

# WOOLPRODUCERS AUSTRALIA

## China Delegation

26 June – 3 July 2015

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## **Definitions**

ACACA	Australia China Agricultural Cooperation Agreement
AWEX	Australian Wool Exchange
AWI	Australian Wool Innovation
AWTA	Australian Wool Testing Authority
ChAFTA	China Australia Free Trade Agreement
CVH	Coefficient of Hauteur
CWTA	China Wool Textile Association
DA	Department of Agriculture
D Certificate	Wool not prepared by an AWEX registered woolclasser
EMI	Eastern Market Indicator
FAWO	Federation of Australian Wool Organisations
JCAWWG	Joint China Australia Wool Working Group
MoA	Ministry of Agriculture
NWD	National Wool Declaration
NWM	Nanjing Wool Market
P Certificate	Wool prepared by an AWEX registered woolclasser
PETA	People for the Ethical Treatment of Animals
RFID	Radio Frequency Identification
TWC	The Woolmark Company
WPA	WoolProducers Australia
WTO	World Trade Organisation

## **Executive Summary**

China takes around three-quarters of Australia's wool for processing for its own domestic retail market and for exports to the other major wool consuming countries. The Chinese wool textile industry faces significant challenges as it responds to rising labour costs, tougher environmental laws and tighter credit availability. It is vital, therefore, that the leaders of Australia's wool growers understand the wide range and scope of China's wool textile industry, from raw wool trade and processing to the manufacture and export and retail sales of wool clothing.

A delegation of five WoolProducers Australia (WPA) Directors and CEO travelled to China from 26 June – 3 July, 2015.

During the eight-day expedition the delegation met with various Chinese organisations that are instrumental in the processing of Australian wool. The main themes that were gleaned from these meetings are outlined below.

### **General perception of Australian wool and industry**

Australian Merino wool is still regarded as the best in the world in terms of quality. Australian wool accounts for 50% of all wool purchases made by China. Traditionally China was considered as only a processing hub for wool, however it is now emerging as a major consumer of wool, with half of all processed wool being sold domestically.

The emergence for the first time of a middle class and cool climate makes wool an attractive fibre to Chinese consumers.

All processing enterprises that the delegation met with had extremely positive views and interactions with the Australian wool industry service providing bodies – AWI, AWEX and AWTA.

The Joint China Australia Wool Working Group (JCAWWG) was considered a crucial forum to discuss both positive and negative issues surrounding the Australian wool industry and the Chinese processing sector. The JCAWWG provides an opportunity to resolve these issues between the trading partners.

### **Clip preparation**

While the overwhelming perception of Australian wool is positive there are still reports of contamination – both with dark and medullated fibres and non-woollen objects. Although different companies reported this in varying levels with some saying that contamination was reducing, while others reported an increase in recent years.

Contamination in Australian wool is still regarded as being in much lower levels than other countries.

While there was some awareness of P and D certificate wools, and some processors having a preference for P certificates it was not regarded as a major consideration when purchasing wool.

The AWEX Woolclasser Code of Practice (COP) was seen as the reason that contamination in Australian wool was lower than other countries and the overall quality of clip preparation of wool was better than competitors.

However two companies also expressed concern that consignments of wool from Australia did not always match the objective measurements in the test data provided by AWTA, with one suggesting that wool growers were able to pack bales in a way that evaded the random sampling.

## **Bale Identification**

Bale RFID was not seen as being of any major benefit to processors, with one viewing it as being fashionable at the moment but would lead to no practical advantage.

The delegation also noticed a number of bales at the processing plants that were not branded correctly, with many bale labels not being completed at all.

## **Mulesing status**

While the demand for non-mulesed wool is not huge (around 10% of total orders) it is reported to be increasing. The demand is coming from European and US customers, while there is no demand coming from Chinese consumers.

All organisations that we met with indicated that they want to have completed NWDs, regardless of mulesing status, accompanying Australian wool. This will provide greater clarity around the volumes of the different types of wool that exist.

While PETA is not active in China they are continuing to target retailers in Hong Kong and Japan over the use of mulesed wool.

## **Price of Australian wool**

There were mixed views on the price of wool – with some processors saying that the current prices were acceptable (given the lower value of the Australian dollar) while others said it was too high and any increases would see a drop in demand.

The processors all expressed frustration with the price volatility of Australian wool and some implying that this is a reason why demand for wool is so low.

Despite the explanation of the free-market system within Australia, it was suggested on more than one occasion that there was market manipulation occurring either by grower or government intervention, due to the dramatic increase in the volume of wool offered for sale when prices rise.

Direct selling was widely viewed as not being a viable option as there was concern that the quality of wool sourced this way would not be reliable or consistent.

## **Value of the Woolmark**

While the delegation only met with first and second stage processors there was still a consistent view that the value of the Woolmark was in significant decline.

It was acknowledged that the Woolmark had previously been held in high regard by consumers but the value had definitely diminished in recent times, due to the lack of knowledge by younger consumers and a change in purchasing habits (i.e. increase in on-line shopping, with only a focus on price).

The Woolmark no longer guarantees market share due to a number of reasons including counterfeiting which is leading to a decreased perception of the value and quality of product and less prominence of pure woollen garments at the retail level.

It was suggested that the promotion of the Woolmark was not being directed effectively.

## **Constraints on the Chinese processing sector**

### *Environmental issues*

The environment is now a first-tier priority of the Chinese government. The entire wool processing industry is facing increased pressure from the government in light of these new environmental laws. All enterprises are now being rated on a 'green index' which are linked to tax incentives/disincentives.

While most plants have had to invest significant amounts of money in order to meet these new standards, many view this as a positive for the sector as it is believed that the stronger companies will meet the standards while the smaller, non-compliant plants will cease to exist.

### *Labour costs*

The processing sector is facing a shortage in labour as the younger generation are no longer satisfied with working in a factory.

