Productivity Commission enquiry on Australia's Export Credit Arrangements

Quickstep Submission

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Not commercially sensitive

Quickstep is an SME that exports most if not all of its production. It specialises in carbon fibre composite manufacturing for Aerospace and Automotive, one of the many globalised and fast growing in the world.

Australia being a resource dominated economy in a country where the enormous majority of jobs are in the manufacturing and service industry creates a market imbalance that have wrecked a number of oil based third world economies and that can only be addressed by government policies that can insulate our industry from the vagaries of the resource markets. The lack of such policies will lead to a gradual disappearance of whole sectors of the economy that will lead to Australia being unprepared for when the resource boom starts to dwindle and will leave high levels of unemployment now and thereafter. The EFIC is one of the instruments that have been very successful to improve the success rate of the Australian industry on the export market. It has done so while being profitable. The Commission should therefore seek to increase its range of services rather than curb some of its products.

We believe that some of the initial draft conclusions of the enquiry would have a very unfair impact on Australian SMEs. SMEs are the core of innovation in Australia as well as worldwide. It is where most ground breaking technologies are being invented and developed. The domestic Australian market is very small and in our globalised economy, it is essential for SMEs to be able to export to be successful. The Australian industry is already facing extremely difficult conditions linked to the strength of the Australian Dollar (AUD) that makes it extremely difficult to compete on international markets. Australian companies are also at a disadvantage as they are not part of a large free trade, single currency block like the US or the Euro zone. Its currency is not only high; it is also very volatile with more than 10% variation of the AUD against the USD in the last 6 months. This makes it difficult for industry to invest and expect any predictable return. This is valid not only for manufacturing but also for R&D investment. These companies are creating a large number of new jobs and their existence is put at risk due to the link of the AUD to the resource industry that represents a small number of jobs in Australia.

SMEs also have a problem of financing that larger companies do not have. New and small companies with large potential do not have access to bank financing as they cannot demonstrate sufficient financial strength. If they have this bank access, a big contract that is likely to come from overseas that can get them to next growth level would be too big compared to their financial strength and would not be supported by banks.

EFIC is presently having a substantial positive effect on such constraints.

It can provide working capital guarantees that will allow an SME to take a large contract overseas and fund its financing requirements that banks would not provide. The smaller the company the more useful this funding becomes as the company does not have access to banking or not to the level required. Limiting access to EFIC for companies that have not exported and have less than AUD25m turnover would prevent such companies from exporting at all. Exporting means the company would have spent a substantial amount to prospect overseas and is only likely to consider contracts that are substantial and therefore beyond the funding capacity of their banks considering their size. The ultimate effect would be to limit the most innovative companies to the very small market of Australia and possibly make them unviable if their market is global. Instead of supporting industry, this measure will contribute to the faster disappearance of high growth globally competitive, but financially small companies.

This particular issue is not shared by other countries that all have very active Export Financing agencies that do not have such limitations. The commission should investigate what other OECD or non OECD countries are proposing to support their exporting industries and make sure the Australian industry is not at a disadvantage against their competitors in the rest of the world.

The concept of offering EFIC support only 3 times seems to be in contradiction with the minimum size of AUD25m. It again would constrain the growth of any company that would be subject to this arbitrary number and seems unfair if one company accesses EFIC for 3 minor contracts when another one can access it for 3 major contracts.

In terms of support for the foreign exchange, the EFIC products are extremely limited. At present, SMEs that want to protect themselves against AUD fluctuation have to take foreign exchange hedges and would have to deposit 25% of the value of these hedges in cash in the bank. If the company has landed a long term contract denominated in foreign currency, like most of them are on the export market, they simply cannot get coverage from the commercial banking system. They therefore have to take the risk of currency fluctuation which can bring them down if the AUD appreciates substantially as it has done in the past several years.

In specific Defence contracts, the government has gone away from buying Australian products in AUD to importing their products off the shelf from large global Original Equipment Manufacturers (OEM) and to introduce Australian companies in these OEMs' supply chains. This means that it will favour small companies with innovative products rather than local subsidiaries of large global companies that manages project rather supply products. It also gives access to more competitive large quantities of the global supply chains rather than the smaller uncompetitive quantities of what Australian Defence buys for its own use. The cornerstone of the government in industry policy for Defence gets SMEs to sell their products to global OEMs, many of which are US companies that not only buy in USD but also provide long term agreements that do not specify firm quantities as these are decided on a yearly basis by the US Congress. It means that this industrial policy transfers the risk of currency from the government to industry, but specifically SMEs and that these companies have long term agreements in USD that cannot be hedged beyond one year as there is no certainty of supply which is conditioned by US congress yearly decision. This makes it extremely difficult to compete without taking large risks.

A product that EFIC should propose is to cover SMEs for the exchange risk they are taking from the date of offer to the date of planned delivery based on the forward rate of exchange that is available on the market without having to deposit 25% of the value with a bank and that would cover say 75% of the deliveries that are forecast but not guaranteed by a US supplier submitted to the annual deliveries from the US government or more generally by their success on the market. This will provide the certainty for companies to seek such contracts and invest in that sector. Similar products are offered by a number of Export Finance Agencies overseas and it would just allow the Australian industry to compete on a level playing field.

I hope this submission will help the commission to understand some of the issues the industry and especially SMEs are facing on a day to day basis and what would make sense for EFIC to propose to get a vibrant competitive exporting industry rather than facing oblivion caused by the interference of a temporary boom in the resource industry.

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