SUBMISSION TO AUSTRALIAN GOVERNMENT'S REVIEW OF TEXTILE, CLOTHING AND FOOTWEAR INDUSTRIES

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NSW Business Chamber

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Declaration of Interest

As an organization that champions the cause and growth of business, the NSW Business Chamber has a direct and significant interest in numerous policy issues relevant to this review. In particular, we have identified five major policy areas that reflect the concerns of members. These are:

1. **Growing a dynamic workforce** by achieving nationally consistent and sensible systems of industrial relations and occupational health and safety, as well as simpler funding models and more responsive infrastructure for education and vocational training.

2. **Strengthening the performance of government** by encouraging sound financial management and administrative efficiency at all levels of Australian government.

3. **Staying competitive** by addressing the vertical fiscal imbalance between the Commonwealth and States, and reducing the volume and complexity of regulations imposed on businesses.

4. **Renewing economic infrastructure** by developing a National Infrastructure Plan between the Commonwealth and the States and Territories, and delivering on outstanding major projects.

5. **Preparing for climate change** by the Federal Government taking leadership of policy development, the States and Territories supporting a national carbon trading scheme, and constructing a trading scheme is revenue-neutral.

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1. EXECUTIVE SUMMARY

TCFL industries in Australia are facing serious challenges, with large declines in industry value-added, employment and exports, driven by competition from emerging economies.

The NSW Business Chamber does not seek ongoing or indefinite forms of industry support and protection for TCFL industries, and endorses the rate of tariff reductions scheduled under the TCF Post-2005 Assistance Package.

The NSW Business Chamber advocates a new innovation programme that helps Australian-based TCFL firms to capitalize on their existing competitive strengths and shift towards higher value-adding activities.

Specifically, the NSW Business Chamber makes the following recommendations:

- **Further reductions in TCFL tariff barriers should be accompanied by actions to redress the negative competitive effects of non-tariff barriers imposed by Australia's trading partners, including discriminatory procurement policies.**

- **The Federal Government should work with business leaders and other stakeholders to forge a long-term vision for the TCFL sector, which identifies the capabilities, resources and relationships that are needed to secure a sustainable competitive position.**

- **The Federal Government should implement a post-2010 Strategic Investment Programme (SIP) that is both more inclusive than previous SIPs, and more focused on enhancing the capacity of TCFL firms to create new niche global markets and compete effectively in established markets.**

- **Existing mechanisms to support R&D in TCFL industries should be made more accessible to small-and-medium sized firms, and include measures to facilitate technology transfer to TCFL from other industries.**

- **The focus of a new TCFL innovation programme should be on recognizing and strengthening the design, management and marketing skills of Australian-based TCFL businesses.**

- **The Federal Government should explore measures to protect the quality and design of Australian TCFL products, and extend global promotion of Australian TCFL businesses.**

- **Any proposed TCFL innovation initiatives should maximize opportunities for external collaboration, and be coordinated with existing innovation and industry policies at both Federal and State/Territory levels.**

2. INTRODUCTION

The NSW Business Chamber welcomes the Federal Government's Review of the Textile, Clothing and Footwear industries, and its commitment to maintain the innovation capacity and international competitiveness of these industries.

The NSW textile, clothing, footwear and leather (TCFL) industries generate over $3 billion *per annum* in sales and services income, about one-third of the Australian total.[1]

There are about 2,000 TCFL enterprises in NSW, which undertake significant production activities in the Sydney, Murray and Central Coast regions.[2]

However, as the Productivity Commission has reported, TCFL industries face serious challenges, with large declines in industry value-added, employment and exports. Job losses are inevitable and firms reliant on standardized products will not survive.[3]

Heightened international competition has compelled a shift from standardized, cost-based production to specialized production for niche markets. And competitive pressures will only intensify, as firms in emerging economies are increasing their technological capacity and ability to satisfy demanding customers.[4]

This long-term trend is evident in statistics on foreign direct investment (FDI). In 1989-91, emerging economies accounted for only 10% of inward flows of FDI to TCFL industries. By 2003-05, their share had jumped to 21%.[5]

