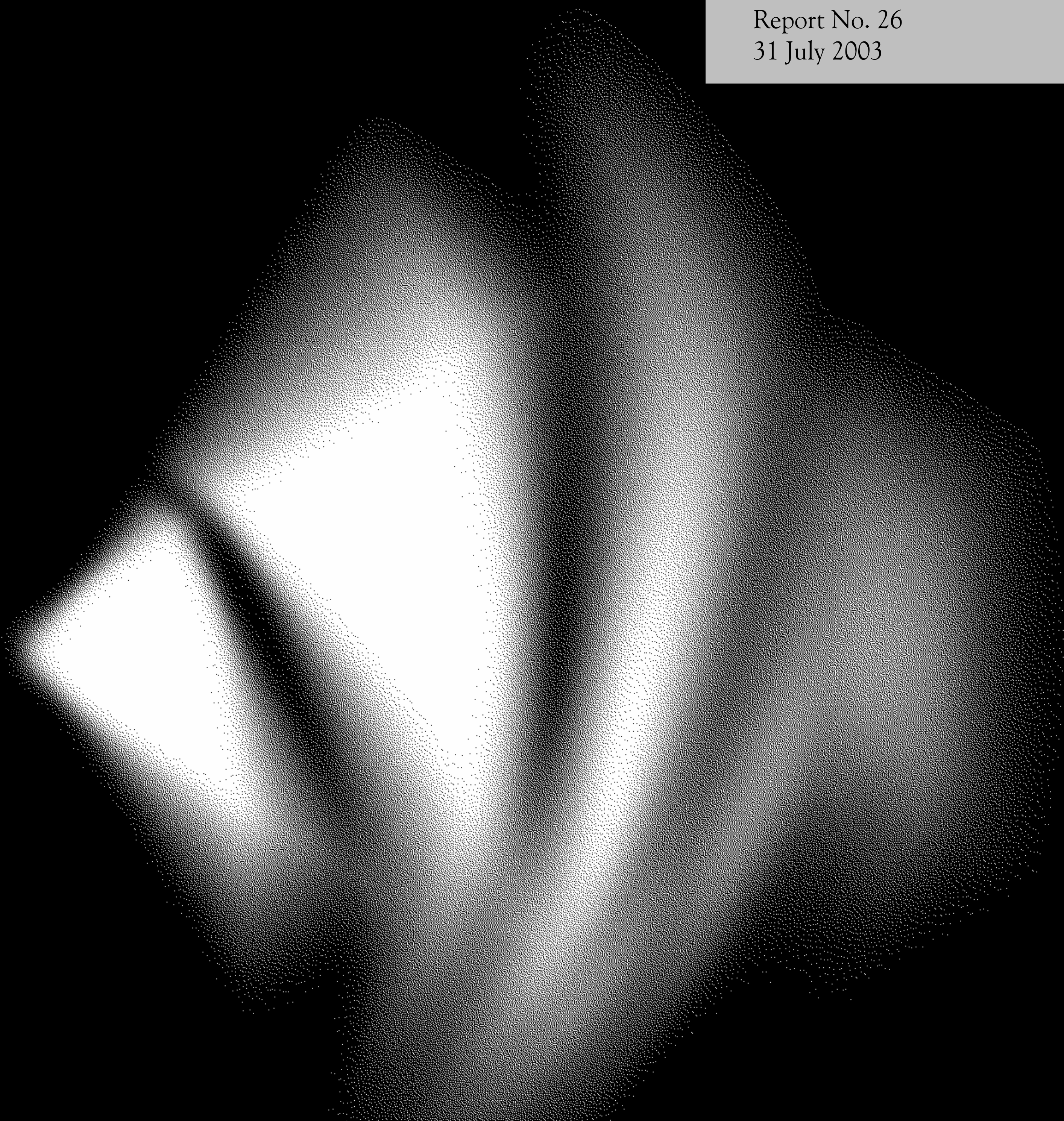
Review of TCF Assistance

Inquiry Report

Report No. 26
31 July 2003



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The Productivity Commission

The Productivity Commission, an independent Commonwealth agency, is the Government's principal review and advisory body on microeconomic policy and regulation. It conducts public inquiries and research into a broad range of economic and social issues affecting the welfare of Australians.

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PRODUCTIVITY COMMISSION

30 July 2003

The Honourable Peter Costello MP
Treasurer
Parliament House
Canberra ACT 2600

Dear Treasurer

In accordance with Section 11 of the *Productivity Commission Act 1998*, we have pleasure in submitting to you the Commission's final report on the *Review of TCF Assistance*.

Yours sincerely

David Robertson
Presiding Commissioner

Philip Weickhardt
Associate Commissioner

Terms of reference

I, PETER COSTELLO, Treasurer, pursuant to Parts 2 and 3 of the *Productivity Commission Act 1998*, refer post 2005 assistance arrangements for the textile, clothing and footwear industries to the Productivity Commission for inquiry and the provision of an information report. The Commission is to report its findings by 31 July 2003 and is to hold hearings for the purpose of the inquiry.

Background

<u>Current TCF Assistance Arrangements</u>

The Government's current assistance arrangements for the textile, clothing and footwear (TCF) industries comprise:

- the Textile, Clothing and Footwear (Strategic Investment Program) Scheme (SIP);
- a commitment to hold tariffs for TCF products at 2001 levels until 2005:
  - at that time tariffs are legislated to reduce from 25 percent to 17.5 percent for clothing & finished textiles; from 15 percent to 10 percent for cotton sheeting and fabrics, carpet, and footwear; and from 10 percent to 7.5 percent for sleeping bags, table linen and footwear parts.
- the Expanded Overseas Assembly Provisions Scheme, specific TCF policy by-laws and market access initiatives.

Other policies that have the potential to impact on the industries include:

- Australia's commitment to free and open trade and investment with APEC members by 2010, its WTO obligations in respect to subsidies and our broader trade liberalisation objectives;
- bilateral trade negotiations and possible Free Trade Agreements;
- the Government's industry and innovation support programs; and
- the market access policies and support programs of other economies towards their domestic TCF industries.

<u>Scope of industry and current performance</u>

TCF manufacturing covers all stages of production of textile, clothing, footwear and leather products, from processing of raw materials such as cotton, wool, leather and synthetics, to the production of final goods. Linkages extend upstream to the supply of natural fibres and downstream to service areas including design, pattern making, retailing and major consumers such as furniture manufacture, engineering and health.

Substantial budget support has been provided to the TCF industries over many years to assist firms in undertaking structural change. The TCF (SIP) Scheme currently provides funding of $678 million over 5 years to 2005 to encourage increased investment and innovation with the objective of achieving international competitiveness. The effective rate of assistance for the TCF sector declined from 85.5 percent in 1989/90 to 25.6 percent in 1999/2000. The effective rate for manufacturing as a whole declined from 16.3 percent to 5 percent over the same period.

The TCF industries directly employ 64,000 people, representing 7 percent of the manufacturing workforce and account for around 4 percent of manufacturing turnover. Exports excluding wool scouring, leather tanning and dressing currently stand at $1.1 billion, with New Zealand as the largest customer. Over the ten years to 1999/2000, turnover in the sector contracted by almost 16 percent and employment declined by 37 percent. Productivity as measured by turnover per employee increased by almost 48 percent.

The pressures for structural change have intensified in recent years due to a range of factors including import competition, technological change and shifts in household expenditure. Firms in the various TCF subsectors have responded by rationalising and modifying their operations through vertical integration, contracting out lower value added activities, and developing higher value and more sophisticated products and applications. Others have sought to maintain their competitiveness with more export activity, increased investment in capital equipment and technology and innovative design. There has also been an increased emphasis on services such as design, logistics and brand management and the establishment of new markets including exporting. Successful firms have emerged with strong brands and technologies. The factors driving this success have included strategic approaches to marketing and investment, managerial skills, innovation and supply chain integration.

Scope of Inquiry

Drawing on the Background, the Commission should consult with a cross section of the industries and other members of the community. In undertaking the inquiry, the Commission should bear in mind the Government’s desire to:

- encourage the sector to adjust into activities where it will be internationally competitive with lower levels of Government assistance; and
- improve the overall performance of the Australian economy.

The inquiry should:

Evaluate Current Arrangements

- Evaluate the effectiveness, efficiency and appropriateness of current assistance programs in meeting the Government's goal of achieving structural change and a more internationally competitive TCF sector by 2005, including a consideration of outcomes at the sub-sector level.

Assess long term viability and opportunities

- Identify and analyse major impediments to the long term viability of the TCF sector. These would include factors such as cost structures, and market and firm characteristics such as import competition, corporate structure, existence of critical mass, management and workforce skills, the purchasing strategies of major retailers, the ability of the sector to attract investment, and international trading arrangements including market access issues.
- Identify major opportunities for the sector and its strengths and weaknesses for securing these opportunities.
- Identify policy options, including tariff options, consistent with the Government's international obligations, such as those under WTO and APEC, which would encourage the sector to adjust to a more viable and sustainable competitive position.
- Analyse the short and long term implications of each policy option for the structure, performance and competitiveness of the sector, investment, employment, consumers, resource allocation, flow on effects for other industries, general growth prospects and appropriate role for government. Particular attention should be given to the impact of policy options on those regions where TCF accounts for a high level of regional industry concentration.
- Examine relevant workplace issues including the more effective use of flexible modes of employment, labour mobility in and out of the sector, especially in regional Australia, and the scope for innovative workplace reform including policy options to improve the competitiveness of the sector.
- Report on the likely impact on the TCF industries of international trade developments, including, but not limited to, the Doha round of trade negotiations and proposed Free Trade Agreements.

Consideration by the Government

The Government will consider the options of the Inquiry and will announce its response as soon as possible after receiving the Inquiry report.

PETER COSTELLO

[Received 19 November 2002]

Contents

Abbreviations

AALI	Australian Association of Leather Industries
ABL	Australian Business Ltd
ABS	Australian Bureau of Statistics
ACCI	Australian Chamber of Commerce and Industry
Ai G	Australia Industry Group
CIE	Centre for International Economics
CoPS	Centre of Policy Studies
DITR	Department of Industry, Tourism and Resources (Commonwealth)
EGS	Excluded Goods Schedule (of the TCS)
EOAP	Expanded Overseas Assembly Provisions Scheme
FMAA	Footwear Manufacturers’ Association of Australia
FTA	Free trade agreement
IAC	Industries Assistance Commission
IC	Industry Commission
NFF	National Farmers Federation
NIEIR	National Institute of Economic and Industry Research
NTBs	Non-tariff barriers
PC	Productivity Commission
SIP	Textile, Clothing and Footwear Strategic Investment Program
SMEs	small and medium enterprises
SUTG	Standard Universal Textiles Group
TCF	Textiles, clothing and footwear (generally used to include leather)
TCFL	Textiles, clothing, footwear and leather
TCFUA	Textile, Clothing and Footwear Union of Australia

TCS	Tariff Concession System
TFIA	Council of Textile & Fashion Industries of Australia
TTNA	Technical Textiles and Nonwoven Association
VFF	Victorian Farmers Federation
WTO	World Trade Organization

Explanations

Data	Data used in this report are drawn from a number of sources including: ABS Manufacturing Survey; ABS Labour Force Survey; ABS Population Census; industry reports; submissions; and information provided by participants in informal discussions. Readers need to bear in mind the often quite substantial differences between these sources. For example, ABS Manufacturing Survey information is restricted to factory-based employment whereas ABS Labour Force Survey data includes outworkers, conceptually at least.
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OVERVIEW

Key points

- Major structural change has occurred in the Australian textile, clothing, footwear and leather (TCF) industries, mainly in response to global competitive pressures affecting producers in all developed countries. More adjustment and job losses are inevitable, regardless of future assistance arrangements.
- Even so, some Australian TCF producers are internationally competitive. Others have the capacity to become so, particularly if impediments and weaknesses that reduce viability can be addressed. Improving workplace outcomes is a priority.
- But large labour cost disadvantages mean that many firms producing standardised clothing and footwear will not survive. This in turn poses threats to some of their suppliers. Workers displaced by change in the sector will need help.
- The current tariff pause and transitional budgetary support have helped some firms to improve their international competitiveness and long term viability. However, this special assistance treatment is costly for others in the community and cannot continue indefinitely.
- Further reductions in tariffs after 2005 would reduce the prices of TCF products for consumers, reinforce incentives for improved performance in the sector and signal Australia's continuing commitment to the APEC trade liberalisation process.
- The Commission's preferred tariff option is to maintain all TCF tariffs at the new legislated 2005 levels until 2010, then reduce most of them to 5 per cent. However, tariffs on apparel and certain finished textiles, which are significantly higher than those on other TCF products, would not be reduced to 5 per cent until 2015.
- To facilitate adjustment to these tariff reductions, the Commission proposes that transitional budgetary support be extended for a further eight years from 2005, but with funding levels reducing over time. Such support should be delivered using a modified version of the current Strategic Investment Program.
- Given the inevitability of more firm closures, the characteristics of the sector's workforce and the importance of TCF activity in some regions, special labour adjustment support is warranted during the tariff transition period. The Commission proposes that such support should be provided through an augmentation to Job Network services when large scale, or regionally significant, retrenchments have occurred or been announced.
- Voluntary approaches based on cooperation between the parties are likely to achieve better compliance with pay and condition requirements for outworkers than would more regulation, or heavy handed attempts to enforce existing regulation.
- Continuing microeconomic reform and government efforts to improve access to overseas markets would help TCF firms to become more internationally competitive.
- But there is little that can or should be done to stop further adjustment out of labour intensive, standardised TCF production in Australia. Rather, the policy focus should be on facilitating and supporting the adjustment process.

Overview

What is the inquiry about?

Major structural change is occurring in the textiles, clothing, footwear and leather (TCF) industries in virtually all developed countries. It is being driven by intense competition from suppliers in developing countries, changes in consumer tastes and technological advances.

The Australian TCF sector (see box 1) has not been immune to these pressures. Sectoral output and employment are declining as production is rationalised; the product mix and supply chains are changing; and exports as well as imports have increased.

Reductions in protection over the past 15 years have added to the pressures confronting Australia's TCF producers. The main purpose of this inquiry is to provide advice to the Government on options for assistance after 2005, at which time TCF tariffs will be reduced further and transitional budgetary support for the sector is due to end.

What are the government's objectives for the TCF sector?

The terms of reference specify that the Government wants to encourage the sector to adjust into activities where it can become internationally competitive with lower assistance, and to improve the overall performance of the Australian economy. This latter objective implies that future support for TCF producers must not be detrimental to Australia's long term economic interests.

Some TCF activities can prosper

The common perception that the entire Australian TCF sector has little future is wrong. Some firms in the sector are already internationally competitive or capable of becoming so. Others, however, are unlikely to survive even if the current high levels of government support were maintained.

Box 1 A snapshot of the Australian TCF sector and market

- TCF manufacturing in Australia covers a diverse range of activities, including: early stage processing of leather and natural fibres; the production of textiles; the transformation of leather, yarns and textiles into clothing and footwear, carpets and other fabric products for the home and office; and ‘technical’ textiles such as shade cloth, medical and sanitary products, filtration products and insulation materials.
- In 2000-01, Australia’s 5000 TCF firms generated turnover of $9 billion and provided factory-based employment for at least 58 000 people (though employment levels have since declined). Clothing producers also rely heavily on outworkers to assemble garments. In the absence of official data, the Commission estimates that there could be the equivalent of 25 000 full time employees engaged in outwork.
- This makes TCF one of Australia’s larger manufacturing sectors — specifically, it accounts for 4 per cent of manufacturing value added and 6 per cent (excluding outworkers) of manufacturing employment, and 0.4 per cent of value added and 0.6 per cent of employment in the economy as a whole.
- TCF production is more significant for some States and regions:
  - It accounts for 6 per cent of value added and 9 per cent of employment in Victoria’s manufacturing sector.
  - While production is mainly based in the capital cities — especially Melbourne and Sydney — there is significant TCF activity in regional centres such as Geelong, Bendigo, Wangaratta, Albury-Wodonga and Devonport.
- The sector includes many small and medium sized privately-owned firms, particularly in the clothing industry. Enterprises employing 20 or fewer people account for a quarter of sector-wide production and a third of the jobs. (Also, in the official industry statistics, many small businesses which undertake some TCF manufacturing are not classified in the sector.)
- In recent years, various global and domestic pressures have led to major changes in the sector:
  - Rationalisation, including many firm closures, has reduced output by 25 per cent and employment by 35 per cent since the early 1990s.
  - Imports, particularly from China, have increased rapidly and now account for over 50 per cent of the domestic TCF market. Australian TCF exports also grew rapidly during the 1990s, albeit from a low base. However, this growth has recently stalled.
  - The mix of domestic TCF production has changed, with more emphasis on high value, capital intensive and niche products, and less on labour intensive, standardised products.
  - The boundaries between manufacturing, distribution and retailing have become blurred. Local TCF suppliers now source more of their products offshore and provide ancillary services such as inventory management for retailers and corporate apparel services. Also, retailers have become major importers and distributors of TCF products.

There are diverse opportunities

Across the spectrum of TCF activities, there are successful firms which are exploiting competitive advantages to develop new products and secure new markets. Many opportunities exist, including where:

- rapid turnaround for short-run orders is required (eg 'quick response' fabric and garment production for the domestic market);
- a value adding service can be combined with 'just-in-time' production (eg corporate apparel and inventory management for retailers);
- proximity to the customer provides logistical benefits (eg the production of complex designer clothing);
- differentiated design and branding provide marketing advantages — even if the products are manufactured offshore;
- advanced scientific and engineering skills, combined with sophisticated machinery, are required to provide innovative, specialised products (eg various non-woven technical textile applications);
- low volume niche supply is unattractive to large overseas producers set up for long output runs; and
- product and market development is facilitated by international linkages that provide advantageous access to inputs, the latest technologies and market information.

Realisation of these opportunities will be assisted by emerging strengths in parts of the sector. These include increased flexibility, responsiveness and innovative capacities, a stronger focus on brand development and customer service, and growing commitment to performance improvement and market development.

Some weaknesses can be addressed

Further rationalisation would enhance viability in parts of the sector

Extensive structural change in the TCF sector in recent years has helped many firms to operate in increasingly competitive markets. Among other things, it has led to:

- more emphasis on high value, capital intensive and niche products, and less on labour intensive, standardised products; and
- greater plant throughput in parts of the sector resulting from rationalisation of production capacity and increased export activity.

Nonetheless, production volumes in most capital intensive areas of the Australian TCF sector remain low by world standards. In some cases, the legacies of previously very high protection for the sector — fragmented production, inefficient location of facilities and separation of the supply chain — continue to impose sizeable cost penalties. Further rationalisation and consolidation of capacity in these parts of the sector therefore offer opportunities for significant competitive gains.

As would improved workplace relations

More flexible and productive workplace arrangements and industrial stability have helped many TCF firms to improve their international competitiveness.

However, improvement is still possible in many parts of the sector:

- Restrictive shift patterns, and constraints on the use of casual employees and contract labour to cater for peaks in demand, typify inflexibilities that detract from performance in some workplaces.
- Wage increases and productivity gains are seldom linked.
- A focus in workplace negotiations on redundancy and employee entitlement issues is deflecting attention from opportunities to improve productivity and efficiency, and thereby to enhance job security in the sector.

Also, recent industrial disputes in some carpet plants in Victoria have been costly.

Greater cooperation and more effective communication between those involved in workplace negotiations would help to address such constraints on firms' performance. Indeed, the competitive pressures confronting the sector leave no place for adversarial workplace relations.

Improving the skills of some of those managing workplace relations, or negotiating on behalf of employees, would assist the parties to take full advantage of Australia's now more flexible arrangements for setting wages and conditions. And, finding a way acceptable to all of the parties to provide greater security for employee entitlements would help to engender a more productive workplace climate, as well as removing a trigger for industrial disputation.

But some firms are unlikely to survive

While the outlook for some firms and parts of the sector is positive, particularly if weaknesses can be addressed, in other areas, prospects are poor.

Clothing and footwear production remains labour intensive, with limited scope for more automation. High unit labour costs in Australia mean that local TCF firms — like those in other developed countries — have a serious competitive disadvantage in producing standardised clothing and footwear. In the past, higher productivity has partially offset this disadvantage. However, there is now little if any productivity difference between Australian producers and efficient suppliers in China, the main source of Australia's clothing imports. Productivity in other developing countries is also improving.

As a result, the profitability of firms still producing standardised TCF commodities is generally poor. Most in the sector accept that such production will continue to decline, regardless of the assistance regime. This in turn will put pressure on upstream yarn, textile and leather firms supplying these vulnerable segments.

However, seeking to offset these competitive disadvantages through high tariffs would be neither effective nor in Australia's interests. As many participants in the inquiry acknowledged, the future of an internationally competitive Australian TCF sector lies elsewhere — mainly in the manufacture of differentiated, high value, innovative products where labour costs are not the primary driver of market success, and in the provision of bundled products and services (such as corporate apparel).

Where current activity is unlikely to be viable in the medium to long term, the policy imperative is to facilitate adjustment into more sustainable activities and to reduce the risk of disruption when firms exit the sector. This has implications for the pace of future assistance reductions, particularly as many TCF employees may have limited alternative job opportunities and the sector is still important in some regions (see below).

The current assistance arrangements have shortcomings

The current TCF assistance package (see box 2) provides for:

- a pause in tariffs at 2000 levels until 2005, when further reductions will occur; and
- nearly $700 million in transitional budgetary support over the period 2000-01 to 2004-05 through the TCF Strategic Investment Program (SIP).

The package is intended to provide 'a period of consolidation' after previous tariff reductions and to encourage investment and innovation that will help the sector to adjust to a 'freer trade environment'.

Box 2 **The current TCF assistance package**

Under the package, which commenced in 2000, tariffs are maintained at 2000 levels until 1 January 2005, when they will be reduced as follows:

- 25 per cent to 17.5 per cent for apparel and certain finished textiles;
- 15 per cent to 10 per cent for cotton sheeting and woven fabrics, carpets and footwear; and
- 10 per cent to 5 per cent for sleeping bags, table linen, tea towels and footwear parts.

Tariffs on items currently at 5 per cent (for example, textile yarns and finished leather) will not change.

The other main element of the package is the Strategic Investment Program. Its objective is to improve the competitiveness of TCF firms by encouraging investment and innovation. The program, which finishes on 30 June 2005, makes available nearly $700 million over the five-year period 2000-01 to 2004-05 — though current indications are that some of this money may not be spent.

SIP funding is available to all entities undertaking TCF manufacturing and/or design activities in Australia, subject to them meeting a minimum expenditure threshold. Grants are payable for:

- investment in new capital equipment (up to 20 per cent of eligible expenditure);
- research and innovation (up to 45 per cent of eligible expenditure);
- value added (where firms have received grants for investment or innovation); and
- certain restructuring costs incurred by firms operating in 'TCF dependent communities' (up to 20 per cent of the cost of state-of-the-art, second hand plant and equipment and ancillary expenditures).

To reduce the risk of complaints to the World Trade Organization, annual SIP funding to individual firms is capped at 5 per cent of their sales in the previous year.

Only 5 per cent of TCF firms have so far received SIP support. But those firms account for around three-quarters of value added and two-thirds of employment in the sector.

Other elements of the package include: Overseas Assembly Provisions to encourage the use of Australian fabrics and leather by clothing and footwear producers in low wage developing countries; and policy by-laws that provide duty free entry for selected yarn and fabric inputs. TCF firms also have access to a range of generally available support measures such as R&D grants and the Export Market Development Grants Scheme. Also, some State Governments provide specific support to the sector.

However, these forms of assistance are minor in comparison to tariff protection and the SIP. Moreover, in terms of the total quantum of assistance provided, tariff protection is worth several times more to the sector than the SIP.

The objectives of the current package are appropriate

Well-designed tariff reductions and transitional assistance can encourage the development of internationally competitive economic activity able to provide sustainable jobs, without imposing excessive costs on consumers and the wider community. They can also reduce the incidence of disruptive adjustment out of non-viable activities. The objectives of the current TCF assistance package — to facilitate further tariff reductions in 2005 with transitional budgetary support — are therefore broadly appropriate.

But aspects of the package detract from its effectiveness

Many firms reported that SIP funding, in combination with the tariff pause, is supporting spending initiatives that will improve their international competitiveness.

Such improvements in competitiveness are not yet apparent in overall sectoral outcomes. Import shares continue to increase, export growth encouraged by the previous assistance regime has stalled, and sectoral value added is still contracting. Also, there has been no discernible increase in sector-wide investment.

Of course, such aggregate data, must be interpreted with caution. For example, the boost to sectoral performance from the activities of firms which are taking advantage of the current arrangements to re-position themselves, or to build on existing competitive strengths, will be offset by firm exits and reduced activity by enterprises with limited prospects.

Nonetheless, aspects of the package are likely to detract from its capacity to induce new spending that will improve firms' international competitiveness. In particular, under the SIP, which is intended to be a key facilitator of change (even though, in quantitative terms, it provides much less assistance than tariffs):

- Firms do not have to increase their levels of investment and innovation to receive SIP support. A portion of total support may therefore be underwriting spending that would have occurred anyway.
- Claims by firms for support are assessed after the spending has taken place. Though several definitional issues have been clarified, uncertainties about the outcomes of claims at the time spending decisions are made, may discourage or delay some worthwhile initiatives.

Certain eligibility restrictions are likely to limit further the SIP's effectiveness:

- It focuses on spending on new plant and equipment, R&D and product development. While this emphasis may be appropriate for some firms, others may be better able to enhance international competitiveness by investing in such things as state-of-the-art second hand equipment, brand support and market development.

- Specific support for rationalisation and consolidation of existing TCF activity is limited to regional areas, with little funding provided so far. Yet rationalisation of existing capacity — in metropolitan as well as regional areas — may be just as important in improving the sector's international competitiveness as spending on new equipment, R&D or innovation.
- The minimum spending threshold (in place partly to contain administrative costs) means that transitional budgetary support is not available to many small TCF firms. Arguably, such support could have most impact on international competitiveness in this part of the sector, given the difficulties that small firms often face in accessing finance for investment and R&D.

Also, the complexity of the SIP means that firms face substantial compliance costs. This dilutes the value of funding received and may discourage some firms from applying for support.

Designing transitional support to induce new spending to improve international competitiveness is not easy, especially in a sector as diverse as TCF. Nonetheless, it is evident that improvements can be made to the current arrangements.

Moreover, in terms of encouraging necessary change in the sector, the tariff pause may be a two-edged sword. On the one hand, it provides breathing space for those firms seeking to invest to improve their international competitiveness and may be facilitating a more orderly exit of firms with limited prospects. But on the other, it may be reducing the pressure on some firms to restructure their activities. Achieving an appropriate balance in this regard is therefore a key issue for the post 2005 assistance regime.

The package is costly for others in the community

Current support for TCF firms and their employees comes at a considerable cost to consumers and industries that use TCF products. (The latter includes various TCF industries that must pay tariff-inflated prices for inputs sourced from other parts of the sector):

- If the prices of TCF products — both locally produced and imported — increase to the full extent of the tariff, the cost to consumers and user industries would currently be about $1 billion a year, or about $150 annually for each Australian household.
- Even after the legislated tariff reductions in 2005, the impost would still be about $750 million a year.

In reality, some of these costs will be manifest through reductions in the quality of the products available at established market price points, rather than through observably higher prices. Also, competitive pressures may see importers or retailers absorb *some* of the impost.

However, these observations do not alter the fact that tariffs on TCF products are a sizeable tax on basic items of household expenditure. Indeed, the tariff revenue collected on TCF imports costs consumers an amount equivalent to around 50 per cent of the GST raised on TCF products. And this ignores the price raising effect of tariffs on locally manufactured items. In addition, the cost to taxpayers of the SIP, though small compared with the consumer cost of tariffs, will still be $140 million a year over the life of the program.

An alternative way of looking at the costs imposed on the community is that tariffs and the SIP together provide support to the sector worth around $13 000 a year for each TCF worker in Australia — including the estimated 25 000 full time equivalent employees engaged in outwork. This subsidy is equivalent to about 35 per cent of average earnings across the sector. And, as a percentage of value added, assistance to TCF production is five times the average for manufacturing as a whole.

Special support for the sector should not continue indefinitely

The preceding discussion suggests that, while the objectives of the current assistance package are sound, changes are warranted to improve the effectiveness of the support provided and to reduce the costs imposed on the rest of the community.

Many (though not all) in the TCF sector accept that the tariff cuts already legislated for 2005 should proceed. But most sought an extended tariff pause after 2005 — with any future reductions linked to 'matching' declines in barriers in other countries — as well as continuing budgetary support at existing or higher levels.

A key plank in the sector's arguments for special assistance treatment was the claim that TCF production makes a unique contribution to the economy in terms of employment, technology development, innovation and design.

However, in the Commission's view, the sector's economic contribution, while significant, does not justify *indefinite* special assistance:

- All industries generate wealth and provide employment, often in regional areas. Many export and contribute to technology development, frequently to a greater extent than the TCF sector.
- Australia should aspire to have industries that are both internationally competitive and which offer well-paid jobs to skilled employees. As firms and

unions alike acknowledge, TCF production which can only survive with high assistance and low wages, is not compatible with this goal.

- By increasing costs, assistance for TCF production reduces the contribution that other industries can make to Australia's economic performance.

Only if the TCF sector provided benefits to other activities for which it received no reward ('spillovers'), and which would not be supported by general industry programs, might there be a case for maintaining special assistance treatment. No evidence was forthcoming to suggest this is the case to any significant extent.

Similarly, the arguments for making reductions in Australia's TCF tariffs conditional on matching cuts in other countries do not stand close scrutiny:

- The concept of 'fairness' underpinning these arguments has other dimensions. For example, many would regard it as unfair that Australia's families pay higher prices for their clothing and footwear to protect domestic TCF producers.
- The scope for Australia to use its TCF tariffs as bargaining coin in international trade negotiations is likely to be very limited. Australia accounts for less than one per cent of global demand for TCF products, and imports already have a high share of the domestic market.
- While better access to overseas markets would benefit Australian TCF firms that are already internationally competitive, it is unlikely to be pivotal to the viability of most firms still moving to that goal. Prospects for these firms will be mainly determined by their capacity to sustain or expand their businesses in the local market in the face of intensifying competition from imports.

Importantly, most of the gains for a country from trade reform come not from the opportunity to increase exports, but from the improvements in efficiency that ensue from greater import competition in the domestic market (see below). This means that, contrary to commonly held views, Australia will benefit from reducing its industry protection even if others do not follow suit.

Further assistance reductions would be beneficial

Much of the debate in this inquiry about the impacts of further reductions in assistance for the TCF sector has focused on the results of the quantitative modelling studies. All of these studies indicate that assistance reductions would, at best, provide only small economy-wide benefits. Those advocating an indefinite continuation of special treatment for the sector have argued that these benefits are not sufficient to justify the costs that reductions in assistance would impose on particular communities or regions.

However, such emphasis on, and use of, the modelling results is inappropriate:

- The models are designed to assess the effects of resource movements between sectors that would ensue from reducing TCF assistance. It is to be expected that these projected resource allocation effects, though beneficial, will be small in an economy-wide sense. The TCF sector accounts for much less than one per cent of economy-wide output and employment, and the extent of its special assistance treatment is less than in the past.
- While the resource allocation benefits are relevant to post 2005 policy settings, so too are other effects that are not embraced by the modelling. Indeed, with the resource allocation benefits now small, the 'dynamic' benefits of assistance reductions and adjustment costs (see below) dominate the future policy calculus.
- It is also to be expected that the effects of reductions in assistance on those regions where TCF production is concentrated will be *proportionately* greater (though absolutely smaller) than the economy-wide effects. The possibility of sizeable contractions in activity in specific regions is relevant to the pace of reform. But provided that firms and regions are given reasonable time to adjust, such contractions in activity are not a reason to forgo reform that would benefit the community as a whole.

The incentives for performance improvement would be reinforced

Reductions in assistance can play a catalytic role in encouraging firms to become more productive and outward oriented. Undoubtedly, adjusting to greater international competition is difficult, requiring firms and their employees to make significant changes. But the experience in a range of Australian industries that have been through this process indicates that the benefits can be substantial. Forced to deal with the removal of their protective cushion, many firms have identified opportunities — previously considered unlikely or impossible — where they can compete with the best in the world.

Australia's strong and sustained growth performance of recent years has accompanied an extensive program of microeconomic reform, including the dismantling of most trade barriers. The much greater responsiveness, innovativeness and flexibility now evident in many Australian firms provide a springboard for sustaining strong output and employment growth in the future. It also increases the resilience of the economy to external shocks.

There is nothing to suggest that these effects of assistance reform are less pronounced in the TCF sector. Hence, assistance reductions after 2005 would reinforce the competitive pressures on TCF firms to improve their productivity, quality and delivery performance, to innovate, and to look for new markets.

While there are limits on the capacity of firms to improve performance, evidence to this inquiry indicates that, in many parts of the sector, substantial gains can still be made. The scope for further rationalisation of excess and inefficient capacity, and for more productive workplace relationships, are previously noted examples. In addition, considerable managerial effort in parts of the TCF sector continues to be devoted to preserving high assistance and looking for ways to garner government support. If this energy and creativity were instead applied to improving international competitiveness, the sector and Australia would ultimately be better off.

A commitment from the Government to remove progressively and unconditionally the sector's special assistance treatment after 2005 would give a clear signal about the need for such a change of focus. It would also send a message to firms in other industries not to waste effort seeking protection from competitive pressures. Conversely, postponing the removal of special treatment, or making it subject to another review, would distract TCF firms from confronting the reality that, in future, they must survive and prosper on their own merits, not on the basis of costly support from the rest of the community.

Consumers and user industries would benefit

Reductions in TCF tariffs after 2005 would undoubtedly benefit consumers and user industries. For many years, these groups have borne the brunt of supporting internationally uncompetitive TCF production. An indefinite tariff pause after 2005 would see this burden continue for many years to come.

Claims that the cost savings from tariff reductions would not be passed on to consumers but would simply boost the profits of importers and retailers, ignore market realities:

- The global TCF industry is brutally competitive, with new production centres and surplus capacity putting intense pressure on wholesale prices. In these circumstances, attempts by importers to retain the benefits of lower tariffs would be futile. Distributors and retailers would simply obtain those items more cheaply elsewhere.
- The Commission has seen no evidence that Australian retailers of TCF products are making excessive profits. Indeed, the real price of TCF products has been falling over time, notwithstanding (until recently) the depreciation of the Australian dollar.

This does not mean that price reductions or quality improvements at established market price points will immediately follow tariff reductions. But over time, the competitive nature of importing, wholesaling and retailing will ensure that benefits flow through to consumers. Several TCF firms acknowledged that, in contrast to a decade ago when tariffs were much higher, Australian consumers can now purchase some clothing and footwear as, or more cheaply, than their counterparts in parts of Asia, Europe and the USA. Reductions in tariffs after 2005 would provide additional price benefits to consumers.

Trade policy interests would be facilitated

Australia has international commitments and broader trade policy interests that impinge on post 2005 TCF assistance. Australia was active in the formation of APEC and is a signatory to the Bogor Agreement to pursue free and open trade and investment in the region, by 2010 for developed countries and by 2020 for developing countries. It is also an active player in WTO negotiations.

The gains for Australia from global trade liberalisation will be many times greater than the effects of changes to its TCF assistance levels. Thus Australia's national interests will be served by assistance policies for the TCF sector that enhance, or at least do not compromise, the prospects of broadly-based liberalisation. An indefinite tariff pause, or making assistance reductions conditional on actions by other countries, could send the wrong signal, particularly to APEC.

The way ahead

The current assistance regime was designed to be transitional and to encourage adjustment into TCF activities that can become viable with levels of support similar to those available to other Australian industries. To put tariff reductions on hold after 2005 — as proposed by many firms, trade unions and some State Governments — would be a counterproductive reversal of an approach that has started to reshape and strengthen Australia's TCF sector and which has reduced the costs of assistance for others in the community.

Thus, just as when the current arrangements were formulated, the key question for the post 2005 assistance regime should be by how much, and over what timeframe, assistance is reduced, not whether it should be reduced.

Adjustment costs are integral to the policy calculus

In establishing a time path for future assistance reductions, adjustment costs are a key consideration.

Much of the impending adjustment in the Australian TCF sector will occur regardless of the assistance regime. Global pressures mean that more firm closures are inevitable and further declines in sectoral output likely, even at current assistance levels. Moreover, the productivity improvements that will help some firms to survive mean that sectoral employment will continue to fall. The value of the Australian dollar will also influence the adjustment process. Indeed, some firms saw the potential for currency appreciation as a much greater threat to their viability than tariff reductions.

However, declines in sectoral output and employment resulting from reductions in assistance will impose additional adjustment costs on firms, their employees and TCF dependent regions. So will initiatives by TCF firms to improve their viability at lower levels of assistance.

As noted, such adjustment costs are not a reason to forgo the enduring community-wide benefits from lower assistance for the TCF sector.

Moreover, the likely declines in TCF output and employment from post 2005 tariff reductions and a phasing out of transitional budgetary support have been exaggerated by some parties. For example, the widely reported '19 000 jobs at risk in Victoria' appears to include estimated job losses in the TCF sector from the already legislated 2005 tariff reductions, as well as flow-on job losses in other sectors, but neglects flow-on gains.

These offsetting employment gains are important in assessing the adjustment implications of job losses in the TCF sector (projected by the modelling studies to be between 1000 and 10 000 Australia-wide) that would ensue from the post 2005 assistance options outlined below. Significantly, the Victorian Government's own modelling suggests that the *net* reduction in that State's output and, by implication, employment would be just 0.02 per cent, equivalent to less than 500 jobs. Net job losses of this magnitude over a period of years would be very small in the context of general employment growth in the Victorian economy.

Even so, changes to the assistance regime must give TCF firms, their employees and surrounding regions time to make necessary adjustments. Reducing assistance levels too quickly after 2005 could put at risk production that could become viable under a more gradual transition process. It would also increase the likelihood of disruptive adjustment, resulting in additional economic and social costs.

In parts of the sector, future adjustment could be somewhat easier than in the past. Some of the least competitive firms have already ceased production; skill levels have improved, increasing the alternative job opportunities for some employees; and most of the TCF dependent regions are now more economically diverse and operate in wider employment catchments — for example, Geelong/Melbourne and Wangaratta/Wodonga.

Nevertheless, in many cases, the adjustment process will still be difficult:

- Firms that have already implemented the ‘easy’ options for improving their international competitiveness may find future adjustment more demanding.
- Characteristics of the TCF workforce suggest that many factory-based employees could still have difficulty finding alternative employment. For outworkers, alternative opportunities may be even more limited (see box 3).
- Though regional dependence on TCF activity is lower than in the past, the closure of large firms in centres like Wangaratta and Devonport would be disruptive to regional economic activity and the social fabric of these communities. The same could also be true for some TCF clusters within metropolitan centres.

In formulating its post 2005 assistance options, the Commission has therefore given particular emphasis to avoiding the imposition of unreasonable adjustment pressures on the sector.

Post 2005 options for tariffs and the SIP

A clear assistance policy path should be established

The pressures and uncertainties confronting firms in the TCF sector are intense. A clear and extended path for assistance reductions would remove one source of uncertainty. Without clear policy direction, investment that would help some firms to operate successfully in a low assistance environment could be put at risk. Accordingly, the post 2005 tariff and transitional support options outlined below establish an assistance regime for the sector for the decade through to 2015, without the need for a further review. Indeed, any provision for another review would be counterproductive (see later).

A 5 per cent tariff should be the target

From 2010, tariffs for all other Australian manufacturing industries will be 5 per cent or less. In the Commission’s view, 5 per cent should therefore be the tariff target for the TCF sector, supported by transitional budgetary assistance in the intervening period through a successor to the SIP. This would maintain the thrust of current policy.

For most parts of the sector, achievement of this target rate by 2010 would not add unduly to adjustment pressures:

Box 3 Factors impeding adjustment in the TCF sector

While future adjustment in parts of the sector may be easier than in the past, characteristics of the TCF workforce may impede adjustment to external shocks, including reductions in assistance:

- Notwithstanding improvements in skill levels across the sector, many factory-based TCF employees have only industry-specific skills and few formal qualifications.
- TCF employees tend to be somewhat older than employees in other manufacturing industries. Female employment is also higher than the manufacturing average.
- The sector employs many recently arrived migrants which means that English language skills are often poor.

These characteristics are likely to make it more difficult for many displaced TCF workers to find alternative employment in their existing locations, or to relocate in search of new work. (Recent data suggest, however, that re-employment rates may be higher, and the average time taken to find new employment lower, than in the past.)

Some of the characteristics impeding adjustment by the factory-based workforce are even more pronounced among outworkers. They are typically women from East Asian backgrounds, often with few English language skills and no recognised educational qualifications. Moreover, cultural and family considerations prevent many outworkers seeking employment outside the home. Outworkers can also have personal equity in sewing equipment which may be difficult to realise in the event they are displaced, and have no notice periods or entitlements to redundancy and other severance payments.

For those firms that have previously availed themselves of readily available opportunities to improve their international competitiveness, future adjustment may be more demanding. Also, some non-profitable firms may be continuing to operate only because they cannot meet, or are unwilling to meet, substantial redundancy payments and other exit costs. This suggests that there is some accumulated adjustment pressure in the sector which could be released by an external economic shock.

The potential for such 'lumpy' adjustment is particularly relevant in a regional context. Small employment bases and constraints on inter-regional mobility make some regional centres vulnerable to firm closures and other lumpy adjustments.

However, the diversity of most TCF-dependent regional economies has been increasing. Also, TCF firms in regional areas tend to employ more males and people from English-speaking backgrounds than their counterparts in metropolitan areas. This may help to reduce any general gap in the adjustment capacity of regional versus metropolitan areas. Indeed, the capacity of many of these regions to cope with further declines in TCF activity may be greater than in some TCF production centres within the capital cities.

- The 2005 tariff reductions will add to the list of TCF products that will already be subject to a 5 per cent rate.
- For most of the other product groups, the required further reduction will only be 5 percentage points.

However, for the most highly assisted TCF products — apparel and certain finished textiles — the required tariff reduction after 2005 will be 12.5 percentage points. Ending special assistance treatment for these items by 2010 would therefore require a faster rate of tariff reduction than under the current assistance package (7.5 percentage points at the end of five years). While such differences are small in the context of the broader competitive pressures confronting many clothing and finished textile producers, too rapid assistance reductions could undermine some potentially viable firms.

Two broad tariff paths emerge

The preceding discussion indicates that there are two broad ways to move to the 5 per cent target, while providing the sector with a 'decade of policy certainty':

- reduce all TCF tariffs to 5 per cent by 2010, and then maintain those rates until 2015; or
- reduce tariffs on products other than apparel and certain finished textiles to 5 per cent by 2010, with tariffs on the latter reduced to 5 per cent no later than 2015.

The Commission's judgment is that the second approach would deliver a better overall outcome. While the benefits to consumers and user industries from lower tariffs for apparel and certain finished textiles would be delayed, the potential for the assistance reductions to trigger disruptive adjustment in these industries would be diminished. The Commission is also mindful of the fact that the fortunes of many local yarn and textile suppliers are closely allied to those of their customers in the clothing and finished textiles industries. Hence, there is a risk that disruptive adjustment at the end of the production chain could create 'knock-on' problems.

The case for 'erring on the side of caution' also provides a reason for delaying the attainment of the 5 per cent target for apparel and certain finished textiles until 2015. Although this would represent a slightly lower rate of reduction over the 10-year period than under the current package, many firms will already have availed themselves of the easier opportunities for performance improvement. Hence, in the future, they may have to work harder to increase their international competitiveness.

In the transition to the 5 per cent tariff target, the choice between annual reductions (phasing) and a pause followed by a larger one-off reduction — the approach employed in the current package — is less important. Given the extended timeframes required to recoup many investments to improve international competitiveness, firms' planning decisions may well depend more heavily on the tariff end point than on the somewhat higher duty rates applying in the intervening period. However, rates in the intervening period will obviously have some impact on decisions — particularly the timing of exits by non-competitive suppliers. In this context, the pause/step-down approach would provide firms with more breathing space and thereby facilitate a smoother adjustment process. It would also avoid the additional compliance costs for both the sector and the Government, associated with smaller annual reductions in duty rates.

The preferred tariff option

The Commission's preferred tariff option (see figure 1) is therefore as follows:

- Maintain all TCF tariffs at 2005 levels until 2010.
- In 2010, reduce tariffs on all TCF products other than apparel and certain finished textiles to 5 per cent and then maintain this rate to 2015.
- Reduce tariffs on apparel and certain finished textiles to 10 per cent in 2010 and then to 5 per cent in 2015.

The Commission recognises that this option might be viewed as less compatible with Australia's APEC commitment and other trade policy interests than options which would reduce all TCF tariffs to 5 per cent by 2010 (see chapter 7).

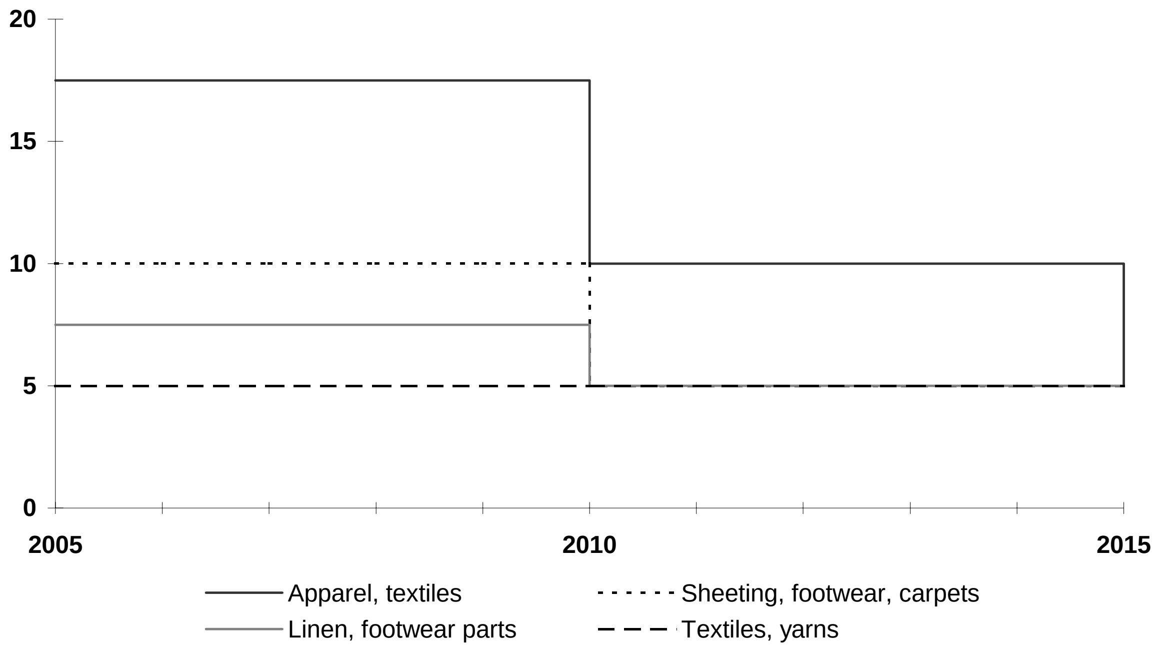
However, these concerns could be addressed by legislating now for all of the post 2005 tariff reductions. Legislating in advance would also reinforce the signal to the sector that the decade after 2005 is to be the last period of preferment for TCF production in Australia — irrespective of what might happen to TCF assistance levels in other countries.

Transitional support to accompany post 2005 tariff reductions

Cessation of transitional support when the current SIP expires in mid 2005 could be counterproductive. Given the magnitude of the adjustment task still facing the sector, immediate cessation in combination with further tariff reductions risks sacrificing some activity with reasonable prospects of becoming viable under more accommodating transitional arrangements.

However, a successor to the SIP should be time limited. And, as part of a package to end the sector's special assistance treatment, it would be difficult to justify higher levels of support than under the current program.

Figure 1 **The Commission's preferred tariff option**



Modifying the SIP would be preferable to introducing a new scheme

To maximise the effectiveness of further transitional budgetary support, the Commission examined three methods of delivery:

- a modified version of the current SIP;
- a bounty based on increases in firms' value added; and
- a competitive bidding scheme under which firms would apply for assistance for *proposed* expenditures to enhance their viability. (As in several other industry support programs, applications would be assessed by an 'expert' panel against a range of selection criteria.)

The Commission's focus was on which of these delivery methods would encourage the most *new* spending by firms to improve their international competitiveness, while keeping compliance and administrative costs within reasonable bounds.

While the incremental value added bounty and competitive bidding approaches would have some advantages over aspects of the current SIP (see box 4), there would be considerable benefits from taking advantage of the learning experience and precedents accumulated under the current scheme. The experience with the SIP illustrates that the costs for firms and the Government alike of bedding down completely new arrangements, and the associated uncertainty about outcomes, can be significant. Largely for this reason, the majority of participants favoured a modified version of the SIP. Moreover, the Commission sees scope to improve the effectiveness of the current program in helping firms to enhance their international competitiveness.

Box 4 **The alternative approaches for delivering transitional support**

Compared with the current SIP, an *incremental value added bounty* would:

- support a wider range of expenditures aimed at improving firms' international competitiveness; and
- in some respects, provide for more 'additionality'— only firms that increased their value added would receive support.

But it would:

- pose definitional and measurement difficulties;
- increase uncertainty for firms, because changes in value added unrelated to spending to improve international competitiveness would affect funding entitlements; and
- provide no support where downsizing/consolidation was a part of a firm's strategy to remain viable.

In contrast to the current SIP, a *competitive bidding scheme* would place the onus on firms to demonstrate that spending proposals would improve their international competitiveness and viability. It could also:

- support a wider range of expenditures to improve competitiveness than the current SIP; and
- in one respect, provide more certainty to firms — decisions on funding support would be finalised before the expenditure concerned was made.

However, it would be difficult to:

- keep compliance costs for firms and administrative costs for the Government within reasonable limits, particularly given the large number of firms in the sector; and
- get the right balance between reliance on pre-determined selection criteria and the degree of discretion afforded the selection panel. Too much discretion could see such a scheme degenerate into a non-transparent 'beauty-parade'.

In the Commission's judgment, there are good reasons for sticking with a SIP-style arrangement after 2005 (see text). Though most participants also supported continuation of the current approach, some noted that a competitive bidding arrangement could be employed as part of a separate scheme for small TCF firms that would continue to have difficulty accessing a modified SIP regime. However, as discussed later in the text, while desirable in principle, the Commission envisages that improving the access of small firms to transitional support would raise implementation challenges.

What modifications are warranted?

Viewed in isolation, many of the proposals from participants to make additional types of expenditures eligible for transitional budgetary support have merit.

However, expanding the range of eligible expenditures, or increasing the number of firms receiving support, will necessarily spread overall funding for the new scheme more thinly. This would reduce its capacity to induce changes that improved firms' international competitiveness. At the extreme, were the current level of support to be distributed proportionately to all firms in the sector, the funding rate would only be around 1.5 per cent of sales — hardly enough to make any difference to firm behaviour. Making too many changes would also impede a relatively 'seamless transition' from the current regime, thereby creating uncertainty and adding to compliance and administrative costs.

Accordingly, the Commission proposes only a handful of 'high level' changes to deliver more effective transitional assistance to TCF manufacturing firms with reasonable prospects of becoming internationally competitive:

- *Provide generally available support for expenditure on state-of-the-art second hand equipment.* Surplus production capacity both in Australia and overseas means that the purchase of state-of-the art second hand equipment can often be a cost-effective way for TCF firms to improve their competitiveness. As noted, under the current SIP, support for the purchase of such equipment is only available when it is part of a restructuring initiative in regional areas. With appropriate safeguards to minimise the risk of gaming and abuse, generalising the current provisions could facilitate the development of internationally competitive firms across the full spectrum of TCF manufacturing.
- *Subsidise investment in market and brand development for locally manufactured TCF products*. Spending in these areas is evidently desirable for firms looking to move out of production of standardised commodities into branded or otherwise differentiated products; to develop export markets; or to exploit market niches more generally. Support for market and brand development could be particularly helpful for clothing manufacturers that have reasonable prospects of becoming internationally competitive. As noted, in many parts of the clothing industry the scope for more automation is limited. Also, garment design and visual appeal are critical to market success. Hence, the current restriction on eligible spending to investment in plant and equipment and 'non-visual' innovation limits the funding support received by some potentially viable clothing manufacturers.
- *Discontinue 'Type 3' value added grants*. As currently implemented, these grants simply increase the rates of subsidy for investment in plant and equipment and spending on R&D and innovation. But the way they are paid means that the

increased rate of subsidy can vary arbitrarily among firms. Discontinuing these grants would help to simplify the new regime. It would also release funds that could be used to directly increase the subsidy rates for investment and R&D, and/or to pay for the two eligibility extensions outlined above.

The Commission also proposes that the new transitional arrangements incorporate a clearly enunciated and explicit objective; namely, to foster the development of Australian TCF manufacturing activity that can be viable and internationally competitive without special assistance.

The Commission emphasises that the detailed implementation of these changes (and some administrative modifications outlined in the report) would require consultation with the sector. It would also be necessary to develop appropriate safeguards against fraud and gaming.

A separate small firm module?

A recurring theme in submissions was that transitional support should be more accessible to small TCF firms. Many suggested that the minimum spending threshold to qualify for support should be reduced. Others proposed the introduction of a separate competitive bidding scheme for small producers (with funding of the order of $15-20 million a year).

In the Commission's view, the in-principle case for not discriminating against small firms is self evident. The entrepreneurial and innovative skills apparent in many small TCF firms suggests that there is good growth potential in this part of the sector. Indeed, given the financing difficulties that small firms often face, transitional budgetary support might induce more new activity to improve international competitiveness than support provided to large, established firms.

However, attempting to bring a large number of small firms within the funding net would see overall support spread much more thinly and could cause administrative costs to escalate sharply. These problems would be particularly acute if better access for small firms were pursued through adjustments to the minimum spending threshold. Under a competitive bidding scheme, it would be possible to use screening criteria to limit the number of applicants. But to be effective in containing administrative costs, these criteria would have to be quite restrictive. The transparency and independence of the vetting procedures would also require attention. In sum, an initiative for small TCF firms warrants further consideration, but careful thought about how to address these practical issues, while still providing cost-effective transitional support, would be required.

The duration and level of funding

In assessing how long transitional support should be extended after 2005, and the level of funding for the new scheme, the following considerations are relevant:

- Under the Commission's preferred tariff option, the reduction to 5 per cent in the tariff on clothing and certain finished textiles would not occur until 2015. Ending transitional funding much earlier would see firms in those segments making the last part of the tariff transition without the support that others in the sector had enjoyed.
- Even though firms elsewhere in the sector would be operating at a 5 per cent tariff from 2010, many could experience knock-on adjustment pressures associated with the impending tariff reductions for clothing and certain finished textiles after that date.
- Reinforcing the message to firms that special assistance treatment is coming to an end is important. This suggests that, like tariffs, transitional support should be progressively reduced.
- As noted, as part of a package to end special assistance treatment, it would be hard to justify funding support higher than that provided by the current SIP.
- At the same time, in facilitating a seamless transition from the current regime, there is a case for maintaining funding levels in the early years of the new program.

In the Commission's judgment, the following funding profile would strike a balance between these sometimes opposing considerations:

- The new transitional support program would operate for eight years from 2005.
- Funding for the first four-year period would be equivalent to total payments in the last four years of the current SIP (in nominal terms).
- Funding for the second four-year period would be halved.
- Transitional support would then end in 2013.

The Commission notes that provided adjustments were made to hold the total quantum of proposed funding constant in present value terms, a time profile of say two five-year periods, or five years and three years, would most likely make little difference to outcomes. Hence, in some senses, the key thrust of the Commission's proposal is to set an indicative benchmark for the present value of funding for the new transitional support arrangement. However, though the Commission sees scope for some variation in the time profile of this support, if the sector's special tariff treatment is not to end until 2015, distributing all funding very quickly after 2005 would raise the prospect of subsequent calls for more transitional assistance.

Assistance for displaced TCF employees

The post 2005 assistance options outlined above give priority to reducing the risk of disruptive adjustment in the sector.

But the possibility of disruptive change cannot be ruled out. The global competitive pressures confronting the sector are likely to see some TCF firms cease operation in the next few years, irrespective of assistance settings.

Assistance for displaced TCF workers in finding alternative employment is sometimes provided by the firms themselves. Assistance with job search (and often financial support) is also available through the Job Network arrangements.

As presently constituted, however, those arrangements might not be adequate in the event of large firm closures (or other major job shedding). In particular, when a large firm closes, it may be difficult to ensure that all displaced workers receive adequate attention, particularly in those regional areas where the number of Job Network providers is limited. Given the inevitability of more firm closures in this sector, the characteristics of the TCF workforce and the importance of TCF activity to some regions, targeted labour market support is warranted during the tariff transition period.

This should not involve a separate scheme operating in parallel with the Job Network. That would be a recipe for wasteful duplication of services.

Rather, such support should augment Job Network services when large scale, or regionally significant, retrenchments occur or are in prospect. Drawing on recent experience with labour market programs in the TCF sector in Australia and abroad, and the input from inquiry participants, this augmentation of the standard Job Network services should:

- provide scope to initiate Job Network-type support when large scale, or regionally significant, retrenchments have been announced, rather than only after job shedding has occurred. (There is evidence suggesting that the prospects of re-employment are improved if support services are made available while those facing retrenchment are still in their jobs); and
- use small teams of people with experience in the TCF sector to work with the displaced employees, or those facing retrenchment.

There is also scope to make mainstream Job Network services more accessible to all displaced TCF employees. Because of limited communication and English language skills, some displaced TCF workers may be reluctant, or find it difficult, to access the Job Network. These difficulties could be ameliorated by regular dissemination of information on Job Network services to the TCF workforce, including outworkers. Indeed, this would be a concrete way to assist outworkers, who might be more difficult to encompass in the specific program designed to deal with major job shedding in the sector.

These initiatives need not be expensive. But they could help to ease the adjustment burden for one of the most vulnerable groups in the workforce.

No changes are required to other parts of the assistance package

The Commission does not see any reason to either abolish or change the Overseas Assembly Provisions or TCF policy by-laws. For most firms, these are minor parts of the assistance package and will become even less relevant as TCF tariffs decline in 2005 and beyond. Making changes could increase uncertainty as new arrangements were bedded down, as well as diverting attention from the main game. Accordingly, the Commission considers that these instruments should be left in place unchanged, until such time as tariff reductions render them redundant.

Similarly, it is not proposing any changes to tariff rates applying on individual TCF items. While participants claimed that various anomalies and inefficiencies arise under the current broad tariff structure, 'band-aid' solutions would inevitably lead to new distortions. By far the cleanest approach to addressing such concerns is to reduce all tariffs to the benchmark rate of 5 per cent as soon as practicable.

A further review would be counterproductive

Many industry interests argued that there should be a 2008 (or later) review of TCF assistance before any post 2005 tariffs cuts go ahead.

However, the prospect of a review would detract from policy certainty and the message to firms that the sector's special assistance treatment must end by 2015. In so doing, it could delay new investments and other adjustments that would help firms to operate successfully in a low tariff environment. Also, previous experience suggests that managerial energy would be diverted into further lobbying to preserve the sector's special assistance treatment.

What else should be done?

Responsibility for addressing many of the impediments and weaknesses that reduce the viability of TCF production in Australia lies with the sector itself. For example, more cooperation and better communication between firms and their employees and representatives is crucial to improving workplace outcomes. Similarly, more dialogue between firms, industry associations and education and training providers would help to ensure that firms have adequate access to necessary skills.

However, government also has responsibility to provide a broader policy framework that facilitates firms' efforts to improve their competitiveness:

- Workplace regulation which allows negotiation of flexible and productive outcomes is important to the sector's future. So too is an industrial relations framework that encourages cooperative resolution of workplace disputes.
- Additional policy initiatives to address employees' legitimate concerns (particularly given history in this sector) about the security of their entitlements in the event of firm closures are warranted. Establishing an independent review to assess the merits of different approaches should be a first step.
- Further microeconomic reform would assist the sector to compete internationally with lower levels of assistance. Improvements in Australia's taxation regime could also be helpful — particular concerns were raised in this inquiry about inefficiencies in current payroll tax arrangements. There remains a strong case for removing the 3 per cent revenue duty imposed under the Tariff Concession System. And governments must ensure that their general industry programs are effective and efficient.
- While Australia's tariffs should not be tied to those in other countries, the Commonwealth and State Governments must continue to place a high priority on securing better access to overseas markets for TCF and other producers. Though some progress has been made, Australian TCF firms still face widespread tariff and non-tariff barriers. These are impeding the efforts of some internationally competitive firms to improve their performance through increased exports.

  That said, care is required in pursuing better market access through bilateral agreements. The likely benefits for Australia, and the effects on particular industries, will depend on both the coverage of an agreement and its detailed rules. Thus, as TCF interests pointed out to this inquiry, the rules of origin for the proposed bilateral agreements with the United States and Thailand will have a crucial bearing on outcomes for the sector.

An appropriate strategy for outworkers

Increasing reliance on outwork is a feature of the clothing industry in Australia and many other countries. This is primarily because of the scope it provides to firms to respond quickly, flexibly and cost effectively to customer demands. Given that short-run, quick response apparel production is one of the key areas where

Australian clothing producers can offer a competitive alternative to imports, such flexibility is very important.

Moreover, some outworkers may prefer to work at home, particularly where flexibility in the pace and timing of tasks allows them to combine earning an income with family responsibilities. Outwork also provides job opportunities for those newly arrived migrants with poor English language skills, limited formal education and sometimes no immediate access to welfare.

At the same time, the potential for the exploitation of outworkers through low rates of pay, long working hours and poor working conditions is a longstanding concern. While there is little hard information on the extent of exploitation, a variety of regulation has been introduced to try to ensure that outworkers are properly remunerated and work under appropriate conditions.

However, regulation is not a panacea for the problems facing outworkers. It can be a two-edged sword — excessive regulation, or heavy handed enforcement, may simply make some production internationally uncompetitive to the detriment of the outworkers concerned. In any event, because of the nature of outwork and its long and convoluted supply chains, regulation has proved difficult to enforce.

Achieving greater compliance with minimum pay and condition requirements for outworkers is therefore the goal of the Homeworkers Code of Practice — a voluntary arrangement among retailers, TCF suppliers and wholesalers, and the main industry union. Recently, the number of signatories to the Code has increased significantly.

In the Commission’s view, the emphasis in the Code on voluntary compliance with current regulatory requirements provides the best way forward in this area. Indeed, there is a risk that heavy handed attempts to enforce existing regulation, or the implementation of more regulation, could undermine the increasing degree of cooperation now emerging under the Code, and therefore be counterproductive.

A stronger and more competitive Australian TCF sector is achievable

A key message that emerges from this inquiry is that there is little that governments in developed countries can or should do to stop labour intensive, standardised TCF production from migrating to developing countries. Further adjustment in Australia’s TCF industries is therefore inevitable.

This change will be difficult for firms, their employees and surrounding communities. Hence, facilitation of, and support for, the adjustment process is essential.

But this does not extend to turning back the clock by locking in tariffs or other barriers to try to avoid or delay inevitable change. The opposite is in fact the case, with further assistance reform having an important role to play in promoting a successful transition by the sector.

With the right transitional policies, the Commission is confident that the development of a smaller but more internationally competitive TCF sector, able to provide well paid and interesting jobs to skilled employees, is achievable in the medium term. This would allow remaining TCF firms and their employees to face the challenges and opportunities of global markets with some confidence, as well as providing substantial benefits to the wider community. The options identified by the Commission in this report would serve to promote these outcomes.

Findings

The following are the Commission's findings on: the TCF sector's future prospects; its capacity for further adjustment; the effects of the current assistance regime; post 2005 assistance arrangements; and other policy-related matters impinging on the sector's future performance and viability. The reasons for these findings are set out in the relevant chapters of the report.

THE TCF SECTOR'S FUTURE PROSPECTS (CHAPTER 3)

- *Some firms and parts of the sector are performing well, exploiting competitive advantages to develop new products and to secure new markets.*
- *Other firms are in a process of transition, with reasonable prospects of operating in a lower assistance environment in the medium to longer term.*
- *For firms producing standardised products in the more labour intensive parts of the sector, future prospects are very limited. Many will not survive, regardless of the assistance regime.*
- *Across the sector as a whole, future assistance levels will be but one influence on firms' prospects. Global market pressures, firms' business models and exchange rates are just some of the many other factors that will impinge on those prospects.*

ADJUSTMENT IN THE TCF SECTOR (CHAPTER 4)

- *Adjustment for workers displaced from the TCF sector, in cities as well as in regions, may be difficult:*
  - *Educational attainment is often limited and skill levels are frequently basic and sector-specific.*
  - *The predominance of female employees and low English language proficiency further reduce labour mobility and therefore re-employment opportunities.*
  - *Many small and medium sized businesses have had a history of being unable or unwilling to pay employee entitlements in the event of closure.*
  - *The prevalence of 'at-risk' firms increases the possibility of lumpy adjustments to an external shock.*
- *The costs of adjustment for displaced outworkers can be higher than for factory-based employees.*
- *Regional dependence on TCF activity has declined significantly over the past 10 years and overall growth in regional activity and employment has generally been strong. Nevertheless, dependence on TCF activity is still high in a few regions.*

- *The long term effects of changes in TCF activity on regions depend on the interplay of several factors, including:*
  - *the degree of dependence on TCF activity in those regions;*
  - *the prospects of individual TCF firms;*
  - *the strength of overall regional growth and employment; and*
  - *job opportunities available in neighbouring regions.*
- *If the need arises, general measures such as the Regional Partnership arrangements are available to help regions experiencing problems from adjustment in the TCF sector.*

CURRENT ASSISTANCE ARRANGEMENTS (CHAPTER 5)

- *The tariff pause coupled with SIP support allows time for consolidation and appears to be encouraging some additional investment and R&D in parts of the sector that should improve international competitiveness.*
- *However, various elements of the package seem likely to limit its overall effectiveness. Moreover, tariffs and the SIP impose large costs on consumers, user industries and taxpayers.*
- *Changes are therefore required so that future support for the sector will better contribute to the Government's objective of encouraging the TCF sector to become internationally competitive at lower levels of assistance and to provide a better balance between this objective and the interests of consumers, taxpayers and the wider community.*

APPROACH TO POST 2005 ASSISTANCE (CHAPTER 6)

- *While TCF activity has some distinguishing characteristics, these do not warrant indefinite preferential treatment for the sector.*
- *A policy of tying tariffs protecting Australian TCF producers to levels in other countries would not be in Australia's interests.*
- *Further TCF tariff reductions would reinforce incentives for productivity improvement, provide benefits to consumers and industries using TCF products, and facilitate Australia's trade policy objectives.*
- *The legislated tariff reductions for the sector should take effect on 1 January 2005 as scheduled and further reductions should be made after 2005. Those reductions should be implemented in a measured manner over time, accompanied by transitional assistance to help facilitate the adjustment process.*
- *The tariff target should be 5 per cent, the maximum rate that will apply to all other Australian industries from 2010.*

- *To avoid uncertainty affecting investment and production decisions, it is important to lay down a path and timetable now for the sector to reach that target.*
- *Making provision for further review of TCF assistance would detract from the policy certainty the sector needs and diminish the pressure on firms to improve their international competitiveness.*

POST 2005 TARIFF OPTIONS (CHAPTER 7)

- *The capacity of apparel and certain finished textile producers to absorb a tariff reduction of 12.5 percentage points over the 2005 to 2010 period without serious disruption is questionable. The reduction in tariffs for those goods to the five per cent target should therefore take place over the longer period to 2015.*
- *For other TCF products, including carpets and footwear, the required tariff reduction after 2005 to reach the five per cent tariff target is five percentage points or less. Making that reduction over the five-year period to 2010 is unlikely to place unreasonable adjustment pressure on those industries.*
- *In moving to the five per cent tariff target, there would be advantages in continuing the step down approach employed in the current assistance package. Hence the Commission's preferred post 2005 tariff option is as follows:*
  - *maintain all TCF tariffs at 2005 levels until 1 January 2010;*
  - *on 1 January 2010, reduce tariffs on apparel and certain finished textiles to 10 per cent and tariffs on other TCF products to 5 per cent; and*
  - *maintain tariffs on apparel and certain finished textiles at 10 per cent until 1 January 2015, and then reduce them to 5 per cent.*
- *Legislating early for all of these tariff reductions would deliver the policy certainty that the sector requires and maintain the pressure on firms to improve their performance. It would also help to minimise any negative perceptions about this option in relation to Australia's commitment to the APEC goal of 'free and open trade and investment' in the region by 2010 for developed countries.*
- *Further reductions in TCF tariffs would effectively continue the phasing out of the TCF policy by-laws and the Expanded Overseas Assembly Provisions. These arrangements should therefore be continued after 2005 without amendment. Sector-wide duty reductions would also diminish the need to consider requests for duty free entry for specific TCF goods not made in Australia.*

TRANSITIONAL ASSISTANCE (CHAPTER 8)

- *A further period of transitional assistance is warranted after 2005 to help TCF firms which manufacture in Australia to improve their international competitiveness, as further tariff reductions are implemented.*

- *Transitional assistance arrangements should avoid spreading funding too thinly to make a difference to firms' behaviour.*
- *Post 2005 transitional assistance should follow the approach of the existing SIP, with some modifications to improve its effectiveness. Although further analysis and discussion with the sector will be needed before operational arrangements are finalised, the following modifications have merit:*
  - *incorporate a clearly enunciated and explicit objective; namely, to foster the development of Australian TCF manufacturing activity that can be viable and internationally competitive without special assistance;*
  - *provide generalised support for purchase of state-of-the-art second hand equipment and for ancillary expenditure;*
  - *subsidise investment in market and brand development associated with the manufacture of TCF products in Australia;*
  - *discontinue specific additional assistance for value added;*
  - *accelerate payments to firms as far as possible;*
  - *eliminate provision for funding support to firms in administration or receivership; and*
  - *enhance transparency and certainty by writing the new arrangements in simple and understandable language.*
- *An initiative to help small TCF firms to access transitional budgetary assistance warrants further consideration, but would require careful thought about how to address significant implementation problems, while still providing cost-effective support.*
- *Transitional support should not be extended to early stage wool processors — although they are currently experiencing some problems, these are not primarily linked to changes in Australian TCF tariffs.*
- *The following funding profile would provide the benefits of a seamless transition from the current SIP, while reinforcing the signal to the sector that its special assistance treatment is coming to an end:*
  - *The new transitional support program would operate for eight years from 2005.*
  - *Funding for the first four year period would be equivalent to total payments in the last four years of the current SIP (in nominal terms).*
  - *Funding for the second four year period would be halved.*
  - *Transitional support would then terminate in 2013.*
- *The transition from the current SIP to the post 2005 arrangements should be as seamless as possible. Funding claims not paid to firms by the end of the current SIP because of the five per cent sales cap should be carried over into the post*

2005 scheme so that the companies concerned can be paid their entitlements in due course.

LABOUR ADJUSTMENT SUPPORT (CHAPTER 9)

- *Implementation of TCF-specific labour adjustment measures could help to reduce the likelihood of disruptive adjustment resulting from post 2005 assistance reductions, or other pressures confronting the sector. Such assistance should focus on addressing large scale, or regionally significant, job shedding in the sector through an augmentation to Job Network services. In doing so it should:*
  - *include provision for early intervention where there is prior notice of large scale, or regionally significant, retrenchments; and*
  - *use people with experience in the TCF industry.*
- *There is also scope to make mainstream Job Network services more accessible to all displaced TCF employees through regular dissemination of information on those services, including to outworkers.*

WORKPLACE ARRANGEMENTS, INDUSTRIAL RELATIONS AND SKILLING (CHAPTER 10)

- *While workplace arrangements in many Australian TCF firms are more productive and flexible than in the past, further improvement would help some firms to compete successfully with lower levels of assistance.*
- *Given the number of 'at-risk' firms, the TCF sector can ill-afford the industrial disputation recently witnessed in some enterprises.*
- *Responsibility for achieving better workplace outcomes rests largely with managers and employees within individual enterprises. Better communication and more cooperation between the parties is crucial.*
- *Human resource and industrial relations skills in the sector require improvement. Among other things, this would help to promote cooperative solutions to industrial relations issues and assist managers to convey to their employees and union representatives the relationship between workplace outcomes and the viability of the enterprise and the industry.*
- *Workplace regulation has an important role in setting the framework for negotiations between firms and their employees and representatives. However, specific proposals put forward to constrain further the rights of employees to take industrial action raise complex issues that would have ramifications in other industries. This means that it is not possible to judge their merits solely on the basis of recent experience in the TCF sector.*
- *The protection of employee entitlements is a legitimate concern for employees in the TCF sector given its history, and has been a trigger for costly disputes in this*

and other sectors. An independent review of the broader entitlements issue is warranted.

