COUNCIL OF TEXTILE & FASHION INDUSTRIES OF AUSTRALIA LIMITED

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Dr Sarah Bachelard
Committee Secretary
Senate Economics Legislation Committee
Room SG.64
Parliament House
Canberra ACT 2600

Dear Dr Bachelard,

The Council of Textile and Fashion Industries Limited (TFIA) is the peak employer industry body for the Australian Textile and Clothing sectors and thanks the Committee for the opportunity to put forward its views on the *Textile, Clothing And Footwear Strategic Investment Program Amendment (Post-2005 Scheme) Bill 2004* and the *Customs Tariff Amendment (Textile, Clothing And Footwear Post-2005 Arrangements) Bill 2004.*

The TFIA has represented the industry at all reviews of TCF assistance and played a significant role in the most recent review and subsequent decision made by the Government. Additionally the TFIA and its members have and continue to work closely with the Department of Industry, Tourism and Resources to develop the Post-2005 SIP package given its importance to the industry's future development and growth.

I have included with this letter a paper that addresses the broader issues the TFIA and its members have in respect to the legislation's current treatment by the Parliament and each of the references provided to the Committee. In addition, copies of various press releases made after the announcement of the package by the Government are also attached.

The TFIA believes it is in the industry's best interests to have this legislation passed without delay. The package provides an appropriate means for the industry to continue operating and re-structuring itself in the face of changing international conditions. The package is the result of a lengthy and detailed review of the industry and the assistance provided to it by the Productivity Commission where the issues of employment, economic growth and other aspects were discussed and considered at length.

While the final package agreed is not fully in line with our original preferences it has our strong support due to the need for the industry to have certainty regarding tariffs and assistance levels. A compromise was made in respect to both the funding amount and linkage between the tariff cut and assistance package as the industry felt it more necessary for there to be a package in place to achieve a certain and sure future adjustment path for the industry.

We reject the contention by some groups that industry was 'blackmailed' into this agreement noting that the arrangement for Post-2005 Assistance follows the precedent set by the current arrangement – namely a tariff cut and pause for five years accompanied by transitional assistance for those five years. This approach is working and more importantly from a certainty aspect is understood and familiar to the industry.

It is the impact of the delays in the legislation's passage that has caused the TFIA and the industry the most concern. The argument revolves largely around the tariff reductions included in the package, the first of which is more than five years away. Industry understands that there is little argument among Senators over the need for transitional assistance for the TCF sector.

We would ask that the Committee in the interests of providing certainty to the industry and given that the first tariff cut is not until 2010 – potentially two elections away – to recommend the legislation be passed. The industry notes and accepts that subsequent Federal Governments may wish to amend the legislation to modify the tariff cuts but seeks to have certainty now.

I look forward to the Committee's consideration of these bills. The TFIA would be more than happy to speak directly with the Committee should they wish. Please contact me for further information or to arrange any meetings.

Yours sincerely,

Ashley Van Krieken
Executive Officer

# 1. Broad Overview and Issues for the Industry

The current Strategic Investment Program was introduced to apply over the financial years 2000-01 to 2004-05 with two pre-program years – 1998-99 and 1999-00. The program is open to all entities undertaking eligible TCF manufacturing and/or design activities in Australia subject to a minimum spending threshold on eligible activities of $200,000 which can be accumulated across the life of the program. The scheme was also coupled with a continuation of the Expanded Overseas Assembly Provisions (EOAP). In conjunction with these programs tariff reductions on TCF products were paused from 2000 to 31 December 2004.

In our original submission to the Productivity Commission (PC) inquiry we noted that the introduction of the current SIP has led to increased exports, stabilised and expanded jobs, particularly in regional Australia and encouraged the rapid expansion of expenditure on capital works and research and development. The SIP program has also supported the introduction of niche products, particularly in the fashion industry. These statements still hold for the scheme in its fourth program year of operation and will continue to apply under the new scheme.

