

27 November 2013

Review of the Australian Automotive Manufacturing Industry  
Productivity Commission  
LB2 Collins Street East  
MELBOURNE VIC 8003

Dear Sir/Madam,

We write to you in relation to the Issues Paper released for the Review of the Australian Automotive Manufacturing Industry.

**Executive Summary:**

The auto-manufacturing sector has long made a significant contribution to the South Australian economy and continues to underpin the high tech manufacturing industry of the State at large. While the industry supports thousands of jobs both directly and indirectly, it also provides a level of knowledge and knowhow which other manufacturers use to leverage from.

The South Australian economy is currently experiencing a very difficult period and contracted slightly over the past twelve months.<sup>1</sup> While the mining boom is yet to eventuate, construction is flat and manufacturers are struggling to compete with a stubbornly high dollar and high costs of production, in particular high business taxes. Fortunately, the State's grain growers are delivering what is expected to be a near record crop on the back of an excellent season across much of the grain belt.

Given Business SA's broad membership base spanning across Industry and Commerce, we have never advocated for permanent support of one industry sector over another. What we do recognise though, as do our members not directly reliant on the future of auto-manufacturing, is the significant economic contribution that auto-manufacturing makes and the time required for South Australia to transition to an environment where the sector is not directly reliant on Government subsidies.

South Australia cannot afford to lose Holden in the current economic climate so the question for the PC will be how to employ subsidies to support auto-manufacturing in the short to medium term while encouraging either structural adjustment or facilitating for altogether exit in the longer term. Business SA does not want to see Adelaide lose Holden but the issues of auto-manufacturing need to be carefully considered in light of the myriad of cost and compliance issues facing the economy at large. In a broader context we need to be able to attract manufacturers to Australia, and not just be concerned about protecting the existing ones.

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<sup>1</sup> State Final Demand – Australian National Accounts, June Quarter 2013 ABS

## **Background:**

The current legislation supporting the auto-manufacturing industry, the *Automotive Transformation Scheme Act 2009*, was introduced with the object to:

- (a) encourage competitive investment and innovation in the Australian automotive industry; and
- (b) to place the industry on an economically sustainable footing.

The Automotive Transformation Scheme (ATS) began on 1 January 2011 and runs through to 31 December 2020, providing over \$3.35 billion of assistance to the automotive industry participants for production of motor vehicles, investment in research and development and investment in plant and equipment. The ATS is structured as follows:

- capped assistance of \$1.5 billion from 2011 to 2015 (Stage 1)
- capped assistance of \$1 billion from 2016 to 2020 (Stage 2)
- uncapped assistance of approximately \$847 million.

Noting for capped assistance, the limit is \$300 million per year which progressively declines from 2018 to just \$50 million in 2020.

Given Ford's pending exit from local manufacturing in 2016, there will be one less auto-manufacturer covered by the current ATS funding.

Australia also subjects imported cars to a 5% tariff to assist domestic producers to compete locally.

To give historical context to the current debate on the level of assistance for Australia's auto-manufacturing sector, Federal Government's of both persuasions have long maintained policies which result in the progressive reduction of both direct and in-direct (tariff) subsidies to the auto-manufacturing sector. As such, this debate should not be shaped by political differences; but rather the question of the best public policy to ensure Australia has a sustainable auto-manufacturing sector in the long term.

## **The South Australian context**

There can be no understating the significant contribution the auto-manufacturing sector makes to South Australia's economy, directly supporting nearly 4,500 jobs, mostly in car and component manufacturing, while indirectly supporting another 5,000 jobs across a range of sectors including other manufacturing, wholesale and retail trade, property, business services and transport.

The auto-manufacturing sector generates approximately \$900 million for South Australia's economy, of which approximately \$575 million is in the form of employee remuneration.<sup>2</sup>

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<sup>2</sup> The Contribution of GMH Elizabeth Operations to the South Australian economy and the Potential Impacts of Closure, University of Adelaide November 2013

Given South Australia's economy is worth approximately \$92 billion, Holden's contribution represents about 1% of our economy. To give this some context, over the past year which has been extremely tough for business in South Australia, our economy contracted by approximately \$145 million<sup>3</sup> so the immediate impact of losing Holden would be akin to several years of similar economic malaise.

While there are many obvious benefits of maintaining local auto-manufacturing, the PC also needs to be cognisant of the more subtle advantages for local companies who, for example, are able to reach agreement with local auto-manufacturers to make provisions in the manufacturing process to allow their post production accessories to be fitted.

The PC also needs to be aware of the role the local auto-manufacturing sector plays as a training ground for skilled engineers who are then sought after by high tech manufacturing companies. Given South Australia's high tech manufacturing sector is still developing, any moves by Government which may jeopardise the supply of skilled labour need to be viewed in the context of how such skills will be replaced.

