

## Government Support For Australian Defence Industry Exports

### Identification of barriers and impediments to the growth of Australia's defence exports

In the 1970's and early 80's Australian defence industry was largely a collection of government owned and operated facilities, with a focus on meeting the needs of the Australian armed services. The commercially owned entities in the defence market place were primarily 'shopfronts' for overseas companies to supply their products into Australia. The result is Australia has never really had a substantive defence export program and this has been recognised in successive defence industry policy statements.

*"The ADF needs ready access to repair and maintenance services that, for practical reasons, can only be delivered by in-country providers. The ADF also needs in-country industry to adapt, modify and, where necessary, manufacture equipment that is suited to Australia's unique operating environment and military doctrine."*<sup>1</sup>

The DCP reinforces this position; in outlining opportunities for Australian industry the DCP offers the following types of advice:

#### Acquisition

- AIR 5432. Australian industry involvement is likely to include complex integration of new systems procured from overseas, with a range of existing sensor and data systems, along with associated test and evaluation.<sup>2</sup>
- AIR 5440. There is limited scope for Australian industry involvement in the Block Upgrades. There is no scope within the design development and modification development elements of the project because of ongoing arrangements with other C-130J users and LM Aero, and also because the method of procurement and contracting will be through the US Foreign Military Sales process.<sup>3</sup>
- SEA 1408. It is expected that the torpedo self-defence system will be acquired through Foreign Military Sales.<sup>4</sup>
- JP 129. It is anticipated that Australian industry will have the opportunity to enhance or upgrade the UAS, and potentially have the opportunity to team with foreign suppliers to implement the small UAS.<sup>5</sup>

#### Through Life Support

- AIR 5432. The industry involvement is expected to be based around developing and maintaining sufficient capability within Australian industry to undertake the through-life maintenance and support activities associated with the components and systems introduced into service by this project.

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<sup>1</sup> Defence and Industry Policy Statement 2007, p. 1

<sup>2</sup> Public DCP 2009, AIR 5432 p 38.

<sup>3</sup> Public DCP 2009, AIR 5440 p 42

<sup>4</sup> Public DCP 2009, SEA 1408, p 189

<sup>5</sup> Public DCP 2009, JP 129, p 68

- AIR 5440. The national installation and the through-life support (TLS) element of the project will be undertaken as Australian unique activities and will require Australian industry participation.
- SEA 1408. The industry requirement will be based on developing sufficient capability within Australian industry to undertake a range of through-life maintenance and support activities.
- JP 129. It is anticipated that Australian industry will have involvement with the through-life support aspects of the ADF tactical and small UAS.

The points above are not intended to be a definitive statement about the entirety of the DCP 2009, more so to provide some additional context as to why Australian defence industry has the focus that it has.

So Australia has a 'defence industry' that is fundamentally geared up to support the needs of the ADF, this is broadly translated to:

- Undertake integration of equipment sourced from overseas suppliers,
- Provide spare parts for, or to undertake repair of, foreign supplied equipment,
- Deliver support services (training, configuration management, etc), and
- Implement modifications of in service equipment.

In fact much of the dialog regarding the Australian defence industry and it's 'role' circles around the points mentioned above. Further reinforcing that these are the roles the Department of Defence needs Australian industry to fulfil.

From a more commercial perspective such roles tend to:

- represent a lower risk profile to the supplier in delivery,
- be less affected by budget reductions and/or deferrals in defence expenditure, as the equipment in service must be supported and maintained.
- Is a larger accessible market and difficult to substitute.

*"Over the next ten years, the DMO estimates that approximately 53 per cent of Australia's expenditure on materiel acquisition and sustainment will be spent in-country. Over the same period, an estimated 37 per cent of capital equipment acquisition expenditure will be spent on domestic activity, while approximately 70 per cent of the ADF's sustainment expenditure will be spent on work performed in Australia."*<sup>6</sup>

Thus it makes sense for businesses to focus on this work.

**Barrier/Impediment** - In simple terms the nature and focus of the defence industry we have established in Australia.

## Exportable Products

The focus of Australia's defence industry is to meet the needs of the ADF, a customer which spends roughly 75% of acquisition funds offshore. In country acquisition expenditure does

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<sup>6</sup> Building Australia's Defence Supply Capabilities 2012, p 8

source 'niche' sub-systems but is largely focussed on establishment of infrastructure and services associated with delivery and establishing the support system.