As an illustration of this consider the following comments (taken from the TFIA's initial submission to the Productivity Commission review):

> *"Our real growth areas can be tracked back to SIP. Without it, we would not be doing all of our research and development and be able to fast-track products. With SIP, you have to be a doer."* Mr Brian Rush, Managing Director, Australian Defence Apparel.[1]

> *"There are a wide range of innovative ideas which we are currently working on and with the assistance of SIP, we will continue to develop them into a commercially viable product. SIP has directly enabled Canning Vale to retain its sales position and ensure that our market share is poised for growth with Australian made, innovative product."* Mr Frank Prainito, Chief Executive Officer, Canning Vale Weaving Mills[2]

**Certainty and Surety for the industry's future Viability**

The legislation that has been referred to the Senate Economics Committee will enable the development of the necessary regulations and mechanisms to put the program into place to deliver the assistance program and tariff reductions. The TFIA is aware of several companies who due to their internal accounting arrangements will as of the 1st of January 2005 no longer be eligible under the current SIP scheme and if the legislation is deferred further could miss out on some of their entitlements under the new scheme.

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[1] ADA, which now exports around 20% of its sales to a range of countries is one of the largest manufacturers in Bendigo and also maintains an operation in Coburg

[2] The Perth based Canning Vale Weaving Mills supplies to icon brands including Sheridan, Martex and Country Road. Export sales are worth more than $10 million annually and the company supplies towel ranges for Bloomigdales and Macys in the United States.

As such their ability to make sound investment and production decisions is significantly hindered and thus the viability of their operations and the supply chain is also threatened. While there is concern with the possible job losses from the package the TFIA would contend that the continued delay in passing the legislation is just as likely to have adverse employment implications for the industry as illustrated in the following quote.

The Chief Executive Officer of Bruck Textiles, Mr Alan Williamson was recently quoted in the Wangaratta Chronicle on this issue.

> *"He said failure to pass the package had influenced the company's projected budget this year - contributing to some 22 voluntary redundancies - and would no doubt be an ongoing consideration."*

The PC in its final report noted that a step-down reduction in tariffs *"…would best meet the goal of enhancing overall community welfare while giving the sector time to adjust and minimising the risk of excessive disruption*" PC Final report pg. 111. The report contended that given the extended timeframes required by companies to recoup investment expenditure the stepped approach provides a fixed end point for companies to plan their investment and operational activities. While neither the Government nor the TFIA can force companies to adjust, the package represents the best and fairest means of assisting the industry to transition.

In the course of the review the argument was made that tariff reductions will result in the loss of jobs and industry in Australia. There is no doubt that under a system of reduced tariffs companies are required to be more competitive however this does not automatically translate into reduced employment or company closures as many groups would have people believe.

All industry sectors move in cycles and as a result so do employment levels. Observing employment data for the clothing sector shows that over the period from 1990-91 to 2002-03 the average change in employment was -1.6% despite their being several significant reductions in clothing tariffs over that time. Additionally even where there were high tariffs employment levels were still subject to cyclical fluctuations.

While tariffs can provide support to an industry, the TFIA recognises that tariffs alone can no longer support the Australian TCF sector. What is important is that assistance is in place to provide the necessary support for the industry to transition. It is clear that Australia has international obligations that are dictating the Government's broad policy regarding tariffs.

For instance, under APEC, Australian governments (both the ALP and Coalition) have agreed to free and open trade by 2010. While TCF products are a special case, Australia is still required to show that it is liberalising its tariffs – the current step down approach meets this need. For tariffs to remain where they are for a longer period could send incorrect signals to our APEC neighbours about our intentions in respect to this agreement.

In addition the numerous bi-lateral trade agreements being negotiated not only by Australia but nearly all other countries are slowly removing the importance of tariffs in the global marketplace. While the industry appreciates higher tariffs it also accepts that broader national objectives such as those above must be met. Indeed it could be seen that a resistance to lowering tariff levels over time might promote retaliation against Australian exports through decreased access to international markets.

Tariffs while holding significant value as a form of protection for an industry can, depending on their level, often be surpassed by other drivers of investment and production decisions including:

- Activities of competitors including pricing and product differentiation.
- Changes in demand for goods including:
  - The buying preferences of the major retail operations in countries;
  - Changes in upstream and downstream industries of the supply chain
  - Consumer preferences.
- Impacts of other Domestic policies such as environmental controls, taxation and those related to the labour force.

