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INDUSTRY FUNDED WOOL PROMOTION
AN ECONOMIC PERSPECTIVE

Stephen Beare

Australian Bureau of Agricultural and Resource Economics

Stephen Beare is Deputy Director of ABARE and is responsible for the management of ABARE's program of economic policy research in resource management. Dr Beare has worked extensively in the analysis of farm financial and physical performance and wool production and marketing since joining ABARE in 1985. His current area of research is the integration of scientific and economic analysis in evaluating multiple land and water use policy options. His professional background is in the areas of mathematical modelling and statistical analysis. Dr Beare holds a PhD and a Masters degree in economics from Oregon State University and a Bachelor of Science degree from the University of California.

The issue of whether industry funded promotion of generic agricultural products pays has been debated for a long time. Despite a number of economic studies, the majority of which attribute significant increases in demand to the promotion of agricultural products, a considerable degree of skepticism appears to remain. The skepticism stems, in part, from the practical difficulties in defining and measuring the impacts of promotional expenditure on product demand and then determining who are the winners along the product chain between primary producers and the final consumer. The question is difficult to answer with any degree of certainty.

The most extensive analysis of wool promotion was published in 1987 by the Bureau of Agricultural Economics (now ABARE) and the former Australian Wool Corporation. The study estimated the net return to Australian wool growers of a five year promotional effort did in fact generate a net benefit. Depending on the assumption made about the extent to which an increase in wool demand translated into higher wool prices, the return was estimated to lie between 3 and 97 per cent.

To what extent does the 1987 study support the ongoing promotional expenditure on wool? Studies for other agricultural products would not support any strong inferences as they have indicated that both the targeted market and the nature of the campaign are important. A study by Coloman Kinnucan (1993) found that US government supported cotton promotion in Asia was effective in some markets and not in others. A significant relationship between promotional expenditure and cotton demand was found for Hong Kong, Japan and South Korea but not for the Philippines, Taiwan or Thailand. So it would be difficult to extend results drawn from the US market to important wool markets such as China, western Europe and Japan.

In a study of meat advertising in the United States, Brester and Schroeder (1995) found a significant relationship between branded advertising of beef, pork and chicken and household demand. However, no significant effects were detected for generic advertising. Again, it would be difficult to extend the results from targeted retail advertising in the United States to "Wool Mark" or other campaigns directed in what many believe to be a different retail apparel trade today then just then years ago.

This would seem to leave wool growers in the rather unenviable position of knowing neither whether promotion is a cost effective way of increasing grower returns nor if cutting back on promotion will have an adverse impact on wool demand and prices. To some extent this may be an inherent difficulty in evaluating the effectiveness of promotion but it may also reflect failure of the industry to insist on the ongoing and independent scrutiny of the expenditure.

This is not simply a call to conduct economic analyses into the effectiveness of promotion. There are some simple questions which can be asked first. Are the institutional arrangements in place to ensure the accountability of promotional expenditure? Would an independent review of wool promotion strategies by independent advertising professionals support the current approach adopted by the IWS?

Even if it was possible to demonstrate a clear return to industry funded wool promotion, the decision still needs to be placed into the context of other investment options for both the industry as a whole and for individual growers. These options include research and development, on and off-farm investments and the repayment of farm debt. There are different levels of expected risks and returns which

may be attached to such investments. There may be a need to shift the balance of the portfolio as these returns change over time with movements in the market costs of funds, emerging opportunities for profitable on-farm investment arising from research and development and shifts in apparel markets that might offer profitable promotion opportunities.

The investment margins on and off farm are generally unique to the farm business. The concert here is about decisions taken on an industry level, where the decision by the majority of growers to invest through a levy imposes financial obligations on all growers. It may be of interest to compare the industry level options of promotion and R&D. On a per farm basis in 1996-97, ABARE estimates that specialist sheep producers spent the equivalent of 20 per cent of their farm cash operating surplus on promotion (ABARE 1997). This compares with an expenditure on R&D of under 3 percent.

Returns to industry expenditure on R&D in agriculture have also been the subject of numerous economic studies and, as with promotion, a great deal of uncertainty remains. However, in contrast to promotion, wool R&D expenditure has historically been subject to a greater degree of evaluation and, correspondingly, there is a greater breadth of analysis reported in Australian economics literature. Research has ranged from estimating the level of return to how best to target expenditure.

Mullen and Cox (1995) estimated the internal rate of return to R&D in broadacre agriculture in a range of 30 to 40 per cent. The nature of broadacre productions systems would suggest that most of these gains have been captured in cropping. This is supported by ABARE estimates of the level of productivity growth in cropping versus livestock industries. Estimated productivity growth on specialist cropping farms was over four times higher than for specialist sheep farms between 1977-78 and 1993-94 (ABARE 1995).

Despite relatively low rates of productivity growth on sheep specialist farms, Scobie, Mullen and Alston (1991) report internal rates of return to wool R&D of between 18 and 25 per cent. Mullen, Alston and Wohlgenant (1989) concluded that farm level research has the greatest potential payoff when compared with research aimed at lowering the cost of textile processing. Nevertheless, the ABARE analysis of CIROSPUN technology suggests that high levels of return to wool growers are possible within the textile industry when research is directed toward improving the processing characteristics of wool.

Concluding Comments

In considering a producer levy to pay for either promotion or R&D, there are three threshold arguments for producers. The first pertains to individual producers and their willingness to support high risk and return activities which require overall participation to obtain results, given the investment and other needs of their individual businesses. The second is to get the balance of any such investment correct. The last is to consider the institutional arrangements by which these investment services are delivered, with the aim of ensuring that future investment decisions are best directed.

The first issue can only be considered by growers in the context of their own circumstance. The second issue raises some interesting consideration of current levels of promotion versus R&D expenditure. When considering rates of return alone, the level of expenditure is not of concern. However when considering a portfolio of investments with limited funding, the balance of spending is important. There is no conclusive evidence as to a favourable shift in the balance of wool industry investment in promotion versus R&D. Both represent relatively high costs (in terms of current industry profit margins) and a high return.

It would seem that there is a good cause to ask advertising providers to compete for support as opposed to relying on traditional allocation for an industry levy. The R&D model, with industry review of proposals from independent providers, is inherently more competitive than internally provided advertising and promotion.

R&D promotion share common features in that the benefits of either are difficult to quantify but given the pace of change in the world about us, it is easy to believe both are a necessity.

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Authorised By: Assoc. Prof. Bill Malcolm, Agriculture and Food Systems
Maintainer: Nanette Esparon, Agriculture and Food Systems
Email: webmaster@landfood.unimelb.edu.au