

Submission from

Gilmour's Pty Ltd  
To the  
Productivity Commission

March 2003

Post 2005 Assistance Arrangements for the Textile Clothing and  
Footwear Industry.

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Regarding Post 2005 Assistance Arrangements  
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As a small, independent retailer Gilmour's Pty Ltd lacks the resources to produce a major economic tome for the consideration of the Productivity Commission.

The major players in the industry, the lobby groups, the importers, big retailers and government will no doubt tease out every last issue connected with protection of the clothing, textile and footwear industries.

All the directors of Gilmour's Pty Ltd and those who prepared and had input into this submission, however, have been and remain actually engaged day to day in the processes of buying and selling shoes. Preparation of this submission, in fact, had to be wedged into free time between serving customers, dealing with suppliers, massaging creditors and Witch Bank, discussing new niche products with local manufacturers and completing BAS and other forms for Government.

We have therefore not sought to suggest policy directions for recommendation by the Commission, but to present some issues which seem to us to be bleedingly obvious.

They are:

- Supply is a critical problem for shoe retailers such as Gilmour's.
- Most of the Australian shoemakers which still supply Gilmour's are small niche players.
- Some bigger Australian shoemakers are still strong enough to deny supply to small independent retailers like Gilmour's.
- Import duties don't mean much any more – they are not as important as currency changes or management issues.
- Some Australian shoemakers and retailers do not understand that high margins available on imports do not compensate for long delivery times and slow stock turns.
- Import duties are really just another tax on consumers and should be designated as such.
- Businesses that don't have protection are sometimes better businesses.

## **What is Gilmour's?**

Gilmour's Shoes, incorporated as Gilmour's Pty Ltd, is an old (established 1919) footwear retailer in Melbourne, specialising in the comfort, orthopaedic and "fittings" sectors of the shoe market. It has annual sales of around \$3.5 Million, selling approximately 35,000 pairs of shoes a year, and has a computerised database of more than 100,000 customers. Approximately, 85 per cent of its sales are to women. Most of the customers come from Melbourne, but Gilmour's Pty Ltd also has a clientele in other states and some overseas who purchase by mail order, responding to the firm's strengths in supplying shoes for "hard to fit" feet.

As a traditional "size and width" shoe retailer, Gilmour's Pty Ltd is sharply differentiated from the fashion sectors of the footwear industry.

This specialisation has been hard to maintain in the face of the shoe trade's global obsession with fast fashion and styling, and its entrenched habit of placing these factors ahead of the traditional values of fitting and comfort. Growth has also been restricted in footwear generally because of the increasing competition for household disposable income from other product and service sectors.

Despite these difficulties, Gilmour's has survived, building its business within the niches of its choice (comfort, orthopaedic and 'hard to fit'), and it has been profitable. The return on funds employed has been modest, rarely over seven per cent net per year – a return that emphasises the firm's dependence on private family ownership and the family's commitment to the trade.

## **Our Biggest Problem**

Although it has met and overcome other problems and is profitable, Gilmour's Pty Ltd faces one serious and almost intractable problem - that of supply, the simple process of obtaining shoes which suit its specialised niche markets.

The number of footwear manufacturers in Australia has declined dramatically in recent years, cutting off major sources of supply to Gilmour's. Even internationally there has been a precipitous drop in the number of manufacturers who produce shoes in the specialised fittings, including sizes and widths, required by Gilmour's. At the same time, the gradual decline of the Australian dollar against European currencies and the US dollar has restricted access to some suppliers in these markets who make the specialised fittings available. The poor purchasing power of the Australian dollar in the last 15 years has priced many foreign products out of reach of Australian consumers.

As a result, Gilmour's has had to look further and further afield for sources of footwear. Its major sources of supply have been a New Zealand company (Kumfs), several US companies (who make the sizes and widths ranges required) and some European firms. Gilmour's has been forced to seek these supplies offshore NOT in the interests of price, but merely for the specialised fittings.

In the last five years, the US manufacturers have been shifting their production from their domestic sites to factories in Asia, mainly in China, the Europeans have shifted to eastern Europe, to lower cost countries in the EU or to north Africa; and even the New Zealand supplier is investigating some shift of production to China. Every time a manufacturer shifts production to a low cost economy it seems that some of the sizes and widths we need drop off the order forms.