- *Some skill shortages and deficiencies in available training packages are evident in parts of the TCF sector. However, identifying what specific responses may be required is beyond the scope of this inquiry. Importantly, responsibility for ensuring that skill and training needs are met lies largely with the sector, educational institutions and training providers, rather than with governments.*

OUTWORKERS (CHAPTER 10)

- *The flexibility provided to manufacturers by the use of outworkers can assist them in responding more effectively and efficiently to the needs of their customers. For some outworkers, there are advantages from being able to combine paid employment with family and other responsibilities.*
- *While it is difficult to ascertain the number of people periodically engaged in outwork, the full-time equivalent number of outworkers in Australia is unlikely to be much above 25 000. Nonetheless, with the decline in factory-based employment in the TCF sector over the past few years, outworker employment is now about 40 per cent of total factory-based employment in the sector and exceeds factory-based clothing employment by about 25 per cent.*
- *Concerns about the exploitation of outworkers appear to have more to do with the levels of compliance with legislated requirements than with the provisions of those requirements.*
- *Given the nature of outwork and the supply chain involved, achieving greater compliance will inevitably require cooperation between retailers, suppliers, their contractors and unions. More regulation, or heavy handed attempts to enforce regulation, could undermine the increasing degree of cooperation now emerging under the voluntary Homeworkers Code of Practice and therefore be counterproductive.*
- *Governments, employer and community groups, industry associations and trade unions have a role to play in promoting compliance with awards and the Code, and the contribution that good employment practices more generally can make to the sector's future prospects.*

OTHER POLICY ISSUES (CHAPTER 11)

- *The 3 per cent revenue duty imposed under the Tariff Concession System continues to disadvantage Australian manufacturers — including TCF firms — and imposes unnecessary costs on their customers.*
- *As currently implemented, payroll tax has significant deficiencies. However, an assessment of possible changes to address those deficiencies, or of the case for abolishing payroll tax, would need to be judged in terms of the community-wide*

impacts, not just the benefits for some TCF producers. The efficiency of replacement revenue raising instruments, and/or the consequences of reducing government expenditures, would be important considerations in assessing the community-wide outcome.

- *Some progress has been made in reducing trade barriers faced by Australia's TCF exporters, but widespread barriers still remain. While Australia's tariff levels should not be tied to assistance levels in other countries, Australian Governments must continue to pursue improved market access for TCF and other sectors in multilateral, regional and bilateral forums.*
- *However, the benefits for Australia from bilateral trade agreements will depend crucially on their coverage and detailed rules. Such agreements are unlikely to be a panacea for market access problems — either generally or in particular sectors — and should not reduce the emphasis given to securing better access through more broadly-based multilateral arrangements.*
- *There is scope for improved cooperation and information sharing between TCF suppliers and major retailers to help optimise the means of providing Australian consumers with TCF products at the lowest overall costs (including all supply chain costs).*
- *The application of 'proof-of-safety' requirements (NICNAS) for new industrial chemicals which have been certified as safe in other developed countries would only be warranted if the regulator can demonstrate both that a particular chemical is 'high risk' and that specific circumstances in Australia make re-testing essential.*

1 About the inquiry

1.1 What has the Commission been asked to do?

Australia's textile, clothing, footwear and leather (TCF) industries are experiencing a sustained period of structural change. Major rationalisation of production has reduced sectoral output and employment; the product mix and supply chains are changing; exports of Australian TCF products have risen, as has the import share of the domestic market.

To a large extent, structural change in the Australian TCF sector is a response to global pressures confronting producers in most developed countries. More intense competition from suppliers in developing countries, changes in consumer spending patterns and technological advances are key factors driving change.

However, as in many other developed countries, reductions in protection for Australian TCF producers over the last decade and a half have added to these pressures. Australia abolished quantitative restrictions on TCF imports in 1993 and has progressively reduced tariff rates. To further encourage the development of an internationally competitive TCF sector, successive governments have also provided targeted budgetary support.

The current assistance package commenced in 2000 following a broad ranging review of the sector and its assistance arrangements by the Industry Commission (1997). The key elements of the package are a pause in tariffs at 2000 levels until 2005 when further reductions will occur, and the provision of nearly $700 million in budgetary assistance over the five-year period 2000-01 to 2004-05 through the TCF Strategic Investment Program (SIP). The main purpose of this inquiry is to provide advice to the Government on options for assistance after 2005.

The terms of reference

In reporting on post 2005 assistance arrangements and a range of related matters that will affect the TCF sector's prospects and future viability, the Commission is to have regard to the Government's desire to:

- encourage the sector to adjust into activities where it will be internationally competitive with lower levels of government assistance; and
- improve the overall performance of the Australian economy.

Among other things, the Commission is to:

- evaluate the effectiveness, efficiency and appropriateness of current assistance programs in achieving structural change and a more internationally competitive TCF sector by 2005;
- analyse the short and long term implications of policy options, including tariff options, consistent with the Government's international obligations, which would encourage the sector to adjust to a more viable and sustainable competitive position, giving particular attention to the impacts on regional areas with significant TCF activity;
- identify major opportunities for the TCF sector, strengths and weaknesses in realising those opportunities and other impediments to its long term viability;
- examine relevant workplace issues and the scope for workplace reform to improve the competitiveness of the sector; and
- report on the likely impact on the sector of international trade developments.

The full terms of reference are reproduced at the front of this report.

1.2 How has the Commission approached its task?

It has provided opportunities for extensive public input

Given the short reporting period for the inquiry, the Commission sought to streamline and expedite its inquiry processes.

Nonetheless, these processes have provided the opportunity for a wide range of interested parties to contribute to the Commission's deliberations:

- At the outset of the inquiry, the Commission invited written submissions on the matters under review. Prior to releasing a Position Paper (see below), it received nearly 100 submissions from a broad cross-section of industry, union, government, regional and community interests, as well as from some retailers and users of TCF products.
- Over the period November 2002 to March 2003, the Commission met with more than 70 organisations and individuals in both capital city and regional locations covering a similar range of interests.

- In April, it released a Position Paper (PC 2003b) outlining its initial views and findings, and setting out preliminary options for post 2005 assistance arrangements for the TCF industries. To elicit views on the paper, the Commission held public hearings in Melbourne, Geelong and Sydney in June. Some 35 organisations and individuals participated in discussions at those hearings. The Commission also received more than 80 additional written submissions responding to the preliminary findings and options in the Position Paper.

More detail on inquiry processes is provided in appendix A, including lists of those with whom the Commission met, those who made submissions and those who participated in the public hearings. The Commission wishes to thank all of the organisations and individuals who contributed to the inquiry.

It has drawn on other relevant analysis

In preparing this report, the Commission has had regard to assessments in recent published studies — listed in appendix A — examining the performance and prospects of the TCF sector and factors impinging on its future viability.

The Commission also engaged three separate organisations to model the potential impacts of some specific post 2005 assistance options on the TCF sector, relevant regions and the wider community. To facilitate public scrutiny of the preliminary results of this modelling, and to allow comparison with some quantitative projections submitted independently by inquiry participants, it organised a modelling workshop prior to the release of the Position Paper (see appendix E).

Following the release of the Position Paper, results from two additional modelling studies were submitted to the Commission:

- Several participants, including the Victorian Government, referred to a study by the National Institute of Economic and Industry Research (NIEIR) examining the effects on regions within Victoria of TCF assistance reductions.
- The Victorian Government also provided some summary results and methodology from its in-house modelling (using the MONASH model) of the post 2005 assistance options for the TCF sector favoured by the Commission in the Position Paper.

However, the limited explanations and details provided about some of these results made it difficult to reconcile them with findings in the other studies (see chapter 6 and appendix E). Given that the Commission's intention in organising the modelling workshop was to avoid such reconciliation difficulties, it was disappointing that the NIEIR did not take up an invitation to participate.

1.3 What is in the rest of the report?

The remainder of this report is structured as follows:

- Chapter 2 outlines key features of the domestic TCF industries and the changes that have occurred in recent years.
- Chapter 3 looks at the prospects for the Australian TCF sector having regard to:
  - global pressures affecting TCF producers in all developed countries;
  - emerging opportunities for local suppliers in both domestic and export markets; and
  - the sector's strengths and weaknesses in realising those opportunities, as well as 'external' threats to its future viability.
- Chapter 4 looks at the capacity of Australian TCF firms, employees and communities to make further adjustments having regard to:
  - broad workforce and regional characteristics; and
  - adjustment experiences in the sector to date.
- The next suite of chapters looks at assistance arrangements for the sector:
  - Chapter 5 examines the effectiveness of the current assistance regime in facilitating structural change and the development of an internationally competitive TCF sector.
  - Chapter 6 discusses the Commission's broad objectives and its approach in developing post 2005 assistance options.
  - Chapter 7 sets out some specific tariff options, as well as examining other tariff-related aspects of the TCF assistance regime — including policy by-laws and the overseas assembly provisions applying to certain TCF production.
  - Chapter 8 spells out options for a further period of transitional budgetary support. These encompass both the design attributes of a successor to the Strategic Investment Program, and the duration and level of funding for a new program.
  - Chapter 9 discusses the role for TCF-specific labour adjustment support in the event of disruptive future change in the sector and outlines some key requirements for such support to be effective.
- The final two chapters discuss industry and broader government policy initiatives that could facilitate adjustment in the sector:
  - Chapter 10 looks at workplace arrangements and skilling issues, including matters relevant to outworkers.

– Chapter 11 examines a range of issues including the role of taxation policy and microeconomic reform in promoting a more competitive sector; anti-dumping; access for Australian TCF producers to overseas markets; relationships between TCF suppliers and retailers; and environmental regulations impacting on TCF production.

Additional data and supporting analysis are contained in appendices to the report.

2 The Australian TCF sector

2.1 A diverse component of Australian manufacturing

Textile, clothing, footwear and leather (TCF) manufacturing in Australia covers all stages of production from the processing of raw materials to the supply of finished products. Despite considerable rationalisation and restructuring, it remains one of Australia's larger manufacturing sectors. Australian TCF producers generated revenue in excess of $9 billion in 2000-01, with the sector accounting for 4 per cent of value added and 6 per cent of employment in broader manufacturing and around 0.4 per cent and 0.6 per cent of value added and employment in the economy as a whole. Formal (factory-based) employment is at least 58 000, with some data sources suggesting a figure of around 70 000 (see appendix B). There is also a significant element of informal employment through 'outwork' (mainly in clothing manufacture). The Commission estimates that the number of outworkers (measured as full-time equivalents) is around 25 000 (see chapter 10).

The sector is most important in the Victorian economy where production accounts for 6 per cent of value added and 9 per cent of employment in manufacturing. While most of this activity is in Melbourne, 15 per cent of total Victorian TCF employment is located in regional centres, such as Geelong, Ballarat, Bendigo, Warnambool, Wangaratta and Wodonga. Regional TCF centres in other States include Devonport (Tasmania), Albury (NSW) and the Gold Coast (Queensland). Sydney is also home to a large number of TCF manufacturers.

TCF manufacturing is diverse. Aside from the range of products manufactured (see box 2.1), diversity is evident in the sector's workforce (see chapter 4) and the characteristics of TCF establishments. At one end of the spectrum, there are some large establishments employing several hundred people. However, as in other developed countries, the Australian TCF sector features many small enterprises. ABS data indicate that firms employing less than 20 persons accounted for a third of total TCF employment and a quarter of production in 2000-01. In addition, there are a large number of micro businesses which combine some TCF design and manufacturing activity with the wholesaling and retailing of finished TCF products. In the official ABS statistics, these firms are generally included in the retail or wholesale services sectors (see appendix B).

Box 2.1 **TCF manufacturing activity**

TCF manufacturing in Australia covers the entire spectrum of activities from processing raw materials through to the production of final goods. Specifically, the supply chain comprises the following activities:

- early stage processing — the preparation or production of leather and textile fibres:
  - leather production including activities such as salting, wet blueing (the first stage of tanning), finishing and fur dressing;
  - natural fibres — mainly cotton and wool but also niche materials such as cashmere and alpaca; and
  - man-made fibres: including cellulosics such as viscose; synthetics such as polyester, nylon, acrylic and polypropylene (all derived from petrochemicals); and fibres made from inorganic materials such as glass, metal or ceramics.
- production of textiles which involves the conversion of fibres into yarns and fabrics (through spinning, weaving, knitting, tufting etc);
- finishing activities — aimed at giving fabrics visual, physical and aesthetic properties (through bleaching, printing, dyeing, impregnating, coating, plasticising etc); and
- transformation of yarns, fabrics and leather into products such as:
  - clothing and footwear (involving design, pattern making, fabric cutting and assembly);
  - carpets (woven, knitted, tufted and flocked) and other textile floor coverings;
  - home and commercial textiles (including towels, bed linen, curtains, furniture coverings); and
  - technical textiles which encompass performance or functional characteristics (including shade cloth, medical products, insulation materials, geotextiles).

Source: TCFL Forum 2002.

The mechanisms for setting wages and conditions also vary across the sector. Employees in small firms are typically covered by awards, while those in large firms tend to operate under enterprise agreements.

The sector draws on a wide range of skills including trade, technical, design, manufacturing, logistics, sales, marketing and general management skills. However, many TCF employees have only basic and/or industry specific skills, educational attainment levels are often low, and employees are more likely to be older, female, married and not proficient in speaking English. These characteristics serve to restrict the mobility of much of the sector's workforce relative to employees in many other parts of the economy (see chapter 4).

2.2 A sector in transition

There has been much rationalisation

The TCF sector in Australia today is very different from that in the past. Traditionally, local activity was characterised by a series of manufacturing processes, with firms along the supply chain purchasing inputs from (mainly local) upstream suppliers and selling outputs to (mainly local) downstream customers. High tariffs and quota protection ensured the continued viability of firms along the chain, restricted the ability to source from competing offshore suppliers and reduced the incentive to find new (export) markets. Retailers played a largely passive role in selling final products designed and supplied by manufacturers with limited direct contribution to purchasing or production decisions (see below).

In recent years, however, competition from emerging low-wage production centres, slowing growth in domestic consumer demand, large reductions in domestic assistance and increased concentration in retailing have collectively placed new pressures on local TCF manufacturers. Many firms have left the sector, while others have rationalised, merged and pursued new sourcing strategies to survive. As a result, aggregate domestic TCF manufacturing activity has contracted and import penetration has risen sharply (see below).

The nature of local TCF activity has changed

The interplay of global and local forces has profoundly affected the structure of the sector. In clothing and footwear, many firms have reorganised their supply systems by relocating part, or all, of their manufacturing processes offshore to reduce labour costs. Other firms have focused domestically on low volume ‘quick response’ supply systems which provide flexibility in responding to demand shifts; some have concentrated on quality, design, service and brand development strategies with production subcontracted to local or overseas manufacturers; and others have sought to cut production costs by rationalising product lines.

There are many examples of firms successfully pursuing these strategies. For instance, Pacific Brands and Gazal Corporation — two of the biggest players in Australia’s clothing industry managing a wide range of established Australian brand names — have shifted the bulk of their manufacturing operations to China. Up-market fashion houses such as Carla Zampatti have prospered by focusing on brand development. They use local and imported fabrics, modify international designs and subcontract production to outworkers. DPK Australia makes and imports fabric, subcontracts clothing manufacture for its larger customers and provides a stock service to small garment makers. Dowd Corporation (a Yakka subsidiary) has a successful business in the 'high-end' corporate apparel market with a significant proportion of revenue coming from the management of customers' total apparel requirements.

For their part, textile producers have responded to the internationalisation of supply chains and the changing strategies of producers of clothing and footwear using various diversification strategies. Where the textile industry was in the past regarded as simply a processor of wool and cotton, it is now more closely identified as a supplier of a broad range of inputs to the latter stages of the TCF supply chain. Bruck Textiles, Bradmill and Melba Tex, for example, supply fabrics which are incorporated into high-end fashion garments and/or specialty industrial clothing sold domestically and in international markets.

Also, technological change (requiring investment in capital and R&D) has provided opportunities to develop new products in areas not traditionally regarded as part of the TCF sector. Specifically, a number of local firms have developed competitive advantages producing and/or using 'niche' technical textile products. Examples include Gale Pacific, which manufactures and exports shade cloth for domestic and commercial use, Textor which produces textiles for applications in the medical, automotive and building industries, Australian Defence Apparel which (among other things) manufactures bulletproof vests, Albany International which makes filtration materials and Kimberly Clark Australia which produces personal care products.

Changes in retailing have reinforced pressures for change

Another major development in the Australian TCF market has been the growing influence of retailers further up the supply chain. TCF retailing has become more concentrated with the larger department store operators — Coles Myer, David Jones, Woolworths and Best and Less — accounting for an increasing share of home textile, clothing and footwear sales. These firms now control some of their own supply chains, organise the manufacture of own brand (or private label) merchandise both here and abroad, as well as stocking brands controlled by local and overseas suppliers and manufacturers.

Greater concentration has also altered the relationship between retailers and their suppliers. Apart from the increased pressure on price, quality and response time that can be exerted by retailers, greater buying power has provided the scope for them to transfer some inventory and delivery risk up the supply chain.

In part, the pressure exerted on TCF producers reflects the extent of competition at the retail level. By way of example, consumer prices for clothing and footwear products have declined by 20 per cent in real terms over the last decade and a half despite the substantial depreciation of the A$ over this period. Producers of clothing and footwear, on the other hand, experienced a real price decline of just 2.5 per cent over this same period. While these divergent experiences would, to some extent, be explained by the shift into higher value products by local TCF manufacturers, lower retail margins may also have been a contributing factor.

In combination with the increased role of manufacturers in wholesale and import activity, the changing relationship between retailers and suppliers has also seen the distinction between different groups in the supply chain become more blurred. One consequence of this is that the interpretation of statistical trends is now more difficult. For example, as some TCF firms have shifted away from manufacturing (into say, distribution) as their *major* activity, they are no longer regarded (by the ABS) as part of the TCF manufacturing sector even though their operations may still involve some production activity. And as noted above, many micro-TCF businesses which manufacture and market their own products would be counted as part of the services sector (see sub. PP167 for some examples of these firms).

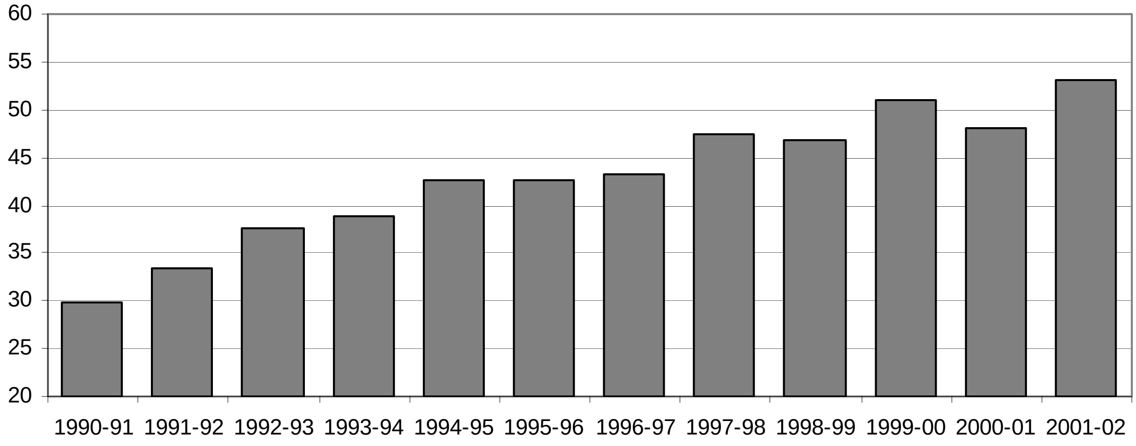
2.3 Impacts of recent changes

Aggregate output and employment have declined

Industry restructuring and rationalisation, in combination with a sharp rise in import penetration to more than 50 per cent of the total TCF market, have resulted in contractions in overall TCF manufacturing output and employment (see figure 2.1 and table 2.1). The sector's aggregate value added fell by more than 30 per cent in real terms between 1990-91 and 2001-02, while employment was approximately 35 per cent lower.

At the TCF industry level, clothing and footwear production has contracted the most with employment losses in these two industries accounting for 60 per cent of the decline in total sectoral employment since 1991 (though there may have been some offsetting increase in the number of outworkers — see chapter 10). This experience has coincided with a surge in imports of clothing and footwear, with China the main source. It supplied nearly 70 per cent of all Australia's imports of clothing and footwear in 2001-02 (see appendix figure B.1).

Figure 2.1 **Import share of the Australian TCF market, 1990-91 to 2001-02**
per cent



Data sources: ABS (2002b - for latest two years) and information supplied by DITR.

Moreover, many remaining firms are still 'at risk' with poor profitability detracting from their future prospects. While the emergence of new production activities (particularly in the technical textiles area) might conceivably see aggregate sectoral output increase in the future, output in some industry segments will almost certainly decline further. Any such contraction will reinforce the likely further decline in sectoral employment which will result from efforts by firms to increase productivity. That said, the significant amount of job shedding that has occurred over the last decade may limit the extent to which firms can use this strategy as a means to confront future competition. Thus, some firms suggested that future reductions in sectoral employment are likely to be smaller than those witnessed in recent years.

But many individual firms have prospered

While the TCF sector has contracted in aggregate, many firms are surviving and even flourishing by developing and exploiting competitive strengths in supplying differentiated products based on leading-edge technology, superior design and marketing attributes, high levels of productivity and/or a focus on customer service.

Table 2.1 **Australian TCF activity, selected measures**

$ billion (constant 2000-01 prices) and '000 persons

	1990-91	*1995-96*	*2001-02*	*% change 1990-91 to 1995-96*	*% change 1995-96 to 2001-02*
Value added	3.5	3.0	2.4	-15.0	-19.5
Exports[a]	0.4	1.1	0.9	177.1	-14.0
Imports	3.7	5.3	6.4	43.6	19.7

	May 1991	*May 1997*	*May 2003*	*% change May 1991 to May 1997*	*% change May 1997 to May 2003*
Employment	102.6	103.7	68.4	1.0	-34.0
Male	41.8	42.9	29.6	2.6	-31.0
Female	60.7	60.8	38.8	0.2	-36.2

[a] Excludes exports of scoured wool, tanned leather and dressed fur.

Sources: ABS (2002a), Labour Force Survey and TFIA (2002b).

Some of these firms have concentrated on servicing domestic market requirements. Others, however, have increasingly been looking toward overseas sales to maintain and expand their businesses. In some cases, firms have chosen to purchase or establish offshore operations to service international markets (for example, Gale Pacific and Billabong). In others, they have licensed their intellectual property (such as clothing designer and supplier Wildcard) and in yet others they have chosen to export directly from Australia (like denim cloth manufacturer Bradmill). Reflecting this more outward looking focus, exports as a share of total sectoral sales increased from just over 4 per cent in 1990-91 to around 14 per cent in 2000-01 (though export levels have since fallen, partly because of the cessation of the Import Credit Scheme — see appendix C).

Notably, individual firms have proved to be internationally competitive across many TCF activities with specific examples including: manchester, outdoor fabrics, industrial applications, fashion design, surfwear, carpets, geotextiles, specialist boots, knitting wools and nonwoven textiles. The reasons for success have been as varied as the products themselves, although most relate to some 'core strengths' becoming increasingly evident in the sector. These strengths are discussed in some detail in chapter 3.

Linkages within the sector have changed

One consequence of export growth, and the changing nature of TCF supply chains more generally, is that there is potentially less interdependence between domestic industry segments than in the past. As the Victorian Government's submission said:

> Today the TCF industry is in transition from its old domestically integrated supply chain structure to a new form. Increasingly, each sector is becoming its own stand-alone industry that imports, exports and services a diverse range of customers. (sub. 78, p. 2)

However, this is not to underplay the strong linkages that still exist in the sector, or to deny that there are benefits from having multiple customers and input suppliers. Indeed, many participants raised concerns about the ramifications for their activities of contraction in both upstream and downstream activities. Some commented that further offshore relocation of clothing manufacture would have major implications for textile plant viability and, in turn, for fibre suppliers. Others mentioned that the loss of volume in the local textile industry could undermine the viability of domestic chemical and machinery suppliers. The existence of some minimum production level below which the industry would collapse has, however, been questioned by some commentators (see chapter 3).

The changing nature of the sector has also increased the importance of linkages in other areas. In particular, the greater emphasis on higher value production and design activities has led to a strengthening of relationships between TCF producers and a number of educational and research institutions. The City of Geelong highlighted the importance of these linkages in noting:

> The Geelong TCFL industry has a strong relationship with local education and research institutions like the Gordon Institute of TAFE, Deakin University, CSIRO Textile and Fibre Technology and the International Fibre Centre. … These education and research institutions provide the local industry with staff training programs and state of the art research capabilities. They give industry the opportunity to form partnerships to facilitate the successful development of value adding opportunities. This type of development assists the industry to become more globally competitive. (sub. 16, p. 11)

There has been offsetting growth in TCF distribution activity

The changes to the sourcing and distribution strategies of both TCF manufacturers and retailers described earlier have served to partly offset the declines in manufacturing production and employment (see appendix table B.3). For example, employment in TCF wholesaling increased by 6300 persons (or 39 per cent) between 1991-92 and 1998-99 (the latest available data). The biggest employment gains occurred in wholesale clothing activity.

2.4 Further restructuring is inevitable

Improved productivity will help some firms remain viable

For some firms, productivity increases will provide a means to offset both global competitive pressures and future reductions in domestic assistance. This will often require investment in new plant and equipment, and R&D. While productivity growth across the entire sector is difficult to measure accurately (see box 2.2), there are many examples of strong productivity gains at the individual firm level which have helped those firms to cope with increasing competition. By way of example, J. Robins and Sons, while suggesting that its scope to improve productivity further was now limited, said:

> For the Robins group, our investment in people has had an excellent payback in terms of our strategic approach to the market. Our labour productivity per person has increased by 28% since 1991 … (sub. 34, p. 6)

More broadly, at the TCF industry level, the Footwear Manufacturers' Association of Australia commented that:

> … industry consolidation continues and we have achieved significant productivity gains over the 1990's. For example:
>
> - value added per employee has increased by 93%. (sub. PP132, p. 1)

And in the carpet industry, the Carpet Institute of Australia reported that:

> … there have been significant productivity gains at the broad industry level since 1997, with sales revenue per carpet manufacturing employee increasing by some 20% over the period. This is on the back of strong growth in overall employment since 1997 (up 14%…). (sub. 35, p. 17)

The Strategic Investment Program (SIP) is designed to encourage investment and R&D to enhance the sustainability and international competitiveness of TCF firms (see chapter 5). To the extent that the program is successful, it should lead to further productivity improvements in recipient firms. However, as discussed in chapter 5, the SIP has not as yet had any discernible effect on aggregate sectoral outcomes.

Box 2.2 TCF productivity performance

Productivity performance can be measured in several different ways. The most commonly cited indicators are trends in labour productivity, measured as output per unit of labour input (see the text for some specific TCF examples), and multifactor productivity which includes the influence of all factors of production, typically labour and physical capital, on output growth.

As part of its suite of work on productivity performance in the Australian economy, the Commission has estimated that since the mid-1980s measured labour productivity in the TCF sector has increased on average by around 2.5 per cent a year, while multifactor productivity has risen by 0.5 per cent a year.

While these measures can provide useful insights into trends in the efficiency with which inputs are used, they need to be interpreted cautiously. Improvements in labour productivity, for example, can result from influences not directly attributable to the more efficient use of a firm's workforce. Increased contracting out (such as through the use of outworkers in a TCF context), or the substitution of capital for labour, are two such influences.

Changes in the composition of output over time can also complicate productivity measurement. In this context, the restructuring and rationalisation which has occurred in the Australian TCF sector over the past decade and a half, has seen a shift away from the production of standardised commodities towards higher quality products embodying greater levels of innovation and design, and more technical features. In many cases, higher quality products have been sold at unchanged market price points. In these circumstances, the ABS estimate of TCF output would be the same even though the real value of that output has increased. As a result, more recent estimates of productivity change in the sector are likely to be understated.

Labour cost disadvantages mean that other firms are unlikely to survive

For some firms, even raising productivity to world's best practice levels would not enable them to overcome their labour cost disadvantages with developing country competitors. Wage rates in developing countries are a fraction of those in Australia (see chapter 3). While low productivity levels overseas have previously reduced total unit labour cost differentials, recent evidence suggests that the productivity of firms in countries such as China (the dominant source of Australia's clothing and footwear imports) often matches or comes close to best-practice developed country standards. Hence, in the standardised product and labour intensive parts of the Australian TCF sector, restructuring and rationalisation will continue regardless of the future assistance regime.

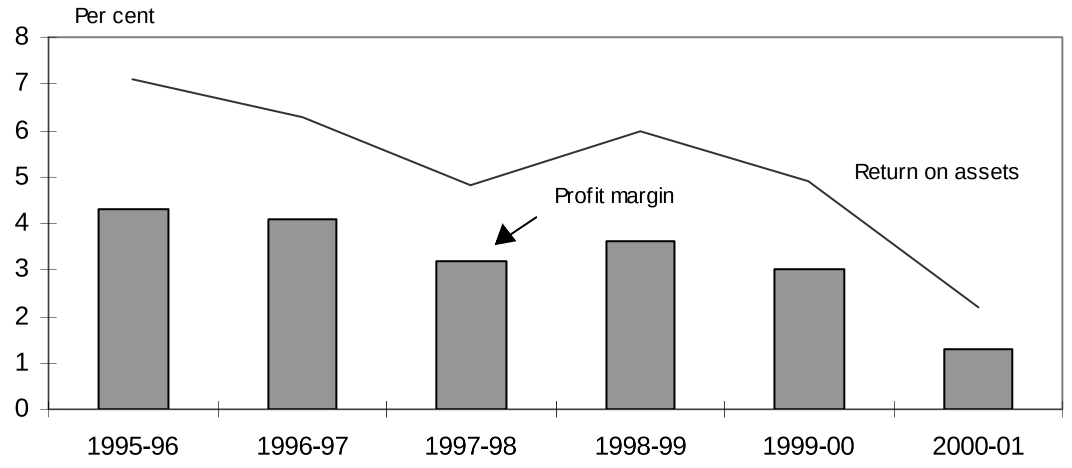
Poor profitability is indicative of the adjustment task ahead

Available estimates suggest that profits as a share of sector-wide sales have declined since the mid-1990s to just 1.3 per cent in 2000-01 (see figure 2.2). Similarly, the sectoral average pre-tax rate of return on assets (a more accurate indicator of firm sustainability) has fallen from around 7 per cent in 1995-96 to just over 2 per cent in 2000-01. This latter figure was one third of the average return on assets for manufacturing as a whole. Those sector-wide trends are indicative of the intense competitive pressures confronting firms, as well as the considerable excess capacity in parts of the sector which is inflating unit costs.

Of course, some firms are doing much better. One told the Commission that its return on assets was above 40 per cent. Others suggested that while their profits are low at present, the effect of recent restructuring and investment initiatives should flow through to higher sales and profit levels in the future.

On the other hand, many firms are recording negative returns, with some appropriately characterised as 'barely hanging on'. Some of these firms continue to operate only because of the high costs of exiting the sector. For example, the Commission was told that substantial redundancy entitlements (see chapters 4 and 10) and the cost of site rehabilitation (in some plants) are delaying the closure of unprofitable production activities. The poor profitability of many firms provides evidence of the adjustment task that still lies ahead.

Figure 2.2 **Profitability in the TCF sector, 1995-96 to 2000-01**
per cent



Note: Profit margin is measured as operating profit before tax as a percentage of operating income. Return on assets is measured as pre-tax profits as a percentage of the total value of assets.

Data source: ABS (2002b).

2.5 Changes in the sector have a range of policy implications

The wide and growing range of outputs, and variations in the underlying international competitiveness of individual TCF industries, suggest the need for an assistance package which recognises this diversity. The blurring of boundaries between manufacturing and other TCF related activities poses further challenges because some activities of TCF manufacturers now lie outside the traditional focus of assistance policy.

The inevitability of further change in the sector also focuses policy attention on adjustment issues. These have long been a central consideration in the formulation of TCF assistance policy and will be no less important in the future. Accordingly the ability of firms, employees and TCF dependent communities to cope with further restructuring is at the forefront of the Commission’s consideration of post 2005 assistance options.

3 Prospects

TCF firms in all developed countries are facing strong competitive pressures. High labour costs compared with those in developing countries; global excess capacity in many TCF products (placing downward pressure on prices and reducing profit margins); declining government assistance; strategic positions apparently being taken by developing countries such as China; changing consumer spending patterns; technological change; the increasing stringency of environmental regulation affecting certain TCF products; and more stringent labour laws designed to promote better treatment of TCF workers; have combined to substantially alter the TCF business environment.

To survive, firms are being forced to change both their methods of operation and the types of products they supply. In particular, production of standardised, labour intensive clothing and footwear products is increasingly migrating to developing countries. Highlighting the fact that Australia is not alone in facing these pressures, the recent TCFL Market Access Study noted:

> It is clear that no developed economy, even countries that have been consolidating their position in the international market … can escape the contraction in local textile and garment production. Further trade liberalisation will only accelerate the decline of local apparel production. Australia is no exception to this. (Werner International 2003, p. 9)

In the face of these broad pressures, and with further reductions in government support for Australian TCF producers legislated to occur in 2005, parts of the sector will continue to contract. At the very least, there is general consensus that efforts by firms to address increased competition by improving productivity will inevitably reduce Australia's TCF workforce.

Nevertheless, the prospects for Australian producers in particular market segments are quite positive. Information from participants indicates that a range of opportunities exist or are likely to emerge in domestic and export markets. Even in market segments where the outlook is less optimistic, there will be niche opportunities for individual firms able to satisfy particular customer requirements.

Such varying prospects illustrate both the diverse nature of Australian TCF activity and the strengths that individual firms have developed in responding to the challenges in increasingly competitive markets. Nevertheless, competition from low-wage production centres and some 'external' impediments will inhibit future prospects.

A detailed assessment of the prospects for each and every segment of the TCF sector is beyond the scope of this inquiry. Recent reports on the sector by the TCFL Forum and others have already provided a solid foundation in this regard. The Commission has sought to synthesise some key themes and messages from those studies and from the input of participants to this inquiry, with a view to establishing an agenda of issues that will need to be addressed by the sector and by governments to assist firms to make the most of future opportunities.

3.1 Global pressures are forcing change

Labour cost differentials are a major influence

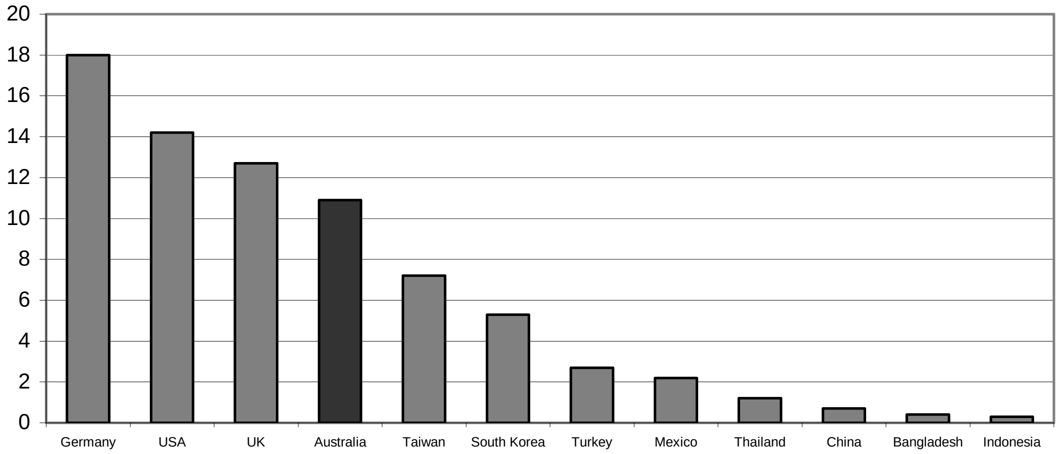
With labour costs accounting for 40 per cent of textile production costs and 60 per cent of clothing and some footwear production costs (ILO 2000), labour intensive elements of production are relocating to developing countries to take advantage of much lower wage rates.

Hourly wage comparisons paint a stark picture (see figure 3.1). In Germany, the United States and the United Kingdom, textile labour costs range from US$12 – 18 per hour, while in Australia they are around US$11 per hour. In China, hourly wages are around US$0.70 and in countries such as Bangladesh, Pakistan and Indonesia they are even lower. With productivity in developing countries such as China growing rapidly and often matching that in best practice developed countries, any offsetting influence on total labour costs has greatly diminished and in some cases disappeared.

Incentives for firms to relocate have been strengthened by the existence of often substantial trade barriers in developing countries that reduce the scope to supply those markets through exports (see chapter 11 and appendix D) and by advances in technology, communications and transport logistics. The upshot of this relocation of production is that developing countries (especially in Asia) now supply more than half of the world's clothing, 40 per cent of its textiles and one quarter of its footwear (ILO 2000).

Figure 3.1 **Labour cost comparisons in the textile industry, selected countries, 2000-01**

US$ per hour



Data sources: Textiles Intelligence (2002) and Werner International (cited in submission no. 44).

Slow growth in consumer demand has exacerbated supply side pressures

Intensifying competition from developing country producers is occurring at the same time as demand for TCF products in developed countries is slowing. Consumers in developed countries have been spending a declining share of their household budgets on TCF products for several decades. This trend results from several changes including: declining relative prices for clothing and footwear products (see chapter 2 for the Australian experience); increased consumption of services as incomes rise; and changing demographics. Australia has not been immune to this international trend and, in fact, had one of the lowest TCF consumption shares among developed countries in 2000 (see appendix table B.4).

Producers in developed countries have responded in variety of ways

As well as relocating labour intensive components of their manufacturing operations, TCF firms in developed countries have responded to these pressures using a range of strategies including: investment in labour saving technologies to lower domestic production costs (resulting in further job losses); pursuit of economies of scale through mergers and acquisitions; and initiatives to raise efficiency, quality and labour productivity. There has also been a notable trend toward higher value added activities based on design, marketing, customer service and brand management (see box 3.1).

Box 3.1 **Some recent business trends in the global TCF market**

In recent years, a number of specific responses to the changing international environment have been observed in TCF enterprises.

- There has been an unprecedented increase in mergers and acquisitions — trebling in Europe in the three years to 2001 — among firms up and down the supply chain (Stengg 2001). In consequence, there has been a blurring of traditional boundaries between activities as manufacturing firms move into distribution. This has been more common in the clothing sector than in textiles; and increasingly evident in medium sized companies which have been acquiring firms in the same market segment (larger firms have tended to make acquisitions in downstream or upstream parts of the supply chain). These changes have been driven by the need to increase the return on investment in existing brands and distribution networks.
- An increasing number of firms have also attempted to exploit the so-called 'fashion system' by which a well known brand name in another sector is acquired and then used to increase the return on investment in TCF products.
- Another trend has been for luxury and up-market clothing manufacturers to diversify into accessories such as jewellery and eyewear. And a shift into the corporate apparel market and customer inventory management are examples of diversification into service activities.
- Traditionally, TCF products were sold to small and medium sized retailers by wholesalers. Distribution in most developed countries is now undertaken by a small number of large retailers who exert considerable pressure on suppliers in terms of price, quality and delivery performance. As a result, the supply chain has changed from being 'industry' driven to 'customer' driven.
- The proliferation of preferential trade agreements has encouraged offshore processing centres to reduce the costs of supplying developed country markets. This has resulted in a more diverse set of supply chains. Examples of these offshore arrangements include Mexico and Caribbean countries supplying the US market, countries in Eastern Europe supplying the EU and, until recently, Fiji being a major supply source for the Australian market.

3.2 A range of new opportunities will emerge

Restructuring and rationalisation have characterised the Australian TCF experience over the past decade and a half. Many firms have left the sector and a considerable number still in operation remain 'at-risk'. Others, however, have been able to adapt successfully to the increasingly trade-exposed environment.

For firms that have adapted successfully, or which are capable of doing so, new opportunities will arise in coming years. As well as the emergence of markets for new products and services, the removal or relaxation of overseas trade barriers should provide opportunities to expand sales in existing product lines (although it will also pose some threats). As the TCFL Forum reported, many of these new opportunities involve building on existing activities and competencies rather than doing something completely new:

> … the new market opportunities for the TCFL industry are more about reinventing ‘old’ products, new approaches to ‘old’ markets and new competitive paradigms for ‘old’ businesses than they are about entirely new products or new markets. (TCFL Forum 2002, p. 8)

Several general characteristics can be identified

The Commission’s discussions with the industry and submissions to the inquiry have identified a variety of specific product opportunities that are likely to either emerge or continue to be relevant to the future success of Australian TCF firms (see box 3.2). Some of the general characteristics of these opportunities include:

- the ability to provide rapid turnaround for short-run orders. Quick response fabric production and garment assembly are the most commonly cited examples, although participants identified such opportunities in several market segments. Offshore sourcing of these sorts of requirements is in fact becoming more feasible. Minimum production runs in Asia have declined; some firms have examined the possibility of locating their warehousing facilities offshore; and airfreighting imported fabric and apparel has become a viable option (although it is seemingly little practised at present). However, the general consensus is that quick turnaround requirements will provide the basis for a significant level of local manufacturing in years to come;

- activities where physical proximity to the customer is important. As the preceding discussion makes clear, proximity to the customer is likely to be an advantage in securing quick turnaround business. But proximity to the customer can be important in a number of other contexts. These include the supply of more complex products where the designer and manufacturer need to be in close contact, vendor-managed inventories (see below) and ‘just-in-time’ supply to the automotive industry;

Box 3.2 Emerging or continuing product opportunities for Australian TCF firms

In terms of specific products, emerging or continuing opportunities identified by participants include:

- lightly processed raw materials (eg wet blue hides, scoured wool);
- wool based products such as carpets and knitting wool for home use;
- specialist nonwoven fabrics for use in medical and sanitary applications;
- industrial textiles, defined to include products such as shade cloth, filter fabrics and geotextiles, often using nonwoven fabrics;
- supply to the automotive industry;
- surf wear and 'wearable' art where cultural recognition is a marketing factor;
- quick response fashion garments and fabric for those garments;
- complex, high fashion low-volume garment production, where proximity of the fabric provider to the Australian designer/producer and brand recognition is important. For example, in commenting on local 'ready-to-wear' designers, Australia Fashion Innovators said:

  > It is the sector in the industry that is looking to generate a premium at retail for their products, given recognition of their brand profile, and many in the industry believe that this is the sector that has the opportunity to actually … be able to support Australian labour content … (trans., p. 435);

- products with well recognised brands where a local manufacturer is more likely to be able to maintain a market position through both the brand premium and competitive total 'end-to-end' costs, even if local manufacture is more expensive than sourcing offshore;
- niche fabric and garment/footwear production such as defence apparel, fire retardant clothing, coated furnishing products and industrial footwear, where Australian firms have developed expertise; and
- the corporate apparel market where service is an important part of the product offering and where 'buy local' policies sometimes provide an additional measure of support.

- scope to combine a service with the physical product to establish a local advantage. As well as 'after-sales' services for the corporate apparel market, local manufacturers are providing inventory management (or 'stock services') for retailers in areas such as towels, men's suits and fabric production. Vendor-managed inventory offers a range of benefits to retailers including quick response to changes in consumer preferences and cost savings through fewer product returns and lower average inventory holdings. Developments in information technology will extend opportunities for this sort of service provision in the future. A February 2002 study cited by Australian Business Limited (sub. 98, p. 12) found that more than 65 per cent of surveyed TCF firms offered at least one service additional to their standard product range;

- the creation of competitive advantage through differentiated technologies, design, branding or marketing, or other forms of embodied intellectual capital. (However, manufacture in Australia is not necessary to realise many of these opportunities — even though it may be efficient in some circumstances — and it may even reduce returns to firms if labour cost disadvantages are not offset by other factors);

- activities with a degree of natural protection because of specific Australian market requirements. Examples include work boots which meet Australian safety standards and woollen carpets that suit Australian preferences;

- activities where proximity to raw material suppliers can provide a basis for competitive supply (for example, cotton, wool scouring and top manufacturing and early stage leather tanning). Traditionally this has been seen as giving Australia an inherent competitive advantage, but access by itself does not guarantee an advantage when offshore operators can buy the same products at similar prices; and/or

- capacity to draw on international linkages providing advantageous access to inputs, the latest technologies and market information which in turn facilitate the development of new products, markets and exports. Indeed, it is unlikely in this increasingly globalising sector that firms will become internationally competitive unless they are constantly abreast of international developments and able to take advantage of them.

Export markets offer a broader range of opportunities

Strong growth in imports in combination with only modest growth in overall demand in the domestic market implies that, for many firms, exporting will be important to secure their future viability. There has already been export growth over the past decade, though some of this growth was dependent on the now defunct Import Credit Scheme (see appendix C). As a result, export growth has stalled in recent years (see chapter 2).

Future opportunities in export markets will be based on similar characteristics to those underpinning opportunities in the domestic market. For example:

- competitively priced and readily available raw materials;

- differentiated technologies;
- marketing advantages from an identification with Australian culture;
- a strong domestic production base (sometimes linked with global players) providing opportunities to leverage international sales. Custom-made woven wool carpets and military garment manufacture are cases in point; and
- the capacity to satisfy low-volume niche products requiring quick response supply.

Other opportunities are likely to be available for the provision of services such as design, and education and training, and for the licensing of technology or established brand names. For example, the TCF Resource Centre of Western Australia commented:

> Australia is design rich, it is technology rich, and it is fresh, lively and innovative, and the rest of the world wants that in their products. (trans., p. 276)

The link between domestic and export opportunities suggests that exports can be a natural transition for firms operating successfully in the Australian market.

Removal of EU and US textile and clothing quotas may create new export opportunities

The prospective elimination of all textile and clothing quotas under the WTO Agreement on Textiles and Clothing (ATC) will affect global patterns of TCF production and trade after 2005 (though the extent of these impacts will partly depend on the degree to which 'safeguard' measures are invoked). China — already the world's leading exporter of textile and clothing products — is expected to derive the greatest benefit from its capacity to provide cost competitive products across the entire TCF commodity range. As well as displacing domestic suppliers in the United States and EU markets, increased Chinese exports will come at the expense of some of the other developing countries currently supplying these markets.

Such developments should, in time, have implications for the Australian TCF sector. There is some concern that a re-direction of products by those developing country suppliers that will be displaced from the US and EU markets may make it more difficult for Australian firms selling in other export markets and may also increase import competition in the domestic market. However, any effects are likely to be primarily in standardised labour intensive products where Australian growth prospects are limited anyway. On the other hand, growth in developing country finished product exports to the US and EU may offer opportunities for Australian intermediate suppliers of wool, cotton, leather, fabrics etc.

As would reductions in tariffs and other trade barriers

A variety of sometimes high tariff and non-tariff barriers presently directly constrain the export activity of some Australian TCF firms (see appendix D). A number of multilateral initiatives are currently underway, with the Doha Round of WTO trade negotiations and APEC being the two most notable examples. There is clearly scepticism in parts of the TCF sector about the degree to which these fora will be successful in reducing trade barriers. Godfrey Hirst, for example, said:

> Looking forward, it is possible that there will be reductions in tariffs as a result of the Doha Round. However the policy of the world's leading players such as the United States of America to make any reductions conditional on being linked and reciprocated means that unilateral unconditional reductions of benefit to the Australian carpet industry are unlikely to occur. (sub. 77, p. 9)

This view was not universal, however, with other participants more optimistic about the additional export opportunities that WTO and APEC processes are likely to provide to the Australian TCF sector. For example, the Technical Textiles and Nonwoven Association (TTNA) commented that:

> … the Australian technical and nonwoven industries' fortunes will be greatly enhanced by the realisation of the WTO's intentions that would provide greater market access to other markets. (sub. 68, p. 8)

Similarly, the Commonwealth Department of Agriculture, Fisheries and Forestry (sub. PP176) suggested that China's accession to the WTO could lead to increased exports of Australian textile fibres (though it noted that use of safeguards and other adjustment measures in China's export markets could limit that increase).

Mooted free trade agreements may benefit some TCF producers

New opportunities could also arise from a free trade agreement (FTA) with the United States — currently being negotiated. Some analysts have suggested that these opportunities would be modest (see, for example, ACIL-Tasman 2003). Conversely, a recent study by the Centre for International Economics (CIE 2001) estimated that an agreement with the United States could provide a major boost to Australian TCF exporters. This latter view was mirrored by several participants. Specialty Coatings Australia said:

> Although The Specialty Group's export sales have declined in the last two years … we are encouraged by the commencement of FTA negotiations between Australia and the

> United States, as this offers to open up significant market access opportunities … (sub. 79, p. 4)

And the Victorian Government commented:

> To date, the Australian Government has signed a free trade agreement with Singapore, commenced negotiations with the US and announced negotiations with Thailand, Japan and China. Through such agreements, particularly with large TCF players such as the US, Thailand and China, Australia has a great opportunity to improve export market access for the TCF industry. (sub. 78, p. 9)

However, it is important to recognise that while prospective FTAs may benefit some Australian TCF exporters, other firms could be disadvantaged by such arrangements. Australian carpet manufacturers, for example, were concerned with the risks inherent in an agreement with the United States. In responding to the Position Paper, Godfrey Hirst said:

> At the industry level, there is a need for effective safeguards to prevent the Australian market being swamped by imported carpet. (sub. PP129, p. 2)

The potential effects of proposed FTAs at the economy-wide level and on the TCF sector will also depend critically on the rules of origin and safeguard measures negotiated in the agreements. For example, there is some concern among Australian TCF producers that a free trade agreement with Thailand could see that country used as a conduit for Chinese product seeking to gain duty free access to Australia. These issues are discussed further in chapter 11.

3.3 The Australian TCF sector is developing important strengths

General features of the Australian economy provide a platform for parts of the sector to remain viable or attain that goal. These include the stable business climate, good basic physical infrastructure and education systems, and domestic access to basic raw material inputs necessary for TCF production.

Flexibility, innovation, customer focus, branding and a commitment to performance improvement are increasingly evident

Successful firms within the TCF sector also have specific strengths which enhance their ability to compete against overseas suppliers in the domestic and export markets. These strengths typically relate to flexibility in adapting products and processes to meet market requirements; a focus on identifying and meeting the needs of customers; a demonstrated capacity to service quick turnaround orders;

skills in using branding to develop and sustain markets; innovativeness (including the development of niche products); and a commitment to productivity and quality enhancement. The case study provided by Specialty Coatings Australia provides a specific example of how these sorts of factors have allowed some firms to successfully meet the challenges of a more competitive market environment (see box 3.3).

Box 3.3 **Success factors for Specialty Coatings Australia**

Specialty Coatings Australia described its business strategy in the following way.

> The company's recent success can be attributed to our conscious pursuit of, and focus on, both short-term and long term strategies including:
>
> - reducing fixed manufacturing and overhead expenses.
> - ensuring satisfactory reporting systems are established.
> - providing our customers with a quality product, in a timely fashion, at a competitive price that is also profitable for the company. Maximising customer service, by adding value at every stage of the selling, production and distribution process.
> - extending existing and developing new (export) markets by focusing on new product development geared around high technology, high value add applications.
> - pursuing growth opportunities in the safety workwear, window furnishings and industrial markets and consolidating the military market, which is looking to move towards laminated textiles.
> - establishment of strategic alliances with key customers, suppliers, research organisations and educational institutions, to develop high performance products such as laminates and advanced coated and breathable industrial products.
> - a commitment to innovation, focused on high performance/ high technology product (specifically technical textiles), underscored by a continued heavy investment in research and development and product development for commercialisation.
> - ongoing market research to identify world trends and pre-empt Australian moves.
> - shifting production towards specialised high value added product rather than concentrating on the commodity end.

Source: (sub. 79, p.3).

More broadly, the TCF sector's increasingly skilled and flexible workforce is contributing to the success of many firms (though in the latter case it is clear that further improvement is possible as well as desirable — see below). Skill development has, in turn, been enhanced by links to research, education and training bodies that have increased the availability of design, technological, brand support and marketing skills needed to develop innovative products sold to high value market segments (see chapter 10).

Examples of participants' views on firm specific and broader strengths are provided in box 3.4.

Box 3.4 Participants' views on strengths

Flexibility/Quick response

Quick response is a key non-price advantage for local supply in a retail market place seeking shorter and shorter lead times. … Further developments are underway to increase these opportunities to better service fast turnaround demand through local supply lines. (sub. 72, p. 3) *Pacific Brands*

… through local manufacturing … Defab is able to offer customers a wide spectrum of potential fabric applications because it produces innovative and effective solutions efficiently and can respond to changing market demand quickly. (sub. 65, p. 2) *Defab Weavers*

… Australian industry players will be primarily niche and ultra niche players whose competitive advantage will be quality and certainty of supply to an international market on time and with short lead-times. (sub. 32, p. 8) *Australian Association of Leather Industries*

Branding

One of the key determinants for long-term viability in the garment industry is 'brand equity'. Pacific Brands' whole 'modus operandi' is based on the premise that without strong brand equity matched with new product development, major retailers have no reason to source through local suppliers and will increasingly reduce their costs through direct retailer imports. (sub. 72, p. 3) *Pacific Brands*

Quality, design and innovation

Australia is amongst the world's best designers and producers of specialty performance and technical textiles, which is undeniably the growth area in the international textile industry. …

The FAI members have sustainable competitive advantages in the following areas:

- High quality
- High level of production expertise
- Production flexibility
- Innovation in raw material processing, yarn and fabrics development, design, quality control and dyeing & finishing techniques. (sub. 70, p. 10) *Fabrics Australia Inc.*

Services

The Yakka philosophy of building quality into its product and then marketing a total service package so that end-users know that they can depend on product quality and reliability has meant that price is not the prime determinant in gaining sales. (sub. 31, p. 5) *Yakka*

Education and research linkages

The Geelong TCFL industry has a strong relationship with local education and research institutions like the Gordon Institute of TAFE, Deakin University, CSIRO Textile and Fibre Technology and the International Fibre Centre. … These … institutions provide the local industry with staff training programs and state of the art research capabilities. They give industry the opportunity to form partnerships to facilitate the successful development of value adding opportunities. This type of development assists the industry to become more globally competitive. (sub. 16, p. 11) *City of Geelong*

3.4 But the sector also has weaknesses

As mentioned earlier, TCF firms in most developed countries are facing pressures on both the supply and demand sides of their operations. High labour costs, shrinking margins, slowing demand growth, and technological and regulatory developments all require new and innovative strategies by firms to survive.

Labour cost disadvantages inhibit growth prospects

While labour cost disadvantages can be offset by productivity increases, the general view is that there is now little productivity difference between Australian suppliers and many suppliers in China (the main source of import competition). Similarly, productivity in other developing countries is improving. As previously noted, this implies that labour intensive production of standardised commodities is unlikely to be viable in Australia in the medium term. Indeed, as in other developed countries, this productivity/wage cost equation has already caused the substantial migration of labour intensive production offshore.

Labour cost differences are, of course, an inherent feature of the global TCF operating environment and not something that government policy intervention should seek to offset. Rather, government policy settings should provide a supportive general business climate and facilitate adjustment into activities where labour costs are less important and where Australia has other advantages. As a wide cross-section of participants acknowledged, there is little if any benefit for the sector, its employees, or the Australian economy of seeking to preserve otherwise undifferentiated and uncompetitive labour intensive production activities.

Lack of scale and fragmentation of the domestic supply chain increases costs

Low volume production sometimes facilitates flexibility and quick response, and can be an asset in niche product markets. Also, in some of the areas in which the sector's best opportunities lie, the unit cost penalties from low production runs are not all that large.

However, low scale/small firm size is much more disadvantageous in capital intensive activities. The resulting cost penalties can be particularly significant where several small producers compete to supply the small domestic market. The unit cost savings available from increased volume have underpinned rationalisation in a number of industry segments.

Lack of scale can also: reduce the opportunity for managerial specialisation; limit access to finance (resulting in under-capitalised operations); make it more difficult to cover the initial fixed costs of exporting and to access training packages and government support programs such as the SIP; and preclude the sort of workplace flexibility that can be achieved under the best enterprise bargaining agreements (although it should be noted that while small firms may not have negotiated a formal EBA this does not mean that they cannot improve their flexibility through informal means).

Fragmentation/small size also disadvantages some suppliers when dealing with the large retail chains. According to suppliers, imbalance in bargaining power (and lack of skills among buyers) sometimes leads to retail purchasing decisions that are inimical to the local industries' future. Previous reports have identified the need for more cooperation between retailers and suppliers, including through sharing information relevant to demand forecasting and inventory management.

Increased scale/firm size in the domestic TCF manufacturing sector should enhance the scope for more sophisticated information and technology linkages with customers, as well as improving firms' marketing and negotiation skills. Relationships between retailers and suppliers are discussed further in chapter 11.

Aspects of workplace arrangements are impeding performance improvement

Improvements in workplace flexibility have been evident across the local TCF sector over the past decade with many, though not all, participants quite positive about their workplace arrangements.

However, there is evidence of continuing inflexibility in some workplace arrangements, including restrictive shift patterns and obstacles to the use of casual employees to cater for peaks in demand. As noted above, in parts of the sector, small firm size may limit the use of EBAs as a vehicle to overcome such inflexibilities. There were also claims that confrontational attitudes in the workplace are an impediment to improving flexibility. For example, Victoria Carpets commented on a reduction in its operating flexibility caused by a change in shift arrangements:

> Union demands and intransigence demonstrate there is very little evidence of any co-operation or understanding of the need to have competitive workplaces. This has worsened in recent years. Last year we discontinued a permanent week-end shift at our Castlemaine mill, due in part to the obstacles and difficulties constantly presented by the union. We now operate at week-ends on overtime rates. (sub. 86, p. 3)

Similarly, while industrial disputation has not been a widespread problem in the sector, recently it has caused significant disruption in the carpet industry in Victoria. There are some concerns that the trigger for these disputes — the issue of employee entitlements — could be the source of costly disputation elsewhere in the sector.

Several firms also indicated that concern about the security of employee entitlements has contributed to an emphasis in their workplace negotiations on redundancy matters rather than on developing workplace arrangements which would enable their businesses to survive and prosper. Some firm-specific ‘solutions’ to guarantee employee entitlements have been expensive.

Moreover, the inability of some firms to meet previously negotiated and accrued entitlements has become a barrier to them exiting the sector. Their continued operation in turn helps to maintain negative perceptions about TCF activity, making it more difficult for those firms with a future to access finance, develop new markets and attract talented staff.

Of course, these costs and workplace problems are not unique to the TCF sector. For this reason, some have suggested that further general policy responses are required to deliver more effective workplace outcomes across the economy as a whole (see chapter 10).

Characteristics of the TCF workforce can reduce labour mobility

The characteristics of the TCF workforce suggest that many employees could find it difficult to secure alternative employment. This is likely to increase the economic and social costs associated with further downsizing and restructuring in the sector. As discussed at length in chapter 4, educational attainment levels are often low, skills are frequently basic and sector-specific, and employees are more likely to be older, female, married and less proficient in speaking English than in other parts of the workforce. A less mobile workforce also means that growing and emerging firms could have some difficulty in attracting employees best suited to their needs.

Other weaknesses include …

- There is evidence of some skill gaps and shortages in several areas including; human resource and financial skills in middle and upper management; specialist sewing machinists (capable of working with designers); textile production workers; tanners and fabric cutters. However, given the relatively basic skill requirements for much of the sector’s activities and the scope for ‘on-the-job’ training, skill deficiencies may not be as important as in some other sectors. Skilling issues are considered in more detail in chapter 10.

- There is a dependency culture in some parts of the TCF sector, that it is up to government to support domestic activity by any means necessary, including through high levels of protection. This culture impedes the drive to confront change required to improve firm viability, whether through improved efficiency, lower costs, increased investment, innovation or pursuit of export opportunities.
- An incomplete statistical platform (particularly in relation to outworkers and very small TCF businesses) makes some aspects of policy making more difficult.

Examples of participants' views on weaknesses and other impediments to their longer term viability are provided in box 3.5.

3.5 TCF firms face a range of threats

As well as the intrinsic weaknesses that detract from performance, various external factors threaten the future viability of parts of the sector.

The competitiveness of developing country producers will continue to improve

The traditional role of TCF manufacturing in the economic development of poorer countries indicates that competition from new low-wage production centres will be a continuing feature of the global TCF industry. The latest manifestation is occurring in countries such as Bangladesh, Pakistan and Vietnam, where labour costs are half those in China. As productivity in these countries improves, there is the distinct possibility that they will take market share from Australian firms in both domestic and export markets, particularly at the commodity end of the production spectrum. Also, as some participants noted, as of July 1 this year least developed countries such as Bangladesh have had duty free access to the Australian market. This has raised a related concern regarding the consequences for Australian TCF firms of rules of origin clauses in this and other tariff preference arrangements (see chapter 11).

Box 3.5 **Participants' views on weaknesses and other impediments**

Lack of scale

The small domestic market creates scale disadvantages for Australian manufacturers. In addition, the market is diverse in terms of consumer taste and fibre preference, and this further constrains production run size. (sub. 35, p. 15) *Carpet Institute of Australia*

… the TCF industry is comprised mostly of small companies. Many small firms do not have the individual resources to make large capital outlays (eg computer pattern making systems). Many technical areas of the industry are still operated manually – this is inefficient. (sub. 82, p. 8) *Fashion Technicians Association Australia*

Workplace flexibility

Employers and the various components of the labour force (employees and unions) must understand that in a low tariff environment the workforce must be prepared to accept change. The opportunity to prosper behind a tariff barrier is gone and there will be no industry, and hence no jobs, unless all players accept the need for change and move to an internationally competitive position. (sub. 80, p. 8) *Feltex Australia*

Industrial disputation

Feltex experienced a costly industrial dispute in 2001 which closed its operations for 6 – 8 weeks. Feltex believes that an adverse industrial relations environment will negatively impact investment decisions … strong legislative measures are needed to provide a stable business environment. (sub. 80, p. 8) *Feltex Australia*

Low wage production centres

It matters little whatever assistance is given the footwear industry by way of tariffs, because production would not be competitive against low cost imports, particularly from China (sub. 27, p. 4) *Sporting Footwear Importers Group*

Entitlements

Australia's high redundancy costs by world standards exaggerates the consequences of long-term viability decisions. In small firms this may lead to delayed adjustment followed by bankruptcy. … Redundancy payments form one of the largest costs in rationalisation and structural improvements to existing operations. (sub. 72, p. 3) *Pacific Brands*

The cost of closing a business with redundancy and long service leave payments is so great that many companies cannot afford to close. (sub. 51, p. 5) *Melbourne Textile Knitting*

Skill shortages and training

The shortage of skills and the inability of firms to attract sufficient numbers of top quality young people into the textiles industry act as major barriers to growth, particularly in regional areas. By way of example, companies contributing to this submission noted that it was difficult to employ laboratory assistants in the Albury-Wodonga area. (sub. 68, p. 13) *Technical Textiles and Nonwoven Association*

Skill shortages exist in a number of areas including sewing machinists, textile production workers and tanners. … Vocational education and training programs in secondary schools should give young [people] greater career alternatives that include TCF&L. (sub. 36, p. 2) *Queensland Light Manufacturing and Industry Training Centre*

The growth in new production centres, together with China's apparent determination to take a strategic position across most elements of the TCF supply chain, indicates that global excess capacity and low profit margins will persist in the TCF business environment for some time to come. 'Dumping' of this excess capacity may also occur from time to time, further increasing the competitive pressure on domestic TCF firms (see chapter 11).

Many firms are sensitive to exchange rate changes

The low value of the Australian dollar in recent years has shielded local TCF firms from some of the adjustment pressures that tariff reductions and global influences would otherwise have brought to bear. Over the year to July 2003, however, the currency has appreciated by around 20 per cent against the US dollar and 15 per cent against the trade weighted index. Many firms indicated that this recent (or any further) appreciation of the Australian dollar threatens their viability. Indeed, for some, the appreciation of the currency was of more concern than tariff reductions.

An appreciating currency will, of course, also reduce the cost of imported inputs (including capital equipment). More broadly, exchange rate variability has been a feature of the general Australian business environment since the A$ was floated in March 1983. It is therefore something that firms in all parts of the economy have to manage.

Contraction in parts of the supply base could raise critical mass concerns

A prominent theme in submissions was that a contraction in parts of the supply chain below a level considered to form a 'critical mass' would put at risk other parts of the supply chain. For example, further contraction in domestic clothing production was seen as threatening textile and yarn production, while continuing contraction in footwear manufacture was argued to be jeopardising leather suppliers. Conversely, there was concern that reduced production of certain yarns and other raw material inputs could put some downstream activities at risk. In this context, it was suggested that it is both difficult and costly to source imported yarns in low volume batches.

Participants also said that a contraction in TCF activity could have implications for the cost and availability of inputs and services sourced from outside the sector. For example, concerns were raised that:

- reduced demand for specialist textile machinery and chemical inputs (such as dyes) could raise costs and/or reduce efficient supply or service options for remaining users of these inputs; and
- a contracting TCF manufacturing base would undermine current linkages between the sector and research and education institutions, as well as spreading the cost of external skills development more thinly.

However, a recent review of the Australian circular knitted fabric sector suggested that critical mass concerns may be overstated, with the reviewers commenting:

> During industry forums the industry made it clear that it believed that there was a critical mass of about 444 [tonnes per week production level] and that if the industry dropped below this level it would implode. However, DRA believe that the Australian industry will respond to what the local market demands, whatever size this market is. The Western European experience has shown that despite the massive falls in production a much smaller and leaner industry has emerged, often involving new owners. (David Rigby Associates 2003, p. 2)

Moreover, supply interdependencies arise in all parts of the economy. It is far from clear that interdependence and the associated critical mass issues in the TCF sector are any more significant than elsewhere. Also, as noted above, increased import and export activity have reduced interdependencies within the Australian TCF supply chain. This is not to deny that contraction in particular parts of the TCF supply base (eg clothing) would have adverse flow-on effects for firms in other areas. However, it is unlikely that there are sudden discontinuities at the industry or sectoral level.

Other potential threats for local TCF suppliers include …

- Delays in securing better access to overseas markets, although it is important not to overstate the benefits that this would bring to the sector as a whole (see chapter 11). Some participants also considered that ‘natural barriers’ such as distance from export markets are a threat to the sector’s future viability. However, as others acknowledged, those same natural barriers can also reduce import competition. For example, local tastes for carpets in Australia provide some cushion from overseas competition.
- The emergence of new technology that leads to rapid asset and technology redundancy (especially in areas such as technical textiles).
- Inflated operating costs arising from inefficient solutions to the employee entitlements issue.
- Increased involvement of retailers in upstream elements of the supply chain.

- Costs associated with the failure to pursue microeconomic and taxation reform.
- Risks for wool processors of continued increases in fibre substitution toward synthetics.
- Uncertainty about future policy settings for the industry.

Examples of participants' views on threats are provided in box 3.6.

3.6 What are the implications?

Contrary to perceptions in some quarters, it is inappropriate to categorise the TCF sector as being in terminal decline. Prospects in particular activities are quite strong and some firms and industry associations are optimistic about their future, even though they face increasing global competition and lower protection.

Nevertheless, further adjustment is not only required, but is inevitable. Accordingly, the mix of production will continue to change. And while optimistic views are that aggregate TCF production may increase from its present level, firms' efforts to improve productivity in response to global competitive forces suggest that employment will continue to decline, irrespective of the support provided to the sector by Australian governments.

In effect, the outlook for the sector is a continuation of the process that has been occurring over the past decade or so — rationalisation of production, firm closures and the emergence of new suppliers and products. Hence, the key task for firms and their employees is to build on strengths and to address weaknesses so the sector can make the most of what are likely to be a diverse array of opportunities.

Governments also have an important role to play in formulating a well understood, stable and predictable assistance policy regime to provide for an appropriate balance between the interests of firms, employees and TCF regions on the one hand, and user industries, consumers and taxpayers on the other. Appropriate policy settings for taxation, workplace arrangements and overseas market access will also be important. The respective roles of the industry and governments in a number of key areas are the subject of the remainder of this report.

Box 3.6 **Participants' views on threats**

Exchange rates

Australian manufacturers' vulnerability to fluctuations in exchange rates remains a significant issue. Australia's main role in international trade is as a supplier of commodity items such as mining and agricultural products. The result is that in the medium term the exchange rate is primarily determined by the state of world commodity and financial markets. The exchange rate therefore does not appropriately reflect the competitiveness of local manufacturing. (sub. 77, p. 10) *Godfrey Hirst*

Critical mass

Domestic demand for early stage processed product has contracted significantly over the last decade. As the clothing industry has increasingly moved offshore … so too in turn does weaving and spinning. This is a fundamental shift in industry; as the weaving sector's competition is not imported fabrics – it is imported garments. This contracting local market and the resultant restructuring pressures have now flowed through to early stage processing. (sub. 45, p. 6) *Australian Wool Processors Council*

… while we are striving to maintain our international competitiveness, we remain concerned about the ability of our core customer base in Australia to retain the necessary critical mass to ensure its own sustainability. (sub. 55, p. 9) *Bruck Textiles*

Market access

The WTO Ministerial Conference at Doha agreed on the parameters of a new round of negotiations as part of the future work programme of the WTO. The round is due to end by 1 January 2005 at the earliest. Even if such a deadline is met, new rules would be unlikely to come into force before 2006, and they would set a target (of tariff reductions) to be reached no sooner than 2010. It is unlikely that this target for 2010 will be less than the scheduled rate of TCF tariffs to be implemented in Australia by 2005. (sub. 75, p. 39) *TFIA*

Competition from low-cost goods

There is also a strong belief within the Australian technical and nonwoven textiles industry that overseas suppliers (usually in low labour cost countries) that have exhausted their quotas to other countries often use Australia to offload excess capacity (and/or cancelled orders) to a quota free Australia. Whilst it may not technically be dumping, nevertheless it has the equivalent effect of pushing the price of domestic production down by allowing an increase in supply of low-cost goods. (sub. 68, p. 17) *Technical Textiles and Nonwoven Association*

Microeconomic reform

There is a strong perception in the carpet industry that the micro-economic reform program has failed to deliver a significant improvement in the cost structures facing the carpet industry. (sub. 35, p. 19) *Carpet Institute of Australia*

The spinning industry in Australia has seen a significant departure of machinery and investment from Australia to New Zealand over the last five years. Undoubtedly this is due partly to the significantly more competitive infrastructure costs applying in New Zealand; I refer particularly to payroll tax and workers' compensation premiums (currently costing us in excess of $1.5 million per annum). Prohibitive sea freight rates from Australia compared to our overseas opposition remain an anti-competitive burden. (sub. 86, p. 3) *Victoria Carpets*

FINDINGS ON THE TCF SECTOR'S PROSPECTS

- *Some firms and parts of the sector are performing well, exploiting competitive advantages to develop new products and to secure new markets.*
- *Other firms are in a process of transition, with reasonable prospects of operating in a lower assistance environment in the medium to longer term.*
- *For firms producing standardised products in the more labour intensive parts of the sector, future prospects are very limited. Many will not survive, regardless of the assistance regime.*
- *Across the sector as a whole, future assistance levels will be but one influence on firms' prospects. Global market pressures, firms' business models and exchange rates are just some of the many other factors that will impinge on those prospects.*

4 Adjusting to change

4.1 A sector in a continuing state of transition

Earlier chapters explain some of the global and domestic influences that contribute to adjustment pressures on the Australian TCF sector.

For many TCF firms, global market pressures overwhelm the influence of domestic assistance settings. As the ACTU acknowledged, in its response to the Position Paper, 'global pressures dwarf the effects of the tariff changes proposed by the PC' (sub. PP169, p. 6). For many labour intensive products, even much higher tariffs would not compensate for the labour cost advantage of developing country TCF suppliers, such as China. Moreover, the quality and range of products available from those overseas suppliers is increasing rapidly.

Australian producers will therefore need to continue efforts to develop new or improved products, to explore new markets and to improve productivity. This will place adjustment pressure on firms, their employees and the communities where they live, particularly where productivity improvements reduce labour requirements. Firm exits will add further to these pressures.

4.2 Change brings benefits as well as costs

Change is a natural part of any market environment. Most firms adapt their activities from time to time in response to increased competition or to take advantage of new opportunities. Even though such change imposes costs on firms, they expect to benefit in the long term. Earlier chapters discuss how many successful Australian TCF firms have expanded the scope of their activities beyond traditional manufacturing, looking increasingly for increased integration with overseas producers and moving into downstream distribution.

Many individuals who leave employment in the TCF sector (or change jobs within it) do so from choice. They may find employment elsewhere, may relocate or may just decide to retire. Indeed, labour turnover is a feature of all parts of the economy, including the TCF sector (box 4.1). Like firms, employees may trade short term costs for long term gains.

Box 4.1 **Job mobility of the TCF workforce**

Workers in the TCF sector are less job mobile than workers in many other sectors. In 2002, for example, around 11 per cent of TCF workers changed jobs compared to 15 per cent of workers in all industries. The corresponding TCF figures for 2000 and for 1996 were 9 per cent and 11 per cent, respectively.