There have also been significant increases in the cost of labour in China, in addition to rising wages and the introduction of penalty rates a further 34% is paid in tax that goes towards socialised funding.

These issues are both leading to an increase in production costs which in turn is seeing other countries such as Bangladesh, India and Vietnam being investigated to process wool.

## **Future of the wool industry**

The future of the wool industry again provided a mixed response from the organisations that the delegation met with.

Generally speaking the state-owned enterprises held a very negative view of the future while private equity companies were extremely positive and saw that there would always be demand for wool.

Competition from synthetics - which are improving in quality, increased cost of manufacturing, volatility of price, changes in purchasing habits, increased demand for sheep meat and the lack of appreciation of the quality of woollen products are all viewed as hindrances to the future of the wool industry.

Quality and the environmentally-friendly production of wool are viewed as positive attributes for the industry.

## **Recommendations**

1. It would be beneficial for Australian wool growers if areas of concern and any relevant issues from the JCAWWG meetings and other Australian wool delegations to China were more widely distributed throughout the growing sector in an attempt to address customer demands and requirements.
2. Greater clarification/education to the wool processing sector around the operations of the free-market system that Australian growers operate under would assist in the understanding of the supply of wool.
3. Given the increased awareness and prioritisation of environmental issues within China that wool's eco-credentials are emphasised and promoted as this is an area that synthetics cannot compete with wool.
4. On-going and increased extension to wool growers around the importance of quality clip preparation and contamination issues.
5. Increased promotion around the adoption of the NWD regardless of mulesing status to Australian growers.

## **Introduction**

A delegation of five WoolProducers Australia (WPA) Directors and CEO travelled to China from 26 June – 3 July, 2015.

The objective of the delegation was to ensure that Australian wool growers have an understanding of the current situation and potential issues in the China wool market, from raw wool through to retail. The focus of the tour was on wool for apparel use. While there are signs of growing demand for wool (including Australian wool) in interior textiles, the relatively short time in-country for the delegation restricted the scope to focusing on apparel wool.

By the end of the tour, participants gained an introduction and some understanding of:

- The trading of raw wool, including the main players, the main sources of wool for China's wool textile industry, the trading links, the importing and quota system.
- The processing of wool in China, the issues facing processors, including sources of wool, environmental concerns, labour constraints, energy availability, transport, competitors and competitive fibres. Participants had the opportunity to discuss with processors what wool attributes they are looking for and the relative importance of these attributes.
- The industry structure of China's wool textile industry, including the vertically integrated companies, the smaller knitwear companies, the distribution and retailing systems and the retailing structure.
- The relative importance of China's domestic retail market and its major export markets.
- The current challenges facing exporters of wool apparel to the main exporting countries of the European Union, Japan and the USA.

The delegation was hosted by the Chinese Ministry of Agriculture and arranged through the Department of Agriculture through the Australian Chinese Agriculture Cooperative Agreement (ACACA).

Australian Wool Innovation (AWI) also hosted the delegation whilst they were in Shanghai.

WPA were also engaged to conduct a consultancy on behalf of the Australia Wool Exchange (AWEX), investigating wool industry supply chain issues from a grower's perspective.

We would like to acknowledge and thank these organisations for enabling this study tour to occur.

The delegation was grateful to the organisations and enterprises that we met with in China for volunteering their time and providing valuable information. A list of organisations that the delegation met with are listed on the itinerary, found at appendix A.

The delegation would specifically like to acknowledge Gerard Zhao who acted as guide and translator; Dr Shi Jixin from the Office of Foreign Affairs and Economic Cooperation – Jiangsu Provincial Commission of Agriculture, who accompanied the delegation for part of the trip and Genevieve Morrow, WPA and Peter O'Donnell, Department of Agriculture who planned and coordinated the trip.

The following reports from the individual enterprises that the delegation met with are as they were reported. It is noted that some information including figures and percentages reported from different enterprises and sometimes within are not consistent.

## **Australian Embassy**

Dr Anna Sommerville – Australian Government Agricultural Councillor (Policy)  
Lachlan Crews – Economic Councillor

### **Overview of Embassy**

60 staff in the following:

- Agriculture
- Immigration
- Customs
- Treasury
- Australian Reserve Bank
- Education

### **China Economy Overview**

China government is in the process of reform, which was initiated in November, 2013, with the aim of rebalancing the economy. Major imbalances and tensions need to be addressed.

There is a 7% growth target, which is considered to be difficult to achieve, it is more likely to be 5-6% (\$8B) pa.

Traditionally China has relied on export driven growth (manufacturing), the government has determined that there will be greater domestic growth by investing in the service sector. The service sector in China currently accounts for 52% of GVP (Australia 75-80%).

With the environment now being a first order priority of the Chinese government the service sector is seen as favourable as it has less environmental impact, whilst also generating greater domestic employment.

There is also a drive to increase the proportion of domestic consumption.

The total amount of social financial debt is currently 275% above GVP.

Middle class expansion will start demanding our commodities:

- reasonably healthy outlook predicted
- fur and fibre predicted to continue to be in demand (71% of Australian wool)
- imported food demand will be strong due to unfavourable Chinese food safety history

Growth for Agricultural Services based on Japanese growth model, with a focus on food manufacturing.

The government is also driving land reform, trying to extract value through lease or selling of agricultural land. There is also a move to large scale farming, particularly in North East China.

China still has 5 year central government plans and it is unclear how the push to a more market driven focus will fit under these plans.

### **China/Australia Free Trade Agreement (ChAFTA)**

The signing of the ChAFTA in the previous week started the ratification process, but will need to go through both Australian and China domestic processes before it comes into effect. It is expected that

this will be quite straight forward in Australia as both the Indian and Korean FTA's has met little resistance. The process will be even more direct in China.

Australian tariffs will be phased out over four years, while China's tariffs will take up to 11 years (beef and milk powder). The 30,000t Country Specific Quota for clean wool will increase by 5% each year to almost 45,000t.