The result is a defence industry that has been geared up to perform local integration activities and provide support to equipment, considered by many to be world class. Unfortunately these don't readily translate into exportable commodities, for any of the following reasons:

- target customers see a value in it being done this way in their own country for the same reasons Australia does,
- they prefer the Prime equipment supplier to take full responsibility and carry liability under the auspices of a fixed price contract, and/or
- local content rules or offset obligations.

The bottom line is generally, to be able to export you must own the IP.

Services can be exported and there are examples of companies that have been able to provide their services as an 'export',

- BAE Systems providing pilot training to the Singapore Defence Force.
- Acoustic Force providing general sonar and acoustic theory training to overseas industry and defence forces<sup>7</sup>.

Note that even in these cases there is IP held by the companies. Unlike in cases of supply of technology, the risk of being replaced can be greater when supplying services, because of the nature of the IP.

In the case of the aforementioned 'niche' products, these are often what have afforded the ADF their capability advantage, this being the case it limits the possibilities for export. This is a limitation, which is understandable; however through proper open engagement it is also manageable. The case which companies have difficulty understanding or accepting are the cases when the ADF selects an alternative solution to theirs and they then cannot obtain a permit or licence for export. The angst generated in such a situation is then further compounded by the inability to obtain clear advice on the basis for denial.

***Barrier/Impediment*** - The inappropriateness of exporting niche products that either give the ADF capability advantages or could diminish a capability advantage, into the region.

## **Ownership of IP**

Much of the manufacturing work being undertaken in Australia has been manufacture under licence. To export you must have control of the Intellectual Property (IP), otherwise the exports are at the behest of the foreign owner. The US International Trafficking of Arms Regulations (ITAR) being probably the best known example of what foreign ownership means in the movement of arms across borders.

***Barrier/Impediment*** - The lack of ownership of IP within Australia.

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<sup>7</sup> From [www.acousticforce.com.au/clients/clients.htm](http://www.acousticforce.com.au/clients/clients.htm) accessed 8 Jul 14

## Market Entry

The reality is our naturally "Allied" nations already have their own substantial defence industrial base. This is a significant barrier even before procurement guidelines/rules are considered and one which is probably not resolvable by articles such as Free Trade Agreements. Australian companies which have successfully penetrated these markets have generally set up a local footprint in the country from which they secure work, an example being Austal and their work in the US LCS program.

The alternative is to look at more accessible markets and this must be done before they start to close their doors.

**Barrier/Impediment** – To great a focus on well established markets with high barriers of entry.

## How Government can better engage and assist Australian defence industry to export its products

If export of defence equipment is deemed important and an aim of the government, current policies and practices will need to be reviewed and modified to reflect such.

The DMO's mission is "*to acquire and sustain equipment for the Australian Defence Force (ADF)*"<sup>8</sup>. Their role is to provide equipment to the ADF "*... on time, on budget and to the required levels of quality and safety...*"<sup>9</sup>.

In contrast the UK's 2002 defence industry policy aimed to "*provide the Armed Forces with the equipment which they require, on time and at best value for money for the taxpayer*".

They are not unexpectedly remarkably similar.

However if we move to the determination of value for money:

From the Australian Government Procurement Statement:

*"Value for money is achieved by encouraging competitive markets, adhering to non-discriminatory purchasing practices, and using efficient, effective, ethical and transparent procurement processes. Importantly, government agencies must assess value for money on a "whole-of-life" basis. This means that agencies take into account a range of considerations other than purchase price when determining what constitutes good value for money. Agencies are not forced to choose lowest-cost suppliers when that choice would in the long-run cost the taxpayer more through the purchase of inferior quality goods or high ongoing service costs, or when that choice would have detrimental social or environmental effects"*<sup>10</sup>.

