraisal guideline accepted by industry in the AWEX Appraisal Guidelines.
- If all required attributes could be successfully tested it would be worthwhile doing a trial on the concept HOWEVER, in the case of SF & UF wools a main differentiator is crimp frequency and there is no agreed test to measure crimp frequency/curvature. Additionally whiteness and other tests, currently too expensive for growers to embrace, would need to be included to differentiate quality SF & UF Merino wool categories.
- Even within the current AWEX Type code, initially some appraisers were reluctant to put genuine SF wool into the ASF category because of style factors such as dust and VM.

To what extent is the 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?

SF & UF would be extremely disadvantaged by an appraisal only system, as at the finer end of the market and in the specialty lines within that market differentiation through crimp frequency, bloom and whiteness, just to name three, are all price makers. The physical inspection of buyers is the only time we realise any premium for these quality aspects.

A selling system void of inspection would be hard pressed to accurately portray differences in wools that experienced buyer’s notice and are willing to pay for.

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

Buyers bid on wools that have the test results they want therefore in SF & UF wools, buyers determine the base set of tests we must have. Limiting the number of tests and therefore the number of buyers interested in bidding on your wool to save a few dollars is a false economy.

Does the information provided on the showfloor meet buyers needs?

- ASWGA has not received any feedback on additional or preferred information required by Buyers.
- ASWGA does canvas Brokers to identify, with an ASWGA logo card on the Lot, ASWGA members wool on the showfloor as ASWGA members practice the strictest classing standards in their clip preparation and no ASWGA branded wool co-resides with any exotic sheep ensuring no D&MF, thus differentiating ASWGA wool from the majority of the Australian clip.

PHASE 4: PRICE REALISATION

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?

- SF & UF Merino is sold through other methods however other selling alternatives for woolgrowers are limited.
- Some growers have ongoing supply contracts with a particular Brand/company; the financial arrangements of these contracts are not public knowledge. AWI has assisted such contracts in the past so perhaps this information is available via the AWI office.
- In the past forward contracts and futures have provided mixed results. Returns are impacted by wild fluctuations in the auction price, our currency or world events and this in turn effect confidence. Futures are not currently available.
- Many growers have struggled to meet contract specifications because of drought or extreme weather events impacting on the ability to meet specifications.
- Acquisition of portions of the clip may still be a possibility incorporating a central marketing body similar to the strategy of merino New Zealand.

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

- Online selling has been successful for some members however anecdotal evidence is that this has occurred after wool has been passed in at a physical auction or when the Brand is already known to the Buyer. So the Buyer in some cases has already inspected the Lot prior to the original auction exposure or there already exists a purchasing history.
- Currently there are so few buyers at the auctions, the auction system actually reduces price discovery. It is difficult to create alternate marketing contracts when buyers can walk into the auction and pay next to nothing for quality UF & SF Merino.
- Would a single desk system work for our type of wool, where price is negotiated – similar to NZMerino?

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?

- Special direct sales by a grower or a group of buyers are rarely sustainable for any length of time. Mostly none of these particular alternatives have enough scale or longevity to solve the problems of the whole industry.
- There is potential for more ownership of wool closer to retail by some entities.

- Today there are few vertically integrated global operations or companies in the trade. Most of those that remain are relatively small. Most early stage processing is still done in China.
- Attempts to set up chain marketing ventures have been undertaken by ASWGA under a separate commercial entity but have not been successful.

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 wool grower and would these savings be passed to the grower?

- Online selling could provide cost savings, but it is doubtful that savings would be passed on to the grower.
- Inevitably the bulk of the clip will eventually be sold by description.
- Other systems may still be needed to market and sell speciality wool.

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

Recently big operators have purchased wool properties in Australia possibly to safe guard their supply and to get the benefits of value adding their own product.

A number of commission buyers hold multiple buying limits from a number of exporters…..

- The biggest impediment to improve prices particularly for superfine wool is the lack of competition. Commission buyers operating on behalf of a number of companies allow them to have a big influence on the market price. Commission buyers are not going to bid one of their orders against another, while this may not technically be collusion it is destroying the fair competition ethic in the open cry auction system and undermining the financial return to the Australian woolgrower.
- Chinese monetary policy reducing the availability of credit to all but a few select and powerful shrewd operators has had a huge impact on prices paid to growers.

Are all costs incurred by the woolgrower sufficiently transparent?