It's an obvious assumption that South Australia could ill afford to lose Holden in the current economic climate, but the real question is how do we ensure our economy, and in particular our manufacturing economy can position itself for long term sustainable growth. The PC should not consider auto-manufacturing in isolation of the myriad of pressures facing all manufacturing companies in South Australia, particularly with respect to business taxes, costs of compliance and WorkCover. While there is no doubt that Australian manufacturing must be world competitive, this can only be achieved if we have a world competitive regulatory framework and flexible labour market. The consistent thread of feedback from Business SA's car industry members is that while financial support for Holden is needed, the more critical issue is the uncompetitive regulatory and compliance burden that all manufacturers face when competing in world markets. We cannot continue to compete on world markets if we are hamstrung by over-regulation and un-competitive business taxes, for this cannot be overcome by Government subsidies alone.

Business SA member feedback also suggests a noticeable labour cost differential between Holden and other manufacturers, particularly component suppliers. While Business SA is not suggesting that our auto-manufacturing sector compete with developing countries on wages, what the PC needs to ensure in determining future subsidies is that auto-manufacturing labour costs are benchmarked against the manufacturing sector at large. We support a fair day's pay for a fair day's work, but if auto-manufacturing continues to receive subsidies, we expect this to be on the basis that all costs, including any employee and management remuneration, are in line with the industry at large.

### **The Question of tying Auto-motive Manufacturing Assistance to Exports**

While Business SA acknowledges that any future assistance to the auto-manufacturing sector should be based on mutual obligation, we question the rationale behind specific export targets. Considering Holden in Adelaide as an example, if the Federal Government were to specify an export target, then how does that fit with the Cruze being developed on a global platform? The Federal Government would essentially be asking Holden to scale back production overseas to give Australian made cars market share.

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<sup>3</sup> State Final Demand – Australian National Accounts, June Quarter 2013 ABS

Business SA is not arguing against the good intent from the Federal Government, rather the impracticality of its implementation. It would obviously make more sense for models only manufactured in Australia, but unless the Australian auto-manufacturing is to develop a genuine niche in the world market, say for affordable performance vehicles, it is going to be extremely difficult to significantly expand exports. Further, Auto markets worldwide are extremely competitive at present, particularly in North America where interest free loans of up to eight years are common place.

Australian made cars are also subject to varying degrees of overseas import tariffs; 2.5% in the US, 10% in Europe, 25% in China, 40% in Indonesia and 60% in India just to name a few. Given the fierce resistance to dropping tariff barriers amongst developing countries, it is not realistic to expect Australian manufacturers can easily expand their sales into such markets without current FTA negotiations providing breaking ground in this respect. And further, non-tariff market barriers are still posing major limits on Australian exports even where Australia has signed FTAs, namely the case of Thailand where, since the Australia/Thailand FTA came into effect, domestic excise duties on engines more likely to be imported have risen substantially.

Car component suppliers are also subject to significant tariff barriers internationally and the PC's focus should give equal weight to their plight, particularly given they employ more people directly than the actual car manufacturers.

### **The Question of Component Supplier Diversification**

Ideally, if subsidies to auto manufacturers were to decline, component suppliers should be encouraged to diversify. And there have been some examples of South Australian based companies successfully diversifying away from local auto manufacturers, into either world supply chains or other sectors, for example caravan components.

The reality though, for many component suppliers in Adelaide geared specifically for Holden production, is that while diversification is optimal, most in the industry have already pursued this path with great angst given the options to diversify are so limited, particularly with Australia's high cost base and international tariff barriers limiting exports. This is not an argument for ongoing subsidies, rather the reality which the PC will need to contend with should it recommend a path forward for component suppliers if subsidies for Australia's two remaining auto-manufacturers post 2016 are ultimately abolished.

### **The Question of Ongoing Subsidies**

One of the biggest hurdles to Australia's long term success in auto-manufacturing is economies of scale. It has been widely documented that Australia's current auto-manufacturing industry is much smaller than required to achieve world competitive economies of scale. For this reason, Business SA is sceptical about any comparisons to international subsidies on a per capita basis which may not reflect the actual benefits of scale achieved by such countries as the US and Germany.



What the PC should be considering is what separates local manufacturers from their international competitors. If local auto-manufacturers are producing a quality product which Australians want to buy, are international manufacturers purely price competitive based on their own domestic subsidies?

### **An Integrated Federal/State Contingency Plan for the Car Industry**

The PC should be investigating how the Federal and State Governments can work together to create an integrated long term plan for the car industry. Such a plan would detail all possible future scenarios for auto-manufacturing, including both an increase and decrease in auto-manufacturing, and what options there are for sectors such as the component industry to adjust. Or, for example, is there still a likely role for engineering services should auto-manufacturing move offshore as is likely to be the case for Ford in Melbourne? This is not to say that Governments should be willing the demise of the car industry, but there should be a plan which has options ready to explore should, for example, one of the auto-manufacturers exit the industry for reasons other than Government subsidies which was the case with Mitsubishi in Adelaide.

### **Who We Are**

As South Australia's peak Chamber of Commerce and Industry, Business SA is South Australia's leading business membership organisation. We represent thousands of businesses through direct membership and affiliated industry associations. These businesses come from all industry sectors, ranging in size from micro-business to multi-national companies. Business SA advocates on behalf of business to propose legislative, regulatory and policy reforms and programs for sustainable economic growth in South Australia.

Should you require any further information or have any questions, please contact Rick Cairney, Director of Policy, Business SA

Yours sincerely

**Nigel McBride**  
**Chief Executive Officer**