



CANTERBURY CHAMBER OF COMMERCE

ECONOMIC BULLETIN

P.O. BOX 187 CHRISTCHURCH, NEW ZEALAND

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BULLETIN No. 577
3/1974

THE WOOL ACQUISITION CONTROVERSY

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A. INTRODUCTION

The most controversial topic in the wool industry over the last 5-10 years has been marketing reform, in particular the question of wool acquisition. Briefly, acquisition means the setting up by legislation of an authority to acquire compulsorily and market all New Zealand wool. Although there are many interpretations of precisely what functions the authority would undertake, the key proposal is that it assumes ownership of the wool at an early stage in the marketing process. Similar marketing reform schemes for wool have been under scrutiny in South Africa and Australia. However, in both these countries the agony seems over and action has been approved by the majority of those involved in the industry.

This paper is mainly concerned with outlining the cases for and against acquisition.

The first section provides background on the structure and organization of the wool industry in New Zealand and traces the recent progress of wool marketing and reform. The second section briefly describes the world textile market of which wool forms a relatively small part, examines the competitive position of wool in this market and outlines an ideal marketing system for wool within such a context.

The third section describes and comments on various wool market reform proposals and puts the case for non-acquisition, that is, the status quo, with minor variations.

B. BACKGROUND

1. *Structure and Organization of the New Zealand*

Wool Industry

Annual N.Z. wool production averages around 300,000-330,000 tonnes from about 60 million sheep. The present value of production is about \$400 million. There are about 38,000 wool growing farmers but wool and sheep meats are the major source of revenue for only about half the farmers.

Most New Zealand wool is of the coarser crossbred type mainly used for household or industrial purposes in contrast to finer Australian wools used mostly for apparel.

The sheep farmer has the option of two major avenues of disposal. He may sell at auction or to private buyers. About 80 per cent is auctioned (mostly in New Zealand but a little is shipped to the U.K.) and the remainder is sold to private buyers. These percentages do not include wool from sheep and lambs slaughtered in New Zealand (known as *slipe wool*) but disposed of

outside the auction system by freezing companies and amounting to about 0.3 million bales of a total clip of 2 million bales.

If the auction option is preferred the wool is delivered to brokers' stores at one of the eight wool selling centres. The broker's function is to prepare and display wool to best advantage for inspection by buyers (acting as agents for local and overseas users) who then bid for it at auction. Buyers pay for wool usually within 18 days of sale and brokers then pay net proceeds to farmers. Buyers may have wool scoured prior to overseas shipment. About 40 per cent of wool exported in 1972/3 had been scoured.

The New Zealand Wool Marketing Corporation which is the statutory Marketing Authority in the industry has a floor price scheme for wool under which it will buy in or supplement the price reached at auction up to a conservative level. The Corporation is also charged with improving the marketing system although as yet it has only made timid steps in reform.

The New Zealand Wool Board is the policy making body for producers. It is dominated by grower members who are elected by an Electoral Committee made up of 25 growers, in turn chosen on a district basis by farmers with 100 or more sheep. The electoral committee also elects grower members to the Meat Board.

On the buying and processing side the brokers and buyers each have an Association to represent their views. There are also a Wool Merchants' Federation and a Wool Scourers' Association.

2. *Marketing progress and reform*

A precedent for acquisition, albeit dubious, can be found in the primary produce inter-Governmental bulk purchase contracts of World War II. In the case of wool the New Zealand-United Kingdom contract covered the clip for the duration of the war and one clip thereafter. Prices paid were in general those ruling before the war. Because of the dislocation of normal trading conditions substantial stocks of U.K. Government owned wool had accumulated by the end of the war. To dispose of these stocks with minimum disturbance to future supplies the Governments of the United Kingdom, Australia, New Zealand and South Africa formed a private company called Joint Organization. Its New Zealand subsidiary was the New Zealand Wool Disposal Commission established under a 1945 Act. As well as disposing of the accumulated wool at auctions (which had recommenced after the war) the Commission established floor prices and was prepared to buy all

wool which did not reach these prices. By mid 1951 all New Zealand Joint Organization wool had been sold at a profit of around \$NZ40 million. In 1951 a new Wool Commission replaced the old. Its major function was to administer an expanded reserve price scheme. The reserve fund consisted of the Joint Organization profits plus \$13 million of industry funds. The Commission appraised all wool sold and set a floor price for each lot, at which it was prepared to buy in if not bought by a commercial buyer. (In 1967 a further support price procedure was added. Instead of buying itself, the Commission could supplement the auction price for wool bought by others up to the floor price. And in 1969 a third option was adopted to permit the Commission to buy in below the floor price.) Naturally the average floor price tended to be conservative. For example, in 1952 it averaged 24d compared with average auction realisations of 40d and in 1957 the corresponding figures were 30d and 55d.

