

Measuring & Improving the International Competitiveness of Australian Book Producers

Interim Report Phase Three

15th April 2004



Australian Government

**Department of Industry
Tourism and Resources**

This project is funded by the Department of Industry, Tourism and Resources under the
Enhanced Printing Industry Competitiveness Scheme – Infrastructure and Industry Growth Fund

TABLE OF CONTENTS

1. INTRODUCTION	2
2. METHOD	2
2.1 Domestic Producers	2
2.2 International Producers	2
2.3 Accuracy and Currency of Data	3
3. CAPITAL STRUCTURES	4
4. OPERATING COSTS	4
5. STRATEGIES	5
5.1 Marketing and operations	5
5.2 Technology	5
5.3 Raw Material Costs	5
5.4 Related Issues	6
CONCLUSION	6

1. INTRODUCTION

This reports the completion of data gathering activities that formed Phase Three of the project to "Measure and Improve the International Competitiveness of Australian Book Producers", as detailed in Schedule 1 to the Deed between Commonwealth of Australia and Printing Industries Association of Australia for the provision of funding for dated 7th February 2004.

The report is aligned with

- The requirements numbered as items 3 in **Schedule 2, Funding Schedule, Performance Indicators and Reporting Requirements**, of the deed, and
- Attachment 3 (Schedule of Activities and Deliverables – Page 2 of 2) of the proposal at Schedule 1, Attachment 1.

It describes the methods by which accuracy, currency and impartiality were assured in the gathering of data concerning

- Capital structures
- Operating costs
- Strategies for:
 - Marketing and operations
 - Technology
 - Raw Material costs, and
 - Related Issues

2. METHOD

Our primary concerns were to ensure firstly that the sampling of producers was representative of both the domestic and international situation, and then that the data was current and accurate.

2.1 Domestic Producers

For domestic producers, the Printing Industries Association of Australia provided a list of 11 large and small book producers across the country¹. The sampling included companies in (each or all of) prepress, printing, and finishing. It included two specialist trade binders.

2.2 International Producers

For international producers we coordinated our sampling through the offices of Avimo International who also arranged visits to producers in Singapore, Hong Kong and China. Some of these companies also had operations elsewhere in Asia (specifically Malaysia and Thailand), and we were able to generalise the data to include them.

The sampling included companies in each or all of prepress, print and finishing. We surveyed a sampling of 10 organisations, representing a total of 2 plants in Singapore, 2 in Malaysia, 1 in Thailand, 7 in Hong Kong and 6 in China.

¹ Refer section 2.4 in the Interim Report – Phase Two, dated 5th March 2004

The table below summarises the extent and spread of the facilities that were covered in our sampling.

Production Facilities Represented in Sample

	PrePress	Print	Finish	Other	TOTAL
a) Australia	9	9	10		28
b) International					
Singapore	2	2	2		6
Malaysia		2	1		3
Thailand		1	1		2
Hong Kong	4	3	4	3	14
China	2	2	2		6
S/Total	8	10	10	3	31
Total Sample	17	19	20	3	59

2.3 Accuracy and Currency of Data

To ensure that the data was accurate and current, we visited each of the survey respondents and conducted our interviews at their production site. In all except 3 cases the interview was followed by a tour of the facilities. We used the touring opportunities to cross reference the accuracy of data gathered during the interview(s) that preceded them².

This was especially important in the foreign plants, where communicating our questions was sometimes hampered by language. Some of our concepts also took a while to explain – particularly those to do with on-costs and productivity rates.

As a further test for accuracy, especially of data regarding plant and people we took as many photographs as we could³. This was especially useful in recording correct manning levels – also for providing proof of some headcounts domestic producers would find hard to believe.

² For instance we counted the equipment, asked questions about shifts worked on individual items of equipment, etc. In all cases our researchers were able to reassure themselves that the correct data had been recorded.

³ This is not an accepted practice in the domestic market so we didn't ask. In Asia (Except for Singapore) our request was accepted each time we asked. (Two of our hosts insisted we take photos of particular pieces of equipment!)

3. CAPITAL STRUCTURES

In the domestic market it was relatively simple to collect data. We had developed a pro-forma balance sheet structure (refer to Section 2.1 in Interim Report – Phase Two) to allow simple, apples-to-apples comparisons and once we had satisfied respondents that their data would be well disguised and not traceable to any individual enterprise, the data was forthcoming.

The international market was somewhat different and required a different approach. Only one of the companies was publicly listed and we extracted their data from published current reports. For the others we used an oblique questioning technique⁴ that allowed us to accurately estimate most of the financial data we needed.

