Submission to

Australian Wool Innovation

WOOL SELLING SYSTEM REVIEW

by

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Introduction

I thank the Wool Selling Systems Review panel for the opportunity to submit comment on the current state of wool selling in Australia, and on the process being undertaken to review it. Unfortunately, I remain sceptical as to the wisdom in conducting such a review, given the cost of doing so, and the potential for dividing the industry. It is unfortunate that from the time the review was first announced, thoughtless language was used, and worse still, quoted in the press, as to what the review was trying to achieve. Such language immediately had brokers, and exporters on the defensive, and questioning of the motive behind conducting such a review. The very same brokers and exporters on whom The Panel will rely for the information required, and who will undoubtedly have contributed most of the submissions. The use in the press of such language as “We want to take the black magic out of it, there are costs that woolgrowers are being charged that they don’t even know what for, …”(Cara Jeffery quoting Stuart McCullough in the Land on November 27, 2014). This is a reference to the Post Sale Charge brokers levy on buyers, comments on which follow later in this submission. A charge that at most is around 20 cents per kilogram, and which buyers build into the price they pay anyway. I contend that wool growers are looking to AWI to find them hundreds of cents per kilogram in wool prices, rather than spending a million dollars (or thereabouts) supposedly exposing a charge that brokers are not even hiding to begin with.

Background

Jemalong Wool is Australia’s original regional flat rate wool broker. Established in 1980 at Forbes in Central West New South Wales, Jemalong Wool grew quickly, and by 1990 was handling in excess of 110,000 bales in five regional centres. Forbes, Dubbo, Walgett, Goulburn and Wagga Wagga. In 1990, the Forbes branch alone handled over 40,000 bales. After changes of ownership, and a brief name change during the 1990’s, acquisitions and rationalisation as the clip was shrinking, Jemalong Wool evolved to what is now, and today operates from three centres, Forbes, Cooma & Tamworth, and handles approximately 45,000 bales.

When Jemalong Wool was established, the entire wool clip was transported by road or rail, to the nearest sea board, mostly to a metropolitan warehouse operated by a commission broker. The objective of the founders of Jemalong Wool was to establish warehousing facilities close to the point of production, hence minimising the freight component of delivering wool to store. With sampling sites within these regional stores, it was only the sample that needed to be transported. Once the wool was sold, only those bales that were being shipped off shore were delivered to the seaboard, whilst the remainder were delivered to a domestic mill, which at that time, were many.

With the establishment of these regional facilities, locally based field staff were also close at hand, facilitating shearing shed visitation for every shearing event, and were accessible at short notice should additional service issues arise. This sudden increase in “client servicing” combined with a low, flat rate, all inclusive fee for every bale of wool handled, rather than a complicated charging structure based on lot size, and gross value, made waves throughout the industry. The “traditional” wool broking companies went to great lengths to discredit this new cost effective concept, even to the point of not allowing them access to the same selling facilities. However, the ultimate wool valuers themselves, the wool buyers, would not have it, and eventually the regional brokers were selling in the same venues as their traditional, and now very threatened counterparts.

Today, most of the clip is handled in this way, and even the companies who ridiculed the flat rate regional concept, offer a similar service themselves.

Wool Preparation

The standard of clip preparation over the last two decades has declined significantly. Again, as one company seeks a competitive edge, or a unique selling point, the advent of minimal clip preparation philosophies ensued. Wool was not being skirted, not classed, and in the most extreme of cases, all wool was simply thrown in the one bale. The practice is then given a catchy name. The grower is persuaded to believe he is delivering to a specific down the line contract for a specific end use, and more often than not, the clip ends up in the auction system again, receiving heavy discounts, and damaging the reputation of Australian Wool, as these un-classed clips need to find their way back into the system. The only saving from a growers point of view, is savings in shed labour. When one quarter (sometimes more) of the growers clip proceeds are spent on wool harvesting, it is understandable why growers see this as an option. Unfortunately, in some(but not all) cases, the lower price received negates the savings made in the shearing shed.

Initially, this came about for the right reasons. There were processing mills prepared to contract directly with growers for their unskirted clips, “all in”. Less shed staff were required, and savings ensued. However, as the national flock, and resultant wool clip continues to decline, it is increasingly difficult to find reliable and skilled shearing shed staff. This leads some growers to continue with this unskirted idea because they simply cannot find enough staff, despite the fact they are being penalised in price for their wool.

