

OPPORTUNITIES FOR OUR COTTON BEYOND THE FARM GATE

Kim Morison
Division Director, Macquarie Cotton, Sydney

Introduction

Australian cotton is highly regarded amongst the world's cotton spinners for its high quality fibre characteristics, reliability of supply and lack of contamination.

As an industry we enjoy access to regular, reliable buyers who are prepared not only to buy Australian cotton, but to buy it forward as much as two years in advance to ensure they secure their supplies early.

However, in this competitive world, we cannot afford to rest on our laurels. There are large competitive threats looming and following the last two years of drought reduced supply, we need to rebuild Australian market share.

This paper addresses the need and the opportunities to pursue an industry-wide campaign beyond the farm gate in order to maintain Australian cotton's global "preferred supplier" ranking, secure our market share, and increase grower profitability.

Global commodity competition

Increased investment and continual improvements in cotton growing and ginning technology are assisting the world's cotton growers to catch up to Australia's leading position in the supply of premium quality cotton fibre.

Australian cotton's main competitive advantages are our high yields, high quality, lack of contamination and reliability of supply. We're competitive as producers on a cost per pound basis – but our high yields come at the expense of high inputs.

We have the highest input costs for production per hectare in the world and our growing costs continue to rise.

In response we've increased yields, thanks to our world leading cotton research programs that have enabled us to achieve some of the best year-on-year productivity gains in world agriculture.

But in the current information age this same technology is transmitted to our markets and competitors easily. Consequently growers in the USA, Brazil or China have the ability to catch up quickly in terms of per hectare yields.

To survive in cotton long-term we have to continue to stay a leap ahead in terms of quality, per hectare yields, per kilogram production costs and finding the next market niche which will provide Australian cotton growers with premiums.

Short-term we are also emerging from two years of drought reduced production. Our annual supply to world markets has halved since this conference was last held in 2002

In response, as growers and merchants we've rationed our supply of premium quality cotton by increasing the asking price. We've demanded a higher premium over other growths during this period. Pleasingly, we've been able to achieve higher premiums and gain ground on our major market substitute, San Joaquin Valley (SJV) Acala styles.

As a grower you will have noticed the basis for Australian cotton at the gin yard has been above normal for the past 24 to 30 months. It's an obvious reaction to the drought, but it would be nice to think we have reached a new level of competitiveness too – or a new level of premiums over other growths.

Thankfully Australian cotton production will rebound in the coming season. At the time of writing, we're not back to three million bales for 2005, but we're a long way better than the previous two seasons where we produced under 1.6 million bales.

Our short-term challenge is to place a larger crop in the market, and at the same time maintain some of the recent hard won premiums over other growths. It's a daunting proposition because we are still seen as a commodity. Australian cotton is highly rated but it has its substitutes from the USA, Brazil, China, West Africa, Uzbekistan and now even Zimbabwe.

Just consider that in a little over three years US cotton exports have grown from below eight million bales to over 13 million bales per year in 2003/04. It's a phenomenal amount of growth, and this is no ordinary competitor.

At the time of writing this paper the A-Index of international cotton values was 61 US cents per pound landed to Northern Europe, New York spot futures were nine cents lower at 52 cents, and yet the US exporter was still receiving an additional 10 cents per pound for every bale shipped for export! That's 20 cents per pound to get it over the Atlantic! Quality adjustments and ocean freight might account for a maximum six to eight cents, so there's a whole lot more there to entice the buyers or fill the exporter's pockets.

It's a rather dramatic example, but demonstrates how competitive the US marketing programs really are. Thankfully as we've heard from previous speakers, the WTO has taken the first steps towards stamping it out.

In Australia we've previously drawn comfort from the fact that Australian cotton was a superior quality to the majority of US production. And this is still the case – but the US is making a concerted effort to catch up. Varietal improvements and gene technology have improved the quality of US cotton significantly in recent years.

The export market competition is not limited to the US. Brazil has gone from a major importing market in the mid-1990s to a net exporter of over 1.2 million bales in 2003/04. This export figure is expected to double this year. Its rapidly expanding production base has not only displaced a whole lot of US and West African cotton from Brazil's large domestic spinning industry, but created a new export competitor. The displaced West African cotton has also had to find a new export market home.

To date, Australia's response to these challenges has been limited. Understandably, as an industry we've been pre-occupied with drought, but now it's time for a re-think on how we move a step ahead of the rest – and fast.