During 2002, Gilmour's sales were supplied overwhelmingly by imports. Less than three per cent of sales involved domestically produced merchandise. Those locally produced shoes which were sold by Gilmour's in calendar 2002 were from Australian factories which were supplying small niches in the market. None of the domestic manufacturers provided large volumes of footwear to Gilmour's.

The major local and foreign suppliers are shown in the accompanying table.

### Major Brands Sold by Gilmour's Pty Ltd 2002

Brand	Manufactured	Pairs	Retail Value
<b>Imported</b>			
KUMFS	NewZealand	5570	\$863,333
SOFT SPOTS	China	2765	\$473,027
ROCKPORT	China - mainly	1455	\$290,510
SALAMANDER	Germany and Hungary	1578	\$271,882
ARA	Germany	1436	\$245,527
HUSH PUPPIES	China	2303	\$228,767
EASYSPIRIT	China	1204	\$143,080
FLY FLOT	Italy	1933	\$125,807
RIEKER	Germany & Tunisia	539	\$87,401
CLARKS	England	843	\$86,585
CORTEBEL	Portugal	1396	\$79,771
VINNELL	Fiji	308	\$58,932
<b>Domestic</b>			
APTITUDES	Melbourne, Australia	236	\$40,894
VIENNA	Melbourne, Australia	133	\$23,202
PAGLIA	Melbourne, Australia	95	\$9,196
GADEAN	Malaga, WA	31	\$6,156
ENOCH TAYLOR	Windsor, NSW	51	\$4,457

### Domestic Suppliers

Each of the remaining Australian domestic sources of footwear for Gilmour's is a niche operator. In the above list, Aptitudes and Vienna supply footwear in very wide fittings, Paglia supplies only two products - traditional women's leather slippers now virtually unknown in other markets - Gadean provides orthopaedic footwear almost on a bespoke basis, and Enoch Taylor supplies work boots made to meet local safety standards.

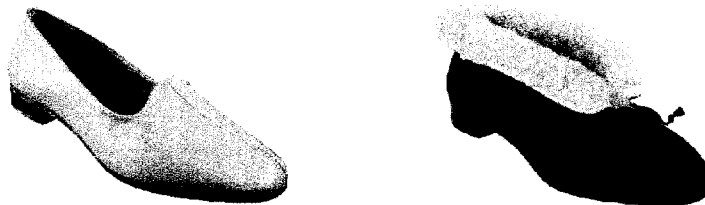
This suggests that any form of protection for these local manufacturers is irrelevant. We will buy the shoes because we need them. Further, we are working with the Aptitudes manufacturer to develop new niche products.

Gilmour's Pty Ltd was involved in the development of one of the products produced by Aptitudes - an extremely wide sandal, as shown in the accompanying picture.



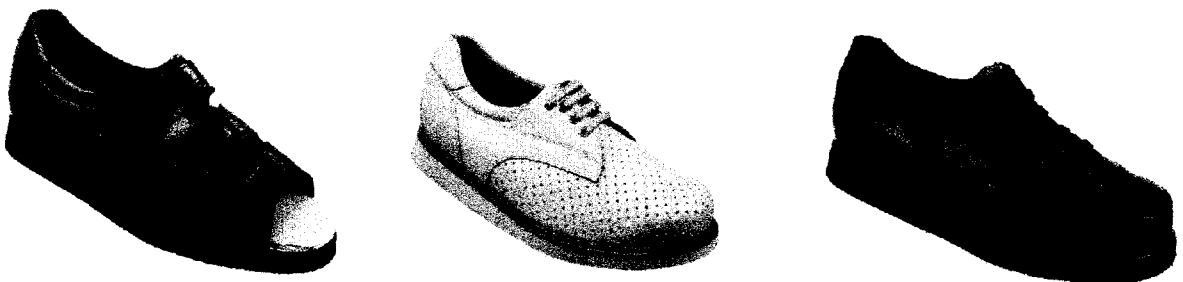
On our measure, this shoe is a EEEEEEE (that is seven E's) – certainly wider than any other women's dress sandal available in the Australian market – or almost any market. It retails for \$215 – nearly double the price of comparable imported products in ordinary widths. There has been some customer resistance to paying the high price, but it is starting to sell steadily in the small niche market at which it is targeted. We have recommended to the manufacturer that he explore export opportunities for this unique product.