In South, East and South-East Asia, TCFL industries recorded the highest growth rate (1625%) in crossborder mergers and acquisitions (M&As) for the period 2005-06. Mining and quarrying was the only industry that had a higher M&A growth rate in the region for the same period (1927%).[6]

The NSW Business Chamber does not seek ongoing or indefinite forms of industry support and protection for TCFL industries. Rather, the Chamber agrees with the Productivity Commission that 'the policy focus should be on facilitating and supporting the adjustment process'.[7]

The NSW Business Chamber endorses the rate of tariff reductions scheduled under the TCF Post-2005 Assistance Package, provided they are accompanied by an appropriate structural adjustment program. The transition to lower tariffs should take into account action by Australia's trading partners in reducing their TCFL trade barriers.

The NSW Business Chamber advocates a new innovation programme that enables TCFL industries to capitalize on their existing competitive strengths and shift towards higher value-adding activities. Central to this programme is the building of marketing and design skills and continued support for a high rate of technological transfer.

3. THE COMPETITIVE CHALLENGE FACING TCFL INDUSTRIES

Economic data on Australian-based TCFL industries highlight the competitive challenge for both business leaders and policymakers.

According to the Australian Bureau of Statistics (ABS), production for TCFL manufacturing fell by 35.2% over 2001-02 to 2005-06, which was the poorest growth rate in manufacturing for the period. TCFL production has been declining each year since 1998-99.[8] In line with this trend, operating profit before tax for the TCFL sector decreased 9.9% from 2003-04 to 2004-05.[9]

It is widely acknowledged that the declining rates of output and profits in Australia's TCFL industries mirrors the experience of other advanced economies, which face similar labour-cost disadvantages.[10]

In addition, Australia has kept pace with its major trading partners in reducing tariffs on TCFL imports, and resisted the temptation to erect new forms of protection.

Table 3.1 shows the latest data from the World Trade Organization (WTO) on most-favoured nation (MFN) applied duties levied on TCFL imports by Australia and its major trading partners. These are the normal non-discriminatory tariffs that are actually charged, as opposed to the bound rates, or legally binding commitments not to increase duties beyond an agreed level.

Table 3.1: Most-favoured nation applied duties levied on TCFL imports by Australia and its major trading partners

	Most-favoured nation applied duties 2006*		
Economy	**Textiles**	**Clothing**	**Footwear/leather**
Australia	**6.8**	**15.4**	**5.6**
China	**9.7**	**16.1**	**13.0**
European Communities	**6.6**	**11.5**	**4.2**
Japan	**5.5**	**9.2**	**15.0**
Republic of Korea	**9.2**	**12.6**	**7.9**
New Zealand	**3.0**	**16.2**	**4.8**
USA	**7.9**	**11.5**	**4.3**

Source: WTO: *World Tariff Profiles 2006*
*** Simple average of the *ad valorem* or *ad valorem* equivalent Harmonized System six-digit duty averages**

Table 3.1 reveals that Australia's MFN applied duties are consistent with those charged by other advanced economies, and that Australia imposes lower tariffs on TCFL imports than China and the Republic of Korea, whose firms enjoy a significant labour-cost advantage.

However, the data in Table 3.1 does not capture additional protectionist measures adopted since 2006 by some of Australia's trading partners. For example, from 1 May 2007, a 15% tariff has been charged by the US Government on certain TCFL products under the Byrd Amendment.[11] Nor does Table 3.1 incorporate the effects of the US Berry Amendment, under which the US Department of Defense must give preference in procurement to domestically produced TCFL products.

Moreover, TCFL members of the NSW Business Chamber have reported that the US-Australia Free Trade Agreement has in no way improved their access to US markets. In 2005, the US Defense Supply Centre, Philadelphia, allocated US$2.5 billion dollars' worth of footwear, clothing and textiles to the US military. Despite Australian companies' ability to develop and manufacture TCF products that are technically superior to their US counterparts, access to this massive market has been largely denied.