These types of factors are very often likely to drive change in companies as much, if not more than, reductions in tariffs. As such the TFIA believes the best option for the industry moving forward and the focus for Government is not relying on tariffs to provide industry support but rather ensuring that adequate assistance is in place to allow industry restructuring and re-positioning in order to take advantage of new markets and consolidate existing ones.

The industry has clearly identified that it must move to increasing its level of innovation and design intensity coupled with seeking improvements in its supply chain relationships for it to continue operating. These trends are already evident across TCF industries. They are leading to value creation in the Australian industry, increasingly building on skills in brand management, supply chain management and Intellectual Property creation.

In a changing global environment the success of a company is driven by more than just high tariff levels and its employment levels are likewise going to be subject to a multitude of factors. It has been noted on numerous occasions that high tariffs do not lead to sustained higher employment levels in an economy alone. It must be accepted, as it has been by industry that tariff protection cannot last forever.

The aim of transitional support under SIP is to help firms make significant efforts to improve their international competitiveness rather than just struggle on. Improved international competitiveness leads to increased sales, production and employment growth. The provision of higher rebate levels for Type 1 and 2 grants compared with the existing system are more likely to encourage additional spending and behavioral change at a company level, even though the actual amount of assistance provided to a company may be lower as a whole. A reduction in grants from five to two also produces several administrative efficiencies within the program.

In the same fashion, maximising the amount of funding available under the SIP component ensures that grants can be distributed to a broader range of companies. The inclusion of a dedicated small business program enhances this aim by providing support for those companies that do not meet the threshold.

A key issue driving the reference was the potential impact on employment from the proposed tariff reductions and assistance package. The argument was made during the PC review that more funding should be assigned to address labour adjustment issues than to help companies adjust. The TFIA disputes this contention arguing that continued industry growth coupled with training will promote job creation and re-skilling.

Many companies are re-structuring their operations to capitalise on their capabilities in innovative product and process design enabling them to produce world-class quality product at globally competitive prices. Very often their operations provide sufficient flexibility for low production runs of niche products. These types of changes, which the Post-2005 SIP is designed to promote, maintain and secure employment in the industry.

The current package provides for structural adjustment funding for employees where job losses occur as a result of industry re-structuring. This is a dedicated program under the package unlike in the previous scheme where it was contained in Type 4 and 5 grants. This represents an excellent means to capture large-scale employment issues, which can occur for a multitude of reasons including more often than not poor management of a company for a significant period of time rather than a tariff reduction.

The TFIA would not object to an increase in the amount of funding or programs provided for labour adjustment as long as it was additional to that already assigned to the package. The package is about improving the competitiveness of the Australian TCF industry through the encouragement of innovation, technological research and development practices and activities in companies to produce high value, very often niche, products saleable globally. Further, under the new program there is a strong possibility that modulation of grants will occur and as such the TFIA would like to ensure that this possibility is not increased due a transfer of funds away from the SIP grant amount.

The TFIA has been heavily involved in the development of the package that the two Bills cover. The package has gained the industry's support as noted by the TFIA President, Paul Cohen at its release in November

> *"There is no doubt that there will be a need for further reconfiguration to strengthen the overall industry as we go forward, and the Government's assistance measures provide support for this transition…..We expect that the combination of measures including the tariff pause…..will place us well to be internationally competitive".*

The TFIA has outlined its concerns and objections to the current delays in implementing this package. The Committee is asked to support the legislation and recommend that it be passed by the Senate as soon as possible.

## 2. Specific Terms of Reference for the Committee

**Does the Strategic Investment Program (SIP) Bill assist small and medium sized enterprises (SME's) to access Government assistance?**

The TFIA believes that the current program as envisaged by the Bill and in discussions held between industry and the Department of Industry, Tourism and Resources will meet the needs of SME's. The lack of access to the existing SIP by SME's who could not meet the threshold was identified in the PC review of Post 2005 Assistance for the TCF industry and by several industry submissions. The report recommended that a separate scheme be established to cover those small businesses that were not eligible for normal SIP assistance.