There have been exceptions to this rule, and these exceptions are why the practice is still performed today in some cases. Mostly, it is Crossbred types, with little to no vegetable fault, and shorter merino types. As long as such sheep are crutched (negating the risk of stain), there is no discounts of consequence at auction for “a few sweaty edges” in a cross bred clip, or a prematurely shorn merino clip. This does not hold true for all cross bred clips, or all short merinos, but for those who can take advantage of it, and given that the crossbred market is as strong today as it has ever been, as is the carding and short merino fleece markets, this presents a viable option to the grower. Merinos shorn with six to nine months wool growth offer the grower savings in crutching costs, and shed staff, as minimal classing is required for the these. Growers can gain advantages in tensile strength, point of break, vegetable matter content, market competition, lambing percentages, lamb survival, and despite the additional shearing cost, in fact grow more wool in one year than they would had they shorn once.

Role of the Wool Broker

The review panel has indicated in their scope, that the initial contact with a wool producer is “The Canvassing Call”. This is not entirely correct.

The relationship a wool broker has with his client is well established long before this. The fact is that most wool producers choose to sell through a particular company due primarily to the relationship with an individual within that company. This relationship began, was nurtured, and any canvassing was done, long before shearing was imminent. Most wool producers will place a significant amount of faith in the information provided by their broker, ranging from production advice, clip preparation advice as well as marketing and selling advice. Where the "canvassing call" concept is correct, is in the case of another broker attempting to win new business. Even in this case, it is more often than not a longer term process, at times taking more than one or two years, and many canvassing calls, as a new relationship is established, nurtured and a building of trust occurs.

Since 1980, the role of the wool broker has expanded significantly. Then, the broker generally was primarily concerned with the preparation of the clip once it had been delivered to wool store. It was the wool producer who organised a shearing team, a wool classer, paid the wages, organised transport for the wool to store, and waited for the tested data to arrive, usually by mail. Today, in many cases, the broker is "expected" to organise most of these functions. Some growers actually expect the broker to organise a shearing team, pay them (and deduct the expenses from sale proceeds), deliver wool packs and other shearing merchandise prior to shearing, visit again at shearing, and then organise the freight in to store. Such expectations have come about as a direct result of competition between brokers. Once such a service is provided by one broker, such as pick up on farm, others follow suit so as not to lose business. A good result for the grower ensues, but extra cost is added to the broker.

Once delivered to store, growers expect to have test data and market exposure of their clip within days, rather than the weeks the process took twenty five years ago.

Very few wool producers will not require some sort of "advance" on their wool proceeds. In most cases, this is simply to pay the shearing contractor, but in a growing number of cases, it is to pay for something unrelated, such as a tractor payment, an interest payment, or simply living expenses until the proceeds of the clip are in the bank. Most wool brokers are required to provide their clientele with some form of finance, in some cases when credit is no longer available by their bank. Brokers will accept the risk so as not to lose their client to another broker.

Throughout the 1990's, and the extended period of drought and low wool prices experienced during that time, wool brokers staff increasingly found themselves as the first point of contact for wool producers suffering as a result, and called upon to offer advice and even councilling. Councilling for such issues as depression are well outside the scope of the broker, but due to the bond between grower and broker, became a daily part of the relationship. Even today, wool brokers staff are trusted enough by their clients for such issues to be discussed. Wool broker staff are often "the shoulder to cry on" for farmers who are feeling the pressure of poor seasons, or bad finance. This has a profound effect on the wool broker, and a significant number of very effective wool technical staff have been lost to the industry as a result.

The notion that wool brokers only handle the clip in store, sell it, and pay the grower, with little or no interaction until the next shearing, is so far from reality, it is laughable. Such an attitude in wool broking would guarantee failure.

All the functions of the broker, from first contact, travel, providing shearing stationary, delivering wool packs, liaison at shearing, providing financial support, organising freight, receival of the clip, lotting, sampling, storage, correcting pressing and classing errors (such as overweight bales), following up on documentation such as the National Wool Declaration, distributing test data, developing systems to facilitate efficient information transfer, establishing a marketing and / or selling strategy, implementing that strategy, travelling to a sale, or simply conducting the sale electronically, accumulating wool proceeds and ensuring payment, whilst all the time keeping the growers clip insured, and maintaining and guaranteeing the integrity of the bulk and samples in a secure warehouse, are what the grower pays for in his fee to the broker.