- Immediate costs are all clearly listed on account sales information following the sale of the wool. Brokers charge for different items and have different charging scales. The level of detail seems satisfactory. Offering a tiered wool broker service/price offering has no advantage to specialty woolgrowers, as all costs need to be known.
- Knowledge on the full break up of all costs and who pays, from the farm gate to the first stage of processing could be helpful, as well as also understanding the full processing costs thereafter.

Auction system and information communications.

- Designated AS superfine sales have had some success in the past but in the current climate there is little opportunity to leverage price. Superfine growers have a current request to AWEX re holding AS sales in Melbourne as well as Sydney.
- The availability of market information particularly to the Chinese does give our dominant buyer a huge advantage.
- Recently AWEX has canvassed buyer masking to protect the confidentiality of buyers.

PHASE 5: INVOICING & PAYMENT

- It would seem that the broker service charge BSC, is inevitably passed back to the woolgrower in the price that buyers pay at auction.
- Similarly when wool is stored in outlying regions the extra freight and shipping costs would be factored into the price paid.
- An industry standard invoice appears to be a positive for easy comparison of charges.

Could there be any material benefit to woolgrowers by extending the exporter payment period for wool from the existing 7 days prompt payment period?

The benefit would have to be substantive to offset any delay of funds back to the grower for wool where all production costs have already been outlayed by the grower over the previous twelve months or longer if the wool has been in store.

PHASE 6: EXPORT PROCESS

- ASWGA did have enquiry from a major international processor re Australian wool being scoured in Australia before being exported. The company posed the hypothetical concept that the current wool levy of 2% be charged on all wool exported raw and scoured wool would not attract a levy. As the average yield in the Australian clip is around 70% there would be a 30% saving on dumping and shipping.
- Exporters have to wait too long for payment
- Some companies renege on contracts.
- Only well-established exporters can survive in the current climate.

Wool Industry Institutions

Talman Solutions could be a vehicle to list growers' wool lots prior to auction. This is currently being explored by ASWGA through an upgraded website.

AWEX & AWTA:

- AWEX & AWTA both perform different tasks and at different times in the wool selling pipeline. Both are dealing with woolgrower data. One is involved in a testing role and one in a monitoring role.
- ASWGA has always received willing assistance and valuable information on enquiries pertinent to their fields, from both companies.
- Whether there are efficiencies to be gained and whether that amalgamation would or would not create savings could only be answered by both companies.

AWEX Market Reporting:

- Fee for service seems reasonable however some information should possibly be kept confidential to benefit the Australian sector of the industry.
- More AWEX information should be available to woolgrowers.
- Overseas wool processors do have an advantage when negotiating with Australian exporters because of the availability of local wool market intelligence. eg. Certain companies may have filled their order book.

Centralisation:

- ASWGA members value the opportunity to liaise with buyers, to attend sales and importantly see how their wool clip presents on the show floor. While this opportunity has been dramatically reduced for many with the closure of several smaller selling centres, it would be completely lost for the majority if there were a centralised centre.

- Centralisation will also mean bigger freight costs for outlying regions.
- For the commodity-based bulk wool it could allow for more wool to be accumulated of similar type and more opportunity for alternate processes for selling those wool types.

Digitalisation:

The bulk of the Australian clip could be sold on line without the need of box samples.

Transparency:

Greater transparency is always helpful and it is through knowledge that confidence is created to change an existing practice.

Selling alternatives:

Industry has limited knowledge, time and capital to access alternate selling methods.

Forward selling & risk management:

Could lack of forward selling & risk management uptake be connected to the poor digital skill currently in the wool industry and lack of technology uptake, both of which are now changing.

IN CONCLUSION:

ASWGA is very aware that the current system does need alteration to restore good competition into the market place however this does not necessarily align with cost cutting. Industry does need to focus on the long-term success of the selling system across all sectors of the wool industry and not aim for short term gratification.

In addition to the information above ASWGA includes three attachments that do contribute to the discussion.

1) The Superfine Wool Industry Strategic Review by John Powell, January 2013, does provide information on appraisal and selling systems for SF & UF Merino wools.
2) A member's letter that contains interesting observations.
3) Stanford University School of Business review of NZ Merino

For a little light relief:

One member wrote in that - the ultimate system would be using Bio-clip and letting the wool fall off in the paddock, collecting it with the hay baler and tipping it straight into the container for shipping.......... and maybe one day that may happen!