AWTA LTD

RESPONSE TO THE WOOL SELLING SYSTEMS REVIEW ISSUES PAPER

AWTA LIMITED

FEBRUARY 2015

About AWTA

The Australian Wool Testing Authority (AWTA) was established in 1957 by the Commonwealth Government in response to requests from the Australian Wool Industry for an independent test house. The government agreed to the industry request on the basis that AWTA be commercially self-supporting; it was not to be supported by the Commonwealth. AWTA's objective then, and now, is to provide accurate and impartial wool test results for use throughout the world.

AWTA was privatised in 1982 and established as a Company Limited by Guarantee to enable the functions of the statutory AWTA to be transferred to the private sector. AWTA Ltd commenced operation on 1st July 1982.

AWTA Ltd is structured as a Company Limited by Guarantee, without shareholding. A Board of Directors, representing all sectors of the Wool Industry, governs the operations of AWTA Ltd ensuring the Company operates impartially and provides services required by the industry. The Members of AWTA Ltd are:

- Australian Council of Wool Exporters Inc (ACWE Inc)
- Australian Wool Processors Council Inc (AWPC Inc)
  - Wool Scourers & Carbonisers Group of Australia (WSCA Group)
  - Wool Textile Manufacturers of Australia Group (WTMA Group)
- Australian Wool Innovation Ltd (AWI Ltd)
- Private Treaty Wool Merchants of Australia Inc (PTWMA Inc)
- The National Council of Wool Selling Brokers of Australia Ltd (NCWSBA Inc)
- WoolProducers Australia

AWTA Ltd's Articles prevent it from distributing any profits to its members. Instead, AWTA aims to minimise fee increases to the advantage of all stakeholders and to provide or fund other industry good activities. A longstanding policy of the Board has been to avoid annual fee increases or at least constrain any necessary increases to less than the annual inflation rate. This policy, coupled with the decrease in wool testing revenue arising from the steady decrease in wool production over the past 15 years means that AWTA has to constantly search for cost savings, efficiencies and ways to expand revenue base.

Having been originally established for the purpose of testing wool and wool products, AWTA has over recent years diversified into the testing of other agricultural products such as grains, hay, fruit, vegetable and processed foods. This strategy of closely related diversification has helped to offset the decrease in revenue from wool testing and allowed for vital wool-related infrastructure and services to be maintained.

Response to AWI WSSR Issues Paper

DELIVERY AND TESTING

- **For a woolgrower to receive a fully certified AWTA test result on their wool they must first have delivered their product to a wool broker's store that has AWTA certified core and grab sampling facilities. Would there be any commercial benefits to the woolgrower in knowing their final test results prior to delivering their wool to a broker's store?**

- **Is there a more efficient logistical process for conducting the testing compared to the current core, grab, tuft sampling, and sample movement process?**

- **Can AWTA testing be performed on-farm or at another regional location of the woolgrower's choice if such alternatives are preferred?**

- **AWTA currently tests for a multitude of measurements including Micron, vegetable matter (VM), Yield, Length, Strength, CVD, CVH, position of break, wool base etc. Are there additional characteristics AWTA should test for that would enhance the objective description process and possibly open up alternative processes for the sale of wool?**

AWTA provides a variety of tests in a variety of ways

The testing of greasy wool is AWTA's principal business and, although there is no compulsion to do so, virtually all Australian greasy wool is measured prior to sale regardless of the method of sale.

As an independent testing house, AWTA believes that it is vital that it provides testing services that are equally relevant to various supply chains or methods of sale. While the auction system has been the dominant method of sale, AWTA has assisted many different companies or groups, to develop new supply chains by adapting the testing services to suit their requirements. In doing so AWTA is flexible, while ensuring that it maintains its own integrity and independence and that the services are fairly costed.