There are currently 160 embassies in China trying to establish or maintain relations with China. Australia is sixth largest exporter (with Hong Kong and Taiwan included in this number) and third largest Agricultural exporter. Australia is not insignificant to China.

### **Regular Bilateral Mechanisms**

- Australian Chinese Agricultural Cooperation Agreement (ACACA) – 30 years old (40 years for all trade between Australian and China)
- Sanitary and Phito-Sanitary (SPS) high level dialogue
- Dairy – supply and demand and foreign investment
- Wool – industry to industry talks (Joint Australia-China Wool Working Group)

There are ongoing discussions about trade negotiations, including technical market access issues.

Chinese consumers are increasingly becoming aware of food production due to recent domestic food safety issues, and are also pursuing the idea of happy, pasture raised, free range animals for consumption rather than intensive production.

### **Shaping engagement**

A number of issues are currently influencing discussion between Australia and China.

- ChAFTA
- White paper on Developing North Australia
- Agricultural Competiveness white paper

### **Current priorities**

- ChAFTA ratification and implementation
- Market access – maintenance and new

### **Key events**

- ChAFTA signing and entry-into-force
- Joint Agricultural Commission

### **Risks**

- Competition – market access, everyone wants to access China
- Food safety environment – number one priority for the government
- Food security sensitivities/food self sufficiency

### **Miscellaneous**

- The government of China is also cracking down on corruption including smuggling/substitution of meat
- Traceability systems are establishing in China but it is not centralised
- There is a kangaroo delegation in China the following week consisting of Senator Barry O'Sullivan (Qld); John Kelly (Kangaroo Industry Association Australia) and Ray Borda (Macro Meats)

## **Ministry of Agriculture**

Mr Wang Jian – Deputy Director

Dr Tian Kechuan – Director, Animal Breeding and Genetics

It is not easy to estimate the current sheep numbers in China but at the peak there were 30M fine wool sheep (19-22 micron), while there are 150M sheep and 150M goats. Sheep numbers are decreasing mainly due to market forces as sheep sold for meat are increasingly in demand and there is an undersupply – this is leading to higher prices.

Their understanding was that Australia's sheep flock was 95% meat, it was clarified that the majority of sheep, including Merino's eventually ended up being sold for meat and that the GVP is currently approximately 50:50 for wool and meat.

Shearing is mainly blade on small farms with mechanisation on larger farms and the majority are currently pasture raised (shedded in winter in Northern China), however there is a part of the flock that is being raised on feed utilising TMR fertilizer.

In China there is mainly a focus on fining up the domestic wool clip and increasing birth rates. There is also starting to be a move away from pasture raising and shepherds to intensive farming for sheep, this will also see an increase in the use of pesticides for disease control which is currently not part of animal husbandry in pasture raised production.

Genetics have mainly come from Australia since 1972, prior to this they came from the old Soviet Union. There is cooperative work with Australia particularly in Western China but they are seeking greater collaboration. There is government support for genetic improvement. China is utilising genetic benchmarking.

We explained that the trend in Australia is currently turning away from wool to meat – but this has plateaued.

Fertility was a point of interest for the MoA and wanted to know if the gains in sheep numbers were due to improvements in fertility. It was explained that there had been improvements in fertility but there was also advances in nutrition and general management that had contributed to improved fertility.

The MoA also wanted to know the make-up of the micron range, where it was explained that the biggest percentage (60%) of the clip 19 micron and finer. They were also interested to know what proportion of the Australian flock was 13 micron or finer (less than 1%).

Professor Tian said he was familiar with the Wool Education Centre but did not expand.

The major challenges in China wool production is that the younger generation are not willing to raise sheep and are moving to the city for employment. The average farm will have 100 sheep which means low efficiencies and hard work. The average age of farmers in China is about 53.

There are currently 414M pigs in China with sheep and cattle account for 12% of total production and poultry 20%. There is 20,000 tonnes of cashmere produced in China and no Mohair.

In regards to the impact of Australian sheep meat exports into China on local producers this was not viewed favourably by the MoA and they said that it had hugely damaged the local industry. The price of sheep meat in China is very high and this has caused smuggling.

The MoA were pretty familiar with AWI and MLA and their functions. China doesn't have a standardised levy system but have 'things' in place.

Dr Tian is head of the Animal Husbandry Industry Association and would like to start working together.

## **China Wool Textile Association (CWTA)**

Madam Huang Shuyuan – President

Mr Liu Yan – Secretary General

Ms Liu Dan – Director, Technology Division

Ms Zhang Shuqin – Director, Foreign Affairs Division

CWTA has been established for 20 years, with around 400 direct members and 10,000 enterprises, representing all areas along the supply chain, from prelim processing to all other areas. They also supply information for importing and domestic manufacturing.

CWTA recently hosted the 84<sup>th</sup> IWTO Congress. The theme of the Congress was 'Looking towards the Future', with a focus on environment and fashion.

80% of imported wool comes from Australia and the CWTA has relationships with all exporting countries.

Madam Huang would not be drawn on quality issues of Australian wool, including the thoughts on unskirted clips, only saying that all wool is cleaned for preliminary processing and different customers want different qualities. The Joint China Australia Wool Working Group discusses these types of issues and will be meeting next in Nanjing in September.

The relationship with AWI was viewed favourably and the Woolmark Prize provided good collaboration, with the four CWTA staff present were all able to train and learn in Australia as part of this partnership. The delegation went onto farms and witnessed shearing.

China is highly dependent on Australian wool, with it being the main source of textile enterprises. Australian wool is the most suitable for production with fine wool being highly sought after.

Because of price and volume (wool currently accounting for less than 1% of global textile) there is a continued shift away from wool. Both wool and cotton are being replaced by synthetics. 400,000t of wool processed to be used in apparel but still only equates to less than 1%.

The low volume of wool is not a concern for Madam Huang as wool can be replaced by synthetics.