Maximising returns and market share

The commodity marketing challenge is to achieve the somewhat incongruous aim of maximising market share and maximising price. Being what they are, the lowest priced commodity usually sells the most volume.

As marketers of Australian cotton we've traditionally viewed the spinner as the customer. The spinner's choice of cotton supply by type, country or fibre characteristic is determined by the yarn market segment they're aiming for – denim, knitwear, wovens underwear or industrial and commercial uses. Spinners fine tune their operations to achieve the biggest possible margin between the price of various specifications of raw cotton and the specific yarn specifications required for the next customer in the chain.

Historically, as Australian cotton production increased, we managed to increase our market share by simply reducing the price of Australian cotton relative to other growths. Interestingly this exercise probably had more benefit to the spinner's margin than anyone else's.

In marketing Australian cotton we have relied on emphasising its quality and reliability characteristics and we made our target market the spinners. The aim was to increase Australian cotton's share of their lay-downs by promoting directly to them. This "supply-push" strategy was effective enough, but only if the price of the commodity was cheap enough by comparison to its many substitutes. Price always won in the end.

More recently the Australian Cotton Shippers Association, Cotton Australia and CRDC have thought hard about ways to create "demand-pull" for Australian cotton.

By demand-pull we're talking about demand from further up the supply chain that would influence cotton spinners to buy Australian cotton over its competitors.

Demand-pull for Australian cotton is about creating a reason for retailers or brand-owners to influence cotton product manufacturers (homewears, garments, Manchester, children's toys, not just fashion) and in turn spinners and/or weavers of cotton yarn to specify that the yarn is made from Australian cotton.

Successful textile fibre branding

In order to be successful with this approach we need to have something that genuinely sets Australian cotton apart from its commodity competitors. We need a point of difference that can easily be recognised by consumers – something meaningful, tangible and ideally something that is difficult for our competitors to copy or replicate.

This point of differentiation can then be branded and promoted, with the resulting benefits flowing back to the Australian cotton industry.

There are several examples of successful branding in commodity markets - perhaps the most prominent Australian example was Woolmark. During the 1980s this was tremendously successful in lifting international demand for apparel wool. However, the problem was that Australian growers, who mostly funded the promotion, were unable to capture the benefits – wool supply increased in China, Russia, Uruguay and Argentina to such an extent that Australian wool was undersold by competitors. The market became oversupplied and prices collapsed.

The International Cotton Advisory Committee (ICAC) estimates that the synthetic fibre market is spending seven times that of the world cotton industry on promotion to consumers. And by virtue of patents and trademarks are able to recoup that investment all to themselves.

As an aside, a recent study by the ICAC found consumers are choosing synthetic fibres over cotton in nearly all countries of the world, including Australia. The study, across 88 countries, looked at consumer's household fibre consumption between 1992 and 2002.

While the total world fibre market continues to increase, cotton's share is decreasing. Between 1992 and 2002, use of synthetic fibres increased by 6% compared to just 3% for cotton. Cotton's market share is falling quicker in developing countries that are consuming more fibre in total than ever before, and the ICAC predicts cotton will have only 38% of the world fibre market by 2010 – compared to just over 40% at present.

Consumers in Australia have followed this trend, with a 2% market decline between 1992 and 2002. The only country surveyed that has increased market share was the USA, with a 1% increase. The average consumption of cotton in the world is 3.4 kilograms per year per person – in Australia it's 8.4 kilograms and in the USA, over 20kg. It is no coincidence that the USA is also the only country making substantial and continued investment in cotton promotion for consumers.

Trademarking a commodity is impossible, but in the global cotton industry there are several examples of successful branding.

Cotton Incorporated (CI) has had demonstrated success in increasing cotton's share of the US apparel market with its Cotton Seal. Its market promotion and research efforts have lifted cotton's US apparel and homewear market share from 34% in 1975 to more than 60% today.

Cotton Incorporated's budget for 2003 was an envious US\$62 million. Funded by US cotton producer and garment importer levies CI was able to run over 4,000 TV commercials and make an estimated 2.5 billion consumer impressions last year!

Little wonder then that 20% of the world's retail cotton demand resides in the USA and that this is the only consumer market in the world where cotton's share of the textiles market increased between 1992 and 2002

The US cotton industry has also had international success with the Cotton Council International's Cotton USA Mark. Funded by the US National Cotton Council, CCI develops, licenses and promotes the Cotton USA Mark for products made of 100% cotton and certified to contain at least 50% US cotton. CCI programs have lifted the preference for consuming US cotton in global markets from 19% in 1989 to 43% in 1998. In its target markets in Asia, brand recognition has reached 84%, translating into increased retail sales. This in turn has influenced garment manufacturers to insist on high US cotton content in cotton yarn. In order to guarantee compliance with the 50% US cotton requirement, CCI employs dedicated officers across the world to check spinner's cotton contracts.