The composition of the figures also varies somewhat from year to year. For example, in the 12 months to February 1996, about 7 per cent of TCF workers found jobs outside the sector and 4 per cent found new jobs in the sector. About 5 per cent of TCF workers in the sector at February 1996 had worked in other industries a year earlier. In the 12 months to February 2002, about 5 per cent of TCF workers found jobs outside the sector and about 6 per cent moved within the sector. At February 2002, about 5 per cent of TCF workers had been employed in other industries a year earlier.

There is also significant movement out of and into work. About 10 per cent of TCF workers at February 1995 were not working 12 months *later*, while about 10 per cent of February 1996 TCF workers were not in work 12 months *earlier*. The corresponding figures for the 2001–2002 period were 9 per cent and 8 per cent, respectively.

Source: Appendix tables B23–B28.

Appropriate and timely change, albeit costly to firms and employees in the short term, may forestall higher costs in the future. For example, failure to respond progressively to the increasing competitiveness of imports could leave firms and possibly whole segments of Australian TCF activity exposed to pent up adjustment in response to an external shock (eg an exchange rate appreciation) which would magnify the adjustment costs otherwise incurred.

But some change, particularly involuntary change, can bring high adjustment costs when an industry or sector is contracting and alternative job opportunities are limited. Firms, their employees, and the regions in which they operate, face not only direct economic costs such as loss of income and employment, but a range of flow-on social and economic costs, arising from closure of regional infrastructure, reductions in property values, loss of self-esteem, and family dislocation. Many such costs — examples of which are listed in box 4.2, with an extract from the TCFUA submission about the effects on workers given in box 4.3 — are not captured in economic models which attempt to estimate the net effects of changes in assistance and other policy parameters. Yet it is important that these costs not be overlooked.

Box 4.2 Listing the 'involuntary' costs of change

Employees:

- loss of income (not fully offset by social welfare support or redundancy payments), leading to debt, mortgage and loan foreclosure;
- inability to obtain work (or future work is casual and intermittent);
- loss of skills (as they become unpractised);
- costs of retraining;
- relocation costs;
- lowered property values;
- social costs (loss of self-esteem, depression, illness, drug and alcohol dependence, family problems).

Firms:

- loss of income;
- reduced value of assets such as buildings and machinery;
- write down of inventory;
- lease exit costs;
- costs of redundancy payments;
- costs of site clean up in the event of closure.

Regions:

- multiplier effects on other firms and their employees;
- longer term effects on social infrastructure (from population drift and lower economic activity levels in the region);
- declines in property values and associated pressure on local government income.

4.3 Industry characteristics suggest adjustment costs could be high

Adjustment costs for workers displaced from the TCF sector are likely to be higher, on average, than for workers displaced from other sectors. There are a number of reasons for this, including:

- Skills are often sector-specific and basic, while educational attainment levels are generally low.
- Capacity to relocate or to travel for job search are often limited.

Box 4.3 Negative effects of retrenchment on workers

According to the TCFUA:

'The negative effects of retrenchment on workers are broad and widely documented. Such effects include the obvious economic problems unemployment brings such as inadequate income, debt, mortgage and loan foreclosure, eviction and also include feelings of boredom, depression, social dislocation, impaired mental health etc.

It has been suggested by counsellors that workers who are retrenched experience a 6-8 week period coming to terms with the loss before they can effectively engage in seeking alternative work.

Work often constitutes the means by which a person defines their identity, this is realised not only by the type of work performed but the sense of well being which ensues from feeling that one is making a contribution to society and being involved in a group.

Job loss, especially when it is sudden, immediately removes this avenue through which people feel part of the work community, this in itself produces feelings of isolation. Moreover, without paid employment, people do not have the fiscal means to engage in activities which would have the effect of ameliorating such feelings of social dislocation. Hence, retrenched workers, despite having ample time to engage in activities which would generate feelings of self worth, have reduced capacity to do so due to lack of fiscal resources.

In addition to feelings of anger, frustration and worthlessness, retrenched workers typically experience financial difficulties which further impacts on their psychological and emotional health. Redundancy payments, when made, provide short-term security, however in a lot of cases retrenched workers are often forced to sell property in order to get by. This is particularly the case in situations where workers who having received little or no warning that their job was threatened have invested in property and other assets and are hence over committed financially. As social security payments are governed by means tests, a number of these workers were deemed ineligible for welfare payments, hence, having no access to basic financial advice, such workers proceeded to fritter away their assets before being eligible to claim unemployment and other benefits.

These financial problems brought about by a lack of information, which is a particular issue for migrant workers who face language and cultural barriers, is common among retrenched workers and is one of the many issues that could be addressed and remedied by a labour adjustment program.'

Source: TCFUA (sub. 33, pp. 69–70).

- TCF adjustment is often 'lumpy' — for example, the closure of firms or factories displacing many workers at the same time — increasing adjustment costs, particularly in regional areas.

In separate recent work, the Commission has prepared weighted indexes for Australian industries of adjustment relevant workforce characteristics, such as the degree of English proficiency, level of educational attainment and age of workers (PC 2003, forthcoming). To the extent that such factors predispose displaced workers to difficulty in finding new employment, the indexes suggest that workers in the TCF industries are particularly vulnerable.

Such workforce characteristics are most acute in the clothing and footwear manufacturing industries. In addition, most non-factory outworking occurs in the clothing industry. Outworkers generally have no redundancy or severance payment entitlements, or notice periods, and often face the loss of personal investment in sewing equipment if they are displaced.

Many firms face high exit costs, including redundancy costs. And the flow on effects to communities and regions from adjustment costs imposed on workers and firms can be high.

Much of the information in the following sections describing workforce characteristics draws on the ABS Labour Force Survey and the Population Census. Each of these data collections encompasses workers in small firms, outworkers, as well as proprietors working in their own businesses, provided the individuals identify themselves as working in the TCF sector. Coverage of outworkers is likely to be incomplete, however, as it is generally believed that many outworkers are reluctant to identify themselves as such. Further, the TCF Resource Centre of WA commented that available data understate the number of firms in the TCF sector and the number of workers (sub. PP167, p. 1). However, this is partly a classification issue — people working in *occupations* commonly associated with TCF (eg design, cutting, sewing) are often classified by the ABS into non-TCF *industries* in the services sector, such as design services, wholesale or retail trade.

Skill profiles and educational levels impede adjustment

The TCF sector exhibits a lower skilled occupational profile than either total manufacturing or the economy as a whole. In 2003, for example, 62 per cent of TCF workers were classified into the lower skilled occupational groups, compared to 46 per cent for manufacturing as a whole (appendix table B.18, groups 6 to 9). Although this does not necessarily mean that individual TCF workers have low skills, the non transferability of the skills used in many areas of the sector could limit alternative job opportunities.

Low educational attainment could also impede adjustment:

- In 2001, nearly two-thirds of TCF workers had no post-school qualifications (compared to around 50 per cent of manufacturing workers overall), with over 40 per cent not having completed the highest level of secondary schooling (appendix table B.14).
- Within TCF manufacturing, the lowest levels of educational attainment were in the footwear industries with 75 per cent of workers without post-school qualifications. In clothing manufacturing, the corresponding figure was around 68 per cent (appendix table B.14).

These skilling and educational characteristics mean that factory-based TCF employees on average earn much less than manufacturing employees in general. In May 2002, average hourly earnings of $18.37 were about 20 per cent lower than the manufacturing average of $22.82 (appendix table B.16). Moreover, the difference between TCF and average manufacturing wages has increased slightly over the last ten years — with the annual average wage increase in TCF being between 0.5 and 0.9 percentage points lower than for manufacturing as a whole (DEWR, sub. 84, p. 10). There is some variability within the TCF sector, however, with the average hourly rate for employees in the textile, fibre and yarn manufacturing industries more than 15 per cent above that for employees in the clothing industries (appendix table B.15), possibly reflecting differences in skill requirements.

Labour mobility is relatively low

As noted in box 4.1, labour mobility of the TCF workforce as a whole is lower than for industry in general. This is partly explained by the age profile of TCF employment and the high proportion of female and migrant workers. (Mobility may be higher in some individual TCF industries, however — for example, Austanners, the ‘only vertically integrated manufacturer of finished apparel and furniture leather in Australia’ (sub. 73, p. 8), noted that its workforce is largely ‘itinerant’ (sub. 73, p. 23).)

An older age profile

The TCF workforce is somewhat older than in many other manufacturing industries, with 72 per cent of TCF workers aged 35 or over in 2003 compared with 62 per cent for manufacturing in general. In parts of the TCF sector, the age profile is noticeably older than the manufacturing average, with the over-35 figure for knitting mills being more than 80 per cent and clothing manufacturing over 70 per cent (appendix table B.11 and appendix figure B.3).

In general, older people are more likely to have established family and community ties to the regions in which they live and to be more reluctant than younger people to move to find work. People closer to retirement age are also less likely to relocate for employment reasons.

Female employment is high

Women accounted for more than 55 per cent of the TCF workforce in 2003, more than double the proportion for manufacturing as a whole (appendix table B.5). But in textile manufacturing and the leather industries the proportion of female workers is lower than the manufacturing average. Further, women in TCF employment account for about 13 per cent of total female manufacturing employment, whereas the corresponding figure for men is just under 4 per cent (appendix table B.5).

For females, alternative work in male dominated manufacturing industries can be hard to find. In addition, a slightly higher proportion of female TCF workers are married than their counterparts in other parts of manufacturing, possibly also contributing to a reluctance to relocate in search of alternative employment (appendix table B.13).

Women have borne more of the burden of recent adjustment in the sector. Over the last 5 years, total female employment has fallen by just over 36 per cent (22 000 persons) compared with 31 per cent (13 300 persons) for male employment (appendix table B.5).

A high proportion with an ethnic background

The sector has historically been an important employer of migrants. Just under half of all TCF workers were born overseas — predominantly in non-English speaking countries — compared with about one third of workers in manufacturing generally (appendix table B.12 and appendix figure B.4). Indeed, the proportion of non-English speaking background (NESB) workers in TCF has increased in recent years from about 41 per cent in May 1997 to about 44 per cent in May 2003 — during that period the corresponding proportion for manufacturing as a whole declined slightly.

Many recent migrants have poor skills in English, as well as lower levels of educational attainment than those born in Australia. This is likely to add to their difficulty of finding alternative employment if displaced from their current jobs, particularly if they are more recent arrivals in Australia.

There is some evidence that the TCF sector provides the first job opportunity for many migrants to Australia. For instance, while ethnic TCF employment in the past was dominated by migrants from Southern Europe, more recently, Asian born (female) workers have become the predominant grouping, in line with the growing migration from South East Asia.

Many outworkers have few alternative job opportunities

As the use of outworkers provides firms with important flexibility advantages, job opportunities for outworkers appear to have increased recently, notwithstanding an overall decline in TCF production levels. Indeed, the TCFUA claimed that previous tariff reductions have led to a 'massive surge' in outworking, though no data were provided (sub. 33, p. 15). A recent Victorian report similarly concluded that the number of outworkers, particularly in the TCF sector, 'has risen with the restructuring of the manufacturing industry over the past ten to fifteen years' (cited in sub. 40, p. 4). The Commission's estimates suggest that the full-time equivalent number of outworkers may have increased slightly since 1997 (see chapter 10).

Nonetheless, when firms contract or close down, outworkers displaced from those firms may find it difficult to obtain new work. As noted above, adjustment costs faced by individual displaced outworkers can be just as high, if not higher, than those faced by factory workers who lose their jobs:

- A recent survey by Christina Cregan (see sub. 30) of 119 outworkers suggests that many work at home because they are unable to find, or their circumstances do not permit them to find, work outside the home. Their often limited education, lack of English proficiency and inability or unwillingness to relocate severely limits alternative job prospects.
- The survey indicated that a small minority prefer to work at home rather than to seek outside work. The likelihood of obtaining alternative employment which offers them this flexibility is often limited, particularly in regional areas.
- Outworkers generally receive lower pay, on an hourly basis and in total, than factory workers. This implies that lost income from unemployment could be lower. But outworkers may lose personal investment in equipment, such as sewing machines. Further, displaced factory workers often receive redundancy payments and may have greater recourse to social welfare support. The longer term cost of job loss for many displaced outworkers could therefore be higher than for workers displaced from factory employment.

Lumpy adjustment adds to costs

When firm closures or rationalisations result in many workers being displaced at the same time, adjustment for individuals can be more difficult and costly than when only a small number of employees lose their jobs, for example as a result of small scale labour shedding by firms continuing in business. Lumpy adjustment results in more people looking for work from the pool of available jobs. If significant numbers seek to relocate, demand for property in a region can stagnate and property values fall. Thus, even where individuals are otherwise prepared to move to find work, difficulty in selling their houses at a satisfactory price may prevent them doing so. The flow-on effects to regional communities will also be larger than if just a few employees are displaced.

Firms can face high exit costs

The adjustment costs for firms depend on many things including: alternative uses for their fixed assets and working capital; costs of paying out leases, dismantling existing operations and paying for necessary site clean up and refurbishment; and accrued employee entitlements.

While the Commission has no information to suggest that most of these exit costs are any greater in the TCF sector than in other industries, there is some evidence that many TCF firms face large redundancy payments in the event of closure.

Many firms, of course, would be able to pay entitlements to their employees if the need arose. But a view expressed during discussions with some participants, and mentioned also in some submissions (see for example, sub. 51 from the Melbourne Textile Knitting Co), was that others could not afford such payments in the event of closure and therefore keep operating despite poor profitability and limited future prospects. There were also suggestions that some firms which could afford to make redundancy payments were unwilling to do so — it being less costly for them to continue to trade, even at a loss, than to close and meet the immediate costs of redundancy payments.

In the short term, continued operation postpones the costs of adjustment. However, it may add to the cost of adjustment in the long term by backing up adjustment pressure which would otherwise have been spread out over a period. As noted above, a deterioration in international competitiveness from an external shock (eg appreciation of the exchange rate) could trigger a lumpy and therefore more costly adjustment episode.

4.4 The regional dimension

Irrespective of location, adjustment costs for individuals can be high

Workforce characteristics affecting mobility (described above) vary by location. Some characteristics are more pronounced in city areas and others more pronounced in the regions. For example, appendix table B.20 shows that (as a broad summary):

- TCF workers in metropolitan areas are more likely to be better qualified with jobs requiring higher skill levels than those in the regions; but
- those in the cities are more likely to be older, female, overseas born and married than regional workers.

There was no substantive evidence presented to the inquiry that, in general, individual TCF workers in the regions face higher adjustment costs than their counterparts in metropolitan areas, or vice versa. Many individuals, irrespective of their city or regional location, have characteristics which suggest that the adjustment costs likely to be imposed on them through loss of their current jobs could be high. On this count, there appears little basis for differentiating between metropolitan and regional areas in future TCF adjustment assistance.

But flow-on costs may be more significant in regional areas

Where TCF firms close down or reduce employment, adjustment costs extend beyond their employees and families to the broader community. Although these flow-on costs can affect city areas — a fact emphasised in several submissions including those from the City of Darebin (sub. 25) and the City of Whittlesea (sub. PP115) — they are potentially more significant in regional areas where the total job pool is smaller and where alternative job prospects are generally more limited than in the metropolitan centres. The repercussions spread to non-TCF firms, their employees, and the region's social infrastructure. The City of Greater Geelong, for example, contended that each textile job leads to the creation of an additional 1.38 jobs elsewhere in the local community, with each clothing and footwear job creating an additional 1.27 places (sub. 16, p. 11). Hence, it argued that a scaling back of TCF activity would adversely affect the Geelong region to a much greater extent than indicated by the direct loss of TCF jobs.

However, while the existence of flow-on effects is unarguable, the longer term regional effects of TCF change depend on the interplay of many factors, including: the importance of TCF employment in the region; employment in individual TCF firms; regional growth, particularly employment growth, and alternative regional job opportunities; and the extent of integration with neighbouring regions. Box 4.4 illustrates some of the relevant factors, with reference to Geelong.

Box 4.4 **The adjustment process in Geelong**

The TCF sector currently directly employs over 2150 people in the Geelong region, accounting for 14 per cent of the region's total manufacturing workforce and 2 per cent of its workforce overall. (In comparison, TCF employment accounts for about 9 per cent of Victoria's manufacturing employment.) The City of Greater Geelong estimated that TCF activity in the region supports somewhat more than this number of jobs in the wider community.

TCF employment in the Geelong region has decreased in recent years as assistance has fallen and global pressures have increased. In the past five years, around 1150 jobs have been lost in the sector.

Nonetheless, the City of Greater Geelong's overall unemployment rate declined from 10.6 per cent in 1997-98 to 5.7 per cent in 2001-02. In the Barwon-Western district as a whole — which includes Geelong — there are now about 21 000 more jobs than five years ago.

The submission from the City of Greater Geelong suggested that the unemployment problem is higher than the official figures suggest, because many of the long term unemployed shift onto social security and leave the workforce, and changes in income tests have encouraged those on welfare to accept part time employment.

Available data, however, show that workforce participation rates in the Barwon-Western district have decreased only slightly since 1996-97. The small reduction is nowhere near sufficient to explain the reduction in the unemployment rate, particularly as the total regional population has increased over the period. Moreover, recent trends identified by the City of Greater Geelong (2002) indicate a reduction in the number of those requiring welfare assistance:

> The Region's buoyant labour market was further supported by Centrelink data that showed the number of unemployed people in the Geelong region that required financial assistance decreasing by 5.8% in the 12 months to 30 June 2002.

Hence, the adverse effects of declining TCF employment in Geelong over the past few years must be seen in the perspective of significant employment growth in other industries and increased regional activity. This is not to deny, however, that even better results for Geelong might have been achieved if that sector had not contracted. Nor does it deny the often high adjustment costs imposed on displaced employees and their families.

Sources: City of Greater Geelong, sub. 16, pp. 10-11 and pp. 14-17, City of Greater Geelong 2002 and table 4.2.

Regional dependence is still high in some regions

About 80 per cent and 75 per cent of TCF employment in Victoria and New South Wales respectively is located in Melbourne and Sydney (appendix table B.8). In May 2003, TCF employment outside those cities was around 6000 persons and 5800 persons, respectively. Across Australia, more than 16 000 people work in the TCF sector outside the capital cities.

Table 4.1 shows that TCF employment still accounts for more than 5 per cent of total manufacturing employment in many regions, although the extent of regional dependency on TCF activity has declined over the past 10 years.

- About one-third of Victoria's regional industry is situated in Geelong, a major production centre for carpets, as well as the home of several large textile manufacturers. The Wangaratta/Wodonga region has the highest regional dependency on TCF in Australia. TCF firms are also major employers in Bendigo, Ballarat and Traralgon.
- In New South Wales, Albury, Tamworth, Goulburn, Unanderra and Gosford have substantial TCF employment.
- Regionally significant TCF centres in other States include the Gold Coast in Queensland and Devonport in Tasmania.

Individual firms are major regional employers

Further contraction of the TCF sector appears inevitable, possibly including closure of major firms or factories. Most of the large regional employers are located in Victoria. However, there are also major employers in regional areas of New South Wales and Tasmania (see box 4.5). In some regions, individual TCF firms account for significant proportions of regional employment. As the Tasmanian Government commented: 'loss of even one key player in a regional community [such as Devonport] would have serious economic consequences' (sub. PP180, p. 3). If such firms were to close, the consequent adjustment costs could be higher than for incremental adjustment, involving similar job losses, over a longer period.

There is no firm evidence to suggest that major firms or factories in regional areas are necessarily any more or less likely to close than those in the cities — this will depend on the particular circumstances of individual firms. For example, Yakka indicated that if or when it contracted to a single manufacturing operation, it was more likely to be in Wodonga than at the Brunswick facility in Melbourne (trans., p. 88). Albany International commented that, if it were starting its operations from scratch again, it 'would still probably end up where we are' at Gosford, rather than in a major metropolitan area (trans., p. 354).

Table 4.1 **Persons employed in the TCF sector: 1991, 1996 and 2001**

Stat. Div. code[a]	*Main centres*	*TCF employ-ment 2001*	*Change since 1996*	*TCF employment*[b] *as a share of total manufacturing employment*			*TCF share of total employ-ment 2001*
				1991[c]	*1996*	*2001*	
		no.	no.	%	%	%	%
105	Sydney	14 033	-5 400	9.3	9.0	6.4	0.8
120	Lismore, Tweed Heads	415	-78	9.0	7.4	6.6	0.6
125	Coffs Harbour	385	-200	7.3	6.7	5.1	0.4
130	Tamworth	421	206	9.1	4.4	8.8	0.6
140	Orange, Bathurst	407	-303	7.9	8.6	5.1	0.6
145	Queanbeyan, Goulburn	506	-81	8.9	10.0	8.4	0.6
155	Albury	364	55	11.7	5.8	5.9	0.8
205	Melbourne	22 416	-8 346	13.8	12.8	9.1	1.5
210	Geelong	2 194	-541	17.3	16.6	13.5	2.2
220	Ballarat	556	-192	11.5	9.8	6.6	1.0
235	Bendigo	748	-234	15.7	11.1	7.9	1.1
245	Wodonga, Wangaratta	977	-79	21.4	16.5	14.5	2.3
255	Traralgon	410	-258	12.0	11.3	6.3	0.7
305	Brisbane	4 498	19	6.3	5.6	5.0	0.6
310	Coolangatta, Surfers	2 002	-8	9.8	8.6	7.0	0.7
405	Adelaide	3 414	-1 015	8.2	6.5	4.8	0.7
505	Perth	3 317	47	4.9	5.4	5.0	0.5
605	Hobart	616	-41	8.0	8.4	8.2	0.8
620	Burnie, Devonport	459	-53	7.7	8.5	8.2	1.2
705	Darwin	123	35	4.4	4.3	4.5	0.2
805	Canberra	221	23	3.8	4.0	4.0	0.1
Total	**Australia**	**64 565**	**-17 482**	**9.4**	**8.5**	**6.4**	**0.8**

[a] A statistical division is listed if it relates to a capital city, or TCF employment in 2001 exceeded 250 and the TCF share of total manufacturing employment exceeded 5 per cent. [b] TCF covers all industries within ANZSIC code 22. [c] Not strictly comparable with data for 1996 and 2001 — TCF covers all industries in ASIC codes 23, 24 and 345.

Source: Estimates based on unpublished ABS Population Census data.

Box 4.5 Examples of employment by individual firms in regional areas

Firm	*Activity*	*Region*	*Employment (no.)*
Victoria			
Australian Defence Apparel	Clothing	Bendigo	160
Australian Country Spinners	Knitting yarns	Wangaratta	250
Bruck Textiles	Textiles	Wangaratta	482
Hilton Fabrics	Fabric dyeing and finishing	Ballarat	80
Oliver Footwear	Footwear mfg	Ballarat	80
Godfrey Hirst	Carpet mfg	Geelong	700
Godfrey Hirst	Carpet mfg	Benalla	140
Huyck Australia	Disposable clothing	Geelong	186
Brintons Carpets	Carpet mfg	Geelong	170
Yakka	Clothing	Wodonga	109
Victoria Carpets	Wool spinning	Castlemaine	100
Victoria Carpets	Carpet mfg	Bendigo	100
Creswick Woollen Mills	Spinning and weaving	Creswick	50
New South Wales			
Macquarie Textiles	Woollen fabrics	Albury	320
Geofabrics	Technical textiles	Albury	60
Kimberly Clark	Technical Textiles	Albury	56
Albany International	Engineered textile products	Gosford	320
Pacific Brands	Clothing	Unanderra	220
Tasmania			
Ulster Tascot	Carpet mfg	Devonport	220
Australian Weaving Mills	Towels and manchester	Devonport	250
James Nelson	Woven fabrics	Launceston	88
Waverley Woollen Mills	Woollen products	Launceston	80

Sources: Visit notes, submissions, direct contacts.

Regional growth and employment has been strong

The costs imposed on individuals, their families and regional communities from loss of TCF activity and employment will be mitigated where regions are growing strongly and have capacity to provide alternative employment to displaced employees. Indeed, in many regions, regional unemployment rates have fallen, while workforce participation rates have been maintained, despite losses in TCF employment (see table 4.2 and box 4.4). Similarly, in providing a metropolitan perspective, Moreland City Council noted that 'we are likely to see a net loss of TCFL businesses and jobs … [but] new business and employment opportunities are also likely' (sub. PP119, p. 29).

Of course, aggregate labour force and employment statistics do not tell the whole story. For example, the Victorian Government reported on a study it commissioned from the National Institute of Economic and Industry Research (NIEIR) on structural unemployment associated with decreased TCF employment. The Government stated that the study:

> … illustrates that structural unemployment has increased significantly in areas that have suffered TCF job losses (even in areas that have experienced overall employment growth), thus creating social and economic inequities not apparent when analysing macro statistics … (sub. 78, p. 12)

Although the full results and methodology of this study were not provided to the Commission, this broad conclusion is not surprising given the characteristics of the TCF workforce discussed above. As noted, those characteristics suggest that adjustment costs for displaced TCF workers are often likely to be higher than for those displaced from other sectors. And it is unarguable that an increase in structural unemployment associated with TCF job loss is likely to increase adjustment costs in the regions concerned. However, this does not undermine the obvious conclusion that regional responses to declines in TCF activity will be easier where there is strong regional growth. Those responses also need to be seen in the context of the overall significance of TCF activity to regional economies — in only two ABS statistical divisions does TCF employment account for more than two per cent of total regional employment, 2.3 per cent for Wodonga/Wangaratta and 2.2 per cent for Geelong (table 4.1).

Some people find employment in neighbouring regions

Regional adjustment costs can be reduced if displaced employees find jobs in neighbouring centres. This is more likely for workers in regions adjacent to major metropolitan centres. For example, 2001 population census data show that almost 25 per cent of employed persons residing in Geelong worked outside the Geelong region, about half of those in Melbourne (Geelong 2002). Similarly, some people living in Wangaratta work in Albury/Wodonga, and vice versa, and some in Wollongong and Newcastle commute to Sydney.

Table 4.2 **Regional employment, unemployment and workforce participation**

Relates to total persons employed, all industries, selected regions

Statistical region	*Total employ-ment, May 2003*	*Change in employ-ment since September 1997*	*Unemploy-ment rate, September 1997*	*Unemploy-ment rate, May 2003*	*Participat-ion rate, September 1997*	*Participat-ion rate, May 2003*
	’000 persons	’000 persons	%	%	%	%
Sydney	2 095.2	200.6	6.2	5.6	64.3	65.0
Hunter	264.3	36.5	12.9	7.0	59.4	58.0
Illawarra and South Eastern	259.8	12.4	10.4	7.6	59.9	60.6
Richmond-Tweed and Mid-North Coast	184.2	43.8	16.5	6.7	50.1	54.3
Northern, Far West-North Western and Central West	215.9	3.8	5.4	6.2	61.9	61.5
Murray-Murrumbidgee	132.7	14.2	9.7	6.0	62.1	66.2
Melbourne	1 769.3	180.0	8.6	6.1	65.0	64.0
Barwon-Western District	166.3	17.1	13.2	6.0	63.0	61.6
Central Highlands-Wimmera	85.3	-4.4	10.9	6.1	62.8	58.9
Loddon-Mallee	141.2	36.1	8.8	4.9	56.8	67.9
Goulburn-Ovens-Murray	121.9	-1.1	6.4	2.9[a]	62.3	61.9
All Gippsland	106.3	33.9	11.5	6.6	56.9	61.3
Brisbane	857.8	119.2	8.6	6.2	66.0	66.3
South and East Moreton	203.3	40.1	9.8	6.9	64.2	65.4
North and West Moreton	136.9	26.7	11.8	7.7	61.2	59.2
Adelaide	530.4	150.3	10.1	6.6	61.0	62.0
Perth	714.0	73.7	7.2	5.9	65.9	65.3
Greater Hobart-Southern	101.6	7.4	11.0	6.9	59.7	59.4
Mersey-Lyell	42.6	-0.7	11.8	9.8	58.0	53.7

[a] Relative standard error greater than 25 per cent.

Source: ABS Labour Force Survey datacubes r1 and RM1.

The scope for such job relocation depends on whether job opportunities in neighbouring regions are suitable for displaced TCF workers. Given the contraction in TCF employment generally, TCF jobs may also be scarce in neighbouring regions, even in the capital cities. And, as noted above, the ability of many current TCF workers to find work in other industries may be limited. Nevertheless, inter-regional linkages are still likely to play some role in reducing the impact of TCF job loss on regional economies and communities.

Existing regional programs can help ease adjustment costs

A number of Commonwealth and State programs provide assistance to regions experiencing adjustment problems. For example, at the Commonwealth level, regions can receive assistance through the Regional Partnerships arrangements, incorporating the previous Regional Assistance Program. One of the objectives of Regional Partnerships is to 'assist in structural adjustment by investing in projects that assist specifically identified communities and regions adjust to major economic, social or environmental change' (http://www.regionalpartnerships.gov.au/). Thus, if the need arises, this program should be available to help regions experiencing problems arising from adjustment in the TCF sector.

Although a generally available assistance measure, rather than a TCF specific regional adjustment program, the Regional Assistance Program received specific supplementation of $22.3 million through the post 2000 TCF assistance package. It is unclear how much of this money has been spent in assisting 'TCF dependent communities'.

4.5 Recent experiences

Case study material about the experiences of individual TCF workers, their families and regions, can be helpful in illustrating the extent to which the workforce and regional characteristics described in preceding sections affect adjustment capacity in practice. Interpreted carefully, it is useful input for future policy development. However, up to date and comprehensive case study information is scarce.

Many participants drew on a study undertaken during the 1990s by Webber and Weller into the experience of around 600 displaced TCF workers (see box 4.6). In particular, many quoted the conclusion that one third of displaced TCF workers 'did not work again'.

However, since that study was completed in 1997, the Australian economy has improved significantly and considerable structural change has occurred in the TCF sector. Thus, the study may not be representative of recent adjustment experience, nor indicative of likely future outcomes. According to DEWR, the number of retrenched workers in the TCF sector declined from 17 700 in the three years to 1997 to 8600 in the three years to June 2001. Furthermore, although results can be skewed by lumpiness in retrenchments, it appears that the re-employment prospects for retrenched workers in TCF improved markedly in the three years to 2001 compared with the three years to 1997:

> Around 79.1 per cent of TCF workers who had become retrenched in the three years to June 2001 had found alternative employment by the time the survey was undertaken in July 2001. This is substantially higher than the 47.5 per cent of TCF workers who had found alternative employment after becoming retrenched in the three years to June 1997 and higher than the proportion of workers in all industries who had found alternative employment by July 2001 after becoming retrenched in the previous three years (67.2 per cent). (sub. 84, p. 11–12)

Box 4.6 **'Refashioning the rag trade'**

A recent book by Webber and Weller (2001) includes information about a longitudinal study of 605 workers retrenched from the TCF sector, mostly during late 1992 and early 1993.

The study indicates that:

> About one third of the workers found a secure new job of similar or better status and conditions to their TCF job, about a third were relegated to insecure, intermittent employment, and the other third did not work again after retrenchment. (p. 7)

The results of the study were often quoted by participants to illustrate the magnitude, and continuing nature of, the adjustment costs faced by individuals who lose employment in the TCF sector.

However, caution is necessary in seeking to generalise the results to today's situation:

- retrenched workers were followed only to April 1997;
- since then, general economic conditions have improved, with unemployment generally lower;
- TCF workforce characteristics have changed, with relatively more concentration on more highly skilled activity;
- regional dependence has reduced substantially; and
- general unemployment assistance has been overhauled.

Today, a higher proportion of displaced employees may well find alternative employment in a more 'reasonable' timeframe (see text, and box 9.2).

In contending that the re-employment prospects for displaced TCF workers continue to be limited, the TCFUA disputed the validity of this data:

> Despite all evidence to the contrary the DEWR statistics suggest that in the three years up to 2001 the rate of re-employment of TCF workers leapfrogged the rate of re-employment of general manufacturing workers … The DEWR statistics would be more realistic if TCF employment was booming and displaced workers could find new employment in other TCF companies (where their specific skills are easily

> transferable). However, this ‘result’ has occurred at a time when the TCF sector has continued to substantially contract in relation to general manufacturing and therefore the statistics are anomalous. (sub. PP154, p. 15)

ABS labour force survey data suggest, however, that employment for the sector as a whole remained relatively constant over the period in question (88 000 in February 1998 and 90 000 in May 2001). During that period, employment rose as high as 93 000 (November 1998 and May 2000) and fell as low as 76 000 (August 1999). Together with the job mobility data set out in appendix tables B23–B28, these data suggest that there was both considerable job turnover and considerable job opportunity within the sector over that period. In the context of a stronger Australian economy compared with the earlier three year period to 1997, the DEWR retrenchment data are not inconsistent with that hypothesis.

However, the stronger re-employment record during the three year period to 2001 may not be indicative of the future. Employment in the sector has since declined sharply to about 68 000 persons.

At a more individual level, the TCFUA presented a number of brief case studies about the experiences of some workers who had been displaced from the sector (see box 4.7). Although most had found further work, this was usually after a delay and it was sometimes part time or casual. Another common theme in those case studies was that many displaced workers had missed out on some or all of their employment entitlements (such as pay, annual leave, long service leave, superannuation, redundancy — see chapter 10).

The TCFUA went on to argue that appropriate help to workers, provided in a timely manner, can ameliorate some of the adverse effects of job displacement. It cited the example of employee retrenchments at Bradmill-Undare, where over half of the workers who participated in a company-specific program had found new jobs within 6 months of being retrenched (box 9.2).

Yakka commented on the experience of its workers displaced by plant closures in recent years. Although indicating that some special circumstances applied, it said that in regard to its closure at Wangaratta:

> … the track record on the number of people who actually got re-employed in the region post the closure was particularly good … I’d suggest that 60 to 70 per cent of them had been re-employed in some capacity in the area within … 12 months … (trans., p. 80)

The company also provided survey information on some 68 workers who had been displaced from its Shepparton site in early 2003. Of the 38 workers responding to the survey (conducted in July 2003), 33 indicated that they had sought work, with 29 obtaining new jobs. For some the wages and conditions were considered to be better and for others, worse. The vast majority of jobs were in the Greater Shepparton area. Depending on the assumptions made about the experience of those who did not respond to the survey, the possible range of success in finding alternative employment ranges between about 40 and 90 per cent.

Box 4.7 **Information provided by the TCFUA about the experiences of individual displaced workers**

Name	Age	Previous employer	Number affected	Received all entitlements	Personal and family impacts	Obtained further employment
Dorothy May Harry	45	United Carpets, Castlemaine	100 approx.	No		Yes
Margaret Gartside	48	United Carpets	100 approx.	No	No	Yes, after 18 months, at a lower wage
Milica Ludas	48	Maison de Couture	20	No	Illness due to stress	Yes
Anne Marie Gatt	43	Gala Fashions		No		Yes, part time
George Sammut		Verona		No	Felt hurt to be treated so badly	Yes
Robyn Dickson	35	John Redpath Fabrics	10	Yes, after a fight		Yes
Lindsay Cook	53	Classweave	160		Hardship	No
Maurice Ruffles	51	Surefit	Up to 40	No		Yes
Slavka Risteska	50	Vincena (Gala Fashions)		Yes, through GEERS		Yes
June Ambler	37	Surefit	30	No		Yes, part time
Rafella Spina	55	Gala Fashions		Some, through GEERS		
Minh Nguyen	50	Sleepmaster				Yes, short term casual work

Source: TCFUA, sub. 33.

4.6 Quantifying regional adjustment costs from further assistance reductions

Modelling commissioned for this inquiry by the Commission, as well as modelling work undertaken for participants, has attempted to measure some of the regional effects of assistance reductions (see chapter 6 for a discussion of economy-wide effects and appendix E for more detail).

While there are differences between the models in terms of the projected magnitudes of the economy-wide and regional impacts, in all models those impacts are generally very small. This confirms what could be expected given the relatively small contribution of TCF activity both to the overall economy and to most regional economies, and the fact that TCF assistance levels are now much lower than in the past.

Specifically, the modelling suggests that, under an assumption of fixed aggregate employment in the economy overall, reducing TCF assistance would lead to a small net loss in production and in overall employment in Victoria, an almost neutral effect on New South Wales, and minor gains in the other States and the Territories. At the statistical division level, the projected effects are not much larger. For example, the MONASH modelling undertaken for the Commission by the Centre of Policy Studies indicated that even in the Barwon region — which includes Geelong — removing the TCF sector's special assistance treatment would reduce total regional employment by just 0.03 per cent (appendix figure E4).

Projections were also made by the Centre of Policy Studies under an assumption of 'short-run sticky wages' — this allows for a short term decline in total employment consequent on a cut in TCF assistance. Here, the projected regional employment effects are larger in the short term, but still small at the economy-wide level in both the short and long term. While most States are projected to suffer employment loss in the short term, only in Victoria is the loss carried into the long term.

Many participants also referred to a modelling study commissioned by the Victorian Government from the NIEIR (sub. PP173). A projection commonly quoted, both in submissions and in media reports, was that 'it [is] estimated that the implementation of the PC's preferred option would lead to the loss of 6300 TCF jobs, and 19 600 direct and indirect jobs in Victoria' (Victorian Government submission, sub. 173, pp. 4–5). This claim is difficult to evaluate, as the full methodology and results of this work were not provided to the Commission. However, it appears not to tell the whole story:

- The projections incorporate effects arising from the already legislated 2005 tariff cuts. When adjusted for this, the projected job loss from the post 2005 assistance reduction options considered by the Commission, decline to about 4000 TCF jobs and 12 000 associated jobs — figures quite consistent with projections from the other models. Indeed, the 4000 figure is very similar to the decline in Victorian TCF employment implicit in the Econtech projections for reductions in tariffs to five per cent and removal of SIP assistance.

- No industry results from the NIEIR work other than for the TCF sector were reported to the Commission. Yet there would be benefits to Victorian industries and consumers from more efficient resource allocation and price reductions consequent on lower TCF assistance. In the other models, the resulting growth in output and employment in other industries largely offsets reduced activity and employment in the TCF sector. For example, Victorian Government projections using the MONASH model indicate a negative impact on Victorian GSP (gross state product) of just 0.02 per cent compared to the NIEIR result of 0.6 per cent — strongly suggesting that the NIEIR does not incorporate positive feedbacks for non-TCF industries and for consumers.

None of the modelling, however, includes several categories of adjustment cost listed in box 4.2. Nor does it include any of the extra costs likely to arise from lumpy rather than smooth adjustment, and the associated flow-ons to other activities. Generally, firms anticipated closure of entire sections of their activity, rather than only changes at the margin. For example, J. Robins (a footwear manufacturer) suggested that its total employment might need to be reduced by between 25 and 35 per cent following the legislated 2005 tariff reduction:

> It is extremely difficult to forecast the effect of the legislated tariff drop of 5% in 2005 on total employee numbers. Factors such as our exchange rate can have such a major effect either way. However, considering the margin pressure (and ensuing profitability) that most TCF companies are under, our estimate based on current trends, is that we will need to reduce employment by between 25 and 35%. (sub. 34, p. 4)

Yakka noted that if, following further tariff reductions post 2005, it cannot continue to support the local fabric industry to the extent it does now, there could be:

> … severe consequences for local fabric mills … YAKKA owned companies are major customers for Bradmill, Bruck and Macquarie, and if they cease buying from them, and import fully made up garments, these fabric mills will be hard pressed to retain critical mass. (sub. 31, p. 5)

For reasons such as these, the regional effects of future assistance reductions are almost certainly underestimated by modelling designed to look at the effects of policy changes on the economy as a whole.

Accordingly, regionally based modelling projections of the effects of TCF job loss, such as those submitted by the Wangaratta City Council and some other Victorian local government bodies, can provide a useful further perspective (box 4.8). Though the multiplier techniques used have limitations (appendix E), the results add weight to the conclusion that TCF job losses consequent on assistance reductions could have sizeable flow-on consequences for particular communities.

Box 4.8 **Regional modelling results — Wangaratta**

The City of Wangaratta (sub. 46, pp. 7–9) commissioned the La Trobe University's Centre for Sustainable Regional Communities (CSRC) to model the impacts of job losses on the Wangaratta region.

This modelling suggests that for every 100 manufacturing jobs lost in Wangaratta another 123 persons would lose their jobs. Output would decrease by $31.45 million and household income by $6.28 million.

More specific information about TCF jobs was provided in a subsequent submission by the CSRC (sub. PP149). It presented results for a range of scenarios, that included some allowance for the possibly beneficial effects for other regional industries of TCF assistance reductions. For a TCF job loss of 100 persons, the projected impacts were a $20–24 million loss of regional output and a total employment loss ranging from 165 to 200 persons. Of course, the base employment loss of 100 persons is arbitrary. Different bases could be chosen — for example, the loss of 79 TCF jobs for Wangaratta projected by the NIEIR (sub. 173) — and the results would adjust accordingly.

4.7 Lessons for the future

Further change is inevitable in the TCF sector, with continued contraction in employment, regardless of future assistance arrangements. The existing workforce (including outworkers) is vulnerable to involuntary displacement, with regional concentration potentially adding to adjustment difficulties in some situations.

Current policy was framed with a recognition of the costs imposed by adjustment. It aims to cushion the adjustment burden by providing a pause in tariff reductions until 2005, as well as providing assistance through SIP to enhance the sector's capacity to compete in a more open market after 2005.

Future assistance policy should not try to stop adjustment. But it needs to continue to encourage transition and cushion the adjustment process. Hence, the Commission has placed adjustment issues at the forefront in formulating its post 2005 assistance options. It has also investigated changes to broader policy settings and industry self-help measures which could further facilitate non-disruptive adjustment (see chapters 10 and 11).

- *Adjustment for workers displaced from the TCF sector, in cities as well as in regions, may be difficult:*
  - *Educational attainment is often limited and skill levels are frequently basic and sector-specific.*
  - *The predominance of female employees and low English language proficiency further reduce labour mobility and therefore re-employment opportunities.*
  - *Many small and medium sized businesses have had a history of being unable or unwilling to pay employee entitlements in the event of closure.*
  - *The prevalence of 'at-risk' firms increases the possibility of lumpy adjustments to an external shock.*
- *The costs of adjustment for displaced outworkers can be higher than for factory-based employees.*
- *Regional dependence on TCF activity has declined significantly over the past 10 years and overall growth in regional activity and employment has generally been strong. Nevertheless, dependence on TCF activity is still high in a few regions.*
- *The long term effects of changes in TCF activity on regions depend on the interplay of several factors, including:*
  - *the degree of dependence on TCF activity in those regions;*
  - *the prospects of individual TCF firms;*
  - *the strength of overall regional growth and employment; and*
  - *job opportunities available in neighbouring regions.*
- *If the need arises, general measures such as the Regional Partnership arrangements are available to help regions experiencing problems from adjustment in the TCF sector.*

5 Current assistance arrangements

5.1 The Government's policy objectives

The terms of reference for this inquiry spell out the Government's desire to:

- encourage the TCF sector to adjust into activities where it will be internationally competitive with lower levels of government assistance; and
- improve the overall performance of the Australian economy.

These objectives are consistent with the broad policy guidelines set out in the *Productivity Commission Act 1998* which focus the Commission's attention on improving the wellbeing of the community as a whole. In pursuing this goal, the Commission needs to have regard not only to economic impacts, but also to a wide range of social, regional and environmental impacts that can follow from policy change.

5.2 Key elements of the current arrangements

The TCF sector has historically benefited from very high levels of government support. Tariffs have been used to protect the sector from import competition since 1908 and, for much of this period, were progressively raised to compensate for the sector's declining international competitiveness. While there has been considerable dispersion in tariff rates across the sector, tariffs on particular products have been as high as 125 per cent. In addition, the sector was previously shielded by a range of non-tariff barriers (such as quotas and import licences) and has received substantial budgetary support in the form of production bounties and a range of 'targeted' assistance programs.

Since the late 1980s, however, Australian governments have pursued the goal of enhancing the ability of the TCF sector to compete with lower levels of assistance. This goal has also underpinned the policy of general tariff reductions elsewhere in the manufacturing sector.

An initial step was the introduction of the TCF industry plan in 1987 which provided for a systematic reduction in tariffs. This plan was modified by the 1991 industry statement which led to the termination of quotas in 1993 and an accelerated timetable for tariff reductions down to a maximum of 25 per cent by 2000.

Under current arrangements, TCF tariff reductions were paused from 2000 to January 2005. Other measures include: the Strategic Investment Program (SIP) — a transitional assistance measure designed to improve competitiveness by promoting investment and innovation; and extension of previous arrangements to encourage overseas assembly of Australian produced fabrics and leather (the Expanded Overseas Assembly Provisions Scheme — EOAP). These arrangements are summarised below, with details given in appendix C.

Tariffs

Different tariff rates currently apply across the range of TCF imports:

- 25 per cent for apparel and certain finished textiles;
- 15 per cent for cotton sheeting, woven fabrics, carpets and footwear;
- 10 per cent for sleeping bags, table linen, tea towels and footwear parts; and
- 5 per cent for textile yarns, sewing threads and finished leather.

Some other commodities, such as unprocessed wool, can be imported free of duty, although quarantine restrictions apply.

Under amendments made in 1999 to the *Customs Tariff Act 1995*, items at 25 per cent will be reduced to 17.5 per cent from January 2005, those at 15 per cent to 10 per cent and those at 10 per cent to 7.5 per cent. Those items currently at 5 per cent or less will not change.

Tariffs do not apply to imports from some countries, including New Zealand under the Closer Economic Relations (CER) agreement, least developed countries (since 1 July 2003), and East Timor. However, imports from major developing country TCF producers such as China, Indonesia and India are dutiable at the applicable general rate. Some TCF imports are allowed concessional entry under policy by-laws or the general Tariff Concession System irrespective of their country of origin.

Revenue from TCF tariffs totalled around $950 million in 2001-02. This was about 26 per cent of total tariff revenue for that year, or about 0.6 per cent of total Commonwealth revenue.

Strategic Investment Program

The SIP applies to the financial years from 2000-01 to 2004-05, with two 'pre-program' years, 1998-99 and 1999-00. Funding is capped at $678 million for the life of the program.

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 over more than one year.

Five types of grants are available:

- Type 1: grants for investment in new equipment, associated buildings or alterations and for environmental upgrading (up to 20 per cent of eligible expenditure);
- Type 2: grants for research and development, including innovative product development (up to 45 per cent of eligible expenditure);
- Type 3: value added grants limited to (and conditional on) the amount received under Types 1, 2 and 4 grants. The maximum Type 3 grant payable is capped at 5 per cent of a firm's TCF value added in the year of the claim or the total amount received under Types 1, 2 and 4, whichever is the lesser;
- Type 4: grants for purchases of state-of-the-art second hand plant and equipment as part of restructuring by firms operating in 'TCF dependent communities' (up to 20 per cent of eligible expenditure); and
- Type 5: special miscellaneous grants for ancillary activities relating to restructuring initiatives by firms operating in 'TCF dependent communities' (up to 20 per cent of eligible expenditure).

To minimise the risk of action against TCF firms under WTO rules, assistance to individual firms in any one year is capped at 5 per cent of their annual sales (see appendix C). Also, the SIP legislation makes provision for annual downward 'modulation' of grants to keep expenditures within the funding cap, but this has not been applied to date. Types 1, 2 and 3 grants are administered by AusIndustry, while Type 4 and 5 grants require Ministerial approval.

Appeals related to SIP claims can be made to AusIndustry. Decisions not to register a firm as eligible to participate in the program, not to pay a claim, or to reduce payment for specific claims can also be appealed through the Administrative Appeals Tribunal (AAT). In 2000-01, 16 decisions on registration and claim assessments were appealed to the AAT. However, in the following year, only 2 decisions — both on claim assessments — were appealed (information supplied by DITR).

In 2000-01, $130 million was paid through the SIP (including some $27 million in respect of the pre-program years) and around $100 million has so far been paid for 2001-02 (see table 5.1). (Final figures for both program years will depend on the outcome of current appeals.) To date, Type 1 and 2 grants have accounted for 60 per cent of SIP payments and Type 3 grants nearly all the rest. (Type 4 and 5 grants in total have accounted for less than 2 per cent of payments so far.)

By number, only 5 per cent of TCF companies have so far received support from the SIP. However, those firms receiving SIP funding in 2000-01 accounted for around three-quarters of the TCF sector's value-added and two-thirds of its employment (Information supplied by AusIndustry).

Table 5.1 **TCF SIP program payments (by program year and grant type)**
$'000

Program year	*Type 1*	*Type 2*	*Type 3*	*Type 4*	*Type 5*	*Total*
2000-01	28 251	27 737	45 797[a]	500	1 263	103 549[b]
2001-02	22 272	34 456	42 148	73	28	98 977

[a] The Type 3 payment figure for 2000-01 includes the payments approved in the two pre-program years. [b] In addition, some $27 million was paid in respect of the two pre-program years for eligible Type 1 spending.

Source: Information supplied by DITR.

Expanded Overseas Assembly Provisions Scheme (EOAP)

This program is intended to encourage the use of Australian fabrics and leather by clothing and footwear manufacturers in low-wage developing countries while retaining the higher value added and skilled activities involved in the production of those inputs in Australia. Under the EOAP (scheduled to expire in 2005), footwear and garments assembled overseas from predominantly Australian fabric and/or leather can be imported into Australia with duty payable only on the cost of overseas processing and content. To use the EOAP, the exporter of the fabric or leather is required to be the importer of the assembled goods. There has only been limited use of the EOAP in recent years.

5.3 How do existing arrangements measure up?

The TCF sector has for many years received more generous assistance than the rest of manufacturing. This continues to be the case under the current assistance arrangements. Such high assistance partly reflects the traditional role of the sector as a provider of a large number of jobs requiring only basic skills. The significance of the sector in some regional locations has also played a role. As most of the assistance now provided to the TCF sector comes in the form of tariffs and the SIP, the following discussion focuses on these measures.

The objective of the assistance package is appropriate

The Commission considers that the broad objective of the current TCF assistance package — namely, encouraging the TCF sector to adjust into activities where it will be internationally competitive with lower levels of government assistance — is appropriate. As the sector itself acknowledges, the high levels of assistance provided in the past served to create an inward-looking business culture, where the incentives to raise productivity, improve quality, innovate and seek out new markets were stifled. The costs imposed by this assistance on other groups in the community were also very substantial.

The current package continues the process of bringing assistance to the sector more into line with that accorded to other Australian industries. As well as reinforcing incentives for performance improvement and reducing costs for consumers and user industries, the tariff reductions legislated to take effect in 2005 send a powerful signal that the Government no longer views high tariff protection as an appropriate strategy for this sector.

At the same time, the package recognises that even firms with good prospects of competing successfully in a low tariff environment may need some support in making the necessary adjustments to their operations. Hence, the SIP is aimed at ‘promoting investment and innovation’ (Moore 1997) that will assist TCF firms to improve their international competitiveness during the transition process. In the Commission’s view, well designed budgetary assistance can be beneficial in assisting such a transition, as well as minimising the adjustment costs for both firms and their employees.

Is the assistance package facilitating spending that will raise competitiveness?

As discussed in chapter 2, there have been major changes in the structure of the Australian TCF sector in recent years as it has been forced to respond to global market pressures and declining levels of assistance at home. The restructuring undertaken by many firms has often necessitated new investment in plant and equipment, and spending on R&D. In moving to a lower tariff environment, further investments in these areas will often be required. This has been explicitly recognised in the stated objectives of the SIP.

However, assessing how much new spending to improve competitiveness has actually been encouraged by the SIP in combination with the tariff pause is inherently difficult. This is because it requires some notion of what spending would have occurred had assistance not been provided, or been provided differently.

The problem of establishing the counterfactual is particularly pertinent when attempting to identify impacts on sectoral outcomes. For the most part, these do not indicate an improvement in the sector's international competitiveness. Since the commencement of the current package, aggregate investment declined in both 2000-01 and 2001-02 (indeed, it fell by more than 20 per cent in the latter year). And while R&D expenditure increased by 50 per cent between 1999-00 and 2000-01, this was from a very low base. Over this two year period, sectoral value added and employment have both fallen sharply (despite the tariff pause) and export growth has stalled.

But the counterfactual issue is not the only problem in interpreting the sectoral data:

- Investment and innovation take time to plan and implement, meaning that many of the effects on sectoral outcomes are likely to be delayed. In addition, some firms may make use of SIP assistance in the later years of the program (with the effects of that spending appearing even later). It is also possible that the SIP will have a generally stronger impact on aggregate investment and R&D in the latter part of the program as firms become more familiar with its requirements.
- The aggregate sectoral data include firms with limited longer term prospects which (given the breathing space provided by the tariff pause) continue to operate but may be reducing their investment and R&D spending. This may be offsetting higher spending by firms that are taking advantage of the current arrangements to shift into more viable activities.
- Firm exits that improve the overall viability of the sector will nonetheless contribute to declines in sectoral output and employment.

Hence, the sectoral data may in fact provide little guidance on the success of the package in meeting the Government's objectives. For these reasons, assessments must also consider effects at the firm level. In this respect, the 'early stage' review of the SIP conducted by the Department of Industry, Tourism and Resources in 2002 (see box 5.1) concluded that:

> The experience of the Scheme to date, including the evidence of the claims process for the first year, does provide some confidence that the TCF sector is undertaking significant investment in new plant and equipment and R&D/product development. (DITR 2002, p. 5)

Box 5.1 **Review of the SIP by the Department of Industry, Tourism and Resources**

The Departmental review of SIP was conduced during 2002 and was based on interviews with 61 TCF firms representing a cross-section of geographic, size and activity characteristics (and nominated by the seven main industry associations), 8 TCF consultancy firms and the program administrator — AusIndustry. Written submissions also formed part of the review process.

Among other items, the Terms of Reference for the review asked DITR to:

- establish whether the policy purposes of the SIP were being met; and
- identify what policy refinements for the Scheme, or other changes, might be warranted.

In general terms, the review found that interviewees were generally satisfied that the aim of the program and that its focus on encouraging investment in new plant and equipment, and R&D/product development, was appropriate to improving international competitiveness in the sector.

However, the review found that there were differing views about the effectiveness of the program in meeting its objectives. The major issues related to:

- the eligibility provisions for plant and equipment under the Type 1 grants, including the restriction of eligibility to new plant and equipment;
- the nature of innovation supported under Type 2 grants and whether this was consistent with the type of innovation being undertaken within the TCF sector; and
- administrative interpretations that were seen to be unreasonably narrow — for example, that the definition of innovation had been based on novelty and risk characteristics that were not appropriate for the TCF sector. This issue was a particular concern for clothing firms which participated in the review.

The review team did not propose significant change to the SIP. This was predicated on the arguably narrow judgment that the review's purpose was primarily to establish whether the policy aims of the program were being met. It also expressed concern that providing a more liberal treatment of eligible activities risked forcing the program into modulation and, as a consequence, spreading the available funding too thinly.

Hence a range of suggested amendments raised by review participants were not pursued. These included: extending Type 1 assistance to second hand equipment; more liberal treatment of brand support; de-linking Type 3 value added grants from Type 1 and 2 grants; removing or reducing the $200 000 threshold; and moving to a quarterly payment basis. Instead, the review team proposed that the broad issue of re-configuration of assistance to the TCF sector be examined by the Commission in its post 2005 assistance inquiry. The same sorts of suggestions have therefore been reiterated to the Commission (see chapter 8).

(Continued next page)

Box 5.1 (continued)

The review team did, however, propose a few interim changes, including provision for grant entitlements over the 5 per cent sales cap to be paid in a later year in some circumstances, and preparation and dissemination of policy and decision-making guidelines in relation to: acquisition of new plant and equipment; eligible expenditure on buildings, warehousing and distribution activities; and innovation.

Source: DITR (2002, pp. 4–12)

Similarly, many participants in this inquiry commented that the current assistance package, and in particular the SIP, has helped them to undertake investment, innovation and other activities that have increased their competitiveness (see box 5.2). A survey by the Australian Industry Group (Ai Group) elicited similar responses from member firms (see box 5.3).

In the Commission's view, it would be surprising if SIP support, coupled with the tariff pause, were not inducing firms with reasonable longer term prospects to undertake some additional spending activity. Both forms of assistance add to the financial resources available to a firm: the tariff by supporting prices and indirectly market share; SIP through a direct contribution to firm revenues conditional on having first made investments in plant and equipment, R&D or product innovation. But a much more difficult judgment to make is whether that additional spending has augmented expenditures above what firms would have done anyway in response to broader competitive pressures.

Aspects of the SIP are likely to limit its effectiveness

As discussed above, the sectoral data shed little light on the effectiveness of the assistance package in encouraging the sector to adjust into activities where it will be internationally competitive at lower levels of assistance. Other indicators of the package's impact are therefore needed to determine whether the Government's objectives are being met.

Box 5.2 **Participants' views on the benefits of SIP**

Most participants held strong views that the SIP has encouraged and accelerated investment in plant and equipment and in R&D and innovation. Examples included:

> SIP has increased exports, stabilised employment and encouraged rapid growth in research and capital expenditure, leading to the development of successful niche products on world markets. (sub. 75, p. 2) *Council of Textile and Fashion Industries of Australia (TFIA)*

> SIP has been vital in securing support for continued investment in the latest technologies in plant and equipment, and fostering innovation in new products and processes. (sub. 35, p. 6) *Carpet Institute of Australia*

> 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. (sub. 75, p. 6) *Australian Defence Apparel*

> SIP has allowed us to develop things faster than normal and some benefits have accrued from bringing new capabilities to market faster. (sub. 32, p. 7) *Australian Association of Leather Industries*

> [SIP] gave us the necessary impetus to accelerate our investment in new plant and equipment and in developing new products. (sub. 79, p. 4) *Speciality Coatings Australia*

Some explicitly referred to the role of the SIP in supporting restructuring in the sector:

> SIP has provided necessary and crucial support to the industry during a crucial period of restructuring. (sub. 33, p. 30) *Textile Clothing and Footwear Union of Australia (TCFUA)*

> … SIP has worked well for Bruck. It has provided the necessary encouragement to enable us to undertake necessary operational restructuring, new capital investment and product development to help us reposition our business. (sub. 55, p. 6) *Bruck Textiles*

> … SIP has assisted in accelerating [the] restructuring process through the acquisition of new plant and equipment …, new computer hardware and software for manufacturing, revision of our management information system with regard to production control, and encouraged an innovative product development strategy. (sub. 64, p. 4) *James Nelson Textiles Group*

Yet others said that the SIP had facilitated access to finance:

> The first SIP payment was a clear message to the banks that the government was also genuinely keen to see the business succeed. The fact that the plan had 4 more years to run and that the business had been successful with its first application gave the banks comfort to consider the expansion plans. (sub. 76, p. 5) *Textor*

One suggested indicator was that the amount actually claimed under the SIP was only around half the anticipated expenditure for both investment and R&D nominated by SIP registrants at the start of the 2000-01 program year (DITR 2002). This has contributed to significant underspending of the SIP funding allocation for the first two program years. A major part of this underspend may, of course, reflect the teething problems associated with bedding down a new program. However, advice provided to the Commission by DITR is that there remains a strong likelihood of an underspend of total program funds over the life of SIP despite the clarification of program guidelines that have emerged from the Department's review and an apparently less restrictive interpretation of innovation (see below).

Box 5.3 **The Ai Group survey and the effects of the SIP**

In January 2003, the Ai Group surveyed 123 TCF firms about their views on post 2005 assistance arrangements for the sector. A part of the survey focused specifically on the impact of the SIP on firm behaviour. According to the survey results, those firms receiving SIP funding were more likely to have:

- invested in new capital;
- engaged in product development;
- undertaken more R&D activity;
- started to export or expand exports;
- rationalised operations;
- improved supply chain control; and
- improved labour flexibility.

The Ai Group commented that the results suggest that, faced with lower tariffs from 2005, firms have adopted measures involving a mix of downsizing domestic operations (including staff cuts, moving production offshore and other rationalisation), and an increasing focus on pursuing growth strategies (including product development, new capital equipment, exports and more R&D). The survey found that those firms receiving SIP funding placed a significantly higher level of importance on technological improvement, R&D and investment than those firms not receiving SIP funds.

Though these findings provide a useful perspective on the effects of the SIP, they need to be treated with caution. The number of firms surveyed represented less than 3 per cent of all TCF firms and only around 10 per cent of the sector by sales. Moreover, it is axiomatic that firms receiving SIP funds are more likely to invest in new capital, R&D and product innovation than those firms not receiving funding. Hence, cause and effect are difficult to establish in the survey results.

Source: Ai Group (sub. 11, pp. 17–19).

Lower than anticipated spending on investment and R&D does not, of course, constitute conclusive evidence of the package's failure to achieve its objectives — although to the extent that SIP funding was based on the Government's expectations of what might be achieved, it certainly raises some questions.

However, in the Commission's view, aspects of the SIP — intended to be an important motivator of change in the assistance package — may detract from its capacity to induce new spending that will improve firms' international competitiveness. In this regard:

- SIP support does not depend on firms undertaking *higher* levels of investment and R&D. A portion of total support may therefore be helping to underwrite spending that would have occurred anyway.

- Claims by firms for support are assessed after investments have been made. Although certain definitional issues have now been clarified and guidelines issued, uncertainty about the likely success of claims at the time of investment may still discourage or delay some worthwhile spending initiatives.

In addition, several eligibility restrictions are likely to detract from the achievement of the Government's policy aims.

Notably, while most participants supported the thrust of the program, many repeated the criticisms of specific aspects of its design and application put previously to the review conducted by DITR. Collectively, these perceived shortcomings are likely to reduce the attraction of the program to many firms and hence its capacity to induce new spending that will enhance the sector's ability to compete internationally at lower levels of assistance. The main issues are discussed below.

Targeting investment, R&D and innovation

In seeking to encourage improved competitiveness, SIP targets investment in new plant and equipment, and expenditure on R&D and innovation. According to the Department's review, this targeting is based on the premise that:

> … the key to sustainable and internationally competitive TCF industries in Australia lies in **significant** investment in new plant and equipment and R&D/product development. (DITR 2002, p. 35) [emphasis added]

For some firms this focus is likely to be appropriate because at some stage of the business cycle they will need to invest in plant and equipment and/or product and process innovation. However, other firms might choose to enhance their efficiency in different ways: by improving workforce flexibility; better training and skilling of employees; improving linkages with suppliers and customers; changes to product range; better supply chain management; improved marketing and branding (recognising that some limited support is provided for brand development for 'innovative' products under the Type 2 grant provisions); improved quality of production; reduction in inventories; better IT systems; efficiencies in work in progress; or purchase of productivity enhancing second-hand equipment. The emphasis on such matters will change over time and vary among firms.

Accordingly, many participants argued that the effectiveness of the SIP would be improved by expanding the range of spending initiatives eligible for funding support. James Nelson Textiles Group, for example, requested that funding be made available to develop export markets. It said:

> JNTG believes a framework like the EMDG scheme could be incorporated into the SIP scheme to support market access initiatives within the TCF industry. (sub. 64, p. 7)

Pacific Brands commented that support for 'brand equity' (or promotion) should be increased by incorporating such spending within the investment grant category:

> Under Type 1 arrangements investment in brand equity (pro rated according to the level the brand is locally produced) should also be directly encouraged with a more open, all-media, definition of brand support than used in the limited areas of Type 2 currently. (sub. PP138, p. 5)

Bruck Textiles sought funding for training initiatives. It said:

> SIP (or the appropriate subsequent program) must recognise … and provide specific assistance for skills development within a company. (sub. 55, p.13)

However, as discussed in chapter 8, achieving the right balance between an appropriate range of eligible spending and avoiding excessive dilution of funding support poses major challenges in a program of this type.

The Commission also notes that the current focus of the program on investment and R&D/innovation may not completely constrain the ways in which many firms use funding to improve their competitiveness. This is because assistance is provided after spending has occurred and, as noted above, does not require that such spending is incremental. Hence, provided firms have sufficient 'base' investment and appropriate R&D/innovative activity, they are eligible for SIP assistance which they are free to use in any way they choose, including spending on other initiatives to improve competitiveness.

Rationalisation and restructuring

Rationalisation (including firm exits) and restructuring may be no less important in helping to improve the viability of the sector than investment in plant and equipment, and R&D. As discussed in chapter 3, while major rationalisation and restructuring has occurred in the sector over the past decade or so, there still appears to be considerable scope for this process to continue — particularly in the capital-intensive parts of the sector.

However, while the SIP does provide some support for restructuring through the Type 4 and 5 grants for purchases of state-of-the-art second hand equipment and for ancillary expenditure, this support has been limited to regional areas only. Moreover, even here, the grants paid have been minor, accounting for less than 2 per cent of total grant payments to date (see table 5.1).

Many participants argued that the lack of support for restructuring in metropolitan areas is a major deficiency. For example, the Footwear Manufacturers' Association of Australia said:

> Type 4 and 5 claims have been negligible. It appears the main reason for this is the bias against assisting rationalisations involving metropolitan facilities — as most footwear firms are located in the metropolitan area this has effectively precluded the footwear sector from participating in this element of the scheme. (sub. 28, p. 17)

There were also concerns from firms operating in regional areas. Rocklea Spinning Mills, for example, stated:

> The Type 4/5 (ie Regional Adjustment) Grants have not achieved their stated objectives. The assistance provided should be required to meet the original policy intent (as discussed with Minister Moore when it was first introduced). (sub. 44. p, 9)

Similarly, Austanners said that the Type 4 and 5 grant provisions were not fulfilling their original intention and that this resulted in a claim to consolidate a number of production facilities on the one regional site being rejected:

> Due to a change from what we had been led to expect as to the interpretation of the SIP arrangements this world scale investment [a greenfields site] was not treated as eligible for assistance under the regional component of the scheme. (sub. 73, p. 8)

The Department's review noted that expanding the coverage of Type 4 and 5 grants to provide generalised support for purchases of second hand equipment would dilute the current emphasis of the scheme on investment in new plant and equipment, R&D and product innovation. It did, however, suggest that such a change be examined in the Commission's post 2005 assistance review.

As discussed in chapter 8, the Commission sees a good case for generalising the current Type 4 and 5 grants — not only to remove the current discrimination against firms operating in metropolitan areas, but also because of the more general role that purchases of state-of-the-art second hand equipment can play in boosting firms' international competitiveness.

The scope of innovation

The interpretation of what constituted innovation under the SIP proved a particular problem in the first program year. This issue, however, appears to have been resolved for many claimants through the clarification of program guidelines regarding innovation that have resulted from the Department's review and the growing case history and precedents establishing what activities qualify as being innovative under the program.

A number of participants pointed to improvements in this aspect of the scheme. For example, the Carpet Institute said:

> AusIndustry's definition of innovation (for SIP) is well understood and now working well — as reflected in the reduced number of appeals in the second program year. (sub. PP126, p. 14)

And the City of Greater Geelong commented:

> Certainly in the first year of the program there was a great deal of confusion about this matter, but AusIndustry now appears to be working closely with claimants to clarify the nature of projects undertaken and the companies concerned have every opportunity to explain the nature of the innovation implemented. (sub. PP118, p. 8)

But the clarification of the definition of innovation has not quelled concerns from the clothing sector about the impact of that definition on its access to SIP funding. In particular, many apparel firms argued that the exclusion of 'visual innovation' from Type 2 funding is discriminatory and discourages spending which would help to improve their international competitiveness. S&R Fashions, for example, said:

> … the exclusion of 'visual innovation' from such encouragement works to exclude fashion from the positives of this approach … (sub. 39, p. 5)

And in recommending amendments to the definition of innovation, Pacific Brands commented:

> Currently the interpretation of 'innovation' is the critical determinant of Government support for the non capital intensive clothing industry. … the interpretation of innovation in product development focussing only on 'non-visual' and physical properties bears little relevance to the visually based clothing industries. … We contend that the definition of 'innovation' should be simplified to: 'innovative means a new, improved or different product, process or characteristic that involves an appreciable element of novelty'. (sub. PP138, pp. 5–6)

The company said that this was the definition of innovation used in the R&D Tax Concession Scheme.

Concern was also expressed about the requirement that process improvements be new to the industry rather than to the firm. Some participants suggested that this meant that some productivity enhancing improvements, which lifted a firm's performance to industry best practice, may not be eligible for support.

A number of clothing producers went on to argue that the current definition of innovation is contributing to a disproportionately small share of SIP funding going to the clothing sector.

As discussed in chapter 8, there is no reason why the allocation of SIP funding should be directly proportional to the share of activity in each of the TCF industries. Rather, funding should be allocated to activities where it is most likely to help firms become internationally competitive. In this context, TCF Services said that there is little point providing SIP support for activities which are unlikely to survive in Australia (sub. PP174, p. 12). At the same time, it is important that potentially viable clothing producers have a reasonable opportunity to access SIP funding. Changes proposed by the Commission to the SIP in chapter 8 are designed to ensure this is the case.

Access to funding for small firms

The current minimum spending threshold and high compliance costs (see below) can make it difficult for small firms to secure SIP funding (see box 5.4). The threshold is partly intended to reduce administrative costs by limiting the number of claimants and the likelihood of many small claims. But it also carries the assumption that small firms are not able to undertake significant investment or R&D/innovation, and that the future of the industry lies with large enterprises. As the Department's review of the SIP noted, any reduction in the threshold would also spread available funding more thinly and therefore reduce its capacity to improve the competitiveness of recipient firms (DITR 2002, pp. 35–36).

Yet, just as there are many ways in which firms can improve their competitiveness, small firms can be as (if not more) competitive as large firms in certain activities. Indeed, smallness may be one of the characteristics which contributes to innovation, responsiveness and success in some market areas (eg clothing design and branding). From this perspective, the minimum threshold may detract from the Government's objectives for the sector. Again, however, getting the right balance between avoiding inappropriate discrimination against smaller firms, containing compliance costs and not spreading funding too thinly, poses challenges for program design.

Administration and compliance costs

The costs of administering the SIP appear to be relatively low at $1.6 million since 2000 (information supplied by DITR), although this figure does not include the cost of appeals to the AAT.

However, the complexities associated with the SIP mean that there can be high costs involved for firms accessing the program. A number of firms commented on the costs of gathering and presenting the requisite claim data and in having this information audited. Additionally, many have resorted to using consultants to assist them with SIP claims. While this presumably reflects their perceived value to firms, payments to consultants are often costing firms the equivalent of 10 per cent of their funding entitlements.

Box 5.4 Small firms and the SIP

Various participants suggested that the SIP discriminates unfairly against small firms. The TCFUA, for example, said:

> The current SIP scheme is substantially biased towards large companies. This is no surprise given that they were the only companies consulted during its development. The TCFUA also believes there is a bias in Government towards large TCF companies because they believe these are the only companies likely to survive the future. (sub. 33, p. 33)

The TCF Resource Centre of Western Australia raised similar concerns by saying:

> The SIP program …. [is] against small business and nothing has changed. Small business does not have the amount of money to access SIP … (trans., p. 278)

Some participants identified both the minimum spending threshold and compliance costs as impediments to small business access. The CSIRO — Textile and Fibre Technology — said the $200 000 threshold:

> … has the effect of excluding many small innovative companies that have the potential to drive the development of new products, processes and markets. (sub. 52, p. 8)

Similarly, the Harold Boot Company said:

> The eligibility threshold is too high. Compliance procedures and the post investment claim feature are too complex for small firms.
>
> Addressing this [and other] criticisms would go some way towards adapting the scheme to meet its aim of helping innovative small firms adapt to change. (sub. PP124, p.3)

The TFIA sought to extend SIP support to small firms but only through increasing the overall funding pool. It suggested:

> Consideration be given to the needs of smaller to medium-sized business operators and how they can be encouraged to instil activities and processes assisted by SIP without damaging the overall value to existing SIP clients. (sub. 75, p. 7)

Such compliance costs appear high in comparison to the Pharmaceutical Industry Investment Program (PIIP — less than 1 per cent) and in the Export Market Development Grant Scheme (EMDG — 7 per cent). (See PC 2003a and Austrade 2000.) While very low firm numbers using the PIIP scheme would help to keep compliance costs low, there are a large number of firms accessing the EMDG Scheme.

The clarifications to guidelines flowing from the DITR review, and increasing familiarity with the program's requirements over time, should lead to a reduction in compliance costs. However, SIP remains complex. Accordingly, the scope to reduce administrative and compliance costs is an issue for any successor to the SIP (see chapter 8).

Other issues

In terms of promoting the Government's objectives for the TCF sector, there were a range of other concerns about SIP raised by participants. These included:

- subsidies for investment may result in (or exacerbate existing) overcapacity in some sectors;
- the exclusion of early stage processing, particularly wool processing;
- capping Type 3 grants and the inability to carry forward amounts which exceed the cap;
- a perceived failure to recognise the claimed special needs of regional business; and
- the absence of a link between the provision of assistance and employment outcomes.

Some of these concerns are canvassed in chapter 8.

The package is costly for others in the community

With the substantial decline in tariffs since the late 1980s, the total cost of assistance to the TCF sector is now much lower than in the past. Nevertheless, costs imposed on consumers, user industries and taxpayers remain high.

The Commission estimates that, if selling prices increase to the full extent permitted by the tariff, the total cost of TCF tariff assistance would currently be around $1 billion a year. It would still be around $750 million a year following the legislated tariff reductions in 2005.

In practice, some of the costs of the tariff will be manifest in reductions in the quality of products that are available at particular market price points. Also, competitive pressures may well see some of the costs absorbed by overseas suppliers or retailers in the form of lower margins.

