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# Global demand prospects for wool

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## Abstract

Fine, medium and coarse wools are used for different consumer products, each of which is influenced by different key drivers. The key drivers of the fine wool market are economic growth in the major consumer countries, consumer preferences, fabric design and fashion trends. The outlook for fine wool is positive, as the demand for luxury apparel is expected to increase in key markets such as the US, Europe, Japan and Korea over the next 1–5 years. Prospects for medium wool will be influenced by price competition from other fibres, continuing consumer interest in natural fibres and new products such as easy-care garments. A modest recovery in economic conditions should support demand for medium fibre diameter wool in China and potential growth in emerging markets such as India and Eastern Europe. New product applications for interior textiles, particularly upholstery and rugs, could develop new consumer markets, and fibre and product attributes such as easy-care and soft lustre may increase consumer demand for medium wool. Key drivers for coarse wool are economic growth, price and attributes of competing fibres or materials, home ownership, prices and lifestyle trends. Increased home ownership in China and Eastern Europe is a positive driver for the coarse wool market, as is the emerging use of wool upholstery in mass-transport vehicles. After 14 years of turbulence, the Australian wool industry is well positioned to respond directly to global demand for consumer products.

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## Introduction

Australian wool has endured more than a decade of turbulent times. Industry issues such as floor prices, stockpiles and other market interventions have been well documented and debated. Wool is now in an era in which the price received by Australian producers reflects the true demand for wool. The wool industry should now focus on issues that influence the demand for wool and endeavour to tailor the supply of wool accordingly.

One barometer of demand is the price paid for wool; over the past 12 years, price trends for fine, medium and coarse wool have generally followed the same direction. There has been great price volatility and the price difference between these three categories of wool has changed a number of times. During the 1990s, these price differentials and trends were masked by wool held in the Australian stockpile, which was heavily biased toward medium type wools. With the stockpile depleted and the wool pipeline somewhat shorter, a continuation of the change in price between fine, medium and coarse wools was evident under the free market conditions of the past two years. Current price changes reflect the demand for wool, although the recent drought in Australia has affected the supply profile. It is thus appropriate to consider the structure of the current Australian wool industry and how it should respond to a demand-driven market.

The Australian Wool Clip has traditionally been marketed through open-cry auctions. Other wool producing countries such as South Africa and New Zealand use similar marketing mechanisms. This system has been refined by the introduction of computer systems, electronic data transfer, accessible wool samples and stores, detailed and standardised testing of wool and modelling of processing performance prior to sale. In addition, vast improvements have been made in market reporting; feedback on raw wool prices for hundreds of different wool types are captured daily and made available to Australian wool producers. The current auction system represents a most efficient

clearing house for buyers and processors of various wool types, who aggregate wool into processing batches for different end users. Despite its efficiency, the current auction system is primarily designed to service a supply-driven industry. Because wool is presented to the market in a uniform, tested and consistent manner for prompt delivery, prices are determined by the market in an open and competitive manner. Whether this system is appropriate for a demand-driven industry is open to question.

The wool pipeline is now shorter than in the past and is showing signs of responding to demand. Furthermore a new route to market, which is more oriented towards wool processing in Asia than in traditional regions such as Europe, has emerged. Given these developments, it should be possible to start linking demand to supply and thus create opportunities for wool to pass through the supply chain in a more efficient manner than in the past. More direct linkage of raw wool prices to those of consumer products would reduce price volatility. The benefits of linking demand to supply are illustrated by the following example of black wool socks.

Black wool socks are consumer products that have predictable sales volumes and a relatively predictable and stable retail price. In the case of Australia, socks are usually processed domestically or in China. Wool destined for the manufacture of socks is typically processed by scouring, combing, spinning, dyeing and knitting. The number of lines into which wool is currently separated in the shearing shed could be reduced because the presence of dark fibres would not be of concern to manufacturers of black socks. Fibre length variation between different parts of the fleece would also be of little concern as top and yarn tolerances for socks can accommodate large variations in length. The need for fibre testing would also be reduced and detailed information concerning length, strength, vegetable matter and colour would not be needed. The number of tests needed for the top-making process could also be reduced. More importantly, the speed and settings of combing machines could be adjusted to reduce combing costs and wool yield losses because wide tolerances in the yarn specifications for socks are possible. The reduction of small lines from growers and subsequent aggregation of wool clips into larger processing batches could be done at an early stage in the supply chain, which would reduce handling costs substantially.

This example shows that if one starts with the end in mind and follows the process through, opportunities to simplify and improve the process in a number of parts of the supply chain become evident. At the other extreme, ultra fine Merino wool produced by sheep in a specific geographic region of a known and consistent bloodline could be linked to premium tailors in London, Tokyo and New York. In this instance, the extra costs of breeding, classing, testing, small runs and tight product tolerances could be absorbed. Such a system would also give the tailor certainty of supply.

Ultimately, the matching of supply to demand would result in the development of forward physical contracts for wool prior to shearing between growers, processors and others involved with the supply chain. The opportunity currently exists to develop demand-driven products as an activity complimentary to the current auction system.

## **Fine wool**

With the exception of the recent drought-affected seasons, fine wool production increased during the 14-year decline in global wool production. Demand for fine wool increased from 1991 to 2005 in volume (115%) and value (122%). The key consumer markets for fine and super-fine wool are Japan, Italy and the US. These dominant markets are supported by other Western European countries (UK and France), China, Korea and Taiwan.

Australian fine wool is the world's fastest-growing luxury fibre. It is the dominant luxury fibre in lightweight knitwear and tailored formal wear. Of fine-wool production, 45% is used for the manufacture of men's wear (e.g., suits, jackets and trousers), 25% for women's wear (e.g., suits, skirts and trousers) and 30% for knitwear (e.g., wool/ cashmere blends, lambs' wool sweaters and underwear).