AWTA sees the demand for testing services falling into 2 very broad areas:

> **IWTO Certificate Testing** - where the original seller and the ultimate buyer are unknown to each other, there is a natural requirement for complete independence in the entire sampling and testing process. The process of IWTO approving testing and sampling protocols, and AWTA ensuring that they are complied with, allows buyers to confidently trust IWTO Certified test results. AWTA's reputation as a professional and totally independent test house underpins smooth trade of wool between unknown sellers and buyers.
>
> Paramount to the certification service is the independence of sampling and testing activities and the security and integrity throughout the process.
>
> **Report Testing** - where the seller and buyer have a closer relationship, they will normally still require objective test results as part of the transaction. However, they may agree on variations to the IWTO accepted protocols (most commonly in the sampling stage) or not require independent supervision of sampling. AWTA provides Test Reports (as opposed to IWTO Test Certificates) in these circumstances.

The industry commonly refers to the IWTO Test Certificates provided by AWTA as "Presale Certificates". Occasionally this term creates an impression that wool cannot be sold until the test is completed. In this way testing is sometimes wrongly identified as being a barrier to forward selling. In reality, forward sales are often negotiated in advance of shearing and testing (either IWTO Test Certificates or Reports) is conducted to finalise the transaction in accordance with agreed rise or fall schedules.

As the major demand is for IWTO Test Certification, AWTA provides sampling services wherever they are demanded under a costing model that is equitable and transparent. In NSW in particular, this has accommodated significant change in the warehousing arrangements for wool in recent decades as wool stores have become increasing regionalised (see Table 1 for current AWTA sampling locations).

Table 1 AWTA Sampling Centres

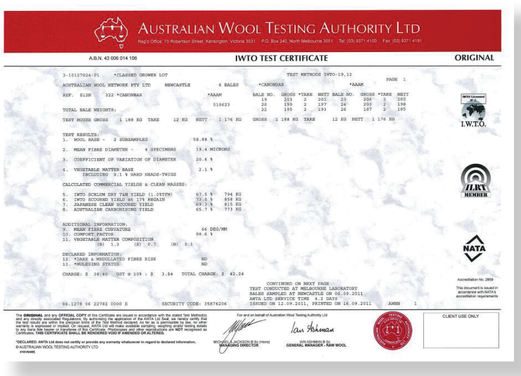
Queensland	New South Wales	Victoria	Tasmania	South Australia	Western Australia
Brisbane	Albury Bathurst Canowindra Condobolin Cooma Cowra Crookwell Dubbo Forbes Goulburn Grenfell Griffith Gunning Inverell Newcastle Parkes Sydney Tamworth Temora Wagga Wagga Yass	Ararat Echuca Geelong Hamilton Melbourne Mildura Portland Winchelsea Yarrawonga	Launceston	Port Adelaide	Fremantle Katanning

Independent Sampling and Testing to Agreed International Standards is the main method of testing

The predominate method of sale and ownership-transfer for about 85% of wool producers is the open-cry auction. Wool sold on in this way is done so on the basis of internationally recognised and agreed wool sampling and testing standards. These standards are produced by the International Wool Textile Organisation (IWTO) and AWTA Ltd provides IWTO Test Certificates to buyers and sellers prior to the wool being offered for sale. Table 2 provides a summary of the different testing parameters measured, along with the fees.

Table 2 Test Results Available for IWTO Certification

	IWTO Greasy Core Test	IWTO Staple Length & Strength Test	IWTO Colour Test
Fee (inc GST)[1]	$44:86 (4 cents/kg)	$32:78 (3 cents/kg)	$10:34 (1 cents/kg)
Includes:	Yield Mean Fibre Diameter – Laserscan CV Diameter Fibre Curvature Comfort Factor Vegetable Matter Base	Staple Length Staple Strength CV Staple Length Position of Break	Clean Colour



[1] Based on 6 Bale lot and average greasy bale weight of 176.4 kg.