The Relationship with the Wool Exporter

It is a matter of public knowledge that brokers levy on the exporter a charge associated with delivery of wool they have purchased. This is most commonly known as the Post Sale Charge (PSC) or Buyers Service Charge (BSC). This fee is levied on the buyer once the wool is purchased to cover such expenses as:

- The continued insurance of the wool purchased (no additional insurance is charged to the buyer, and in most cases, the wool remains insured by the broker, to the point of delivery).
- Free storage for an already understood and accepted period.
- Retreival from the storage location once the wool has been “ordered out” post sale.
- Marking of the Bales with the exporters mark or countermark, as per their instruction.
- Loading of the wool onto transport for delivery to the specified destination.
- Guaranteed delivery within the required time frame to meet dumping and shipping deadlines.
- Data transfer, invoicing, and other administrative functions.

Freight to Destination.

In most cases, this PSC is a fee less than the one charged to the grower for the initial handling and sampling of the wool, but in all cases, it is mostly made up of freight. Over the last twenty plus years, freight rates and insurance costs have increased by as much as 150% for freight, and 300 – 400 % for insurance.

There is a broad range of PSC’s between selling brokers. Growers are entitled to know what this charge is, and what it’s for, and there is not one wool selling broker who will not disclose this information to his client if asked. Understandably, he would not necessarily openly disclose it to his competitors, just as an exporter does not freely disclose to his competitors who he is buying for and at what price. Some things in business have commercial sensitivity, and the wool industry is not immune to these. There would understandably be a reaction if exporters were forced to disclose the margin they were taking on wool purchases.

Prompt and Free Storage Period

The final factor that constitutes part of the PSC is the payment terms afforded to the wool buyer / exporter. These are defined clearly in the Wool Selling Brokers Terms of Sale, which are displayed at the auction sale rooms, and are held on file with the Australian Wool Exchange. They are easily accessed by any and all wool buyers / exporters. It clearly states in the Brokers Terms of Sale that the act of "bidding on an auction catalogue constitutes acceptance of these terms of sale" or words to that effect.

In 2011, the buying and exporting community were under significant pressure financially, as the best market level in two decades and a significantly higher than parity exchange rate with the USD made funding wool purchasers increasingly difficult. Exporters were making it clear to wool brokers that the 7 day prompt and free storage period was too short, and was hampering their ability to fund their purchases. Through representation to industry bodies, including the National Auction Selling Committee, buyers were making it clear they would appreciate, and in fact needed the prompt extended. Most brokers elected to remain with the 7 day prompt, but not all.

Jemalong Wool, and one other broker, heeded the call, and extended the prompt and free storage period to 14 days. Before doing so, advice was sought from exporters as to whether there would be increased competition on the Jemalong Wool catalogue as a result. Exporters indicated strongly that there would be price advantages for implementing an extended prompt. Exporters were asked to provide testimonial comment for the benefit of Jemalong clients, and all agreed to do so. Most delivered on the promise, however some have not managed to "get around to it" despite taking advantage of the more favourable payment terms. Wool growers were advised, and accepted that the extended prompt would benefit them also.

We maintain, that price benefits ARE being realised through greater competition as a direct result of extending the prompt and free storage period to 14 days. It is therefore disheartening to learn that exporters are still of the belief that all brokers operate on a 7 day prompt. It would naturally follow then, that some exporters are unaware of the details of the Terms of Sale they are accepting when they bid.

It therefore seems, in our case, " a bit rich" to read submissions by some exporters questioning the relevance of the Post Sale Charge. As stated earlier, for what is provided, apart from the freight component, the price is arguably below cost recovery. It is the freight component that is the main contributing factor to elevations in the PSC.

Payment

Despite acceptance of the brokers terms of sale and the extended prompt and free storage, some exporters continue to be late with payment, and in the worst of cases, it has become habitual. Being late with payment attracts penalty interest in most cases, but brokers are continually, and increasingly receiving shipping advices for wool that has not been paid for. Most brokers will pay their grower clients' wool proceeds either on the day of the buyer prompt, or the very next day. When the buyer (who has already agreed to the brokers terms of sale) fails to pay for the wool on time, and still expects the broker to load the wool, this causes additional cost, (which is not passed on to the buyer) in administration staff's time and additional call costs chasing payment for wool that the buyer expects to have loaded and delivered. It is not uncommon for administration staff to spend an entire morning "chasing payment", while an unloaded truck waits in the shipping bay. However, where it adds the most cost for the broker, is in rearranging loads and the time it takes to do so. If a transport company arrives at the brokers store to load 120 bales of wool, and is forced to leave 40 behind because they are not paid for, and in the worst case scenario, bales had been loaded, and then had to be unloaded because of non payment, additional costs are incurred by the broker, the transport company, but NOT the buyer. Most brokers will have stated in their terms of sale that wool will not be shipped until it is paid for. As recently as this week, there remain some exporters, and one exporter in particular who has ordered wool out from a sale two weeks ago, is still buying lots this week, and has yet to pay for the purchases he has ordered out.

