Forum

Floor Prices and Wool Promotion: Some Further Hidden Costs?

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This paper focuses on some emerging and recurring issues of wool promotion policy. In particular it examines the implications for wool promotion of recent developments in raw wool marketing policy. The issues analysed are the relationship between International Wool Secretariat (IWS) promotion and wool stockpiles held by statutory authorities, market development for wool, the integration of IWS activities with those of statutory wool marketing authorities and the future organization and control of IWS.

These issues are real and significant ones even if largely unsuspected by the majority of woolgrowers. Indeed, unless they are satisfactorily resolved, serious strains could arise within the partnership that forms the IWS. The eventual outcome could be the disintegration of a co-operative promotion programme, initiated forty-two years ago. Even if this does not happen, promotion funds may well be applied to inappropriate uses and the overall effectiveness of wool promotion substantially reduced. *Prima facie*, the introduction of a price stabilization programme for Australian wool in 1970 would not have been expected to have a major impact on the promotion programme except, perhaps, amongst those who believed that more stable auction prices would either greatly potentiate the promotion programme or render it redundant. It was not long, however, before a number of major interactions made themselves apparent.

Market Support by IWS Promotion

As the Australian Wool Commission's stockpile of wool, accumulated for price stabilization purposes, began to reach sizable proportions in 1971, there was talk of "neglected wools" and suggestions that IWS should re-orientate its promotion efforts so as to move into consumption those wools disproportionately represented in the stockpile.

There was some precedent for this. In 1967 the New Zealand Wool Board (NZWB) had practically exhausted its financial reserves and had built up sizable stocks of stronger wools by its single-handed support of the world price for these types. The IWS was asked to help strengthen the markets for coarser wools. At the time, New Zealand's partners were somewhat reluctant to depart from the long-established IWS policy of promoting wool generally and of not addressing promotion to the support of wools of specific type or national origin. However, in view of the plight of the NZWB, an exceptional departure from the standing policy was decided upon.

* For those who believe that where you stand on an issue depends on where you sit, the author confesses to having been an employee of the International Wool Secretariat for the last eight and a half years. He wishes to emphasize, however, that the opening *caveat* to the effect that the views expressed in this article are not necessarily shared or confessed by his employers, and/or colleagues, is, on this occasion, no mere formality.

The main actions taken to generate greater demand for stronger wools included an increase in allocations to carpet promotion and a number of product development programmes featuring items containing stronger wools. The German Branch launched a major product marketing programme for the "Country Look", promoting a range of men's wear and women's wear in rustic textures and colours.

IWS experience with these special measures to provide support for stronger wools would tend to cast doubt on the effectiveness of promotion as an instrument for offsetting or countering short term market disturbances. Certainly the pay-off period for most of the product development projects, undertaken to provide relief for stronger wools, was too long for their outcome to have relevance for that purpose. Moreover, the economics of maintaining a shelf of product developments, for use as and when necessary to provide selective support for certain classes of wool, would be extremely dubious. Not only would discounting of future returns tend to make such ventures relatively unattractive but modern competitive conditions in the fibre and textile industry strongly favour vigorous and early steps to exploit innovations, while you still have a lead on your competitors, rather than "mothballing" them for several years.

In the event, the upsurge in wool prices at the beginning of 1972 and the rapid disposal of the Australian Wool Commission's stocks temporarily eased pressures for IWS programmes for "neglected" wools. This issue began to simmer again, however, in 1975 with an increase in the stocks of wool purchased by the Australian Wool Corporation (AWC) and by mid-1977 strong pressures were being exerted for IWS to provide selective support for finer wools.

A view was expressed at that time that the size of the stockpile could be regarded as a measure of the effectiveness of promotion and that IWS's budgetary problems reflected its patent failure to dispose of, or to prevent the accretion of, burdensome stocks held by price stabilization authorities. This displayed, paradoxically, a refreshing faith in promotion. It implied that, by spending on promotion approximately 3 per cent of wool revenue, it ought to be possible to operate a buffer stock programme without buffer stocks. The proponents of this view would probably stop short, however, of accepting its corollary, namely that, if IWS could so easily establish promotion as a far cheaper method of stabilizing prices, the *raison d'etre* of buffer stock programmes would be placed in question.

Demands for IWS to shift the balance of promotional thrust towards the finer wools led in June, 1977, to a decision to "tilt" IWS operations for a two-year period in order to provide greater support for wools in the 19 to 23 micron range. The "tilt" was to be accomplished by shifting promotion expenditures from woollen to worsted fabrics, from knitwear of the Shetland and lambswool type to Botany/worsted spun products, and from end-use products containing stronger wools (blankets, hand knitting yarns, carpets, etc.), to categories of merchandise containing finer wools.