Commercial forces decide which tests are conducted, and the method by which they are conducted

AWTA has never received subsidisation from the Australian Government, or from the levies paid by woolgrowers. Nor has wool testing ever been mandated. AWTA has always relied solely on commercial demand for its testing services for its revenue. As such, it is relevant to reflect on the forces that drove the rapid uptake of objective measurement of wool in the early 1970's.

Initially, topmakers started to write purchase specifications on the basis of IWTO Certified Yield, Micron and VM results because it provided them with the ability to more reliably produce tops to their spinner customer's requirements. However, in those early days, exporters continued to rely on subjective appraisal to source wool for those orders. The exporter would then have to commission post-sale testing at its cost and, more significantly, carry the risk that the test results would not match the requirements of the order. The inherent inefficiencies in this approach encouraged exporters to buy wool with more confidence when the seller offered it for sale with presale test results available. With more competition for presale tested wool, price premiums became apparent and sellers became convinced that it was worthwhile to pay for their wool to be tested before sale. It is these commercial, or market forces, that have created the "pull" for the almost universal uptake of presale Yield Micron and VM testing by wool sellers.

In a similar way, the demand for objective Staple Length and Strength information to better predict and control the fibre length parameters of topmaking has resulted in widespread adoption of these tests for combing length wools, but not necessarily for carding types.

In other cases, for example colour testing, the downstream demand has not yet been sufficient to encourage sellers to pay for the cost of testing and in those cases there has been very little sustained uptake of the service.

In short, sellers are discerning in deciding which of the various available tests they will pay for. They look at the premium which develops when there is sufficient market demand for the information provided and generally make rational decisions. AWTA facilitates this by allowing sellers to select from a range of testing options, rather than bundling them all into one testing package.

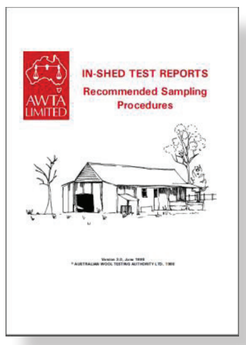
AWTA offers testing that suits all methods of sale

Table 3 below shows a number of different selling methods and identifies whether Certified or Report Tests are generally used. For all selling methods AWTA offers a service.

Table 3 Wool Selling Methods and Testing Options

Selling Method [2]	IWTO Certified Tests Used?	Report Tests Used?
Open-cry 'progressive' auction – The preferred method of sale and ownership transfer for about 85% of wool producers. This system is facilitated and managed by wool brokers, guarantees payment, and allows maximum exposure and competition for wool at sale time, with all major buyers of Australian wool present in the auction rooms.	YES	NO
Private treaty – Prices are negotiated privately with buyers at or about the time of shearing. Wool may be sold either tested or untested; however, untested wools will not be paid the same as tested wools.	YES	YES
Forward sales – A contract is made before shearing to deliver wool to an agreed specification and to an agreed price schedule. Payment is made against the actual test results.	YES	YES
Direct to topmaker/exporter – Similar to forward contract, but a spot sale through an exporter for delivery direct to a topmaker.	YES	YES
Internet selling – Electronic offer board where wool is available for sale to buyers 24 hours a day, 7 days a week. A reserve price is 'posted' (presented for sale on computer screen) and can be simultaneously seen by all registered buyers. Submission of bids and final sale is facilitated via the offer board, and not directly with the seller.	YES	NO
Grower marketing groups – Grower based marketing groups established to sell direct to processors and manufacturers.	YES	YES
Wool Pools – A contract is made to deliver a volume of a shearing or yearly production to the pool up to 12 months prior to shearing. By participating in the pool you are assigning the risk management of your wool portfolio to a third party. The aim is to reduce exposure to price volatility. An upfront payment occurs after delivery based on a percentage of the current market. At the close of the pool a final payment is made based on the performance of the pool against the physical market.	YES	NO
Grid Sales Similar to selling livestock "over the hooks", prices are offered from a set grid of prices for wool delivered to store. Prices are generated from all stages of the demand chain as the various businesses feed direct orders from the pipeline. Most wool selling brokers will offer some form of grid sales or a price at door pricing system for their clients.	YES	YES
Partnership Processing – retained ownership Some processors offer an option to growers allowing the grower to retain ownership of the wool beyond the greasy form.	YES	YES
Mill Direct Marketing wool through Mill Direct enables an offer of growers' wool directly to a network of international processors at your own set price. It provides the opportunity to receive valuable feedback on your product and build strong relationships for future orders.	YES	YES