From Paglia shoes we purchase two styles of women's slippers as pictured. They sell at retail level for \$95 and \$115, and continue to meet the requirements of a



small local clientele who purchase them not because of price but because of quality. Similar products are imported from time to time at substantially lower cost, but never match either the quality or the finish of the Australian product.

The Gadean products include orthopaedic shoes such as these.



Gadean products are available in very small orders, even in single pairs, and the Gadean factory will also make up odd pairs to special order. Its prices, up to \$250 a pair, reflect this extraordinary service and are largely unaffected by imports and probably never will be. There is no offshore factory with which we have dealt which will provide such service, making Gadean almost immune to competition. But its volume is very small.

In the case of Enoch Taylor, price is a more critical factor, because its main products are work boots. To some extent it enjoys protection because the factory has met the standards set for safety footwear by the Australian Standards Association, something that few overseas manufacturers appear to have done. It has also specialised in wider than average fittings, emphasising its interest in supplying a niche. In more than 40 years of selling Enoch Taylor products – marketed under the label T-Boots – we have never encountered meaningful imported competitive products. Many importers have brought work boots into Australia, but none has induced us or our customers to abandon our affection for the T-Boots.

Further, one of the Enoch Taylor products - a work/hiking boot which we retail for only \$129 and which is pictured below has met enthusiastic support of buyers in overseas markets who have their choice of the world's best work/hiking boots .



On current trends, Australian factories are unlikely to become significant suppliers to Gilmour's Shoes in the foreseeable future.

### **Some Australian Companies Will Not Supply**

Gilmour's has not obtained supply from three significant Australian manufacturers which are reputedly innovative and successful. The Ritchie organisation (Sandler/Jane Debster) of NSW has refused to supply us, claiming they lack sufficient capacity. Blundstone Pty Ltd of Tasmania has refused to supply because it is already supplying footwear to shops geographically close to Gilmour's. Walk On Shoes has offered supply, but only through a retail competitor of Gilmour's – a condition which Gilmour's finds unacceptable.

There are other manufacturers in Australia supplying fashion sectors of the market, but even if these firms were willing to supply Gilmour's, it is unlikely that there would be a major shift of emphasis by Gilmour's to domestic sources. None of the

three firms above and no other Australian manufacturer makes footwear in the size and width ranges we require.

### The Size Width Handicap

Permutations of sizes and widths in the shoes required by Gilmour's mean that very large stocks are involved, imposing a heavy cost burden on us and our suppliers.

A typical women's multiple fitting shoe might involve a total of more than 40 different fittings. The accompanying table shows a typical range of sizes and widths in a shoe made in four widths and 15 different sizes. Some suppliers in the US provide shoes in six widths and 20 sizes (making 120 possible permutations).

Typical Size/Width Matrix of Women's Basic Shoe  
Shoes stocked shown as X

	5	5.5	6	6.5	7	7.5	8	8.5	9	9.5	10	10.5	11	11.5	12
Narrow					X	X	X	X	X	X	X		X		X
Medium	X	X	X	X	X	X	X	X	X	X	X		X		X
Wide			X	X	X	X	X	X	X	X	X		X		X
Extra Wide			X	X	X	X	X	X	X	X	X				

Only large markets, such as the US, providing great volumes, can sustain such diversity. No Australian manufacturer has made such a range at any time in the last 10 years. The New Zealand manufacturer Kumfs makes wide ranges of sizes and widths, but does so thanks to a wide market acceptance in New Zealand and Australia and the United States.

Modern technology exacerbates the cost issues of such a wide range of shoes. The vast majority of comfort shoes have soles formed in very expensive moulds - the cost of which can only be amortised over very large production runs.

### What Impact is the Current Import Duty?

Analysis of our company's trading figures also suggests that the level of import duty at 15 per cent is only a minor element of the costs involved in our buying of footwear.

The relevant data of a recent fairly typical airfreight shipment of footwear by Gilmour's Pty Ltd are shown in the following table. This shipment involved the importing of 296 pairs of women's shoes from an American company. The shoes were made in China shipped in bulk to the US and sent to us from the US warehouse.