There are, however, a number of counter arguments. For example, manufacturers and retailers might well be mystified or unimpressed by the diversion of promotion funds away from currently fashionable merchandise and it should be noted that, fortunately for the survival of the wool industry, fashion can sometimes be influenced towards particular fibre types but can *not* be manipulated at will. Moreover, the favouring of particular processing routes, e.g., the worsted system in preference to the woollen system, could tend to remove from the market some of the products most difficult to simulate in synthetic fibres and contributing most to the glory of wool. The woollen industry is indeed a more significant user of Australian wools than is commonly appreciated and its use of noils (the by-product from topmaking) means that the worsted and woollen systems cannot be considered wholly independently of each other.

There are two major issues involved in the decision to "tilt" the balance of promotion for selective support of specific wool types. In the first place, should promotion activities be confined to those wools produced by IWS-member countries so as to deny support to wools from countries which contribute nothing to wool promotion funds? Secondly, should promotion activities be co-ordinated with the price stabilization programmes of IWS member countries by means of short-term adjustments in the trim of wool promotion programmes or is promotion more effectively directed at building the longer-term demand for wool? It is not intended in this paper to attempt a definitive analysis of these questions. However, a brief examination of some of the many considerations involved will demonstrate that the issues are by no means simple.

First, take the question whether the traditional policy of promoting wool in general without regard to its national origin should give way to an attempt to prevent leakage of wool promotion benefits to free-loaders. Denial of promotion benefits to non-contributors may not be feasible if the world market for wool works as well as is implicitly conceded when the effects of Australian and New Zealand reserve price schemes upon prices of other wools is recognized. Moreover, even if it were feasible to prevent others sharing in the additional demand created, a loss in total benefits from promotion might well be involved, sufficient to outweigh any gains accruing to IWS sponsors from an increased share. The Industries Assistance Commission suggested that the IWS partner countries succeed in extracting 70 cents for every dollar of benefit flowing to wool producers from promotion.[1] If this is correct, any reduction of more than 30 per cent in the aggregate effect of promotion on wool demand, due to the attempt to offload freeloaders, would leave the IWS partners worse off than if they retained current IWS policy.

Furthermore, the wool textile industry is not characterised by a high degree of vertical integration except to some extent in woollen mills. Weavers are usually, therefore, unaware of the precise national source of the wool in yarns purchased and garment makers may have even less idea of the origin of the wool content in their fabrics. Top makers often blend wools from different sources to produce a standard product. In these circumstances any attempt to make promotional support conditional upon the use, at first processing stage, of certain raw wool suppliers could misfire. Also while IWS could, conceivably, withhold support from those countries or merchandise categories, which utilize raw wool from non-IWS countries, this might often involve withdrawal from markets offering a relatively high marginal response to promotion expenditures.

[1] Industries Assistance Commission (1976), *Financing Promotion of Rural Products*, Canberra, p. 53.

The second question involved is whether IWS should try to channel its activities towards those specific wool types in oversupply at the prices set by marketing authorities in woolgrowing countries. It may seem logical enough, *prima facie*, that wool promotion should be thus co-ordinated with price stabilization programmes. It is difficult though to know whether wools are "neglected" because they have been overpriced by the price stabilization authority, in which case an adjustment in the reserve price *bareme* or schedule might well be a better means of correcting an imbalance in stock holdings. Even if this is not so, there is something to be said for the view that the reserve price authority should be prepared to hold stocks until a period of more buoyant demand and should not expect promotion to bring about a more or less instant transformation of demand relationships as and when required.

In any case, it is doubtful whether promotion can be used effectively to support the market for particular types, which happen to be suffering a weakness in demand. The operation of the market suggests a reasonably high elasticity of substitution between types in the medium term and the substitution possibilities may currently be increasing as a result of technological developments in blending wool with other fibres. Practically identical blended products can be made from a wide range of wool types, provided appropriate adjustments are made in the diameter of synthetic fibres used.

It is likely that smaller responses per dollar, in terms of the increase brought about in aggregate wool demand, will generally be obtained from promotion programmes directed at relieving temporary stresses in the price stabilization scheme.

One special programme for selective promotion of specific wool types is the Merino Extrafine Wool (MEW) project, launched by IWS in 1978 to generate demand for products containing wools in the 16 to 19.5 micron categories. These wools were heavily overrepresented in the AWC stockpile partly as a result of fashion swings, the decline of the bespoke tailoring trade and heavy supplies of "hunger fine" wool due to drought. IWS was called upon to run a special promotion for this quite diverse group of wools with a modest advertising budget financed separately from the main IWS operation.