From the Defence Procurement Policy Manual (DPPM) section 1.2:

Value for money should be evaluated on a whole-of-life basis and cost is not the only factor in determining value for money. It is influenced by a number of factors including<sup>11</sup>:

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<sup>8</sup> Sourced from [www.defence.gov.au/dmo/](http://www.defence.gov.au/dmo/) accessed 10 Jul 14

<sup>9</sup> *ibid*

<sup>10</sup> Australian Government Procurement Statement July 09

<sup>11</sup> DPPM Jul 11 p 1.2-2

- fitness for purpose;
- the performance history of each tenderer;
- the relative risk of each proposal;
- the flexibility to adapt to possible change over the lifecycle of the property or service;
- financial considerations including all relevant direct or indirect benefits and costs over the whole procurement cycle; and
- the evaluation of contract options (for example, contract extension options).

The value for money assessment must take a holistic view of the tenderer and its offer against the evaluation criteria. The value for money assessment should include:<sup>12</sup>

- compliance and risk assessments for all tenderers against the conditions of participation and evaluation criteria, including relative ranking of tenderers against each criterion;
- an explanation of the key areas for discrimination between the tenderers;
- a presentation of tendered prices and an explanation of cost risk attributable to each tenderer;
- any implications relating to through life support;
- an overall assessment of the risks associated with each tender and an indication of the risk management strategies that are considered necessary;
- an explanation of the actions that would be necessary to enter into a contract i.e. negotiation required in relation to contractual non-compliance, in the form of a draft Negotiation Directive; and
- a ranking of shortlisted tenderers.

By comparison and in the context of “*best value for money for the taxpayer*”, the UK government sought to “*maximise the economic benefit to the UK from our defence expenditure, a healthy and globally competitive defence industry and the development of a high value technologically skilled industrial base, consistent with the Government’s wider manufacturing strategy.*”

This is a broad statement and might present some difficulty in measurement, but the additional focal areas of the assessment are recognisable. It is a policy developed in the framework of having a significant established defence industrial base, employing approximately 300,000 people<sup>13</sup>. More importantly it serves to highlight how policy and practices may need to be adjusted, to reflect a revised position on export.

Furthermore the government will have to clearly define the aims [in terms of defence exports], backed by specific, realistic and measurable targets.

#### Recommendation/s

The Government must clearly define the targets for defence exports.

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<sup>12</sup> DPPM July 11 p 5.6-10

<sup>13</sup> The Telegraph “*UK defence industry: in numbers*” 11 Jul 14

### **Focal Areas for Australian Defence Industry**

The capacity of Australia's defence industry is limited, it is unlikely that Australia will ever seek to establish the capability to locally design and manufacture main battle tanks. The question must then be in what areas does it make sense? Or more importantly in what areas does the government consider it relevant?

PICs could be considered as the focal areas for defence industry, they are currently:

- Electronic Warfare
- High Frequency and Phased Array Radars
- 'High End' System and 'System of Systems' Integration
- Through-life and Real Time Support of Mission and Safety Critical Software
- Anti-Tampering Capabilities
- Signature Management
- In-service Support of Collins Combat System
- Acoustic Technologies and Systems
- Ship Dry Docking Facilities and Common User Facilities
- Selected Ballistic Munitions and Explosives
- Infantry Weapons and Remote Weapons Stations
- Combat Clothing and Personal Equipment

Of the twelve capability areas identified as PICs, seven are support focussed. The other five include development of products and technology, though it may not be prudent to export it. This further highlights the focus on support and sustainment, not export.

As stated previously, it is unlikely that Australia will be able to develop and produce major items of military equipment competitively and nor should we. Specific areas should be targeted.

One possible basis for selection would be the PICs, then aligned with the needs of the ADF, as elucidated in the DCP. Consider SEA 1408 as an example, from the DCP, "Torpedoes pose a significant and lethal threat as their acoustic, tactical and dynamic capabilities are advanced, rendering simple counter-manoevres or countermeasures ineffective". The project resides in an area considered to be a Priority Industry Capability, that of Acoustic Technologies and Systems, it is highlighted as such in the DCP<sup>14</sup>. However, noting the earlier comments on the expectation for acquisition under SEA 1408, this project is unlikely to do much in developing or sustaining this PIC for the country. The natural follow on is that there will be little opportunity to secure any export sales in this area.

On the assumption this is an important capability, considerations should include:

- Should TCM be an area that Australia should look to establish a solid capability in?
- Should the Government facilitate this development?