The Bill does this through the creation of a Small Business Package and allocates it a fixed guaranteed amount of funding per year for the life of the SIP scheme - $2.5 million per annum for ten years. This scheme is dedicated to small businesses and provides support for those companies that are unable to meet the SIP threshold addressing in some part the lack of accessibility for some SME's inherent under the current program.

Given the increasing role that SME's are taking in the industry this will enhance their traditional position as drivers of innovation, development and growth within the economy. Additional benefit is afforded to SME's through the provisions for supply chain developments. Many SME's provide critical inputs to the productive processes of larger firms. Assisting SME's to adapt new technologies and innovation will secure their place in the supply chain. By focusing on supply chain efficiencies and improvements the scheme will allow companies to benefit additionally from the SIP.

**Does the SIP Bill improve market access overseas?**

The TFIA believes that the SIP scheme will improve company's access to overseas markets given its ability to allow improved efficiencies for a company's operations and the ability for the program to assist in the development of innovation and branding of a product. Both these elements work to increase a company's competitiveness and allow companies to successfully differentiate their products in the global marketplace.

The Product Diversification Scheme encourages investment in Australia and production of goods by providing a relatively straight-forward means of delivering support to those companies facing the greatest adjustment. Given the competitive nature and structure of global textile and clothing markets this scheme allows companies to develop and produce products in Australia that have an advantage over other products in the marketplace. The credit earned under this scheme can then be used to import those products for which Australia is not cost competitive. In a similar fashion the Extended Overseas Assembly Provisions (EOAP) offer a similar benefit.

**The phase down of the SIP funding from 2009 threatens the future of the industry and employment**

The Bills being considered emerged as a result of an intensive review process undertaken by the Productivity Commission. A clear finding of the inquiry, that was supported by the TFIA, was that SIP funding was required for those industries / companies most at risk from tariff reductions. This risk will be due in part to the tariff reduction but also from the existing industry structure and supply chain the company operates in.

After 2009 the majority of tariffs will fall to 5% - the general tariff level currently for the majority of manufactured products - and only a small number of finished textiles and clothing products will still have tariffs above 5%. The industry agrees with the principle that after 2010 where a company faces a 5% tariff they should not require transitional assistance. By providing assistance only to those companies producing TCF products with tariffs higher than 5% the program allows more funding at higher levels for firms facing the largest adjustment pressures.

The TFIA strongly supported the proposed scheme and attached tariff reductions on the basis of the certainty that they would provide the industry when legislated. Such certainty allows companies to be fully aware of the future path for their respective industry sector and to make the correct investment and business operation decisions to ensure that they can operate in a lower tariff environment.

The TFIA cannot say that no companies will cease operations nor that some employment may be lost as both tariff and assistance levels reduce but disagrees that the phase down of assistance after 2009 alone will threaten the future of the industry. The scheme encourages companies to restructure through technological development and innovation/branding development to secure future markets both domestically and internationally with a clearly determined timeframe. As such it opens up a raft of opportunities for companies to radically change their operations and products to guarantee their future.

The Product Diversification Scheme and EOAP provide companies with an ability to improve their efficiencies and cost structures increasing their profit margin and future sustainability leading to maintenance of employment and investment.

Likewise where failures may occur the provision of the Structural Adjustment Fund exists to ensure that those employees re-trenched from closures or re-structuring will be provided with opportunities to re-train and re-skill.

**Provides adequate support for high value exports** and **Provides adequate support for production value added activity**

The EOAP will provide the means for Australian industry to add value to intermediate products, which are generally exported. High value added products come from the ability to use technology and innovation to enhance the value of inputs. These aspects are encouraged by the SIP scheme.

The TFIA believes the package will provide additional impetus to trends already emerging for companies to adapt flexible manufacturing processes delivering high value added products into niche markets both domestically and overseas.