The key drivers of the fine-wool market are economic growth in the major consumer countries, consumer preferences, fabric design and fashion trends. The outlook for private consumption growth in key apparel markets is positive: an economic recovery is forecast for Western Europe; Japan is showing a sustained but moderate economic recovery; economic growth is expected to be solid over the next five years in the US and South Korea; economic growth is forecast for China. Consumer preferences indicate there is a trend towards comfort, fineness and softness, a growing demand for lightweight consumer products, awareness and desire for luxury and a preference for affordable prices.

In summary, there are prospects for fine wool as the demand for luxury apparel increases in key markets such as the US, Europe, Japan and Korea over the next 1–5 years. Product improvements will include appearance, crease resistance, easy-care properties, softness, lightweight fabric and natural comfort to cater for consumer demands for a premium luxury product.

## Medium wool

Medium wool production has continued to decrease in parallel with the global production decline. There has been decreasing demand for medium wool from 1991 to 2003 in volume (–62%) and value (–55%). Key consumer markets for medium wool are China, US, UK, Italy and Japan. These markets are supported by Germany, France, Spain and other parts of Western Europe, Taiwan, Korea, India, Turkey and by re-development in Russia and other parts of Eastern Europe. Consumer end use for medium wool includes men's wear (30%; e.g., suits, trousers and jackets), women's wear (32%; e.g., jackets, suits, trousers and coats), knitwear (35%; e.g., lambs' and worsted knits, wool socks, hand-knitting types) and interior textiles (3%; e.g., upholstery and rugs). Medium wool is used extensively for low-price garments and is often used in blends.

The key drivers for future prospects for medium wool are economic growth, prices of competing fibres, retail prices and fashion trends. Prices of competing fibres are a key issue, as prices of medium wool and synthetic fibres have increased sharply from 2002 to 2005:

- Raw material for acrylic doubled in price between 2003 and 2005.
- Raw material for polyester increased by 60% in price between 2003 and 2005.
- The cotton price recovered from 45 US cents per pound in 2004 to 55 US cents per pound in 2005.
- The price ratio of wool to Cotton is 4:1
- The price ratio of wool to synthetic fibre is 3:1

From 1991 to 2002, there was no increase in the retail price of consumer products in the medium wool category of key consumer markets. In essence, this was a deflationary environment for clothing. Prospects and opportunities for medium wool will be influenced by price competition from other fibres, continuing consumer interest in natural fibres and new products such as easy-care garments.

In summary, a modest recovery in economic conditions in the major wool-consuming countries is expected during the next 1–5 years. This should support demand for medium fibre diameter wool in China and potential growth in emerging markets such as India and Eastern Europe. The price sensitivity of these markets may be partly offset by the favourable price ratio between wool and synthetics. Product developments include new blends with cotton and newly developed high-price synthetic fibres. New product applications in interior textiles, particularly upholstery and rugs, could develop new consumer markets. Development of fibre and product attributes such as easy-care and soft lustre will also expand consumer demand for medium wool.

## Coarse wool

Coarse wool represents a small segment of the Australian wool clip and is often characterised as a by-product of sheep meat production. Demand for coarse wool decreased in volume (–51%) and value (–47%) from 1991 to 2005. Key consumer markets for coarse wool are China, US, UK, Germany, Turkey and Australia, supported by Italy and Western Europe. Developing markets include India, Pakistan, South Asia, Japan, Russia and other parts of Eastern Europe, North Africa and the Middle East. Coarse-wool consumer products include interior textiles (55%; e.g., carpets, rugs, bedding and upholstery), women's wear (10%; winter-weight coats and jackets), men's wear (5%; e.g., winter-weight jackets and coats) and knitwear (30%; e.g., hand-knitting and military knitwear).

Key drivers for the prospects of coarse wool are economic growth, price and attributes of competing fibres or materials, home ownership, prices and lifestyle trends. Home ownership and improvements represent opportunities and risks for the use of interior textiles, depending on expendable income and lifestyle changes. Increased home ownership in China and Eastern Europe is a very positive driver for this category, as is the emerging use of wool upholstery in mass transport vehicles. The trend towards sports and outdoor clothing also favours wool. Bedding remains a dominant application for coarse wools and this market should continue to expand as awareness of the benefits of natural fibres grows. Commercial applications for coarse wool such as upholstery in offices and aged-care facilities are expanding. Product attributes such as improved colour fastness of wool carpets, easy care of upholstery and bedding and comfort are being developed for coarser wools, which will enhance their attractiveness to consumers.

In summary, prospects for coarse wool depend on a modest recovery in the global economy in key wool-consuming countries. This will influence home ownership and markets for upholstery, bedding, carpets, sports and outdoor clothing.

## Conclusion

After 14 years of turbulence, the Australian wool industry is well positioned to respond directly to global demand for consumer products. Key drivers for Australian wool products have been identified and the outlook for many of these categories is extremely positive. These can be summarised as follows for 2005–2006:

- A balance between supply and demand for raw wool is forecast.
- The global economy is expected to remain relatively stable and growth is forecast to be broad-based in 2006.
- Fashion trends are positive for wool.
- Wool prices are competitive with those of synthetics.
- The competitiveness of wool against cotton is improving but still low.
- Global wool production is constant.
- There are indications of a cyclic recovery in 2006

The opportunity exists to bring about structural changes within the industry in response to this demand-driven environment. A number of Australian exporters and processors are embracing this opportunity to not only secure a viable global wool industry for Australia, but to expand the industry on a truly commercial and de-regulated basis.