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<sup>14</sup> Public DCP 2009 p 215

- If so how?
- How would the Government then facilitate export of the resultant product?

Determination of this is not trivial, the segments must obviously be deemed viable, but consideration of the potential negative impacts is also required. Will we damage relations with our allies? Or major trading partners? Should we establish a joint development program and improve a relationship?

In any case they must be considered, determined and promulgated.

### **Small to Medium-Sized Enterprises**

Much has been said about the importance of small to medium-sized enterprises (SMEs) to the Australian defence industry, including the following types of headline statements:

- "... account for approximately 50% of employment, or some 15,000 people, in the Australian defence industry sector".<sup>15</sup>
- It has been estimated that around 30% of the work sourced from the eight traditional 'Prime' contractors is sub-contracted to SMEs in Australia and overseas.
- innovation comes from the SMEs and they should be fostered.

The last point is one which constantly referred to, "innovation comes from the SMEs" and that they should be fostered. The question is how? There is a natural reticence for handouts and these are often not viable in the longer term. This is difficult to answer and could represent a substantive paper in its own right. The natural link though is that the results of the innovation in some variant should be available to export.

These points above are positive statements, however SMEs must be considered in an appropriate context, common traits, in no particular order, include:

1. Limited resources, which includes human, plant, capacity and capital.
2. Often have a limited 'mature' product range.
3. Limited references for their products.
4. Market experience is what has been gained from the local Australian market.
5. The Australian procurement model promotes engagement of SMEs largely through the traditional primes.

These common traits do of course put SMEs at a disadvantage, in the local market and export markets.

So the question is how can they be addressed? There is in fact an array of programs in place which aim to address some of these traits, some of which are also available to the larger members of industry. Examples include:

- PICIP
- DIRF
- GSC

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<sup>15</sup> Submission by the Australian Industry Group Defence Council to the 2013 Defence White Paper process

- EMDG
- SADI
- Enterprise Connect

So the next step is to assess how effective these programs have been.

As an outsider it is difficult to quantifiably gauge how effective they have been. In many areas data is scant, or not obtainable due to privacy requirements, or the only data available is the overly positive press releases. The result is an assessment can only be done by entity with unfettered access to the relevant data.

#### Recommendation/s

Establish a means for tangibly assessing the effectiveness of government operated programs and publish the findings.

Ensure mechanisms to support the ongoing stimulation of innovation in Australia, particularly within SMEs.

#### Equipment in Use with Parent Forces

In almost all of our discussions with overseas customers, the first question is along the lines of *"Is this in service with the Australian Navy?"*

Not surprisingly this is the first step in attempting to understand what risk may be attached to the product. For the same reasons Australian procurement benchmarks procurement options/business cases against OTS so do other nations. This is not to claim that when the answer is *"it's not currently in use with the ADF"*, the opportunity for export is lost, it does however introduce complications and will increase the effort required to secure sales.

Australia is not unique in this regard this is a view shared by Canadian defence industry is the apparent or perceived reticence to purchase locally; *"...delays caused by regulatory requirements are one issue for us. Another is that Canadian defence and security buyers seem reluctant to purchase Canadian technology, which definitely affects our competitiveness abroad."*<sup>16</sup>

Local industry must as a minimum get fair and reasonable access to the local opportunities, at the other end of the scale would be an approach which proactively encourages procurement of equipment from Australian defence industry.

Though it is somewhat outside the scope of this inquiry, there is a potential commensurate benefit to the ADF in the form of the potential to reduce the cost of through life support, due to the establishment of a larger user base.

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<sup>16</sup> Ken Walker, Vice-President for Government Relations for Ultra Electronics Canada



## Australian Product Promotion

The global defence market is highly competitive and the introduction of new competitors will only serve to increase this. This must be recognised and similar approaches adopted by the Australian government.

Recognition of the advantage for [UK] industry that can be gained through the use of their uniformed service personnel is clear from the following statement “*Demonstrating the potential of a capability by our highly skilled Armed Forces is a huge selling point for UK industry, and such support is of vital importance if we are to maintain an edge in an increasingly competitive global market*”<sup>17</sup>. The UK is not unique in this regard, there are other nations using similar advocacy methods, the US and French for example.