Nonetheless, tariff assistance for the TCF sector adds considerably to the cost of purchasing one of the 'necessities' of life. In effect, TCF tariffs are a 'defacto' surcharge on purchases of clothing and footwear. Indeed, the tariff revenue collected on TCF imports adds an impost equivalent to around 50 per cent of the GST raised on TCF products. And this ignores the price raising effect of tariffs on locally manufactured items. Tariff protection also adds to the costs of industries such as furniture manufacturing which use TCF inputs as well as to the costs of those TCF firms that purchase items from other producers in the sector.

The costs to the community of TCF assistance are increased further by taxpayer funding of the SIP program — some $678 million over a five year period (if available funding is fully expended). However, in terms of the total quantum of assistance provided, tariff protection is worth several times more to the sector than the SIP.

An alternative way of looking at the costs imposed on the community is that tariffs and the SIP together provide support to the sector worth around $13 000 a year for each TCF worker in Australia — including the estimated 25 000 full time equivalent employees engaged in outwork. This is equivalent to around 35 per cent of average earnings across the sector.

This support is much more generous than that provided to other Australian manufacturing industries. The Commission estimates that the TCF sector's effective rate of assistance — a measure which aggregates all forms of assistance into a single measure and expresses it as a percentage of value added — is about five times the manufacturing sector average.

Conclusion

In the Commission's view, the objective of the current assistance package — to assist the sector to adjust into activities where it can be internationally competitive with lower levels of assistance — is appropriate.

However, as a means of giving effect to this broad objective, the current assistance package has shortcomings. In particular, while it appears to be encouraging some new spending that should raise international competitiveness, it is far from clear whether the overall level of induced activity has been, or will be, all that great. The costs imposed on others in the community by the package are also high. For these reasons, simply 'rolling over' the current assistance package after 2005 would not be appropriate. In the following chapters, the Commission has detailed a range of options for post 2005 assistance that would give better effect to the Government's stated objectives for the sector.

FINDINGS ON THE CURRENT ASSISTANCE ARRANGEMENTS

- *The tariff pause coupled with SIP support allows time for consolidation and appears to be encouraging some additional investment and R&D in parts of the sector that should improve international competitiveness.*
- *However, various elements of the package seem likely to limit its overall effectiveness. Moreover, tariffs and the SIP impose large costs on consumers, user industries and taxpayers.*

- *Changes are therefore required so that future support for the sector will better contribute to the Government's objective of encouraging the TCF sector to become internationally competitive at lower levels of assistance and to provide a better balance between this objective and the interests of consumers, taxpayers and the wider community.*

6 Approach to post 2005 assistance

6.1 Views about future TCF assistance

There were a range of views on future assistance policy

Most participants in this inquiry represented TCF (including leather) firms, their industry associations, employees in the sector or particular regions in which the sector operates. Generally, they supported ongoing assistance for the sector (box 6.1) in the form of tariffs and budgetary assistance.

- In regard to the 2005 legislated tariff reductions:
  - Some argued that those reductions should be deferred or cancelled.
  - But many, including some key industry associations, were prepared to accept them, usually with the proviso that considerable budgetary assistance should continue beyond 2005.
- In regard to post 2005 assistance:
  - Nearly all TCF interests argued for an extended tariff pause after 2005. Some countenanced further tariff reductions after such a pause, sometimes nominating particular reduction schedules, but generally with provisos about improved access for exports to other countries, another review of TCF assistance in 2008 or later, and/or significant continued budgetary assistance.
- Some TCF industry participants requested the removal of tariffs on certain imported products, such as some footwear parts, fabrics and yarns.

Only limited input was received from industrial users of TCF products, other sectors affected by TCF tariffs and consumer interests:

- The Furnishing Industry Association of Australia, representing a major textiles and leather using industry, requested 'redress' of the effects of the 'furniture tax' (ie TCF tariffs) on the furnishing industry (sub. 22, covering letter). However, it emphasised that it was not calling for TCF tariff reductions or removal (sub. PP125).

Box 6.1 **Illustrating the assistance requests of TCF interests**

The legislated 2005 tariff reductions:

> … tariff rates for the TCF sector remain at their current (2003) levels until such time as it is proven to be in the interest of Australian workers, their families and communities to reduce them further. That no further review of tariff levels be considered until at least 2012. (sub. 33, p. 6) *TCFUA*
>
> … tariff reductions have been legislated to occur after 1 January 2005, however the City will be actively campaigning to have this legislation repealed. (sub. 16, covering letter, p. 2) *City of Greater Geelong*
>
> The City of Ballarat and local industries would prefer to have the tariff freeze extended beyond 2005 … (sub. 14, p. 5) *City of Ballarat*
>
> We are writing to express our concern at the forthcoming reduction of the tariffs in 2005 … [this] will threaten the jobs of our 53 staff and may result in the closure of our factory. (sub. 8, p. 1) *Tuffa Workwear*

Post 2005 assistance:

> … hold [footwear tariffs] at the 10% [2005] level for the future [until 2015] … any future reductions to be conditional upon reciprocal trade liberalisation occurring globally … a full review before any changes take place … (sub. PP132, pp. 6, 9) *Footwear Manufacturers' Association of Australia*
>
> … the carpet tariff should be held at the 2005 levels for a period of at least 5 years, and any further reductions should be the subject of an Industry Tariff Review. (sub. 35, p. 6) *Carpet Institute of Australia*
>
> Bruck recognises that tariffs are legislated to come down again on 1 January 2005, to 17.5% and 10% respectively for clothing and fabrics … It is imperative … that these duty rates be not reduced further before 2010, at least. (sub. 55, p. 10) *Bruck Textiles*
>
> Our position on the subject of TCF import tariffs on footwear is that they should remain at the legislated level of 10% and that percentage to be maintained indefinitely … any proposed reduction in future tariff levels should be offset by commensurate increases in industry grants and incentives. (sub. 12, p. 1) *National Footwear Retailers' Association*
>
> From SUTG's perspective the preferred option is to defer any further reductions in tariffs [beyond the 2005 cuts] until at least 2010 pending the results of a review of international progress in reducing trade barriers. (sub. 71, p. 16) *Standard Universal Textile Group*
>
> … a 3 step reduction program from current garment rates of 25% down to 10% in 2015 is achievable with minimum economic and social disruption if accompanied by an adequate SIP program extending the current program in place. (sub. 50, p. 2) *Berkeley Apparel*
>
> [The TFIA accepts further] tariff adjustments in the period post 2010 … subject to a commitment by the relevant authorities to examination and finding [that] Australian industry is not faced with the inability to access markets offshore, while continuing to see their own domestic market share eroded … [and subject to] continuation of direct assistance … through the period 2005 to 2015. (sub. PP164, pp. 1,2) *TFIA*
>
> An Australian Industry Group survey of 123 TCF members, representing some 10 per cent of Australia's TCF sector, indicated that some firms would be prepared to accept further tariff declines after 2005, but 'contingent on a pause in tariffs until 2010 and continued government support for domestic TCF firms'. (sub. 11, pp. 17, 36) *Australian Industry Group*

- The National Farmers' Federation recommended that TCF tariffs be reduced as originally planned in 2005 and then be rapidly eliminated by 2010 in line with Australia's APEC commitments (sub. PP104). (Membership of the NFF, the peak industry body representing farmers at a national level, includes producers of fibres such as wool and cotton, which are key inputs into the TCF industries.) WoolProducers, the peak body for wool producers in Australia, supported the NFF's recommendations (sub. PP103), as did Australian Wool Innovation (sub. PP158) and the Victorian Farmers Federation (sub. PP152). This latter organisation also called for cessation of the SIP program on 30 June 2005 as currently scheduled.
- Some importers and retailers requested the selective reduction or removal of tariffs on some particular products, including sporting footwear and clothing.

There was some divergence of views between State Governments. The Victorian, South Australian and Tasmanian Governments opposed further tariff reductions until better overseas market access for Australia's TCF producers was obtained:

> … the Victorian Government will oppose any future unilateral reduction in tariff levels unless progress is achieved …[in]… supporting labour market adjustment; maintaining a critical mass of the manufacturing base; improving export market access; providing incentives for increased innovation and R&D; developing a highly skilled and collaborative workforce; and encouraging inter-firm collaboration. (sub. 78, pp. 4, 2)
>
> The South Australian Government recommends the retention of 2005 level tariffs from 2005 until at least 2010 and until real market access outcomes for TCF companies are achieved … acceptance of tariff reduction in 2005 is contingent upon … continued budgetary assistance … for at least another five years beyond 2005. (sub. 87, covering letter)
>
> The Tasmanian Government agrees with the general principle that reduced Commonwealth Government assistance and protection, and the promotion of international free trade, helps create efficient and competitive industries and businesses … The Tasmanian Government maintains that current tariff rates should be preserved at current levels until our major trading partners bring their tariff and non-tariff barriers into line with ours. (sub. PP180, p. 2)

In contrast, the New South Wales Government indicated that it:

> … would support a continuation of the TCF tariff reduction policy post 2005 until such time as it reaches the general manufacturing tariff rate of 5 per cent … The proposed tariff policy would take the form of transparent, pre-announced, incremental reductions in the tariff level, at a rate that would be similar to the 'effective annual percentage reduction' between 2000 and 2005. (sub. PP175, p. 3)

Support by New South Wales for tariff reductions was conditional on further transitional assistance for the sector, though it also suggested that such assistance ‘should, in principle, be progressively reduced over the proposed period of the tariff reduction and cease within a specified timeframe’ (sub. PP175, covering letter).

The Western Australian Department of Industry and Resources similarly supported the reduction of TCF tariffs to five per cent by 2015 for apparel and certain finished textiles and by 2010 for other TCF products (sub. PP179, p. 2).

Many participants also commented on other assistance measures, particularly the Expanded Overseas Assembly Provisions Scheme (EOAP). Some called for new assistance measures, for example to support export market development and an ‘outreach’ program for small and medium size enterprises.

A variety of supporting arguments were advanced

Those supporting continuing assistance for the sector at 2005 or higher levels presented many different arguments:

- the sector makes an important contribution to the Australian economy;
- many TCF firms would be unable to compete at lower assistance levels;
- reductions in assistance would adversely affect employees, and the cities, towns and regions in which they live;
- more time is required to adjust to existing tariff levels;
- previous government policies impose costs on the sector which should be compensated;
- the potential community gains from further tariff reductions would be small;
- the cost savings from lower tariffs would be retained by retailers rather than leading to lower prices for consumers;
- it would be unfair to the industry if Australia was to reduce its TCF tariffs while other countries maintain their trade barriers;
- unilateral reductions by Australia would squander ‘negotiating coin’ in international negotiations; and
- government revenue would be lost.

Participants’ rationales are explored in detail below, but the following extract from the submission from the Council of Textile and Fashion Industries of Australia (TFIA) provides a summary of many of their views:

> Australia’s textiles, clothing and footwear and fashion industries are on the cusp of a new period of growth and development. With fair and reasonable encouragement and assistance, the industry is gradually redefining itself with a combination of the strengths

from traditional operations and the opportunities arising through a modern strategic industry based on innovation, export success and greater efficiency … The industry provides substantial employment in regional and metropolitan areas, particularly for females. Much of the workforce is particularly difficult to redeploy in other sectors of the economy … Australia is now one of the most open TCF markets in the world. The pace of overall global reform has slowed and the use of non-tariff barriers in overseas markets has complicated historical comparisons of tariff rates … The two most important issues for the Australian industry are **certainty** and **fairness**. (sub. 75, p. 2) [emphasis in original]

Many in the TCF sector believe that they would be disadvantaged by the sort of tariff reduction options outlined by the Commission in its Position Paper. These would see the sector's special assistance treatment removed by 2015, at the latest, irrespective of assistance policy in other countries (chapter 7). The TFIA presented the results of a telephone survey of 87 of its members which, not unexpectedly, found that most respondents preferred the TFIA's conditional approach to future assistance reductions (sub. 164, pp. 6–7).

On the other side of the argument, some participants focused on the benefits to the community of reductions in TCF assistance, or the costs imposed on other industry sectors by continuation of that assistance. For instance, the New South Wales Government identified a number of benefits from tariff reduction:

Such a [tariff reduction] policy would be desirable because it would:

- be in line with broad industry trends for continuing microeconomic reform policies;
- reduce input costs for other sectors and lead to lower costs for consumers;
- facilitate the growth of a TCF import/distribution industry in Australia; and
- signal to other countries Australia's continuing commitment to the APEC trade liberalisation process. (sub. PP175, pp. 3–4)

The NFF considered that the 'fear of job losses' was not a valid argument against tariff reductions. It pointed to the negative effect on farmers of TCF tariffs:

Agriculture is a much larger regional employer than the TCF industries, and is hurt by TCF tariffs. Continued tariff reform is needed to ensure farmers remain competitive and can provide employment in rural and regional Australia. (sub. PP104, p. 9)

It also rejected 'strategic industry arguments' for TCF support (sub. PP104, p. 9) and argued against the view expressed by the TCF industry and some State Governments that unilateral tariff reductions would not be in Australia's best interests.

Although it did not explicitly call for TCF tariff reductions, the Furnishing Industry Association commented on the negative impact of TCF tariffs on its industry:

> The Furniture Tax [ie TCF tariffs] is clearly having a negative impact on the manufacture of product in the industry and is unsustainable. The Tax is a significant depressant on production, employment and industry competitiveness. Local imposts such as the Furniture Tax can make the difference between success and failure in the industry. The future of the furnishing industry in Australia is dependent on the redress of the Tax in a manner which supports the industry's potential to grow and become world competitive. (sub. 22, covering letter)

6.2 The Commission's response

The policy guidelines set out in the *Productivity Commission Act 1998* focus the Commission's attention on improving the welfare of the community as a whole. Similarly, the current terms of reference indicate the Government's desire to improve the overall performance of the Australian economy. In pursuing these objectives, the Commission must consider the wide range of social, regional, economic and environmental interests of the community.

It is explicit in the terms of reference that facilitating the development of a more internationally competitive TCF sector in Australia is an important efficiency goal. Nevertheless, it is important to recognise that assistance for TCF production, for example through tariffs and budgetary support, imposes costs on consumers and other industries — as Gilmour's (a footwear importer and retailer) noted, 'import duties are really just another tax on consumers' (sub. 81, p. 3). Just as the benefits of TCF activity flow through the economy, so too do the costs of assisting that activity.

These costs have two separate dimensions. First, assistance to the TCF sector affects the efficiency of resource use across all sectors of the economy, including within the TCF sector itself. Second, assistance to the TCF sector imposes costs on users and consumers of TCF products. The Commission's task is to formulate policy options that balance competing interests to produce beneficial outcomes for the community as a whole.

When considered within this framework, the arguments advanced for continuing special assistance treatment for the TCF sector are not persuasive. On the contrary, there are good reasons why the legislated 2005 tariff reductions need to go ahead and further tariff reductions made beyond that date. The rest of this current section discusses arguments for and against assistance reductions in some detail, while the next section (section 6.3) sets out the Commission's approach to post 2005 assistance.

Assessing arguments against further assistance reductions

The sector's economic contribution is no justification for continuing special treatment

The TFIA presented a range of information and data about the role of the TCF sector in the Australian economy (box 6.2). It contended that:

> The economic significance and contribution of the TCF&L industries is unique — whether the focus is employment, technology, design or involvement in a knowledge-based economy. Its economic importance and strategic significance has been well recognised, and responded to, by Governments all around the world. (sub. 75, p. 18)

The Commission recognises that the workforce and regional characteristics of the sector are somewhat different from other manufacturing (chapter 4), and that reductions in TCF assistance would impose costs on firms and their employees, as well as flow-on costs in the cities, towns and regions in which they are located. For this reason, the Commission has given particular weight to adjustment issues when evaluating future assistance strategies (see below).

But a sector's contribution to the economy, however important, does not itself justify special assistance treatment:

- Industries and firms in all sectors contribute to the economy. All manufacturing industries, for example, provide employment, produce and invest, purchase inputs and sell outputs. Many export. To a greater or lesser extent, all industries form part of vertically integrated activity. Hence, multiplier effects flow from all such activity.
- Australia should aspire to have industries that are internationally competitive while offering well paid jobs to skilled employees. Those parts of the TCF sector which can only survive with high assistance and by keeping wages low, do not contribute to this goal.
- Assistance to a particular sector, such as TCF, imposes costs on other sectors which reduces their economic contribution.

There might be a case for special assistance treatment if the sector provided substantial benefits to other parts of the economy, for which the sector itself received no reward. For example, expenditure on R&D by a particular firm might 'spill over' and be freely employed by other firms throughout the economy. But, notably, the TCF sector's expenditure on R&D is lower than in most other industries. Moreover, even in the absence of SIP, the TCF sector would still have access to the various general programs designed to encourage investment in R&D.

If there are deficiencies in these general programs, it is usually better to address them directly, than to provide compensating support to specific sectors.

Box 6.2 **Summary of the TFIA's comments on the significance of the sector**

The TCF&L industries provide employment for nearly 80 000 people (ABS Labour Force Survey estimates). For every job generated in the sector, a further 2.5 to 3 jobs are created indirectly.

This is of particular significance to key regional areas, such as Geelong, Bendigo, Devonport and Wangaratta, which are heavily reliant on employment opportunities created by the sector.

As well, it employs a large number of females. TCF firms employ between 15 and 18 per cent of females involved in manufacturing in New South Wales and Victoria.

Industry investment is substantial (nearly $10 billion over the past decade), industry output was over $9 billion in 2000-01 and value added of $2.6 billion in that year accounted for over 3.6 per cent of total manufacturing value added. There are close linkages with other industries, both in manufacturing and in the services sector.

The TFIA believes that the TCF sector contributes to the Australian economy in several areas that are not generally recognised. For instance, TCF firms significantly invest in human capital and skills formation, invest in product and process improvement, are adopting best practice manufacturing methods and technologies, and help to build Australia's reputation as an exporter of complex manufactured products. Assistance from SIP and developing closer links to universities and research institutions have helped in this process.

According to the TFIA, there is potential for the TCF&L industries to grow at a significantly faster rate in the next five to ten years. The main sources of this growth would be:

- improved productivity associated with effective use of new IT and production technologies;
- the continued development of niche demands in the Australian market;
- increased exports of innovative products; and
- further growth through demand for innovative Australian fashion designs.

TCF&L manufacturers, by demanding high standards of cost and quality competitiveness from suppliers of materials, will also spur greater productivity and competitiveness across the wider economy.

Source: TFIA (sub. 75, pp. 18–24).

Tariffs and other assistance should not be used to compensate for other policies

The Footwear Manufacturers' Association of Australia (FMAA) sought assistance to 'offset costs associated with the effects of previous policies' such as:

- state based decentralisation programs causing structural inefficiencies and fragmenting capacity;
- import replacement and self sufficiency manufacturing strategies;
- employment intensive operations. (sub. 132, p. 4)

Certainly, some previous assistance and other government policies may have caused, or helped to sustain, inefficiencies in the sector. Rather than continuing to provide indefinite compensation for the costs imposed, however, the sensible policy approach is to seek to remove the causes of distortion in a considered and timely manner. This is especially so when the means of compensation, such as tariff protection for the TCF sector, itself causes economic and equity distortions elsewhere in the economy.

Trade based arguments are understandable but not compelling

Not surprisingly, Australian producers competing with TCF imports, albeit subject to tariff, regard it as 'unfair' that they cannot gain satisfactory access to many other countries' markets because of trade barriers. Many argued that further tariff reductions by Australia before other countries lowered their trade barriers would exacerbate this situation. The Australian Industry Group, for example, contended that there should be no reduction in Australia's TCF import tariffs 'until tariff and non-tariff barriers in overseas countries are reduced proportionately to levels that exist in Australia' (sub. 11, p. 39). The ACTU indicated that it:

> … believes the TCF sector has a viable future in Australian manufacturing and is of continuing importance to rural and regional Australia. To secure this future it is vital that tariffs be paused at present levels until further Review in 2012 or such time as tariffs and non-tariff market access barriers in other countries are significantly reduced. (sub. 92, p. 1)

The Geelong Chamber of Commerce similarly argued that:

> … to be fair to all involved, Australia should not 'lead the march' world-wide to reduce its import tariffs. The Chamber believes and strongly makes the point that Australia should not allow any further tariff reductions unless there is open, transparent and unconditional agreement and a guarantee that its trading partners will definitely do likewise. (sub. 62, p. 4)

And the TFIA commented:

> … the industry is struggling to understand how the unilateral reductions in the Australian instance could lead to a better outcome overall if the export focused companies cannot obtain at least the volume of production that is lost due to the reduction in the Australian barrier arrangements. (sub. PP164, p. 8)

However, there are good reasons why Australia's assistance policies should not be set on the basis of 'fairness' nor be automatically linked to progress in trade liberalisation overseas. Fairness/equity is in the eye of the beholder. For example, Australian TCF tariffs could be regarded as unfair to those groups in the community that must pay higher prices for footwear, clothing and other items to support local producers. Also, other industries might see it as unfair that they do not get similar assistance.

Moreover, the concept of fairness would be very difficult to apply in trade or assistance policy formation. For instance, which of the many different countries and assistance regimes would be chosen to trigger assistance changes in Australia? Would different countries or trigger levels apply to different commodities? Rules of thumb — such as the suggestion by the FMAA that further tariff reductions for footwear only occur if 'more than 85% of world trade in footwear is subject to a tariff of 10%' (sub. PP132, p. 6) — could be used. But how would non-trade barriers be factored in? Such rules, if adopted by several countries, would just become a recipe for inaction. Multilateral negotiations in the WTO and other international trade organisations pursue a rules-based global trading system, divorced from emotive and ill-conceived sectoral notions of fair or balanced trade.

Above all, linking Australia's assistance policies automatically to overseas policies would disregard what is in Australia's national interest. For instance, such linking would ignore the range of domestic considerations that have been central to assistance reductions for the TCF and other sectors over the past 15 years and which remain relevant to future assistance decisions. As discussed below, these include the costs imposed on consumers and other Australian industries, including exporters, by TCF tariffs, as well as the potential productivity stimulus from exposing the sector to greater international competition.

These domestic considerations have meant that, in the past, the gains to Australia from trade liberalisation have come mainly from unilateral removal of protection rather than from the bargaining with other countries. This is likely still to be true — CIE modelling commissioned for this inquiry indicates that the benefits to Australia from unilateral TCF tariff removal would exceed the benefits it would receive from removal of TCF protection by either the United States, the EU or China (CIE 2003). Further, the gains from Australia's own liberalisation efforts are more certain, and more immediate, than those dependent on liberalisation elsewhere.

There might conceivably be some benefits from slowing or pausing assistance reductions in Australia if this were to increase leverage in international trade negotiations, or if it avoided short term damage to domestic producers which would be viable in the longer term with better access to overseas markets.

Arguments about negotiating leverage were raised by several participants. For example, the Carpet Institute of Australia argued that:

> … further tariff reductions should only arise as a result of negotiated outcomes with our trading partners and where there is clear reciprocation in trade liberalisation from those partners. Furthermore, it would be counterproductive to reduce Australia's TCF tariffs unilaterally as a result of this Review as this would eliminate our negotiating leverage in future trade talks. (sub. 35, p. 28)

Similarly, Bruck Textiles contended:

> If Australia is embarking on a series of FTA negotiations, then surely it is in our interests to retain our global tariffs as high as possible, so that we have some negotiating leverage. This applies equally to the Doha Round negotiations as it does to individual bilaterals. (sub. 55, p. 14)

And the Victorian Government stated:

> If Australian TCF tariffs are reduced unilaterally, and Australia's negotiation partners are already able to import relatively freely, Australia will have limited leverage in seeking TCF tariff and non-tariff barrier reductions in future trade negotiations. (sub. 78, p. 5)

However, the Australian market is small in world terms, accounting for less than one per cent of global TCF sales. As well, imports already have around 50 per cent of the domestic TCF market, and as much as 70 per cent of the clothing and footwear market (chapter 2). Hence, for other countries collectively, there can only be a very modest gain from better access to the Australian TCF market.

Even if the potential gain for a particular country was more significant, WTO rules effectively prohibit countries from negotiating product specific deals limited to two trading partners. Also, multilateral negotiations proceed on the basis of 'bound' rather than applied rates. Australia's bound rates for TCF tariffs are much higher than the rates currently applied. Were the negotiating coin argument for TCF to have any weight, and this is extremely doubtful, the option of negotiation on the basis of these higher bound rates would remain open to Australia, even if it were to further reduce its applied tariffs.

Finally, it would appear that very few 'at risk' Australian TCF firms would have their future guaranteed by better access to overseas markets. Discussions with, and submissions from, participants provided no notable examples. Although a recent study conducted for the sector estimated that Australia could expect to gain additional exports in the range of US$50–100 million from improved market access in Asia (Werner 2003, p. 7), this figure is small in the context of existing sales levels of about $9 billion and exports of about $1 billion. This reinforces the conclusion that the future viability of most firms will depend on inherent features of their business models and sustainable competitive advantages. While improved overseas market access could help some firms which are already internationally competitive, in the Commission's view, it is seldom likely to be a make or break issue for firms yet to make this transition.

This is not to argue that Australia should in any way relax its attempts to secure improved overseas market access for TCF and other exporters (chapter 11). Internationally competitive exporters would clearly be better off if they had unfettered access to overseas markets.

In summary, future Australian TCF assistance reductions should not be linked to improved access to overseas markets. Such an approach would have few benefits. And any benefits would be highly unlikely to outweigh the costs and risks involved.

Loss of tax revenue?

Although the purpose of TCF tariffs is to protect local activity, they raised revenue of some $950 million in 2001-02. Flicker's Australia (sub. 63, p. 7) suggested that 'there can be no net benefit to the economy as tariff revenue lost is replaced by tax increases elsewhere domestically or by reduced domestic government spending'.

TCF tariff revenue, however, makes up less than 0.6 per cent of total Commonwealth Government revenue. Moreover, the tariff options considered by the Commission (chapter 7) involve only gradual removal of tariffs at a time when imports are likely to continue to grow. Thus, the revenue effect from lower tariffs would be offset to some extent by increases in import levels.

More importantly, the revenue generated is not, of itself, a reason for maintaining tariffs provided that the overall effect of tariff reductions on community welfare is positive (taking account of the benefits and costs arising from increases in other taxes or reductions in government spending to match any loss of tax revenue). The quantitative modelling undertaken for the Commission during this inquiry incorporates the net effects of changes in tariff revenue and tax mix.

Arguments favouring further tariff reductions

While the potential for resource allocation benefits has diminished, there are worthwhile long term gains

Reductions in TCF assistance will allow some economic resources to shift into activities that generate higher returns for the community. But with assistance now much lower than in the past, and the sector shrinking, the potential for resource allocation gains from further tariff reductions is diminishing. Hence, the quantitative modelling commissioned for this inquiry — which focuses primarily on such resource allocation effects — not surprisingly indicates that gains from removing the sector's preferred assistance treatment would be very small (box 6.3 and appendix E). Because the static resource allocation benefits of future TCF assistance reductions are small, benefits and costs not encompassed in the modelling, together with considerations of equity, have become the primary consideration in policy formation.

Assistance reductions encourage firms to become more productive and internationally competitive. Undoubtedly, adjusting to increased international competition is often hard, requiring that firms and their employees make significant changes. But the experience in many industries that have been through this process shows that the benefits can be substantial. In being forced to deal with the removal of their protective cushion, many firms have identified opportunities — previously considered unlikely or impossible — where they can compete with the best in the world.

Australia's strong and sustained growth performance of recent years has paralleled a broadly-based program of microeconomic reform, including the progressive dismantling of most trade barriers. The much greater responsiveness, innovativeness and flexibility now evident in many Australian firms should provide a springboard for sustaining strong output and employment growth in the future. It also increases the resilience of the economy to external shocks.

There is nothing to suggest that these effects of assistance reduction will be less pronounced in the TCF sector. Indeed, earlier chapters describe changes in the sector which have come about in response to a wide range of global and domestic pressures, including domestic assistance settings. While the TCF sector as a whole has contracted, many firms have responded well to increased competitive pressure by reducing costs, improving productivity, developing innovative products, and improving customer service and links to suppliers.

Box 6.3 Modelling the effects of TCF tariff reductions

Economic modelling can indicate some of the likely effects and adjustment pressures of post 2005 assistance options for the sector, TCF regions and the wider community. Modelling, of course, cannot replicate reality. For example, it does not take account of the full range of adjustment costs, nor does it allow for the productivity improvements likely to be stimulated by reduced TCF assistance (see text). For such reasons, modelling can be only one input into an assessment of policy options.

The modelling results (appendix E) suggest that the resource allocation gains from reducing tariffs to 5 per cent after 2005 would be very small. After adding in terms of trade effects, the projected community welfare gains would become even smaller, and possibly negative. (These terms of trade effects depend on assumptions about export demand elasticities which, as noted in appendix E, are a subject of controversy.) This outcome contrasts with previous modelling exercises where terms of trade effects were swamped by the resource allocation gains from reducing very high protection.

At a more detailed level, the modelling projections indicate that a reduction in TCF tariffs to 5 per cent, together with the cessation of SIP support, would over the longer term:

- Reduce activity and employment in the TCF sector relative to the ‘business as usual’ base case. In the MONASH model, projected reductions in output and employment across the TCF industries average about 4 per cent, with somewhat larger falls in the footwear and knitting mill products industries. In the Econtech MM600+ model, aggregate output and employment in TCF are projected to decline by up to 15 per cent in the long term. Results of ACIL-Tasman modelling lie in between. The National Institute of Economic and Industry Research (NIEIR) results presented by the Victorian Government suggest a total TCF employment loss in Victoria of about 6300 jobs, but this estimate includes the effect of the already legislated 2005 tariff reductions. As discussed in chapter 4, when adjusted for this, projections of TCF job loss in the State from the post 2005 assistance options considered by the Commission decline to about 4000 — a figure quite consistent with projections from the other models. Employment results for the TCF sector from MONASH modelling undertaken by the Victorian Treasury were not reported.
- Lead to a slight decline in total employment in Victoria relative to the base case — by 0.4 per cent (7800 jobs) in the MM600+ projections, and 0.02 per cent (460 jobs) in the MONASH longer term projections — with even smaller balancing increases in employment in most of the other States and Territories. Total state employment projections were not provided in the ACIL-Tasman, the NIEIR or the Victorian Treasury results. In the latter case, though, the projected reduction in the State’s output of just 0.02 per cent suggests that the net employment loss would also be very small.

From this perspective, further reductions in assistance could reinforce competitive pressures on TCF producers to improve technology, to better integrate production and distribution, to improve firm and industry organisation, and to improve workforce flexibility and workplace arrangements. Also, managerial effort that, in parts of the sector, has been devoted to preserving high assistance and looking for ways to garner and 'game' government support, could be directed to improving international competitiveness. As well as enhancing the sector's future prospects and bringing lasting benefits to TCF firms and their employees, such changes would benefit the wider community.

Some participants specifically alluded to the role of earlier tariff reductions in spurring improvement within the sector. For example, the New South Wales Government considered that TCF reforms have 'enabled many Australian manufacturers to become more flexible and responsive to emerging market opportunities' (sub. PP175, p. 1). The Technical Textiles and Nonwoven Association commented that:

> Trade liberalisation and, thus, increased competition across all global economic activities has produced comprehensive changes to markets worldwide … Indeed, the most influential factor in shaping Australian manufacturing has been the process of opening Australia to the influence of international market forces through the reduction of tariffs. The impact of lowering tariffs is a transitional force across products in all targeted tariff chapters and has resulted in considerable change to the industry, its products, their competitiveness and the way in which business is done. (sub. 68, p. 3)

Ulster Tascot similarly noted that:

> Tariff reductions to date, have had the desired effect of opening our markets to competition and encouraging manufacturers to produce quality products at world competitive prices. (sub. 53, p. 4)

Conversely, continuing tariff assistance could stimulate production which, without tariff assistance, would not be sustainable. For example, the Northern Grampians Shire Council asserted that a new cut-and-sew project at AUNDE Australia 'progressed on the basis that tariff protection enabled the facility to be competitive against the existing supplier in Thailand' (sub. PP133, p. 1). It is clearly not in Australia's longer term interests to broaden its activity base if that needs high government support to survive.

None of this suggests that achieving further productivity improvement in response to reduced assistance will be easy or will come without cost. This is why, as discussed below, the Commission considers that future tariff reductions should be accompanied by substantial transitional budgetary assistance. But it does indicate that the benefits of a successful transition by the TCF sector to lower assistance are potentially sizeable.

Users and consumers would benefit

Further reduction of TCF tariffs would undoubtedly reduce the costs imposed on user industries and final consumers of TCF products. Existing tariffs tax these groups by up to about $1 billion a year (chapter 5).

As noted, the furnishings industry pointed to the costs currently imposed on it by TCF tariffs, referring to these as the ‘furniture tax’. Even some firms within the TCF sector would benefit from cost reductions arising from further tariff reductions. Indeed, users of intermediate TCF goods such as fabrics and footwear parts requested tariff reductions on those goods (see below).

Several participants argued that cost savings from lower tariffs on TCF products would simply increase the profit margins of distributors, retailers and shopping centres, rather than benefit consumers.

In the Commission’s view, however, that ignores market realities. The global TCF industry is brutally competitive, with new production centres and surplus capacity putting intense pressure on wholesale prices. In these circumstances, attempts by importers to retain the benefits of lower tariffs would be futile — distributors and retailers would simply source those items more cheaply elsewhere.

Similarly, the Commission has seen no evidence that Australian retailers are making excessive profits. On the contrary, as Coles Myer asserted:

> The retail environment is intensely competitive with growing numbers of retailers of all sizes, often operating with very similar offers. Each retailer is striving to gain a greater share of the consumer’s limited spend on apparel which is placing continuing downward pressure on prices. (sub. 95, p. 1)

Indeed, the real price of TCF products has been falling over time, notwithstanding (until recently) depreciation of the Australian dollar. The Commission also notes that nominal prices at the retail level have been rising more slowly than the wholesale prices received by Australian TCF producers.

This does not mean that price reductions or quality improvements at established market price points will immediately follow tariff reductions But over time, the competitive nature of importing, wholesaling and retailing will inevitably see benefits flow through to consumers. Several TCF firms made the point that, in contrast to a decade ago when tariffs were much higher, Australian consumers can now purchase some clothing and footwear as cheaply as, or more cheaply than, their counterparts in parts of Asia, Europe and the USA. Carpet producers similarly acknowledged that increased import competition has resulted in consumer price reductions (see sub. 173, p. 9). Further tariff reductions would provide further cost savings for consumers.

Further assistance reductions could contribute to Australia's broader trade policy objectives

Australia has a number of international commitments which are relevant to consideration of future TCF assistance. The terms of reference draw particular attention to:

- Australia's commitment to free and open trade and investment with APEC members by 2010 [the Bogor goal], its WTO obligations with respect to subsidies and its broader trade liberalisation objectives; and
- bilateral trade negotiations and possible Free Trade Agreements.

The economic gains to Australia from further global trade liberalisation are many times greater than the effects of changes to its TCF assistance levels. Thus Australia's national interests would not be served by assistance policies for the TCF sector that in any way compromised the prospects for wider trade liberalisation. A policy of indefinite preferment for the sector, or making assistance reductions conditional on actions by other countries, would send the wrong signal, not only in an APEC context, but also in wider forums. The National Farmers' Federation argued that Australia's 'international credibility could be totally undermined if we say one thing at the WTO but do the opposite back home' (sub. PP104, p. 11). More specifically, WoolProducers stated that it supports the 'removal of domestic tariffs [as that would] enhance opportunities for reducing tariff barriers for our wool exports' (sub. PP103, p. 1).

6.3 The Commission's approach

For the reasons set out in the previous section, the Commission considers that further tariff reductions would bring community-wide benefits in the medium to longer term that would more than offset the adjustment costs imposed on the TCF sector. However, reductions should be made in a measured manner, accompanied by continuing transitional assistance, to help ease the adjustment process.

Re-commence tariff reductions

In the Commission's view, the options of reversing the legislated 2005 tariff reductions, or pausing TCF tariffs at 2005 levels for a very extended period, should be immediately ruled out. It believes that tariff reductions already legislated should come into effect on 1 January 2005 as scheduled and that there are good reasons for legislating further tariff reductions for the sector beyond that date.

There are no overriding characteristics of the TCF sector, or of the markets in which it operates, which, in the Commission's view, would justify providing the sector with higher long term levels of assistance than are provided to other Australian industries. Except for the TCF sector, all general tariffs in Australia will be at five per cent or less by early 2010. In the Commission's view, the tariff target for the TCF sector should also be five per cent.

The Commission rejects charges by some participants that it is driven by ideology. It also rejects the charge of the ACTU that the Commission 'goes to farcical lengths to support its prior view that TCF tariffs should be cut' (sub. PP169, p. 4). The discussion above recognises that there will be costs from further tariff reductions for the TCF sector, its workforce and affected regions. But the Commission's analysis and judgment is that the medium to longer term benefits to the community overall will more than outweigh those costs, given appropriate phasing of tariff reductions and the provision of adequate transitional assistance. In particular:

- Assistance reductions would encourage the sector to continue to improve its international competitiveness through such means as increased investment and innovation, technological development, enhanced quality and more cooperative workplace arrangements. Such changes would help to secure the future of TCF firms and their employees and increase the value of the sector's contribution to the Australian economy.
- It would also send a message to producers across the economy that the government is not in the business of sheltering firms from competitive pressures to the detriment of the wider community.
- Consumers and users of TCF products, including some firms in the TCF sector itself, would benefit from lower prices. The imperative to seek assistance reductions through other arrangements such as the Tariff Concession System and the EOAP would thereby be reduced, with savings in administrative and compliance costs.
- Further reductions in tariffs after 2005 would send helpful signals to other countries about Australia's commitment to reduce trade barriers in line with its APEC and other international trade policy commitments.

Allow sufficient time for adjustment

As noted, the Commission considers that adjustment capacity is a crucial concern in determining the pace of future assistance reductions:

- past adjustment has already imposed costs on TCF firms, their employees and the regions in which they operate;
- many of the sector's workers (particularly employees and outworkers in the apparel industry) are among the most vulnerable in the community; and
- although regional TCF activity is lower than in the past, and regional economic growth and development has been generally strong in recent years, some particular towns and regions remain vulnerable to firm closures and reduced output.

Too rapid a reduction in assistance would add unnecessarily to the broader and significant competitive pressures confronting the sector. In so doing, it might affect adversely the prospects of some firms which, given more time, could become internationally competitive.

Achieving the right balance between the community-wide gains from assistance reductions and adjustment costs requires careful judgment. However, in the Commission's view, the need to minimise the risk of disruptive adjustment associated with assistance reductions rules out the option of very quickly removing the sector's preferred assistance treatment after 2005.

Continued transitional assistance is justified

The current SIP is intended to assist TCF firms to prepare for the tariff reductions legislated for 2005: that is, to help them compete successfully with lower levels of assistance. Given the Commission's view that further tariff reductions should be made post 2005, it would be appropriate to extend transitional assistance. Indeed, without an extension of such support, it may be difficult to meet the Government's objectives for the sector in a reasonable timeframe without undue disruption.

In the Commission's view, however, the continuation of transitional assistance post 2005 should be conditional on the recommencement of tariff reductions. Without this link, budgetary support would just become an additional form of long term assistance for the TCF sector. While many in the sector sought continuation of SIP assistance without linkage to further tariff reform, Pacific Brands agreed that 'acceptance of transitional adjustment assistance [should be] conditional on the acceptance of lower tariffs' (sub. PP138, p. 2).

There is a need for policy certainty

The pressures and uncertainties confronting firms in the TCF sector are intense. A clear and extended path for assistance reductions would remove one source of uncertainty. Without clear policy direction, investment that would help some firms to operate successfully with low assistance could be put at risk. Accordingly, the post 2005 tariff and transitional support options outlined below establish an assistance regime for the sector for the decade through to 2015.

A further review would be counterproductive

Many participants argued that there should be a 2008 (or later) review of TCF assistance before any post 2005 tariffs cuts went ahead. For example, the TFIA noted that:

> … the industry has continued to argue that there should be a review in 2008 (or there about) of the reforms in tariff and non-tariff barriers that are being implemented [overseas, before further tariff reductions go ahead in Australia]. (sub. PP164, p. 8)

In the Commission's view, the prospect of a 2008 (or later) review would:

- detract significantly from the policy certainty that is vital for the sector at its current stage of development;
- induce some firms to delay new investments and other adjustments that would help them to operate successfully with lower tariffs; and
- inevitably divert managerial energy into further lobbying to preserve the sector's special assistance treatment.

For these reasons, the Commission does not favour a further review.

FINDINGS ON THE APPROACH TO POST 2005 TCF ASSISTANCE

- *While TCF activity has some distinguishing characteristics, these do not warrant indefinite preferential treatment for the sector.*
- *A policy of tying tariffs protecting Australian TCF producers to levels in other countries would not be in Australia's interests.*
- *Further TCF tariff reductions would reinforce incentives for productivity improvement, provide benefits to consumers and industries using TCF products, and facilitate Australia's trade policy objectives.*
- *The legislated tariff reductions for the sector should take effect on 1 January 2005 as scheduled and further reductions should be made after 2005. Those reductions should be implemented in a measured manner over time, accompanied by transitional assistance to help facilitate the adjustment process.*

- *The tariff target should be 5 per cent, the maximum rate that will apply to all other Australian industries from 2010.*
- *To avoid uncertainty affecting investment and production decisions, it is important to lay down a path and timetable now for the sector to reach that target.*
- *Making provision for further review of TCF assistance would detract from the policy certainty the sector needs and diminish the pressure on firms to improve their international competitiveness.*

7 Post 2005 tariffs and related assistance issues

A range of tariff reduction options would be consistent with the Commission's approach to post 2005 tariffs outlined above. Judgment is required about which particular option, in conjunction with transitional assistance (chapter 8), offers the best chance of encouraging increased international competitiveness in the TCF sector, in a reasonable timeframe, while minimising adjustment costs. This chapter also discusses several tariff related issues including policy by-laws, the Expanded Overseas Assembly Provisions Scheme (EOAP) and requests for duty free entry of particular TCF products.

7.1 Tariff options outlined in the Commission's Position Paper

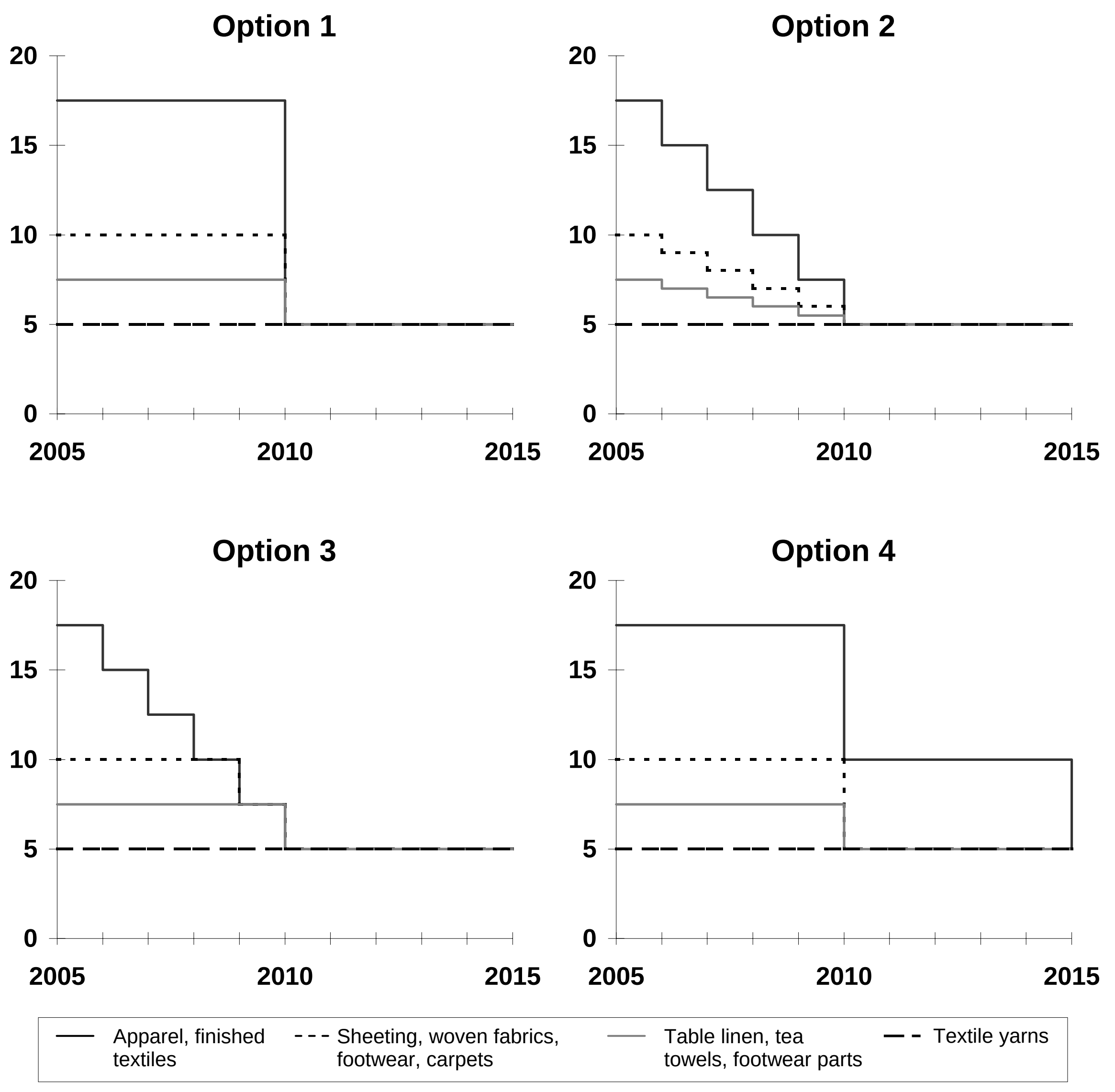
The Position Paper set out four options to illustrate the issues involved in choosing a preferred tariff time path. In these options, all reductions would occur on 1 January in the relevant year (figure 7.1):

- Option 1: Maintain all TCF tariffs at 2005 levels until 2010, then reduce to 5 per cent and maintain to 2015.
- Option 2: Reduce all 2005 TCF tariffs in even annual steps to achieve 5 per cent in 2010, then maintain to 2015.
- Option 3: 'Tops down' to 5 per cent in 2010, then maintain to 2015. (That is, higher tariffs are reduced before lower tariffs.)
- Option 4: As for option 1, but reduce tariffs on apparel and certain finished textiles to 10 per cent in 2010 and then to 5 per cent in 2015.

Apart from the differences in the treatment of apparel and certain finished textiles — option 4 would delay the final tariff adjustment for those industries until 2015 — the main difference between these options relates to the manner in which the tariff adjustments are made: stepping (ie at the end of the relevant period), phasing (during the period), or a combination of the two (tops down). Self evidently, phasing or tops down adjustment could also be incorporated in the option 4 approach.

Figure 7.1 **Post 2005 tariff options**

per cent



In the Position Paper, the Commission indicated that, subject to further consideration in response to participants' comments on the advantages and disadvantages of the different options, it preferred option 4.

In reaching this judgment, the Commission considered it is appropriate for tariffs on goods other that apparel and certain finished textiles to be reduced to 5 per cent in 2010 — this would require further tariff reductions (after 2005) of five percentage points or less. However, the Commission expressed doubt about the capacity of apparel and certain finished textile producers to absorb a tariff reduction of 12.5

percentage points over the 2005 – 2010 period, as required by options 1 to 3. It acknowledged that there would be some risk that such a rate of tariff reduction might cause excessive disruption in those industries.

Participants' responses

Many participants reiterated their general views on tariffs (discussed in chapter 6), rather than commenting on the merits of the four options proposed by the Commission. Some, including the TFIA, the Carpet Institute of Australia and the FMAA, did propose possible future tariff change arrangements. But these were conditional on improved overseas market access and involved slower changes and/or higher tariff end points than contemplated by the Commission.

It can be surmised that, if forced to choose, most industry participants would favour the 'softer' stepped down approach to tariff reduction over the 'tougher' phasing or tops down approaches. Yakka, for example, commented that 'a 5-year period of stability and then a stepped down approach is much more manageable for the industry' (sub. PP128, p, 6).

However, the Carpet Institute and the FMAA supported variations of the tops down approach which, in effect, would enable the carpet and footwear industries to retain their current tariff rates for a longer period than under any of the options outlined in the Position Paper. Indeed, the Carpet Institute, together with some individual carpet manufacturing firms, argued that an 'anomaly' exists in the tariff treatment of carpets. It claimed that in the 1991 Industry Statement, which accelerated tariff reductions for the TCF sector, 'carpet was inadvertently linked in with intermediate products', whereas carpet should have been treated as a finished consumer textile product and thus subject to the same tariff as apparel and certain finished textiles. Although it did not request the carpet tariff be increased, the Carpet Institute proposed that 'further reductions in carpet tariffs (after 2005) should be deferred until other finished consumer textile products come down to carpet level' (sub. PP126, p. 10). The Commission, however, does not accept the tariff 'anomaly' argument: there are other finished TCF products that have lower tariffs than carpets; and in any case, so-called 'anomalous' tariff decisions made 12 years ago or more, provide no guidance for appropriate post 2005 tariff arrangements.

The Commonwealth Department of Agriculture Fisheries and Forestry favoured option 2 or option 3, on the basis that they were considered to be most in line with Australia's trade interests (sub. PP176, att. A, p. 2).

The New South Wales Government favoured a tariff option in which annual reductions in tariffs would occur post 2005, with the target of five per cent being met, depending on the product, from 2009 to 2014. It considered that annual reductions should then continue until imported TCF products became duty free. It stated that this option was preferred because:

> … it would establish tariff reductions that are broadly consistent with the effective annual tariff reductions that:
>
> - are currently being imposed upon the industry (between 2000 and 2005); and
> - had previously been imposed upon the general manufacturing sector between 1991 and 2000 (of around 1.1 per cent p.a.). (sub. PP175, p. 3)

7.2 The Commission's findings on post 2005 tariff levels

Two main issues arise in considering post 2005 tariff assistance under the approach outlined by the Commission in chapter 6. First, when should the tariff target of five per cent be achieved: should it be 2010 for all products; or should some parts of the sector be given until as late as 2015? Second, what sort of arrangement — stepping, phasing, tops down, or some other combination — should be employed to achieve the target of five per cent by the chosen due date or dates?

As noted earlier, the maximum remaining required tariff reduction post 2005 for all TCF products, other than apparel and certain finished textiles, is just five percentage points. In the Commission's judgment, a tariff reduction of this magnitude could be made over the five year period to 2010, without placing unreasonable adjustment pressure on producers. This assessment includes the carpets and footwear industries — there is no convincing evidence that producers of those products require, or deserve, differential treatment.

The Commission would envisage this five per cent tariff being subsequently maintained through to 2015. This is in line with its view that policy certainty should be provided for the sector through the decade until then (chapter 6). Even if tariffs for other goods were reduced below that rate, the cost to the community as a whole of providing this certainty and stability to the TCF sector would not be large.

In contrast to the tariffs for other TCF products, there are arguments for delaying the achievement of a five per cent tariff for clothing and certain finished textiles beyond 2010 — these goods face further reductions after 2005 of 12.5 percentage points to achieve that rate. While the benefits to consumers and user industries from lower tariffs for apparel and finished textiles would be delayed by deferring the full reduction, the potential for the assistance reforms to trigger disruptive adjustment would be diminished. The Commission is also mindful that the fortunes of many local yarn and textile suppliers are closely allied to those of their customers in the clothing and finished textiles industries. Hence, there is a risk that disruptive adjustment at the end of the production chain could create ‘knock-on’ problems.

The case for ‘erring on the side of caution’ also provides a reason for delaying the attainment of the 5 per cent target for apparel and finished textiles until 2015. Although this would represent a slightly lower rate of reduction over the 10 year-period than under the current package, many firms will already have availed themselves of the easier opportunities for performance improvement. Hence, in the future, they will have to work harder to improve their competitiveness.

Delaying removal of special tariff treatment for some TCF products until 2015 might be seen as less compatible with Australia’s commitment to the APEC Bogor goal of ‘free and open trade and investment’ in the region by 2010 for developed countries than options that would reduce all TCF tariffs to 5 per cent by 2010. However, the tariff approach favoured by the Commission would signal a clear move in that direction: from 2010 a maximum tariff of 5 per cent would apply to all imports into Australia, other than apparel and certain finished textiles. Any remaining negative perceptions could be minimised if all the future TCF tariff reductions, including those to occur in 2015, were to be legislated as soon as possible, just as the 2005 reductions were legislated in 1998.

In the transition to the 5 per cent tariff target, the choice between annual reductions (phasing) and a pause followed by a larger one-off reduction — the approach employed in the current package — is less important. Given the extended timeframes required to recoup many investments to improve international competitiveness, firms’ planning decisions may well depend more heavily on the tariff end point than on the somewhat higher duty rates applying in the intervening period. However, rates in the intervening period will obviously have some impact on decisions — particularly the timing of exits by non-internationally competitive suppliers. In this context, the pause/step-down approach would provide firms with more breathing space and thereby facilitate a smoother adjustment process. It would also avoid the additional compliance costs for both the sector and the Government, associated with smaller annual reductions in duty rates.

In summary, the Commission prefers a reduction to five per cent by 2010 for goods other than apparel and certain finished textiles; a reduction to five per cent by 2015 for those latter goods; with tariff reductions made at the end of each relevant five year period (ie option 4). This would best meet the goal of enhancing overall community welfare while giving the sector time to adjust and minimising the risk of excessive disruption. The Commission also considers that the required tariff reductions should be legislated as soon as possible after the Government makes a decision on post 2005 TCF assistance.

7.3 Other tariff related issues

Policy by-laws

Around 20 policy by-laws enable certain TCF goods to be imported duty free. These cover mainly blended cotton and blended synthetic lightweight fabrics. Duty forgone in 2001-02 under these by-laws was around $40 million (ACS 2002b) compared to some $150 million in 1994-95 and $110 million in 1995-96.

If these by-laws were removed, the goods they cover would become subject to the criteria of the more widely available Tariff Concession System. If the goods were accorded concessional entry under that scheme, they would become dutiable at three per cent rather than free of duty as under the current policy by-laws. (As discussed in chapter 11, the Commission considers that the revenue duty of three per cent should be abolished.) If, however, they were not accorded concessional entry, either because they failed to meet the criteria for such entry or they became subject to the Excluded Goods Schedule (see below), they would become dutiable at the applicable general rate, currently 15 per cent falling to 10 per cent in 2005.

In the Commission’s view, such increases in duty consequent on the removal of the policy by-laws would be counterproductive. They would increase costs for some producers and would lead to unpredictable changes, both up and down, in the levels of assistance accorded particular activities in the sector. Given that the future reductions in tariffs proposed by the Commission would reduce the impacts of these by-laws, it considers that they should be left in place unchanged until such time as they become redundant.

In commenting on the Position Paper, the TFIA agreed that there is no need at this stage to change the policy by-law regime (sub. PP164, p. 14). A request from Wax Converters Textiles to create a new policy by-law for certain cotton polyester and cotton fabrics is discussed below.

EOAP

As noted in chapter 5, the EOAP scheme allows footwear and garments assembled overseas from predominantly Australian fabric and/or leather to be imported into Australia with duty payable only on the cost of overseas processing and content. There has been only limited use of the scheme, at least in recent years, with duty forgone in 2001-02 of only $4.75 million.

The Victorian Farmers Federation called for the EOAP to lapse on 30 June 2005 as currently scheduled (sub. PP152, p. 4). However, notwithstanding its now limited use, several participants called for the scheme to be continued, for its product scope to be expanded and/or for duty free entry to be allowed for the foreign as well as the Australian content of imported product (box 7.1).

Box 7.1 **Examples of participants' views on the EOAP**

Several called for its continuation:

> This scheme [the EOAP] should be continued as it helps to retain higher value-added activities in the Australian market if labour intensive stages are moved off-shore. (sub. 62, p. 9) *Geelong Chamber of Commerce*
>
> … EOAP provides valuable support to Victoria's textile manufacturing base … The Victorian Government believes this program has been used extensively and is beneficial to industry. It should be extended beyond 2005 as Victorian companies continue to adjust to global changes. (sub. 78, p. 18) *Victorian Government*

Some wanted further products included:

> The expansion of [the] EOAP Program to all sectors of the TCF industries will ensure the continuing existence of growth of sectors of the TCF that are subject to labour market pressures. (sub. 49, p. 2) *Albany International*
>
> TTNA recommends the EOAP scheme should be extended to include additional products. (sub. 68, p. 4) *Technical Textiles and Nonwoven Association*
>
> The EOAP arrangements should be continued, but they need to be extended beyond garments to encompass make up of the full range of textile products. (sub. 55, p. 13) *Bruck Textiles*
>
> EOAP should be extended till 2010 for all imports of leather footwear, shoe uppers and components, leather goods, garments and finished leather where wet-blue, crust or finished leather imported from Australia was used. (sub. PP110, p. 5) *ENVITAN Consultancy*

Some called for duty free entry to be extended to the foreign content:

> Consideration should also be given to introducing fully duty free access of EOAP products, where the fabric is entirely of Australian make up, to maintain the effectiveness of the scheme, once tariffs are further reduced on 1 January 2005. (sub. 55, p. 13) *Bruck Textiles*
>
> EOAP could provide for the full remission of duty when Australian leather is used as the upper in finished footwear. (sub. 73, p. 22) *Austanners*

The TFIA suggested the scheme could be modified to provide for duty credits that could be applied to other imports:

> There could … be a factor applied to EOAP imports that developed a duty credit to encourage the internationalisation of the Australian markets through further duty free imports of apparel, garments or textiles of the same nature as the EOAP import. (sub. PP164, p. 14)

However, the extent to which changes of this sort would increase usage of the scheme is unclear. Given the growing competitiveness of direct imports from third countries, such as China, and reductions in Australian general tariffs, the basic economics of even an enhanced EOAP would remain questionable for many firms. As Pacific Brands noted:

> The operation of EOAP arrangements were of considerable importance in the mid to late 90s when end-product tariff levels were of a higher order. Pacific Brands was the initiator and principal user of the OAP arrangements for virtually all of this period. Under new tariff arrangements we now see this policy dimension to be of limited strategic relevance to our operations especially in view of the long supply lines involved and the increasing retailer pressure for short lead times. (sub. 72, p. 2)

Similarly, Charles Parsons commented that 'whilst the structure of the scheme is sound and some companies have found it a useful scheme, it has proven to be impracticable due to the costs involved and the lead times for delivery' (sub. 26, p. 4).

More importantly, enhancing the EOAP would be a questionable policy approach at a time when general tariff rates are falling. Any enhancement could only give a temporary benefit to some Australian producers of intermediate TCF products — benefits that could come at some short term costs for any Australian producers of the products concerned. The Commission therefore considers that, like the policy by-laws, the EOAP should simply be continued past 2005, without any fundamental change. With further reductions in TCF tariffs, this would effectively represent a continued phasing out of these arrangements over time.

Requests for duty free entry

Some participants made requests for duty free entry of particular goods. For example:

- *Sporting footwear, clothing and bras*. The Sporting Footwear Importers Group contended that there is no production in Australia of sporting footwear, except bowls shoes and riding boots and that 'removal of Customs duties will not impact on Australian industry manufacturing fashion, semi-fashion and casual footwear' (sub. 27, p. 4). In a request directed at reducing tariffs on some categories of imported clothing, the Group also requested the removal of TCF products from the TCS Excluded Goods Schedule (see below), or even abolition of the EGS altogether (sub. PP122, p. 6). Similarly, Coles Myer suggested removal of TCF product chapters from the EGS because products such as sporting footwear and women's bras are not made in Australia (sub. 95, p. 2).
- *Footwear parts*. According to the FMAA, removing the duty on footwear parts would 'enhance the use of parts as opposed to the importation of finished footwear and thus encourage further employment in the Australian factories' (sub. 28, p. 19). The Association made it clear that it was seeking tariff removal

only on footwear uppers, and not on bottom stock (trans., p. 411). (Shoe Lasts & Components indicated it made bottom stock, such as soles, lasts and heels in Australia (sub. PP172, p. 1).)

- *Yarns*. Australian Weaving Mills said that the legislated 2005 tariff reductions would impose 'significant pressures on our cost competitiveness if the duty on our key input (ie yarns) is not reduced at the same time' (sub. 67, p. 5). It further contended that 'elimination of yarn tariffs should not impact adversely on local yarn producers (sub. 67, p. 5), but would allow it to import duty free those yarns which cannot be made locally. Bruck similarly noted that as many man made fibre yarns and ring spun cotton yarns are only available from offshore, they should become duty free, particularly as tariffs on fabrics are to be reduced in 2005 (sub. 55, p. 10). Similarly, Melba Tex requested removal of duties on yarns not manufactured in Australia, including Aramid, Meta Aramid and Multifiliment Textured Polyester yarns (sub. 83, p. 6).
- *Cotton polyester and cotton fabrics*. A user of such imported goods, Wax Converters Textiles, sought elimination of the 10 per cent tariff 'at the earliest opportunity'. Alternatively, it sought the creation of a policy by-law covering these goods to take effect from 1 January 2004 (sub. PP171, p. 3).

Some of these requests appear to be driven by the desire to reduce costs for particular TCF manufacturing activities in Australia. Some are based on the premise that the goods in question are not made in Australia. Others are because these goods would be ineligible for consideration for concessional entry under the TCS or that, if granted concessional entry, they would still be subject to the three per cent revenue duty.

The focus of the current tariff arrangements and, hence, of this inquiry is on the TCF sector and its component industries in the broad, rather than on particular TCF products. Nevertheless, the Sporting Footwear Importers Group considered that it is within the brief of the Commission 'to recommend the introduction of permanent rates of duty such as 5% … or minimum rates, if there is no Australian manufacturer' (sub. PP122, p. 1).

In the Commission's view, however, recommendations to make tariff exceptions for individual TCF products would detract from the general approach to post 2005 tariff reductions outlined in this chapter and in chapter 6. In practice, examination of the case for duty free substantive rates for particular products would require the Commission to go over the same ground as that currently canvassed by Customs in its assessments of applications under the TCS: that is, the extent to which there are substitutable goods produced in Australia. And although the Commission considers that the three per cent revenue raising duty on business inputs under the TCS should be abolished (see chapter 11), pending that abolition there would be little justification for making an exception for particular TCF products merely because they have been brought to attention in this particular inquiry.

Goods such as sporting footwear, clothing and bras are in a somewhat different situation. As part of the Excluded Goods Schedule under the TCS, the merits of any case for concessional entry cannot even be considered. The rationale for the schedule — which includes a range of foodstuffs, apparel, footwear, jewellery and furniture — is as follows:

> Within certain classes of goods there exists a wide and comprehensive range of both Australian made and imported goods which, notwithstanding differences in character, construction, quality, price, etc., basically compete with each other in the market place. Such goods are excluded by Regulation from concessional entry. (ACS 2003b, p. 11)

In effect, the EGS seeks to limit the costs of Customs, applicants and Australian producers by ruling out numerous applications for concessional entry of certain categories of goods which, prima facie, are likely to be substitutable with Australian made goods. However, as the schedule is necessarily specified in broad terms, there is always the possibility of automatic exclusion from concessional entry of particular goods which would have received concessional entry if the merits of their case could have been assessed.

Currently, it is possible 'in extraordinary circumstances' to have particular goods removed from the EGS. This requires approval from the Minister for Industry, Tourism and Resources, after consultation with other relevant Ministers. When so removed, the case for concessional entry for those goods can be assessed under the usual TCS criteria. Some categories of studded sports footwear were in fact removed from the schedule following such a process, with concessional entry subsequently granted.

The Position Paper commented that, in principle, the opportunity to argue for the removal of goods from the EGS should be generally available to importers, not just 'in extraordinary circumstances'. It said that applications should ideally be assessed against appropriate, publicly available, evaluation criteria. However, it went on to note that, in practice, administrative and compliance costs may militate against moving too far in this direction. Further, it commented that a balance could be difficult to strike, given that the underlying criterion for exemption from the EGS would necessarily be the same as that used in assessing application for concessional entry under the TCS: that is, the degree of substitutability of imports with locally produced goods. With a view to exploring this issue further in its final report, the Commission invited comment on the advantages and disadvantages of making the opportunity to apply for exemption from the EGS more generally available, together with suggestions for controlling the associated administrative and compliance costs.

Responses from the various sectional interests involved, however, have done little to clarify where an appropriate balance might lie. Those supporting the status quo pointed to the compliance and administrative costs likely to be associated with, and follow, changes to the EGS, as local manufacturers and importers argued issues of product substitutability. Those seeking change reiterated their views that the EGS acts to prevent concessional importation of goods for which there are no locally made substitutes (box 7.2).

Box 7.2 Sporting shoes and substitutability

The Sporting Footwear Importers Group argued that there is no Australian manufacturer of sporting footwear (sub. 27) and that the retailing of this footwear is also specialised. Although it noted that 'some low cost imitation sporting footwear is imported and sold through discount footwear stores [and] it could be argued that this type of footwear may substitute for, say, a casual shoe of the type made locally' (sub. 27, p. 3), it argued that 'you don't use that for cross-country running or basketball or playing tennis and things like that' (trans., pp. 416–7).

In contrast, Coles Myer said that language 'such as "cheap, imitation" is both inaccurate and misleading' and that 'there can be no artificial divide in the broad sporting footwear category based on notional attributes or concepts of quality' (sub. PP143, pp. 2–3).

These statements taken together suggest that sporting footwear does substitute, to some extent, for casual footwear. Indeed, it would be surprising if this were not the case. But this begs the question of whether the degree of substitutability is sufficient to preclude concessional entry under the TCS, were the EGS hurdle overcome.

The Importers Group was not optimistic about prospects for concessional entry. It said that the FMAA's attitude that 'a shoe is a shoe' would be sufficient to bar concessional importation of sporting footwear irrespective of whether it were taken off the EGS or not.

The Commission notes that all of these issues will become of much less concern as TCF tariffs are reduced in 2005 and subsequent years. It notes also that, in any case, removal from the EGS might not do much to help importers, unless the criteria for the TCS were to be changed (box 7.2). That matter, and the possible abolition of the EGS as a whole, are beyond the scope of the current inquiry.

Arrangements with Fiji

Submissions and supporting material from the TCF Council of Fiji and Fiji Ministry of Commerce, Business Development and Investment, and from some other participants, raised issues about the relationship of the Australian TCF sector with TCF producers in Fiji. Some of those issues, for example the extension of SIP support to include Australian investment in Fiji, the provision of Australian aid money to help initiate Fiji's own SIP-type scheme, and a proposal for the introduction of a Partnership Development Program for Australia-Fiji trade, are considered to be outside the scope of the inquiry.

Submissions also canvassed the operation of the SPARTECA-TCF arrangements which were introduced to help cushion the impact of the termination of the Import Credit Scheme on the Fijian TCF industry (appendix C). The TCF Council of Fiji (sub. 66, p. 24) stated that the scheme 'has not proved as beneficial for the industry as had been hoped (and promised)'. It sought a number of changes including reductions in the local content necessary to secure duty free entry into Australia and extended scheme coverage to include wool products. Similarly, Bruck Textiles, the Australian TCF firm with the largest operations in Fiji, considered that 'urgent action' was required to ensure that the stated objectives of the scheme are achieved (sub. PP109, p. 5).

However, a number of proposed modifications to the SPARTECA-TCF arrangements — for example, a reduction in the local content threshold to 25 per cent, as proposed by Fiji, or allowing cash redemption of content points, as suggested by Bruck Textiles — could have ramifications beyond this inquiry for issues of trade and aid more generally, as well as for rules of origin. The Commission therefore considers these issues are beyond the scope of the current inquiry.

In any event, the merits of modifying these special TCF arrangements with Fiji are open to question. As witnessed by requests to extend these arrangements, even the assistance currently provided to Fiji has proved insufficient for it to build or sustain a competitive advantage. Continuing reductions in Australia's general TCF tariffs will erode that advantage further in the future. (This is perhaps the reason why Fiji sought continuation of Australian TCF tariffs at relatively high levels beyond 2010.)

Rules of origin issues

Bruck Textiles (sub. PP109, p. 6), Yakka (sub. PP128, p. 8) and the TFIA (sub. PP164, p. 15) expressed concern about the rules of origin associated with the Australian Government's decision to allow all imports from the 49 Least Developed Countries and East Timor duty free access to the Australian market from 1 July 2003. They noted that the proposed rules will allow defined local content to include content from third party least developed countries and defined Developing Countries, including China. Their concern was that this will erode tariff protection for Australian apparel manufacturers and will reduce the incentive for producers in LDCs to use Australian produced textiles.

The TFIA stated that 'similar issues' also arise in relation to other bilateral trade agreements being currently pursued by the Government, including those with the United States and with Thailand:

> … while the consultation and discussions with the government representatives on the USA FTA have been significant and inclusive, the same cannot be said for the Thai negotiations … The TFIA has supported the Singapore, USA and LDC initiatives and will continue to work through them. (sub. PP164, p. 14)

However, while the Commission understands these concerns, the underlying issues are complex and affect many sectors, and are again considered beyond the scope of this current inquiry into TCF assistance post 2005.

FINDINGS ON POST 2005 TARIFFS AND RELATED ASSISTANCE ISSUES

- *The capacity of apparel and certain finished textile producers to absorb a tariff reduction of 12.5 percentage points over the 2005 to 2010 period without serious disruption is questionable. The reduction in tariffs for those goods to the five per cent target should therefore take place over the longer period to 2015.*
- *For other TCF products, including carpets and footwear, the required tariff reduction after 2005 to reach the five per cent tariff target is five percentage points or less. Making that reduction over the five-year period to 2010 is unlikely to place unreasonable adjustment pressure on those industries.*
- *In moving to the five per cent tariff target, there would be advantages in continuing the step down approach employed in the current assistance package. Hence the Commission's preferred post 2005 tariff option is as follows:*
  - *maintain all TCF tariffs at 2005 levels until 1 January 2010;*
  - *on 1 January 2010, reduce tariffs on apparel and certain finished textiles to 10 per cent and tariffs on other TCF products to 5 per cent; and*
  - *maintain tariffs on apparel and certain finished textiles at 10 per cent until 1 January 2015, and then reduce them to 5 per cent.*
- *Legislating early for all of these tariff reductions would deliver the policy certainty that the sector requires and maintain the pressure on firms to improve their performance. It would also help to minimise any negative perceptions about this option in relation to Australia's commitment to the APEC goal of 'free and open trade and investment' in the region by 2010 for developed countries.*
- *Further reductions in TCF tariffs would effectively continue the phasing out of the TCF policy by-laws and the Expanded Overseas Assembly Provisions. These arrangements should therefore be continued after 2005 without amendment. Sector-wide duty reductions would also diminish the need to consider requests for duty free entry for specific TCF goods not made in Australia.*

8 Transitional assistance

The Commission's broad approach to post 2005 assistance for the TCF sector comprises further tariff reductions, phased over a period to allow sufficient time for adjustment, together with the provision of transitional budgetary assistance. Without an extension of such transitional support, it may be difficult to meet the Government's objectives for the sector in a reasonable timeframe without risk of undue disruption.

In the Commission's view, transitional assistance should be focused on the objective of assisting TCF firms which manufacture in Australia to improve their ability to compete in domestic and export markets without the need for ongoing preferential tariff assistance. In this context, this chapter considers appropriate arrangements for transitional assistance, including issues relating to design, duration and funding.

8.1 Options canvassed in the Position Paper

The Position Paper noted that participants proposed an array of changes to overcome the perceived deficiencies of the current SIP arrangements. The Commission concluded that, viewed in isolation, many of these suggestions for change might have merit. However, it noted that, with total funding capped, changing arrangements to meet the needs of particular firms or industries would reduce funding available for others.

The Commission therefore outlined some design criteria, related to efficiency and effectiveness, to assist in evaluating the tradeoffs between alternatives (box 8.1). It observed, however, that designing a scheme which satisfied all of these principles simultaneously is impossible.

Three options for further consideration were canvassed in the Position Paper — these are briefly summarised in box 8.2. Two of them, options A and B, would continue the present 'entitlements' approach — that is, all firms which demonstrate that they have met the necessary qualifying criteria would be entitled to assistance. Option C would be a 'competitive' approach. Under that approach, firms would apply for assistance before undertaking spending, their proposals would be assessed against specified criteria and the higher ranking proposals funded first — some firms might miss out.

Box 8.1 **Efficiency and effectiveness criteria for evaluating transitional assistance**

As far as possible, transitional assistance should:

- Reward incremental/new activity rather than subsidise activity that would have been undertaken without support.
- Give firms flexibility to judge what spending will best promote their future competitiveness (including, where appropriate, reducing dependence on TCF manufacturing activity).
- Provide support to the firms most likely to survive and prosper as a result of that support.
- Provide a sufficient level of support to make a difference to firm behaviour.
- Take account of the extent of the tariff reductions facing firms in different parts of the sector.
- Not discriminate against small firms, which otherwise meet assistance criteria.
- Promote certainty and transparency.
- Keep administrative and compliance costs low, while minimising the risk of gaming and abuse.
- Minimise the risk of complaints to the WTO.