The MEW programme is already being regarded as a model for other such programmes, linking IWS more closely with the activities of the Wool Boards/Corporations (B/Cs). One danger in the proliferation of such specific programmes is that their full opportunity costs might not be readily apparent. These programmes make substantial demands on the time of senior marketing executives and fabric development staff, not, perhaps, to the extent that the main body of wools are neglected but certainly to the point where it is becoming apparent that only a limited number of such programmes can be undertaken concurrently without substantial increases in product marketing staff and research and development resources.

There is also the possibility that too many such ventures could undermine the unity and effectiveness of IWS operations, based traditionally on the principle that there should be no IWS logos or stylized scripts implying superiority to the Woolmark (in IWS jargon no "Golden Woolmarks") and that wool promotion funds should not be dissipated on short-lived projects from which no lasting equity is established.

Market Development

Another area in which raw wool marketing activities have had spillover effects upon promotion is market development. Thus the Wool Industry Act of 1972 empowers the AWC to undertake "market development" for Australian wools. Market development can be, and has been, interpreted rather widely. It encompasses efforts to open up new markets or to expand existing ones by such means as the location of stocks at convenient overseas sites for prompt delivery to processors, the sale of wool on special terms and joint ventures with processors, or special arrangements for the supply and conversion of wool to tops or yarn for sale in particular countries. It has also been interpreted to include promotion-type activities (including special product marketing programmes such as the current wool-minority blends programme of the AWC in the United States) and the provision of supporting technical and marketing services to wool users. In this sense, market development subsumes promotion and immediately establishes a need to define respective jurisdictions of organizations charged primarily with price stabilization on the one hand and wool promotion on the other. These problems are far from being resolved.

One outcome has been that product marketing programmes have been imposed upon IWS, with a resulting diversion of funds and personnel, from projects preferred by the IWS branch concerned, to those projects represented as necessary to serve the market development objectives of the B/Cs. This was the case for the Celsius 21 programme for all-season men's suits of wool-synthetic blended fabric, carried out in the United States at the request of the AWC. (The current promotion of wool-minority blends, in the United States of America, however, is being carried out independently and at its own expense by the AWC.) Whatever the arrangements for financing them, such programmes can give rise to problems. The two main areas of conflict to date have concerned activities in developing countries and policy with respect to the promotion of wool-poor blends (or wool-rich blends in those end-uses for which IWS policy is to promote pure new wool products only).

With regard to blends, IWS is sometimes represented as clinging obstinately to an outmoded emphasis on pure new wool or wool-rich products, despite an alleged large increase in the share of wool consumption accounted for by blends containing a minority of wool. The argument comes close occasionally to an assertion that wool-poor blends should be promoted by IWS simply because they are, or will be, there. It is, however, by no means certain that aggregate wool demand will be increased by switching promotion funds to wool-poor blends. For many end-uses the incorporation of small quantities of wool in a blend does not noticeably affect the comfort or aesthetic properties of the fabric. An "a little wool goes a long way" theme would be misleading the consumer in these cases. Often the motivation for blending is simply to gain consumer appeal by exploiting the popularity of natural fibres and including the word "wool" in the fibre-content label. Wool-poor blends tend, moreover, to be downmarket products sold in a very price-competitive sector. It is doubtful whether wool's long-term interests would best be served by using promotion funds to move more wool into those end-uses most subject to fibre substitution on price grounds.

In any case, any projected major increase in the proportion of wool used in wool-poor blends is open to argument. There has been in a number of countries some growth in this sector during the last decade but this is by no means certain to continue. Moreover, the statistics need careful interpretation.

Even though the share of wool consumption, accounted for by wool-poor blends, is as high as 17 or 18 per cent in some countries, much of this consists of the long established 55 per cent polyester/45 per cent wool fabrics for men's and women's outerwear. The situation also varies widely between countries. 1977 figures for the eight largest wool consuming countries of the West were: United States of America 9 per cent; United Kingdom 9; France 18; Germany 16; Japan 9; Italy 12; Netherlands 5 and Belgium 17 per cent.

Similar differences in projection and interpretation of statistics surround claims that the developed countries will account for a continually declining share of wool consumption and that both centrally-planned economies and developing countries will take a substantially larger share. Even if mill consumption rather than final consumer usage is being discussed, this is by no means beyond dispute. The centrally planned economies are increasing their synthetic fibre production and, because of payments difficulties, may be less willing, in future, to allocate foreign currency to wool imports.