The US government's motivation in protecting their domestic TCF producers is based on the principle of guaranteeing that the US military has a 'warm industrial base' with reliable domestic suppliers. This is regarded as a critical national security requirement. This is in stark contrast to the procurement policies of the Australian Defence Force, where little consideration is given to Australian suppliers. For example, all of the Australian Defence Force's dress shoes are now made in Vietnam.[12]

Recommendation

Further reductions in TCFL tariff barriers should be accompanied by actions to redress the negative competitive effects of non-tariff barriers imposed by Australia's trading partners, including discriminatory procurement policies.

Commentators and policymakers often assume that all labour-intensive activities are destined to be outsourced to emerging economies, and that national competitive advantage hinges solely on creating and hosting high-tech industries.

Yet empirical analyses undertaken by economists for the Australian Business Foundation demonstrate that Australia's low and medium-tech sectors are no less knowledge-intensive or productive than its high-tech ones.

Prof. Alan Hughes and Vadim Grinevich examined the labour productivity growth contributions of 49 market sectors in Australia (excluding property and business services) between 1980 and 2004. They found that the three sectors of financial intermediation, wholesale and commissioned trade, and miscellaneous business services accounted for 96% of national labour productivity acceleration between 1980-92 and 1992-2004.[13]

Similarly, Prof. Keith Smith points out that that Australia's low and medium-tech sectors maintain high rates of productivity growth through continual innovation, including in market research, training and skill development, and the application of new technologies produced elsewhere.[14]

The ability of Australian-based businesses to compete successfully in low and medium-tech industries suggests that the decline of the TCFL sector need not be terminal. The NSW Business Chamber submits that the Federal Government should help TCFL industries to formulate a long-term competitive strategy and provide appropriate assistance to ensure its success.

The Europeans have already formulated a strategic vision for their textile and clothing sector. The European Apparel and Textile Organisation (Euratex) has advanced a vision for 2020 that consists of the following elements:

- assigning research priorities in the areas of ‘From Commodities towards Specialities’, ‘New Textile Applications’ and ‘Towards Customisation’;
- an innovation-friendly regulatory framework;
- an educational system that accommodates textile innovation;
- innovation-supporting standardization; and
- capacities for effective management of innovation and technological change.[15]

There are also precedents set by other Australian industries. In winemaking, entrepreneurial champions, together with an array of specialist national associations, drew on industry levies and government initiatives to formulate a coordinated, long-term vision (documented in ‘Strategy 2025’) that contained benchmarks, targets and a commitment to innovation and product quality. This vehicle enabled investors to make informed risk-management and business-development decisions.[16]

Similarly, in the case of mining, the Australasian Joint Ore Reserves Committee (JORC) – intended by industry professionals as a technical and professional code – was eventually transformed by mining associations and financial institutions into an enforceable standard for describing valuable mineral reserves and resources.[17]

<u>Recommendation</u>

The Federal Government should work with business leaders and other stakeholders to forge a long-term vision for the TCFL sector, which identifies the capabilities, resources and relationships that are needed to secure a sustainable competitive position.

4. MAXIMIZING THE INNOVATIVE POTENTIAL OF TCFL BUSINESSES

While Australia's TCFL sector lags behind other sectors in terms of growth and value-added, its capacity to generate new products and processes is close to the average for the total manufacturing sector, and compares favourably to the average for Australian business as a whole.

Table 2 below indicates that the proportion of TCFL businesses that introduced new or significantly improved goods or services was only slightly less than the proportion of total manufacturing businesses, and considerably more than the proportion of total Australian businesses.

Table 4.1: Innovation in goods or services in textiles, clothing, footwear and leather, compared with total manufacturing, 1991-2005

Proportion of Australian businesses that introduced new or significantly improved goods or services (%)			
Period	TCFL	Total manufacturing	All industries
1991-94	31.7	36.8	~
1994-97	32.8	31.9	~
2001-03	23.0	27.1	16.6
2004-05	26.3	26.9	19.4

Source: ABS Cat. 8158.0

Table 3 shows that the proportion of TCFL businesses that introduced new or significantly improved operational processes was again only slightly less than the proportion of total manufacturing businesses, and consistent with the proportion of total Australian businesses.