Chinese wool roughly accounts for 10% of the total volume and growers cannot provide consistency in product, but it is thought that 13,000t of fine wool is produced per annum. There is no standardised system for selling wool in China, with agents going on-farm to inspect wool and offer a price or buy via a small auction.

Madam Huang said that she hoped that both the classing requirements were stricter and that testing results were fairer within. When asked for clarification on this she indicated that the greasy wool being received was different to the AWTA test results. When asked how we could assist she said that the Joint Australian-China Wool Working Group would look at this issue.

The number of enterprises using the Woolmark is decreasing. Some enterprises are not meeting the standards but there is a belief that as the Woolmark does not guarantee market share and during the sales process it is not seen as adding enough value to justify the expense of licensing.

The Chinese government is clamping down on pollutions meaning that enterprises can no longer do what they used to and must adhere to the law.

The CWTA host many communication projects and activities with many members participating. There have been discussions about upgrading and renewal of facilities with members willing to share information.

CWTA saw the ChAFTA having little impact because they have enough product and quota. Members will not see much benefit.

## **Michell Wool Pty Ltd**

Dr Andrew Liang – General Manager

### **Overview**

Michell's moved to the current location in 2007, following a change in the processing environment in Australia. They are the only processing plant in this area. Half of the machinery in the plant came from Adelaide and the remaining from Taiwan – they are now in the process of upgrading this machinery.

Michell's had always had leading environmental credentials, however the new Chinese environmental laws recently introduced has seen them having to upgrade their water treatment facilities to comply. They are currently in discussions with the local government on utilising mud from the wool for compost.

Three main lines are currently processed at Michell's:

- carbonised wool – 6000t pa (16,000t in Michell's Australia)
- Superwash – 2000t pa
- tops for the bedding industry

Michell's have issues with the quota as they are strictly controlled and it is not expected that ChAFTA will address these issues. Wool under quota attracts 1% export duties while wool outside the quota attract 8%. There are two types of quotas, one for tops and one for greasy and scoured wool – 90% of wool from Australia is in the greasy form.

When Michell's moved to China they started with a zero quota and after eight years they now have 3,000t quota, while they are currently processing 6,000t. They are currently operating under a 50:50 ratio of processing their own wool and contract processing to other companies.

Andrew did mention that other mills that have been operating for 50 years are only getting a couple of hundred tonnes.

Operating in China is quite difficult, due to the following reasons:

- Relationship with the local government – operations are continually scrutinised and monitored and protocols must be met
- Labour costs increase – in addition to higher wages and penalty rates (8 hours normal pay and 4 hours at time and a half) there is an additional 34% tax that goes towards socialised funding
- Environmental laws – particularly stringent for foreign invested enterprises as they must have higher standards than local companies. If processors cannot meet these standards the government withholds their license until the problems are rectified, if these standards are not met within a set period of time the licences are with withdrawn. Waste water treatment accounts for 25% of cost of production

Michell's is a member of CWTA and the China Wool Merchant Association.

Michell's employ 140 staff over two 12 hour shifts per day, working near capacity. They currently have 2-3 months' supply of greasy wool – scour and carbonising work. They are currently building a new warehouse to store greasy wool as in the last season a lot of wool was covered and stored outside.

There is 8% lanolin in adult wool and 5% lanolin in lamb's wool. Lanolin pricing has increased trading at \$2.90/kg in 2014 to \$4.50/kg currently.

Michell's still regard Australian wool as the best in the world in terms of quality, handle and preparation (it was noted that contamination is not an issue at all for Australian wool any more).

South Africa is gaining in quality for 17-19 micron wool but there preparation and contamination is a massive issue.

In terms of P and D certificate wool, it is not considered an issue for carbonised wool but is posing a problem for combing wool. They do have a preference for P certificate wool.

Wool from mulesed sheep is raised often for exported product to Europe, with some buyers being very strict, but domestically nobody is interested. Michell's have to declare a lot of wool as 'unknown status' and it would be better for everybody if growers filled out NWDs regardless of mulesing status.

There are no logistical issues getting wool from Australia, with wool being transported from Shanghai Port to the plant by road (80kms) and transportation is currently considered cheap. However there are problems with import inspection services in China with the process taking up to 10 days.

Electronic bale identification is regarded as 'fashionable' at the moment but is not delivering any practical benefits at the processing end.

Andrew considered the Woolmark as still being an important tool and provides value to the product, but Michell's doesn't use it much as it is more a tool targeted to end users. However there is an issue with quality in that the Woolmark represents 100% wool but does not consider the quality of that wool.

Also mentioned was the standard for environmental safeguards has impeded business with severe penalties in some incidents causing closure by not renewing their license.

Andrew's thought that in ten years China will still be the major player in wool processing more so in early stage processing.

## **Jiangsu Australia Harvest Group Co, Ltd**

Mr Zhongxing Zhu – CEO

Mr Zhongxian Zhu – President

### **Overview**

Over all Australian Harvest is happy with Australian clip preparation, but according to the CEO the most serious problem is cotted wool and medullated fibres from comeback wools, there are also wools that haven't been classed properly. While the Chairman said that the CVH of Australian is worse than South Africa (too long) and the tensile strength does not meet their standards.

They prefer medium/fine wool (19.5-22.6 micron) which accounts for 70%, 18.5 micron 15% and 15.5, 16.5, 17.5, 26.8 and 28.6 15%.

Australian Harvest has a close relationship with AWI and Stuart McCullough and Michael Jackson from AWTA. They are happy with the test data from AWTA.

They see the Woolmark as very important to verify the product.

The CEO said that there should be less production of wool as there is an oversupply. This will keep the price higher and stimulate competition. He mentioned that information from the Australian government is that production has been reducing by 2%, they have also heard that meat is now more valuable than wool from comebacks.

In terms of micron ranges there is no fixed trend as it is reliant on consumer demand.