Another recent example of highly successful cotton branding is the cotton seed brand Fibermax, developed by Bayer CropScience. Bayer is now licensing US cotton growers who buy Bayer's seeds as Fibermax suppliers and, together with US cotton merchants, is actively promoting Fibermax to spinners in Asia. In June this year Bayer hosted a conference of Asian spinners in Singapore with over 130 delegates attending. According to participants, it was a well organised and well funded assault on Australian and SJV market-share.

With a high proportion of Australian genetic material and breeding lines involved - courtesy of Cotton Seed International - the biggest selling point for Fibermax is that it can be substituted for Australian cotton. Fibermax's promotional brochure even highlights this as one of its attributes! Notably there has generally been a five to eight cents price difference - which has understandably made Fibermax a very attractive proposition for Asian spinners in the last two years.

But we can take some heart from this particular brand success! Imitation is the better form of flattery. And in this case it is Australian cotton they are trying to emulate.

Research, first by Truschler and CRDC in 2000 and more recently Stuart Gordon's work at CSIRO Geelong has independently verified the world class spinning qualities of Australian cotton. But our fibre properties alone are not unique. In order to stay ahead of our commodity competitors we need to develop our own version of differentiation.

The BMP opportunity

One of the unique aspects of Australian cotton production is the Best Management Practices program. BMP represents the foundation opportunity to differentiate ourselves in the supply chain and create demand pull for our fibre.

Devised in 1995, the BMP program has now achieved an uptake of approximately 23% of growers and 50% of the area of cotton under production in Australia.

The merits of the system have been recognised beyond the farm gate by the likes of the Australian Cotton Shippers Association, ACIC, CRDC and Cotton Australia as well as

Australian Governments, green groups like WWF and the International Cotton Advisory Committee.

As an industry we're moving to implement the disciplines of BMP across the post-farm gate supply chain. This program will be supported through Federal Government assistance under the EMS Pathways to Industry program announced in April 2004 by Senator Judith Troeth.

BMP represents something unique about Australian cotton. The BMP approach – and its extension post-farm gate - is very difficult for any other cotton producing country to replicate.

The key to realising a greater benefit from BMP is to develop an effective marketing campaign.

Cotton Australia and the Australian Cotton Shippers Association have already conducted some research into BMP's market viability.

The world's consumers are increasingly trending towards "clean and green" ideals. Consumers are demanding to know the origin of the products they are purchasing and they are genuinely concerned about the future of the planet. This trend is providing some commodities a differentiation edge and a resulting market preference, increased sales or an increase in margins.

Just take a look at any menu of the restaurants you dine at here on the Gold Coast. You'll probably notice examples like "1874" prime beef from Heytesbury's pastoral empire; Coffin Bay or Wallis Lake oysters; "Mandalong" lamb; King Island or Margaret River cheese to name a few.

Identity Preservation and environmental awareness are powerful influences on consumers today. And there is no reason why this should be limited to foodstuffs alone. There are two rationales for branding Australian cotton. First, consumers are seeking environmentally friendly products, and second, and perhaps more powerfully, retailers and brand-owners are seeking to demonstrate their environmental credentials (mostly to governments and pressure groups) by ensuring their products have a good environmental story to tell.

This sets up a mighty opportunity for Australian BMP cotton.

A number of international and Australian retailers and brand-owners have already expressed interest in our ability to supply garments from BMP cotton to their stores. They believe the "clean green" message attached to Australian BMP cotton is a powerful attribute to attract increased turnover and elevate their status as environmentally sensitive companies.

Gowings in Australia is already using BMP cotton in a range of t-shirts and promotes this fact through swing tags and a seasonal catalogue.

Take also the example of the UK's Marks and Spencer, one of the largest textile retailers in the world. One of its executives, Graeme Burden, visited Australia to speak at the ACSA Conference last year.

At that seminar he clearly communicated M&S's keen interest to stock garments made from BMP cotton as a means to appeal to environmentally conscious buyers, to meet M&S's environmental policy, to elevate M&S's green credentials and to attach a "great story" to their cotton products.