**Provides adequate support for R&D activities** & **The reduction in grant types from 5 to 2 will decrease access for some TCF firms**

The new legislation takes the number of grant types from five in the existing system to two in the new system and both of these improve the focus on R&D activities under the program. The TFIA does not believe the decrease in grant types from five to two will limit the scheme's accessibility for TCF firms. The PC review noted that the current Type 3 (value added) grant introduced a degree of complexity and variability into the calculation of a firms entitlement and leads to considerable confusion among applicants. In respect to Type 4 and 5 grants the review noted that these are available at the Ministers discretion and could be better applied as a separate initiative under any new scheme.

The two types of grant available under the new scheme will in the TFIA’s opinion focus company attention on innovation and research and development. The Type 1 (Investment) grants will provide the necessary assistance for companies to upgrade their equipment and plant to incorporate new technologies and new products. These investments are often made as part of an R&D program, with the SIP providing a partial offset of the inherent R&D risk.

The changes made to branding and to enhancing the Type 2 (Innovation) grants in the new scheme likewise support R&D activities by providing companies with an opportunity to invest in market differentiation of the products in both international and domestic markets. For a new product or process emerging from R&D one of the critical issues highlighted by companies is the importance of being able to tell the market and customers what qualities, functions etc the product exhibits. For most TCF products Australian producers cannot compete on price and therefore need to be able to compete on product differentiation in global markets.

The inclusion of a specific small business package will further enhance the scheme and is likely to increase the number of companies eligible for funding. Likewise, the inherent efficiencies provided to the administration of the new scheme by reducing the number of grants – and hence removing what many identified as a source of confusion in the current scheme – will allow increased monitoring and review and hence much more targeted assistance.

**The cut in tariff will have an adverse effect on the industry, economy, generally, employment and sustainability of regional cities and towns**

The tariff reductions under the package are stepped over two five-year periods allowing companies definitive end points to target. This is preferable to a progressive tariff reduction over the ten-year period as it removes a degree of administrative burden and provides greater surety for the industry.

This reference has been addressed in the first section above. In addition other issues such as customer demand, international trade obligations and other Government domestic policies and activities (such as this reference and delay in passing the legislation) will have as much influence on the decisions of the industry and economy more generally than the tariff cut.

By legislating tariff reductions and transitional assistance the Government is providing enough time for companies to re-orientate their operations and structures to ensure that they remain competitive. The TFIA would agree that a tariff drop to 5% immediately on 1 January 2005 would produce an adverse effect on the industry and economy. However the approach taken under this program produces a sustainable means for the industry to adjust.

**Our trading partners are reducing tariffs at the same rate as Australia**

Of Australia's major trading partners in TCF products we have or are discussing with nearly all of them preferential trade arrangements. Under these arrangements both countries agree to reducing tariffs and other barriers according to a set timeframe. This is occurring in agreements with Thailand and the United States and would form part of any potential Free Trade Agreement negotiated between Australia and China.

While the TFIA does not support the negotiation of an FTA with China until there is a level playing field between the two countries it cannot, nor can the committee, ignore the fact that China has agreed in joining the WTO to remove these barriers and others. While it may not be as rapid as many would want it clearly shows that China – Australia's largest import source – is committed to opening its economy to competition.

**The combination of these two bills and US FTA will adversely impact on the future of the industry and on employment**

The TFIA has noted on numerous occasions that for the majority of TCF products the Australia-United States FTA largely maintains the status quo of trade between the two countries. The need to meet yarn and fibre forward rules of origin for Australian TCF exports to the United States restricts Australian exports to the United States while the 2% margin provided on Australian tariffs for US TCF products does not provide a significant additional benefit for US producers. The agreement does not prevent companies from trading outside of preferential tariff rates and it does allow a small number of TCF products to enter the US markets. Likewise, many textile products are produced as inputs to other final goods such as automobiles and furnishings and thus increased sales to the US from these goods is likely to pull through demand for Australian textiles.

Given this stance and combined with our view that the SIP package will assist the industry we cannot see how the contention that the combination of these two factors will disadvantage the industry. In many respects the improved assistance to develop innovative and new technological products may allow companies to compete in US markets even without a preferential duty rate.