8.2 Participants' responses to the Position Paper's options

Most participants which commented on future transitional assistance supported option A, implicitly or explicitly — that is, they supported various modified versions of the existing SIP arrangements. Some of their suggestions for change were outlined in chapter 5 and other examples are listed in box 8.3.

Those few participants that explicitly compared the merits of the Position Paper's three options generally favoured option A. One important reason was articulated by Pacific Brands which, although it saw some merit in the option C approach, preferred to work with 'the essentially strong SIP approach and to correct administrative flaws':

> The desire to develop a completely new policy approach has been a major weakness of policy moves in the past. We support the maximising of the investment firms have

made in understanding the operation of the current SIP entitlement approach. (sub. PP138, p. 3)

Box 8.2 Transitional assistance options canvassed in the Position Paper

Option A — modify existing arrangements. Most of the basic parameters of the existing SIP would remain in place, with modifications to its detailed requirements to improve its effectiveness in encouraging firms to increase expenditure in ways which would improve their international competitiveness.

Option B — a bounty based on additional value added. Firms would be entitled to assistance each year solely on the basis of increases in their value added relative to a base period or periods.

Option C — firms 'compete' for assistance. Firms would apply for assistance on the basis of proposed expenditures to facilitate future viability and improved competitiveness in a lower tariff environment. Applications would be assessed by an 'expert' panel against a range of selection criteria. Eligible expenditure categories could potentially include expenditure in such areas as investment, R&D, innovation, IT, enhancement of product range, quality improvement, brand and market development (including export markets), and workforce skilling. An assistance rate (or rates) could be specified in the program's design parameters. Alternatively, or as well, the panel could be given some discretion in varying assistance rates between firms.

The Carpet Institute of Australia similarly favoured continuation of the current SIP approach because it is 'well known and understood and [the] least disruptive approach'. In contrast, option B 'creates definitional problems and generates uncertainty' while option C 'is workable but tantamount to picking winners' (sub. PP126, p. 12).

Likewise, TCF Services considered that 'the simplest and most effective way of providing certainty, and improve alignment with government policy, is to recommend simple modification of the existing SIP scheme' (sub. PP174, p. 5). Its two proposed variations to existing arrangements, however, each effectively incorporated some of the elements of option C:

- under the first proposal, assistance to small firms would be provided on an entitlements basis, but large firms would need to make a case to the Government for funding, before they spent the money;
- under the second proposal, all firms would be entitled to assistance, subject to eligible expenditure exceeding $100 000. However, there would be additional provisions for 'loans' to firms for proposed future expenditure.

Box 8.3 Illustrating participants' views on overcoming the deficiencies of SIP

… the basic SIP principles should be supplemented to provide industry assistance across the fundamental industry drivers: product development, investment, technology and sales (sub. 77, p. 17) *Godfrey Hirst*

SIP funding arrangements [should] be changed to provide for a greater degree of flexibility in funding investment, R & D, and process improvement activities. (sub. 11, p. 30) *Australian Industry Group*

A program similar to the current Strategic Investment Program (SIP), as provided to the rest of the TCFL sector, needs to be made available to the whole wool processing supply chain. (sub. 45, p. 14) *Australian Wool Processors Council*

Consideration [should] be given to the needs of smaller to medium-sized business operators and how they can be encouraged to instil activities and processes assisted by SIP without damaging the overall value to existing SIP clients. (sub. 75, p. 7) *TFIA*

The scope of the SIP program should be expanded to accelerate the development of emerging new businesses in the TCF sector. These businesses are particularly vulnerable to market inequities and are the likely source of growth in employment … (sub. PP180, p. 16) *Tasmanian Government*

It is vital that the Government introduces greater flexibility under SIP to ensure it is more relevant for the spinning sector. (sub. 44, p. 7) *Rocklea Spinning Mills*

Inclusion of current state of the art second hand equipment as eligible … (sub. 32, p. 13) *Australian Association of Leather Industries*

Capital Expenditure grant payments should be increased from 20% to 30% or higher of eligible expenditure to assist with the ongoing essential task of substantial re-equipment with state of art technology. (sub. 53, p. 4) *Ulster Tascot*

… [delinking] Type 3 grants from Type 1 and 2 grants … would be to put in place a type of production bounty that rewarded those companies employing Australian workers. The TCFUA supports this type of proposal … (sub. 33, p. 32) *TCFUA*

… examination of the merits of paying the Type 3 payments as import credits … incorporation of 'investment in brand equity' as well as 'investment in physical assets' as currently applies under Type 1. (sub. 72, pp. 3–4) *Pacific Brands*

Types 4/5 grants need to be completely revisited and they should be restructured to match the original intent of the draft scheme … (sub. 67, p. 8) *Australian Weaving Mills*

… consideration should be given to ways of improving the level of certainty participants have about the value of projects undertaken under the auspices of the program. (sub. 73, p. 12) *Austanners*

Research and development needs to be clarified so that the scheme is easier to manage. The scheme should have an R&D focus or simply day to day development rather than the fashionable yet vague definition – innovation. (sub. 65, p. 9) *Defab Weavers*

A key concern raised about option B was the problem of defining 'value added' and 'incremental' so that firms would have sufficient certainty about likely levels of support, and problems of gaming would be avoided. Bruck Textiles, for example, believed that a bounty system based on increments in value added:

> … would create too much confusion over the uncertainty about what is meant by value added and the manner in which increments are determined. (sub. PP109, p. 4)

Another important concern related to the subsidisation of labour expenditure. The Australian Association of Leather Industries considered that 'there is no logical basis for providing support to value added in isolation [as in option B]':

> … such a move would merely reward labour intensive industries with minimal prospect for substantial export earnings. (sub. PP161, p. 2)

The Australian Industry Group was of the opinion that 'funding should embrace not only R & D and investment, but also the other main driver of competitiveness, ie labour productivity' (sub. PP140, p. 4). But it considered that this could be done through option A.

Some participants also pointed out that, in the context of the contracting TCF sector, option B might fail to support activity that would lead to improved international competitiveness. For example, Pacific Brands considered that the 'incremental notion' is:

> … of little relevance in an industry (especially clothing) with massive underlying contraction potential. (sub. PP138, p. 3)

There was little unqualified support for option C, although Bruck, while supporting option A, indicated it was 'not opposed to the concept of a competitive scheme (ie picking winners), provided the right criteria for selection are applied' (sub. PP109, p. 4). Some participants, for example the Footwear Manufacturers' Association of Australia, pointed to the unsatisfactory experience with similar arrangements in the past:

> Historically this [option C] approach has always reduced the number of recipients, had a very mixed record of success and meant that application costs, time and the use of consultants increases dramatically — as evidenced by the TCFDA experience. (sub. PP132, p. 7)

However, several participants, including footwear manufacturing firms and the Victorian Government (sub. PP173, p. 7), suggested that an option C type approach might offer a means of extending transitional assistance to small firms that are excluded from the current SIP by the minimum spending threshold. For instance, the Harold Boot Company, in noting that the current SIP is limited in its application to small firms, considered that 'Option C would provide assistance in a more cost-effective way especially for smaller firms' (sub. PP124, p. 3). It suggested that a limited number of pilot projects might be tried, targeting small firms 'judged capable of and likely to grow and remain as efficient manufacturers in Australia in the long term' (sub. PP124, p. 3). The TFIA also proposed that some SIP funding should be set aside for:

> … the smaller elements of the industry that have significant projects or investments relevant to their size yet are outside the current SIP criteria. (sub. PP164, p. 3)

And the Carpet Institute of Australia commented that:

> … there may be merit in providing specific support to SMEs for specific activities that will lead to future growth. But this would need to be a stand-alone program, with a specific amount of funding quarantined for just that purpose. (sub. PP162, p. 4)

While the Western Australian Department of Industry and Resources considered that option C ‘appears to be the most equitable of the three options’, this conclusion was premised on the ‘fact that the overwhelming majority of TCFL industries in Western Australia fall into the small, mini and micro business category’ and that options A and B would fail to meet the needs of those smaller businesses (sub. PP179, p. 3).

8.3 Judging transitional assistance options

The many different schemes and variants of adjustment assistance for the TCF sector tried (and abandoned) in recent years bear testament to the difficulty of translating efficiency and effectiveness objectives into operationally sound adjustment schemes. For this reason, the Commission has not tried to flesh out all the administrative details, nuances and safeguards which would have to be built into future transitional assistance — it realises that ongoing analysis and discussion would be needed on such issues, including with the sector, before operational arrangements are finalised.

The main conclusions

Earlier chapters describe the rapid and ongoing change occurring in the TCF sector. In particular, many firms have ceased or reduced manufacturing activity in Australia and have moved more into design, purchasing/importation, distribution, marketing and selling. Indeed, without such diversification, some of these firms might not have been able to continue in the sector. Nevertheless, the Commission believes that the focus of future transitional assistance needs to remain on firms undertaking TCF manufacturing and design activity in Australia, as it is such activity which is directly affected by past and future tariff reductions. For this reason, the Commission considers there is no reason to depart from the definitions of eligible TCF activity under the present SIP.

This emphasis on targeting manufacturing and design activity in Australia should help internationally competitive TCF firms, or those with this potential, to grow and thereby to increase or to sustain employment. However, in the Commission's view, it is not appropriate to make transitional assistance conditional on employment levels as called for by the TCFUA. Many of the changes required by firms to enable them to become internationally competitive will require them to use labour more efficiently. Discouraging such changes by requiring firms to maintain or increase employment to qualify for transitional assistance would be counterproductive.

Having weighed up comments from participants in response to the Position Paper, the Commission's main conclusions about the broad approach to post 2005 transitional assistance are as follows:

- For larger TCF firms, future transitional assistance would be best provided through a modified version of the existing SIP approach, ie option A.
- There is in-principle merit in extending transitional assistance to smaller firms. However, significantly lowering the existing $200 000 qualifying threshold for eligible expenditure would risk spreading assistance too thinly and would increase administrative costs. Any assistance to smaller firms might best be provided through a separate arrangement, perhaps along the lines of option C. Even then, administrative costs and difficulties would need careful consideration to avoid detracting from the contribution such assistance would make towards improving the sector's international competitiveness.

The rest of this section presents the detailed reasons for these conclusions, while the next examines possible modifications to SIP.

The reasons

The aim of transitional assistance is to help firms to make significant efforts to improve their international competitiveness, rather than just to 'struggle on'. This means that strong emphasis should be given to *additionality*, ie encouraging firms to take steps they would not otherwise take to improve their international competitiveness.

As some participants noted, additionality is a difficult concept to operationalise. Additional spending or value added (compared to a base period) may arise from, for example, general market growth, rather than *additionality* in its true sense. Further, when placed in the context of a declining sector such as TCF, actions taken by a firm to improve competitiveness (for example, enhancing productivity or modernising but rationalising its product range) may not result in increased output or value added overall. To some extent, options A and C can overcome these difficulties by indirect means (see below). But it is a particularly serious flaw with option B, which explicitly targets increased value added.

Additionality can be encouraged by ensuring that assistance is not spread too thinly — the higher the subsidy rate the more likely the subsidy is to encourage additional spending and behavioural change at a firm level. As well, careful choice of target variables can induce firms to do something new and desirable. For that reason, adjustment programs often target investment, R&D/innovation, or market development, rather than linking assistance with production or sales levels. Further, paying assistance in advance of expenditure, rather than after the event, can also enhance additionality by providing firms with certainty of funding. Depending on their specific provisions, both options A and C are better in these terms than option B.

At the same time, assistance should be *flexible* and not unduly proscribe what steps should be taken by a firm to improve competitiveness. But too much flexibility could compromise the additionality objective in two ways: the wider the range of eligible expenditure, the closer the arrangement comes to an unconditional production bounty rather than an encouragement to real change. Wider eligibility of spending types, or numbers of firms, will also necessarily spread funding more thinly, thereby diluting any impact on firm behaviour. Option C in theory offers a direct way to control these tradeoffs, but careful modification of SIP, ie option A, could introduce more flexibility without unduly diminishing the focus on change.

The *extent of tariff reduction faced* by different industries and firms, while relevant, is less important than the other assessment criteria. As well as depending on changes in its tariff protection, the need for a firm to improve international competitiveness may also be affected by changes in tariff protection for its upstream suppliers or downstream customers. Further, as the Carpet Institute noted:

> … the focus of positive assistance should not be simply to help hold up industry suffering from increased import competition, but to develop the industry so that it can become internationally competitive and sustain this position. Such positive development is vital for all sectors. (sub. PP162, p. 2)

In any case, this criterion offers little guidance in choosing between options A, B and C — each would be able to accommodate differences in tariff reduction levels through variation in subsidy rates, were that considered to be desirable.

Certainty and *transparency* are important in facilitating additionality — transitional support is unlikely to induce significant change if firms are uncertain whether they will receive funding for a particular spending initiative to improve competitiveness, or cannot understand assistance arrangements. Transparency is also important in assuring the community that administration is efficient and funding is provided appropriately.

As noted by participants, option A has the advantage of building on experience with the existing SIP. Past experience with value added bounties (option B) indicates that their simplicity can be more apparent than real. Giving too much discretion under option C to the scheme's administrators could significantly undermine transparency and certainty — but too little would negate some of the potential advantages of this option.

Finally, it is obviously important to avoid unnecessary *administrative and compliance costs*. There is little information on which to judge the relative merits of the options in this regard although, given the nature of these sorts of arrangements, each would inevitably entail significant costs. However, any departure from existing arrangements would add to such costs, at least in the short term. (TCF Services considered it would take up to two years to bed in an entirely new scheme (sub. PP174, p. 5).) Hence, because option A builds on the current SIP arrangements, it should entail lower transition costs than the other two options.

In conclusion, while the incremental value added bounty (option B) and competitive bidding (option C) approaches would have some advantages over aspects of the current SIP, there would be considerable benefits from utilising the learning experience and precedents accumulated under the current scheme. The experience with the SIP illustrates that the costs for firms and the Government alike of bedding down completely new arrangements, and the associated uncertainty about outcomes, can be significant. Largely for this reason, the majority of participants favoured a modified version of the SIP (option A). Moreover, the Commission sees scope to improve the effectiveness of the current program in encouraging firms to improve their international competitiveness.

Small firms

A recurring theme in submissions was that transitional support should be more accessible to small firms. Many suggested that the minimum spending threshold to qualify for support should be reduced. Others suggested the introduction of a separate competitive bidding scheme for small producers.

In the Commission's view, the in-principle case for not discriminating against small firms is self evident. The entrepreneurial and innovative skills apparent in many small TCF firms suggest that there is good growth potential in this part of the sector. Indeed, given the financing difficulties that small firms often face, transitional budgetary support might induce more new activity to improve international competitiveness than support provided to larger, established firms.

However, attempting to bring the large number of small firms in the sector within the funding net would spread support much more thinly and could cause administrative costs to escalate sharply. These problems would be particularly acute if better access for small firms was pursued through adjustments to the minimum spending threshold.

Developing a separate transitional assistance scheme for small firms along the lines of the option C approach would bring a host of challenges too. These would include: defining the meaning of ‘small firms’ for the purpose of the scheme; setting eligibility thresholds to avoid spreading assistance too thinly; and defining the scope of activities to be assisted. There would also be the need to determine the balance between being too prescriptive, in which case the main advantages of the option C approach would be lost, and leaving everything to the judgment of the ‘expert panel’ administering the scheme, risking loss of transparency and certainty. As well, finding panel members with the necessary knowledge, expertise and experience to administer such a scheme, while avoiding vested interests, would be difficult.

Funding allocated to such a scheme would need, in the Commission’s view, to come out of total funding allocated for transitional assistance to the TCF sector, rather than add to it (see below). Thus, there would be a tradeoff between funding the mainstream program and establishing a small firm arrangement. The amount required would not necessarily be large — some participants nominated annual amounts in the order of $15–20 million as appropriate. But such a figure implies tight targeting of assistance given the large number of small firms in the sector. The cost of developing such a scheme, and the ongoing administrative and compliance costs necessarily incurred, would be further factors militating against such an approach, especially if funding levels were low.

In sum, although the in-principle merit of extending transitional assistance to small firms is undoubted, and the possible mechanisms for providing support to small firms warrant further consideration, the practical problems could be difficult to overcome.

8.4 Modifying existing arrangements

This section discusses some modifications to the existing SIP which the Commission believes would better focus transitional assistance on encouraging improved international competitiveness. It also discusses some changes suggested by participants which the Commission considers would detract from that objective.

As noted, scheme design is difficult, with the ‘devil in the detail’. The Commission recognises that further study and consultation with the sector would be needed before future arrangements could be finalised.

Incorporate a clear and explicit objective

The 2002 DITR review of SIP illustrated some community and industry misunderstanding about the objectives of the program. To some extent, the problem has been rectified since then, through efforts to clarify definitions of R&D/innovation, for example. However, to avoid similar problems with the post 2005 arrangement, the Commission considers that there is a need to incorporate a clearly enunciated and explicit objective, both in the enabling legislation and in the detailed specifications of the arrangements. This objective should be to foster the development of Australian TCF manufacturing activity that can be viable and internationally competitive without special assistance.

Provide more general support for purchase of state-of-the-art second hand equipment and for ancillary expenditure

Under the current SIP, assistance is available for the purchase of state-of-the-art second hand equipment and ancillary expenditure by firms in defined regions of TCF dependence (Types 4 and 5 assistance). In each case, such assistance must relate to a ‘restructuring initiative’ between two or more unrelated entities. Another requirement is that the resultant entity is likely to be more financially viable than if the restructuring initiative did not take place.

However, restructuring of metropolitan firms can be just as valuable in improving the TCF sector’s international competitiveness as restructuring of firms in regional areas. Perhaps more importantly, independently of restructuring initiatives, purchase of appropriate state-of-the-art second hand equipment can offer many firms an efficient and effective way to improve their competitiveness.

The Commission therefore considers that there is a good case for generalising and liberalising Types 4 and 5 assistance. The geographic restriction should be removed, as should the requirement for assistance to be associated with a restructuring initiative between unrelated entities.

The Commission acknowledges that some firms might be able to improve their competitiveness through the purchase of second hand equipment, not judged to be state-of-the-art. But, partly for administrative reasons, and partly because genuine improvement in international competitiveness is more likely to be achieved, the Commission considers that a state-of-the-art restriction is desirable.

Even with this restriction, additional administrative safeguards would be required. State-of-the-art would have to be clearly defined. Many participants requested that assistance should be made available to help with restructuring *within* firms, as well as restructuring of unrelated entities. However, to prevent gaming and abuse, requirements for purchase of state-of-the-art second hand equipment to be at arms length, at fair market values, and from a non-related entity, would probably be required. There would also need to be controls on resale. Similarly, assistance for ancillary expenditure might have to be restricted to payments made to external unrelated entities.

Subsidise investment in market and brand development

Many participants considered that the current restriction of SIP support to investment and R&D/innovation limits their flexibility to enhance competitiveness in the most efficient and effective ways (see chapter 5). Many ideas for extension of the menu of allowable expenditures were put forward.

While such extension could, in principle, encourage increased competitiveness in more firms, the Commission considers that, to avoid excessive dilution of assistance and for administrative reasons, the menu should continue to be restricted. For the large firms in particular, this would not greatly limit their options — as discussed in chapter 5, payment arrangements effectively allow firms the freedom to choose forms of expenditure most likely to improve their future competitiveness, *provided* they incur the necessary qualifying expenditure in the form of investment and/or R&D/innovation.

Nonetheless, many participants argued that the current restrictions particularly affect the clothing industry. As discussed above, there is no sound reason for transitional assistance to TCF industries to be allocated in proportion to the tariff reductions they face. Nor is there prima facie reason for assistance to be divided in proportion to industry output or sales. However, the Commission accepts that the current focus on investment, and the current definitions of R&D/innovation, can make it difficult for clothing firms to access SIP assistance, even when they are, for example, making considerable efforts to improve their competitiveness through market and brand development, or through ‘visual’ innovation.

For this reason, there was much comment from participants on the merits, or otherwise, of further liberalising the current definitions of R&D and innovation to extend assistance to a greater range of activity. For example, the TFIA considered that current definitions under SIP do not 'properly accommodate the innovative product development … in the wider clothing and fashion industries' (sub. PP164, p. 3). But firms in some other industry segments opposed such extension of eligible activity, as that would possibly dilute their assistance.

In the Commission's view, substantially widening the scope of eligible R&D and innovation would be likely to reopen considerable uncertainty about interpretation experienced earlier in the life of the SIP. Importantly, this has diminished in importance, as time has passed, and appeals have declined, to the benefit of all parties. Further, the Commission is not convinced that assisting 'visual innovation' will necessarily result in a sustainable competitive advantage for clothing firms.

Rather than attempting to expand the scope of the current definitions of R&D and innovation, the Commission considers that a better alternative would be to expand eligible expenditure to include market and brand development, including for export markets. This would help firms in the clothing industry with a reasonable prospect of becoming competitive in a lower tariff environment and, in turn, help their suppliers to maintain their domestic markets. But more generally, many firms, not just those in the clothing industry, undertake considerable market and brand development to improve competitiveness. Spending in these areas will clearly be necessary for firms looking to move out of production of standardised commodities into branded or otherwise differentiated products, or to develop export markets, and to exploit market niches more generally.

Accordingly, the Commission considers that in the post 2005 transitional support regime it would be appropriate to extend the eligible expenditure categories to investment by firms in market and brand development (including export market development), in both instances in respect to TCF products manufactured in Australia. Precise definitions would again require careful formulation to help ensure that subsidies contributed to a genuine improvement in the long term competitiveness of recipient firms, rather than simply subsidising 'business as usual' expenditure.

Fine tune definitions of R&D and innovation?

While the Commission considers that it would be preferable to extend support to market and brand development than to liberalise the existing definitions of R&D and innovation, there would be merit in giving further consideration to whether:

- current limits on R&D salaries remain appropriate;
- collaborative R&D/innovation by groups of firms should be eligible for assistance; and

- expenditure on process improvement to bring a firm up to industry best practice should be eligible for funding support.

Discontinue Type 3 assistance

According to the 2002 DITR report on SIP, the rationale for the current Type 3 value added assistance is to reward additional value added arising from investment or R&D/innovation by the firm. However, in practice, Type 3 assistance is *not* contingent on additional value added being achieved — it is provided automatically, provided qualifying expenditure on investment etc. is made, and the relevant caps are not exceeded (see below). From this perspective, it is not clear why the subsidy rates for Types 1 and 2 assistance were not just set at higher rates in the first place — Bruck Textiles commented that, for many firms, Type 3 operates purely as a doubling mechanism (trans., p. 331).

Discontinuing Type 3 assistance would have implications for the distribution of assistance for some firms. This is because, in contrast to eligible claims in excess of the overall assistance cap of five per cent of sales, which can be rolled over into subsequent years, value added in excess of the separate Type 3 cap cannot. Textor claimed that:

> A larger company has less chance of capping out on Type 3 and hence receives an effective 40% for an approved capital investment. In the 2002 claim Textor will receive an effective 26% grant due to the cap out in Type 3 grants. (sub. PP135, p. 2)

Nevertheless, the Commission considers that Type 3 assistance should be discontinued. As currently implemented, these grants simply increase the rates of subsidy for investment in plant and equipment and spending on R&D and innovation. But the way they are paid means that the increased rate of subsidy can vary arbitrarily among firms. Discontinuing these grants would help to simplify the new regime. It would also release funds that could be used to increase the subsidy rates for investment and R&D, and/or to pay for the eligibility extensions outlined above.

If Type 3 assistance were to be continued, however, then the Commission considers that it should continue to be linked to the receipt of assistance under the other grant types. As discussed in relation to option B in the previous section, the case for subsidisation of value added (alone) is not strong. Further, if Type 3 assistance were to continue, the current cap based on value added should be discontinued, with WTO compliance issues addressed solely through the overall funding to sales cap.

Speed up payment to firms

Under the present SIP arrangements, all payments to firms are made in retrospect. The period for reimbursements varies widely — from as little as two months or so, to a year or more.

Self evidently, avoiding long delays in payment would enhance a firm's cash flow, and improve certainty, with possibly beneficial flow-on effects to competitiveness.

However, the payment lag depends, to some extent, on the actions of the firm:

- Assistance for eligible expenditure, particularly investment, made late in a financial year can often be paid to the firm very early in the next financial year. (Reimbursement for R&D/innovation can take longer to process.)
- Advances of 50 per cent of the expected assistance amount can be paid to a firm before AusIndustry's full auditing and assessment of a claim is completed — this brings forward a significant part of the payment where these administrative processes are expected to be lengthy.

Administrative requirements, including the need to allow for the possibility of modulation, mean that some delay in payment is inevitable. Payment rates for a particular financial year cannot be finalised until all relevant claims have been submitted.

The available 50 per cent advance is an attempt to overcome this problem, without running the risk of 'overpaying' firms, and requiring grant repayments if a significant degree of modulation eventuates. Keeping the advance to less than 100 per cent also allows a 'margin of safety' for the circumstance where a firm's claim was overstated.

Nevertheless, under present arrangements, modulation has not been required so far. Indeed, there are suggestions that there could be some considerable underspending of total SIP funds available over the life of the program. In this situation, there is merit in investigating ways to speed up payment to firms. For example, at least for the remainder of the present scheme, the proportion of advance payment could be increased quite substantially to, say, 75 per cent. (This would require reassessment in the post 2005 regime, however, as the suggestions discussed above could have considerable implications for the amount and distribution of funding.)

Finally, there would be merit in speeding up decision making as far as possible, without incurring excessive administrative costs in AusIndustry.

Eliminate payments to firms in administration/receivership

Providing assistance to firms which are likely to leave TCF manufacturing, or even go out of business, is wasteful when assessed against the objective of fostering the development of internationally competitive TCF firms in a low tariff environment. Although such support could help firms to 'exit gracefully' and possibly assist them to pay employee entitlements, the Commission considers that these latter objectives are better encouraged by a further tariff pause to 2010 (after the 2005 cuts take effect), and by explicit mechanisms to assist displaced workers (see chapter 9 and section 10.2).

Some provisions in the current SIP seek to ensure that a firm receiving funding support is viable and likely to continue TCF operations beyond the period of the SIP scheme. But, in practice, judging a firm's prospects has sometimes proved difficult. Hence, there have been examples of firms which have gone offshore, left the sector, or failed shortly after receiving SIP assistance.

Current arrangements make provision for special advance payments to firms in administration/receivership, but still in operation. Again, the Commission recognises that, in some cases, payment of assistance — a reimbursement for expenditure already made — could enhance a firm's capacity to trade through and survive. In other cases, such assistance could help fund redundancy payments and other exit costs. Nevertheless, given the objective of transitional budgetary assistance, and limited overall funding, the Commission considers that firms in administration/receivership at the time assistance would normally be paid should be ineligible for assistance under the post 2005 transitional support regime.

Enhance transparency and certainty, simplify administration and compliance

Enhancing transparency and certainty, and simplifying administration and compliance, would reduce costs for firms and the Government. It would also help to assure the wider community that the scheme is administered efficiently and funding provided appropriately. But, perhaps more importantly, it would enhance the prospects of firms undertaking additional expenditure that is likely to improve their future competitiveness.

However, there are limits on the extent of transparency and certainty possible in an inherently complex scheme such as SIP. Specification of clear objectives would be an improvement in this context (see above). But some of the possible changes mooted above might reduce certainty and transparency, at least while they were being bedded down.

Nonetheless, particularly given the apparent complexity of SIP compared with other assistance programs such as the Automotive Competitiveness and Investment Scheme, there are areas in which improvements could be made to enhance transparency and certainty:

- Write the new scheme in simple and understandable language. This would provide some compliance cost savings by enabling more firms to prepare claims using their own internal resources, rather than consultants. As such, it would be particularly helpful for smaller firms.
- Continue to clarify definitions such as R&D and innovation. The objective should be to increase certainty and clarity, rather than to expand the scope of assistance.

In the Position Paper, the Commission raised the possibility of a system of binding rulings to enhance transparency and certainty. This received some support from participants, for example from TCF Services (sub. PP174, p. 8).

Implementing a system of binding rulings would, however, raise difficult practical issues. For example, would they apply firm by firm or generically? Would commercial-in-confidence restrictions limit their usefulness? How much flexibility would there be for a firm to vary agreed expenditure plans before the ruling lost effect? Should there be negative as well as positive binding rulings?

Further, given learning and precedent as SIP has progressed through its third year, certainty about the eligibility of various types of spending has improved significantly. Thus, while the issue of binding rulings might be worth considering again in the context of a future modified arrangement, at this stage the benefits of developing a system for binding rulings are unlikely to outweigh the costs.

Reconsider subsidy rates and qualifying thresholds

Implementation of the kinds of changes discussed above would have implications for subsidy rates and qualifying expenditure thresholds. These issues require full assessment in the context of the timing and funding arrangements for future transitional assistance (see below). They are complex and further clouded by uncertainty about whether all of the available SIP funding will be spent by the end of the current program. But whatever adjustments are finally made, the Commission considers that it is important that subsidy rates and expenditure thresholds together ensure that assistance provided to individual firms is sufficient to encourage spending that can make a real difference to their future competitiveness.

Several participants requested ‘regional uplift factors’ — that is, higher rates of assistance for firms located in regional areas. As discussed above, however, the Commission considers that firms in metropolitan areas often face challenges just as severe as those faced by regional firms. Indeed, some firms noted advantages in operating in regional areas. More importantly, the objective of transitional assistance is to assist firms to improve their competitiveness, not to deal with regional problems. The Commission notes that, if the need arises, general measures such as the Regional Partnership arrangements are available to help regions experiencing problems from adjustment in the TCF sector (chapter 4).

No justification for extending support to upstream or downstream activities, including early stage processing

During the inquiry, several participants requested the Commission to consider transitional assistance for early stage wool processing. For example, the Australian Wool Processors Council sought inclusion of the early stage processing (ESP) industry in TCF support programs through introduction of:

> … a special early stage wool processing industry development program. The special industry development program would be geared towards the specific needs of the early stage wool processors given the unique market conditions now confronting the industry. Funding grants of up to 7.5% of a company’s value added triggered by agreed expenditure or performance targets should be made available to ensure the long term future of the Australian ESP industry. (sub. 127, p. 2)

It estimated this assistance would cost about $12 million a year. While the Council acknowledged that the ESP industry ‘does not need access to a SIP like program to facilitate adjustment to a reduction in tariffs’ it said that such activity was ‘recognised as a part of the TCF industry’ (sub. 127, pp. 2–3). It further argued that the ESP industry needed assistance to ‘consolidate and reposition itself’ in response to ‘an extremely difficult competitive position at this time’ (sub. PP127, p. 1).

The Commission accepts that many early stage processors are currently facing difficulties because of protective barriers overseas, the growing competitiveness of China, global overcapacity and a decline in the production of Australian wool. It also acknowledges some linkages between the ESP industry and later stages of TCF production in Australia. Nevertheless, the ESP industry’s current difficulties are not primarily linked to changes in Australian TCF tariffs. Thus, the Commission does not consider that transitional budgetary assistance available for the TCF sector should be extended to such production activity.

8.5 How much for how long?

The Position Paper approach

The Commission noted that under its preferred tariff option at that stage, parts of the TCF sector would not face a 5 per cent tariff until 2015. It argued that ending SIP-style funding much before then would see firms in those segments making the last part of the transition to lower tariffs without the support that others in the sector would have enjoyed. It further noted that extension of budgetary support beyond 2010 could provide an additional adjustment cushion for the rest of the sector in its efforts to operate successfully under the 5 per cent tariff applying from 2010.

The Commission also pointed to the need to strike a balance between giving the sector time to adjust to future tariff changes and signalling that its special assistance treatment will need to end no later than 2015. It therefore argued that, like tariffs, transitional support should be progressively reduced. Given the competing considerations, however, the Commission commented that the appropriate duration of, and funding levels for, a successor to the SIP was a matter of judgment. To encourage comment, the Commission put forward the following possible approach in the Position Paper:

- After current arrangements expire in July 2005, budgetary support be provided for a further period of eight years.
- Total funding for the four year period 2005-06 to 2008-09 should match existing annual average available funding in nominal terms.
- Funding then be halved for the second four year period 2009-10 to 2012-13.
- Budgetary assistance terminate on 1 July 2013.

Responses to the Position Paper

There was some limited support for the approach put forward in the Position Paper: for example, from Australian Weaving Mills (sub. PP163, p. 2), the Australian Chamber of Commerce and Industry (sub. PP147, p. 9) and TCF Services (sub. PP174, p. 4). The New South Wales Government also supported an eight year timeframe, but suggested year by year reductions in levels of support from $182 million in 2005-06, scaling down each year to $23 million in the final year (sub. PP175, pp. 6–7) — delivering about the same total overall funding as the Position Paper proposal.

Generally, however, participants reiterated their initial requests for at least a 10-year extension of transitional assistance, with no reductions in annual funding levels over the period. Often their requests were aligned to the view that tariffs should be maintained, and budgetary support provided, until other countries increased access to their markets (chapter 6).

Pacific Brands adopted a somewhat different approach. While supporting a 10-year extension of transitional assistance, in line with its views (see above) that assistance should be more focused on the clothing industry, it suggested that:

> If there is a case for reduced funding in the second 5 years … this would be better implemented by reducing the coverage of the adjustment assistance to those in transition rather than spreading the funding reductions across all sectors whether still moving to the 5% end point or not. (sub. PP138, p. 3)

The Commission's views on timing and funding

A range of considerations are relevant in determining how long transitional support should extend beyond 2005, and its level of funding:

- Under the Commission's preferred tariff option, the reduction to 5 per cent in the tariff on clothing and finished textiles would not occur until 2015. As noted, ending transitional funding much earlier would see firms in those segments making the last part of the tariff transition without the sort of support that others in the sector had enjoyed.
- Even though firms elsewhere in the sector would be operating at a 5 per cent tariff from 2010, many could experience knock-on adjustment pressures associated with the impending tariff reduction for clothing and finished textiles in 2015.
- Reinforcing the message to firms that special assistance treatment is coming to an end is important. This suggests that, like tariffs, transitional support should be progressively reduced.
- As part of a package to end the sector's special assistance treatment, it would be difficult to justify funding support higher than that provided by the current SIP.
- But at the same time, in facilitating a seamless transition from the current regime, there is a case for maintaining funding levels in the early years of the new program.

The Commission remains of the view that the funding profile outlined in the Position Paper would strike a reasonable balance between these sometimes opposing considerations:

- The new transitional support program would operate for eight years from 2005.
- Funding for the first four year period would be equivalent to total payments in the last four years of the current SIP (in nominal terms).
- Funding for the subsequent four year period would be halved.
- Transitional support would then terminate in 2013.

There are other possible options, of course, including that proposed by Pacific Brands. A view can be taken that the prime purpose of transitional assistance is to help firms enhance their international competitiveness in the face of *future* tariff reductions, not those made in the *past*. Indeed, this is the rationale of the current SIP arrangements. From this viewpoint, there would be some merit in ending access to transitional assistance by 2010 for all firms except those in the apparel and certain finished textiles industries, with access for those latter groups ending no later than 2015. Against this, as noted above, linkages between firms mean that TCF industries that provide intermediate inputs to apparel and certain finished textile products would inevitably face further tariff related adjustment pressures after 2010. For this reason, as discussed above, it is not appropriate to make a precise delineation of transitional assistance between TCF industries based on the extent of the future tariff reductions they face.

Another approach would be that proposed by the New South Wales Government, for higher funding in the early years, scaling down year by year. This lined up with its proposal for tariffs to be similarly scaled down (chapter 6). In the final years of such an arrangement, however, available assistance would be so small as to make little difference to firm behaviour. Yet possibly significant administrative and compliance costs would continue to be incurred.

Finally, the Commission notes that provided adjustments were made to hold the total quantum of funding constant in present value terms, a time profile of say two five year periods, or five years and three years, would most likely make little difference to outcomes. Hence, in some senses, the key thrust of the Commission's proposal is to set an indicative benchmark for the present value of funding for the new transitional support arrangement. However, though the Commission sees scope for some variation in the time profile of this support, if the sector's special tariff treatment is not to end until 2015, distributing all funding very quickly after 2005 would raise the prospect of subsequent calls for more transitional assistance.

Facilitating a seamless transition

As seamless a transition as possible from the current SIP to the post 2005 arrangements would be of considerable benefit to firms. Hence, the Commission considers that claim moneys not paid by the end of the current SIP program because of the five per cent sales cap should be carried over into the modified scheme so that the companies concerned can be paid their entitlements in due course. The Technical Textiles and Nonwoven Association pointed out that this 'provides certainty and … ensures that programs being developed aren't put on hold' (trans., p. 362). However, it is important to distinguish between funding for this purpose and those funds uncommitted because of the lack of eligible spending by firms. In the Commission's view, such funds should lapse, with any underspend reflected in funding levels for the post 2005 transitional support instrument.

FINDINGS ON TRANSITIONAL ASSISTANCE

- *A further period of transitional assistance is warranted after 2005 to help TCF firms which manufacture in Australia to improve their international competitiveness, as further tariff reductions are implemented.*
- *Transitional assistance arrangements should avoid spreading funding too thinly to make a difference to firms' behaviour.*
- *Post 2005 transitional assistance should follow the approach of the existing SIP, with some modifications to improve its effectiveness. Although further analysis and discussion with the sector will be needed before operational arrangements are finalised, the following modifications have merit:*
  - *incorporate a clearly enunciated and explicit objective; namely, to foster the development of Australian TCF manufacturing activity that can be viable and internationally competitive without special assistance;*
  - *provide generalised support for purchase of state-of-the-art second hand equipment and for ancillary expenditure;*
  - *subsidise investment in market and brand development associated with the manufacture of TCF products in Australia;*
  - *discontinue specific additional assistance for value added;*
  - *accelerate payments to firms as far as possible;*
  - *eliminate provision for funding support to firms in administration or receivership; and*
  - *enhance transparency and certainty by writing the new arrangements in simple and understandable language.*
- *An initiative to help small TCF firms to access transitional budgetary assistance warrants further consideration, but would require careful thought about how to address significant implementation problems, while still providing cost-effective support.*

- *Transitional support should not be extended to early stage wool processors — although they are currently experiencing some problems, these are not primarily linked to changes in Australian TCF tariffs.*
- *The following funding profile would provide the benefits of a seamless transition from the current SIP, while reinforcing the signal to the sector that its special assistance treatment is coming to an end:*
  - *The new transitional support program would operate for eight years from 2005.*
  - *Funding for the first four year period would be equivalent to total payments in the last four years of the current SIP (in nominal terms).*
  - *Funding for the second four year period would be halved.*
  - *Transitional support would then terminate in 2013.*
- *The transition from the current SIP to the post 2005 arrangements should be as seamless as possible. Funding claims not paid to firms by the end of the current SIP because of the five per cent sales cap should be carried over into the post 2005 scheme so that the companies concerned can be paid their entitlements in due course.*

9 Labour adjustment support

Current labour adjustment assistance arrangements provide support to those who lose their jobs, including income support and help with retraining or re-employment. However, such arrangements are not specifically designed to cater for large scale job losses resulting from the closure of large firms.

This is particularly relevant in the case of the TCF sector. As noted in earlier chapters, there is still extensive adjustment to occur in the sector and inevitably there will be more firm closures. Given the ethnic and educational characteristics of much of the TCF workforce and the continuing importance of TCF activity in some regions, those losing their jobs may often have difficulty in finding alternative employment, particularly if they are part of a large group of workers retrenched at the one time. Accordingly, in the Position Paper the Commission sought advice from participants on how best to deliver targeted support to retrenched TCF workers in these sorts of situations.

In response, there was agreement from many participants that special support for retrenched TCF workers, beyond the general support that is currently available, would help to facilitate what may prove to be a difficult adjustment process. Encapsulating these views, the South Australian Government said:

> … the particular characteristics of the TCF workforce, as well as the significant adjustment still ahead of the sector, demand a more targeted approach. (sub. PP177, p. 4)

This chapter proceeds on the basis that there will be a justifiable need for specific adjustment assistance to TCF workers during the transition period, where large scale, or regionally significant, job shedding occurs and there is a risk of disruptive adjustment. It describes some current general arrangements, examines why they might not be sufficient to meet the needs of displaced TCF workers in these situations and considers what sort of additional responses could facilitate re-employment.

9.1 What general support is available

Commonwealth Government assistance to displaced workers is currently provided through:

- *Newstart Allowance*, which provides income support to job seekers. Payments are subject to income/assets tests applied to both the job seeker and their partner. Job seekers who have received a redundancy package may have to wait up to 13 weeks to receive support. Mutual obligation requires recipients to undertake job search, usually through the Job Network, or participate in other activities such as Work for the Dole.
- *The Job Network*, which provides help in finding employment for all registered job seekers. More information on the Job Network is provided below.

In addition, some State Governments provide labour adjustment support, although these are all on a much smaller scale than the Commonwealth programs and in some cases firms themselves provide assistance (see below).

The Job Network

Since 1998 the Commonwealth Government has purchased and regulated employment services for job seekers through the Job Network. The network now encompasses over 100 private, community and State Government organisations that are awarded business through a competitive tender process.

Job Network providers are remunerated by the Government according to the services they provide and the outcomes that they achieve. Providers are required to provide a minimum level of services to each job seeker, but may provide more at their discretion. Some reimbursement is on a fee-for-service basis, with an additional outcome fee paid if the provider places a job seeker into either employment or further education.

Outcome payments are linked to the estimated difficulty of finding a job for particular categories of individuals. Hence, job seekers that are likely to have more difficulty finding work, for example older workers, those from a non-English speaking background and the long term unemployed, will attract a higher outcome fee for the successful provider.

Job Network processes and associated income support are triggered when displaced workers register with Centrelink. The timing of the particular services delivered to a job seeker will depend on their length of unemployment and on their assessed degree of disadvantage in finding employment:

- All job seekers can use job placement services. This includes access to job advertisements, the use of telephones, faxes and computers and some advice on résumé preparation.

- More intensive support is provided to those who have been unemployed for 3 months or who are assessed as having a high level of disadvantage. These intensive support services vary depending on the needs of the individual and the judgment of their provider and range from simple job search training (such as help with résumé preparation and interview skills), through to more tailored support (such as English language courses) provided to the more disadvantaged job seekers and the long term unemployed.
- Provision also exists to provide highly specialised support (not necessarily to find work) to those assessed as having 'severe' disadvantage. These provisions apply to less than 5 per cent of Job Network registrants.

The Job Network was the subject of a recent review by the Productivity Commission (PC 2002a). While the Commission found that overall employment outcomes were similar to previous programs, the Job Network achieved them at lower cost.

State Government programs

In recent years, some State Governments, notably Queensland, Victoria and Western Australia, have sought to augment Commonwealth employment services, especially in regard to assistance to disadvantaged job seekers. However, job seekers receiving assistance under State Government programs are generally not permitted to access corresponding Commonwealth assistance and visa versa.

Some of these programs have specifically targeted retrenched workers. For instance in Queensland, the Worker Assistance Program (WAP) provides assistance where 15 or more workers are facing retrenchment. Where larger scale retrenchments have been announced or have occurred, there is provision to establish a 'shop front' to provide assistance to those workers concerned. Special assistance programs are also in place in Victoria and Western Australia for forestry employees facing retrenchment as a result of changes to government forestry policies. These programs all offer a combination of training (including assistance with résumé preparation and interview techniques) and re-skilling, wage subsidies and relocation support.

The Victorian and Western Australian WAPs have only been running since late 2002, while the Queensland WAP began in 1999. Over 3500 workers have received assistance under the Queensland scheme since 1999, with 63 per cent of recipients subsequently finding employment. This percentage is similar to the success rate achieved by the Victorian WAP for 350 forestry workers so far assisted.

9.2 Does current Job Network support meet the specific needs of TCF workers?

The Job Network is designed to address the needs of individual job seekers rather than the requirements of a large group of retrenched workers from a single firm or factory. Hence, when a large firm closes it may be difficult to ensure that all displaced workers receive adequate attention in the short term. This could be a particular problem in regional areas where often there are a limited number of Job Network providers.

Another problem is that to access the Job Network, individuals are required to be unemployed and registered with Centrelink. For some, accessing Job Network services after retrenchment may not be a problem. However, displaced workers without good communication skills or a limited knowledge of Australia's unemployment support arrangements, may find it more difficult to access these services. This is relevant in the TCF industry, since there is a high proportion of employees who are from a non-English speaking background or who do not have recent experience of looking for work (see chapter 4).

Moreover, this 'retrospectivity' effectively rules out early intervention by Job Network providers to assess the job search skills and training needs of workers where retrenchments have been announced, but not yet given effect. In the course of the Job Network review, the Commission was told that, because services can only be provided to those who have become unemployed, Job Network providers are unable to provide 'on site' assistance to employees prior to the closure of a firm.

A consequence of the Job Network's focus on outcomes is that it concentrates assistance on those who are perceived as having the greatest chance of finding employment. For this reason, the support provided to those displaced TCF workers considered to be more difficult to place in employment may vary considerably under the normal Job Network provisions.

In summary, considerations such as these suggest that, by itself, the Job Network may not be sufficient to meet the needs of some displaced workers, including TCF workers, particularly where large scale, or regionally significant, job shedding is involved.

9.3 What augmentation is required and how should services be delivered?

Designing assistance that delivers effective labour adjustment support is a job best left to those with direct experience in delivering and administering such support. Hence, in the context of augmenting the Job Network services available to displaced TCF workers, the following discussion confines itself to the broad objectives of labour adjustment assistance and desirable features of the support to be provided. Examples of the views of participants are set out in box 9.1.

Box 9.1 **Participants' suggestions for labour adjustment assistance**

The Textiles, Clothing and Footwear Union of Australia said that its experience suggests that:

- targeted assistance is far more effective than general assistance;
- it is vital to access workers prior to them leaving the workplace;
- the people delivering the assistance must be known to the workers and be trusted by them;
- the providers of the assistance need to be located near the workplace but not be in the workplace;
- non-English speaking workers are reluctant to approach Centrelink and training providers;
- if workers are not provided with income assistance they are unable to consider re-training options as they are driven by the need for immediate income;
- an integrated advocacy approach is required, in effect a one-stop shop which provides and identifies what workers require and helps them navigate existing services and find out what assistance is available. (sub. PP154, p. 14)

The City of Darebin called for:

> … more practical solutions through programs to re/up skill employees who are forced into redundancy through business closures resulting from tariff reductions. (sub. PP151, p. 4)

The Geelong and Region Trades and Labour Council suggested that government:

> Fund a retraining program similar to the Labour Adjustment Program (LAP) that is specific to the TCF sector and pays workers for the period of retraining. (sub. PP141, p. 2)

The South Australian Government stated that:

> the particular characteristics of the TCF workforce … demand a more targeted approach … [there should be] a sector-specific communications campaign … which informs workers of programs (general and direct) which would be available to them should they be displaced from their employment … [this] should be targeted at workers prior to loss of employment … (sub. PP177, p. 4)

In general, the Commission considers that special labour adjustment support for the TCF sector should concentrate on situations where large scale, or regionally significant, job losses are involved and attempt to:

- improve the prospects of TCF workers who have been retrenched or have been given notice of retrenchment in finding employment in a reasonable timeframe;
- provide such outcomes in a cost-effective manner; and
- avoid as far as possible duplication of the services already available through the Job Network and any other current arrangements.

Some participants argued that assistance should include non-means tested financial support during retraining or where displaced TCF workers do not receive their full entitlements (over and above any support from the General Employee Entitlements Redundancy Scheme). For example, the TCFUA, 'strongly advocates for future retraining programs to incorporate income support that is not means tested' (sub. 33, p. 73).

However, delivering such support could be expensive. Further, income support, albeit means tested, is generally available to all displaced workers including those from the TCF sector. (As discussed in chapter 10, the Commission has proposed an independent inquiry to examine efficient ways of providing greater security for employee entitlements.)

The Commission considers that sector-specific support should focus on addressing the gaps in the Job Network and generally available programs in keeping with the objectives outlined above.

Past experience and overseas approaches can provide guidance

In seeking to meet the above objectives, there is considerable experience to draw on. This experience includes previous TCF-specific assistance and other overseas labour adjustment schemes. A description of some of these programs is contained in box 9.2.

The experience of previous programs points to features likely to promote better outcomes for retrenched workers and, just as importantly, some that will not. For instance, the TCF Labour Adjustment Program (LAP), which operated during the 1990s, did not permit participants to find alternative employment in the TCF sector. In hindsight, this restriction appears to have been an integral factor in the poor outcomes achieved. Appendix table B.17 shows that in the 3 years to 1997 (part of the period for which the LAP ran), 28 per cent of retrenched TCF workers, subsequently found employment in the TCF sector. Yet this avenue of re-employment was denied to LAP participants.

Box 9.2 **Labour adjustment programs in Australia and overseas**

The TCF Labour Adjustment Program

The TCF Labour Adjustment Program (LAP) ran from 1988 to 1997 and assisted retrenched TCF workers to gain employment outside the sector. The LAP provided participants with wage subsidies, training (the most common form of assistance provided) and relocation assistance for up to one year. Under the program, participants were not permitted to find re-employment in the TCF sector, nor were they permitted to develop TCF-specific skills.

In total, 25 per cent of LAP participants found employment within three months of receiving assistance. Although these employment outcomes are low, they were at least partly affected by the bar on participants finding work in the TCF sector.

Firm specific adjustment assistance

Recently, firm specific assistance has been provided to workers at Bradmill and Yakka. In the former case, assistance funded by the receivers was delivered by the TCFUA. In the latter case, the support was provided by the company when it closed a plant at Shepparton. In both cases, workers were contacted prior to retrenchment and were helped to:

- find employment, through the use of project officers who contacted TCF companies and other employers on behalf of the workers;
- develop their job seeking skills, including help with resume preparation, interview skills and motivation; and
- access training programs, including English language courses.

In the case of the Bradmill workers, the TCFUA placed project officers, with former experience in the TCF industry, close to the Bradmill factories concerned. In conversations with retrenched workers, these project officers found that most participants were not interested in lengthy training courses. Most could not afford the time out of work and were cautious about re-entering formal education.

In both cases, over half of those that responded to the follow up surveys found employment within a six month period. Although it is unclear that this success rate is much better than that achieved by the Job Network, the characteristics of some of those who found new jobs (many were of mature age and from a non-English speaking background) may have inhibited their re-employment prospects. [Indeed, the results of these programs were slightly better and were achieved over a shorter time period than those from the Webber and Weller (2001) study which surveyed TCF workers retrenched during late 1992 and early 1993. The results of this study were widely cited by participants.] Moreover, the aspects of these programs that contributed to majority of participants finding employment are clearly relevant in the context of sector-wide adjustment support.

(Continued next page)

Box 9.2 **(continued)**

Overseas programs

In the United Kingdom and the United States, there is general assistance available to workers when a large factory closes down.

In the UK, the Job Transition Service (previously known as Rapid Response units) provides tailored support in areas where large scale redundancies are occurring and where the existing assistance infrastructure may not be able to deliver the necessary support. The assistance provided includes:

- setting up a 'job shop' on the employer's premises;
- a fast track claims process for redundant employees; and
- early access to employment service programs (such as basic English skills, basic employment training and, in some cases, specific vocational training).

In the US, the Economic Dislocation and Worker Adjustment program requires large employers to give prior notice of retrenchments. Federal agencies then provide these retrenched workers with a combination of training, job search assistance, relocation allowances, as well as income support, beyond that provided by unemployment insurance. In some senses, however, this more generous adjustment assistance provided in the US can be viewed as compensation for the lack of a broad social safety net that exists in the EU, Canada and Australia.

Source: IC (1997), TCFUA (2002), US Department of Labour (2001) and UK Secretary of State for Education and Employment (2001)

Further, the focus on retraining in the LAP — a necessary consequence of the restriction on re-employment — appears to have further contributed to the poor outcomes achieved. This is particularly so as LAP participants were not required to look for work while retraining — possibly leading some participants to reduce their job search for the duration of the training period, and further eroding their employment prospects.

Taking a more pro-active approach

The recent experience with the firm-specific assistance delivered by the TCFUA at Bradmill and by Yakka, suggests that early intervention can improve retrenched workers' chances of finding alternative employment. Such early intervention is also a key feature of Queensland's Worker Assistance Program and the UK Job Transition Service (box 9.2).

Early intervention, where there is prior notice of retrenchment, would provide a 'bridge' to assistance for those workers who because of information or communication problems could otherwise have difficulty in accessing the Job Network. Moreover, early intervention would enable assistance to be provided to retrenched workers prior to their leaving the workforce rather than after they have become unemployed. The establishment of a ‘job shop’ in firms anticipating large scale retrenchments, similar to that of the Queensland Worker Assistance Program and the UK Job Transition Service, would be one vehicle for delivering such support.

Even where there is no prior notice of retrenchment, there may still be scope to provide assistance to displaced TCF workers at the time of, and following, retrenchment to assist them in finding alternative employment.

Involving people that workers are familiar with

Involving individuals with previous experience in the TCF industry could also help retrenched workers find new jobs or access general assistance programs. The TCFUA reported that workers responded positively to project officers, employed in delivering assistance to Bradmill workers, that had previous experience in the sector.

Focusing on finding a job

The TCFUA experience of delivering assistance to Bradmill workers suggests that many retrenched workers are not interested in retraining, instead putting a priority on re-employment. Indeed, the firm-specific assistance delivered by the TCFUA at Bradmill and by Yakka focused on finding a job for participants, directing them to retraining only when clearly necessary, rather than as a matter of course. This feature is also integral to Job Network arrangements and would also be appropriate in any future sector-specific arrangement.

However, some individuals may not be able to obtain a further job without some retraining or re-skilling. The nature of the training provided in these circumstances should, of course, depend on the needs of each individual. As a general rule, however, training provisions would probably concentrate on addressing TCF sector-related barriers to re-employment including, where relevant, providing basic English language and literacy skills for those from a non-English speaking background, or job marketing skills (such as résumé preparation and interview skills) for those who have not actively sought employment for some time.

Making mainstream Job Network services more accessible

There is also scope to make mainstream Job Network services more accessible to displaced TCF employees across the sector generally. As noted, because of poor communication and English language skills, some displaced TCF workers may be reluctant, or find it difficult, to access the Job Network. These difficulties could be ameliorated by regular dissemination of information on Job Network services to the TCF workforce, including outworkers. Indeed, this would be a concrete way of assisting outworkers, who might be more difficult to encompass in the specific support designed to deal with major job shedding in the sector.

What sort of institutional changes would be required?

The types of support outlined above could be readily delivered through an inexpensive augmentation of the existing Job Network. Job Network providers already provide similar assistance, albeit after an individual has become unemployed. The key emphasis in sector-specific arrangements would be to make this sort of assistance more readily accessible for TCF workers, prior to and at the time of large scale, or regionally significant, retrenchments.

Apart from reducing the risks of service duplication, delivery via an augmentation of the Job Network would be more cost effective and administratively efficient than two possible alternatives identified in the Position Paper (a stand alone scheme or assistance delivered on a case-by-case basis). Further, this type of focus could be a cost-effective way to test the merits of incorporating such assistance more generally within the Job Network framework.

FINDINGS ON LABOUR ADJUSTMENT SUPPORT

- *Implementation of TCF-specific labour adjustment measures could help to reduce the likelihood of disruptive adjustment resulting from post 2005 assistance reductions, or other pressures confronting the sector. Such assistance should focus on addressing large scale, or regionally significant, job shedding in the sector through an augmentation to Job Network services. In doing so it should:*
  - *include provision for early intervention where there is prior notice of large scale, or regionally significant, retrenchments; and*
  - *use people with experience in the TCF industry.*
- *There is also scope to make mainstream Job Network services more accessible to all displaced TCF employees through regular dissemination of information on those services, including to outworkers.*

10 Workplace arrangements and skilling issues

Effective and flexible workplace arrangements allow for the efficient use of employee skills and capital equipment and the adoption of new technologies that are important to improving productivity and competitiveness. There have been improvements in TCF workplace arrangements in recent years achieved across diverse workplace structures (see chapter 3). Indeed, in submissions and discussion with the Commission, a number of firms expressed satisfaction with the flexibility that their current arrangements provide and with the relationships they have built with their employees.

However, further improvements which could enhance the viability of firms, give employees more job security and higher remuneration, and deliver taxpayers better value for their assistance dollar are still possible. The recent Victorian TCFL Strategic Audit summarised the problems that continue to be evident in the sector:

> Many employers are concerned about the difficulties of obtaining the necessary degree of workforce flexibility required for sustainability. The Textile Clothing and Footwear Union of Australia (TCFUA) is concerned at the poor management practices in the industry, the lack of security for their members, occupational health and safety … (Victorian Government 2000)

While problems in some workplaces may have inhibited productivity growth rather than caused costly production stoppages, the issue of employee entitlements continues to be a threat to industrial relations stability, as well as deflecting attention in workplace negotiations from improving the viability of firms.

The use of outworkers in the clothing industry also raises important policy issues — in particular, ensuring appropriate protection of this group from exploitation while, at the same time, providing firms with the flexibility and 'just-in-time' production capability that this form of employment arrangement can deliver.

10.1 Current workplace arrangements

The diversity in TCF activities described in earlier chapters is also evident in workplace structures. Wage and condition setting, union representation and work organisation vary widely among firms and regions within the sector.

The award system dominates wage and condition setting

Because the sector contains many small firms, awards remain the dominant mechanism for determining wages and working conditions. According to the Department of Employment and Workplace Relations (DEWR), more than 80 per cent of the factory based TCF workforce operate under the award system.[1] Large firms, typically in the capital intensive textile and carpet sectors, tend to operate with enterprise bargaining agreements (EBAs).

Notably, many firms expressed a strong preference for using the award system because it suits their individual circumstances; provides flexibility to tailor wage outcomes to improved work organisation; and reduces transaction costs and risks of industrial disputes associated with re-negotiating EBAs.

Some firms operating with EBAs commented that this system has done little to improve their productivity and has simply been a mechanism for increasing wages.

However, as DEWR observed, this may have more to do with the failure of firms to take advantage of the opportunities provided by the EBA process than with shortcomings in the regime itself:

> … the industry has generally failed to use the options which would allow it to move from the 'one size fits all' workplace arrangements of awards to a more tailored approach to meet the competitive needs of individual businesses. A number of enterprise agreements appear to have an over-representation of provisions that benefit unions at the cost of business, and hence jobs. This, coupled with an under-representation of workplace relations initiatives to improve flexibility, further erodes the labour productivity and global competitiveness of many TCF businesses. (sub. 84, p. 1)

Firms which have taken advantage of the flexibility offered by enterprise bargaining saw considerable merit in the process. For example, the Technical Textile and Nonwoven Association (TTNA) said:

1 The four main awards relevant to the TCF sector are the Clothing Trades Award, the Textile Industry Award, the Footwear Manufacturing and Component Industries Award and the Felt Hatting (Consolidated) Award.

> There is no doubt that enterprise bargaining has played a significant role in the welfare of the Australian technical and nonwovens textile industry over the last ten years. Enterprise bargaining has enabled progressive firms to minimise demarcation problems and to create skills based promotional structures. The reforms to the system in recent years have strengthened firms' abilities to put into practice workplace arrangements appropriate to the needs of individual enterprises. (sub. 68, p. 21)

Union membership is low

Union participation in determining workplace outcomes varies across the sector. While in some plants the workforce is completely unionised, other plants have no union membership. In the sector as a whole, less than 25 per cent of employees belong to a union — lower than in the mid 1990s and the present average for the broader manufacturing sector (see appendix table B.22). The dominant union is the Textile Clothing and Footwear Union of Australia (TCFUA) although there is some representation by other unions.[2]

Workplace flexibility has improved

Over the past decade or so, there have been improvements in arrangements in many TCF workplaces. Examples include:

- more flexibility in work hours, allowing more efficient and longer use of capital equipment. Some firms now operate on a 24 hour, three-shift basis with several, especially in the nonwoven technical textiles sector, maintaining continuous production seven days a week;
- the use of casual and contract labour to meet seasonal peaks in demand, (although for some firms this remains a problem);
- the ability to re-organise leave arrangements to cater for fluctuations in demand using the existing workforce; and
- fewer restrictive work practices and less rigid demarcation of tasks, allowing increased emphasis on team-based work and multi-skilling.

2 These include the Australian Manufacturing Workers Union, the National Union of Workers and the Liquor, Hospitality and Miscellaneous Workers Union.

But inflexibility continues to impede productivity improvement

While increased flexibility in work organisation is apparent in many firms (irrespective of whether they operate under an award or an EBA), there are areas where workplace arrangements still impede productivity improvement and reduce firm viability. Restrictions on optimal shift patterns, the scope to substitute time-off-in-lieu for penalty rates of pay, and on the use of casual and contract employees are examples. DEWR highlighted reliance on the use of overtime to manage variations in production as a major inflexibility. It said:

> Analysis of federal certified agreements shows that 71% of current TCF agreements contain overtime provisions. … This indicates that managing peaks in production is an important issue for the industry. However the way in which this is managed varies. The traditional overtime arrangement has its limitations. … Alternatives such as time off in lieu (TOIL), flextime, annualised salary and other innovations can provide more appropriate options which meet the needs of both the business and the employees for managing the cost of overtime. (sub. 84, p. 4)

In advocating the need for more flexibility in employment arrangements, the TFIA said:

> … the general industry perspective is that as the external environment is changing, it is imperative that the appropriate adjustments be made at the enterprise level to strengthen the position of all participants. Flexibilities such as the use of external contractors are and always will be a requirement for the TCF sector, if for no other reason than for the difficult if not impossible task of measuring demand at any point in time.
>
> The industry needs to ensure that it has a well-paid, motivated and appropriately skilled workforce. This will entail a significant mix of manufacturing and supplying alternatives ranging from full-time factory based employees through to offsite casual and sub-contract labour. (sub. 75, pp. 9–10)

Achievement of more effective workplace outcomes is also impeded by:

- the absence, in most enterprises, of a link between pay and productivity improvements;
- skill deficiencies among managers and employees in both factory based settings and in the outwork sector (see section 10.3);
- the difficulty of satisfactorily addressing the employee entitlements' issue (see below) which has recently caused damaging industrial action in the carpet industry; and
- an associated focus in workplace negotiations on redundancy matters rather than on how to assist firms become more viable.

On this last point, Australian Defence Apparel echoed the views of several firms that a problem faced by the industry:

> … is a union that is preoccupied with redundancy … . We are confronted with a union that embarks upon industrial relationships purely based on what they can get; no attempt to work with firms to improve productivity, but produce a wish list that is usually headed by redundancy. (trans., p. 63)

Increased coincidence of interests would reduce inflexibilities

While current institutional arrangements provide scope for firms and their employees to improve workplace flexibility, this is hindered in some enterprises by ineffective communication and a lack of cooperation between managers and their employees. Notably, the Commission was told during discussions that the relationship between the union and TCF firms in Victoria is more adversarial than in other States.

To achieve more productive workplace outcomes, many firms must improve their understanding of industrial relations issues and communicate better with employees and their representatives. The harmonious relationship that exists between some firms, their employees and the unions sets a benchmark for others.

Employees and their unions must give more recognition to the relationship between workplace outcomes, international competitiveness, and the viability of firms and the sector. With many firms ‘at-risk’, this is crucial to facilitate the transition of those enterprises capable of becoming internationally competitive without high levels of government support.

In turn, this suggests that appropriate skilling and training for all of those participating in workplace negotiations will be an important contributor to effective workplace outcomes. According to the Ai Group, the lack of specialist human resource managers in many small and medium sized firms, and inadequate training of shop-floor union stewards has:

> … not promoted the development of HR/IR skills generally across the sector. This is evidenced by the fact that there is a tendency for grievances to escalate into disputes because of the inability of parties to develop practical solutions. This may have the further consequence of damaging relations between management and employees.
>
> Given the obvious importance of effective grievance resolution at the workplace, it would be appropriate to establish effective training in this area, run by a genuinely independent body. (sub. 11, pp. 43–44)

The Commission notes that improvements in workplace relations would also be facilitated by further consolidation in the sector, given that there is often more scope for specialisation and professionalism in human resource management in larger firms.

The sector can ill afford industrial disputation

Compared with other parts of the economy (notably the automotive industry), industrial disputation has not been a widespread problem in the TCF sector. Many participants reported that they had not had an industrial dispute for several years and were confident that their relationship with employees would ensure this continued in the future.

Recently, however, industrial action has been evident in parts of the Victorian TCF sector. This is partly a result of the nature of TCF activity in that State. Victoria has more large capital-intensive textile firms which face higher costs from production stoppages than smaller firms. Combined with a highly unionised workforce, this increases the potential for industrial disputation compared with clothing production, for example, which relies heavily on a disparate and non-unionised group of outworkers to supply market requirements.

It is not automatic that larger, highly unionised firms will experience industrial relations problems, however. The Commission notes that many large TCF plants have good industrial relations records. A key reason has been that managers, employees and their representatives have acknowledged that it is in their joint interests to work together to advance firms' prospects. Effective communication and cooperation has provided the scope for issues to be resolved without recourse to industrial action.

Also, the catalyst for the recent high profile disputes at two Victorian carpet manufacturers — employee entitlements — has been an issue not just in the TCF sector, but across manufacturing and services industries generally. It has become more acute with the fallout from high profile corporate collapses such as National Textiles, Coogi and Ansett. As large firms vulnerable to stoppages, Godfrey Hirst and Feltex were targeted in pursuit of a broad union agenda on the entitlements issue. The TCFUA acknowledged that certain firms had been 'singled out' commenting that:

> It is not fair on those companies that we continue to have disagreements with and disputes with, that they are the only companies that bear the brunt of the disgruntlement and fear and concern of thousands of workers about their entitlements. (trans., p. 40)

As discussed below, it would be highly beneficial to firms in the TCF sector (as well as in other industries) if the entitlements trigger for industrial action could be defused. Given the number of 'at-risk' firms that remain, the TCF sector is among the least able to cope with the costs of this sort of disputation (see box 10.1).

Box 10.1 **Industrial disputation in the TCF sector**

According to the ABS, industrial disputation in the TCF sector during the latter part of the 1990s was only slightly higher than the all-industry average — although there has been a recent increase (see appendix figure B.7). Moreover, industrial disputation was not generally regarded as a widespread problem by inquiry participants. It has, however, been a costly source of lost production in the Victorian carpet industry.

During negotiations for a new enterprise bargaining agreement, Feltex Australia was the subject of 'protected' industrial action in October 2001 which adversely affected production for more than 6 weeks. According to the company, the issue of employee entitlements was the main catalyst for the dispute, with the TCFUA arguing that a trust fund be established to guarantee accrued entitlements.

The cost of lost production was substantial with the loss of operating cash flow to the company, and lost wages to employees, totalling millions of dollars. Employees eventually returned to work when the union and the company agreed to continue negotiations on an 'appropriate industry-wide mechanism which would be acceptable to both parties' to deal with the entitlements issue.

Similarly, the expiration of Godfrey Hirst's enterprise agreement at the end of 2001 coincided with 'protected' industrial action aimed at the establishment of a trust fund to guarantee entitlements (including redundancy payments). This caused significant disruption to the business with overtime bans, the ending of shifts prior to normal completion times (shutting down machinery and causing additional waste, downtime and start-up production losses in a 24 hour shift operation) and rolling stoppages over a seven week period.

Godrey Hirst suggested that the cost to its business was substantial, comprising production losses 'running into millions of dollars', the permanent loss of export sales to competing suppliers, and additional costs arising from the need to outsource certain processes to reduce production losses. In a longer term context, the company believed its reputation as a quality product supplier was permanently damaged by the dispute.

The EBA negotiations were eventually completed without concession to the trust fund proposals of the TCFUA. As a consequence, the company indicated that the potential for further industrial action over this issue remains a major, and ongoing, concern.

Further assistance reductions could reinforce incentives for cooperation

Increased competitive pressures in the sector that would flow from reductions in assistance could facilitate better workplace outcomes. Specifically, reductions in assistance could:

- focus more managerial and employee attention on the need to improve productivity and efficiency;
- encourage greater cooperation to achieve this goal; and
- increase incentives to avoid costly industrial disputation.

Some participants also suggested that such induced improvements in workplace arrangements could have flow-on benefits for other industries. For example, the Victorian Farmers Federation said:

> … tariffs are restricting industrial relations reform by protecting manufacturing industries from pressure to contain labour costs. This results in less political support for reforms that would benefit labour-intensive industries, including agriculture.
>
> … there is a strong concern in the farming sector that industries that have received tariff relief over the past three and a half years have not taken the full opportunities to adopt workplace flexibility measures to make them more cost competitive. (trans., pp. 309–11)

10.2 Policy responses to particular workplace issues

Proposed changes to workplace regulations raise complex issues

In the light of recent industrial action and concerns about the possibility of further disputes over the entitlements issue, some groups suggested that changes to the Workplace Relations Act are necessary. The Ai Group proposed that Federal industrial relations legislation be amended to: constrain 'protected' industrial action further and to give the Australian Industrial Relations Commission (AIRC) more power to intervene in disputes causing 'significant damage' to particular firms (see box 10.2).

The Ai Group's proposals have a similar intent to Commonwealth Government amendments (either recently legislated, blocked or still being considered) to the Workplace Relations Act. For example, the Act was amended in November 2002 to constrain protected industrial action by:

- providing for 'defined consequences' in cases of pattern bargaining; and
- allowing the AIRC to suspend or terminate a bargaining period on the grounds that a party is not genuinely trying to reach agreement.

The originating Bill had also sought to provide the AIRC with the power to order cooling off periods in cases of protected industrial action (also suggested by the Ai Group), but this provision was blocked by the Senate.

Box 10.2 The Ai Group's proposed changes to the Workplace Relations Act

In a submission to the Commission, the Ai Group suggested a number of amendments to the Workplace Relations Act. These proposals — which were endorsed by several firms and associations — included the following:

- Additional powers be given to the AIRC to suspend or terminate a bargaining period. These powers would apply where protected action is:
  - causing significant damage to an enterprise; and
  - significantly endangering the welfare of employees in an enterprise.
- Protected action be outlawed for the purposes of pattern bargaining.
- The AIRC be given the power to establish a 'cooling-off' period in appropriate circumstances.
- Secret ballots be mandatory before protected action can be taken.
- The Workplace Relations Act be amended to clarify that protected action cannot be taken prior to the expiry date of a certified agreement.

Source: Ai Group (sub. 11).

Another amendment suggested to the Commission by the Ai Group — introducing secret ballots as a precondition for protected industrial action — was put forward in a separate Bill and also rejected by the Senate (in March 2003). Yet a further amendment is currently before the Senate which aims to strengthen the AIRC's ability to stop 'unprotected' industrial action (especially during the life of a certified agreement), and for applications for a cessation order by affected parties to be determined within 48 hours (with the discretion to issue interim orders stopping industrial action where this is not possible).

However, legislative amendments of the kind proposed by the Ai Group raise complex issues with ramifications beyond the TCF sector which could not be properly addressed in a sectoral inquiry of this nature. Moreover, as the Commission argued in its recent report on post 2005 assistance for the automotive industry (PC 2002b), measures constraining the scope for employees to take industrial action should be viewed as a safety-valve. Most workplace disagreements should be addressed cooperatively and without the need to resort to strike action or the threatened use of regulatory sanctions. In commenting on a similar set of proposals put forward by the Ai Group in that inquiry, the Commission noted among other things that:

- Establishing that an enterprise is suffering 'significant damage' is a much easier hurdle than establishing the likelihood of significant damage for 'the economy or a significant part of it', as applies under the current legislation. While the bar could be too high at present, it is equally possible that the Ai Group's proposals could go too far in the opposite direction.

- The difficulty of establishing whether the proposals would achieve the right balance in constraining industrial action would be compounded by uncertainty about the AIRC's interpretation of terms such as 'significant damage'.
- Shortcomings in the current regulatory arrangements may relate more to the inadequacy of sanctions for non-compliance (the intent of the pattern bargaining amendment mentioned above), than to unduly high hurdles for securing orders to terminate protected action.
- Firms could make better use of the existing regulatory provisions.
- If proposals to further constrain the right to take 'protected' industrial action are generally perceived by the community as too stringent and therefore unfair, it is conceivable that their implementation could serve to reduce the commitment of employees to further necessary workplace change.

In the light of these considerations, the Commission concluded that:

> … whether the proposed regulatory changes would strike a better balance between the rights of employees to further their perceived interests through industrial action and the rights of those who suffer significant damage from such action, is a more difficult judgment to make. (PC 2002b, p. 67)

Moreover, given that much of the potential for disputation in the TCF sector appears to relate to the entitlements issue, dealing with that issue specifically may reduce the need for what would inevitably be contentious changes to workplace regulations in general.