Wool Brokers organise most of the freight. In a few, and a decreasing number of cases, buyers organise their own freight for which most brokers will issue a freight rebate. From a brokers point of view, this is counterproductive. Brokers, using volume as the key bargaining tool, negotiate the best possible rate with a transport company. It is in the brokers, and buyers best interest to take advantage of this competitive negotiated rate. As a result brokers will only rebate a percentage of the buyer organised freight, so as to protect the business relationship with the brokers carrier.

In addition to increases in freight costs, transport operators do from time to time add a fuel levy to counter rises in fuel costs. Whilst this has abated in recent weeks, it is still a cost, which needs to be absorbed by the broker, as it would be impractical to amend PSC's as often as transport operators invoke fuel levies.

<u>The Efficiency of the current greasy wool selling system in terms of minimising costs associated with the transfer of greasy wool from sellers to buyers</u>

Despite it's perceived failings, the open cry auction system is still the most accurate form of price discovery, with the maximum amount of competition, concentrated in one place at one time.

The inefficiencies in the current auction system are mainly as a result of duplication, and logistics. On any given selling day, multiple companies offer their clients wool for sale in a public auction, utilising many staff each, who have in most cases travelled hundreds of kilometres from their regional bases, conducted a sale of usually only an hour or two duration, only to then embark on the return journey of hundreds of kilometres. For example, a typical sale day for a wool brokers staff would commence at 4.00 am, for a 5.00 am departure. Meet clients travelling to the sale to see their wool sold, travel five or six hours to the show floor, inspect the wool with the grower, hopefully meet with exporters for some "buyer feedback" on their clip preparation, and then conduct the sale. Once the sale has concluded, further negotiation may occur with exporter staff to discuss passed in lots. Then, once communications with the brokers head office have established that all sale information has been received and processed, the broker embarks on the return five or six hour journey, usually stopping en-route for refreshments or a meal with their clients. It is quite common for brokers staff to arrive home around 11.00 pm – 12.00 am, resulting in a 20 hour day. This is then repeated weekly.

This raises the question of why, given the amount of wool currently on the market, do auction sales need to be conducted weekly?

The alternatives, Wooltrade and Auctions Plus Wool have been available for years, but the industry is slow to accept them. Wooltrade, where the grower can list his wool and make it available to the market the very instant test data is available, at a price he is willing to take, does not receive the patronage it should. Auctions Plus, the first viable electronic auction platform has experienced issues with speed and cost, and to date, has failed to compete with the current auction system due to this.

Such systems need to be encouraged.

Wooltrade is already established as a viable alternative to the current auction system, and is widely accepted by both sides of the trade. It simply lacks volume, and suffers from being a "parking bay" for overpriced wool. Auctions Plus does work, albeit too slowly. Furthermore, both these services are owned by companies who are also wool brokers, which tends to discourage some from utilising these services.

<u>The Processs of Local Cartage, Sampling and Testing</u>

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

This in not possible. The result would not be the final test result. The advantage of testing in store is that the integrity of the sample is maintained. The sampling is conducted under controlled conditions, and to a uniform and internationally accepted standard. Anyone who has ever sampled wool in a shed will know that to replicate that on farm would not be possible. Even if it were possible, who is going to guarantee the integrity of the sample, and the bulk? The cost of conducting such sampling will be duplicated when the sample has to be then "confirmed" once it arrives in store. The most simplistic issues prevent this from being an option. For example;

- some growers have wool shorn in multiple locations
- some are extremely remote
- unsealed roads make access impossible when wet
- who will actually sample the wool?
- the wool still needs to be moved off farm at some point, sampled or not

Conclusion

I trust the information provided in this submission is useful and of benefit to the review panel. We have a strong commitment to our wool grower clients to provide them with cost effective wool production, handling and marketing services in order for them to maximise their return. Equally, we have such a commitment to our exporter clients, whom we feel are integral to the success of the industry.

We will be pleased to be given the opportunity to offer further insight to the review panel if and when required.

Rowan Woods

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