The main style involved in this shipment was that pictured here. It is a tubular moccasin construction with a leather upper and a polyurethane sole and is available in widths of N, M, W, WW and in sizes from 5 (US) to 13 (US). There is no factory in Australia which makes comparable shoes, and none making shoes in so many widths and sizes. The complexity of the size/width combinations imposes a heavy holding cost burden on the wholesaler and retailers and forces a relatively high retail mark-up. The cost pressures are exacerbated because the technology of the shoes - moulded polyurethane soles.

Gilmour's average recovered retail price for this shoe over the last 12 months has been \$160 including GST.



The cost structure of the shipment was as follows:

Recent Shipment of 296 Pairs			
	296 Pairs	Per Pair	%
	\$A	\$A	
Fob cost US	\$13,891.37	\$ 46.93	64%
International Freight	\$ 2,394.64	\$ 8.09	11%
Duty and Customs Charges	\$ 2,177.97	\$ 7.36	10%
Buying agent's Charges	\$ 1,423.02	\$ 4.81	7%
Sub Total	\$19,887.00	\$ 67.19	91%
GST	\$ 1,988.70	\$ 6.72	9%
<b>Total Into Store Cost</b>	<b>\$21,875.70</b>	<b>\$ 73.90</b>	<b>100%</b>

These figures show that import duty and customs charges comprise 10 per cent of our landed cost (when including GST in the cost). Obviously, import duty and customs charges are significant, but if their purpose is to protect the Australian industry they are no longer a sufficient component of costs to make a substantial difference. The fact that these shoes bear import duty into America (albeit at a very low rate) and again into Australia also suggests that price – and therefore duty rates – are not critical factors to their reception in the Australian market.

A few percentage points change in the parities of the Australian dollar and the US dollar would have as much impact. As pointed out earlier, the long term decline of the Australian dollar against European currencies and the US dollar has also had a major impact on our access to products.

In our view, the decline of the Australian dollar's value over the last 15 years has been a far more important element of protection for Australian manufacturers than the rate of duty.

In the period from the 1970's to the present, the decline of the Australian dollar has increased the cost of some German footwear by a factor of three. The concurrent reduction in import duty from 45 per cent of the fob price to 15 per cent is almost irrelevant by comparison.



## **Retail Margins and GMROI**

From its long history of trading in shoes, Gilmour's Pty Ltd has had the opportunity to gain some historic perspective about the footwear industry. At the risk of revealing trade secrets, we would invite the Commission's consideration of retail margins.

In its first three decades of operation, Gilmour's operated on mark-ups of 25 per cent on men's shoes and 33 per cent on women's, making for gross profit margins of 20 per cent and 25 per cent respectively. In the next two decades it gradually moved to 45 per cent (31% gp) and 50 per cent (33% gp) respectively, and since the 1970's mark-ups have risen consistently to 100 per cent (50% gp) for men's shoes and more, sometimes 120 per cent (55% gp), for women's. We are aware of many retailers, particularly in high fashion footwear, who work on at least 200% markup (for a gp of 66%).

There are few signs of dramatic improvements in profitability to match this growth in mark-ups, suggesting that costs have kept pace.

A critical cost, of course, is that of capital, and we would suggest that an understanding of the costs of capital in the distribution of footwear is another more important factor relating to protection of the Australian manufacturing sector

A key measure of profitability and performance in retailing is the level of gross profit in dollars earned each year measured against the investment in inventory. This key measure is being adopted increasingly by retailers under the awkward acronym GMROI - meaning the Gross Margin Return On Investment.

At Gilmour's and most footwear retailers, GMROI is critical. It tells us how much gross profit in dollars is generated by each dollar of investment in inventory.

GMROI is a function of margin (derived from mark-up) and the number of times stock is turned over in the period of review. It is calculated as the product of stock turn and mark-up, and expressed as a simple number rather than percentage. For instance a product which turns twice a year (a stock turn of 2.0) and provides a mark-up of 100% (i.e. a gross profit of 50% of sales) produces a GMROI of 2 ( $2 \times 100\%$ ).