A review of the entitlements issue would be beneficial

Given the large number of firm closures in the TCF sector in recent years and that the process of firm rationalisation is yet to run its course, the securing of employee entitlements is a very important issue. As the TCFL Forum noted:

> Some firms have exited without having adequate reserves to cover employee entitlements. The unions now spend considerable time on protecting workers' jobs and entitlements, which can heighten tensions in industrial relations. (TCFL Forum 2002, p. 39)

Legislative attempts to provide for security of entitlements have so far failed to quell the concerns of employees and the union movement. The General Employee

Entitlements Redundancy Scheme (GEERS) was established in September 2001.[3] It provides payments for unpaid wages; accrued annual leave and long service leave; accrued pay in lieu of notice; and up to 8 weeks redundancy pay. The maximum allowable redundancy amount is set with reference to an annually indexed salary cap ($81 500 in 2002-03). Contractors (which may include some TCF outworkers) are not covered by the scheme. By 30 June 2002, payments to some 4500 individuals had been made under GEERS, with an average payment amount of around $10 000.

The main criticism of the scheme has been that the level of redundancy payment is insufficient to cover the substantial redundancy entitlements accrued by employees in some parts of manufacturing, including the TCF sector. There have also been criticisms that GEERS does not cover unpaid superannuation entitlements. In summarising its concerns, the TCFUA contended:

> Although GEERS provides enhanced benefits for employees who are terminated in the context of their employer becoming insolvent, the TCFUA views both GEERS and its predecessor EESS as fundamentally flawed schemes. Neither EESS or GEERS satisfies the primary objectives of securing and protecting 100% of entitlements for workers in the TCF industries … (sub. 33, p. 50)

To illustrate the perceived inadequacy of the GEERS safety net and the importance of the entitlements issue more generally, the union provided a list of examples of firm closures where employees received none, or only part, of their entitlements (see box 10.3). As further evidence of the extent of the potential shortfall between redundancy-related GEERS support and accrued redundancy entitlements, the Commission was told in discussions that entitlements to more than 70 weeks pay are not unheard of in the TCF sector. (Even where less generous provisions are in place, entitlements are often well in excess of the GEERS safety net.) Moreover, entitlements in particular firms have been uncapped and therefore continue to increase the financial exposure of firms (and risks to employees).

The union was also concerned about the length of time taken to process GEERS claims and for payments to be made suggesting that ‘it takes a minimum of 6 months before GEERS is in a position to make payments…’ (sub. 33, p. 55). A recent report by the Australian National Audit Office commented specifically on this aspect of the scheme. It said:

> There are substantial challenges in making prompt payments under the EESS and GEERS schemes. Overall, DEWR has taken 26 weeks to clear 80 per cent of claims, well short of either its original published standard, 80 per cent in 12 weeks, or its

3 GEERS replaced the Employee Entitlements Support Scheme (EESS) which was introduced on 1 January 2000 and which was applicable to employees retrenched between 1 January 2000 and 11 September 2001 due to the insolvency or bankruptcy of their employer.

> revised standard, 80 per cent in 16 weeks. This may be attributable in part to the difficulty DEWR has in obtaining, promptly, verified information from [insolvency practitioners] on unpaid employee entitlements. However, it will only be possible to clarify this if DEWR keeps more detailed records of the key steps in processing. (ANAO 2003, p. 5)

The union further noted that the GEERS process only begins when an insolvency practitioner (administrator, liquidator, receiver and manager, or controller) has been appointed to an insolvent company. In practice, this means that an employee made redundant prior to a firm being declared insolvent has no recourse to GEERS until that condition has been met.

Box 10.3 **Access to employee entitlements following TCF firm closures**

Examples of TCF firm closures over the last few years highlight a diversity of outcomes for employees in securing their accrued entitlements. Examples include:

National Textiles

- Ceased trading January 2000
- 342 employees owed $11 million in entitlements
- Company deed of arrangement and a Commonwealth budget appropriation resulted in entitlements being paid out in full

Coogi Australia Manufacturing Pty Ltd

- Placed in administration July 2002
- Employees owed $3.7 million in entitlements (including superannuation)
- Application for GEERS funding made November 2002
- GEERS payment covering annual and long service leave and 8 weeks redundancy made March 2003
- $0.4 million in superannuation entitlements as yet unrecovered

Tadbury Australia Pty Ltd

- Placed in administration October 1999 (pre EESS and GEERS)
- 18 employees owed $1.3 million in entitlements (unrecovered)

Dan Apparel Pty Ltd

- Liquidator appointed September 1996 (pre EESS and GEERS)
- 39 employees owed $0.6 million in entitlements (unrecovered)

Bedico Trading Pty Ltd

- Administrator appointed February 2000
- 61 employees owed $0.6 million in entitlements
- EESS pays entitlements to the value of 26 per cent of amount outstanding

Sources: TCFUA (sub. 33) and Bickerdyke, Lattimore and Madge (2000).

But not all participants viewed GEERS as inadequate. Both the Ai Group and Australian Business Limited (ABL) voiced strong support for the scheme. In commenting specifically on the GEERS redundancy provisions, the Ai Group argued that the 8 week cap is in fact a 'community standard' and that paying entitlements on the basis of negotiated outcomes in enterprise agreements would discriminate between employers depending on their particular circumstances:

> The community standard for redundancy pay is found in the Termination Change and Redundancy provisions in the AIRC test case and the many and various awards which have adopted it. If the Federal Government's scheme provided for a higher level of redundancy pay or unlimited benefits, the system would not treat all employees fairly. Some employees would receive the community standard while others would be more generously rewarded. By following the community standard, the Government is ensuring that all Australian workers are treated fairly in the relatively small number of cases when a company becomes insolvent and is unable to pay employees' entitlements. (sub. PP140, pp. 13–14)

Nonetheless, the inadequacy, from the employees' perspective, of the GEERS safety net has led to various negotiated firm specific responses to secure entitlements. Some firms have set aside an amount of working capital to cover redundancy entitlements. And one firm told the Commission that it had moved from an uncapped scheme to one limited to 8 weeks pay (for new employees) in exchange for a number of new conditions (including a wage rise).

In some cases, firm-level solutions may be effective and efficient. However, firm-level responses can be costly — particularly for 'at-risk' firms. Moreover, negotiations on this issue at the firm level have been accompanied by industrial disputation and production stoppages. Even where there has been no formal dispute, the focus of negotiations appears to have been on ways to secure entitlements rather than on how to improve the prospects of the firm and thereby increase employment security. In either case, firm performance will have been diminished.

Several alternatives to GEERS have been suggested to deal with the issue including: industry-wide trust funds; levy schemes such as that used to make provision for the entitlements lost after the collapse of Ansett Airlines; compulsory pooled insurance schemes; and amendments to the Corporations Law which would place employees above secured creditors in claims on the assets of insolvent companies.

A somewhat different approach was advocated by DEWR which emphasised a need for firms to minimise or reduce their financial exposure to employee entitlements in the event of closure. It said:

> There are other options to trust funds. Audits can be conducted and liabilities could be reduced over time through mechanisms such as cashing out leave. Further, employers and employees should refrain from developing overly generous redundancy

> arrangements. Many firms report that the potential cost of redundancy has hampered their ability to restructure and adapt, eventually undermining the company's long term viability. (sub. 84, p. 9)

However, all these approaches have shortcomings (see also box 10.4).

Trust funds have been criticised on several grounds, including that they would tie up large amounts of the working capital of viable (and secure) firms. The Ai Group estimated that employers would need to contribute close to 20 per cent of their payroll into a fund to cover entitlements. It also raised a range of tax-related issues and concerns (see sub. PP140, pp. 10–11).

Problems with other suggested approaches to securing employee entitlements include:

- Taxpayer funded solutions could potentially send inappropriate signals to firms regarding the need to have adequate financial resources to pay for entitlements.
- Amendments to the Corporations Law to treat employees more favourably than other creditors disadvantaged by firm closures raise equity issues and could, in turn, lead to the failure of creditor companies. According to the Ai Group it would also raise the cost of obtaining finance for firms (sub. PP140, pp. 16–18).
- As concerns expressed by participants about workers compensation arrangements illustrate (see chapter 11), designing efficient pooled insurance arrangements would be difficult.
- The strategy proposed by DEWR may suit new firms, or viable established firms, but it is unlikely to be particularly helpful for firms which are 'at-risk' and therefore more likely to be unable to fully cover employee entitlements.

Nonetheless, in the Position Paper, the Commission argued that given the potentially large costs of failing to resolve this issue in the TCF sector and other parts of the economy, a 'circuit-breaker' was needed. In bringing the parties together to develop a constructive way forward, the Commission suggested that a useful first step would be to conduct an independent review of the issue. It saw this as providing the basis for a thorough and unbiased assessment of the economy-wide magnitude of the problem and the relative merits of alternative solutions to it.

Box 10.4 Alternative approaches to protecting employee entitlements

A 2000 study by Productivity Commission staff into the impacts of business failures in Australia assessed, among other things, four approaches to the protection of employee entitlements. These approaches differ in terms of whether employees, governments or employers provide the funding, the basis on which payments would be made and the treatment of insolvency risk. They include schemes with characteristics similar to GEERS and those preferred by the union movement (trust funds).

Voluntary employee insurance

This would see *employees* purchasing insurance cover privately to protect their entitlements in the event of firm insolvency. Advantages of this approach were argued to include: providing employees with a choice of risk cover based on their individual needs; sending effective price signals (through differences in premiums) about the risk of firm insolvency to employees; and premiums that would vary with the size of the entitlements at stake.

Potential problems identified included: employees viewing self-insurance of their legal entitlements as unjust; employees not seeking cover because of ignorance about the risks; prohibitive costs associated with monitoring and administering a large number of policies; and (if insurance premiums were initially set to cover average risk because of problems with identifying different degrees of insolvency risk across firms) the potential for only high risk employees, or no one, to eventually be left insured.

Government provision (without risk rating of employers)

The second approach examined was *government* provision of a national fund to insure, collectively, all employees for lost entitlements in the event of insolvency. This is the basis on which GEERS operates and is also the most common approach overseas. This mechanism was preferred by the authors (see below) with significant advantages identified as: by providing universal coverage, it avoids the potential problem with voluntary schemes of only some employees being left insured; it relies on existing mechanisms (taxation) for funding; it is simple and international experience shows administrative costs to be low.

Limitations noted by the authors included: the failure to take account of differences in firms' insolvency risk means firms are not provided with incentives (through insurance premiums) to reduce insolvency risk; budget funding exposes governments to unknown future liabilities; and that capping practices commonly associated with such mechanisms mean that some employees could receive low levels of insurance cover relative to entitlements.

Continued next page

Box 10.4 (continued)

Compulsory risk-rated insurance funded by employers

A third option canvassed the provision of private insurance cover by *employers* to protect employee entitlements in case of insolvency. Under this approach, insurance premiums would be based on the likely insolvency risk and associated non-payment of entitlements. The main advantage was found to be that it provides incentives (through potentially lower premiums) to employers to take steps to reduce their risk of insolvency.

However, administrative complexity (common to risk-rated insurance schemes in general) was seen as a potentially major difficulty. To be effective, premiums would need to be commensurate with the likelihood of failure — and that can be difficult for commercial insurers to estimate.

Trust funds

Finally, the study assessed the use of *employer* funded trusts to safeguard accrued entitlements in the case of insolvency. The study noted that as well as covering accrued entitlements such as annual leave and long service leave, trust funds could also have a contingent liability element to cover potential insolvency expenses such as redundancy payments. The main advantage of this arrangement was seen as providing employees with secured creditor status in the event of insolvency.

Problems identified with the approach included: ensuring that payments by employers found their way to the trust fund at regular intervals (avoiding similar problems with superannuation guarantee payments raised by the TCFUA); and accurately determining contingent liabilities leading to the possibility of excess provision and associated loss of working capital. And, unlike other approaches, trust fund mechanisms would introduce transitional issues as existing businesses would need time to move to full provisioning for entitlements.

Findings

The study concluded that *government* provision of employee protection funds (such as GEERS) has some significant design advantages. However, in the context of current redundancy entitlement levels in the TCF sector and other parts of manufacturing, the study's observations on the adverse implications of capping are pertinent.

Source: Bickerdyke, Lattimore and Madge (2000).

There was widespread support for this suggestion from a cross-section of TCF interests, with the TFIA representatives at the public hearings summarising the views of the industry as follows:

> It [the entitlements issue] cannot be resolved at a firm level; it just simply cannot be. I welcome the position that the Commission took, and that is some sort of a tribunal perhaps that could be set up, or a commission of inquiry or something, that could maybe look at all these issues and get all of the participants around the table, including

> the Ai Group, the unions, employers, employer groups et cetera, and just to thrash the thing around. To some extent I think that perhaps all of those participants don't know some of the problems of the others within the process and they need to clearly understand some of these implications. (trans., p. 33)

The union movement also expressed general support for a review, with the ACTU commenting on both the need to canvass options and to educate company directors on their responsibilities.

> … even if we could get a debate about options we would be a step ahead. It is not our will to break the industry. We actually understand that profitable industry means jobs and it means investment and it means growth. We are in this together but we cannot stand back and watch … industry just abdicate its responsibility for this and we say to them let us find the cheapest possible means for you to guarantee these most vulnerable workers their entitlements and we will stand with you. (trans., p. 426)

But, while welcoming the proposed review, the TCFUA argued that the Commission had not gone far enough in making a specific recommendation as part of its evaluation of the TCF sector.

The only outright opposition to the Commission’s suggestion came from the two employer groups (though not from some of their member companies) and DEWR. The Ai Group, for example, opposed a review on the basis of its perception that existing arrangements provide adequate protection for employees. It said:

> Ai Group does not believe that it is practicable or desirable for an industry level scheme to be implemented to protect entitlements in the TCF sector. Ai Group favours the Federal Government legislating the terms of GEERS as a safety net scheme generally applicable to all Australians. We therefore see no need for an independent review. (sub. PP140, p. 7)

DEWR did not support a review on the grounds that aspects of the issue are already being considered by a Parliamentary Committee and that GEERS should not be regarded as inadequate for not covering negotiated entitlements which are ‘overly generous’. DEWR said:

> The Department does not support such a review. An inquiry into Australia’s insolvency laws is currently being conducted by the Parliamentary Joint Statutory Committee on Corporations and Financial Services. The treatment of employee entitlements is included in the terms of reference for that inquiry.
>
> … employers and employees need to refrain from developing overly generous redundancy arrangements. We recommend that the final report of the Commission contain recommendations for implementation at the workplace level that would reduce the incidence of abnormally high levels of redundancy entitlements in this industry, which have been identified as an impediment to restructuring. (sub. PP131, p.1)

Australian Business Limited also opposed a review and expressed a commitment to the GEERS arrangements:

> ABL agrees with the preliminary finding that security of entitlements has been a concern for employees and has been associated with costly industrial action in TCF and elsewhere. It does not support a review of entitlements. ABL is supportive of the current GEER Scheme. (sub. PP181, p. 7)

Notwithstanding these concerns, the Commission remains of the view that an independent inquiry would be a useful circuit-breaker and a means of progressing this divisive and complex issue. Without some action, there is a prospect of more damaging industrial disputation in the TCF and other sectors, and a continued diversion of effort in workplace negotiations away from initiatives to improve firms' viability. Moreover, the Commission is encouraged by the broad cross-section of support it has received for its review proposal given that progression of this issue through an inquiry process and beyond will require considerable cooperation between the parties.

It also reiterates that all the possible 'solutions' raised to date have problems and that no one solution is clearly preferable. Some level of compromise will inevitably be required. This is precisely the reason why an independent, economy-wide review would be helpful — to assess the costs and benefits of each option in a dispassionate way, placing the community's interests ahead of the individual concerns of firms and employees. In progressing this issue, the Commission also endorses the argument put by the ACTU that there is a need to ensure that employers fully understand their obligations in this area. It is equally important that employees understand the consequences for firm viability of pursuing inappropriate means of securing their entitlements. Hence, industry associations, employer groups and unions all have an important educative role to play.

FINDINGS ON WORKPLACE ARRANGEMENTS

- *While workplace arrangements in many Australian TCF firms are more productive and flexible than in the past, further improvement would help some firms to compete successfully with lower levels of assistance.*
- *Given the number of 'at-risk' firms, the TCF sector can ill-afford the industrial disputation recently witnessed in some enterprises.*
- *Responsibility for achieving better workplace outcomes rests largely with managers and employees within individual enterprises. Better communication and more cooperation between the parties is crucial.*
- *Human resource and industrial relations skills in the sector require improvement. Among other things, this would help to promote cooperative solutions to industrial relations issues and assist managers to convey to their*

employees and union representatives the relationship between workplace outcomes and the viability of the enterprise and the industry.

- *Workplace regulation has an important role in setting the framework for negotiations between firms and their employees and representatives. However, specific proposals put forward to constrain further the rights of employees to take industrial action raise complex issues that would have ramifications in other industries. This means that it is not possible to judge their merits solely on the basis of recent experience in the TCF sector.*
- *The protection of employee entitlements is a legitimate concern for employees in the TCF sector given its history, and has been a trigger for costly disputes in this and other sectors. An independent review of the broader entitlements issue is warranted.*

10.3 Skilling and training issues

The sector's skill requirements are changing

The TCF sector draws on a wide range of skills including trade, technical, design, manufacturing, logistics, sales, marketing and general management skills. The required skill set has changed as the sector has moved toward higher value products, the boundaries between manufacturing and distribution have blurred, and new technologies have been introduced. Design, sales, marketing, information technology and e-commerce skills have become more important, while demand for traditional trade skills has declined. With the growing emphasis on innovation, an appropriately skilled workforce and supportive education and training infrastructure are becoming more important to the future international competitiveness of the sector.

Despite the shift in TCF activity and the associated changes in skill requirements, there has not been a marked change in 'entry level' skills in the sector (see table 10.1). This does not necessarily mean that there is a skills problem in the sector, however, because much skill development, as in manufacturing more generally, occurs within the workplace.

Table 10.1 **Educational attainment of TCF workers, 1996 and 2001**

per cent

	Textiles, clothing and footwear		*All manufacturing*	
	1996	*2001*	*1996*	*2001*
Bachelor degree or higher	8	8	8	11
Skilled vocational	13	7	25	25
Other post-school[a]	10	19	13	14
Total with post-school qualifications	**31**	**34**	**46**	**50**
Total without post-school qualifications	**69**	**66**	**54**	**50**

[a] Includes basic vocational training, undergraduate diplomas and associate diplomas.

Sources: IC (1997) and ABS (2001b). See also appendix table B.14.

Skill shortages are emerging in some areas

Skill shortages were a concern for some participants, with designers, sewing machinists, textile production workers, tanners and fabric cutters being the most common employee-related examples cited (see box 10.5). A number of participants also pointed to deficiencies in management skills, particularly in the financial, industrial relations and human resource areas (see section 10.2).

Some participants suggested skill shortages and deficiencies will become a more pressing issue for the sector in the next few years because of:

- the sector's ageing workforce;
- a decline in apprenticeships making it more difficult for parts of the sector to access necessary trade skills (though others disputed that this was an issue);
- negative perceptions about the sector as a career choice;
- the failure of training institutions to adapt to the changing needs of TCF firms;
- loss of 'critical mass' making it difficult to retain certain skills; and
- a continuing lack of emphasis in some parts of the sector on skill development, with some participants commenting that the preponderance of small businesses poses particular challenges given financial and time constraints on operators and a lack of knowledge of training options.

Box 10.5 **Participants' views on skill shortages**

Skill shortages and their underlying causes and consequences were discussed at length in some submissions. For example, the TCFUA said:

> It is expected that within the next three years the departure of a number of experienced sewing machine operators and cutters will leave skill gaps in the clothing sector. Alongside this the need for TCF mechanics remains high, while the need for textile technicians and technologists has increased as many companies look to innovation in order to remain competitive. Other trade areas such as electricians and fitters will be required to service the burgeoning number of small enterprises. Due to the current unpopularity of the TCF&L industries as a career choice for young people (with the exception of clothing design), the exit of experienced human resources presents a challenge for the industry.
>
> Concurrently, the industry will start relying even more on professional occupations such as sales people, marketing and warehousing personnel, who will all require high-level skills in information and communication technologies and supply chain management. (sub. 33, pp. 83–84)

Defab Weavers commented that :

> The difficulties facing TCF companies adjusting to the changes in the sector include the … shortage of skilled labour entering the TCF industry and the lack of educational institutions offering textile related courses. Consequently, wages have steadily increased (eg skilled weavers) whilst the average age for TCF workers has also increased as younger people are choosing not to enter the TCF industry due to its relatively negative image. Whilst labour costs through awards have kept within the CPI, TCF companies, in reality, have to pay a premium for skilled labour well above award (eg dyers, technicians and administration). (sub. 65, p. 3)

In commenting on the scope for the education and training regime to remedy skill gaps of this type, participants pointed to various deficiencies in that infrastructure (see the text below). Problems with education and training in the sector have also been canvassed extensively in some recent reports on the sector. For example, the Victorian TCFL Strategic Audit noted:

> Because of the low priority given to training by the industries neither vocational education and training (VET), nor higher education systems have recognised the nature of the industries' problems or responded to them. … There is a view in industry that not enough government training funds 'hits the floor', that too many private providers offer poor value and quality, and that government training providers are inflexible with too little workplace provision available. (Victorian Government 2000, p. 16)

A responsive education and training system is important

Notwithstanding the heavy emphasis on 'on-the-job-training', formal education and training programs have an important role to play in helping to develop and maintain workforce and management skills in the TCF sector. TCF specific education and training includes vocational secondary school education, formal Vocational Education and Training (VET) and Higher Education.

TCF employees also have access to generally available programs, including the Workplace/Workbased English Language and Literacy Program (WELL) funded at an annual level of $12 million since 1992 (sub. 41, p. 11), and the National Program for Excellence in Education and Training ($10 million in overall funding). Guidance on training issues is provided by several bodies including the Australian National Training Authority (ANTA), Light Manufacturing Training Australia (LMTA) and State based Industry Training and Advisory Boards (ITABs).

The nature of education and training requirements has been changing as the skill set demanded by the sector has evolved. The growth of the technical textiles industry, for example, has increased the demand for skills in engineering, computer assisted design and manufacturing, industrial chemistry and project management.

The main delivery vehicle for TCF training — the VET sector — has undergone considerable change over the last 15 years with the introduction of competency based training under the National Training Framework (NTF). The development of a specific TCF Training Package (currently being reviewed) setting industry skills within Units of Competency and providing national qualifications from Certificate to Advanced Diploma levels, is an important outcome of the NTF. Some TCF firms are registered VET providers. Allied to the development of a sector specific training package, a number of educational institutions have expanded their course offerings with components oriented to skill development in TCF-relevant areas.

Development of the training infrastructure has also extended to collaborative links between some universities, firms and organisations in the TCF sector. For example, the TTNA said that through collaborative linkages it had been able to implement training in areas that were previously not catered for:

> Until recently, there were no courses or even modules on offer for this vital industry sector. To address this, the TTNA collaboratively with RMIT and the IFC, obtained the licence to deliver the EDANA nonwoven course annually in Melbourne. Whilst only a three day event, it covers all aspects of nonwoven technology and production and has been a considerable success. (sub. 68, p. 22)

The TTNA further noted that it was planning to work collaboratively with the RMIT to attract students to the technical and nonwoven textile sector by way of scholarships (sub. 68, p. 20).

While ‘in-house’ training will continue to be the major source of skill formation in the TCF sector, the evolution in institutional training options witnessed in recent years will need to continue in the future. The need for responsiveness relates not just to the delivery by educational and training institutions of ‘off-site’ courses that meet the sector’s changing needs, but also to those training packages that are delivered ‘in-house’. Indeed, the TFIA signalled the need for a shift in emphasis toward enterprise-based training saying:

> One clear issue is that the national training programs focus on the delivery of a qualification to a person in a particular field, whereas often the real need is for specialist training or skills acquisition to meet the needs of a particular enterprise. There needs to be more flexibility based on enterprise-based improvements through tailored programs. The training must be driven by the demand, not the supply. The TFIA believes that a shift towards enterprise needs as opposed to packaged learning objectives would be a valuable and positive contribution. (sub. 75, p. 8)

Responsibility for improving current arrangements mainly rests with the industry and training providers

From a policy perspective, it is important to recognise that *periodic* skill shortages, and lags in the focus of training packages relative to the needs of industry, characterise most labour markets. They do not necessarily require remedial action. If firms, education institutions and associated training infrastructure have the capacity to respond effectively and quickly to changing skill needs, deficiencies in skilling and training outcomes should be short-lived.

However, there are some concerns that the current education and training system is not sufficiently responsive to the TCF sector’s changing needs and that, as a consequence, skill problems are likely to worsen in the future. Reasons given for this lack of responsiveness include the low priority accorded TCF training by training institutions because of the low skill image of the sector; insufficient dialogue between firms and education and training providers; a continuing over-emphasis in current training packages on the lower end of the TCF skill spectrum; and the large number of small firms in the sector. In regard to the latter point, the TCF Resource Centre of WA, which has been organising training workshops for small TCF firms for the past five to six years, said that:

> … the national training packages for TCF are really good, but TCF assistance for the actual small business operator still is nonexistent. There are many, many gaps. Small business people in Australia need training provided to them in a way that they can afford to take it. (trans., p. 273)

In the Commission’s view, much of the responsibility for addressing these sorts of concerns lies with the sector and the education and training providers rather than with government. As in the case of workplace arrangements, effective communication between the parties is a pre-requisite for the development of courses and training packages that meet the sector’s changing needs. The various industry associations have an important role to play in this area, both in communicating the sector’s needs to providers and in liasing with government where ‘systemic’ deficiencies are identified. This point was acknowledged by the TTNA when it commented on inadequacies in the current training infrastructure:

> The industry requires for the future a rising number of skilled workers who are able to cover broad areas of employment with the support of flexible training. Rigid vocational training no longer does justice to the capital equipment and end-applications. A responsive educational and training system is crucial to all manufacturing industry sectors, as is ongoing dialogue between industry and training providers. (sub. 68, p. 21)

The Commission also notes that the current review of national TCF training provides an opportunity to address these sorts of issues so as to improve the sector's training regime. As Light Manufacturing Training Australia said:

> This Review presents the industry and governments (national, state and territories) with a unique opportunity to analyse the role that education and training has played in assisting the TCF industry to adjust into activities where it is internationally competitive and how it will help the industry to contribute to the overall improved performance of the Australian economy.
>
> The TCF Review will look closely at emerging needs and prepare Units of Competency to reflect the management and workforce skills to match these changes in business operations and systems. (sub. 41, p. 3)

Some changes in detailed policy settings — particularly at the State and Territory level — may be required as a result of this review to facilitate the efforts of firms, industry associations and training providers more generally. A range of possible changes to those detailed settings were discussed in submissions from training organisations. However, an assessment of those proposals is beyond the scope of this inquiry.

There is a related policy issue of whether Commonwealth budgetary support for the TCF sector should include specific funding assistance for training. Several participants raised concerns about the impact of expenditure cuts to TCF related programs in May 2002 (due to take effect at the end of 2003) and the earlier cessation of a TCF specific WELL program.

The Commission notes that funding for several other industry specific training programs will also be discontinued at the end of 2003. More importantly, it is not clear that the needs of the TCF sector are sufficiently different from other activities as to warrant the ongoing provision by the Commonwealth of sector specific training support. While the workforce has some different characteristics to other industries, these are at least partly addressed through generally available programs funded by the Commonwealth. Moreover, there are various industry extension-type programs with the capacity to provide support for training operating at the State level. Notably, concerns about the prospective end to the Commonwealth programs were less evident amongst firms than from entities delivering training to the sector.

- *Some skill shortages and deficiencies in available training packages are evident in parts of the TCF sector. However, identifying what specific responses may be required is beyond the scope of this inquiry. Importantly, responsibility for ensuring that skill and training needs are met lies largely with the sector, educational institutions and training providers, rather than with governments.*

10.4 Outworkers

As in other countries, outworkers are a feature of clothing manufacturing in Australia. From the perspective of the manufacturer, outworkers can provide flexibility to respond quickly to varying customer needs which can be more difficult to achieve in a factory setting. The flexibilities offered by outworkers are particularly important in Australia now that much of the high volume clothing production has moved offshore with domestic producers now concentrating on the quick response/low volume production which can be difficult to source from imports.

Some outworkers may benefit from the flexibility in pace and timing of work and being able to combine family responsibilities and paid employment. In some cultures sewing is seen as a traditional occupation for women which is compatible with home and family responsibilities. Indeed, outwork may provide one of the few job opportunities for newly arrived migrants, particularly those with poor English language skills and relatively low levels of formal education.

At the same time, however, the use of outworkers raises concerns about exploitation. These relate not only to inadequate rates of pay, but also to excessive hours of work, poor working conditions and the use of children in outwork. Those engaged in outworking are typically women from East Asian backgrounds with often basic skills and frequently with low levels of English language proficiency and limited formal education. With few alternative job opportunities, they may also have limited negotiating power over pay and working conditions. DEWR commented on some of the consequences:

> It is generally accepted that TCF industry outworkers often receive payment and work under conditions which are inferior to those applicable to factory workers doing comparable work. Contract outworkers are often particularly disadvantaged due to a lack of clarity concerning their rights and entitlements. (sub. PP131, p. 2)

Several recent reports have similarly pointed to examples of exploitation and various examples and claims of exploitation were also raised in submissions to this inquiry (see box 10.6).

In response to such concerns, governments have implemented a range of legislation to try to ensure outworkers receive at least minimum rates of pay and work in appropriate conditions. However, such minimum standards are widely regarded as having been ineffective because of difficulties in enforcement (or a lack of resources devoted to enforcement). Also, others have raised concerns about the potential for regulation, or heavy handed attempts to enforce regulation, to push more clothing production offshore, thereby reducing job opportunities for outworkers.

However, there are indications that compliance with the legal requirements has recently improved (see below). Also, there are a number of factors that tend to limit the use of outworkers and hence the potential for exploitation. For example, the use of outworkers can result in poor quality control and variability in production due to the long and convoluted supply chains in garment production which removes contact between the principal/retailer and the outworker. Moreover, given the negative perception associated with this form of employment, some producers told the Commission they do not use outworkers, while some retailers indicated that they will not deal with suppliers who use outworkers.

Box 10.6 **Concerns regarding clothing outworkers**

According to a 2001 study by Cregan (sub. 30) covering a small group of 119 outworkers, the average hourly rate paid to them was substantially below the award rate and hours of work in peak times ranged between 12 and 18 hours a day, 7 days a week. In addition, the TCFUA (sub. 33) claimed that:

- while outworkers rarely receive any workers compensation, they commonly suffer from overuse injuries caused by poor working conditions, long hours and a lack of adequate occupational health and safety procedures;
- children and other family members are often used to assist in meeting production deadlines;
- outworkers are often not paid for the work they do and receive no sick leave, annual leave, superannuation or overtime rates of pay; and
- because the supply chain consists of numerous subcontractors, outworkers may often not know the identity of the principal manufacturer, making it difficult for them to pursue any unpaid monies and/or other entitlements.

How many outworkers are there?

Estimating the number of people engaged in outwork in the TCF sector has proved to be difficult. This is partly due to the nature of outwork and the complex supply chains involved. Also, where outworkers are paid in cash, they may wish to remain unidentified for tax or social security reasons.

A 2002 Parliamentary inquiry into the conditions of clothing outworkers in Victoria (Parliament of Victoria 2002) was 'constantly aware of the invisible nature of outwork'. Similarly, Webber and Weller (2001) concluded that:

> Outworkers are often employed in the unregulated economy or on the margin of regulations, so the workers have been difficult to locate and study. (p. 291)

Further, the seasonal demand patterns of the clothing industry mean that the number of outworkers employed at any one time is likely to fluctuate.

Previous estimates of the number of outworkers have been compiled using different bases. For example, the TCFUA estimated that there are around 330 000 persons engaged in outworking in some capacity (sub. 33). This estimate is from the TCFUA's 1994 'National Outwork Information Campaign' which estimated the total pool of people who undertake outwork on either a part-time, full-time or irregular basis. In its 1997 inquiry into the sector, the Industry Commission (IC 1997) estimated there were around 23 000 full-time equivalent outworkers, an estimate often quoted as the most reliable available at that time.

Since 1997, there have been several factors impacting on the number of outworkers. With the relocation of much high volume standardised production offshore and the associated increase in import penetration of the local market, total domestic clothing production has declined. This will have tended to reduce employment opportunities for outworkers.

On the other hand, there has also been a shift of garment assembly from factories to the outworking sector to give firms greater flexibility to meet customer demands for fast turnaround supply. As Calcoup Knitting commented:

> … [of] the people that use outworkers the majority have already moved a lot of their stuff offshore … the outworker is only giving them the quick response back here in Australia on the short runs that they can't fill overseas because it's taking them about eight weeks to get the turnaround to get it back. (trans., pp. 458-59)

Such contracting out of quick response/low volume production is likely to have increased the demand for outworkers. A further factor likely to have increased the number of people involved in outwork is the growth of open air market retailing, which has also provided outworkers and their associates with the opportunity to retail the garments they produce.

It is very difficult to gauge the net effect of these developments on the total number of outworkers in Australia. Some participants, such as the TCFUA, thought that the number of outworkers had increased significantly since the Industry Commission's 1997 inquiry, though they provided no supporting data. However, using similar methodologies to update the figures from the 1997 inquiry, it seems unlikely that the full-time equivalent number would be much more than 25 000 (see box 10.7).

Box 10.7 **Estimating the number of outworkers**

The Industry Commission (1997) estimated there were 23 000 full-time equivalent outworkers in 1997. This estimate was constructed from data supplied by the TCF industry on the number of workers required to manufacture the total volume of locally produced apparel.

If the proportional share of local clothing output attributed to outworkers in 1997 had remained constant, in line with the subsequent decline in total output, there would have been around 16 400 full time equivalent outworkers in 2002.

However, the significant shift in garment production out of factories since 1997 indicates that this number would now be considerably higher. Assuming that every factory based position lost since 1997 was transferred to the outwork sector would see the 16 400 figure increase to around 27 500. To the extent that productivity levels in the outwork sector are lower than in a factory based setting, this figure would increase further. On the other hand, part of the decline in employment in the clothing industry since 1997 reflects the shift of garment production offshore reducing the implied number of outworkers below the upper bound figure.

Taking all these factors into account, the Commission considers that the full-time equivalent number of outworkers is unlikely to be much above 25 000. Nonetheless, with the decline in TCF employment over the last few years, this would mean that outworker employment is now around 40 per cent of total factory based employment across the whole TCF sector and exceeds factory based clothing manufacturing employment by about 25 per cent.

Initiatives to protect outworkers

Initiatives to protect outworkers have generally not sought to eliminate home-based work. Rather, the focus has been on ensuring that outworkers are provided with similar minimum pay and conditions as factory based workers.

Clothing Trades Awards prescribe wages and conditions for factory based employees and outworkers alike

The Federal Clothing Trades Award 1999 seeks to provide parity between factory based employees and outworkers irrespective of whether the latter are classed as employees or independent contractors. To this end, it prescribes rates of pay, the timing of payment of wages and the records employers are required to maintain with respect to outworkers. Under the award, an employer who engages contractors or outworkers is required to register with the Clothing Trades Board of Reference, comprised of union, employer and Australian Industrial Relations Commission representatives. At present, there are 111 firms registered across Australia. Registered employers are not allowed to employ more than 10 outworkers without the consent of the Board or the TCFUA. Failure to register can result in prosecution under the award (sub. 84). The award also requires employers and outworkers to enter into a written agreement concerning hours of work. This Federal award is mirrored closely by the clothing trades awards in each State.

Enforcement of these awards as they apply to outworkers requires either an outworker to make a complaint that requirements concerning pay and conditions have been breached, or the TCFUA or relevant government industrial department to identify instances of non-compliance.

However, it is widely acknowledged that compliance with these award requirements in parts of the sector has been poor. This has partly been attributed to the fact that outworkers may be unaware of the existence of the award, or unwilling to report breaches for fear of losing work. Moreover, the long and convoluted supply chains in garment production may make it difficult for the outworker to identify their actual employer. Given such concerns, additional initiatives have been implemented or proposed to encourage greater compliance with the award requirements.

A Code of Practice has been established

Negotiations between the TCFUA, retailers and the TCF manufacturing sector to establish a system of self-regulation commenced in 1996, following a Senate Inquiry into the conditions of outworkers. These negotiations resulted in the Homeworkers Code of Practice which is aimed at monitoring the production chain from the outworker to the retailer to encourage compliance with minimum wages and conditions for outworkers. However, the Code has only been widely operational since October 2002 when a large number of retailers became signatories.

The Code has two parts. The first is an agreement between the Australian Retailers Association (ARA) and the TCFUA. It obliges retailers to require their suppliers to comply with the awards and other relevant legislation, spells out the role of the TCFUA in monitoring compliance, and establishes procedures in the event of breaches of the Code. It also allows retailers, through the ‘No Sweatshop’ label, to promote that they do not deal with companies that exploit outworkers. However, as far as the Commission is aware, such labelling has been little used to date — the Brotherhood of St Laurence’s Hunter-Gatherer retail establishment was the only example drawn to the Commission’s attention (sub. 74).

The second part of the Code deals with manufacturers, wholesalers and fashion houses. It establishes a code of practice for manufacturers in dealing with their suppliers, provides for the accreditation of manufacturers complying with the Code and sets out dispute settlement procedures (see box 10.8).

While the Code is now well supported by retailers, only four of over 130 manufacturers and wholesalers signing the Code have become accredited. The Victorian Parliamentary Committee inquiry commented that manufacturers had been slow to seek accreditation as they were unsure about the commitment of retailers to either the Code or to those suppliers which achieve accreditation. It also found that the administration fee of $2200 was a deterrent for small manufacturers and contractors to seek accreditation (Parliament of Victoria 2002). However, the Commission was told that with the large number of major retailers signing on to the Code in late 2002, there should be a major ‘knock-on’ effect with more manufacturers and wholesalers seeking to become accredited.

New legislation has been introduced

Both the Commonwealth and a number of State Governments have implemented, or are proposing to introduce, legislation to add to the protection already provided to outworkers in awards and to achieve increased compliance with these awards.

The New South Wales *Industrial Relations (Ethical Clothing Trades) Act 2001*, which commenced in February 2002, inserted special provisions into the *Industrial Relations Act 1996* to ensure that outworkers are deemed to be employees; provides for outworkers to claim for unpaid remuneration by serving a written notice on the person that the outworker believes to be their employer; and increases the power of inspectors regarding access to records of employers and residential premises used in the clothing trade.

Box 10.8 **The Homeworkers Code of Practice**

Provisions for retailers

Under the Code retailers must require their TCF suppliers to comply with the award provisions and other relevant laws in respect of outworkers. The TCFUA is responsible for monitoring compliance and advising retailers of any breaches of the Code by suppliers.

As part of the arrangements, the ARA is to compile a list of all names and addresses of TCF suppliers from information provided by individual retailers. Where the TCFUA can demonstrate a likely breach of the Code by a particular supplier, the ARA will pass on details of the retailers dealing with the supplier. The relevant retailers must then provide assistance in investigating the matter.

If the Code has been breached, the supplier is required to take remedial action. Where it does not do so, retailers are to cease dealing with that supplier.

As part of the agreement, retailers may promote that they deal only with TCF suppliers that do not exploit outworkers.

Provisions for manufacturers, wholesalers and others

The second part of the Code establishes a Code of Practice Committee consisting of an equal number of employers and TCFUA representatives. The Committee deals with accreditation of manufacturers, disputes settlement in relation to the Code and the development of standard product specifications. (These standard specifications are designed to assist in determining whether outworkers are receiving prescribed rates of pay.)

To become accredited, TCF suppliers are required to provide records or demonstrate that they or their sub-contractors are meeting the prescribed pay and conditions.

Where a breach of the Code is identified by the TCFUA and is not rectified within an appropriate time, the accredited supplier will cease dealing with that contractor. Suppliers risk losing accreditation and contracts with retailers if their contractors continue to fail to pay outworkers correctly or do not otherwise comply with the Code.

The legislation also established an Ethical Clothing Trades Council comprising retailers, manufacturers, the TCFUA and community groups. The Council's role is to:

- provide advice to the New South Wales Government on the levels of compliance with both legal and voluntary obligations to outworkers;
- promote compliance with, and enhance the use of self regulatory mechanisms such as the Homeworkers Code of Practice; and

- advise the New South Wales Government on whether there is a need to introduce a mandatory code for the clothing industry and the content of any such code.

In Victoria, the Outworkers (Improved Protection) Act — which is similar to the New South Wales legislation — was passed in May 2003. It defines outworkers as employees for the purposes of the legislation and makes it easier for them to claim for unpaid wages. As in New South Wales, the Victorian legislation also provides for an Ethical Clothing Trades Council of Victoria consisting of industry and employee representatives appointed by the Minister.

The Victorian Government noted that the role of the Council is to foster the development of voluntary self-regulation and that further mandatory requirements would only be introduced if these arrangements were inadequate in improving compliance. It said:

> - a primary role of the Ethical Clothing Trades Council of Victoria established under the *Outworkers (Improved Protection) Act 2003 (Vic)* (the Act) is to monitor and foster the development within the industry of voluntary self-regulatory mechanisms as a means of ensuring that outworkers receive their entitlements;
> - the Council will promote, as may be appropriate, the Homeworkers Code of Practice; and
> - a mandatory code of practice in Victoria with respect to outworkers can only be made under the Act if it is considered that current self-regulatory mechanisms are inadequate to achieve improvements in the level of compliance or that persons in the industry are not attempting in good faith to negotiate improvements or extensions to those voluntary self-regulatory mechanisms. (sub. PP173, p. 10)

Also, in Queensland and South Australia there is similar industrial relations legislation that deems outworkers to be employees.

In contrast, proposed Commonwealth legislation, the Workplace Relations Amendment (Improved Protection for Victorian Workers) Bill 2002, sought to preserve the status of those outworkers not covered by federal awards or agreements as contractors. (Victoria's industrial jurisdiction was transferred to the Commonwealth by agreement in 1996.) Among a range of measures, the Bill would provide for minimum rates of pay for TCF contract outworkers equivalent to the rates of pay applicable had that work been carried out by an employee.

Other initiatives

Some State Government procurement policies specify that outworkers are not to be used in the manufacture of goods supplied to government agencies. As mentioned earlier, public awareness campaigns and 'No Sweatshop' label initiatives have also been used to promote the fair treatment of outworkers. For example, part of the New South Wales Government's Clothing Outworker Strategy involves:

- education and training to assist outworkers; and
- informing employers of their legal obligations through publications, conducting seminars and workplace visits. (sub. PP175, p. 2)

Further, retailers such as Coles Myer (sub. 95) have taken steps to reduce the risk that their buyers sourcing direct from Asia could purchase goods produced under 'exploitative' conditions. One motivation has been to avoid negative publicity which has affected some high profile global companies in the TCF sector.

A more recent approach has involved Nike signing an ethical clothing deed with the TCFUA to ensure that the company's suppliers comply with legislated requirements. Under this deed, as part of their contract with Nike, suppliers will be required to allow the TCFUA to audit their compliance with the award.

At the international level, the ILO adopted a convention (no. 177) on homework in 1996. (Conventions provide binding legal obligations if they are ratified by a member country.) The convention requires the member country to implement a national policy to promote, as far as possible, equality of treatment between homeworkers and other wage earners, particularly in respect of minimum wage levels and working conditions.

At the vote to adopt the convention, a number of countries including Australia and New Zealand, Switzerland, Bulgaria, Malaysia and Indonesia abstained, while others including the United Kingdom and Germany voted against its adoption. At the time, the Australian Government noted that homework arrangements can provide flexibility benefits to both employees and employers and that Australia already had adequate policies and legislation in place to protect outworkers. Hence, it did not support the adoption of the convention and has not proposed to ratify it.

Does anything else need to be done?

Despite the industrial relations legislation and awards in place at both the State and Federal level to provide outworkers with the same minimum pay and conditions as TCF workers operating in a factory environment, concerns about the degree of compliance with these requirements are still clearly widespread.

Consequently, the focus of recent and proposed initiatives in relation to outworkers has been on improving compliance with legislated requirements relating to pay and conditions, through either:

- the use of voluntary arrangements as embodied in the Code (as favoured by retailers and manufacturers); or
- further legislation, including making the Code requirements mandatory (as favoured by the TCFUA and social welfare groups).

In the Position Paper, in comparing the two approaches, the Commission noted the argument that further legislation could be a ‘double edged’ sword in that it could force further production offshore to the detriment of the outworkers concerned.

In considering the likely magnitude of such an outcome, it is of course important to recognise the different types of production outworkers are engaged in:

- standard apparel;
- ‘high-end fashion’ garments based on very small production runs focusing on quality;
- quick response/small production run garments often to cater for late season ‘top up’ demand; and
- apparel for the open air market trade, sold in some cases by the outworkers themselves.

The degree of price sensitivity attaching to these different types of production is likely to vary. For example, at one end of the spectrum, apparel produced for the market trade is likely to be highly price sensitive owing to competition from low cost imports and retail outlets. Conversely, in the high-end fashion market, the focus is on quality, design and brand rather than price.

Discussions with clothing producers since the release of the Position Paper, indicate that a substantial number of outworkers are now engaged in the production of less price sensitive items, particularly in the quick response/low volume market segment which by its very nature is more difficult to source offshore. Consequently, concerns that more legislation to improve award compliance could simply see further large blocks of production migrate offshore may now have less force than in the past. That said, if further regulation were to be particularly intrusive, or there were heavy handed attempts to enforce regulation, there is the risk that retailers might simply vacate the markets concerned, or invest to establish air freight alternatives for their quick response requirements. In these circumstances, job opportunities for outworkers would be lost.

The Commission also notes that the regulatory and voluntary approaches to encouraging compliance with award requirements applying to outworkers are not necessarily mutually exclusive. At present, in the two main TCF producing States, compliance with the voluntary Homeworkers Code is underpinned by the ‘threat’ of mandatory regulation. That is, the current arrangements in New South Wales and Victoria place the industry on notice to improve compliance with the existing requirements or have mandatory regulations introduced.

In the Commission's view, the threat of more regulation should provide a strong incentive for TCF retailers and suppliers to comply with the Code requirements. Indeed, this threat may well have been a factor explaining the recent large increase in signatories to the Code.

Further, given the nature of outwork and the supply chains involved, promoting compliance with award requirements will clearly require a considerable degree of cooperation between retailers, suppliers, their contractors and the unions. The implementation of more regulation, or heavy handed attempts to enforce regulation, could undermine such cooperation and in so doing reduce rather than increase compliance. In this regard, several participants indicated that were further regulations to be introduced, suppliers and retailers would seek to reduce their risk of exposure to any fines and penalties by devolving as much responsibility for ensuring compliance as legally possible down the supply chain. For these reasons, the Commission considers that to move quickly to legislate the Code requirements would be an unnecessary and possibly counterproductive step. Indeed, legislation itself is unlikely to ensure compliance without an extensive and potentially costly enforcement regime.

In encouraging compliance with the requirements of awards and the Code, there is also an educative role for governments, employer and community groups, industry associations and trade unions. This role could variously involve dissemination of information on legal responsibilities, encouraging members to sign up to the Code and outlining the virtues of good employment practices to the sector's future. In the end, negative perceptions concerning the treatment of outworkers are unlikely to assist in the development of an internationally competitive TCF sector. Nor will they motivate Australian consumers to purchase locally made products in preference to those manufactured offshore.

FINDINGS ON OUTWORKERS

- *The flexibility provided to manufacturers by the use of outworkers can assist them in responding more effectively and efficiently to the needs of their customers. For some outworkers, there are advantages from being able to combine paid employment with family and other responsibilities.*
- *While it is difficult to ascertain the number of people periodically engaged in outwork, the full-time equivalent number of outworkers in Australia is unlikely to be much above 25 000. Nonetheless, with the decline in factory based employment in the TCF sector over the past few years, outworker employment is*

now about 40 per cent of total factory based employment in the sector and exceeds factory based clothing employment by about 25 per cent.

- *Concerns about the exploitation of outworkers appear to have more to do with the levels of compliance with legislated requirements than with the provisions of those requirements.*
- *Given the nature of outwork and the supply chain involved, achieving greater compliance will inevitably require cooperation between retailers, suppliers, their contractors and unions. More regulation, or heavy handed attempts to enforce regulation, could undermine the increasing degree of cooperation now emerging under the voluntary Homeworkers Code of Practice and therefore be counterproductive.*
- *Governments, employer and community groups, industry associations and trade unions have a role to play in promoting compliance with awards and the Code, and the contribution that good employment practices more generally can make to the sector's future prospects.*

11 Other issues

Addressing the range of other weaknesses and impediments identified in chapter 3 would also help the textiles, clothing, footwear and leather (TCF) sector to become more internationally competitive. In many instances, action to address these weaknesses and impediments is largely in the hands of the industry. In some cases, however, changes in government policy settings are needed.

11.1 Microeconomic reform and taxes and charges

During this inquiry there were relatively few concerns raised by participants about the costs and reliability of infrastructure services. This may be because microeconomic reform initiatives in recent years have increased the efficiency of service provision in many of these areas.

It is important to note that not all microeconomic reforms that benefit the economy will benefit the TCF sector. In some cases, by removing cross subsidies and other distortions, the cost of infrastructure services may have increased for some users. However, this is not to deny the need for governments to continue to push ahead with microeconomic reform. Inefficiencies in service delivery are still a concern for some TCF firms (see box 11.1) and a constraint on improvements in international competitiveness across the economy in general.

Similarly, there is a need to ensure that taxation arrangements are appropriate and efficient. Participants in this inquiry drew attention to various taxes and charges which they claim disadvantage them vis a vis overseas competitors, making it more difficult for them to make the transition to a lower assistance environment.

The Tariff Concession System

The Tariff Concession System (TCS) incorporates a 3 per cent duty on business inputs which before 1996 had been duty free. As it only applies to goods for which close substitutes are not produced in Australia, it provides no protection to local production and is just a revenue tax on imports.

Box 11.1 Some concerns relating to infrastructure service provision

Defab Weavers said:

> Power costs are increasing each year that is taking away the energy advantage we have enjoyed over major textile nations. (sub. 65, p. 6)

The Technical Textiles and Nonwoven Association noted:

> The Australian technical and nonwoven textile industry is a considerable user of infrastructure inputs including electricity, gas, telecommunications, road, rail and air and sea freight.
>
> By and large, these services have undergone many changes in structure, ownership and the way by which they do business over the last decade. While some cost savings were delivered, regional enterprises, particularly in Albury have reported paying more per unit than what is charged in the metropolitan areas. (sub. 68, p. 18)

Genevieve Yarn Dyers said that because of peak pricing structures for setting electricity charges:

> We're paying for energy that we're not using. (trans., p. 119)

The Carpet Institute of Australia commented:

> There is a strong perception in the carpet industry that the micro-economic reform program has failed to deliver a significant improvement in the cost structures facing the carpet industry. (sub. 35, p. 19)

While it raises only a modest amount of revenue for the Government — less than $200 million a year — it does put particular manufacturers at a competitive disadvantage in relation to their overseas competitors. Indeed, it is partly because of the existence of this impost that the Commission has suggested that the TCF policy by-laws remain in place.

In its Review of the General Tariff Arrangements, the Commission (PC 2000) recommended that the concessional rate for business inputs be reduced to zero. No evidence has come to light in this inquiry that would invalidate this position — a position that was widely supported by inquiry participants.

FINDING ON THE TCS DUTY

- *The 3 per cent revenue duty imposed under the Tariff Concession System continues to disadvantage Australian manufacturers — including TCF firms — and imposes unnecessary costs on their customers.*

Payroll tax

Many participants alluded to the impact of payroll tax levied by State and Territory Governments on firms' costs and hence their competitiveness against imports.

Synthesising these concerns, the Carpet Institute of Australia said that payroll tax acts:

> … as an employment disincentive and increas[es] the cost of doing business. (sub. 35, p. 28)

On initial examination, a tax on labour that reinforces inherent labour cost disadvantages is unhelpful to the sector. This led the Footwear Manufacturers Association of Australia (sub. PP132, p. 5), amongst others, to request that compensation for payroll tax liabilities be provided from the SIP funding pool.

However, assessment of the efficacy of payroll tax on the TCF sector and efficiency more generally must have regard to a range other considerations. For example:

- in broad terms, payroll tax is more fiscally efficient than many narrowly based taxes used by State Governments;
- many of the adverse efficiency impacts of the tax are a result of the thresholds and rules that vary between States and the drawbacks and special exemptions provided by State and Territory Governments (see box 11.2);
- yet these same threshold exemptions for small business benefit many small TCF firms which could be disadvantaged if payroll tax were replaced by an alternative tax instrument.

Box 11.2 **Is payroll tax a good way to raise revenue?**

In 1999-00, payroll tax accounted for around 20 per cent of State and Territory taxation revenue (taxes on property accounted for nearly 40 per cent) (ABS Cat. no. 5506.0). While a major source of revenue, its revenue raising capacity is diminished by thresholds applied partly to minimise administration/compliance costs, but also to assist small business. In addition, State Governments have frequently granted exemptions for companies with larger payrolls in order to attract or retain investment and employment.

A Productivity Commission staff research paper by Gabbitas and Eldridge (1998), found that the revenue forgone from such exemptions was just under half the total annual revenue collected from payroll tax, indicating that there was scope to improve efficiency by broadening the base and lowering the tax rate. The study also suggested that more harmonisation of payroll tax schemes between States (uniform definitions and exemptions) would lower compliance costs.

Similarly, a report by Econtech (1998) suggested that the replacement of payroll tax by a broad based consumption tax would increase employment in the short to medium term and, in the long run, reduce the cost to the community of raising the revenue involved by around $600 million a year.

Moreover, while there may be more efficient ways to raise revenue currently collected as payroll tax, it would be inappropriate for this inquiry to propose any specific changes. Any assessment of proposals for change would need to have regard to the effects across the whole of the community, not just the TCF sector, of replacing payroll tax with an alternative revenue raising instrument or reducing government expenditures in line with the revenue shortfall.

FINDING ON PAYROLL TAX

- *As currently implemented, payroll tax has significant deficiencies. However, an assessment of possible changes to address those deficiencies, or of the case for abolishing payroll tax, would need to be judged in terms of the community-wide impacts, not just the benefits for some TCF producers. The efficiency of replacement revenue raising instruments, and/or the consequences of reducing government expenditures, would be important considerations in assessing the community-wide outcome.*

Workers compensation and other levies

Some firms raised concerns about workers compensation arrangements, including:

- the cost of premiums and their impact on international competitiveness;
- the inability of firms to influence premiums through their own actions; and
- the complexity of the arrangements.

For example, Genevieve Yarn Dyers commented:

> One of our biggest expenses in textiles is WorkCover. Now, we understand that textiles is very high labour, very intensive and there are a lot of back injuries and other injuries so we can expect a high level of WorkCover costs, but what the government doesn't differentiate [in setting premiums] is between the white collar side of the company and shop floor side. (trans., p. 118)

Workers compensation provisions are complex and subject to frequent changes. There are different schemes in each State and Territory as well as Commonwealth arrangements.

In a separate terms of reference, the Commission has been directed to undertake a review of national frameworks for workers compensation and occupational health and safety. Given that workers compensation arrangements, like payroll tax, impact on all sectors of the economy, not just TCF, this broader review is the most appropriate forum to discuss the sort of concerns outlined above. The Commission has therefore passed on submissions to this inquiry dealing with workers compensation issues to the concurrent review. The Commission intends to release an interim report, including preliminary proposals, for that review in September 2003.

Other cost imposts raised by TCF firms included, maternity leave, penalty rates of pay and various levies imposed by Commonwealth and State Governments. Again, however, these costs are not unique to the TCF sector, being general features of Australia's business environment.

11.2 Facilitating market access

While some progress has been made in reducing the barriers faced by Australian TCF exporters, significant tariff and non-tariff barriers still remain (see chapter 3 and appendix D). These were of considerable concern to many inquiry participants.

Making Australia's assistance policies conditional on what other countries do would not be in Australia's best interests (see chapter 6). Many of the gains from trade liberalisation come from changes induced in the domestic economy that are largely independent of other countries' actions. Moreover, Australia's assistance regime in general, and for the TCF sector in particular, is unlikely to provide any real bargaining coin in international trade negotiations. This is because the Australian market is small, imports already account for over half of the local market and protection on most TCF products is already relatively low.

However, this is not to deny that improved market access could assist some firms to compete successfully in the international marketplace with little or no government support. Indeed, for leading edge Australian TCF firms, barriers to entry in overseas markets will often be a significant constraint on growth. Accordingly, continuing endeavours by Australian Governments to achieve better market access for TCF (and other Australian) exporters are very important (see chapter 3).

In this regard, many in the TCF sector have focused on the role of bilateral agreements, including those with the United States and Thailand. Some studies suggest that depending on their coverage and detailed rules, these agreements could provide significant benefits to Australian TCF firms and the economy more generally (see appendix D).

However, a policy emphasis on bilateral agreements at the expense of continued efforts in multi-country forums such as the WTO and APEC would raise a number of concerns. For example:

- In contrast to multilateral tariff reductions, the overall benefit to participating countries in bilateral arrangements depends on the extent to which they create additional trade, as distinct from merely diverting it from other countries.

- A proliferation of bilateral arrangements could result in a 'spaghetti bowl' of trade rules covering things such as rules of origin, resulting in significant administrative and compliance costs. Yet as TCF interests in this inquiry have pointed out, those rules will be crucial to the outcomes for Australia and specific sectors such as TCF.

Also, even though a particular arrangement may be beneficial to a country as a whole, suppliers in particular industries may be disadvantaged. For example, in a TCF context, the prospective free trade agreement with the United States might see Australian carpet producers facing much greater import competition given that the United States is by far the largest producer of synthetic floor covering in the world.

The implication of the preceding discussion is that bilateral agreements are unlikely to be a panacea for improving market access generally or in particular sectors, and should not reduce the emphasis given to securing better access through the more broadly-based multilateral arrangements.

FINDINGS ON MARKET ACCESS

- *Some progress has been made in reducing trade barriers faced by Australia's TCF exporters, but widespread barriers still remain. While Australia's tariff levels should not be tied to assistance levels in other countries, Australian Governments must continue to pursue improved market access for TCF and other sectors in multilateral, regional and bilateral forums.*
- *However, the benefits for Australia from bilateral trade agreements will depend crucially on their coverage and detailed rules. Such agreements are unlikely to be a panacea for market access problems — either generally or in particular sectors — and should not reduce the emphasis given to securing better access through more broadly-based multilateral arrangements.*

11.3 Dumping

'Dumping' (defined as the sale of exported goods at below the price they sell for in their country of origin) has always been a contentious issue. Such practices can cause damage to competing local producers in the export markets concerned. However, there are a whole range of commercial reasons why producers might choose to sell at lower prices in export markets, for example, quitting excess stock, filling capacity and developing new markets. Hence, distinguishing between normal competitive pricing behaviour and intentional predatory behaviour designed to damage local competitors is very difficult. Also, consumers and user industries will benefit from lower prices.

WTO rules do not prohibit 'dumping', but focus on how governments can or cannot react to it . In effect, these rules discipline anti-dumping actions, and are contained in what is commonly referred to as the "Anti-Dumping Agreement". In the absence of such rules, competitive overseas suppliers could be unreasonably subject to anti-dumping duties.

The legal definitions are more precise, but broadly speaking the WTO agreement allows governments to act against 'dumping' where there is genuine ('material') injury to the competing local industry. In order to take action, the government has to be able to show that 'dumping' is taking place, calculate the extent of 'dumping' (how much lower the export price is compared to the exporter's home market price) and show that the dumping is causing injury. This is a complex and data intensive exercise.

Few anti-dumping actions have been initiated by the Australian TCF sector

According to the Global Trade Protection Report, on a global basis the TCF industries accounted for 10 per cent of all anti-dumping cases initiated in 2001 (sub. 33). In contrast, in Australia, the TCF sector has accounted for only 5 per cent of all cases initiated in the last 5 years and there have been no cases in this sector since 1998-99 (PC 2002c). Consequently, as at February 2003, there were no anti-dumping measures in place against TCF imports into Australia (ACS 2003a).

Disincentives for the TCF industries to take anti-dumping action

However, this does not mean that 'dumping' is not a problem for the Australian TCF sector. Taking anti-dumping action can be costly, time consuming and uncertain in outcomes because it is often difficult to determine if 'actionable' dumping has occurred. For example, in taking action against least developed countries or countries with state-owned enterprises, it can be very difficult to determine the cost structure of the product allegedly dumped. Charles Parsons and Co. commented:

> Anti-dumping can be an effective tool but it is rarely used within TCF as target countries are those with 'economies in transition' where normal values and standard costs are not known. (sub. 26, p. 9).

Also, some alleged dumping in the TCF sector is likely to be of a short term nature to dispose of excess stocks associated with fashion changes and ends of seasons. Thus, the TCFUA said:

> The TCF sector is also vulnerable in regards to fashion clothing because our season is at the tail end of the European season and it is a convenient place to off-load goods unsold overseas. (sub. 33, p. 28)

The Technical Textiles and Nonwoven Association similarly commented:

> When it's winter in the United States the factories are slow. What do they do with the product they make? They dump it. It comes pouring into Australia and into Asia … (trans., p. 360)

While such selling practices may cause damage to both local producers and other importers, several participants suggested that Australia's anti-dumping system does not provide effective remedies. For example, Standard Universal Textile Group said:

> … the Australian anti-dumping system is unable to inhibit or remedy the damage associated with one-off shipments of finished consumer items that are each individually off-loaded at opportunistic prices in Australia. (sub. 71, p. 8)

Moreover, local TCF manufacturers may be reluctant to take anti-dumping action where the importer is the retailer to whom they also supply product. The Footwear Manufacturers Association of Australia commented that:

> … Australian companies are often wary of reprisals from their customers if they lodge dumping claims, which are often the major retailers. (trans., p. 408)

Should anti-dumping arrangements be modified?

Proposed amendments to Australia's anti-dumping rules in relation to economies in transition would deal with one of the TCF sector's major concerns. These amendments will provide greater flexibility in determining 'normal value' in respect of exports from countries such as China whose economies are in transition from command to market economies, including scope to use the price of a good in a surrogate country to determine its normal value. The TFIA said that it fully supports these amendments that deal with the 'main issue' confronting TCF firms in this area (trans., p. 11)

However, a range of other possible changes to the current regime were proposed by participants most of which involved making remedies more accessible to local TCF suppliers including automatic triggers for the imposition of dumping duties (ie reversing the onus of proof). The Footwear Manufacturers' Association of Australia said:

> In order to respond quickly to dumping we believe a set of automatic triggers should be set in place and through this the Australian Customs could automatically initiate an Inquiry and an appropriate bond once the set criteria had been passed. (sub. 28, p. 20)

Similarly, Standard Universal Textile Group contended:

> … anti-dumping provisions should be set in place to automatically initiate an inquiry and apply a bond when potentially injurious shipments enter Australia. (sub. 71, p. 8)

A further proposed change was to pass on the duty raised in any countervailing action to the local supplier concerned. In this context, the TCFUA and others referred to the Byrd amendment which provides for such an arrangement in the USA (sub. 33).

The views that the regime should be strengthened are not universally accepted. For example, as the outgoing Chairman of the Australian Competition and Consumer Commission (ACCC) , Professor Allan Fels, recently remarked:

> The dumping laws … deny consumers the benefits of much fair competition from abroad. The principles of dumping law are quite incompatible with the principles that we [ACCC] apply in relation to predatory pricing. A private study commissioned by the OECD found that most cases that succeeded under dumping law because of lower prices would have failed under competition law. (Fels, 2003, p. 11)

However, whatever the merits of these very different positions, changes of the sort put forward by participants would have wide-ranging ramifications beyond the TCF sector. Accordingly, an assessment of such changes would need to be encompassed in a broad ranging review of Australia's anti-dumping arrangements.

Nonetheless, even under the existing regime, the interests of all parties would be served by ensuring that any anti-dumping actions are processed transparently and expeditiously. The Commission notes that in 2001-02, one-third of all anti-dumping investigations took longer to process than the 155 days provided for in the revised guidelines stemming from the Willett Review of anti-dumping measures (ACS 2002a). The time taken by Ministers to make decisions following an investigation can further add to these delays. Such extended time frames are unlikely to be helpful to TCF suppliers or producers in other industries.

11.4 Other matters

Relationships between suppliers and retailers

Some local TCF suppliers told the Commission that the practices of retailers are frustrating rather than helping the sector to improve its international competitiveness.

Some of these concerns reflected the perceived use by large retailers of their purchasing power to unreasonably squeeze suppliers' margins.

However, a price viewed as 'unreasonable' by a supplier may simply reflect commercial reality. Given the considerable competitive pressures on retailers to deliver value for money products to consumers and the growing availability of low cost imports, it is inevitable that many suppliers will be under pressure to constrain prices. As Coles Myer commented:

> The retail environment is intensely competitive with growing numbers of retailers of all sizes, often operating with very similar offers. Each retailer is striving to gain a greater share of the consumer's limited spend on apparel which is placing downward pressure on prices. (sub. 95, p. 1)

Moreover, the pressure on suppliers to constrain prices does not preclude constructive and effective working relationships. Indeed, the Commission met with a number of smaller suppliers who appear to have developed such a relationship with the major retailers.

A possibly more significant concern is the contention that recent purchasing decisions taken by buyers for the major retailers to source offshore had often been made purely on the basis of product price, and had not fully taken into account the supply chain management costs, which are often higher for imported products. While this contention is difficult to substantiate, purchasing decisions which ignore some supply chain costs could be inimical to the interests of both local TCF suppliers and Australian consumers. Greater cooperation and information sharing between retailers and their suppliers to ensure that sourcing decisions properly reflect all the costs involved would therefore be beneficial.

At a more specific level, previous reviews such as the TCFL Forum Strategic Plan (TCFL Forum 2002) identified scope for a more cooperative approach between suppliers and retailers in regard to the provision of logistical services by suppliers. There has been some progress made in this area with several Australian TCF producers offering retailers vendor managed inventory services (see chapter 3). The scope for such arrangements is increasing with IT developments in the areas of barcoding and scanning, enabling suppliers to offer a more sophisticated 'just-in-time' stock service.

Further development of these sorts of relationships and associated services will almost certainly occur as part of the evolution of the TCF sector. Indeed, it was pointed out to the Commission that retailers want and need a local TCF sector. As Coles Myer said:

> Coles Myer is the largest purchaser of local product and we would like to see a viable local industry. (sub. 95, p. 2)

FINDING ON RELATIONSHIPS BETWEEN SUPPLIERS AND RETAILERS

- *There is scope for improved cooperation and information sharing between TCF suppliers and major retailers to help optimise the means of providing Australian* *consumers with TCF products at the lowest overall costs (including all supply chain costs).*

Environmental legislation

As discussed in chapter 3, increasingly stringent environmental regulation is one of the variety of pressures helping to reshape the TCF industries globally. For some local TCF producers, this will be a new source of opportunity. For example, the Technical Textiles and Nonwovens Association (sub. 68) noted that stringent controls to promote better environmental outcomes more generally are increasing the demand for technical textiles.

In other cases, however, more stringent environmental regulation may adversely impact on the competitiveness of TCF firms. For example, the costs imposed on Australian tanning and dyeing operations by effluent disposal regulations are apparently in the order of $3 to $5 per hide, compared to only $1 per hide in China. Also, Australia's site rehabilitation requirements may be costly and inhibit the exit of some non-viable firms from the sector.

The fact that such costs are higher in Australia than in some other countries does not of itself indicate that there is a problem. Environmental regulation has to balance many interests that extend well beyond the compliance costs for firms. While those costs may make it more difficult for Australian producers to compete against countries with lower standards, relaxing those regulations could impose significant environmental and clean-up costs on the wider community and may not be acceptable. Also, while Australia may have more stringent environmental regulations than many developing countries, the Australian regime is apparently less stringent than in some other developed countries.

That said, it is important that procedures for determining regulations are transparent, provide scope for input from all affected parties and are administratively efficient.

The issue of procedural efficiency is particularly germane to another environmental issue drawn to the Commission's attention in this inquiry. Several participants told the Commission that complying with Australia's NICNAS (National Industrial Chemicals Notification and Assessment Scheme) has delayed firms' access to chemicals used by their overseas competitors, even though those chemicals have undergone testing in countries (such as Germany) which have equally stringent environmental regulation. In commenting on the associated cost implications, Genevieve Yarn Dyers said that this means:

… [a firm has] to spend $75 000 or whatever it costs to get a product into this country, when all the work's been done in Europe or America where it's manufactured. (trans., p. 119)

In the Commission's view, requirements for the retesting of chemicals that have already been demonstrated to be safe are inefficient and conflict with the thrust of standards reform in Australia. An important element of those reforms has been mutual recognition of compliance with like standards across jurisdictions. Consistent with this approach, proof of safety for new industrial chemicals which have been certified as safe in other developed countries, would seemingly only be warranted if the regulator can demonstrate both that a particular chemical is 'high risk' and that specific circumstances in Australia make retesting essential.

FINDING ON THE TESTING OF NEW INDUSTRIAL CHEMICALS

- *The application of 'proof-of-safety' requirements (NICNAS) for new industrial chemicals which have been certified as safe in other developed countries would only be warranted if the regulator can demonstrate both that a particular chemical is 'high risk' and that specific circumstances in Australia make re-testing essential.*

A Inquiry processes and information sources

Because of the relatively short reporting period for the inquiry, the Commission streamlined its inquiry processes. Among other things, it:

- sought information on key issues using a list of questions circulated to inquiry participants rather than through a detailed Issues Paper;
- produced a Position Paper, rather than a full Draft Report, concentrating on preliminary options for post 2005 assistance for the TCF sector — the principle focus of the inquiry; and
- elected not to hold public hearings prior to releasing the Position Paper. In preparing that paper, it relied on information gained from an extensive program of industry visits, written submissions and a number of recent reports on the Australian TCF sector (see below).

Discussions with interested parties

Over the period November 2002 to March 2003 the Commission met with more than 70 interested parties. They are listed below.

Submissions

At the outset of the inquiry, the Commission indicated that it was seeking written submissions on the matters under reference. Prior to the release of the Position Paper, the Commission received nearly 100 submissions. More than 80 additional submissions commenting on the analysis and preliminary findings in the Position Paper were subsequently received. A full listing of those who made submissions to the inquiry is provided below.

Public hearings

To elicit views on the Position Paper, the Commission held public hearings in Melbourne on 3 and 4 June, in Geelong on 5 June, and in Sydney on 12 and 13 June. Some 35 entities participated in discussions with the Commission at those hearings. They are listed below.

Consultancies

The Commission engaged three organisations — the Centre of Policy Studies, Econtech and the Centre for International Economics — to provide quantitative modelling services to the inquiry (see appendix E). The contracts for these consultancies, 'stylised' modelling scenarios and the modelling reports were posted on the inquiry website.

Modelling workshop

A workshop to discuss preliminary results from some of the modelling studies available to the inquiry was held in Canberra on 20 March 2003. As well as the modellers, representatives from the TCF industries, unions, government and academia attended the workshop. The Commission placed a summary of the workshop proceedings and final versions of the papers presented on the inquiry website.

However, some modelling work undertaken for inquiry participants after the release of the Position Paper was not discussed at the workshop. The limited explanation and details provided for some of the results provided to the Commission made it difficult to reconcile all of them with related results in the studies which were exposed to scrutiny at the workshop (see chapter 6 and appendix E).

Previous reports

Since the 1997 review of the TCF sector by the Industry Commission, there have been several reports looking at the sector and its prospects, and at related government policy settings. These reports include:

- an action agenda for the textile, clothing, footwear and leather industries prepared by the TCFL Action Agenda Advisory Board (2000);
- a strategic plan for the industries arising from this action agenda, prepared by the TCFL Forum (2002);
- two reports prepared for the TCFL Forum on overseas market access issues (TFIA 2002a, Werner International 2003);
- the Victorian Government's (2000) strategic audit of that State's textile, clothing, footwear and leather industries;
- the ensuing Victorian Government (2002) plan for the industries; and
- the review by the Commonwealth Department of Industry, Tourism and Resources (2002) of the TCF Strategic Investment Program.

While inquiry participants have questioned aspects of some of these reports, the information they contain assisted the Commission to identify and analyse matters germane to its terms of reference.