For clients wanting on-farm sampling methods, AWTA has worked with grower and supplier groups over the years to assist in the development of sampling and testing protocols for alternative selling systems. AWTA has, with the cooperation of others, developed a manual for use by wool growers or their agents for the sampling and weighing bales on-farm, allowing the retention of wool on farm for storage and marketing. This manual provides a comprehensive guide to the sampling equipment required and methods necessary to obtain representative and consistent samples.



[2] Selling methods listed adapted from website: http://www.makingmorefromsheep.com.au/market-focussed-wool-production/procedure_2.3.htm

WOOL APPRAISAL

The Review Panel is seeking input on the item of wool appraisal and valuation.

- **Can any efficiencies or cost savings be achieved within the appraisal stage of the wool supply chain through some consolidation of the three forms of inspection? For example, why not just have the AWTA apply an AWEX type rather than have the wool broker and AWEX both complete this task?**

- **Can a combination of AWTA test results and a singular, industry accepted valuation standard provide an online platform for wool to be appraised and valued? If so what efficiencies and costs savings (if any) can be achieved?**

- **Could woolgrowers exercise more discretion in the type of tests performed on their wool in order to save costs?**

- **Certification and independent appraisal of non-measured characteristics is feasible.**

As stated above, the majority of Australian wool is sold at open-cry auction. Most auctions lots are presented using the 'sale by sample' method, where representative samples are displayed on a show-floor for evaluation by wool buyers. This system has worked well since it was introduced in the 1970's. However, new systems have evolved that improve efficiency and flexibility of the sale process.

In these new selling systems, lots are usually sold without the requirement for a show-floor with display samples. Such systems lend themselves to the sale of certain wool types (e.g. 'bread & butter' Merino fleece wool), where the objective test results and an appraised type largely determine the sale price and buyer evaluation of a display sample is usually not necessary.

One of the impediments to larger scale adoption of the sale of wool without a display sample has been the lack of guaranteed, independent assessment on the non-measured characteristics of the wool. In 2006, following approaches from two major brokers, AWTA Ltd agreed to facilitate a 'Wool Appraisal Trial' whereby AWTA Ltd provided an independent, subjective appraisal of the wool type. This type was in the form of an AWEX-ID, along with the latest TEAM-3 processing predictions, and the wool typing was guaranteed by AWTA Ltd.

The aim of the Wool Appraisal Trial was to evaluate another alternative to existing selling systems, not to replace the open-cry auction system. Further, it is clear that certain types of wools will likely always require a display sample (or even the bales themselves) for buyer evaluation. Such wools include speciality superfine and carding lots.

The majority of combing length merino fleece wool, excluding speciality types, could be regarded suitable for sale based on objective test data with a guaranteed wool AWEX-ID wool type, subject to the seller's requirements.

The trial involved South Australian Merino fleece wool as most of this wool is of a very consistent type, in the 20 to 23 □m diameter range, and able to be adequately appraised and sold without sample. This type of wool is already sold on electronic offer boards around Australia without a display sample being readily available. More information on this trial is available at www.awta.com.au

As part of the Wool Appraisal Trial AWTA Ltd provided a guarantee on the subjective wool type.

> *"AWTA Ltd will provide a guarantee, based on an assessment of the display sample taken in accordance with IWTO Standards, that the AWEX-ID determined is a fair and adequate description of the non-measured wool characteristics as applied by a qualified AWEX-ID Appraiser. This guarantee does not extend to processing quality or performance."*

Despite support for the trial from the principals of many buying firms the trial concluded after only two months with many auction room buyers shunning the lots offered and the two major brokers choosing to focus on other projects.