Table 4.2: Innovation in operational processes in textiles, clothing, footwear and leather, compared with total manufacturing, 1991-2005

Proportion of Australian businesses that introduced new or significantly improved operational processes (%)			
Period	TCFL	Total manufacturing	All industries
1991-94	28.0	30.5	~
1994-97	30.1	26.0	~
2001-03	20.7	29.7	22.9
2004-05	26.6	27.3	24.9

Source: ABS Cat. 8158.0

These data suggest that Australian-based TCFL industries have the potential to adapt to external pressures and create new markets, even if this potential is not currently being realized.
Some general lessons for Australia can be drawn from an instructive report published by the Organisation of Economic Co-operation and Development (OECD) in 2004, entitled *A New Map in Textiles and Clothing: Adjusting to Change.* According to the OECD, the key to competitive success in these industries lies in developing human capital that is able to produce high-quality and well-regarded products on demand.

The OECD notes that the successful exportation of textiles and clothing requires a quality that can only be provided by technological inputs imported from advanced economies. However, the OECD also points out that whenever major industries shift production to emerging economies, it is only a matter of time before inputs are produced there as well. And the labour intensity of textiles and clothing production reinforces the tendency to shift the entire manufacturing process to other locations.[18]

The OECD further observes that 'the R&D intensities of textiles and clothing industries is quite low throughout the OECD area'.[19] Based on an analysis of textiles and clothing industries in 16 advanced economies, the OECD concludes that 'there is no significant correlation between the increase in R&D and trade performance'.[20] This is because most technological innovations in textiles and clothing originate in other industries. Consequently, 'the technological competitiveness of producers of textiles and clothing largely depends on their ability to adopt new products and processes developed elsewhere'.[21]

Recommendation

Existing mechanisms to support R&D in TCFL industries should be made more accessible to small-and-medium sized firms, and include measures to facilitate technology transfer to TCFL from other industries.

At the same time, the OECD acknowledges that continual technological innovation is a necessary but insufficient condition for long-term competitiveness in textiles an clothing. Even if entire production lines become automated, they will be more suited to long production runs of standardized articles, rather than short production runs of specialized articles that must be responsive to transient fashions.[22] Therefore, as the OECD puts it, 'reputation increasingly becomes a key factor of competitiveness.'[23]

Recommendation

The Federal Government should implement a post-2010 Strategic Investment Programme (SIP) that is both more inclusive than previous SIPs, and more focused on enhancing the capacity of TCFL firms to create new niche global markets and compete effectively in established markets.

5. EXISTING COMPETITIVE ADVANTAGES AND LESSONS FROM THE EUROPEAN UNION

Australian-based TCFL businesses already enjoy a number of competitive advantages, including:

- easy access to world's best quality raw materials, for example wool and cotton;
- a high level of technological innovation in computer-aided design and manufacturing, marking and grading systems, and quick-response production systems;
- a strong base of creative talent in fashion and lifestyle product design;
- a cosmopolitan population that serves as both a market for advanced TCFL products and a source of creativity;[24]
- a seasonal difference that allows US and European buyers to order items with a longer lead time for production than is available in other established markets.

Nonetheless, if Australia is to retain a share in the international TCFL market, resident firms must constantly improve through more innovative designs, greater and more imaginative use of information and communication technologies, and maintaining a clear focus on generating products with high quality and/or fashion content (rather than attempting to sustain low-skilled, labour intensive activities).[25]

The experience of EU economies demonstrates that product differentiation through design is an especially important element of competitive advantage. Italian clothing and accessory makers have had to rethink what they do, and to promote aggressively the idea that something made in Italy cannot really be replicated anywhere else.[26] This is what the Australian TCFL sector needs: to be recognised for its distinctive quality and design.

The NSW Business Chamber takes an active role in promoting the design capabilities of Australians through its annual *NSW Business Chamber Fashion and Textile Award.* These awards are sponsored with the Faculty of Design of the University of Technology, Sydney, for final year students completing courses in business planning and fashion design.

Winners of the Award receive $3,000 in cash and in-kind support from NSW Business Chamber, including advice on how to establish and run a successful business and how to get their fashions labels into overseas stores.