It was not until the 1966/67 and 1967/68 seasons that, due to falling demand, the Commission was forced to buy or supplement substantial quantities of wool. In mid 1966 the Commission's capital was \$74 million. By November 1967 this was completely exhausted, the Commission meantime having had to buy in around 700,000 bales. In addition a further \$9 million borrowed from the Reserve Bank had been spent on supplementation. Subsequently although wool prices did not rise substantially until 1972-3 only about 20,000 bales had to be bought in by the Commission. All stocks had been disposed of by the end of 1972. From commencement in 1951 until the end of its operations in 1972 the Commission bought 835,000 bales and supplemented 987,000 bales at a cost of \$10 million out of a throughput of approximately 28 million bales.

Meantime back in 1964 the Wool Board and Wool Commission had set up a study group of wool motivated experts to examine the causes of wool price fluctuations, to seek their minimisation and to report on methods of wool marketing. The group presented its final report in November 1967. It recommended that an appraisal and purchase system be instituted under which all wool would be bought by an authority through existing channels. The Board and Commission then set up a "practical" group to examine the findings and to make further recommendations. Its Report of November 1968 rejected an acquisition authority but recommended lesser changes. Controversy on wool marketing was by this time at its height with wool prices at the lowest level for 20 years. After further discussion the Wool Board in December 1970 commissioned the Battelle Institute of Ohio, U.S.A. to make yet another detailed study of all aspects of the wool industry. The rationale was that a dispassionate objective study by an outside group was required. Its report became available in August 1971 and recommended major changes in the marketing system designed to reduce fragmentation and provide more centralised decision making. The Board and Government then set up the Wool Marketing Establishment Company to determine the most desirable form of marketing organization. After discussions in New Zealand and overseas the Company recommended a grower controlled Marketing Corporation which would acquire all shorn wool from July 1973 and other wools at a later date. The plan was approved by the Electoral Committee and the Meat & Wool Section Council of Federated Farmers. At this stage vocal groups of dissident farmers sprang up around the country and joined together to form the Wool Action Committee. As a result, legislation setting up the Cor-

poration was delayed because the Government considered wool grower support was not strong enough.

After some hesitation the Wool Board then proposed to Government that the acquisition clauses of the Bill be deferred pending a referendum of growers. Accordingly the Corporation, which also absorbed the Wool Commission, came into being in December 1972 but without the power of acquisition. Subsequently the Labour Party became the Government and repealed the referendum clause.

Nevertheless the advent of acquisition is still uncertain. The Corporation requires a 12 month planning period, a majority on the newly elected Electoral Committee do not support it, and the Wool Board has said that acquisition would come only with the approval of a clear majority of the latter Committee and the Meat & Wool Section of Federated Farmers .

C. AN IDEAL MARKETING SYSTEM FOR WOOL

1. *General*

The numerous proposals that have been put forward over the years for marketing reform can only be properly evaluated in terms of needs in the market place. This requires examination of the world textile market of which wool forms a relatively minor part and is in direct competition with synthetic fibres.

(a) Supply and price trends for fibres:

1973/4 estimates are that total world fibre production is around 25,500 million kilograms, of which synthetics account for 11,400 M, cotton 12,700 M and wool 1425 M. Thus wool is under 5 per cent of the total. Although wool production has been relatively steady since 1960 and cotton production has only increased slightly, synthetics have increased by 500 per cent and are continuing to capture a larger share of the expanding market. Wool is being seriously challenged because of its relative inelasticity of supply.

Further, prices for wool fluctuate widely and erratically compared with man-made fibres or even cotton. Consider the ten year period 1963/4 to 1972/3. New Zealand wool at auction averaged \$1.01 per kg. greasy in 1963/4, dropped to a low of 50 cents in 1967/8, rose to 62 cents in 1968/9, dropped again to 53 cents in 1970/71 and rose to \$1.44 in 1972/3. Nylon started at \$US2.73 per kg., fell steadily to \$2.12 in 1967/8 and has remained at that list price at least until recently. Similarly, polyester started at \$US2.51 per kg., dropped to \$1.34 in 1968/9 and has remained there. Even cotton has fluctuated only within a range of from US63 cents to 88 cents. In summary, wool to a textile user is relatively scarce and relatively price unstable. It has of course other advantages which may compensate.