Given sufficient support from buyers and sellers, such a system could easily be introduced on a wide scale within 12 months.

AWTA Service Time

The reports states standard turnaround is approximately 3 to 4 weeks to get the wool from farm gate to auction show-floor. It should be noted that AWTA offers three levels of service to customers. The service time – from when the sample is taken by AWTA to when the result is issued to the client - is shown below. Many clients core sample one day and receive the results the next day.

Test Type	Turnaround Time	Normal	Fast	Express
Yield & Micron	Average (days)	3.2	2.0	1.5
Length & Strength	Average (days)	3.9	2.2	1.6

PRICE REALISATION

The Review Panel is seeking information and evidence on the effectiveness of the current open cry wool auction system as a mechanism for competitive and cost effective price realisation, in particular:

- **What other selling alternatives exist for woolgrowers in the market place today and how do the selling costs to the woolgrower compare to the traditional auction method? What other methods are worthy of investigation?**

AWTA has been deeply involved in electronic selling systems

In the late 1990's AWTA developed a computer based electronic selling system called Woolink. This system allowed several forms of electronic trading including a screen based auction, offer boards and spot sales. In September 1999 a live auction was conducted using the Woolink system with three brokers and 12 exporters participating. The auction itself was successful, demonstrating that the concept was technically possible but the concept did not receive the general support of the trade and was abandoned. Other organisations have since gone on to successfully commercialise electronic selling systems and AWTA has cooperated fully with the development of these systems.

The wool industry has cooperated over many years to develop a sophisticated electronic mailbox system that allows the seamless exchange of a myriad of standardised electronic documents ranging from test data to wool delivery instructions. The data necessary for any selling systems is built upon the test data and AWTA has collaborated with the developers of alternative selling systems to ensure test data is available in a multitude of ways in suitable formats. The efficiency gains and cost savings delivered to the industry by this system should not be underestimated.

In short, electronic selling and exchange of ownership has been a reality for many years. Online systems already exist for the sale of wool, both in Australia and internationally and live electronic auctions could be efficiently conducted with existing infrastructure and computer systems.

GENERAL

Wool industry institutions

- **AWEX undertakes a variety of tasks, including market reporting and ensuring accuracy in wool description, that help the wool market to perform efficiently. In a similar vein, AWTA supports market efficiency by providing critical data describing the range of wool characteristics. Would there be advantage in combining the activities of AWEX and AWTA?**

- **Is there an opportunity to increase competition in wool testing services currently provided by AWTA? Should woolgrowers be able to nominate what tests they would like performed on their product and pay accordingly for the services provided?**

- **Are there other changes to the institutions serving the wool industry that would reduce costs or enhance returns associated with the first exchange of wool ownership?**

- **Talman Solutions provide the majority of wool exporters and a large number of wool brokers with inventory management IT systems. Do the systems provided by Talman Solutions generally meet the requirements of their customers? Is there potential for greater competition for this service offering within the wool industry?**

Consolidation of Wool Industry Services is feasible and would save money

Over the past decade or more the quantity of wool produced in Australia has steadily declined. The industry has become increasingly fragmented and has lost some of the 'economies of scale' enjoyed in more prosperous times. The reduction in production has impacted significantly on companies and organisations whose revenue is largely dependent on the quantity of wool available. As such, the industry faces real current and long-term challenges in being able to manage and fund the required commercial and 'industry good' services in a cost efficient and sustainable manner.

In 2006 AWEX initiated discussions with AWTA to ask it to consider increased cooperation to identify synergies which could reduce cost to industry. After preliminary discussions, AWEX initially terminated those discussions, before reopening them a year later.