Gilmour's Pty Ltd along with most retailers has accepted that stock turn is much more critical to GMROI than margin. If an item provides only a low stock turn, a much greater margin is required to generate the same dollar value of gross profit on the invested capital.

For practical purposes, a GMROI table like that following which shows the relationship of stock turn and margin to GMROI is used by Gilmour's to guide its buying decisions.



The GMROI figures indicate to Gilmour's that a local factory can afford to charge a higher price than an importer IF it can compensate by providing a rapid turn around and quick re-stocking. We believe that this point is becoming more widely appreciated by retailers. It is of interest to us that few Australian manufacturers ever have understood this point, and to the best of our knowledge NO Australian manufacturer ever has sought to teach retailers the importance of the GMROI numbers.

We look forward to consumers recognising the corollary – that shoes produced locally might be selling at more competitive prices.

Gilmour's Pty Ltd has embraced the GMROI concept as a measure of stock performance as result of attendance by key staff of many training seminars conducted by shoe trade associations in the United States.

If the GMROI measure were more widely appreciated and used, there may be more work for local factories and less pressure for absurdly high retail margins.

### **Who are we protecting?**

The decline of local manufacturing to niche player status in the shoe trade, the irrelevance of import duties, the broader impact of other factors on the industry has forced Gilmour's Pty Ltd and we believe many other retailers to question why import duties remain in force.

Surely the only reason is that they represent a source of revenue for the Federal Government and are the cause of much economic activity by businesses such as customs agents, public servants and a reason for the existence of organisations like the Productivity Commission.

They are just a tax on consumers. If the above import cost data are replicated in all imports, it would seem that consumers are in effect paying 10 per cent more for shoes than they need - the 10 per cent at retail reflecting the impact of a 15 per cent import duty on the factory cost.

The nonsense of the current protection regime and the debate about the ongoing role of import duties is that we still fail to recognise import duties as an outdated but subtle means of extracting money from the pockets of consumers.

We invite the Commission to consider whether a 10 per cent increase in retail prices of shoes imposed on 20 million consumers is justified in the effort to protect a handful of local factories with perhaps three thousand employees.

The duty does not even protect the factories, but makes them dependent and worse makes them think they are dependent.

We would also highlight the manner in which the 15 per cent import duty has a multiplier effect on retail prices. The Australian Government's practice of calculating GST on imports inclusive of import duty means that GST is charged on the duty as well as the base price and freight and handling. At the time the GST was introduced, consumers were led to believe that the tax would not be added to other taxes and duties.

### **An Alternative Case**

Because it is an old business, well capitalised and conservative, Gilmour's Pty Ltd has from time to time used its resources to invest in other businesses or assist other businesses to become established.

One such venture has been an investment in a hi tech manufacturing business which makes computerised labelling equipment in Melbourne. The business is Tronics Pty Ltd of Northgate Drive Thomastown. Gilmour's Pty Ltd has invested about \$0.5Million in cash in Tronics and much more in guarantees and directors' time and effort and has approximately one sixth of the equity in that company. Gilmour's Pty Ltd Chairman John Gilmour is also Chairman of Tronics. Tronics is not protected from imports and it does not want such protection because it recognises that by exposing itself to the global labelling machine market it has learned to compete in a global environment – and this has empowered it to export its products all over the world.

At the very time that Gilmour's Pty Ltd was working on this submission and listening to some local shoe manufacturers bellyache about the need for more import duties and protection, Tronics was completing formalities for a sale of \$1.2M of its labelling machines to one client in the United States. That order will bring Tronics' exports in the last 10 years to more than \$30 Million – all achieved because the company was strong enough and independent enough to compete in a global market and was not sheltered in an unreal and limited world by high import duties. Instead of whingeing about competition, it got out there and beat it.

Gilmour's Pty Ltd has also learned that lesson. In the 1960's it was almost dead. It had one shop in a poor location and was unable to compete with a nearby regional shopping centre or discount chains. It did not fly to government seeking help or subsidies, but decided to build on its strengths – its fitting skills, its knowledge of shoes, and a determination to survive and prosper.

It now employs 35 people in three locations and is facing the future with some confidence. If the Productivity Commission or some other Government Department came offering subsidies and protection for Gilmour's now, we would reject it on the grounds that we don't want crutches. We can walk!

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