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The Wool Corporation's Stocks

John Hyde

Except when addressing their dogs, woolgrowers are a mild-mannered lot. Nevertheless, I imagine that the response to someone who advised leaving half the clip in the shed and borrowing its value at around 20% interest, would be colourful. To cover two-years interest charges alone, the woolgrower would have to get 144% of the present price. Yet that is what the Australian Wool Corporation (AWC) is doing with his wool.

So far this season the AWC has purchased over half of the Australian wool clip at an average minimum reserve price of 870c per kilogram. Its stock is already 1.8 million bales. It has already spent its $1.8 billion cash reserves and borrowed $500 million. And now it is asking the Government if it may borrow more than its statutory limit of $1025 million.

By June the AWC expects to have stocks of 2.5 million bales. This wool mountain has been financed from an interest-free "loan" levied at 8% upon growers' receipts and by borrowing. At current interest rates, interest-free loans are, for all practical purposes, gifts, and compulsory loans are taxes. Because the AWC expects to be out of cash by February, the Wool Council has written to the Minister for Primary Industry asking that the Wool Tax Act be amended to raise the current 10% maximum levy to 15%.

The whole policy is irresponsible and pointless.

By raising the price and keeping half the clip off the market the policy has allowed synthetics and wool from other countries to fill orders which would have been filled by lower priced Australian wool. When the AWC comes to sell its stock the increased volume then on offer will depress the price. At that time most of the lost markets will probably be recaptured, but the purpose of the whole costly, risky exercise escapes me. The reserve and buffer-stock policy, unless it crashes, produces a stable price---that is a price which consistently fails to convey appropriate messages to producers about the state of demand and to consumers about the state of supply. It contains the seeds of its own destruction.

Buffer-stock schemes always break down because those who manage them cannot be trusted not to ride too high a boom into too deep a recession. The International Tin Council (ITC), which comprised the goverments of producer and consumer nations, once had a successful record in managing the tin market. Then, in 1985, things went spectacularly wrong when its managers guessed wrongly. AWC has acquired big stocks before. Each time it has managed to sell them, and growers and politicians have tended to assume that it will always do so. Should there come a day, however, when it becomes apparent that a huge wool stock must be liquidated to meet the AWC's interest bills, we can expect the wool market to collapse until the stock is cleared. Incidentally, growers should not be fooled by AWC "profits" which are based on inflation. Growers should, instead, ask whether the AWC has done better with their money than they could have done themselves.

AWC borrowings do not enjoy a government guarantee but I can't see the government allowing the AWC to default, as the ITC defaulted. If, however, it is the government's intention to allow default, should the AWC run out of funds, then the government should, in all decency, say so now.

Alternatively, and I think more responsibly, the government might refuse to increase the wool tax, because to increase the tax would allow the AWC to increase the size of the bubble. The AWC might be rescued from its folly by devaluation which disguises a big fall in the reserve price as it affects foreigners. But, if the AWC cannot operate within its present powers, the government should take over the stock pile and the debts, and cancel the reserve price. The stock pile then should be quarantined from the market for 12 months and fed onto it at a steady predetermined rate.

Finally, the government should vow that such a situation will never be allowed to develop again. The wool industry is too important to the Australian economy for us to afford a debacle like that which reserve prices and ITC stocks inflicted on tin producers and the Malaysian economy.

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