Nonetheless, if the Australian TCFL sector is to establish a global reputation for distinctive quality and design, then new and significant investment in human capital is essential. Leading TCFL businesses stem from nations that take their TCFL industries seriously and devote resources to positioning their designers and managers as world leaders.

In contrast to Australia, Italy has many fashion design and technical training schools and universities. Bocconi University, which is based in Milan, offers a Masters in Fashion, Experience and Design Management. This exemplifies an awareness that the knowledge required for TCFL business extends to higher education, in particular the management of production of fashion and design.

Recommendation

The focus of a new TCFL innovation programme should be on recognizing and strengthening the design, management and marketing skills of Australian-based TCFL businesses.

The potential of Australian TCFL designs is reflected in the success of Sydney Fashion Week. Tim Harcourt, Chief Economist of Austrade, observes that this international event both launches the careers of new designers and consolidates the efforts of more established names. He also attests that Australian TCFL exporters are making inroads into emerging Asian markets, where Australia's proximity serves as a competitive advantage.[27]

One potential barrier to the generation of non-replicable Australian designs is Australia's intellectual property laws. NSW Business Chamber members have affirmed that the cost of registering a design is prohibitive, and that in any case Australia's IP laws are not strong enough to protect the original designs and hence discourage new entrants into high-value TCFL markets. That said, difficulties in enforcing IP rights in TCFL industries are not confined to Australia.

Italian TCFL companies are seeking to defend their standards of quality and fashion design by advocating that the tag 'Made in Italy' be given legal weight.[28] The Institut Français de la Mode (IFM) refers to this policy as 'a deterrent against remote sourcing which does not generate any European value added' and 'a real effort for clarification and coherence, but also in certain areas to rebuild adequate value chains, and to develop a quality content within certificates of origin.'[29]

The point of a 'Made in' standard is not to appeal to the nationalism of domestic consumers, but to recognise and promote the quality and design embedded in Australian high-value TCFL products.

Recommendation

The Federal Government should explore measures to protect the quality and design of Australian TCFL products, and extend global promotion of Australian TCFL businesses.

6. COORDINATING TCFL INNOVATION MEASURES WITH OVERALL INNOVATION POLICY

The Federal Government has appointed a panel to review Australia's innovation system and to achieve (among other things) the following:

- develop a set of national innovation priorities to complement the national research priorities, ensuring the objectives of research programs and other innovation initiatives are complementary;
- identify regulatory and other barriers to innovation and recommend ways to minimize these; and
- examine the scope for simplifying and reducing program duplication and ensuring that any support provided is well-targeted and easy to access.[30]

The NSW Business Chamber endorses the streamlining of innovation priorities and policies where they do not result in a net decrease in public support for business transformation.[31]

Moreover, as noted above, the TCFL sector already depends heavily on the adoption of technologies pioneered elsewhere, and its future competitiveness requires further investment in design, marketing and management skills that are similar to those practiced in other sectors.

Therefore, any innovation measures designed to assist TCFL industries should maximize opportunities for collaboration with other industries and creative organisations, and complement existing government policies at all levels of government.

Recommendation

Any proposed TCFL innovation initiatives should maximize opportunities for external collaboration, and be coordinated with existing innovation and industry policies at both Federal and State/Territory levels.

NOTES

[1] NSW Department of State and Regional Development, *Textile Clothing Footwear Leather.* <http://www.business.nsw.gov.au/industry/textile>
[2] ibid., p. 571.
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[5] United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development,* United Nations, New York and Geneva, p. 227. <http://www.unctad.org/en/docs/wir2007_en.pdf>
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[18] OECD, *A New World Map in Textiles and Clothing: Adjusting to Change,* Paris, 2004, pp. 142, 144, 146f.
[19] ibid., p. 150.
[20] ibid., p. 151.
[21] ibid., p. 152.
[22] ibid., p. 161.
[23] ibid., p. 162.

[24] NSW Department of State and Regional Development, *Textile Clothing Footwear Leather.* <http://www.business.nsw.gov.au/industry/textile>
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