Regulations and policies implemented by government states that Australian Harvest does not exhibit extravagance with government officials when doing business. The army also now has regulation not to exhibit extravagance and therefore aren't using as much wool in their uniforms therefore this has caused demand to drop dramatically.

The Chairman said that demand for wool in China is concerning for everyone and is interested in increasing demand. Wool is now high end and fashionable but his 25 years' experience tells him that wool is susceptible to influence of other fibres.

An increase in price in wool will cause demand to drop. In the future if the price for wool is at high levels consumers will choose alternatives and Top Makers would chose other raw materials. At the start of the year 1170c no one was willing to buy wool but when it was 900c demand increased. The price at 1000c will see demand remain sloppy.

The recent volatility and specifically the spike in early June has caused orders to stop. The three months following July will see less demand for wool.

According to the Chairman, in order to sell more wool there needs to be:

- a fashionable product designed
- cost saving – many other types of fibre competing with wool
- focus by growers to produce different types of wool – don't flood the market with one type

The Chairman also contradicted the CEO by saying that wool production should increase and that the \$A is now agreeable.

## **Tianyu Wool Industry**

Helen Han – Marketing Director

### **Overview**

Tianyu employs 400 staff over 3 shifts, 7 days a week and imports 23-25kt clean wool per year, with 80% of that coming from Australia. Tianyu generally buy through auction and a small amount through traders. They are interested in sourcing wool directly from growers using brokers who approach them.

Tianyu keep a large supply on hand with 3 months' worth of greasy wool but they don't stockpile tops as there is a demand for this as the high quality is known.

Tianyu established a waste water treatment facility in 2008, spending more than \$A25M to be compliant with the new environmental laws that are stricter than Italy. They see this as a good as stronger companies will get more competitive and gain a competitive edge.

They have a very good relationship with Jimmy Jackson from AWI and appreciate the technical support they also receive from AWI.

They regard Australian wool as the best but contamination is still an issue, although not as bad as other countries. Medullated fibres are not such an issue. Some unskirted clips are coming through and this is an issue.

A small percentage (far less than 10%) of European customers are requesting non-mulesed wool, while Japanese, Korean and Turkish customers do not care about it. Tianyu would like to see growers using the NWD.

There is an issue with bale labels missing on the bottom caused by dumping. Bale RFID might assist in this area and they asked that we speak to AWEX about this. Tianyu will buy finer wool undumped.

Issues with AWTA test results with wool not matching test data.

Tianyu would like to see stability across supply and price. Staple length is dependent on the market with short wool currently being too hot.

They saw the Woolmark as valuable as consumers to check for it at the point-of-sale, but Tianyu don't use it as they are only raw wool suppliers.

Tianyu requested the breakdown of microns in the Australian clip, we provided an undertaking that we would provide this information.

Tianyu commented that Mr Wang believes in the life cycle of wool.

## **SDIC – Nanjing Wool Market Company**

Mr Jian Chen – Deputy General Manager

Mr Huo Yan – Vice General Manager

Madam Yang Xiaoxiong – President

### **Overview**

SDIC are involved with wool, cotton, timber, chemicals, and steel, warehousing and logistics services. They are the former China Textile Corporation Company which belongs to the Ministry of Textiles and conducts all imports on behalf of Chinese government.

The Nanjing Wool Market (NWM) was established in 1987 with the construction of the first warehouse at Nanjing Port, which was sponsored by the Australian and Chinese governments.

There are eight functions of NWM:

**1. Information and website**

The NWM Information (newsletter) is issued weekly. With the website Woolmarket.com.cn being available in English

**2. Training**

Provides regular training of wool businesses (over 70) for Chinese and wool producing countries.

Chinese wool classer training – working with AWI, AWEX and AWTA. AWEX assists with training on an annual basis for Australian Wool Classification and Appraisal Training Program and has converted the Wool Classers' COP into Chinese.

NWM also host wool grower delegations and provides domestic wool education.

**3. Auction and Trade**

NWM organise auctions for domestic and Australian wool (Elders) – using wool display samples.

**4. NWM Conference**

Established in 1988, over 600 participants (100 from Australia)

This year it will be held on 11-13 September in Qingda, themed 'New Market, New Rules'.

**5. Social Services**

Secretariat of Wool Special Committee of Chinese Wool Textile, Joint China Australia Wool Working Group and are about to establish Joint NZ/China Wool Working Group  
NWM established CWTA

**6. Arbitration Functions**

NWM can settle disputes for trade issues. They are partners with Jiangsu Commodity Inspection Bureau providing members with integrated services for wool testing services

**7. Finance Functions**

Cooperate with banks to finance services, including warehouse receipt of materials to pawn, discounting, Bills of Exchange and letters of credit, etc.

**8. NWM Certification**

NWM Certification incorporates in the China Wool Textile Animal Welfare System Verifying mulesing status of wool

The China wool textile industry is 139 years old. The current ranking of fabrics are as follows:

1. Synthetics
2. Cotton
3. Wool
4. Silk

Wool currently accounts for about 3.5% of the total textile outputs. The domestic market accounts for 70-80% of wool products which has been stable for the last 5 years.

In 2014 there was 260,488 tonnes of wool processed in China, down 8% from the previous year. While Jan – May 2015 there has been 122.600 tonnes processed up 35.8% on the same time as 2014. This has mainly been double-phase material in demand, which is expected to continue for the rest of the year. Meanwhile cotton trade has remained stable since 2005.

Blanket and carpet wools currently accounts for 55% of all woollen exports from China.

### **Global Tariff Quota**

WTO tariff – 287,000 tonnes attracting 1 cent, anything over this amount attracts 13 cents.

ChAFTA will see the country specific quota for Australia grow from the initial 30,000 tonnes by 5% each year until it reaches 45,000 tonnes. New Zealand's quota under their free trade agreement will expand to 37,000 tonnes (currently NZ exported about 6,000 tonnes of wool to China in 2014).