As far as the developing countries are concerned, a protectionist climate is currently being fostered by relatively high levels of unemployment and by problems of controlling inflation. The latter inhibit the generation of alternative employment opportunities. Protectionist measures can be expected to persist for some years in developed countries and to limit the growth of their import trade in textile products.

There is also an undoubted tendency for developments in textile machinery to make the textile industry a more capital-intensive, high-technology industry. The same trend is beginning to occur in garment making. Countries with a sophisticated labour force and well-developed industrial infrastructure generally manage to operate modern textile equipment more productively than less developed countries.

As a result, the balance of comparative advantage may, in future, move towards the developed countries, reversing the tendency of the last fifteen to twenty years, when wage equality for women and minority groups and more varied employment opportunities for the class of labour traditionally employed, have favoured the establishment of textile and apparel manufacture in low-wage countries. Raoul Verret, President of Werner International is one authority predicting a long-run trend towards improvement in the competitive position of developed countries by virtue of their greater ability to maintain and run sophisticated machinery.[2] Political and exchange rate instability may also discourage future foreign investment in developing countries.

Nevertheless IWS often encounters criticism that it is devoting an excessive proportion of its resources to maintaining and expanding markets in developed countries and receives suggestions that it should provide more support for developing countries wishing to develop an export trade in textiles.

These pressures are not infrequently accompanied by optimistic claims of large potential outlets for wool in developing countries and by predictions of a coming shortage of processing capacity for wool in the developed countries. The vision of the future implied is that technological progress towards high-

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[2] Raoul Verret (1975), "Capital Investment May Lead to Leadership, Mere Survival or Bankruptcy", *IFCATI*, Vol. 16, pp. 13–23.

speed machinery and the longer production runs necessary to utilize expensive machinery economically, will tend to drive wool out as a textile fibre in developed countries and that its future survival will depend increasingly on getting it processed in low-wage countries.

IWS responses to suggestions that it revise its geographical allocation of funds to take account of these factors often sound something like the Pope protesting that he is already a Catholic. IWS has active branches in Korea, Taiwan, Hong Kong, India, Iran, and Turkey and offices providing quality control on Woolmark products for export and technical service to licensees, in Mexico, Mauritius and Uruguay. It extends similar services to a number of other developing countries from neighbouring IWS branches. It devotes, moreover, a lot of effort to international promotions to help market wool products from developing countries and to upgrading the fashion appeal of the merchandise involved.

It needs to be remembered that IWS has no charter to dispense woolgrower funds as economic aid to developing countries or to subsidize textile production. There would be no lack of entrepreneurs willing to produce wool merchandise if they did not themselves have to invest in establishing distribution channels but could simply produce and let IWS provide the facilities and do all the legwork necessary to sell the output. In addition the reaction of wool-users in developed countries to discriminatory treatment of this kind should, perhaps, not be overlooked.

Enough has been said, however, to indicate that the overseas market development initiatives of woolgrowing country marketing authorities have had an impact upon promotion and to question whether the optimal reconciliation of activities is likely to be achieved, if the B/Cs place overriding values on their market development objectives and impose these on the promotion programme.

Integration

Potentially by far the most significant impact of the B/Cs' market development initiatives upon wool promotion activities could come from proposals for what has been termed "integrated marketing" but which would more accurately be described as "integrated promotion", that is to say, the linking of IWS promotions to support directly the selling efforts of raw wool marketing bodies in the IWS-member countries. The ideas canvassed range from package deals (in which, in effect, a slice of the IWS budget would be offered with every bale sold under market development programmes) to arrangements enabling the B/Cs to sell wool into IWS product marketing programmes. The latter proposal implies limiting promotional support to products containing wool of specified origin and, perhaps, even requiring, as a condition of eligibility for promotional assistance, that processors purchase intermediate wool products from specified suppliers.

It has been contended that such arrangements would bring wool promotion and marketing more into line with practice in synthetic fibre distribution and would represent a movement towards fully integrated promotion exerting pressure on demand at all points along the pipeline. The IWS, it has been claimed, is currently giving insufficient attention in its promotion efforts to early stage processors and too much to consumers and to the later stages of textile and apparel manufacturing and distribution.

A more extreme form of vertical integration is suggested from time to time. The IWS is urged to investigate an alternative approach to demand building. Instead of traditional promotion operations, the argument runs, the IWS should consider the use of its budget allocation each year to purchase a little of the factory and the shop. After a number of years enough of the industry and distributive trade could be controlled to be able to influence fibre-choice decisions directly.