(b) Fibre marketing systems:

(i) *Wool*

New Zealand wool is produced by 38,000 independent producers. If sold by auction it is transported to 8 different selling centres. There in warehouses operated by wool brokers (23 throughout New Zealand), it is visually classed into some hundreds of types and displayed for subjective valuation by up to 80 buyers plus floor price appraisers. Post auction, the brokers acting under instruction from buyers, may arrange for dumping (compressing two or three bales into one) at one of a number of facilities and transport

to storage at dispersed locations until export. If sold privately, wool merchants process their wool through some of these stages. As the bulk of auction wool is sold between September and June and mills require wool throughout the year, they need to provide storage. Further, users are located far from New Zealand. Our main users are the E.E.C., followed by U.S.A., Japan and Russia.

Promotion, market and product research and development and technical services are provided by a wide range of organizations of varying competence, including the Wool Board and Corporation, the Wool Research Organization and the International Wool Secretariat. Marketing strategies are usually widely publicized and debated before being put into operation.

Wool marketing operations are thus complex and costly with responsibility for preparing and moving the clip fragmented among many groups. The variable quality and price flows unevenly to the user.

(ii) *Synthetics marketing system*

Synthetic fibres are produced and sold by a small number of large firms direct to the user. Production plants are located relatively close to users. When demand exceeds supply (and hence is likely to affect price), users can be rated and given priority on the basis of present and future requirements and reliability. Price is set by the producer based on competition and long term marketing strategy. Decisions on promotion and market research and development are made within individual organizations so that competitive advantage is retained.

(iii) *Cotton marketing system*

After ginning, cotton is generally sold by farmers' agents direct to spinning mills at a negotiated price. The relative stability of world cotton prices is partly due to the ability of producers to respond quickly to price changes (the production period is short) and partly to the price stabilisation policy of the U.S.A. Government which involves stockholding.

2. *The performance of wool in fibre competition*

The competitiveness of wool in the world textile market is influenced by a number of factors including the following:

(i) *Fibre properties:*

Critical fibre properties include utility and processing ability. By utility is meant the characteristics imparted to the end product. It is here that wool continues to retain its relative advantage. However in processing, wool is inferior to synthetics. Disadvantages include the number of primary processing stages necessary before it is ready for spinning, its relative weakness necessitating slow processing speeds, its high specific gravity and hence lower output and the fairly high degree of waste.

(ii) *Fibre availability:*

Wool is generally more inflexible in supply than synthetics and the location of supply is

distant from the major textile producing countries.

(iii) *Price:*

Price fluctuates widely due mostly to fluctuating demand occasioned by the general level of economic activity and to inelastic supply.

(iv) *Specification:*

Without objective measurement accurate specification of quality (and hence a repeatable product over time) is not possible.

(v) *Handling and distribution:*

Unlike synthetics wool does not provide prompt delivery time in clean and homogeneous packages which are easy to handle and store.

(vi) *Market information and development:*

Detailed, up-to-date information, readily available to all, on user requirements and a co-ordinated world-wide strategy for market development, is not provided by the present wool marketing system, although the I.W.S. should be doing this.

On balance these factors are resulting in continuing erosion of wool's competitive position in the world fibre market place. Therefore some change in the present wool marketing system is imperative.

3. *An ideal wool marketing system*

On the basis of the considerations discussed, criteria for an ideal wool marketing system include:

- (i) Provide users with wool of a specified and repeatable type at the required place and time, uniformly packaged and at a stable price.
- (ii) Ensure a favourable production environment for wool growers by stabilising prices.
- (iii) Increase the efficiency of the wool handling, selling and distribution system so that associated costs are as low as possible.
- (iv) Ensure an improved information flow between user and producer.
- (v) Undertake further market development.

However, unless central and direct management and control can be exercised in assembly, sale and disposal, it is not possible to satisfy all the above criteria.

In essence this is the justification for wool acquisition.

D. MAJOR NEW ZEALAND MARKETING REFORM PROPOSALS

1. *The Wool Board/Wool Marketing Corporation Plan*

Recall, the question of acquisition is still unresolved. However, the functions and powers of the Corporation were set out in a major policy statement by the Wool Board in May 1972.

These are:

To acquire wool and market it in any manner thought best within and outside New Zealand.

To develop greater efficiency in preparation, handling, processing, distribution, shipping and selling. The Corporation may itself engage in these activities.

To develop existing and new markets, to provide information on market requirements and to encourage production of wool suited to these requirements.

To administer a minimum prices scheme.

At the same time the Corporation's method of operation was rather vaguely outlined. Presumably the vagueness was intentional. The Corporation was not then in existence and its flexibility and competitive advantage could have been compromised. Also no doubt detailed operating procedures just were not known.