We also met with three specialist financial advisors to the Asian based industry. Two were based at a large international accounting firm and the other a retired partner of a second large international firm, who is still active as an advisor to investors in the printing industry in Hong Kong and China. They provided a cross check on the assumption we had made to fill in gaps in our data. They also verified some of the regulatory aspects we had uncovered in our fieldwork.

In both domestic and international segments, we found that only a few industry people understand – let alone use – the concept of weighted average cost of capital, which was the metric by which we had intended to measure the cost of capital employed. We reverted to the interest paid on finance loans because that seems to be universally used⁵.

The result is a verifiable summary of capital structures that will allow us to compare like to like between domestic and international producers, and a clear understanding of the concepts applied by industry investors in Asia.

4. OPERATING COSTS

Our model was designed to show a gross margin and net margin, and to detail costs accordingly.

Gathering this data proved somewhat difficult because there are various descriptions of gross margin across the domestic and international industries. Some include operating overhead while others exclude it. The same is true for administrative overhead. However, for purposes of this project, the salient point is the net margin, which seems to be a standard measure in all cases. So, where we encountered any lack of clarity or were not able to verify the data, we defaulted to a concentration on net margins.

Within this constraint, we were very interested to learn the actual direct labour costs in each location, and the on-costs that apply. The analysis will report details, but we can already see a huge discrepancy in both the nominal hourly rates paid to workers and the labour content in finished product sold.

⁴ For example: having ascertained what total sales were (information that most producers are happy to share), and how long debtors took to pay, it was a simple to estimate the value of accounts receivable.

⁵ In that regard, we uncovered empirical evidence that at least one Asian government subsidises the interest paid for loans to buy equipment. We will check this as part of our analysis.

One major surprise, which will influence the like-to-like comparisons, is the different treatments of depreciation. They range from a straight-line 15 year regime in some domestic companies to a 1 year total write down for companies registered in Hong Kong. Details, and the effect on margins will be covered in our analysis.

5. STRATEGIES

We found no difficulties in gathering data in this area, and made several observations that will help our analysis.

Researchers made two interesting general observations concerning the differences between domestic and international players in the industry.

- Domestic producers were less likely to articulate their strategic intentions in most areas, (although some were very clear). In every case, the international producers were very definite in their description of strategy, to the point of illustrating where it was evidently successful.
- Domestic producers tended to talk in terms of constraints to be overcome (competitive pricing, lack of consistent volume, and the cost of new technologies all rated high), while foreign producers tend to talk about growth and volume.

Our analysis will provide an opportunity to test if this observation is borne out in the data itself.

Our researchers made the following observations regarding various elements of strategy across domestic and foreign producers. These are recorded here as a matter of interest only – our analysis will determine if they constitute significant factors for comparison.

5.1 Marketing and operations

Responses range across a wide gamut of strategic intent, including a focus on rapid response, technological innovation and a commitment to customer service.

While it was not specified in our planning, fieldwork indicates that our analysis should, and therefore it will, include specific examination of the role that specialist brokers play in the foreign market, where they are a significant factor.

5.2 Technology

A general observation is that foreign producers have been slow to abandon film but are now converting to CtP, whereas domestic producers assume CtP is a necessity.

At the other end of the process, strategies for finishing reveal a deep difference between the domestic need to reduce the amount of direct labour, while foreign producers (at least those in China) recognise no such need, and many base their strategy at least in part on factors that demand high labour input.

5.3 Raw Material Costs

While domestic producers are generally locked into a merchant-based supply scenario, foreign producers tend to take a position on paper supply, in which they can leverage off their volume to achieve significant price concessions. (One printer we spoke to buys over USD100 million p.a. of paper).

We think – and the analysis will test – that the proximity to raw material producers is also a help to foreign producers. Every plant we visited had large

stocks of one brand of paper, produced at a new mill near Shanghai. We also found plates made in China, with a brand name that we don't see in Australia.

5.4 Related Issues

We expect that other aspects will emerge from our analysis of the quite comprehensive amount and range of data we captured during the month of fieldwork undertaken.

CONCLUSION

The sampling of producers was comprehensive in both the domestic and international sectors. We were able to gather representative data that provide a deep and broad base on which to build our analyses.

We were also able to verify the data through a series of cross checks and validations that included reference to independent specialists in the Asian sector. Our local knowledge qualified us for this task in the domestic sector.

The analysis of the data has begun and we will conclude it on schedule late in April.