A.1 List of meetings with interested parties

Industry associations and groups

Australian Association of Leather Industries
Australian Business Limited
Australian Industry Group
Australian Retailers Association
Australian Wool Industries Secretariat/Australian Wool Processors Council
Carpet Institute of Australia
Council of Textile and Fashion Industries of Australia
Footwear Manufacturers' Association of Australia
Furnishing Industry Association of Australia
Technical Textiles and Nonwoven Association
Victorian Wool Processors

Labour associations

Textile Clothing and Footwear Union of Australia

TCF suppliers

Auspac
Austanners (Vic)
Australian Country Spinners
Australian Defence Apparel
Australian Weaving Mills
Bekaert (Australia)
Berkeley Apparel
Billabong (by phone conference)
Bisconte Leather
Bradmill Textiles
Brooks
Bruck Textiles
Canningvale Towels (by phone conference)
Dowd Corporation
DPK Australia
Driza-Bone
DR Manufacturing
Feltex Carpets
Figleaf Clothing
Gale Pacific
Geofabrics Australasia
Godfrey Hirst Australia
Harold Boot Company
Howe Leather
J. Robins and Sons
Kimberly Clark
Lisa Barron Fashion Design
Logan Textiles
Macquarie Textiles
Neat n' Trim Uniforms
New Balance Australia
Norman Ritchie Textile Group
Pacific Brands
R.M. Williams
Rocklea Spinning Mills
S & R Fashions
Standard Universal Textile Group
Textor

Ulster Tascot Carpets
Victorian Hide & Skin Producers
Wild Card
Yakka

Commonwealth Government

AusIndustry
Department of Employment and Workplace Relations
Department of Foreign Affairs and Trade
Department of Industry, Tourism and Resources

State Governments

New South Wales Government (Cabinet Office, Departments of Industrial Relations, State and Regional Development)
Queensland Government (Departments of Industrial Relations, Employment and Training)
South Australian Government (Departments of Premier and Cabinet, Industry and Trade)
Tasmanian Government (Department of Economic and State Development)
Victorian Government (Departments of Industry and Regional Development, Premier and Cabinet, Treasury and Finance)

Local Government and regional associations

Geelong Council
Geelong Textile Network
Wangaratta Chamber of Commerce and Industry
Wangaratta Council

Other

Coles Myer
Kreitals Consulting Group
Logistinet
Mr Peter Morgan, Chairman TCFL Forum
Ms Sally Weller
TCF Services

A.2 Modelling workshop participants

Access Economics
ACIL Tasman
Australian Business Limited
Centre for International Economics
Centre for Sustainable Regional Communities
Centre of Policy Studies
Council of Textile & Fashion Industries of Australia
Department of Industry and Regional Development (Vic)

Department of Industry, Tourism and Resources
Department of Treasury and Finance (Vic)
Econtech
Kreitals Consulting Group
Textile, Clothing and Footwear Union of Australia
Wangaratta Council

A.3 Public hearing participants

Melbourne, 3 June 2003

Council of Textile and Fashion Industries of Australia
Godfrey Hirst
Textile, Clothing and Footwear Union of Australia
Australian Dyeing Company
Australian Defence Apparel
Yakka
Carpet Institute of Australia
Furnishing Industry Association of Australia

Melbourne, 4 June 2003

NIETL/Northlink
Flickers Australia
City of Whittlesea
Harold Boot Co
Australian Industry Group
Textor
Moreland City Council
Feltex Australia

Geelong, 5 June 2003

City of Greater Geelong
Geelong Manufacturing Council/Geelong Textile Network
Ian Trezise MLA, Member for Geelong
Textile, Clothing and Footwear Union of Australia
City of Ballarat
Geelong and Region Trades and Labour Council
Geelong West Branch of the ALP
Geelong Chamber of Commerce
TCF Resource Centre of Western Australia
Victorian Farmers' Federation
Australian Wool Processors Council
Western Region Councils Forum

Sydney, 12 June 2003
Bruck Textiles
Albany International
Technical Textiles and Nonwoven Association
Geofabrics Australasia
Pacific Brands
Footwear Manufacturers' Association of Australia
Sporting Footwear Importers Group
Australian Council of Trade Unions
Australian Fashion Innovators

Sydney, 13 June 2003
Australian Business Limited

A.4 List of submissions

Note: 'PP' indicates submission was received after the Position Paper was finalised.

Name	***Sub. No.***
A Linear Bridal	58
A.I. Topper & Co Pty Ltd	38
Albany International Pty Ltd	49, PP142
Anderson, Mr John	PP145
Austanners (Vic) Pty Ltd	73
Austrade	85
Australian Association of Leather Industries	32, PP161
Australian Business Limited	98, PP181
Australian Chamber of Commerce and Industry	PP147
Australian Council of Trade Unions	92, PP169
Australian Defence Apparel	24, PP130
Australian Dyeing Company	1, PP106, PP121, PP137
Australian Fashion Innovators	PP 144
Australian Industry Group	11, PP140
Australian Manufacturing Workers' Union	9
Australian Weaving Mills	67, PP163
Australian Wool Innovation Limited	PP158
Australian Wool Processors Council Inc	45, PP127
Banyule City Council	PP170
Berkeley Apparel Pty Ltd	50
Bradsal	90

Name	*Sub. No.*
Brotherhood of St. Laurence	74
Bruck Textiles	55, PP109, PP165
Carpet Institute of Australia Limited	35, PP126, PP162
Casaveen Knitwear	6
Centre For Sustainable Regional Communities (La Trobe University)	PP 149
Charles Parsons & Co.	26
City of Ballarat	14, PP112
City of Darebin	25, PP 151
City of Greater Bendigo	PP150
City of Greater Geelong	16, PP118
City of Whittlesea	PP102, PP115
Colbeck, Senator Richard	61, PP166
Coles Myer	95, PP143
Coronet	10
Council of Textile & Fashion Industries of Australia Ltd	75, 97, PP100, PP164
Cregan, Ms Christina	30
CSIRO - Textile and Fibre Technology	52
Defab Weavers	65
Department of Agriculture Fisheries & Forestry	PP176
Department of Employment and Workplace Relations	84, PP131
Department of Industry and Resources (WA)	PP179
Done Art and Design	93
DR Manufacturing	57, PP146
Draggin' Jeans Pty Ltd	17
Enterprise Skills	29
Envitan Consultancy — Tannery, Technology & Environment	PP110
Fabrics Australia Inc.	70
Fashion Technicians Association of Australia	82
Feltex Australia Pty Ltd	80, PP116
Flicker's Australia Pty Ltd	63, PP168
Footwear Manufacturers' Association of Australia	28, PP132
Furnishing Industry Association of Australia Ltd	22, PP125
Furst Fashions	2
Geelong Chamber of Commerce	62, PP114, PP136
Geelong and Region Trades and Labour Council	18, PP141
Geelong Manufacturing Council and Geelong Textile Network	47, PP139

Name	*Sub. No.*
Geelong West Branch of the ALP	23
Gilmour's Pty Ltd	81
Godfrey Hirst Australia Pty Ltd	77, PP129
Hampshire, Mr Don	20
Harold Boot Company	PP124, PP157
J. Robins & Sons Pty Ltd	34
James Nelson Textiles Group	64
Job Watch Inc.	43
Koci, Mr Stephen	PP178
Labour Council of NSW	60
Light Manufacturing Industry Training Council (WA) Inc.	48
Light Manufacturing Training Australia	41
LincLab Australia	56
Longina Phillips Designs Pty Ltd	99
Macpherson, Ms Elizabeth	5
Melba Tex Pty Ltd	83
Melbourne Textiles Knitting Co.	4, 51, PP134
Mitchell Shire Council	PP 148
Moreland City Council	PP119
Municipal Association of Victoria	PP159
National Farmers Federation	PP104
National Footwear Retailers' Association Ltd	12
New South Wales Government	PP175
NIETL/North Link	96
Northern Grampians Shire Council	PP133
Pacific Brands	72, PP138
PHM (NSW) Pty Ltd	3, 15, 91
Queensland Light Manufacturing Industry Training Council Inc.	36
Rocklea Spinning Mills	44, PP108
S & R Fashions Pty Ltd	39, PP120
SHARP Dummies Pty Ltd	13, PP107, PP155
Shoe Last & Components	PP172
South Australian Government	87, PP177
South West Trades and Labour Council	19
Specialty Coatings (Aust.) Pty Ltd	79
Sporting Footwear Importers Group	27, PP122

Name	*Sub. No.*
Standard Universal Textile Group	71
SuitsU Pty Ltd	PP105
Tasmanian Government	89, PP180
TCF Council of Fiji and Fiji Ministry of Commerce, Business Development and Investment	66, 94, PP117
TCF&L Manufacturers of SA	37
TCF Resource Centre (WA)	69, PP111, PP167
TCF Services Pty Ltd	PP174
Technical Textiles and Nonwoven Association	68, PP113
Textile, Clothing and Footwear Union of Australia	33, 88, PP154
Textor Pty Ltd	76, PP135
The Textile Institute	PP153
The Uniting Church in Australia	59, PP160
Tuffa Workwear Pty Ltd	8
Ulster Tascot Carpets	53
Uniform City Pty Ltd	PP123
Victor Footwear	54, PP156
Victoria Carpet Co Pty Ltd	86
Victorian Council of Social Service	42
Victorian Farmers Federation	PP 152
Victorian Government	78, PP173
Victorian Regional Trades and Labour Councils Association	21
Victorian Trades Hall Council	40
Wangaratta Chamber of Commerce	7
Wangaratta Rural City Council	46
Wax Convertors Textiles	PP171
Wool Interiors Limited	PP101
Wool Producers	PP103
Yakka Pty Ltd	31, PP128

B Industry and workforce data

As in the rest of the report, the abbreviation TCF has been used to describe the entire textiles, clothing, footwear and leather sector. The figures presented in this appendix cover all of these segments.

B.1 Market data

Table B.1 **Industry composition — 2000-01**

Industry	*Employment at end of June*[a]	*Sales and service income*	*Industry value added (production)*
	Number	$m	$m
Wool scouring	1 792	746	172
Synthetic fibre textile mfg	2 960	602	191
Cotton textile mfg	2 172	359	112
Wool textile mfg	1 628	188	82
Textile finishing	1 215	169	73
Made-up textile product mfg	8 447	1 018	321
Textile floor covering mfg	3 307	823	227
Rope, cordage and twine mfg	407	92	27[b]
Textile product mfg n.e.c.	2 003	214	78
Hosiery mfg	2 121	277	48
Cardigan and pullover mfg	1 126	151	39
Knitting mill product mfg n.e.c.	2 246	422	124
Men’s and boys’ wear mfg	5 970	729	225
Women’s and girls’ wear mfg	7 780	1 033	251
Sleepwear, underwear and infant clothing mfg	1 384	268	74
Clothing mfg n.e.c.	5 797	581	191
Footwear mfg	4 223	558	182
Leather tanning and fur dressing	2 787	843	156
Leather and leather substitute product mfg	399	39	12
All TCF	**57 764**	**9 111**	**2 583**

[a] Includes working properties. [b] Data subject to sampling variability of between 25 per cent and 50 per cent.

Note: n.e.c means not elsewhere classified.

Source: Manufacturing Industry, Australia, 2000-01 (cat. no. 8221.0).

Table B.2 **Industry shares of sectoral employment and production, 2000-01**

	Employment	*Share of total*	*Value added*	*Share of total*
	Number	Per cent	$ million	Per cent
Textile fibre, yarn and woven fabric mfg	9 766	16.9	629.9	24.4
Textile product mfg	14 164	24.5	652.8	25.3
Knitting mills	5 493	9.5	211.0	8.2
Clothing mfg	20 931	36.2	740.4	28.7
Footwear mfg	4 223	7.3	181.7	7.0
Leather and leather product mfg	3 187	5.5	167.5	6.5
All TCF	**57 764**	**100.0**	**2 583.3**	**100.0**

Source: ABS 8221.0.

Table B.3 **TCF-related wholesaling and retailing employment, 1991-92 and 1998-99**[a]

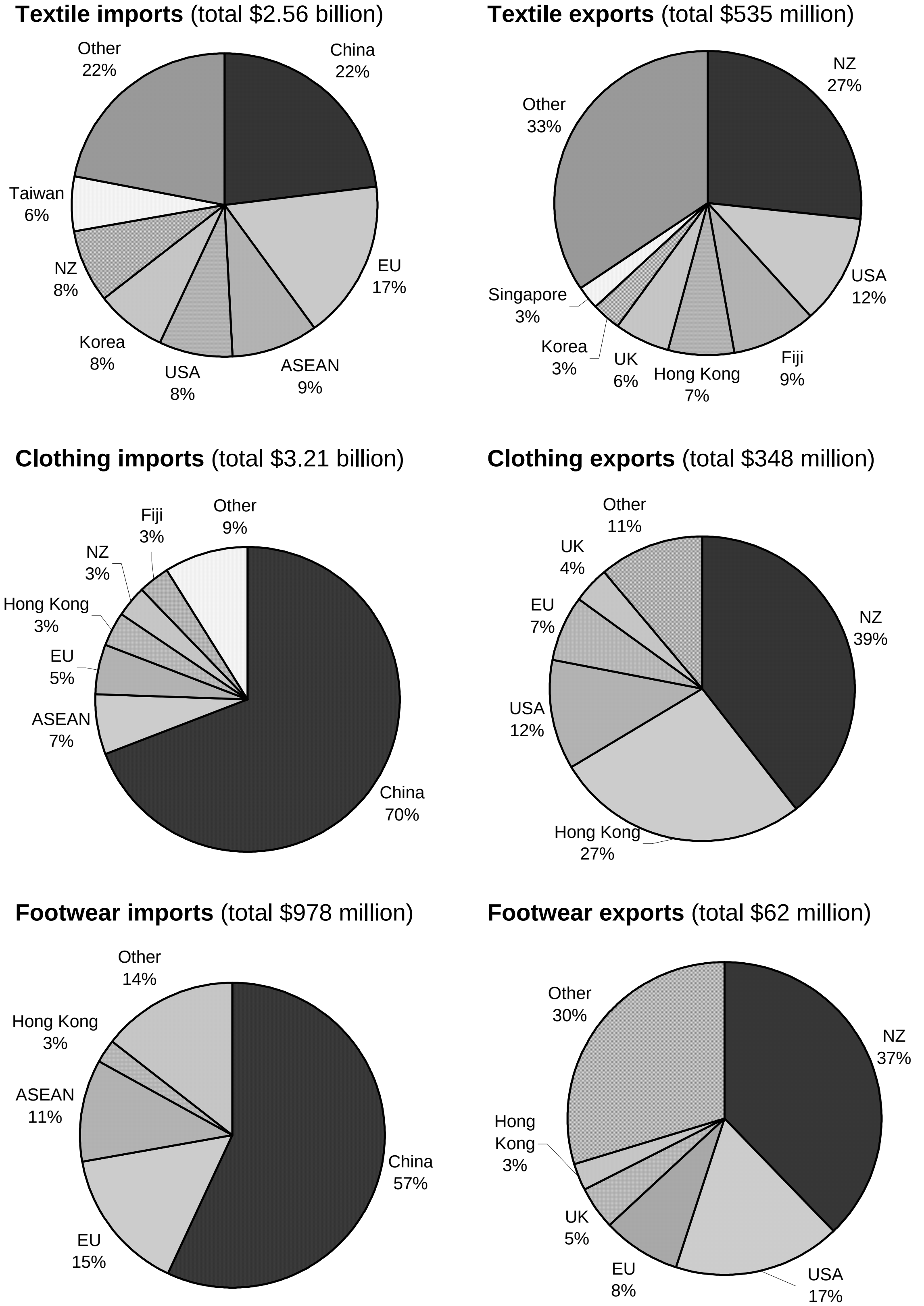
ANZSIC industry	*1991-92*	*1998-99*	*Change 1991-92 to 1998-99*
	'000	'000	%
Wholesaling			
Textile products	6.3	8.0	27.0
Clothing	7.5	11.9	58.7
Footwear	1.0	1.5	50.0
Floor coverings	1.4	1.1	-21.4
Total wholesaling	**16.2**	**22.5**	**38.9**
Retailing			
Fabrics and other soft goods	10.7	10.9	6.9
Department stores	93.5	103.1	10.3
Clothing	53.2	55.0	3.4
Footwear	11.8	13.3	12.7
Floor coverings	4.2	4.3	2.4
Total retailing	**173.4**	**186.7**	**7.7**
Total wholesaling and retailing	**189.6**	**209.2**	**10.3**

[a] Some establishments do not deal exclusively in TCF products (eg department stores).

Source: ABS (2000a, 2000b).

Figure B.1 **Australia's TCF trade by country and sub-sector, 2001-02**

Percentage shares



Data source: TFIA (2002b).

Table B.4 **Share of clothing and footwear consumption in total household consumption, 1990 to 2000**

per cent

	1990	*1995*	*2000*	*% change 1990 to 2000*
Australia	**4.9**	**4.3**	**3.8**	**-22.0**
France	6.3	5.4	4.9	-21.9
Italy	10.3	9.6	9.3	-9.8
Japan	7.5	7.1	6.0	-19.9
United Kingdom	6.3	6.3	5.8	-7.3
United States	6.8	5.5	5.3	-22.1

Source: OECD (2002).

B.2 Workforce data

This section presents data relating to the characteristics of the TCF workforce. Much of this data is drawn from the ABS Labour Force Survey or the ABS Population Census. This is mainly because they provide more detailed data on workplace characteristics than other sources of information such as the ABS Manufacturing Survey.

The Manufacturing Survey indicates that sectoral employment in the TCF sector was around 58 000 persons at June 2001, whereas the Labour Force Survey suggests a figure of around 90 000 at that time. (TCF employment as measured by the Labour Force Survey has since declined to about 68 000 (May 2003).) This difference arises from three main sources: different methodologies between collections, sampling error and changes in industry structure. In particular, the manufacturing survey data exclude sole proprietors and owner operators; and also all persons working on commission, contract or as consultants, including outworkers. In contrast, the Labour Force Survey and the Population Census data include outworkers to the extent that they identify themselves as such.

Most of the data presented in this section relate to the period from 1996-97. As far as possible, they are presented on a comparable basis to the data presented in the Industry Commission's earlier report into assistance arrangements for the TCF sector (IC 1997). However, some of the data presented in that report have since been revised by the ABS.

Table B.5 **Employed persons: May 1997 and May 2003**[a]

ANZSIC industry	*May 1997*			*May 2003*			*Change May 1997 to May 2003*		
	Male	*Female*	*Persons*	*Male*	*Female*	*Persons*	*Male*	*Female*	*Persons*
	’000	’000	’000	’000	’000	’000	%	%	%
Textile fibre, yarn and woven fabric mfg (221)	6.9	*4.7*	11.6	5.5	*1.4*	6.9	-20.2	*-70.3*	-40.5
Textile product mfg (222)	11.9	9.9	21.8	9.1	9.4	18.5	-23.5	-5.0	-15.1
Knitting mills (223)	*1.1*	*2.6*	*3.7*	*0.9*	*1.2*	*2.1*	*-18.2*	*-53.8*	*-43.2*
Clothing mfg (224)	13.1	36.5	49.6	10.4	24.4	34.8	-20.6	-33.2	-29.8
Footwear mfg (225)	*4.0*	*2.9*	6.9	*1.2*	*1.8*	3.0	*-69.9*	*-37.9*	-56.5
Leather and leather product mfg (226)	5.9	*4.2*	10.1	*2.5*	*0.6*	3.1	*-57.6*	*-85.7*	*-69.3*
All TCF (22)	**42.9**	**60.8**	**103.7**	**29.6**	**38.8**	**68.4**	**-31.0**	**-36.2**	**-34.0**
All mfg	**830.3**	**297.4**	**1 127.7**	**810.6**	**296.9**	**1 107.5**	**-2.4**	**-0.2**	**-1.8**
All industries	**4 754.3**	**3 629.0**	**8 383.3**	**5 269.7**	**4 248.9**	**9 518.6**	**10.8**	**17.1**	**13.5**

[a] See tables C.2, C.3 and C.10 in IC 1997 for earlier data.

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

Source: ABS Labour Force Survey Data.

Table B.6 **The contribution of TCF employment to overall employment, 2001[a]**

	TCF employment as a proportion of :					
	Total manufacturing employment in			*Total employment in*		
	Metro	*Other*	*Total*	*Metro*	*Other*	*Total*
	%	%	%	%	%	%
NSW	6.3	4.9	5.9	0.8	0.5	0.7
Vic	9.0	8.2	8.9	1.5	1.1	1.4
Qld	5.0	4.5	4.7	0.6	0.4	0.5
WA	5.0	2.4	4.4	0.5	0.2	0.3
SA	4.8	2.6	4.2	0.7	0.3	0.6
Tas	8.1	6.5	6.9	0.8	0.8	0.8
NT	4.5	2.7	3.9	-	-	0.2
ACT	4.0	-	4.0	-	-	0.1
Australia	**6.8**	**5.3**	**6.4**	**0.9**	**0.6**	**0.8**

a See table C.4 in IC 1997 for earlier data.

Source: ABS 2002 Census Data.

Table B.7 **Distribution of TCF employment by State, May 2003**[a]

ANZSIC industry	*NSW*	*VIC*	*QLD*	*WA*	*SA*	*TAS*	*NT*	*ACT*	*Australia*
	'000	'000	'000	'000	'000	'000	'000	'000	'000
Textile fibre, yarn and woven fabric mfg (221)	*1.9*	*2.6*	*0.8*	*0.9*	*0.5*	*0.3*	-	-	6.9
Textile product mfg (222)	*5.4*	7.0	*1.8*	*1.9*	*1.8*	*0.6*	-	*0.1*	18.5
Knitting mills (223)	-	*2.1*	-	-	-	*0.1*	-	-	*2.1*
Clothing mfg (224)	14.2	15.2	*2.6*	*1.3*	*0.8*	*0.5*	*0.1*	*0.1*	34.8
Footwear mfg (225)	*1.1*	*1.2*	*0.2*	-	*0.3*	*0.2*	-	-	*3.0*
Leather and leather product mfg (226)	*0.7*	*0.8*	*1.3*	-	*0.2*	*0.1*	-	-	*3.1*
All TCF (22)	**23.2**	**28.8**	**6.7**	**4.0**	**3.6**	**1.7**	***0.1***	***0.2***	**68.4**
All manufacturing	**344.2**	**351.4**	**181.3**	**100.5**	**96.9**	**22.8**	**3.8**	**6.7**	**1 107.5**
All industries	**3 152.1**	**2 390.4**	**1 814.9**	**972.3**	**716.5**	**206.6**	**94.5**	**171.5**	**9 518.6**
	%	%	%	%	%	%	%	%	%
Textile fibre, yarn and woven fabric mfg (221)	*27.1*	*37.1*	*11.4*	*12.9*	*7.2*	*4.3*	-	-	100.0
Textile product mfg (222)	*29.0*	37.6	*9.7*	*10.3*	*9.7*	*3.2*	-	*0.5*	100.0
Knitting mills (223)	-	*95.2*	-	-	-	*4.8*	-	-	100.0
Clothing mfg (224)	40.8	43.7	*7.5*	*3.7*	*2.3*	*1.4*	*0.3*	*0.3*	100.0
Footwear mfg (225)	*36.7*	*40.0*	*6.6*	-	*10.0*	*6.7*	-	-	100.0
Leather and leather product mfg (226)	*22.6*	*25.8*	*41.9*	-	*6.5*	*3.2*	-	-	100.0
All TCF (22)	**34.0**	**42.2**	**9.8**	**5.8**	**5.3**	**2.5**	***0.1***	**0.3**	**100.0**
All manufacturing	**31.0**	**31.7**	**16.5**	**9.1**	**8.7**	**2.1**	**0.3**	**0.6**	**100.0**
All industries	**33.1**	**25.1**	**19.1**	**10.2**	**7.5**	**2.2**	**1.0**	**1.8**	**100.0**

[a] See table C.5 in IC 1997 for earlier data.

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

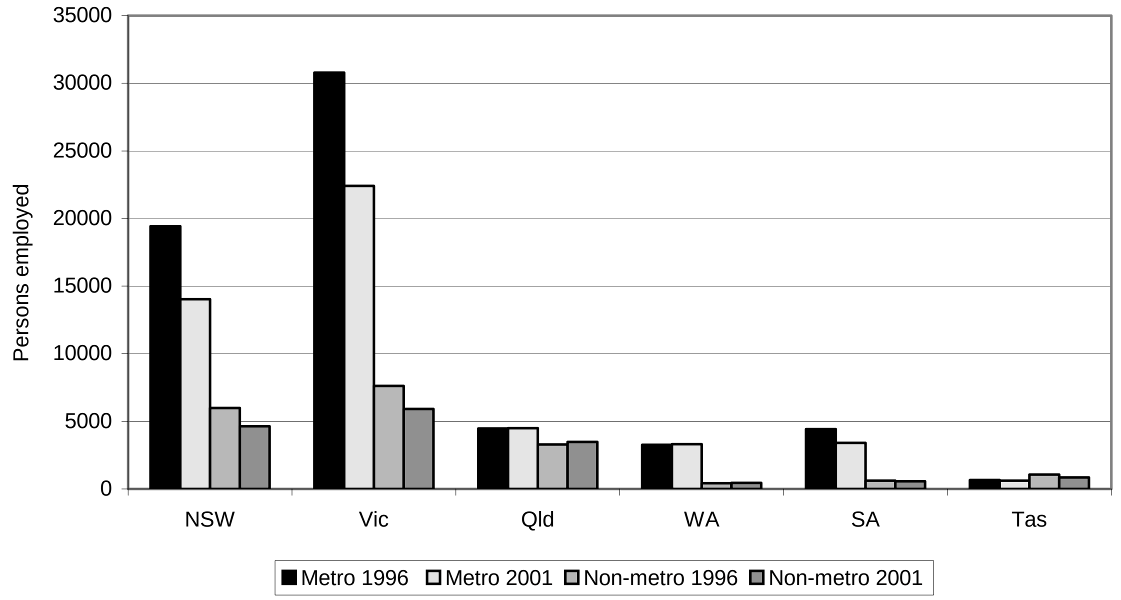
Source: ABS Labour Force Survey data.

Table B.8 **Regional distribution of TCF employment within States, 2001**

State	*Statistical Division and code*	*Main centres*	*Per cent of State TCF employment*
NSW	Sydney 105	Sydney	75.2
	Illawarra 115	Wollongong	4.6
	Hunter 110	Newcastle	4.0
	South Eastern 145	Queanbeyan, Goulburn	2.7
	Richmond-Tweed 120	Lismore, Tweed Heads	2.2
	Northern 130	Tamworth	2.2
	Other NSW		9.1
			100.0
VIC	Melbourne 205	Melbourne	79.1
	Barwon 210	Geelong	7.7
	Ovens Murray 245	Wodonga, Wangaratta	3.4
	Loddon 235	Bendigo, Castelmaine	2.6
	Other VIC		7.1
			100.0
QLD	Brisbane 305	Brisbane	56.4
	Moreton 310	Gold Coast, Sunshine Coast Ipswich	25.1
	Darling Downs 320	Toowoomba	5.0
	Wide Bay –Burnett 315	Maryborough, Bundaberg	3.8
	Other QLD		9.8
			100.0
WA	Perth 505	Perth	88.2
	South West 510	Bunbury, Busselton	4.7
	Other WA		7.1
			100.0
SA	Adelaide 405	Adelaide	85.8
	Outer Adelaide 410	Mt Barker	5.3
	South-East 425	Mt Gambier, Bordertown	4.9
	Other SA		4.0
			100.0
TAS	Greater Hobart 605	Hobart	41.8
	Mersey – Lyell 620	Burnie, Devonport	31.2
	Northern 615	Launceston	20.7
	Other TAS		6.3
			100.0

Source: ABS 2002 Census Data.

Figure B.2 **Geographical distribution of TCF manufacturing employment July 1996 and July 2001[a]**



[a] See table C.3 in IC 1997 for earlier data.

Data source: ABS 2002 and 1996 Census Data.

Table B.9 **TCF manufacturing employment by 3 digit ANZIC code as a proportion of total State TCF employment, May 2003[a]**

	Textile fibre, yarn and woven fabric mfg (221)	*Textile product mfg (222)*	*Knitting mills (223)*	*Clothing mfg (224)*	*Footwear mfg (225)*	*Leather and leather product mfg (226)*	*Total State TCF employment*
	%	%	%	%	%	%	'000
NSW	*8.2*	*23.3*	-	61.2	*4.7*	*3.0*	23.2
Vic	*9.0*	24.3	*7.3*	52.8	*4.2*	*2.8*	28.8
Qld	*11.9*	*26.9*	-	*38.8*	*3.0*	*19.4*	6.7
WA	*22.5*	*47.5*	-	*32.5*	-	-	4.0
SA	*13.9*	*50.0*	-	*22.2*	*8.3*	*5.6*	3.6
Tas	*17.6*	*35.3*	*5.9*	*29.4*	*11.8*	*5.9*	1.7
NT	-	-	-	*100.0*	-	-	*0.1*
ACT	-	*50.0*	-	*50.0*	-	-	*0.2*
Australia	**10.1**	**27.0**	***3.1***	**50.9**	***4.4***	***4.5***	**68.4**

[a] See table C.6 in IC 1997 for earlier data.

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

Source: ABS Labour Force Survey data.

Table B.10 **Part time employment, November 1997 and May 2003**

ANZSIC industry	*Part time employees as a proportion of total*	
	1997	2003
	%	%
Textile fibre, yarn and woven fabric mfg (221)	16.1	*8.7*
Textile product mfg (222)	11.2	16.8
Knitting mills (223)	*35.5*	*28.6*
Clothing mfg (224)	17.4	19.3
Footwear mfg (225)	12.1	*6.7*
Leather and leather product mfg (226)	*7.7*	*9.7*
All TCF (22)	**16.2**	**16.7**
All manufacturing	**11.0**	**11.8**
All industries	**26.0**	**28.9**

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

Source: ABS Labour Force Survey data.

Table B.11 **Age profile of employed persons, May 2003[a]**

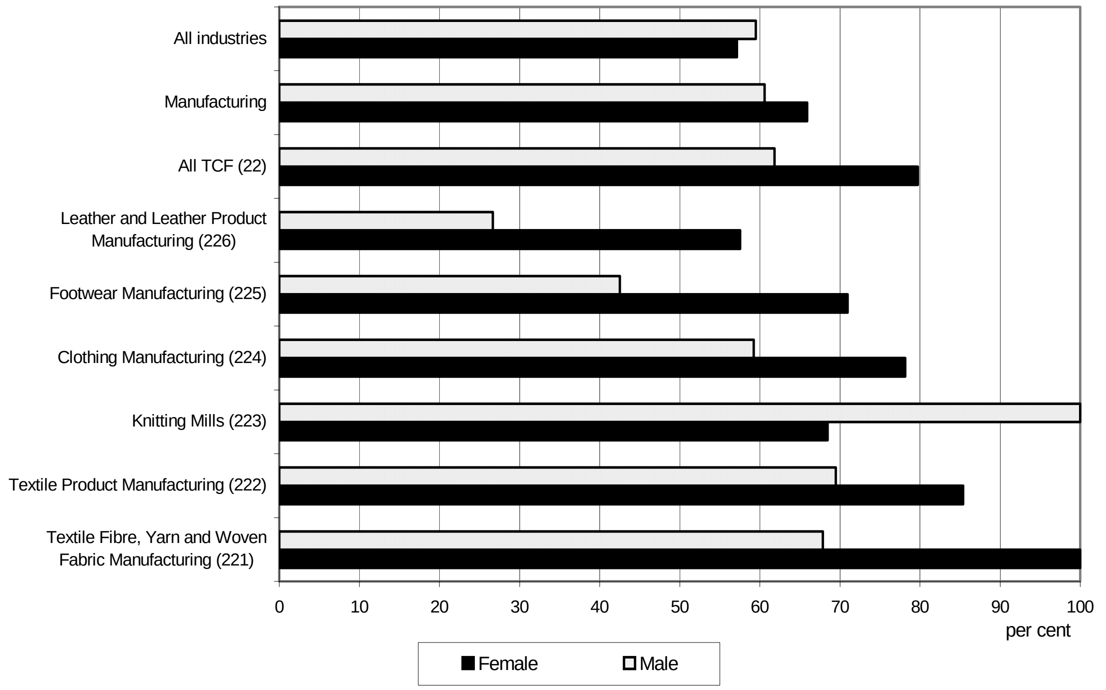
ANZSIC industry	*Employment distribution by age*				*Total employees*
	15-19	*20-34*	*35-54*	*55+*	
	%	%	%	%	'000
Textile fibre, yarn and woven fabric mfg (221)	*2.9*	*23.1*	*55.0*	*18.8*	6.9
Textile product mfg (222)	*1.1*	*21.2*	61.6	*16.2*	18.5
Knitting mills (223)	-	*19.0*	*66.6*	*14.3*	*2.1*
Clothing mfg (224)	*2.9*	24.4	58.3	14.3	34.8
Footwear mfg (225)	-	*40.4*	*43.3*	*16.7*	*3.0*
Leather and leather product mfg (226)	*12.9*	*54.8*	*32.2*	-	*3.1*
All TCF (22)	**2.6**	**25.3**	**57.3**	**14.8**	**68.4**
All manufacturing	**3.9**	**34.1**	**49.2**	**12.8**	**1 107.5**
All industries	**7.1**	**34.4**	**46.1**	**12.4**	**9 518.6**

a See table C.9 in IC 1997 for earlier data.

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

Source: ABS Labour Force Survey data.

Figure B.3 **Workforce aged 35 or more by industry, May 2003[a]**



[a] See figure C.4 in IC 1997 for earlier data.

Data source: ABS Labour Force Survey data.

Table B.12 **Employment distribution by country of birth, May 2003[a]**

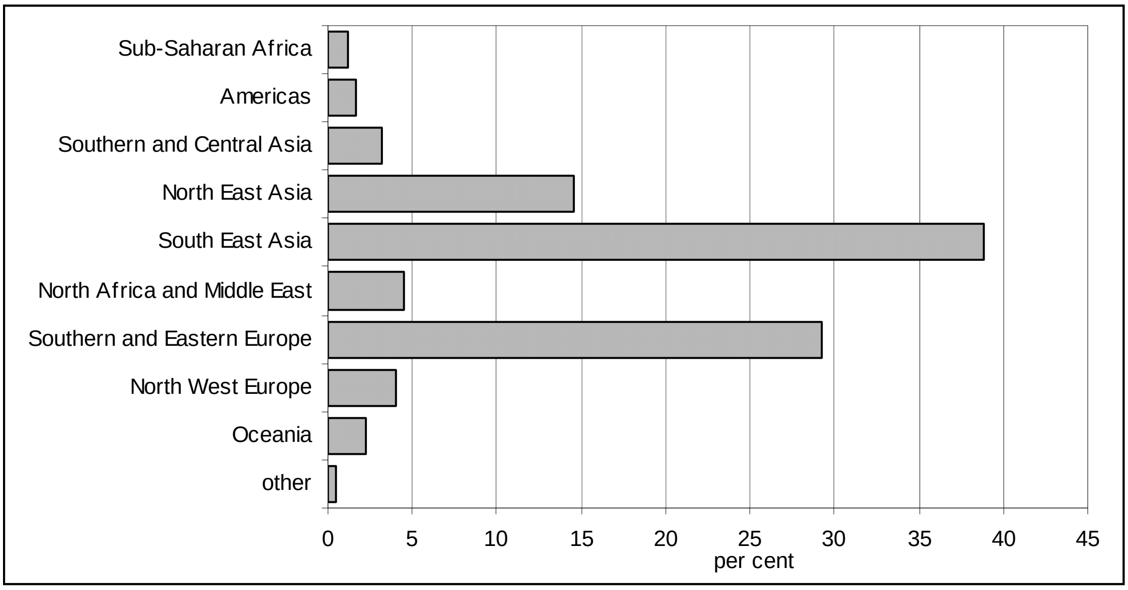
ANZSIC industry	*Australia*	*MES Country* [b]	*Other Country*	*Total Employees*
	%	%	%	'000
Textile fibre, yarn and woven fabric mfg (221)	*62.2*	*4.3*	*33.5*	6.9
Textile product mfg (222)	73.2	*4.5*	*22.3*	18.5
Knitting mills (223)	*47.0*	*13.0*	*40.0*	*2.1*
Clothing mfg (224)	38.8	*2.5*	58.7	34.8
Footwear mfg (225)	*30.9*	-	*69.1*	*3.0*
Leather and leather product mfg (226)	*78.6*	*11.5*	*9.9*	*3.1*
All TCF (22)	**52.2**	***3.8***	**43.9**	**68.4**
All manufacturing	**66.8**	**11.2**	**22.0**	**1 107.5**
All industries	**75.2**	**10.4**	**14.4**	**9 518.6**

[a] See table C.11 in IC 1997 for earlier data. [b] The ABS defines main English speaking (MES) countries as Canada, New Zealand, South Africa, United Kingdom, Ireland and the United States.

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

Source: ABS Labour Force Survey data.

Figure B.4 **Country of birth of non-MES[a] born TCF employees, 2001[b]**



[a] The ABS defines main English speaking (MES) countries as Canada, New Zealand, South Africa, United Kingdom, Ireland and the United States. [b] See figure C.5 in IC 1997 for earlier data.

Data source: ABS 2002 Census data.

Table B.13 **Marital status of TCF employees, May 2003[a]**

ANZSIC industry	*Proportion of employees who are married*		
	Male	*Female*	*Persons*
	%	%	%
Textile fibre, yarn and woven fabric mfg (221)	*69.3*	*64.2*	68.5
Textile product mfg (222)	71.0	70.2	70.8
Knitting mills (223)	*100.0*	*50.0*	*71.4*
Clothing mfg (224)	78.8	75.0	76.1
Footwear mfg (225)	*41.6*	*88.8*	*70.0*
Leather and leather product mfg (226)	*56.0*	*50.0*	*51.6*
All TCF (22)	**71.9**	**72.9**	**72.3**
All manufacturing	**68.7**	**69.5**	**69.0**
All industries	**65.2**	**62.3**	**64.0**

[a] See table C.12 in IC 1997 for earlier data.

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

Source: ABS Labour Force Survey data.

Table B.14 **Educational profile of the TCF and manufacturing workforce, May 2001 (per cent)[a]**

ANZSIC industry	*Bachelor Degree or higher*	*Skilled vocational qualification*	*No post-school qualifications*	*Did not complete highest level of schooling*
Textile, fibre, yarn and woven fabric mfg (221)	na	na	*66.3*	*32.7*
Textile products mfg (222)	*10.0*	*7.6*	62.9	45.4
Knitting mills (223)	na	na	*57.8*	*47.0*
Clothing mfg (224)	*5.6*	*4.6*	67.8	42.9
Footwear mfg (225)	na	*19.3*	*74.4*	*59.2*
Leather and leather product mfg (226)	*16.6*	na	*55.1*	40.2
All TCF (22)	**7.7**	**6.9**	**65.4**	**43.8**
All manufacturing	**11.2**	**24.5**	**49.6**	**34.4**
All industries	**20.3**	**14.7**	**44.3**	**26.6**

[a] See table C.16 in IC 1997 for earlier data. Categories are not complete nor mutually exclusive.

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

na: not available

Source: ABS 2001b (Cat. no. 6227.0).

Table B.15 **TCF employee weekly earnings and hours, May 2000**

ANZSIC industry	*Average weekly total earnings*	*Average weekly paid hours*
Textile, fibre, yarn and woven fabric manufacturing (221)	$774	42.5
Textile products manufacturing (222)	$552	35.9
Knitting mills (223)	np	np
Clothing manufacturing (224)	$485	31.0
Footwear manufacturing (225)	$480	33.0
Leather and leather product manufacturing (226	$576	38.8
All TCF (22)	$592	35.6
All manufacturing	$740	37.2

[a] See table C.18 in IC 1997 for earlier data.

np: not provided

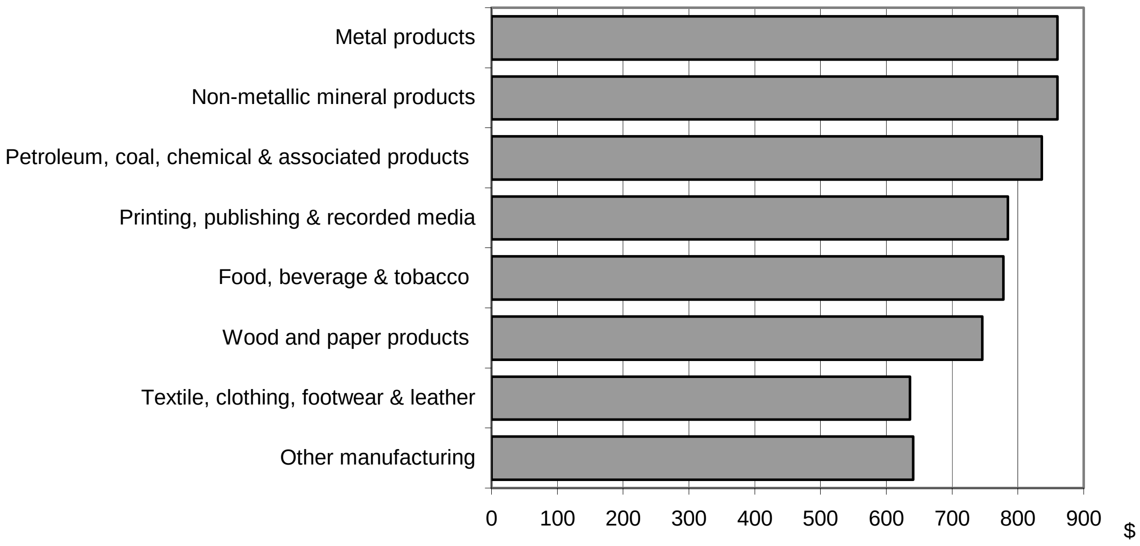
Source: ABS Employee Earnings and Hours survey.

Table B.16 **Average weekly earnings and hours, May 2002**

	Full time adult total weekly earnings	*Average hours per week*	*Average income per hour*
TCF	$670	36.47	$18.37
Manufacturing	$874	38.31	$22.82

Source: ABS Labour Force Survey and Average Weekly Earnings information.

Figure B.5 **Average weekly earnings in the manufacturing sector, May 2002**



Data source: ABS Labour Force Survey data.

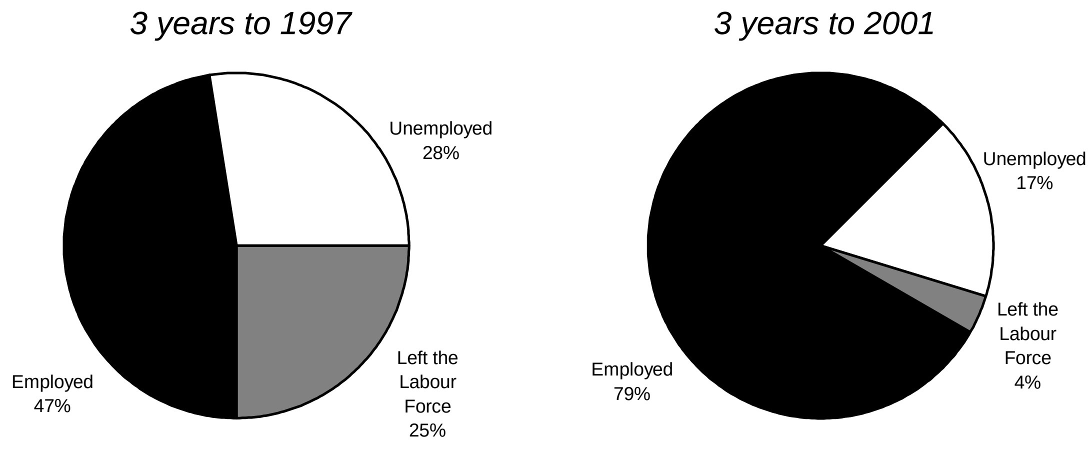
Table B.17 **Labour market experience of retrenched workers**

	3 years to June 1997			*3 years to June 2001*		
	Industry from which retrenched			*Industry from which retrenched*		
	TCF	*Mfg*	*All industries*	*TCF*	*Mfg*	*All industries*
Current labour force status	’000	’000	’000	’000	’000	’000
Employed	8.4	89.0	374.9	6.8	80.7	400.5
Unemployed	4.9	53.6	200.5	1.5	26.3	99.1
Not in the Labour Force (NILF)	4.4	24.2	110.0	0.3	15.0	96.8
Total	17. 7	166.9	685.4	8.6	122.1	596.4
Labour market outcomes	%	%	%	%	%	%
Employed	47.5	53.3	54.7	79.1	66.1	67.2
Unemployed	27.7	32.1	29.3	17.4	21.5	16.6
NILF	24.9	14.5	16.0	3.5	12.3	16.2
Unemployed or NILF	52.5	46.6	45.3	20.9	33.8	32.8
Labour Mobility	%	%	%	%	%	%
Found job in TCF	27.4	3.4	1.3	27.9	5.5	1.3
Found job in Mfg	45.2	49.3	18.2	39.7	49.7	15.4
Found job in other industries	54.8	50.7	81.8	60.3	50.4	84.6

Note: The data is drawn from surveys of workers who had been retrenched, at any stage, in the three years to June 1997 or the three years to June 2001.

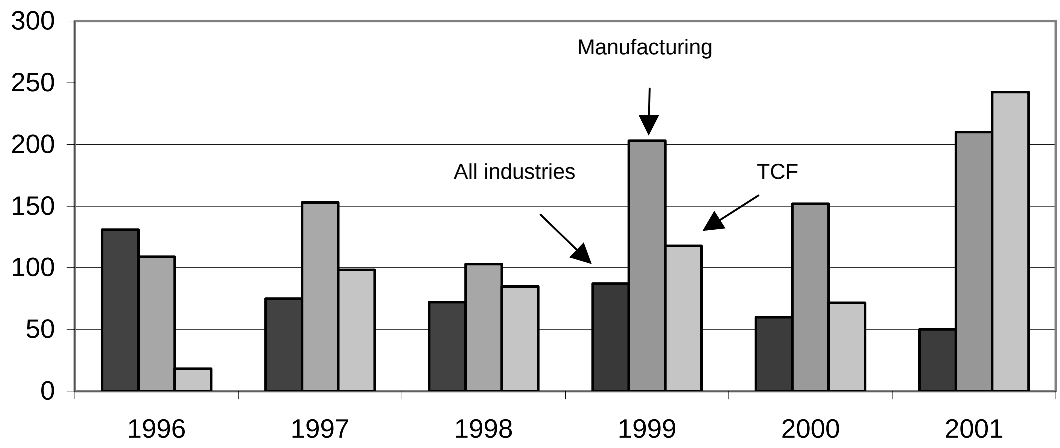
Source: Unpublished ABS *Retrenched and Redundancy* data (Cat. no. 6266.0), included in sub. 84.

Figure B.6 **Outcomes for retrenched TCF workers, 3 years to 1997 and 3 years to 2001**



Data source: Table B17.

Figure B.7 **Working days lost per thousand employees due to industrial disputes — 1996 to 2001**



Data source: DEWR.

Table B.18 **Workforce occupational composition, persons employed, August 1996 and May 2003**[a]

	All TCF				*All manufacturing*				*All industries*			
ASCO occupation (and code)	*1996*		*2003*		*1996*		*2003*		*1996*		*2003*	
	’000	%	’000	%	’000	%	’000	%	’000	%	’000	%
Managers and administrators (1)	7.8	7.4	8.0	11.6	86.5	7.7	113.4	10.2	624.1	7.5	677.7	7.1
Professionals (2)	*2.9*	*2.8*	*4.1*	*6.1*	87.2	7.8	109.8	9.9	1 389.7	16.7	1 757.7	18.5
Associate professionals (3)	*2.4*	*2.3*	*2.8*	*4.1*	55.8	5.0	60.4	5.5	867.2	10.4	1 191.7	12.5
Tradespersons and related workers (4)	18.7	17.8	9.5	13.9	291.4	26.1	283.9	25.6	1 141.2	13.7	1 220.0	12.8
Advanced clerical and service workers (5)	*3.3*	*3.1*	*1.3*	*1.9*	35.7	3.2	26.4	2.4	403.2	4.9	382.0	4.0
Intermediate clerical, sales and service workers (6)	7.8	7.4	6.1	8.8	102.7	9.2	114.6	10.3	1 394.8	16.8	1 645.2	17.3
Intermediate production and transport workers (7)	46.7	44.5	30.4	44.5	240.0	21.5	203.6	18.4	793.4	9.5	817.3	8.6
Elementary clerical, sales and service workers (8)	*2.8*	*2.7*	*2.1*	*3.0*	26.0	2.3	17.4	1.6	862.3	10.4	956.5	10.0
Labourers and related workers (9)	12.5	11.9	*4.1*	*6.1*	192.9	17.3	178.0	16.1	834.4	10.0	870.6	9.1
Total	**104.9**	**100.0**	**68.4**	**100.0**	**1 118.2**	**100.1**	**1 107.5**	**100.0**	**8 310.3**	**100.0**	**9 518.6**	**100.0**

a See table C.14 in IC 1997 for earlier data.

Note: Figures in italics have relative standard errors greater than 25 per cent, or are derived from such data.

Source: ABS Labour Force Survey data.

Table B.19 **TCF persons employed by occupation, August 1996 and May 2003**[a]
’000

	1996			2003		
ASCO occupation	*Male*	*Fem.*	*Pers.*	*Male*	*Fem.*	*Pers.*
Managers and administrators	5.3	*2.5*	7.8	6.4	*1.6*	8.0
Professionals	*1.1*	*1.8*	*2.9*	*1.6*	*2.6*	*4.1*
Associate professionals	*1.5*	*0.9*	*2.4*	*1.7*	*1.1*	*2.8*
Tradespersons and related workers	10.2	8.4	18.7	*4.3*	5.3	9.5
Advanced clerical and service workers	*0.2*	*3.1*	*3.3*	-	*1.3*	*1.3*
Intermediate clerical, sales and service workers	*1.9*	5.8	7.8	*1.1*	4.9	6.1
Intermediate production and transport workers	18.2	28.6	46.7	11.0	19.4	30.4
Elementary clerical, sales and service workers	*0.4*	*2.4*	*2.8*	*1.0*	*1.1*	*2.1*
Labourers and related workers	6.5	6.0	12.5	*2.5*	*1.6*	*4.1*
Total	**45.3**	**59.6**	**104.9**	**29.6**	**38.8**	**68.4**

a See table C.15 in IC 1997 for earlier data.

Note: Figures in italics have relative standard errors greater than 25 per cent, or are derived from such data.

Source: ABS Labour Force Survey data.

Table B.20 **Selected TCF regional workforce characteristics, 2001**

per cent of total

Stat. Div. code[a]	*Main centres*	*No post-school qualific-ations*	*Not complet-ed year 12 or equival-ent*	*Lower skilled occupat-ional groups*[b]	*Aged 35 or more*	*Female*	*Born overseas*	*Married*
105	Sydney	60.4	51.6	52.7	73.4	59.2	65.1	65.2
120	Lismore, Tweed Heads	53.7	74.9	49.4	76.7	65.1	20.2	53.5
125	Coffs Harbour	60.3	76.8	44.3	71.3	54.6	11.2	61.6
130	Tamworth	58.5	72.9	55.2	54.8	31.1	5.2	52.4
140	Orange, Bathurst	67.0	77.1	63.9	64.2	33.7	7.5	57.6
145	Queanbeyan, Goulburn	64.9	75.5	62.5	68.7	55.3	17.0	56.9
155	Albury	63.1	76.2	64.6	70.1	46.3	18.6	60.1
205	Melbourne	67.5	59.2	62.3	72.5	54.6	63.0	67.0
210	Geelong	65.6	67.8	66.6	66.0	44.6	26.0	57.2
220	Ballarat	68.3	73.4	61.9	69.2	41.9	11.9	58.1
235	Bendigo	73.4	79.2	74.0	67.8	59.0	9.3	55.9
245	Wodonga, Wangaratta	66.3	76.5	74.4	69.3	39.0	17.2	58.4
255	Traralgon	66.5	80.8	72.1	70.5	58.0	12.0	56.8
305	Brisbane	70.5	62.1	57.1	68.7	60.3	44.4	62.2
310	Coolangatta, Surfers	65.7	67.0	49.4	72.3	62.2	35.8	55.9
405	Adelaide	67.6	66.7	58.9	70.1	56.2	39.1	58.9
505	Perth	63.6	60.8	52.9	67.8	59.1	54.7	60.6
605	Hobart	68.3	74.5	57.6	45.9	51.3	10.3	42.5
620	Burnie, Devonport	70.2	82.0	73.5	61.6	53.9	8.4	54.8
705	Darwin	65.9	71.3	39.7	63.0	64.3	24.6	48.8
805	Canberra	53.0	44.8	35.9	73.3	67.4	42.8	61.1
Total	**Australia**	**65.5**	**62.0**	**58.4**	**70.9**	**56.0**	**49.1**	**63.1**

a A statistical division is listed if it relates to a capital city or TCF employment in 2001 equalled or exceeded 250 and the TCF share of total manufacturing employment equalled or exceeded 5 per cent. **b** These groups refer to intermediate clerical, sales and service workers, intermediate production and transport workers, elementary clerical, sales and service workers and labourers and related workers.

Source: Estimates based on unpublished ABS Population Census data.

Table B.21 **Employees without leave entitlements, August 2002**[a]

Previously known as casual employees

ANZSIC industry	*Proportion of total employees*	*Total employees*
	%	’000
Textile, fibre, yarn and woven fabric mfg (221)	*13.2*	7.6
Textile products mfg (222)	*25.2*	15.1
Knitting mills (223)	S	5.0
Clothing mfg (224)	28.6	32.2
Footwear mfg (225)	-	*2.9*
Leather and leather product mfg (226)	S	*3.2*
All TCF (22)	22.9	66.0
All manufacturing	16.2	1 055.4
All industries	**27.3**	**7 927.0**

[a] See table C.8 in IC 1997 for earlier data.

Note: Figures in italics have relative standard errors greater than 25 per cent, or are derived from such data.

S: denotes estimate suppressed because of insufficient sample.

Source: ABS, Employee Earnings, Benefits and Trade Union Membership, August 2002.

Table B.22 **Employees with and without leave entitlements by trade union membership, August 2002**

Previously known as permanent and casual employees

	With leave entitlements			*Without leave entitlements*			*Total*		
ANZSIC industry	*Trade union member*	*Not trade union member*	*Total*[a]	*Trade union member*	*Not trade union member*	*Total*[a]	*Trade union member*	*Not trade union member*	*Total*[a]
	’000	’000	’000	’000	’000	’000	’000	’000	’000
All TCF (22)	13.2	35.9	50.9	*1.1*	13.5	15.1	14.4	49.4	66.0
All manufacturing	269.6	590.8	883.9	18.8	148.8	171.4	288.4	739.7	1 055.4
All industries	1 646.3	3 998.9	5 766.7	187.4	1 927.1	2 160.3	1 833.7	5 926.0	7 927.0
	%	%	%	%	%	%	%	%	%
All TCF (22)	26.9	73.1	100.0	*7.5*	92.5	100.0	22.6	77.4	100.0
All manufacturing	31.3	68.7	100.0	11.2	88.8	100.0	28.1	71.9	100.0
All industries	29.2	70.8	100.0	8.9	91.1	100.0	23.6	76.4	100.0

[a] Total numbers includes persons whose trade union membership status is not known. Percentages refer to persons whose trade union membership status is known.

Note: Figures in italics have relative standard errors greater than 25 per cent, or are derived from such data.

Source: ABS, Employee Earnings, Benefits and Trade Union Membership, August 2002.

Table B.23 **Labour mobility — TCF, February 1995 to February 1996**

'000 employed persons

Working in TCF at beginning of survey year			105.7
Less:	Not working at end of survey year:		
	- Employer/business/locality changed during year	*1.0*	
	- Did not change employer/business/locality during year	9.7	
	Working in other industries at end of survey year	7.2	
Working in TCF at beginning and at end of survey year:			87.8
- Did not change employer/business/locality		84.7	
- Changed employer/business/locality		*3.1*	
Plus:	Working in TCF at end, but not beginning, of survey year:		
	- Working in other industries at beginning of survey year	5.3	
	- Not working at beginning of survey year	10.3	
Working in TCF at end of survey year			103.4

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

Source: Unpublished ABS data.

Table B.24 **Labour mobility — all industries, February 1995 to February 1996**

'000 employed persons

Working at beginning of survey year			8047.7
Less:	Not working at end of survey year:		
	- Employer/business/locality changed during year	128.4	
	- Did not change employer/business/locality during year	430.2	
Working at beginning and at end of survey year:			7489.1
- Did not change employer/business/locality		6412.4	
- Changed employer/business/locality		1076.7	
Plus:	Not working at beginning of survey year	790.5	
Working at end of survey year			8279.6

Source: Unpublished ABS data.

Table B.25 **Labour mobility — TCF, February 1999 to February 2000**

’000 employed persons

Working in TCF at beginning of survey year		90.9
Less: Not working at end of survey year:		
- Employer/business/locality changed during year	*0.5*	
- Did not change employer/business/locality during year	7.8	
Working in other industries at end of survey year	4.9	
Working in TCF at beginning and at end of survey year:		77.7
- Did not change employer/business/locality	74.5	
- Changed employer/business/locality	*3.2*	
Plus: Working in TCF at end, but not beginning, of survey year:		
- Working in other industries at beginning of survey year	*3.8*	
- Not working at beginning of survey year	4.7	
Working in TCF at end of survey year		86.2

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

Source: Unpublished ABS data.

Table B.26 **Labour mobility — all industries, February 1999 to February 2000**

’000 employed persons

Working at beginning of survey year		8583.7
Less: Not working at end of survey year:		
- Employer/business/locality changed during year	110.3	
- Did not change employer/business/locality during year	436.5	
Working at beginning and at end of survey year:		8036.9
- Did not change employer/business/locality	6844.7	
- Changed employer/business/locality	1192.3	
Plus: Not working at beginning of survey year	834.5	
Working at end of survey year		8871.5

Source: Unpublished ABS data.

Table B.27 **Labour mobility — TCF, February 2001 to February 2002**

'000 employed persons

Working in TCF at beginning of survey year		80.9
Less: Not working at end of survey year:		
- Employer/business/locality changed during year	*0.6*	
- Did not change employer/business/locality during year	6.9	
Working in other industries at end of survey year	*3.9*	
Working in TCF at beginning and at end of survey year:		69.5
- Did not change employer/business/locality	65.3	
- Changed employer/business/locality	*4.2*	
Plus: Working in TCF at end, but not beginning, of survey year:		
- Working in other industries at beginning of survey year	*4.0*	
- Not working at beginning of survey year	6.8	
Working in TCF at end of survey year		80.3

Note: Figures in *italics* have relative standard errors greater than 25 per cent, or are derived from such data.

Source: Unpublished ABS data.

Table B.28 **Labour mobility — all industries, February 2001 to February 2002**

'000 employed persons

Working at beginning of survey year		8813.9
Less: Not working at end of survey year:		
- Employer/business/locality changed during year	115.4	
- Did not change employer/business/locality during year	458.2	
Working at beginning and at end of survey year:		8240.3
- Did not change employer/business/locality	7070.3	
- Changed employer/business/locality	1170.0	
Plus: Not working at beginning of survey year	820.4	
Working at end of survey year		9060.7

Source: Unpublished ABS data.

C Current assistance arrangements

Australia, like most developed countries, has a long history of protecting its textile, clothing, footwear and leather (TCF) sector.

However, since the late 1980s a succession of Australian Governments have sought to expose the TCF sector to greater international competition in keeping with the general shift in assistance policy. A major initial step was the TCF industry plan in 1987 which included a systematic reduction in tariffs. These reductions were accelerated in the 1991 industry statement and import quotas were terminated in 1993.

In conjunction with the reductions in protection, a range of adjustment assistance was provided. For example, the 1987 TCF industry plan included the Industry Development Strategy and a Labour Adjustment Program. Following the 1991 statement, some programs were modified and additional programs such as the Import Credit Scheme, Overseas Assembly Provisions Program and the Further Wool Processing Program were introduced. Further modifications of existing programs and the introduction of new programs occurred following the 1995-96 Commonwealth budget and as part of the TCF 2000 Development Strategy.

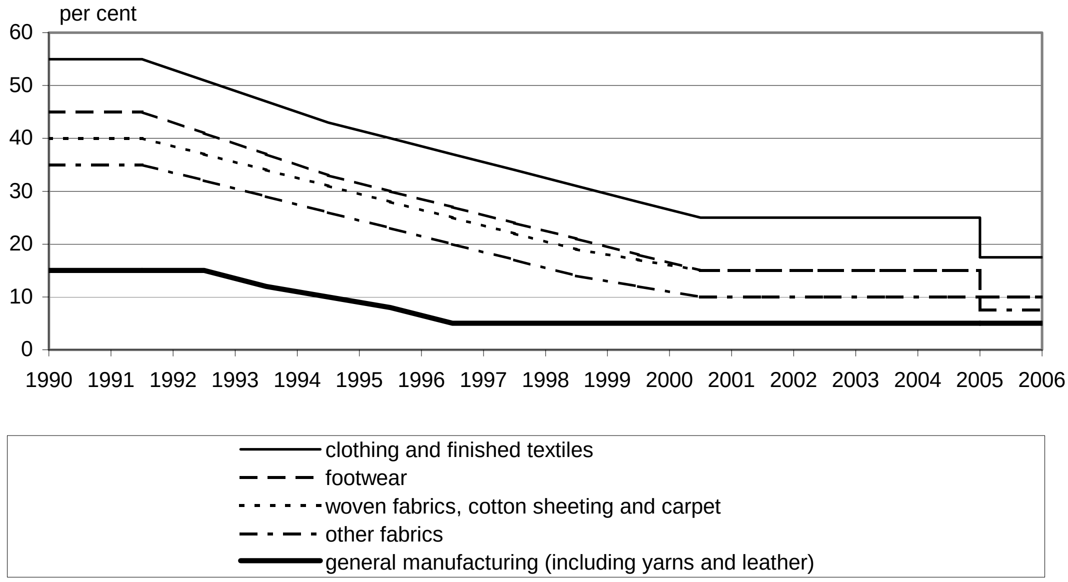
In July 2000, after 13 years of the gradual phasing down of TCF tariffs, further reductions were put on hold until January 2005. One effect of this pause has been to maintain a disparity in tariff rates for the TCF sector and the rest of manufacturing (see figure C.1). The sector has, however, continued to receive budgetary support to help it prepare for lower levels of tariff protection that will apply from 2005.

The current assistance regime for the TCF industries is complex. It consists of:

- tariffs on imports which vary across products;
- budgetary assistance through the Textile, Clothing and Footwear Strategic Investment Program (SIP);
- policy by-laws specific to the sector which enable concessional entry for certain imported TCF products; and
- concessional entry for some imports through the Expanded Overseas Assembly Provisions Scheme (EOAP).

Tariffs and the SIP are by far the most important of these measures. TCF firms also have access to general industry support offered by the Commonwealth and State Governments. The latter also provide a small amount of sector-specific assistance.

Figure C.1 **TCF and manufacturing sector tariff rates, 1990 to 2005**



C.1 Tariffs

The pause in tariff reductions until January 2005 has left general tariff levels at:

- 25 per cent for apparel and certain finished textiles;
- 15 per cent for cotton sheeting and woven fabrics, carpets and footwear;
- 10 per cent for sleeping bags, table linen, tea towels and footwear parts; and
- 5 per cent for textile yarns, sewing threads and finished leather.

There are no tariffs on unprocessed wool, although importation is subject to quarantine regulations.

In January 2005, following amendments made in 1999 to the *Customs Tariff Act 1995*, items at 25 per cent will be reduced to 17.5 per cent, those at 15 per cent to 10 per cent and those at 10 per cent to 7.5 per cent. Those items currently at 5 per cent will not change.

C.2 The TCF Strategic Investment Program (SIP)

The SIP is intended to encourage TCF firms to improve their international competitiveness by increasing their levels of investment and innovation. It also makes financial assistance available for firm restructuring in 'TCF dependent communities'.

The SIP, which was developed in consultation with the sector, was introduced in conjunction with the tariff pause in 2000. It applies to the financial years from 2000-01 to 2004-05, but included two 'pre-program' years, 1998-99 and 1999-00.

The program is open to any entity undertaking eligible TCF manufacturing and/or design activities in Australia. These are defined as activities involving goods which fall under the ANZSIC industry classification of textiles, clothing, footwear and leather.

Funding under the scheme is capped at $700 million, an amount equivalent to the anticipated cost of the previous Import Credit Scheme (see box C.1) had it continued past its termination date of July 2000 through to June 2005 (Department of the Parliamentary Library, 1999). Of this, around $22 million has been used to supplement the Regional Assistance Program. The remaining $678 million is available for distribution as one of five grant types (see below).

Box C.1 **Import Credit Scheme**

The Import Credit Scheme commenced in 1991 as part of a larger package of tariff and other reforms. It was aimed at making the TCF sector more trade orientated and capable of taking advantage of overseas opportunities.

Under the Scheme, companies were provided with 'import credits' in return for exports of TCF products. These credits, which were freely tradeable, could then be used to reduce customs duty on TCF imports. At the high point of the scheme in 1995-96, nearly $150 million of duty was forgone under the scheme.

In effect, the scheme made available a subsidy to TCF exports. That is, at a firm level it was profitable to subsidise exports provided that the required level of subsidy was less than the value of the import credits earned. As such, the scheme was vulnerable to action as a prohibited subsidy under WTO rules. This led to its replacement with the current SIP arrangement which focuses on promoting investment and R&D, rather than directly fostering exports (see text).

There is provision for a 'modulation' factor to be applied to grants to prevent the total funding cap from being exceeded. Further, assistance to an individual firm in any given year is capped at 5 per cent of the firm's sales of eligible products in the previous year. This is because, at the time the scheme was being developed, WTO rules specified that subsidies of more than 5 per cent were deemed to cause 'serious prejudice' to competing activities in other countries. While this rule is no longer explicit, maintaining subsidies below this level is likely to minimise the risk of actions in the WTO.

So far, modulation has not been applied. However, a number of firms have 'capped out' at the 5 per cent limit. Following a 2002 review by the Department of Industry, Tourism and Resources (DITR), the Government agreed to amend the scheme to enable firms to carry forward grant entitlements in excess of the 5 per cent sales cap.

Grants available under SIP

There are five types of grants available under the SIP:

- Type 1: grants for investment (up to 20 per cent of eligible expenditure);
- Type 2: grants for research and development including product development (up to 45 per cent of eligible expenditure);
- Type 3: matching value added grants (see below);
- Type 4: grants to purchase state-of-the-art second hand plant and equipment for restructuring by firms in TCF dependent communities (up to 20 per cent of eligible expenditure); and
- Type 5: special miscellaneous grants for ancillary activities relating to restructuring initiatives in TCF dependent communities (up to 20 per cent of eligible expenditure).

To access Type 1, 2 and 3 grants, which are administered by AusIndustry, a firm must have a minimum of $200 000 of eligible expenditure:

- Eligibility for Type 1 grants is restricted to expenditure on new TCF plant and equipment; the buildings or alterations to house that plant and equipment; and the upgrading of existing plant or equipment to comply with environmental legislation. Investment in second hand equipment, other than for environmental upgrading, does not qualify for Type 1 assistance.
- Eligible expenditure for Type 2 grants includes both research and development and product development activities that are considered to be 'innovative'. SIP does not define precisely what is 'innovative', instead placing the onus on the applicant to make a case . However, various guidelines have been put in place to assist claimants (see box C.2).

- Type 3 grants enable a firm to claim additional support linked to the value added in the program year the claim was made for a Type 1, 2 or 4 grant. These grants are capped at either 5 per cent of the total eligible value added, or by the sum of the Type 1, 2 and 4 grants received, whichever is the lesser. Valued added grants in excess of the cap cannot be carried forward. In effect, access to Type 3 grants means that, subject to its capping arrangements, firms can receive a subsidy of up to 40 per cent on investment in plant and equipment and up to 90 per cent for research and product development expenditures.

The reasons for the 5 per cent cap on value added grants are obscure. According to the DITR review, this 5 per cent was applied 'to minimise WTO compliance risks' (DITR 2002, p. 31). However, it is not clear why the overall 5 per cent cap on funding as a proportion of a firm's sales would not be sufficient to address concerns in regard to action in the WTO.

Box C.2 **Innovation and the SIP**

While there is no precise definition of 'innovation' in the SIP, AusIndustry has provided guidelines to assist applicants applying for Type 2 grants for product development.

The guidelines note that innovation does not encompass:

- activities that are routinely undertaken;
- doing more of the same type of activities;
- day-to-day design activities that are a standard part of the production process; and
- activities directed at achieving visual differences in a product (eg style, colour).

Rather, 'innovative' activities must involve introducing something new or different in the sense of changing the manner in which a product is developed. Applicants are generally required to demonstrate that their innovation is new to the industry as opposed to being new to the firm. For example, developing fabrics to overcome specific usage problems such as moisture build up in sporting clothes, or to increase fabric strength for industrial clothing, would be considered eligible, but variations in style such as fabric colour or clothing style would be ineligible in the absence of any functional innovation.

Design activities are eligible where they relate to new or improved methods of design such as computer assisted design systems that enable integration with computerised fabric cutting.

Source: AusIndustry (2002).

In order to facilitate the access of smaller firms to funding support, eligible spending activity can be cumulated over several years.

The other two types of grants to facilitate restructuring in TCF dependent communities, require Ministerial approval. They are available to support expenditures such as the purchase of state-of-the-art second hand equipment as part of the consolidation of TCF activity in those communities.

SIP includes provision for appeals against decisions not to register a firm as eligible to participate in the program, as well against non or reduced payments for specific claims. Appeals can be made to the scheme's administrators and to the Administrative Appeals Tribunal.

The operation of SIP to date

A total of 400 firms were registered under the program in 2001-02, slightly down from the previous year of operation (DITR 2002). Of these registered firms, 264 or around 5 per cent of total TCF enterprises had funding approved for the 2000-01 program year. However, those firms receiving SIP funding in 2000-01 accounted for around three-quarters of the TCF sector's value-added and two-thirds of its employment (information supplied by AusIndustry).

In the 2000-01 program year, $130 million of SIP payments were made (including some $27 million in respect of the pre-program years) and around $100 million has so far been paid for 2001-02. To date, Types 1 and 2 grants have accounted for about 60 per cent of payments and the Type 3 grants nearly all the rest (see table C.1).

Table C.1 **TCF SIP program payments (by program year and grant type)[a]**

Program year	*Type 1*	*Type 2*	*Type 3*	*Type 4*	*Type 5*	*Total*
	$'000	$'000	$'000	$'000	$'000	$'000
Pre program 1998-99	11 522	na	-	-	-	-
Pre program 1999-00	14 660	na	-	-	380	-
2000-01	28 251	27 737	45 797	500	1 263	130 112[b]
2001-02	22 272	34 456	42 147	72	28	98 977
Total	**76 705**	**62 193**	**87 944**	**572**	**1 671**	**229 089**

[a] The exact totals for each type of grant may vary slightly as some apportioning has been done between the three types to reflect the effect of the capping requirement. Payment figures for both the 2000-01 and 2001-02 program years are also still subject to change pending any reconsideration or appeals that are in the pipeline pertaining to these years.

[b] This total includes some $27 million paid in respect of the two pre-program years.

na: not applicable

Source: Information supplied by DITR.

By industry, of the funding paid in the first two years of the program, textiles fibre manufacturing received 39 per cent, textile product manufacturing (including carpet manufacturing) 27 per cent, clothing and footwear 23 per cent and leather 4 per cent (see table C.2).

Table C.2 **SIP funding by industry for 2000-01 and 2001-02**

Industry	*Payments*	*Share of funding*
	$'000	per cent
Textile fibre, yarn and woven fabrics	90 035	39.3
Textile product	62 116	27.1
Knitting mills	11 150	4.9
Clothing	34 019	14.8
Footwear	19 855	8.7
Leather and leather products	9 733	4.2
Other	2 176	1.0
Total	**229 089**	**100.00**

Source: Information supplied by DITR.

All payments are made in arrears of the firm undertaking eligible expenditure. The period between undertaking the expenditure and receiving payment can vary widely — from as little as two months or so, to a year or more. The lag in payment depends on administrative and modulation processing requirements and to some extent on when the firm lodges its claim. For example, assistance for expenditure, particularly investment, made late in a financial year can often be received by the firm very early in the next financial year. Reimbursement for R&D/innovation can take longer to process. However, advances of 50 per cent of the expected assistance can be paid to a firm prior to AusIndustry's full auditing and assessment of the claim.

AusIndustry employs 18 people to administer the scheme, with administrative costs of about $1.6 million since 2000 (information supplied by DITR). In addition there are:

- application costs for firms, with many using consultants (see chapter 5); and
- costs associated with the appeals process.

In the first program year, there were 16 appeals to the AAT or around 4 per cent of total claims. Of these, 12 were resolved by negotiation, 1 was withdrawn, 1 went to hearing and was decided in the favour of the applicant and the other 2 matters are still before the Tribunal. However, in the second program year there were only 2 appeals, one of which is still being processed with the other dismissed by the Tribunal.

C.3 Recently terminated schemes

Three smaller Commonwealth grant schemes for the sector — the Market Development Program, the National Framework for Excellence in TCF Training and Education and the TCF Technology Development Fund — were closed from July 2002 as part of the May 2002 Commonwealth Budget. These schemes had been initiated specifically as part of the post 2000 assistance package for the sector.

Funding for these three schemes during their limited period of operation was $32 million (McFarlane 2002).

Limited comment was received from participants regarding these terminated schemes.

C.4 The EOAP Scheme

The EOAP Scheme provides incentives for the offshore assembly of fabrics and leather manufactured in Australia. In essence, the scheme seeks to preserve the higher value and skilled parts of the production process in Australia by allowing the lower skilled, labour intensive assembly stages to be carried out offshore. Under the scheme, duty on imported footwear and garments assembled from predominantly Australian fabric and/or leather is only payable on the cost of the overseas processing and content (see box C.3).