### **China's Wool Production Standards**

China has 139.6M sheep, producing 90% meat and 10% wool (400,057t greasy wool in 2012). In 2013 China produced 132,000 tonnes greasy fine wool and 135,000t greasy semi-fine wool with an average 47% yield. About 56,7000t for worsted and semi-worsted and 58,000t for carpet production.

China fine wool – averages 20-22.5 micron, 60-85mm and 40-55% yield, grazing mainly in the north of China.

### **Sheep Stock on Farm**

Heilongjiang Province – 3.3M sheep, 22.6 – 24.1 micron

Gunsunn Province – 1,180,400 (701,000 fine wool), 21 micron

No 77 Group Xinjian Production and Construction Corps (Army) – 51,000, 19.5 – 21 micron

Wushenqu Province – 1.2M, 19.5 – 21 micron

Sanjiaocheng Sheep Breeding Farm Qinghai – 450,000

The average farm has 400-500 sheep per family, with natural grazing all year round except for winter where they are shedded and fed hay and grain.

### **Types of sheep in China**

- China Merino, four types:
  - Xinji
  - Erdos Superfine
  - Gansu Mountain
  - Soviet
- Aohan fine wool
- Xinjiang fine wool
- East-northern fine wool
- Introduced Polwarth
- Introduced Romney
- Introduced Guman Meat Merino

### **Wool Preparation**

Blade and mechanical shearing (many second cuts) and the poor preparation of Chinese wool is due to the lower prices paid domestically. Wool bales weigh between 100-130kgs.

Shearing season starts late May and finishes mid-June, with wool sold in July and August.

NWM provides information on domestic wool production and quality, this information is provided to the mills who go to the farm at shearing time to appraise and purchase the wool.

Wool is generally purchased through private negotiations and only sold through the auction system when prices are low.

### **Miscellaneous**

Australian wool generally has no problems except for contamination, including dark fibres. It is viewed that the Wool Classers' COP is the reason for higher standards.

Demand for non-mulesed wool is not as strong as it has been previously due to a decline in exportation, the heat has gone out of the issue.

Bale RFID is not seen as beneficial to NWM.

The Woolmark is not seen as valuable due to problems in promotion by AWI. It is believed that they have not chosen the right direction for the Woolmark. Manufacturers are not putting the label on clothes as the younger generation is not interested – the label needs to have the composition of the fabric.

Many people are now shopping online and don't care if the product is made of wool – their only consideration is the price. Only white collar workers would touch fabric and this trend is declining and this is coupled with the improvement in quality of synthetics.

Demand for man-made fabrics is increasing and wool is decreasing. AWI should be focussing on marketing wool to the masses. Celebrity endorsement of wool would not increase wool sales in China.

Supply of wool is currently matching demand, an increase in supply would affect the current prices. Madam Yang believes that demand will continue to decline, but it will stabilise and exist.

Online wool selling maybe an option however many questions would need to be resolved before it became common place.

Madam Yang also believes that in 50-100 years sheep will only be used for meat as competition from synthetics are too strong. While she enjoys her job she will not let her children enter the industry as there is no future. The market is getting smaller and there is no improvement – this is why Australian farmers are getting older.

## **Ningbo Haufeng Knitting**

Jiagguo Chen – Director

### **Overview**

Privately owned equity firm established 1992 officially started production in mid-1993 using second hand machinery imported from Europe. Yarn spinning using wool, used to provide underwear but not since closing the second factory that produced these products.

Employs 130 staff in 3 shifts over 24 hours. Currently using 600t – 900t of tops per year, down from 1,000t, seldom using other materials.

Mainly producing top end products, with the main exporting countries being Europe and New Zealand but the majority of product is consumed domestically. Used to export a lot of yarn to Australia but not anymore.

Sources tops from New Chewa, shifting away from Australian Harvest and Tianyu. Cost is part of the reason for sourcing from New Chewa, but it is also geographically closer therefore making logistics easier and the tops are of equal quality. Tianyu provide shorter tops and they require longer.

The order-to-shipment time differs depending on the season, during busy seasons it takes 2 months from order to start production and one month to produce yarn. During the slow seasons it can take one month – 2 weeks to start production and 2 weeks to finish).

Quality of tops has improved in the last 20 years and is improving over time. Imported machinery has helped.

### **Future of Haufeng**

It is hard to anticipate the future as the wool industry is labour intensive and younger people do not want to work three shifts. There is also an increase in labour costs.

In the past the wool manufacturing countries moved to China but now they are moving away due to labour costs. This is also happening in the cotton industry where they are moving processing to Vietnam.

There is probably not much scope for increased efficiencies as the industry has matured.

Improvements could be made in terms of shrinkage control. Superwash is not environmentally friendly and the US and European countries are not satisfied with Superwash's eco credentials – technologies for manufacturing could be improved.

### **Woolmark**

Since the focus of the business has been just on yarn manufacture they are not really interested in the Woolmark, but believe that the Woolmark is losing relevance for the following reasons:

1. Not all licensees are abiding by the standards and there are many cases where blended woollen products are being labelled with the Woolmark
2. Concept and value are decreasing because of misuse
3. Decreasing production and less prominence of pure-wool products

### **Relationship with AWI**

Close relationship, particularly with Jimmy Jackson and the Shanghai office, but since the removal of the clothing production the relationship has declined but they are still in touch.

### **Animal Welfare**

There are requirements for animal welfare and this is increasing, with many clients requiring sheep to be treated well. Australian sheep meet these standards.

Demand for non-mulesed wool is increasing each year, with about 10% of clients currently seeking this type of wool. This demand is coming from Australia, NZ, US and Europe, but there is no demand within China.

The NWD is a must and there is a secondary certification that top makers need to provide regarding mulesing status (NWM certification)

### **Wool Prices**

Price volatility is annoying to them and hinders their business – they want to see more stable prices.