In 2007 AWTA prepared a concept proposal to integrate the Operational Activities of AWEX into its own structure where Operational Activities were identified as:

a. Commercial Services: Services provided on a fee for service basis (eg Market Reporting, Wool Clearing, Network and Database Services, Wool Pack Approval and Testing, Classer Registration etc).

b. Industry Good Services: Services that help support the efficient operation of the industry but are not readily funded on a fee for service basis (eg implementing, monitoring and reviewing the effectiveness of the agreed industry standards, rules and regulations. Providing administrative support to Industry Committees. Assisting industry education or R&D initiatives etc)

After consultation with its member base, AWEX informed AWTA that it would not take the proposal any further as it did not believe that it had the support necessary to succeed as a Special Resolution under the AWEX constitution.

Had it proceeded it may have provided the industry a significant reduction in the cost of overheads, the ability to easily integrate activities, and a broader platform for potential industry based innovation. Some of the potential synergies that could be delivered by a merger between the two organisations include:

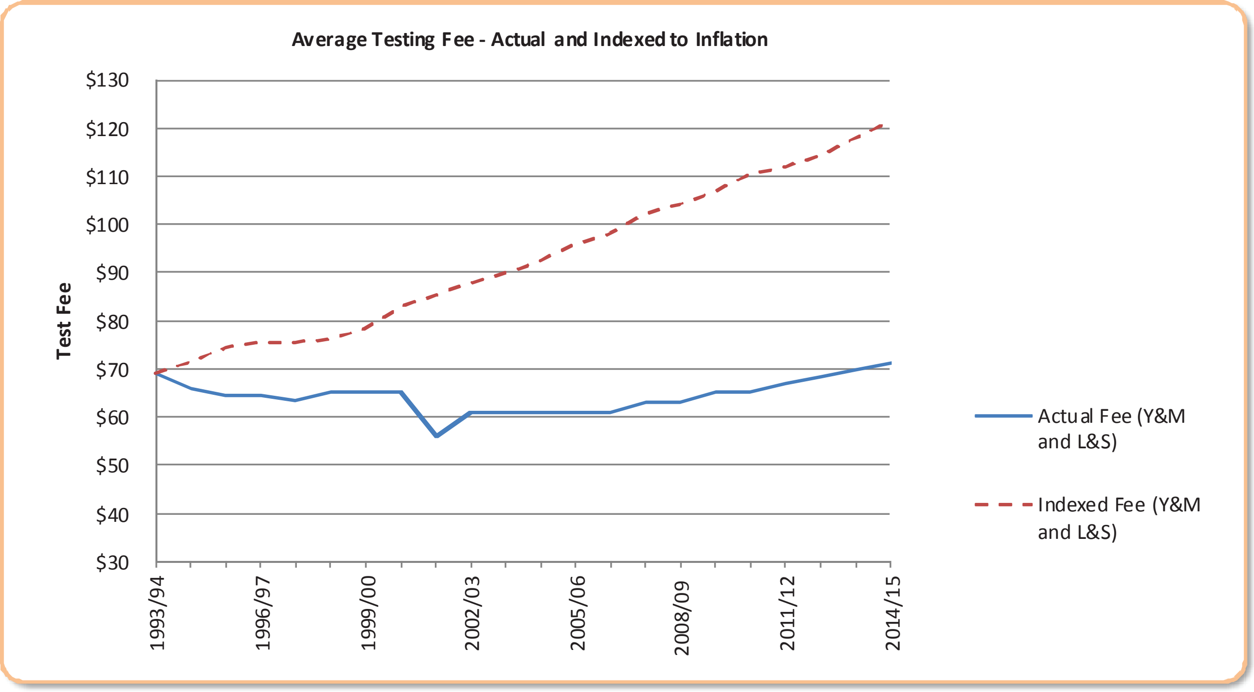
- One Board of Directors.
- One corporate Head Office.
- Regional office rationalisation – one office in each region.
- Computer hardware rationalisation.
- One industry database (with some changes to AWTA database structure).