Cotton merchants and spinners present at the conference were able to quickly draw up a supply chain using M&S's existing preferred garment suppliers.

Without going into too much detail, this would involve BMP certified cotton being shipped to spinners in Indonesia, Thailand or Korea, the resulting yarn shipped to weavers or knitters in those same countries, or China and the resulting fabrics then made into garments in the likes of China, Vietnam, Bangladesh and Sri Lanka. From there, garments would be shipped to M&S stores world-wide.

The specifications for all the products in the supply chain – garments, fabric, yarn and cotton are ultimately determined to meet the specifications of the retailer or brand-owner. Marks & Spencer has specific requirements for colour, fabric weight, stitch, durability etc, which influence all the manufacturers along the chain right back to fibre supply.

By influencing brand-owners such as Marks & Spencer to also demand that all or part of the garment contain clean and green BMP Australian cotton, we can effectively establish a demand pull force for our benefit.

Making it happen

Looking at the Cotton Incorporated annual budget, I'm afraid our industry doesn't have the dollars for this kind of exercise. But the promotional aspects of this plan do not need to cost us a fortune, and we only have three million bales to place. The likes of Marks and Spencers have the huge promotional budgets that we can leverage off. We just need to have a good product and a good story to tell.

I believe there are just three areas of development in which we need to spend money to make this program happen.

First, BMP needs a brand - something that conveys the attributes of the BMP system and the attributes of Australian cotton. Best Management Practices itself does not mean anything to a consumer in Europe, Japan or Australia for that matter – and it's difficult to see it conveying the resulting story. The term BMP could relate to any process in any industry in the world and it is not particularly catchy.

I mean no disrespect to the originators back in 1995 - BMP means something to us as Australian cotton producers because we've all been educated about it – but there are only some 1,200 growers here in a relatively small industry. To appeal to millions of global retail customers we need something more catchy and conveying. Something that can tell the story or capture the essence of what is on offer.

Green 'n' clean, Spinsure, Envirofibre, Enviroasure, Fibercheck, Aussie...something? Hey, it's not my area of expertise - but I can assure you Fibermax is making the textile sector take notice of US cotton again and we're all familiar with Lycra, Tencel and Sportswool!

Second, we need a verification system. We need to capture the benefits of this program for accredited Australian BMP growers. If this is going to lift the volume of BMP cotton in demand, the returns need to flow to Australian BMP growers in the form of increased sales, and hopefully increased prices as a result.

In this on-line age, the verification system could be quite simple. We cannot afford the expense of hiring teams of international brand police to visit mills across Asia and the Sub-Continent, as does CCI.

With some co-operation we could devise an on-line password protected database storing select details of BMP accredited growers. This could allow merchants and spinners to verify and then issue certificates of authenticated BMP bales purchased and spun - to the next processor along the chain. These certificates could be endorsed and transferred all the way through the chain to the brand-owners or retailers. We don't want to act as Big Brother here - only limited information would be required such as perhaps ABN numbers and bale tag numbers - no names, addresses, farm locations, classing information, contract details, merchant or spinner details would be required.

Third, to be successful we need to be clear on our objectives. As an example - is this an environmental story or a Quality Assurance program?

BMP is clearly an on-farm environmental best practice regime. While there are undoubtedly quality assurance benefits from this process, there will be 100% BMP accredited farms producing short-staple or high-mic or rained-on cotton.

We need to work out the objectives of the promotional campaign - if it is QA then we have to work out what happens if we can't supply 21-3-36 tight mic and high strength cotton. This is obviously an issue for further debate, and I'm sure there will be more contribution to this issue during the remainder of the conference.

Conclusion

In conclusion, Australia's cotton industry has a highly successful track record. Thanks to world leading research programs and the competition borne of a free market system we've been able to position our cotton as a fibre of choice around the world.

We don't necessarily face any lesser competition in the years ahead than what has gone before, but improved technology and its ability to be more easily communicated and shared means some of those competitors will gain ground on us as cotton producers quicker than they have in the past.

We need to reposition Australian cotton in response. We need to develop a post-farm gate strategy - and BMP represents a very exciting opportunity to do so.

It is admirable that ACIC is now pursuing this concept, and the Federal Government's support is very welcome. But I would like to think that given the return of confidence to the industry in the form of a larger crop ahead, we can step up our pace of development. Another two to three years of research might only serve to frustrate our potential brand-owner and retail partners – the opportunity is present and there to be taken right now.