The statements merely summed to the intention to license brokers and dealers to act on its behalf to receive wool. It would then be appraised and the producers paid promptly on this basis.

Subsequently non-acquisition has reduced the Corporation to the status of paper tiger. It is now in the second year of its existence and has been effectively ineffectual. No significant changes in marketing have been made. A scheme for combining small lots has been announced and the Corporation is buying small quantities of wool for what it calls marketing experiments. Plans for acquisition are a little more definite. The auction system would continue with the Corporation as sole vendor, producers having delivered their wool through the existing channels. Producers would receive a schedule price plus possibly an end-of-season payment. Private buyers and co-operatives could buy wool from the Corporation. To contain price fluctuations the selling season would be extended and a buffer stockpile would be created. Sale by sample would be extended and the number of types standardized. So much for the plans.

Given non-acquisition, the Corporation should be putting major efforts into market research (e.g. user needs) and development but does not show signs of great activity in these areas.

2. *The Stock and Station Agents' Plan*

This group includes the major handling and selling agents and has about \$25 million invested in wool stores and plant.

Briefly it is against acquisition but in favour of handling economies. An Authority would be established to make immediate payments to farmers on the appraised value of their wool, to control wool flows on to the market, to introduce wool standards and to participate with the industry in improvements in handling and selling. Later, a marketing Corporation might be set up to buy and sell wool in open competition.

3. *The Wool Buyers' Association Plan*

Acquisition is favoured. However, the authority would dispose of wool at auction or at auction determined prices, through the existing buyer structure (accredited exporters). The authority would not trade in wool itself except through a marketing unit mainly concerned with new product development.

4. *The Federation of New Zealand Wool Merchants' Plan*

Opposed to any form of acquisition.

The Wool Commission would become a trading organization with power to purchase wool and sell direct to world markets or as otherwise seen fit. It would thus be familiar with user requirements, and in a position to undertake market development.

5. *Assessment of Plans*

Consider these plans on the basis of needs for wool in the world textile market place. The Board/Corporation proposal is the only one which has all the major elements required. The Wool Buyers' plan is thoughtful. The alternatives mostly reflect the protection of special interest groups (however legitimate this may be). They also indicate just how intractable the problems are.

E. THE ANTI-ACQUISITION ARGUMENTS

Reform proposals involving acquisition by an organization acting under legislative authority have been mainly criticised on the following grounds:

1. *Loss of freedom:*

This is the major argument of growers and the Wool Action Committee argument. Freedom is the right of the producer to choose to whom the wool should be sold, in what form, at what time and at what price. However, the existing system does not permit complete freedom of choice in all these matters.

2. *Changing a proven sales method:*

It is claimed that the present method has been operating by and large successfully over a long period, to effectively dispose of the wool clip. Further, it is constantly undergoing change and improvement as the market place dictates.

3. *Cost effectiveness:*

The setting up of yet another organization in the marketing chain must increase costs. Furthermore, it will be large, bureaucratic and employ salaried staff without a stake in the product. Hence it must operate inefficiently.

4. *Government control:*

The Authority is set up under Government legislation, has Government nominees on its Board and would be supported by Government funds if necessary. It is thus under the influence of Government and may not have the necessary commercial orientation. Also, at some later stage, Government could decide to nationalise the industry, the groundwork having already been laid.

5. *Interfering with supply and demand in the market place and disrupting trading channels.* This was basically a view put forward by existing traders.

In fact acquisition could discourage the continuing involvement of commercial organizations with their capital and expertise and contacts with users.

F. SUMMARY

Reform in the marketing of wool has been under intense discussion for the last 2-3 years. The most controversial and far-reaching element of reform is the setting up of an authority to acquire and market all wool.

This paper has examined the competitive position of wool in the world textile market in order to establish criteria for a marketing system best suited to enhance wool's competitive ability. The conclusion is that a single authority participating in and exercising control in selling, handling and transport and engaging in market research is necessary. There are some valid objections to such a system but from the point of view of the economy as a whole potential benefits exceed potential costs.

Meantime the New Zealand Wool Marketing Corporation has had to operate without acquisition and is making nil progress in reform. It is unlikely that the present members of the Electoral Committee will agree to acquisition so the Corporation will continue to be ineffectual and a target for "told you so's". A substantial fall in wool prices would cause producer intransigence to collapse but such a drop is unlikely in the near future. A record of commercial success by the proposed Australian or South African Corporations could rally grower support here but results may not be apparent for some time. Accordingly the great New Zealand wool debate will drag on for some time yet with a wool marketing system of bygone days teetering precariously on an antiquated but oh so venerable foundation.