This proposal reveals a lack of quantitative perspective. The oft-lamented fact that only a few per cent of the price of, say, a man's suit accrues to the woolgrower indicates not that there are quick profits, or a lack of competition, in textile and clothing manufacture and distribution but simply that there is a great deal more employment and investment there than in the woolgrowing industry itself. Even if IWS's budget were exclusively devoted for, say, fifty years to the takeover of the apparel industry, the proportion of fibre usage controlled in this way would be very small. One would, moreover, hesitate to counsel such a massive investment by growers in such an uncertain enterprise.

The less ambitious concept of integration, *viz.*, merely linking IWS promotions with the market development activities or other selling efforts of the B/Cs, has, however, received most attention. On examination, a number of snags, originally unsuspected by its proponents, became apparent. Not least is the likelihood that the practice would invite attention under anti-trust legislation in some countries (possibly leading to loss of ownership and control of certification trade marks such as the Woolmark) and could adversely affect the taxation status of remittances from woolgrowing countries for promotion purposes.

Moreover, integrated promotion activities in support of specific wools might be excessively demanded by IWS-members, were the costs to be borne by the partnership as a whole (and hence only fractionally by the particular B/C responsible). Stresses on the partnership could occur if a gap between social and private marginal costs distorted the demand for promotions in support of wools of specific national origin.

A possible "second-best" solution would be that, if such integrated promotion/market development ventures had to be undertaken at all, their costs should be met by the individual B/C responsible and not from the common purse. Although encountering objections on the grounds that an additional impost for this purpose would allegedly be unacceptable to woolgrowers, this compromise has been adopted in some of the integrated marketing ventures actually undertaken by the B/Cs.

The whole question of integrated promotion tends to become linked with the quest for additional marketing powers for B/Cs. There is a temptation to ensure that experimental marketing ventures in, say, the United States have everything going for them even if promotional funds have to be diverted from other demand building activities of IWS.

Organization and Control

From a management viewpoint the issues posed above resolve into the question whether wool promotion should become, as it were, an extension of price stabilization and raw wool marketing in the four IWS member countries or continue as a joint operation addressed to the general aim of enlarging the global demand for wool.

While it is easy to assume uncritically that developments at the raw wool end should bring about radical changes in IWS's approach and thus permit improvements in the effectiveness of promotion, it is rather more difficult to be specific and to point convincingly to examples of what IWS should do differently. The mere facts that price variance at auction is somewhat reduced, that stocks are held in different hands than formerly and that certain other marketing functions are now performed by the B/C's instead of by the trade, does not, necessarily, mean that IWS's charter or mode of operation should be drastically revised.

The structure of the IWS Board may tend, perhaps, to encourage a preoccupation with raw wool marketing since it is made up almost wholly of representatives of the constituent B/Cs.

Given the emerging overlap and interactions of raw wool marketing and promotion, it would not be surprising if, in future, there were support for the merger or closer integration of IWS planning with that of the B/Cs. This need not go so far as advocating that IWS should orientate its activities to serve primarily the objectives of the B/Cs nor the adoption of a simplified planning nexus in which the B/Cs tell IWS what their objectives are and leave it to IWS to devise the means of achieving these objectives.

Even so, unless restraint were exercised, joint planning could tend to subordinate the established goals of the promotion programme to the pursuit of narrower, shorter term objectives including some for which promotion should properly not be regarded as a policy instrument.

A further consequence of such a trend might be the downgrading of the status of IWS management, if the organization were expected more and more to respond to the directives of chief executives and senior staff of B/Cs in the four IWS-member countries. For example, the use of meetings at staff level to merge, or handle concurrently, the planning process for IWS and the raw wool marketing authorities would, in effect, create a second-tier IWS Board and should not be entered into lightly.

Leaving aside the question whether the IWS ship can be conned from afar without loss of effectiveness, the position of the IWS Managing Director could become rather invidious. There could be a temptation to appoint as Managing Director a compliant individual prepared to divert promotion resources from demand building to supply support operations.

A tendency for management to respond more to the hobby-horses of IWS Board members than to its own perception of market needs and opportunities should be avoided as should a tendency for the IWS Board to go beyond the conventional role of a board and aspire itself to manage. This would represent a retrogression towards the earlier unsatisfactory system in which IWS had no managing director but was run by a triumvirate of representatives from the founder woolgrowing countries.

If governments and woolgrowers permitted such a development to proceed unchecked, they would have done much to ensure that the diminished effectiveness, perhaps even the demise, of the co-operative wool promotioc campaign would, in the future, be counted amongst the hidden costs of prine stabilization schemes.