The current EMI is acceptable to them.

### **Wool Specifications**

There is a preference for higher than average strength – most spinning machines run very fast so need strong wool.

Higher than average length, 70mm with a maximum of 98mm.

Strict requirements for contaminants in their tops, including vegetable matter.

### **Environmental Law**

Entire industry facing increased pressure from the government. Many dye factories have closed for this reason.

### **Wool Quality**

Biggest concern regarding contamination is stain and fine nylon fibres from bales while fine grasses are hard to process, but spiral and medium grasses can be combed.

## **New Chuwa Wool Company (Xiano Textiles)**

Mr Hua Xinzhong – Director

### **Overview**

Xiano Textile is an equity controlled company and is the parent company of New Chuwa Wool, who produce tops and a dyeing company. It was established in 1991, mainly purchasing wool from Australia and was listed on the Stock Exchange at the end of 2014.

New Chuwa employs 300 people over two shifts (workers don't like three shifts), six days per week. Labour costs are increasing every year.

New Chuwa is a joint venture between China and Taiwan and the functions are:

- Scouring
- Combing
- Spinning

Xiano Textiles produce 75,000t knitting yarns and 7,000t of tops pa, with 50% and 60-65% of this being exported respectively. They also conduct chemical treatment of tops (anti-shrinking, etc.). New Chuwa and the dyeing company are controlled by Xiano but operate independently.

The dyeing factory provides top and yarn dyeing to Xiano and other companies.

Greasy wool is sourced from Australia, New Zealand and South Africa, with 80% coming from Australia. All wool is less than 23 micron (16-23 micron) with a length between 65-110mm. This wool is mainly combing wools. New Chuwa have a preference to have finer wool delivered undumped and at the moment this is viable due to the low freight costs.

From the Shanghai Port they transport wool to the factories via roads.

### **Future of New Chuwa**

They have been in this industry for so long that they have developed an emotional attachment to wool – they view wool as a necessity and have been increasing their consumption of wool.

Xiano has this year also purchased a wool property in Aspley, Victoria.

They see synthetics, global warming and the volatility of the price of wool as reasons as to why the proportion of wool now only accounts for 3.5% of the consumption market.

### **Perceptions of Australian Wool**

Overall the quality is good but contamination is increasing from coloured (black and stain) fibre in recent years, including 17 micron wools.

Clothing and other foreign materials are also being found. Australian growers (shed staff) need to improve their management as they have had to stop using automated methods of emptying bales and utilise manual labour to check contents of the bales.

There is also a strong belief that the wool on the peripheral of the bales is better quality and the middle wool in the pack is bad – it is believed that this is deliberately done to deceive buyers. It was explained that core sampling is completely random and coupled with the size of clips that this is not

practical or feasible for growers to do. They responded by saying that they don't know how it is done but it is reality.

New Chuwa mainly purchase P certified wool in farm lots due to the requirements. They may consider it preferable that lot sizes are bigger than the average of six bales but they are aware that there are a lot of different size farms and this may not be possible.

### **Bale RFID**

They considered that this may be useful but were concerned that it would be additional labour for them removing the chips. It was explained that they would not have to remove it as the chip would be in the label.

### **Animal Welfare**

The demand for non-mulesed wool is increasing. They have recently started buying several hundred tonnes of wool from South Africa as they cannot purchase enough from Australia, even though they are disappointed with the quality of South African wool.

The customers are mainly from Europe and the US.

New Chuwa sees a need for all wool to be accompanied by an NWD.

### **Environmental laws**

There is increasing pressure for environmental protection and part of their responsibility of owning an enterprise is increasing investment in this area. Although there is a price increase they will develop better technologies to be more efficient.

The company has invested around \$A25M in establishing a new scouring plant.

There is also 10,000sq meters of gardens at the factory site to help counter the 'dirty' image that the wool processing sector has in China.

### **Woolmark**

It was very valuable to them as a company and started using it when they were established as it helped their business grow, however it is losing its status particularly with younger customers – knowledge of wool is decreasing.

Wool products are good quality and are quite expensive so therefore is not targeting younger consumers who are more interested with keeping up with changing fashions.

### **Relationship with AWI**

They have a close relationship with AWI, particularly regarding technology.

### **Direct Selling**

They have considered purchasing direct from growers previously but have concerns about the quality of product and also the amount of resources it would take for them to negotiate deals. It was explained that all wool preparation is standardised in Australia so regardless of the way that wool is purchased the quality would be the same.

There is some trust/confidence in brokers sourcing wool directly as they know the growers and the product.

They also think they may be able to develop close relationships with the neighbours from Aspley and purchase wool that way.

The wool they purchase from NZ is purchased direct from growers.

They were not overly keen on sale by description as they believe that different clients want different things.

The volatility of the wool market is a massive concern to them and believe that this comes from wool growers influencing the market, believing that the market is controlled due to fluctuations in the volume of wool for sale through the auction system.

It was explained that growers will store wool until the market improves and then there is an influx of wool through the system – price fluctuations are also a major problem for growers.

## **Australian Wool Innovation/The Woolmark Company**

Alex Lai – Country Manager, Hong Kong

### **Perceptions of Australian wool**

50% of the wool imported into China is Australian. The main feedback that AWI are hearing is skin pieces being an issue for processors over the past 2-3 years.

PETA is also a big issue for industry, whilst not in China they are continuing to target retailers in Japan, Korea and Hong Kong regarding mulesing. We were assured that the traders and retailers know the real story through briefings provided by AWI.

The issue of lower quality Australian wool is that the exporters are source cheaper wool to blend but then are not satisfied with the end product.

### **China Wool Industry**

China is expected to have 7% GDP growth in 2015. The luxury market value was worth \$US25 billion in 2014 which was down 11% y-o-y.

Many retailers including Hugo Boss, Zegna, Burberry and Chanel have closed many stores in China over the past 12 months.