AWTA does not seek to compete with AWEX but remains open to discussing means of reducing industry costs with all interested parties.

AWTA is a sole service provider

AWTA is the sole provider for certified testing of wool in Australia. Whilst other organisations have operated certified wool testing laboratories in Australia in the past, these ventures have been relatively short-lived. As discussed in the "About AWTA" section above, AWTA's Board of Directors is also its customers and this structure ensures that fee minimisation is a key objective of the Company. Past performance shows this focus has returned significant benefits to its customers.

Figure 1 AWTA actual fee change vs inflation



Talman Costs

Some years ago, the wool industry was faced with large increases in electronic mailbox operating and data transmission fees from Talman Solutions. In response to this, AWTA adapted its own mailbox system for general industry use for the exchange of all document types and offered a commercial service at significantly lower rates. These lower AWTA fees led to a reduction in Talman fees and resulted in significant savings to the industry.

AWTA has decided to maintain this capability, should the industry need or wish to utilise its mailbox facility in the future.

Transparency

- **What scope is there to allow woolgrowers to make better informed decisions in relation to what it is costing them to sell their wool? More specifically would greater understanding of the costs and returns reflected in their final price received facilitate improved commercial decisions concerning their own wool growing enterprise?**

Providing a yearly breakdown of all industry costs is vital

AWTA strongly believes that every effort should be made to continue to resource and publish the Sheep's-Back-To-Mill document. This independent publication identifies in considerable detail the various costs associated with the harvesting, handling and marketing costs incurred by growers and buyers. These costs are quantified in various forms such as per greasy kilogram of wool, per head and industry totals.

The extract below from the last published Sheep's Back to Mill clearly and concisely highlighted the magnitude of costs in the supply chain.

Table 2

INDUSTRY COST – CENTS PER KG GREASY

HARVESTING, SELLING AND LOGISTICS COSTS FOR AUSTRALIAN WOOL

Activity / Item	2006/2007	2009/2010	3 yr change
DIRECT COST TO WOOL GROWER			
Harvesting Costs	Greasy c/kg	Greasy c/kg	%
1) Crutching	22.38*	25.44	+ 12.03
2) Shearing	77.08*	77.27	+ 0.25
3) Wool Classing	13.96	12.86	- 7.88
4) Shed hands	24.51	23.63	- 3.59
5) Wool pressing	12.83	12.44	- 3.04
6) Wool packs	6.31	5.62	- 9.98
7) On Farm Fibre Measurement	0.48	0.51	+ 6.25
Sub total	158.28 cents	157.83 cents	- 0.28 %
Transport to Brokers Store Costs			
8) Transport to store	8.67	9.00	+ 5.54
9) Insurance to store	0.87	0.93	+ 3.45
Sub total	9.54 cents	9.93 cents	+ 5.35%
AWTA Testing charges			
10) Core testing & certification	3.82	4.12	+ 7.85
11) Length & Strength testing & certification	2.28	2.31	+ 1.30
Sub total	6.10 cents	6.43 cents	+ 5.41 %
Brokers Handling and selling charges			
12) Warehousing	10.58	11.60	+ 9.64
13) Insurance store fire	1.29	1.60	+24.03
14) Interlotting service charge	0.12	0.12	=
15) Re-handling - Bulk classing	1.50	1.93	+ 28.67
16) Grower storage	0.04	0.08	+ 100.00
17) Brokers Commission	6.41	8.10	+ 26.36
18) Sale sample value	Not Included	1.21	Na
Sub total	19.94 cents	24.64 cents	+ 23.57 %
Fees and levies			
19) AWEX revenue/fees	0.26	0.88	+ 238.46
20) AWI wool levy	10.52	10.30	- 2.09
Sub total	10.78 cents	11.18 cents	+ 3.71 %
DIRECT COST TO WOOL GROWER TOTAL	204.64 cents/kg	210.01 cents	+ 2.62 %