The scheme, which commenced in 1992, was rolled over in June 1999 and is scheduled to end in 2005. To date, usage has been limited — in 2001-02, only $4.75 million of duty was forgone under the arrangements (ACS 2002b).

Box C.3 **Key features of the EOAP scheme**

Any Australian textile, clothing, footwear, leather manufacturing or design firm can participate in the scheme. To qualify for concessional duty treatment:

- the participant must be both the exporter of the fabric and/or leather and the importer of the assembled goods;
- there can be no transfer of ownership of the materials or the assembled goods between the time of export from, and import into, Australia; and
- the value of non-Australian fabric and/or leather must be no greater than 20 per cent of the total value of fabric and/or leather used to manufacture each article.

Source: AusIndustry (1999).

C.5 The Tariff Concession System and policy by-laws

Under the generally applicable Tariff Concession System (TCS), concessional entry is available for otherwise dutiable products deemed to have no locally produced Australian substitute. (Consumption goods are afforded duty free entry, while business inputs are subject to a 3 per cent revenue duty.)

While a few items, such as specialist footwear, incontinence pants and rubber gloves, receive concessional entry under the TCS, most clothing, footwear and headwear is excluded from the system by virtue of its listing on the Excluded Goods Schedule (see chapter 7).

However, there are around 20 so-called policy by-laws which enable specified TCF goods to be imported duty free. These are mainly blended cotton and blended synthetic lightweight fabrics.

In contrast to the TCS, concessional entry under the policy by-laws is available even if there is actual or potential domestic production of substitute goods. Thus, while reducing the costs of firms using the products concerned, it is possible that these by-laws adversely affect some other Australian TCF producers.

As general tariffs have declined and the local TCF sector has contracted, the amount of duty forgone under these policy by-laws has fallen substantially. Duty forgone in 2001-02 was around $40 million compared to a (recent) peak of $150 million in 1994-95 (ACS 2002b). Moreover, two by-laws accounted for over 80 per cent of the total duty forgone in 2001-02:

- Nearly half was accounted for by a by-law for certain dyed and printed plain weave cotton fabrics.
- A further one-third was accounted for by the by-law applicable to synthetic fabrics for use in headwear and clothing manufacture. (information provided by Australian Customs Service).

C.6 Other concessional provisions

In addition to concessional entry under the EOAP, the TCS and policy by-laws, some imported TCF products enter duty free, or at reduced rates, under other (generally applicable) arrangements:

- developing country and least developed country preferences;
- free trade agreements with New Zealand, and most recently Singapore; and

- the South Pacific Regional Trade and Economic Cooperation Agreement (SPARTECA) providing duty free access to the Australian and New Zealand markets for goods produced in Forum Island countries.

The removal of tariff preferences for TCF imports from countries such as China, India and Indonesia has greatly reduced the significance of the developing country preference regime for Australia's TCF sector. However, from 1 July 2003, imports — including TCF products — from least developed countries and from East Timor have been allowed duty free entry. This may lead to some increase in TCF imports from countries such as Bangladesh. As discussed in chapter 11, concerns have also been expressed that the rules of origin applying to imports from least developed countries may allow for duty free entry of significant embodied content from countries such as China.

There is also considerable TCF trade between New Zealand and Australia under the Closer Economic Relations (CER) arrangement and, until recently, significant duty free importation of clothing from Fiji under the SPARTECA provisions.

In the latter case, however, the now defunct Import Credit Scheme (ICS), rather than duty free access under SPARTECA, was the main driver of this trade. As described in box C.1, the ICS provided duty or 'import' credits in return for exports of Australian TCF products. Along with incentives offered by the Fijian Government and high tariffs in Australia on imports from most other countries, these credits made it profitable to export fabric to Fiji for assembly into clothing for subsequent re-import into Australia duty free.

However, with the termination of the ICS, reductions in Australian TCF tariffs and political unrest in Fiji, assembly of clothing (and footwear) in that country for the Australian market has declined markedly. This is despite the provision for the reduction from 50 to 35 per cent in the minimum local content of TCF products necessary to qualify for duty free entry into Australia and New Zealand under the SPARTECA-TCF provisions. (This reduced level of local content is in turn conditional on Fijian producers accruing 'Excess Local Area Content' from the production of finished garments, or other eligible TCF products, which have local area content of more than 70 per cent). In effect, without capacity to earn duty credits on fabric exports and with general tariffs on TCF products now lower, the benefits for most firms from duty free access to the Australian market for finished clothing products from Fiji are not sufficient to outweigh the additional freight and logistical costs of this sort of operation. (It is for much the same reason that there has been only limited recent use of the EOAP provisions.)

C.7 State Government support

Most State Governments provide support to industry, including TCF firms, through generally available schemes such as business innovation and regional development programs. Some limited TCF-specific assistance is also provided by certain State Governments (see box C.4).

Box C.4 Examples of State Government TCF-specific assistance

Victoria released its TCFL Strategic Plan in June 2002. It includes a business innovation program for the sector, a supply chain management program and a market access and development forum. Funding for these programs amounts to $1.5 million. The Victorian Government is also providing around $1 million annually to fund a training and education program for the sector and has provided over $1 million to establish the TCFL centres of excellence (Victorian Government 2002).

The Tasmanian Government now holds 49 per cent of the equity in Australian Weaving Mills (AWM) to secure employment in the Devonport area after the major equity holder, National Textiles, was placed in receivership. The Tasmanian Government has also provided debt funding for plant and equipment upgrades.

D Market access

Notwithstanding the recent progress in liberalising world trade in manufactured goods, TCF trade barriers remain relatively high and frequent in both developing and developed nations. While these barriers have similar effects, the rationales for their use differ somewhat between the two country groupings. In developed countries, TCF industries are often large employers of low skilled workers and receive government support as a means of protecting these jobs. Developing countries, on the other hand, often view TCF manufacturing as a vehicle to industrialisation and TCF trade barriers have been used to facilitate this process.

Many participants to this inquiry argued that high barriers in overseas markets restrict exports of Australian TCF products and thereby impede the development of the Australian TCF sector. For instance, the Council of Textile and Fashion Industries of Australia (TFIA) stated that:

> Enhanced market access provides the key platform for the TCF industry's future development. It is fundamental for the industry in the future to be growing on the basis of an export platform, especially as in the aggregate, the domestic market share will become more and more pressured as import penetration grows. (sub. 164, p. 9)

Improved market access will not be a panacea for most of the TCF sector, however. As the quote from the TFIA recognises, future increases in imports will place increasing pressure on many domestic producers (especially those engaged in the production of standardised labour intensive commodities). While some may be able to develop alternative markets overseas, others will not be able to compete internationally. In this regard, a recent market access study prepared for the TCFL Forum estimated that, trade liberalisation in Asian markets (which according to many participants are virtually impenetrable at present) would lead to export growth equivalent to less than 1 per cent of the current turnover of the Australian TCF sector (Werner International 2003).

Nonetheless, progress in reducing the extensive array of barriers to TCF trade would assist some internationally competitive Australian TCF firms to expand their businesses. For example, trade barriers on finished clothing from developing countries to the US and the EU (see below), restrict demand for Australian yarns, textiles and leather. And while some successful Australian TCF firms (such as Billabong and Gale Pacific) have established offshore manufacturing facilities to circumvent trade barriers, others (who may otherwise be globally competitive) lack the resources to do the same.

D.1 What is the current state of play?

TCF tariffs, quotas and a variety of non-tariff barriers impose large costs on the world economy.[1] In addition, some countries (including Australia) provide direct subsidies to TCF firms, which further distort world TCF trade. However, quotas on textiles and clothing products from WTO members are scheduled to be removed in 2005 and some countries have been able to reduce the barriers that they face in overseas markets by entering into preferential trading agreements.

Tariff barriers vary considerably across countries and TCF products

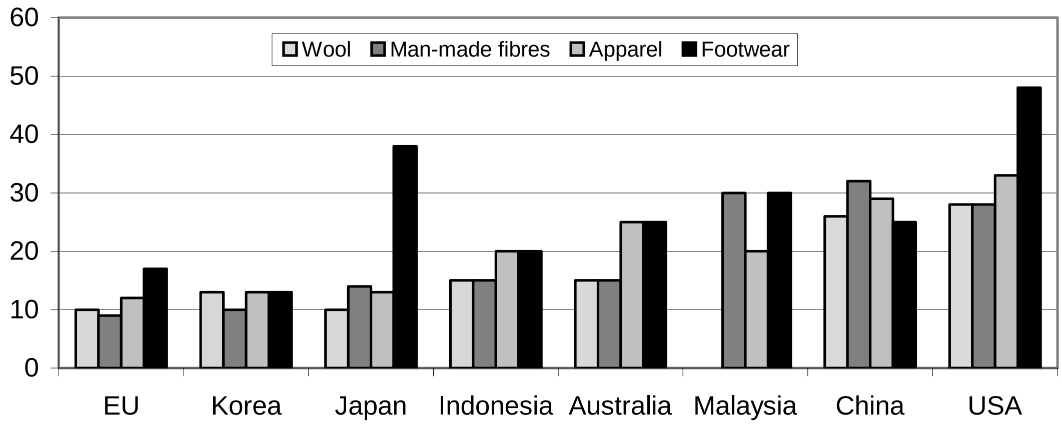
Some key characteristics of global TCF tariff barriers are listed below:

- Among developed countries, maximum applied tariffs are higher in the United States than in the European Union (EU) or Japan (these three markets accounted for 50 per cent of world textile and clothing imports in 2001). Since the mid-1990s, maximum tariff rates in these three markets have for the most part either fallen marginally or remained stable (a notable exception being a sharp rise in certain man-made fibre tariffs in the United States).
- Tariffs in developing countries have generally been falling at a faster rate than those in most developed countries (DFAT 1998). For example, China's accession to the WTO in 2001 required it to reduce tariffs across a broad range of TCF products (by up to 22 percentage points from the maximum levels applied in the mid-1990s). Nonetheless, tariffs in many developing countries are still higher than in developed countries and in a few cases have risen, rather than fallen. Korea, for instance, has raised tariffs on most TCF products in the last five years (though this has been from a low base).
- In Australia, in contrast to the EU, the US and Japan, tariffs on all TCF products have been reduced significantly over the last decade and a half (albeit from a much higher starting point). For example, tariffs on clothing, footwear and woven fabrics have fallen by between 10 and 30 percentage points since 1990. Further reductions have been legislated to take effect from 2005 (see appendix C).

[1] A recent study by the IMF and World Bank estimated the cost to be about US$65 billion. The study further found that, on average, every job saved in developed countries (as a result of textiles and clothing protection) costs 35 jobs in developing countries. (IMF and World Bank, 2002).

Figure D.1 **Maximum applied tariff rates for selected TCF products, selected countries/regions**[a]

per cent



[a] Figures for Australia, the United States and the European Union refer to 2002. Figures for China, Indonesia, Japan and Malaysia refer to 2000.

Data source: Information provided by DFAT.

Quota restrictions have been a highly distorting influence on global TCF trade

Despite the extensive use of tariffs, developed countries have historically used import quotas as the main mechanism for protecting their textiles and clothing industries. Since 1961, bilateral agreements have allowed certain developed countries to impose quotas on imports of textiles and clothing from a range of developing countries. The United States, the EU and Canada continue to restrict imports through such quotas. (Australia imposed quotas on all TCF imports between 1971 and 1993.)

Although Australian TCF exports are not subject to these restraints directly, the impact on world trade is likely to have adversely affected some Australian TCF firms. As noted above, the restriction on exports of final TCF products from developing countries, such as China, India and Pakistan, has almost certainly reduced demand for Australian intermediate goods (such as yarns, textiles and leather). Further, quota restrictions may have caused a redirection of some finished textile and clothing products (from countries that cannot access quota protected markets) to Australia. Allegations that some products are commonly sold at less than their 'normal value', or dumped in Australia have been raised in this context (see below).

Developed countries have agreed to remove quotas by 2005

Recognising the costs to the global economy of TCF quotas, an outcome of recent multilateral trade initiatives was an agreement to phase out their use. The Agreement on Textiles and Clothing (ATC), signed during the Uruguay Round of trade negotiations, establishes a schedule to remove remaining textiles and clothing quotas that apply to WTO members by 2005. (Importantly, however, quotas on Chinese exports, the world's largest producer of textiles and clothing, can potentially remain in place until 2008, as China was only admitted to the WTO in 2001.)

Other non-tariff barriers are commonplace

As well as these remaining quantitative restrictions, a variety of other non-tariff barriers (NTBs) serve to restrict trade in TCF products.

It is important to recognise that, while some NTBs are specifically imposed to reduce imports, others may be in place for primarily non trade-related reasons. For instance, quarantine restrictions may reduce imports, but are usually enacted for health and environmental reasons. Similarly, country specific product labelling requirements are often intended to provide information to consumers, rather than being a protective device against imports.

From a firm's viewpoint, however, the underlying intent of barriers which prevent them from accessing overseas markets will be of little significance. Hence, the examples put forward by inquiry participants included (see table D.1) incidental barriers to trade (see table D.1).

This is not to deny, however, that some of the barriers mentioned in table D.1, have the intent of restricting imports. For example, TCF Services commented on the effect of cumbersome customs procedures on apparel exports:

> In the absence of the exact export paperwork required by each country including quotas, import licences, country of origin certificates etc., the whole shipment is often embargoed by the overseas Customs department, and later sent back to Australia. Because of the interruption to supply, orders are then lost, customer relationships are damaged, and export marketing investment is wasted. (sub. 174, p. 3)

Further, export constraints that reduce the price of raw materials (such as leather) in India, China and Bangladesh, in turn reduce the costs of early stage processors within those countries. This can harm early stage processors in Australia which compete against those producers.

In recognition of their deleterious impact on trade, the removal of such restrictions is currently on the agenda for the Doha Round of multilateral trade negotiations. Further, the WTO Agreement on Technical Barriers to Trade already encourages members to ensure that regulations, standards, testing and certification procedures do not create unnecessary obstacles.

Concerns about dumping and anti-dumping actions

As quota removal under the auspices of the ATC draws nearer, many developing countries are concerned about the possible proliferation of anti-dumping measures as a substitute for other forms of industry protection.

Conversely, many TCF producers in developed countries see dumping as an activity which unfairly undermines their viability. In this inquiry, a number of participants commented on the alleged dumping of TCF products into the Australian market. Participants were particularly concerned about the difficulty of preventing dumping due to its seasonal and short-term nature and because current administrative processes are protracted and unwieldy (see chapter 11).

Regional trading arrangements have a major impact on TCF trade and production

Regional trading blocs, such as NAFTA and the EU, can greatly reduce trade opportunities for non-member countries. This is illustrated by the high levels of intra-bloc trade within the EU and NAFTA, including in TCF products. Under NAFTA, for example, there has been a major shift of production facilities from the United States to Mexico to take advantage of duty free access back into the US market. As a result, Mexico at one stage became the largest textile and clothing supplier to the United States. China has now assumed that mantle.

Table D.1 **Participants' examples of non-tariff barriers to TCF trade**

Country	*Non-tariff barrier*	*Description*
Argentina	Customs procedures	Exchange control procedure does not allow pre-payment, nor payment terms less than 90 days
	Labelling	Fibre composition, care instructions, name of manufacturer, importer and exporter
China	Distribution systems	Importers may receive lower prices than domestic producers
	Internal taxes	Value added taxes increase with the degree of processing and are arbitrarily applied
	Customs procedures	Arbitrarily imposed labelling requirements
	Labelling	Name and address of manufacturer, size, fibre composition, care instructions
EU	Labelling	Fibre composition, care instructions, fire hazard warning on children's garments
India	Customs procedures	Arbitrary valuation and classification of goods
	Labelling	Name and address of manufacture, description and sort number of cloth, care instructions, length in metres and width in cm, month and year of packing, health/environmental certificate
Indonesia	Customs procedures	Non-transparent procedures, corruption ('unofficial fees' often required)
	Distribution systems	Regulations favour local manufacturers
	Taxation	VAT charged on imported goods but not always on domestic goods
Japan	Labelling	Name of manufacturer/supplier, fibre composition, care instructions, size in metric units and fire hazard warnings on children's clothing
New Zealand	Labelling	Fibre composition, care instructions, country of origin, size in metric units, fire hazard warning for children's clothing
South Korea	Distribution systems	Most internal trade controlled by domestic monopolists who generally shut out imported goods
	Labelling	Name of manufacturer/importer, date of manufacture, size, country of origin, fibre composition, care instructions
Thailand	Customs procedures	Arbitrary valuation and classification of goods, excessive documentation, customs clearance fees
United States	Customs procedures	Burdensome compulsory origin of product documentation

Source: Werner International (2003) and TFIA (2002a).

The United States and the EU also grant duty and quota free access to a number of developing countries. For example, the USA has bilateral free trade agreements with emerging TCF producers such as Vietnam; gives preferential access to least developed countries in sub-Saharan Africa; and uses countries in the Caribbean Basin for overseas assembly arrangements. Similarly, the EU gives duty free entry to non-member countries such as Morocco, Turkey and Tunisia and uses countries in Eastern Europe (such as Romania and Poland) for its overseas assembly requirements (Stengg 2001).

There is also considerable TCF trade between Australia and New Zealand under the auspices of the Closer Economic Relations Agreement. In addition, provision of duty free entry into Australia for products from Fiji, in combination with a previous export facilitation scheme for the TCF sector in Australia, led to thriving offshore assembly operations in Fiji during the 1990s (see appendix C).

Financial incentives for TCF producers are widely available

The use of government financial incentives to support TCF activity has also been a feature of government TCF support programs in some countries. As well as budgetary support for specific investments, TCF firms often benefit from subsidies for R&D and for regional development. Signatories to the WTO Agreement on Subsidies and Countervailing Measures are, however, constrained in relation to the types of incentives that can be provided specifically to TCF producers (see box D.1).

Moreover, compared with some other manufacturing industries (notably the automotive industry), the use of sector-specific government subsidies to support TCF activity has been relatively modest. In one respect, the extensive use of quotas and other non-tariff barriers on textiles and clothing products has reduced the 'need' for such subsidies. Some specific examples of TCF subsidies include:

- In South Africa, exports of textiles and clothing earn import duty credits in a manner similar to Australia's now defunct Import Credit Scheme (see appendix C).
- The South Korean Government is providing US$600 million towards the 'Milano Project', a program designed to establish the city of Daegu as a major textile and clothing manufacturing centre.
- The Indian Government plans to spend US$6 billion to modernise its textile and clothing sector.
- In the United States, AMTEX and the Textile/Clothing Technology Corporation programs both offer R&D assistance exclusively to textiles and clothing firms.

The schemes are of limited significance, however, providing around US$6 million annually.

Box D.1 WTO agreement on Subsidies and Countervailing Measures

The Agreement on Subsidies and Countervailing Measures (SCM) regulates the use of ‘specific’ subsidies (that is, subsidies which are not available to all industries). A subsidy is:

- *Prohibited* if it is contingent on export performance or on the use of domestic inputs over imported goods.
- *Actionable* if it causes adverse trade effects. For example, a production subsidy (through its effects on exports) may cause material injury or serious prejudice to producers in the importing country.

In the past, the conditions under which serious prejudice was deemed to exist included cases where the total subsidy provided to a product was greater than 5 per cent of its sales value in the previous year. This benchmark had a significant impact on the design parameters of Australia’s SIP arrangements and the Automotive Competitiveness and Investment Scheme. While this transitional benchmark formally lapsed at the end of 1999, the 5 per cent level will inevitably still be a consideration in evaluating whether a subsidy is likely to be actionable.

Source: WTO (2003a).

In most developed countries, TCF producers receive the bulk of any budgetary support through more general programs. Most of these general programs are designed to either subsidise R&D or to support disadvantaged regional areas. For instance, participants to this inquiry reported that leather processors in Italy receive large amounts of funding under a regional EU scheme. Australia has been an important exception to this general pattern, with the TCF sector receiving very substantial sector specific support in recent years through the Strategic Investment Program (SIP — see chapter 5 and appendix C).

While production subsidies (whether general or sector-specific) do not directly restrict trade, they can affect the location of production and thereby indirectly impact on trade patterns. That said, they currently appear to have less influence on TCF production and trade than tariffs, quantitative restrictions or other non-tariff barriers. In the case of Australia, for example, the Commission estimates that the value of tariff assistance to TCF producers is several times greater than the value of support provided through the SIP.

D.2 What is in prospect?

Removal of quotas by the US, the EU and Canada under the ATC, and multilateral initiatives to reduce tariffs and non-tariff barriers, should lead to a more open trading environment for TCF products in the medium term. Current multilateral negotiations are moving slowly, although this has also been typical of the early stages of past negotiations. In parallel to these negotiations, many countries (including Australia) are entering into free trade agreements which will further liberalise trade in TCF goods.

Quota removal under the ATC

Progress under the ATC has been slow and there are fears that full implementation may not be achieved by 2005. For instance, in a recent review of the ATC, the WTO found that in the United States, the EU and Canada, products on which quotas had been removed were predominantly less sensitive items such as yarns, fabrics and finished textile products (WTO 2002).

For their part, Canada, the EU and the United States have re-affirmed their commitment to the full removal of quotas by 1 January 2005 and point to significantly higher levels of import penetration by developing countries as evidence of the extent of liberalisation to date.

Developing countries will benefit most from the removal of quotas

The elimination of quotas under the ATC would provide a major fillip to TCF production in developing countries — China in particular. One study cited by the WTO estimates that quota removal could increase developing country textile and clothing exports to OECD countries by 82 per cent and 93 per cent respectively (WTO 2003c). The potential for China to increase its exports to North America and the EU is illustrated by the growth in Chinese exports to developed countries that no longer apply quotas. For example, since quotas were removed in Australia, Chinese clothing exports have increased 3 fold and now account for 70 per cent of Australia’s clothing imports. A similar outcome has been evident in Japan since it removed quotas on Chinese clothing products.

But the effect on the Australian TCF sector is less clear

The flow-on impacts of future quota removal in the United States, the EU and Canada on Australia’s TCF sector will depend on a range of factors. These include the extent to which:

- Chinese exports currently going to Australia are diverted to the United States, the EU and Canada;
- Australian products are displaced in those markets by developing country producers no longer facing quotas;
- there are increased opportunities to export intermediate inputs to developing countries, consequent on their increased exports of finished goods to the United States, the EU and Canada; and
- quotas are replaced by alternative trade barriers.

In this inquiry, there were differing views on how these factors would play out for Australian firms. Some saw competitive pressures in the domestic market easing as a result of the diversion of Chinese textiles and clothing to the much larger US and EU markets. Others, however, envisaged no significant lessening of competition from Chinese imports and potentially greater competition from those developing countries displaced by China in the United States and the EU.

Quantitative modelling undertaken for the Commission by the Centre for International Economics (CIE 2003 — see appendix E) sheds some light on the net impact of global trade liberalisation on the Australian sector. It suggests that the removal of quotas and tariffs on textiles and clothing products by the United States would result in higher production of Australian textile and leather intermediate inputs mainly because China would significantly expand its finished product exports to the US.

But it also projects that some Australian products would be displaced by exports from developing countries. For example, in the case of EU liberalisation, some developing countries face significantly higher barriers than Australia in EU markets and would receive a larger competitive boost from EU trade liberalisation leading to a substitution away from Australian TCF products.

The Doha Round offers scope for further reductions in protection

The latest round of trade negotiations — the Doha Development Agenda — is in progress and WTO members aim to finalise these negotiations by 1 January 2005. Particularly relevant to the TCF sector will be negotiations on market access for non-agricultural products. The three key aims of negotiations on these products are to reduce or eliminate:

- tariff peaks, usually tariffs of or above 15 per cent for developed countries;
- tariff escalation (tariffs that increase with the degree of processing); and
- non-tariff barriers.

As with the removal of textiles and clothing quotas, multilateral tariff reductions would have both benefits and costs for the Australian TCF sector. In this respect, the modelling undertaken by the CIE, projects that global removal of protective barriers would in fact decrease total Australian production of textiles and clothing substantially. However, more optimistic commentators suggest that global trade liberalisation will lead to an increase in Australian exports of textiles and clothing (see, for example, Werner International 2003).

In any event, many participants in this inquiry expressed scepticism about the degree of liberalisation that would come from WTO processes. For example, the TFIA said:

> Looking forward, it is possible that there will be reductions in TCF&L tariffs as a result of the Doha Round. However, the policy of the world's leading players to make any reductions conditional on being linked and reciprocated means that unilateral unconditional reductions are unlikely to occur.
>
> … There is, therefore, little to suggest [that] the Australian TCF&L industries will significantly benefit in the next five to 10 years from reductions in … tariffs. (sub. 75, p. 30)

Yet at the same time, the TFIA recognised that aspects of these processes could be helpful to Australian firms:

> Equally with China's entry into the WTO, and the resulting commitments to open its markets, the opportunity exists for the Australian TCF&L industries to take advantage of the inherent demand in China and supply appropriate products into the Chinese market, thereby further diversifying Australia's exports. (sub. 75, p. 30)

The APEC process may also provide opportunities

APEC was established in 1989 as a forum to progress the liberalisation of trade and investment among both members and non-members. A milestone for APEC was the 1994 Bogor Declaration in which member countries agreed to the goal of achieving free and open trade and investment in the region, by 2010 for developed member countries and by 2020 for developing member countries.

Unlike WTO agreements, APEC is not predicated on the notion of reciprocal 'concessions' by member countries. Nor does it impose penalties for failure to meet its goals. It seems generally accepted that achievement of the Bogor timetable for free trade and investment in the region is less certain than if it involved a binding agreement. Nonetheless, in its own right and in supporting the WTO process, APEC should help to promote further trade liberalisation, including in TCF products.

Some mooted free trade agreements could benefit local TCF firms

Australia has been negotiating a free trade agreement (FTA) with the United States since a framework was agreed upon in June 2002. A recent ACIL Tasman study (2003) projected that an FTA with the US would result in a small overall welfare loss for the Australian economy (though it did not forecast impacts for the Australian TCF sector). Conversely, a study by the CIE (2001) projected that the removal of tariffs on trade between the two countries would increase consumption in both Australia and the US and, in so doing lead to an increase in Australian TCF exports and production of around 10 and 1.5 per cent respectively. Such projections are, however, likely to overstate the impacts of an FTA because they do not account for potentially restrictive rules of origin conditions usually included in such agreements (see chapter 11).

But regardless of the overall effect on the Australian economy and the TCF sector specifically, there are likely to be both winners and losers among individual TCF firms. In this context, concern was expressed by some participants about the likely impacts of an FTA with the United States on particular segments of TCF production (such as carpet manufacture — see chapter 3). There were also concerns that the application of the existing US ‘yarn forward’ rule (stipulating that TCF products must be made from both domestically produced yarn and fabric to gain duty free entry to the US) would significantly limit the scope for many Australian TCF firms to expand their exports to the US.

Australia also recently signed an FTA with Singapore and is discussing a similar agreement with Thailand. Manufacturing trade between Singapore and Australia was largely unencumbered prior to the signing of the FTA, which suggests that the agreement is likely to have a minimal impact on the Australian TCF sector. There is some concern, however, that an agreement with Thailand could pose a threat to Australian apparel manufacturers. As well as being a low-cost producer of garments in its own right, some participants suggested that Thailand could be used as a conduit for Chinese product seeking to gain duty free access to Australia.

D.3 Implications for the Australian TCF sector

Market access is an important issue for the sector, with some positive developments in prospect. Removal of quota restrictions in the United States and the EU is likely to create some new opportunities for Australian suppliers of yarns, textiles and leather to developing countries. And further reductions in barriers to TCF trade resulting from the Doha Round of trade negotiations should benefit some Australian TCF firms.

What is less clear, however, is whether trade liberalisation in overseas countries will provide a significant boost to the sector's overall export performance. The Australian TCF sector faces strong competitive pressures from low-wage countries, pressures that are likely to increase with global trade liberalisation. For many TCF products, high Australian labour costs, in conjunction with improving productivity and quality in developing countries, will militate against export growth even if trade barriers are reduced. Indeed, it is possible that, in aggregate, opportunities for Australian textiles and clothing producers, may be reduced rather than increased by liberalisation in the world's major TCF markets.

Nonetheless, some TCF firms would share in the very significant benefits that broadly based trade liberalisation would bring to the Australian economy. Hence it is imperative that Australian Governments continue to pursue further trade liberalisation, including in the TCF sector, in multinational, regional and bilateral forums.

E Modelling the effects of assistance options

The reference requires the Commission to analyse post 2005 assistance options that would encourage the textiles, clothing, footwear and leather (TCF) sector to adjust into activities where it will be internationally competitive with lower levels of assistance. This appendix summarises the quantitative evaluations, undertaken during this inquiry, of some potential assistance options beyond 2005.

Quantitative analysis of the industry and economy–wide impacts of changes in domestic assistance options was undertaken for the Commission by the Centre of Policy Studies (CoPS) at Monash University, and by Econtech Pty Ltd. A quantitative assessment of the implications of international developments in assistance to TCF activity was provided to the Commission by the Centre for International Economics (CIE).

In addition to these analyses sponsored by the Commission, the results from a number of other modelling studies were made available to the inquiry:

- ACIL-Tasman undertook an analysis of the implications of domestic and global TCF assistance developments for the Council of Textile and Fashion Industries of Australia.
- The Victorian Department of Treasury and Finance provided summary results from in-house modelling of the impacts of implementing the Commission's preliminary preferred post 2005 assistance options (as set out in the Position Paper — PC 2003).
- The National Institute for Economic and Industry Research (NIEIR) undertook an analysis, for Victoria's Manufacturing Industry Consultative Council, of the regional employment effects in Victoria of TCF sector developments, including an implementation of the Commission's preliminary preferred post 2005 assistance options.
- At a regional level, the Centre for Sustainable Regional Communities at Latrobe University assessed the effects of changes in TCF activity for the Wangaratta Rural City Council, the City of Greater Bendigo and the Western Region Councils Forum.

The modelling studies sponsored by the Commission, and those undertaken for the Council of Textile and Fashion Industries of Australia and the Wangaratta Rural City Council, were presented in draft form at a workshop in Canberra on 20 March 2003. The final versions of the papers sponsored by the Commission are posted on the Commission's web site. Also included in submissions that are available on the web site is the modelling work undertaken for the Council of Textile and Fashion Industries of Australia (submission PP100), the Victorian Government (submission PP173), the Wangaratta Rural City Council (submissions 46 and PP149), and the City of Greater Bendigo (submission PP150).

E.1 Modelling of assistance scenarios

Modelling domestic policies

The effects of post 2005 reductions in assistance for the Australian TCF sector were analysed for the Commission by Econtech using the MM600+ comparative static long run equilibrium model of the Australian economy (Murphy 2002) and by CoPS using the MONASH dynamic general equilibrium model of the Australian economy (Dixon and Rimmer 2002).

In the base case scenario for these simulations, it is assumed that:

- tariffs on TCF products will fall as legislated, from current levels of 25 per cent, 15 per cent and 10 per cent, to 17.5 per cent, 10 per cent and 7.5 per cent, respectively, on 1 January 2005; and
- SIP funding, currently capped at $678 million for the 5 year period to 30 June 2005, will continue at a level such that the ratio of SIP funding to turnover in each TCF industry is consistent with that observed to date.

Modelled assistance options beyond 2005 were:

- all TCF tariffs lowered to 5 per cent in 2010; and
- SIP style funding removed in 2010.

Although the modelling specifications on the Commission's web-site identify these changes as occurring in 2010, they represent an assistance outcome that would not be fully realised until 2015 under the Commission's preferred tariff and SIP options (see chapters 7 and 8).

In the remainder of this appendix, the likely effects of changes in domestic TCF assistance are primarily illustrated using the results from the Econtech (2003) and

CoPS (2003) studies. However, most of the projected outcomes are similar across all of the modelling studies. Where relevant, projections from the modelling work submitted by inquiry participants are reported for comparative purposes.

In preparing this final report, the Commission did not ask Econtech or CoPS to model its preferred option for TCF assistance reduction. Given the relatively small differences between the preferred option and the assistance scenarios modelled by Econtech and CoPS, and the very small magnitude of the economy–wide outcomes projected by all the modelling exercises, the Commission's judgment was that such additional projections would add little value. However, the Commission provided detailed information and assistance to the Victorian Department of Treasury and Finance to assist them in their modelling of the Commission preferred assistance option, as set out in the Position paper. At least as far as the modelling specifications are concerned, this option was identical to the Commission's final preferred option for tariffs and SIP funding.

Model Features

The MM600+ model distinguishes 108 industries in 23 regions producing 672 products. It includes the ANZSIC 3 digit TCF industries of (i) textile fibres, yarns and woven fabrics; (ii) textile products; (iii) knitting mill products; (iv) clothing; (v) footwear; and (vi) leather and leather products. The model quantifies output for 57 separate products of these sectors.

The MM600+ model results provide a long run snapshot of the impacts of policy options, once they have been fully implemented and all subsequent economic adjustments have taken place. The results from MM600+ are interpreted as deviations from a long run base case. The base case uses the 1993-94 ABS input-output tables, but is updated to include 1998-99 labour force survey data, the new tax system introduced in Australia in 2000, and reductions in government assistance for the TCF industry that will have occurred by 2005.

The MONASH model distinguishes 144 industries disaggregated to 57 sub-state regions, and includes results for a single aggregated product for each of the same six TCF industries as the MM600+ model. In contrast to the MM600+ model, the MONASH model allows examination of the effects of an assistance reduction over time. Thus, the MONASH model projects the effects of policy changes, such as variations in TCF assistance, as deviations from a base case, or business-as-usual future path.

The base case in the MONASH model has been formulated by first undertaking an historical analysis of the TCF industry to update the database from 1996-97 to

2001-02. This historical analysis not only facilitates the development of a hypothesised database for the TCF industry, but can then be projected forward in time to include the influence of macroeconomic factors.

However, constructing base cases of what might happen to an industry or sector in the absence of an assistance reduction is fraught with difficulty. If the base case is to reflect recent experience, then construction requires extrapolation into the future of trends evident today. The base cases that such extrapolations produce may become unrealistic the further forward in time they are taken.

This is a particular problem in the construction of a base case for the modelling in this inquiry:

- Were the Commission's preferred tariff option to be implemented, the reduction to 5 per cent in tariffs on clothing and certain finished textile products would not occur until 2015. Hence, to project the impacts of such tariff reductions requires the base case to be extended out for at least another 15 years from 2003.
- Extrapolating the output and employment declines recently observed in the sector over an extended time frame will lead to output and employment levels that are much lower than present levels. However, as noted in chapter 2, TCF employment may not have fallen as rapidly as the manufacturing statistics show.[1] Also, some in the sector believe that recent steep declines in employment will not continue at the same rate into the future (TCFL Forum 2002).
- It is difficult to distinguish the respective contributions of global competitive pressures and lagged adjustment to previous reductions in TCF assistance, to recent changes in activity and employment in the sector.

In modelling the policy options, both the MM600+ and MONASH models assume:

- Substitution between domestic and imported products occurs in response to changes in the relative prices of these products;
- Export demand is responsive to prices;
- Investment is responsive to post-tax rates of return; and
- Real wealth of Australians is the same under each policy option in the long run as in the base case. This means that any change in household incomes as a result of changes in assistance levels is assumed to be manifested in current

[1] The recent decline in TCF manufacturing employment has been accompanied by an increase in TCF-related employment in distribution activities – some firms previously recorded as undertaking mainly manufacturing activities have moved to sourcing a majority of their products from offshore and are now recorded as retail or wholesale firms. Also, part of the recent decline in TCF manufacturing employment, as reported by the ABS, may reflect outsourcing of garment assembly to outworkers.

consumption levels rather than affecting the level of savings and hence capital stocks. This assumption allows aggregate real consumption to be used as a single indicator of the change in economic welfare resulting from a change in TCF assistance.

The MONASH model was run with two 'closure' assumptions regarding employment. The first assumes wage rates adjust slowly in the short run but are fully flexible in the long run. This allows aggregate employment to change in the short run in response to a policy change. The second assumes fully flexible wage rates with the result that aggregate employment is the same as in the base case in both the short and long run. The latter closure assumption is also used by the MM600+ model.

The levels of assistance for the ANZSIC 3 digit TCF sectors used in modelling assistance options are detailed in table E.1. In both the MM600+ and MONASH models, reductions in TCF tariffs from the base case levels can be modelled directly. Changes in the level of funding provided under SIP are incorporated in both models by treating SIP funding as a subsidy to TCF production, with the subsidy rate calculated by dividing recent levels of funding by corresponding turnover figures. These modelled production subsidies range from 0.5 per cent of annual turnover in leather and leather products manufacturing, to 2 per cent for textile fibres, yarns and woven fabrics manufacturing.

Table E.1 **Modelled levels of assistance**
Per cent

	Tariffs [a]			*SIP* [b]	
	Current	*At 2005*	*Cut to 5 per cent*	*Current*	*No SIP*
Textile fibres, yarns, and woven fabrics	4.5	3.5	2.2	2.0	0.0
Textile products	7.1	6.4	3.4	1.6	0.0
Knitting mill products	15.8	13.5	4.6	0.7	0.0
Clothing	16.4	13.9	4.1	0.7	0.0
Footwear	11.8	8.7	4.7	1.8	0.0
Leather and leather products	3.5	1.2	1.2	0.5	0.0

a cif basis; **b** per cent of annual turnover in each industry sector.
Source: PC estimates and Econtech (2003).

Modelling international developments

The implications of changes in global assistance levels to the TCF industries were analysed for the Commission by the CIE using GTAP (Hertel 1997). GTAP is a multi-commodity, multi-region comparative static model of the world economy. A region may be either a single country or a composite of many countries. Each region produces its own version of each commodity, which is imperfectly substitutable with the versions produced by other regions.

The CIE used GTAP to examine how the following scenarios would affect the broad prospects for the Australian TCF industry:

- unilateral and multilateral liberalisation in, and between, Australia, the US, the EU, China and the APEC region; and
- full TCF liberalisation (Australia and the rest of the world).

The tariff rates in the GTAP base case are derived from country rates applicable in 1997. For Australia, the average modelled tariff rates on TCF imports were 15.8 per cent for textiles, 27.4 per cent for clothing and 12.1 per cent for leather products. These rates are well above current tariff rates and the even lower rates that will apply from 2005. This means that some of the projected impacts of the modelled scenarios may have already been felt in the Australian economy in the period since 1997, or will be evident prior to 2005.

In addition to tariffs, TCF trade is often restricted by import quotas (see appendix D). In GTAP, import quotas in the protected country are treated as destination specific export taxes from the point of view of the exporting countries. The largest export taxes in GTAP apply to textile and clothing exports from China, Malaysia, Singapore and Japan to the US and Canada.

E.2 Impacts of domestic assistance reductions

Economy–wide impacts on welfare

Changes in the level of assistance to an industry generate winners and losers across the economy as a whole. Not surprisingly, the model results indicate that a reduction in TCF assistance, through either lower tariffs and/or a lower level of SIP funding, will reduce TCF activity in Australia (the impacts are detailed in the following section). However, a reduction in TCF activity need not translate to adverse affects for the economy as a whole. In both the MM600+ and MONASH models, the projected overall outcomes for the economy will depend on the interplay of the following factors:

- Improved allocative efficiency — resources will be directed toward more productive and less protected activities in the economy.

- An increased resource base for the economy — reductions in tariffs may stimulate investment and a net inflow of capital from overseas (as by assumption, additional capital is financed by foreign inflows and real wealth of Australians is held constant in the long term).
- A decline in the terms of trade and an associated depreciation in the exchange rate — other factors being equal, while Australia's exports rise, the price of these exports declines relative to the price of imports, imposing a cost on the economy (see box E.1).

Overall, the MM600+ and MONASH model results suggest that the economy–wide effects of tariff and SIP reductions would be very small (see figure E.1 and table E.2). This is because:

- the TCF industry is a comparatively small component of the Australian economy; and
- TCF assistance levels are now much lower than in the past — as assistance levels fall, the allocative efficiency gains from further reductions also diminish.

The projected allocative gains from tariff reductions are consistently higher than those projected to arise from an elimination of SIP funding. This is because tariffs account for the bulk of assistance provided to the sector and also that tariff reductions are projected to have a larger effect on trade than does the removal of SIP support (see table E.2). Reducing tariffs leads to a more open economy than does the elimination of SIP, and therefore the supply of exports increases to restore the trade balance.[2]

[2] These outcomes are based on TCF export demand elasticities of 10 to 12 in the MM600+ model, 4 in the MONASH model and about 20 implicit in GTAP. Lower assumed values for this elasticity result in lower projected export growth in response to reductions in assistance levels, and can contribute to terms of trade effects which dominate allocative efficiency and capital effects, to yield small losses in welfare rather than increases. A detailed discussion of the implications of alternative values of export elasticities is included in Productivity Commission (2002b) for the MONASH model and in Econtech (2003) for the MM600+ model.

Box E.1 **Putting terms of trade effects in context**

A feature of the modelling for both the current TCF inquiry and the recent automotive inquiry (PC 2002b) is that projected small allocative efficiency gains from further tariff reductions are largely (or more than) offset by projected welfare losses associated with a decline in Australia's terms of trade. As tariff levels fall, the projected allocative efficiency gains from further reductions also diminish. This has meant that in analysing the potential impact of assistance reductions, there is now more weight in the modelling outcomes on the still small terms of trade effects which were previously swamped by significant resource allocation gains.

Such terms of trade effects are often viewed as being inconsistent with Australia's position as a small country with little influence on world prices for goods and services. However, terms of trade effects are consistent with the idea that Australian firms may sell differentiated products into niche markets — increased sales may require a lower price for the Australian product, even if all other overseas prices are unaltered (see Brown 1987 for an elaboration of this argument). A reduction in the prices received for Australia's exports relative to prices paid for its imports imposes a cost on the Australian economy, even if activity levels in some industries have risen in the process.

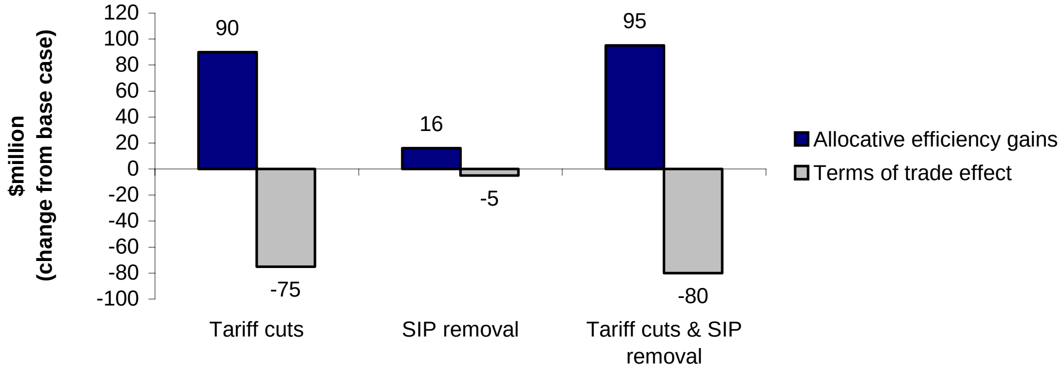
However, any terms of trade effects associated with reductions in Australia's TCF assistance need to be considered in a multilateral context. As some submissions to the inquiry noted, the projected adverse terms of trade effects from unilateral reductions in Australia's support for the TCF sector may be mitigated if other countries are also reducing the level of assistance to their TCF industries.

More importantly, in considering results from the MM600+, MONASH and GTAP models, it should be recognised that in each of these models the terms of trade effects are projected to be small. But with projected resource allocation gains also now small, assessments of the impacts of TCF assistance reductions at an economy–wide level tend to swing, with underlying model assumptions playing a disproportionate role in whether assistance reductions are projected to result in a small gain or a small loss for the economy.

Thus, with TCF tariff levels at comparatively low levels, it is factors not included in the modelling which are critical in determining the appropriate future direction of assistance. As discussed in chapter 6, these factors include the extent to which assistance reductions would reinforce incentives for firms to lower production costs further, to innovate and improve the quality of their products; and the magnitude of accompanying adjustment costs for firms, their employees and surrounding regions.

Figure E.1 **Economy–wide impacts**

MM600+ model projections: change from base case in the long run



Data source: Econtech (2003).

Table E.2 **Economy wide effects of post 2005 assistance options**

Model projections: percentage deviation from base case in the long run

	Tariff cuts	*SIP removal*	*Tariff cuts and SIP removal*	
	MM600+	*MM600+*	*MM600+*	*MONASH*
Real GDP	0.03	0.01	0.04	0.00
Real Consumption	0.0	0.0	0.0	-0.01
Real Investment	0.0	0.0	0.0	-0.01
Export volumes	0.6	0.1	0.8	0.07
Import volumes	0.5	0.1	0.6	0.07
Consumer price index	-0.1	0.1	0.0	0.00
Exchange rate	-0.2	-0.1	-0.2	-0.05
Real after tax wage rate	0.0	0.0	0.0	0.00

Source: Econtech (2003) and CoPS (2003).

That the economy–wide impacts would be very small is supported in modelling undertaken independently by ACIL-Tasman using a version of the GTAP model and an analysis of the Commission's preliminary preferred assistance option by the Victorian Department of Treasury and Finance using a version of the MONASH model. In both the ACIL-Tasman and the Victorian Department of Treasury and Finance studies, the projected small allocative efficiency gains for the Australian economy associated with a reduction in TCF assistance, lie between the projections of the MM600+ and MONASH models. Specifically, the Victorian Department of Treasury and Finance reported that the Commission's preliminary preferred TCF assistance option would result in a small allocative efficiency gain of 0.01 per cent.

As in the MM600+ and MONASH models, these projected gains are at least partially offset by small terms of trade losses.[3]

The relative contribution of allocative efficiency gains and terms of trade effects differs between the models for several reasons:

- The need, for computational reasons, to restrict the number of commodities and to assign relatively small export demand elasticities (or import substitution elasticities in multi-country models), may reduce projected allocative efficiency gains and increase terms of trade losses, respectively. This means that the gains to Australia from reductions in TCF assistance may be higher than projected by models such as MONASH or GTAP. Econtech (2003) shows that increased commodity disaggregation results in greater projected allocative efficiency gains, and justifies the use of higher export demand elasticities (or import substitution elasticities in multi-country models), at least in the long run, thereby reducing projected terms of trade costs.
- In the version of the MONASH model used by CoPS, there is an annual updating of the base case to include underlying trends such as improvements in labour productivity and reductions in the local firms' share of the domestic TCF market. This means that TCF output and employment are smaller in the long run in the MONASH model than in the MM600+ and ACIL-Tasman models. Hence, the projected allocative efficiency effects of policy changes are also lower. Further, assumed lower substitutability between domestic and imported TCF products in the MONASH and ACIL-Tasman models means that for a given fall in the relative price of TCF imports, the increase in import volumes tends to be smaller than in the MM600+ model.

Impacts of assistance reductions on the TCF industry

Table E.3 presents the projected long run effects of the modelled assistance options on output in the TCF sector, under the MM600+ and MONASH models. With a reduction in TCF tariffs to 5 per cent and an elimination of SIP funding, TCF production is projected by Econtech to be 15 per cent lower and by CoPS to be 4 per cent lower, than would otherwise be the case in the long run. Using a different version of the MONASH model, the Victorian Department of Treasury and Finance

[3] The results presented by ACIL-Tasman are not directly comparable with those generated by the MM600+ and MONASH models because the ACIL-Tasman base case assumes that tariffs are retained at current levels rather than the legislated 2005 levels. Nevertheless, a comparison of ACIL-Tasman's 'accelerated tariff reduction' scenario (which assumes tariffs on apparel and textiles are reduced to 5 per cent by 2015) with its 'business as usual' scenario, provides a basis for comparison with the MONASH and MM600+ model projections.

projected that the Commission's preliminary preferred TCF assistance option would similarly reduce TCF production by around 4 per cent.[4]

Table E.3 **Effects of post 2005 assistance reductions on TCF activity**

Model projections: percentage deviation of output from base case in the long run

	Tariff cuts	*SIP removal*	*Tariff cuts and SIP removal*	
	MM600+	*MM600+*	*MM600+*	*MONASH*
Textile fibres, yarns & woven fabrics	-6.7	-8.1	-14.4	-3.9
Textile products	-1.2	-2.3	-3.5	-2.7
Knitting mill products	-19.3	-3.7	-22.5	-5.7
Clothing	-19.8	-3.2	-22.9	-4.3
Footwear	-2.1	-2.2	-4.2	-8.4
Leather & leather products	-0.1	-3.1	-3.2	-1.9
TCF total	-10.5	-4.5	-14.8	-3.5

Source: Econtech (2003) and CoPS (2003).

The reduction in sectoral production reflects both a loss in domestic market share of finished TCF products and a reduction in exports (see figure E.2). These changes arise because the price of TCF products available from overseas suppliers falls relative to locally produced substitutes — reducing TCF tariffs directly lowers the price of imported TCF products while eliminating SIP funding effectively raises the price of locally produced items. In turn, lower output of finished TCF products reduces demand for intermediate products such as yarns and textiles, reinforcing the overall decline in sectoral output. In the MM600+ results, the projected declines in production are largest in the clothing, knitting mill products and textiles industries. In the MONASH results, footwear, knitting mill products and clothing are the most affected industries. The variations in the degree of projected contraction between industries arise from differences in:

- current assistance levels afforded to individual TCF industries and hence, the extent of the reductions involved in moving to a 5 per cent tariff level and abolishing SIP funding[5]; and

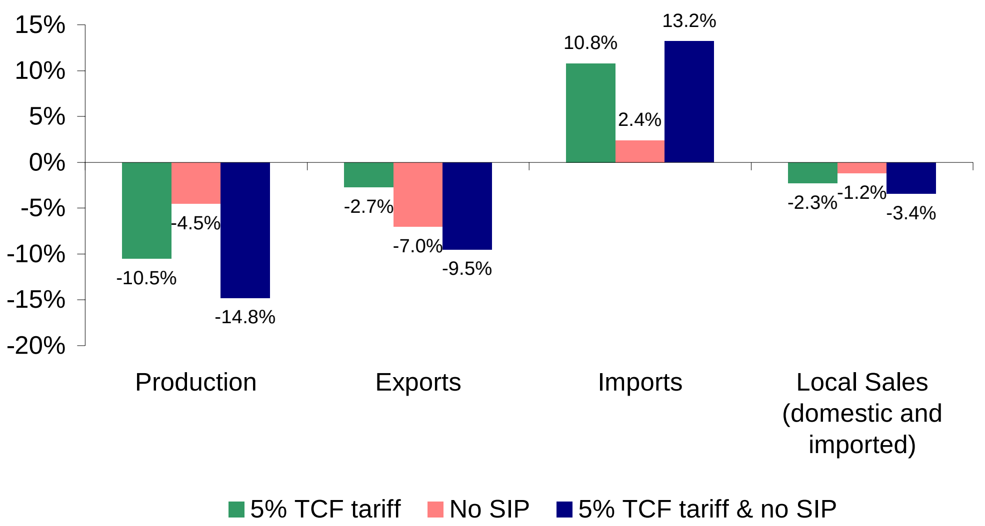
[4] Details of the in-house modelling undertaken by the Victorian Government are not reported in its submission. However, it is likely that the base case in the version of the MONASH model used may be slightly different from that used by CoPS, due to differences in historical updates and forecast procedures.

[5] SIP funding to date has been concentrated in the more capital intensive sectors of textile fibres, yarns and woven fabrics manufacturing (see table E.1). Hence the removal of SIP initially affects mainly intermediate products, with flow on impacts to downstream TCF producers. For example, the domestic clothing industry uses about 40 per cent of the combined output of the textile fibres, yarns and woven fabrics industries (ABS 2001a).

- the assumed substitutability between imported and domestic products in these industries (relatively high for textile fibres and yarns, and knitting mill products, but relatively low for textile products, and leather and leather products).

Figure E.2 **Changes in the composition of TCF activity** [a]

MM600+ model projections: percentage deviation from base case in the long run



a All activity components include both intermediate and final products. *Data source:* Econtech (2003).

Consistent with the decline in TCF production, employment in the sector is projected in the MM600+ and MONASH models to be 15 and 4 per cent lower, respectively, than in the base case in the long run (see table E.4). From the MM600+ model, this would correspond to a reduction of around 9600 in the TCF workforce, with the largest reductions projected to occur in the clothing, knitting mill products and textiles industries.

With its lower import substitution elasticities and smaller base case TCF sector, the projected employment impacts in the MONASH model are much lower. Specifically, the MONASH results suggest that a reduction in tariffs to 5 per cent and the removal of SIP funding could reduce the TCF workforce by around 1590 jobs, relative to the base case, in 2010, easing to a loss of 1080 jobs in the long run. The largest projected decline occurs in the footwear industry because of a comparatively high degree of substitutability assumed between imported and locally produced footwear.

Notably, the projected reductions in TCF employment are small compared with declines that have occurred in the sector's workforce in recent years. They are also likely to be smaller than future reductions in employment that will inevitably occur in response to the global competitive pressures confronting TCF producers in all developed countries (refer to chapters 2 and 3 of this report).

Table E.4 **Effects of post 2005 assistance reductions on TCF employment**
Model projections: deviation of employment from base case in the long run

	Tariff cuts	*SIP removal*	*Tariff cuts and SIP removal*			
	MM600+	*MM600+*	*MM600+*		*MONASH*	
	Number of jobs	*Number of jobs*	*Number of jobs*	*%*	*Number of jobs*	*%*
Textile fibres, yarns & woven fabrics	-1074	-1285	-2292	-14.4		-3.6
Textile products	-131	-253	-384	-3.5		-2.6
Knitting mill products	-1138	-216	-1325	-22.5		-5.4
Clothing	-4532	-737	-5247	-22.9		-4.0
Footwear	-114	-119	-225	-4.2		-8.0
Leather & leather products	-4	-87	-90	-3.2		-1.9
TCF total [a]	-6993	-2697	-9563	-15.0	-1080	-3.6

[a] While the effects on activity and employment for individual TCF industries are approximately equivalent, the effects on total TCF employment differ slightly from the effects on total TCF production because of different weights used to aggregate the individual industries to the totals. *Sources*: Econtech (2003) and CoPS (2003)

Moreover, the projected impacts of assistance reductions on sectoral output and employment may be unduly pessimistic because neither model is able to allow for the likelihood that assistance reductions will reinforce the incentives for firms to innovate, improve quality and productivity, and reduce production costs. Nor does the modelling allow for the possibility that further rationalisation of TCF activity may raise the output of individual producers, thereby generating productivity improvements through economies of scale. The exclusion of these effects means that the results presented here may overstate the adjustment pressure on the sector and TCF dependent regions that will arise from post 2005 assistance reductions.

Wider industry and regional impacts

Industries projected in both the MM600+ and MONASH model results to benefit from reductions in assistance to the TCF sector include:

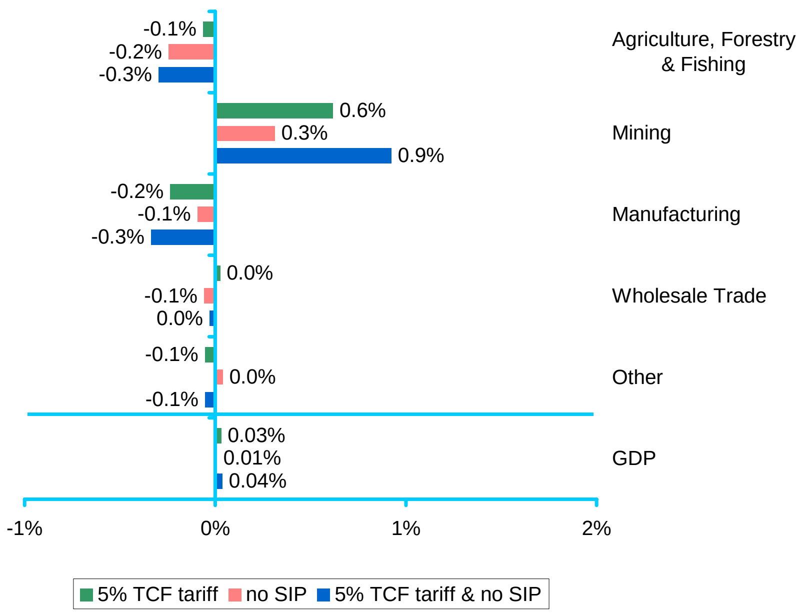
- Export industries, particularly those that are capital intensive, such as mining. These industries are well positioned to benefit from the projected small decline in capital costs (relative to wages) and the depreciation in the Australian dollar.
- Industries that purchase TCF products as inputs, including the furniture and hospitality industries. These industries benefit from the lower prices for TCF products as a result of tariff reductions.

- Industries such as retail and wholesale trade that benefit from increased activity stimulated by the tariff reductions.

Apart from the TCF sector itself, industries that may be adversely affected by a reduction in TCF assistance are those which provide inputs to the sector and, to a lesser extent, labour intensive activities in the services sector. Notably, the projections suggest that a decline in TCF output would reduce the sector's demand for inputs from agricultural industries such as cotton, wool and livestock hides. However, the Victorian Farmers Federation (submission PP152) and the Commonwealth Department of Agriculture, Fisheries and Forestry (submission PP176) argued that overall, a reduction in TCF assistance could be expected to have a positive impact on agricultural production. Specifically, they noted that as production in Australia's cotton, wool and livestock hides industries is largely determined by international demand and prices, the positive effects on agricultural production of the small projected depreciation in the Australian dollar are likely to outweigh any reduction in domestic TCF demand for agricultural inputs. A decomposition of the industry impacts projected by the MM600+ model is presented in figure E.3.

Figure E.3 **Effects on the output of selected industries**

MM600+ model projections: percentage deviation from base case in the long run

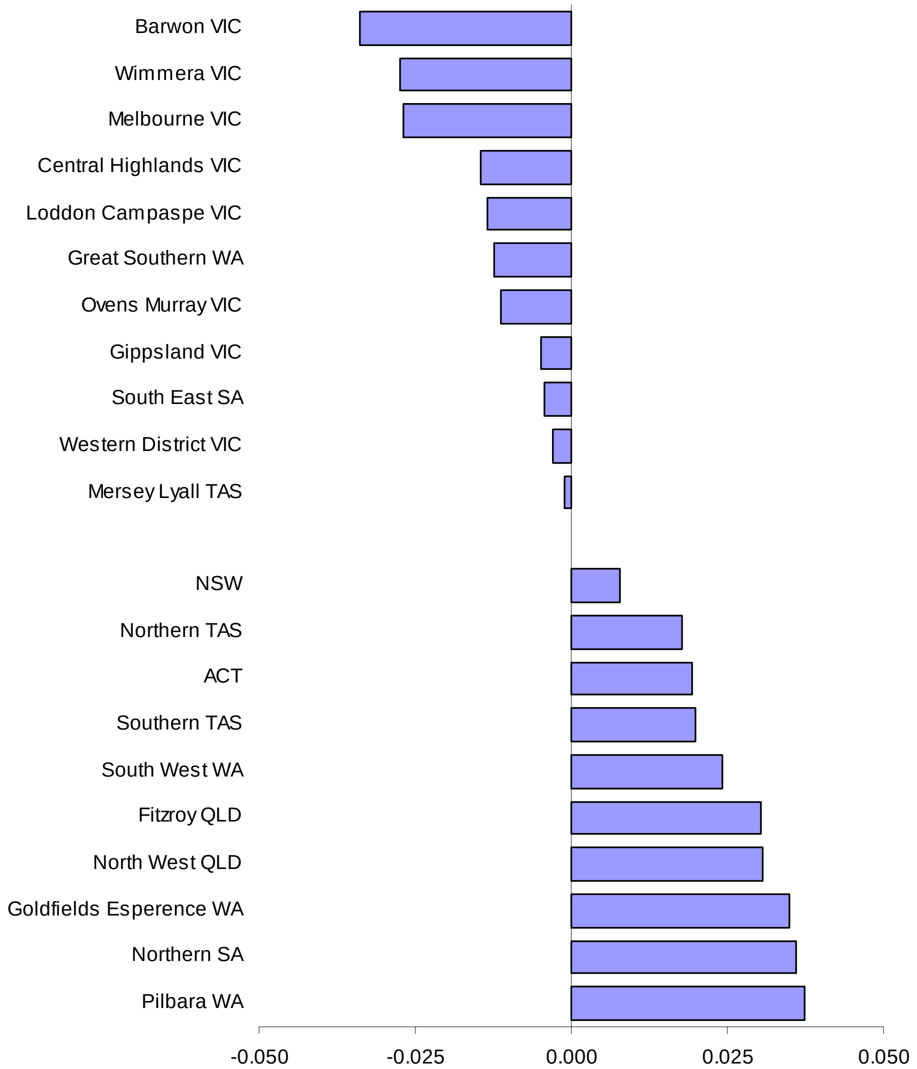


Data source: Econtech (2003).

At the regional level also, the MM600+ and MONASH model results are very similar. They indicate that the employment effects of reducing TCF assistance would generally be small (see figure E.4), particularly in light of recent strong employment growth in many of the regions where TCF activity is located (see chapter 4).

Figure E.4 **Employment effects for selected regions**[a]

MONASH model projections: percentage deviation from base case in long run



a The numerical TCF employment changes associated with the projected percentage deviations may be comparatively small for some statistical divisions (for example in the Wimmera) and comparatively large in other regions (for example in NSW). *Data source:* CoPS (2003).

Axiomatically, the regions most adversely affected by a reduction in TCF assistance are those where TCF industries are located. The greatest declines (albeit small) in total activity are expected to occur in Victoria. Output in that State is projected by the MM600+ model to be around 0.3 per cent lower, which translates to a loss of around 7800 TCF and non-TCF jobs in the long run. With its lower import substitution elasticities and smaller base case TCF sector, the MONASH model projects a much smaller employment loss for Victoria of 0.02 per cent in the long run, or about 460 TCF and non-TCF jobs. This is consistent with MONASH model projections reported by the Victorian Government indicating that implementation of the Commission's preliminary preferred assistance option would reduce Victoria's gross state product by 0.02 per cent. At the statistical division level, Barwon (with its regional centre being Geelong) and Melbourne are projected to incur the greatest reductions in employment.

However, these projected effects may be an underestimate of the immediate employment consequences for particular regions of lower TCF assistance. This is because the MM600+ and MONASH models are unable to adequately capture the lumpy adjustment that often occurs in response to assistance reductions. In the models, output and employment of regional industries move in line with the economy–wide outcomes, subject to restrictions on which products are traded between regions. In reality, adjustment through firm closures will mean that the impacts on regions may be more variable.

An estimate of the regional employment effects of a reduction in TCF assistance was provided to the Victorian Government by the NIEIR. The NIEIR work suggests that implementation of the legislated 2005 tariff reductions and the Commission's preliminary preferred option for post 2005 assistance, would lead to a total job loss in Victoria of 19 600 — 6300 of which would be in the TCF sector. When adjusted to remove the effects of the legislated 2005 tariff cuts, projected job losses in the TCF sector decline to around 4000 post 2005, with a total reduction of around 12 000 direct and indirect jobs in Victoria. The largest losses are projected to occur in the Yarra, Whittlesea, Whitehorse and Greater Geelong areas. At a State level, the TCF employment changes projected by the NIEIR are higher than those projected by the MONASH model (as reported by both CoPS and the Victorian Department of Treasury and Finance) but lower than the MM600+ model projections.[6]

While little detail has been provided to the Commission on the models used by NIEIR and no industry results are presented other than for the TCF sector, the results do not appear to incorporate any positive flow–on effects for either the TCF sector or for non-TCF industries. The studies by Econtech, CoPS and the Victorian Department of Treasury and Finance indicate that TCF assistance reductions would provide benefits to Victorian industries and consumers through a more efficient

6 While the NIEIR does not report its assumptions about changes in TCF output and employment in the absence of a policy change, the use of input-output tables as a basis for its approach suggests that its results are likely to be more comparable to the static approach taken in the MM600+ model than to the MONASH model (which allows, in its base case, for the TCF sector to continue to contract over time as a result of broader competitive pressures).

allocation of resources and TCF price reductions. Indeed, the Victorian Department of Treasury and Finance modelling suggests that the overall impact on state employment is likely to be very small, particularly in the context of general growth in that State's employment base.

Modelling of regional impacts was also undertaken by the Centre for Sustainable Regional Communities for several local government authorities. These projections use regional multipliers to estimate the effects of TCF job reductions — whether due to assistance reductions or more general competitive pressures. For the Wangaratta region, which has a TCF workforce of 785 persons, a loss of 100 TCF jobs was projected to reduce the value of the sector's output by around 14 per cent. Flow-on effects to other industries (principally agricultural, wholesale and retail trade industries) were estimated to result in the loss of a further 70 jobs, with offsetting gains in the region of 5 jobs in TCF user industries as a result of lower prices for TCF inputs.

Less detailed results were provided to the Commission for modelling by the Centre of the impacts of TCF assistance reductions in the regions encompassed by the Bendigo and Western Region Councils Forum.[7] In the Greater Bendigo economy, the TCF sector directly employs nearly 500 people and contributes almost $100 million to regional turnover. Loss from the region of the entire TCF sector and all businesses which indirectly rely on the sector was projected to reduce employment by 1300 jobs, with a corresponding reduction in regional output of nearly $200 million. Similarly, in the western region of Melbourne, loss of the entire TCF sector was projected to result in direct employment losses of over 1900 persons with an additional 3400 jobs lost in other sectors in the region and an associated reduction in gross regional output of $370 million.

While providing an indication of the potential magnitudes of first round effects of a reduction in TCF activity in the regions concerned, the projections for the Greater Bendigo and Western Region Councils Forum do not allow for the positive regional effects associated with lower prices for TCF products for consumers and user industries (including within the TCF sector). Also not captured in the Centre's projections of regional output effects is that some of those workers who lose jobs in the TCF sector will find employment in other sectors. Welfare payments and access to employee entitlements will act to further cushion declines in regional output.

[7] The Western Region Councils Forum is a partnership of the local government areas of Brimbank, Hobsons Bay, Maribyrnong, Melton, Moonee Valley and Wyndham.

Estimated adjustment costs

The Econtech, ACIL-Tasman and the Victorian Department of Treasury and Finance modelling do not capture any of the potential adjustment costs associated with a reduction in TCF assistance. However, using MONASH model projections, CoPS (2003) provided an estimate of two aspects of adjustment costs — the loss of labour input through unemployment and retraining costs. In deriving an estimate for the latter, CoPS assume that training costs for displaced TCF workers are equivalent to 0.25 of a labour year per person.

Under the assumption that aggregate employment is unchanged from the base case, such adjustment costs associated with a reduction in TCF assistance are projected to be very small, reducing aggregate economic welfare by an estimated $2.5 million. Under the alternative assumption that wage rates adjust slowly in the short term, economy–wide employment is projected to fall in the short term by around 0.03 per cent, or 2700 jobs. As a result of this additional unemployment in the economy and the associated lost productivity and retraining costs, projected adjustment costs increase to around $100 million.

However, the reductions in aggregate employment underlying these projected adjustment costs are small relative to employment growth that has recently been observed in many of the regions where TCF activity is located (see chapter 4). Equally, it is important to recognise that there may be other adjustment costs associated with a reduction in assistance — for example, relocation costs and costs associated with a premature scrapping of capital — which the above estimates do not capture.

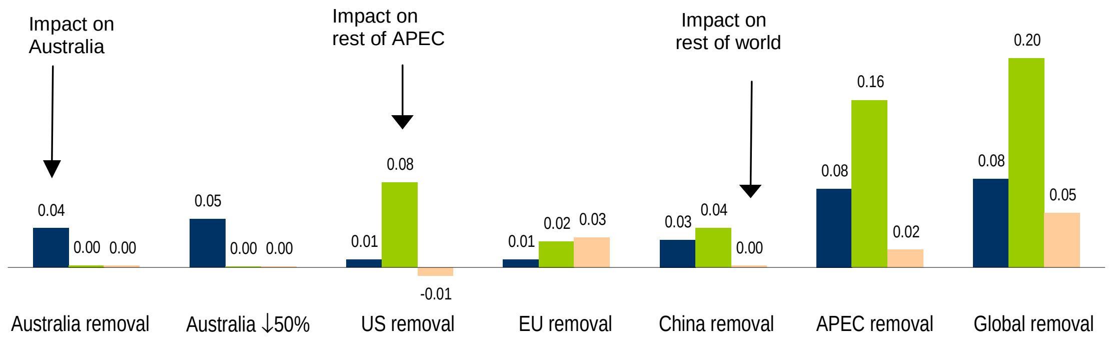
E.3 Effects of international developments in assistance on Australia

Results from a GTAP analysis by the CIE (2003) of alternative scenarios for reductions in assistance to TCF industries in Australia and other countries, are summarised in figure E.5. As in the MM600+ and MONASH studies, these projections suggest that the gains to Australia from a unilateral reduction in TCF tariffs would be small, with an increase in real income of less than 0.05 per cent in the long run.[8]

[8] While this projected gain to Australia is marginally above the projections of the MM600+ and MONASH models, it should be noted that the comparatively higher level of tariffs in the GTAP base case combined with a simulated complete removal of tariffs, means that the modelled tariff reduction in GTAP is substantially greater than that in the MM600+ and MONASH models.

Figure E.5 **Impact of international TCF assistance reductions**

GTAP model projections: percentage change in real income from base case



Data source: CIE (2003).

Though small, the overall benefits to Australia from a unilateral removal of its TCF tariffs are projected to exceed the benefits that Australia would receive from a unilateral reduction of protection in other countries (the US, the EU or China). The principal reason for this is that Australia is a net importer of TCF products and most of these imports are final products. Hence, although liberalisation in other countries may reduce the price that Australia pays for its TCF imports (and provide some benefits to consumers of these products), it is not expected to generate any significant allocative efficiency improvements within the economy. For Australia, the largest projected gains from TCF assistance reductions in other countries come through collective liberalisation in the APEC region, with little additional benefit from liberalisation in a wider group of countries.[9]

While providing small benefits for Australia as a whole, unilateral liberalisation of TCF assistance in the US, the EU, China and APEC are all projected to have a very small dampening effect on the Australian TCF sector. In the cases of liberalisation by the US and the EU for example, current barriers to imports of Australian TCF products are low compared with those on products from Asian countries. Hence, a general reduction in restrictions enables other countries to displace Australia in those markets. The ACIL-Tasman study similarly projected a small negative impact on Australia's clothing, footwear and leather products industries from the prospective removal of Multi Fibre Agreement quotas in 2005.

The CIE projections indicate that the least adverse result for Australia's TCF sector would come from a unilateral removal of TCF protection in the US. Unilateral removal by the US would provide small benefits to the Australian textiles and

[9] However, GTAP projections reported in Productivity Commission (2002b) indicate that there are likely to be substantial benefits for Australia if liberalisation extends to all other industries and occurs globally.

leather industries from higher demand by final good producers in countries such as China which would have better access to the US market. However, such liberalisation would also lower the price of clothing on the world market leading to a projected contraction in the Australian clothing industry. Indeed, under all of the liberalisation scenarios considered by the CIE, output of Australia's clothing and footwear industry is projected to fall.

E.4 Summary of modelling outcomes

Overall, the quantitative analyses presented above suggest that the economy–wide impacts of TCF tariff reductions in Australia and the abolition of SIP funding would be very small. This is because the TCF sector is a comparatively small component of the Australian economy and because assistance afforded the sector is much lower than in the past. While the models differ over whether there would be a small gain or a small loss at the economy–wide level, very small orders of magnitude one way or the other are a feature of both the Commission sponsored studies by Econtech, CoPS and the CIE, and the independently conducted studies by ACIL-Tasman and the Victorian Department of Treasury and Finance.

The Commission did not explicitly model its preferred option for post 2005 TCF assistance reduction. However, the similarities between the modelling outcomes of the CoPS and Victorian Department of Treasury and Finance studies— which, in terms of tariff levels and post 2005 SIP support, did model the Commission's preferred option — indicate that there is little additional information to be gained from using long run general equilibrium type approaches to undertake further more detailed modelling of the timing of TCF assistance reductions.

The Econtech, CoPS and the Victorian Department of Treasury and Finance studies concur that some of the largest impacts of TCF assistance reductions will be evident in Victoria. Reflecting this, the other modelling studies (by the NIEIR and the Centre for Sustainable Regional Communities) focussed on regional impacts within Victoria. At a State level, the NIEIR projections for TCF employment losses are higher than those suggested by CoPS but below those suggested by the Econtech modelling. The Wangaratta study by the Centre for Sustainable Regional Communities indicates that flow–on effects of job losses in the TCF sector resulting from assistance reductions may be sizeable in some regions. Nevertheless, projected employment losses as a result of TCF assistance reductions are small compared with the employment growth observed recently in many regions where TCF activity is located.

Finally, the CIE and ACIL-Tasman studies indicate that gains to Australia from TCF liberalisation in other countries are likely to be at best, very small, with the possibility that such liberalisation may lead to reductions rather than increases in TCF sector output and employment. This projected outcome reinforces the notion that liberalisation in overseas markets will not be a panacea for the local TCF sector.

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