There is greater importance of domestic market but manufacturing is servicing both domestic and exported materials.

Increasing demand of fashion consumption causing an increase in demand of fashion design, style and material quality – especially in the light-weight fabrics.

Even though there is a common brand vision the key market drivers need to be revisited due to a lack of knowledge from the younger demographic regarding wool.

China is the hub of the global textile industry and also the largest wool processing and supplier of woollen products, currently taking 75% of all of Australia's wool.

The total import of wool into China is 126.25mkg pa.

### **Quota**

In terms of secondary processors (spinners and weavers) wanting access to the wool quota, the larger firms have quotas while smaller ones don't – therefore the Chinese government does not allocate quotas to them. There is a desire by some of these secondary processors to gain quota so that they can conduct commissioned scouring as an additional source of income.

### **Pressures and Challenges**

- Labour – shortage due to younger people not wanting to work in factories and increasing wages
- Production costs – environment and land use
- Competition – processing is occurring in Bangladesh, India and Vietnam
- Consumer trends – consumers are now less brand aware
- Environment – stricter laws
- Market – volatility

Alex believes that the wool industry needs to target and compete with silk and cashmere as they also have high cost of production rather the cheaper than poly and synthetics.

There is a need to improve industry innovation capability through product development as the entire supply chain is being squeezed meaning tight margins for those involved in producing and processing wool. There has to be a new breakthrough in brand building.

### **Environment**

Enterprises are now being rated on a green index – the higher the rating the higher tax that has to be paid.

The Northern Hemisphere is for the first time scrutinising China's impacts from processing wool and China has to respond.

AWI are conducting a high end restructure in this area to be announced soon.

### **TWC Activities**

Farm to fashion - improving productivity and wool quality to build demand. There is a need to increase demand for wool by addressing barriers, informing consumers of benefits and providing brand support.

Increasing demand for wool by integrating and commercialising research, development and marketing activities with stakeholders.

There is a need to look at new textile technologies from other industries to make wool products competitive. Consumer trends drive innovations and innovation adds value through increasing versatility of Merino wool. Wool need to be known as more than just formal wear.

- Merino Touch – softness and luxury targeted at the higher end.
- Merino Care – for the garment, wearer and the planet
- Merino Visual – new looks and textures for casual wear in order to attract the younger generation to wool which will create and build demand for wool

### **Innovations Development**

A presentation and samples were provided on the new types of fabrics that have been developed, including:

- MW Wool
- Mercerized Merino
- Retract Merino
- Wrinkled Merino
- 3D Merino
- Merino Devore
- Mottled Merino
- Merino Air Yarns
- Nevlana Elite and Sports
- Wool Wadding
- Functional products

### **Woolmark Overview**

When there was counterfeiting of Woolmark that those caught misusing the brand had their licences removed.

There are a total of 200 licensees of Woolmark, each paying \$7,000 per licence.

In China people know the value of the Woolmark but the younger generation is not as familiar with it therefore there is a lot of education, training and marketing being conducted.

### **Marketing Campaigns:**

#### **International Woolmark Prize**

Designers from Europe, India, Middle East, Asia, Australian and the US.

The women's wear awards were held in Beijing this year – the first time it has been held outside of Europe, and had Victoria Beckham as a judge.

The 2015/16 Asia finals will be held in July and has Tom Brown, Lu Yen (model), the Editor of Asian Vogue and two boutiques as the judges.

#### **Cool Wool – 'When it's hot, it's not'**

Trans-season concept that has been conducted in India and Dubai for the past couple of years. This is being rolled out in China this summer (July), and will work with well-known brand partners.

Celebrity endorsement will also be utilised as well as social media, culminating in the GQ Awards in September.

#### **Campaign for Wool**

Fourth year in Shanghai, utilising an increasing number of brand partners.

There will be an October promotion utilising a number of promotional platforms.

#### **Miscellaneous**

The working relationships with AWEX and AWTA are very good. AWI also host FAWO when they visit China.

Selling system in Australia is a big problem as it generates a low competition. If SE Asia and Russia entered the market there could be a big change. Alex agreed that direct selling of wool would be beneficial.

He also said that there was an understanding of processors of the free-market system within Australia and that they will always suggest that there is market manipulation occurring in Australia despite their knowledge.

The future of wool in China is regarded as 'brilliant' due to the cold climate and the fact that Chinese love wool, but it is key that the younger generation need to be educated in using wool.

## **Appendix A**

Date	Organisation	Location	Host
26 June	Australian Embassy	Beijing	Dr Anna Sommerville – Agricultural Councillor (Policy) Lachlan Crews – Economic Councillor
	Ministry of Agriculture	Beijing	Mr Wang Jian – Deputy Director Dr Tian Kechuan – Director, Animal Breeding and Genetics
	Chinese Wool Textile Association	Beijing	Madam Huang Shuyuan – President Mr Liu Yan – Secretary General Ms Liu Dan – Director, Technology Division Ms Zhang Shuqin – Director, Foreign Affairs Division
29 June	Michell Wool Pty Ltd	Zhang Jiagang Free Trade Zone	Dr Andrew Liang – General Manager
	Jiangsu Australia Harvest Group Co, Ltd	Jiangsu	Mr Zhongxing Zhu – CEO Mr Zhongxian Zhu – President
	Tianyu Wool Industry	Jiangsu	Ms Helen Han – Marketing Director
30 June	SDIC - Nanjing Wool Market Company	Nanjing	Mr Jian Chen – Deputy General Manager Mr Huo Yan – Vice General Manager Madam Yang Xiaoxiong – President
1 July	Ningbo Haufeng Knitting	Ningbo	Mr Jiagguo Chen – Director
2 July	New Chuwa Wool Company (Xiano Textiles)	Hangzhou	Mr Hua Xinzong – Director
3 July	Australian Wool Innovation/The Woolmark Company	Shanghai	Mr Alex Lai – Country Manager