Programs such as Team Australia are a good initiative, however are they sufficient to counter the approach being adopted by our ‘competitors’? The next reality to come to grips with is that fact that in this case our competitors, will to a significant degree be our allies. Australia will have to adopt a more hands on approach to promoting Australian defence equipment.

### Recommendation/s

Use the breadth of resources available to the government to raise awareness of Australian products in service.

Australian developed products in service with the ADF should be identified and agreement struck between the supplier and government for how to promote them.

## Operation of the Defence Export Control Office

This topic extends beyond the Defence Export Control Office, because the issue of Export Control and more importantly the processing and assessment of applications is broader than that office. The process has been considered as elements of a lifecycle, which we have labelled; 1 Pre-application; 2 Application; 3 Assessment; 4 Advice; and 5 Review.

### Pre-Application

Provision of or access to information which would have relevance to the pursuit of an export, and a potential application, would help companies to make informed decisions about whether or not to pursue an export.

Why is it not possible to inform members of Australian defence industry about Government assessments which would or could affect a potential defence export? Specific details of the basis for the decision do not have to be disclosed; however such a brief could be done as a classified briefing, ensuring no doubt about the sensitivity of the information. Advice along the lines of “we know more than you do about what’s going on in that region” whilst quite probably correct, does not help to inform companies regarding investment.

It is acknowledged that this would result in an increased workload within the department; however this would hopefully be offset through:

- Avoiding wasted efforts by companies pursuing export opportunities that wouldn’t obtain approval, and
- Reduction in applications needing processing by the department.

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<sup>17</sup> Ibid p 24

## **Application**

The application process is relatively straight forward and the new online process has, in our experience, proven to be easy to follow and simple to complete.

Some questions that have been posed to us by overseas customers in relation to data about items to be exported:

- At what classification are the information systems that hold the data covering an exported item?
- Who has access to those repositories?
- How secure are the data repositories which store the information about the equipment and systems being exported?

The context is that some customers, particularly for certain types of equipment, will deem certain sets of information, once collated, to be classified on the basis that as a 'suite' of information it provides insight into their resultant capability.

This is likely to be a greater problem as Australian defence industry can progress further up the technology chain. The processes and supporting infrastructure will need to be capable of addressing this issue in the future.

## **Recommendation/s**

Establish suitable processes and systems for handling and storing information regarding an export, which have been deemed 'classified' by an end user.

## **Assessment**

There are two components of the assessment stage that must be considered, one is the actual process and the other is the time to process.

### **The Assessment Process**

The assessment process is outlined in higher level broad terms and it is this high level explanation that is referred to when queries regarding the assessment are posed.

The process is not transparent, and it is understood that there are quite valid reasons for ensuring some elements of the assessment process remain 'hidden'. Unfortunately it is the broad high level outline that is referred to when an applicant seeks further information. Unfortunately for a business this is insufficient to make substantive decisions on investment regarding advancing existing products or developing new ones.

Under the current arrangements, when an export permit is denied, it is not possible to obtain advice on the actual grounds/reasons for denial. Or at least it has not been possible for us to obtain definitive advice regarding the grounds for refusal.

In the face of such a position how can a business improve decision making?

In such cases where there appears grounds for a denial exist, the aim should be to work with the company to determine if it might be possible to address those elements such that an export could proceed.

#### Recommendation/s

Establish a means to enable engagement with applicants to work through the issues identified in an application for export. Such that when the Department becomes aware, through processing an application, that grounds exist to decline an export permit, the engagement process is initiated.

#### The Assessment Timeline

The DECO advice on time for processing applications for export is:

*“Other than in exceptional circumstances, the assessment time for routine applications is up to 15 working days, (commencing from the date a complete application, with all supporting documentation, is received). For applications requiring referral to SIDCDE, the assessment time is up to 35 working days. DECO will inform applicants of the referral.”*

In our experience we have rarely had applications processed within these timeframes, which is without question the result of almost all our applications having to be referred to the SIDCDE. Earlier this year we had MIP approvals processed in one day. Cases referred to the SIDCDE invariably take longer than the 35 days, the longest approval in the last two years has been in the order of 7 ½ months.

The question must be asked, if the tables were turned and it was the ADF seeking an item from overseas, would it be acceptable to wait such periods to get an approval?

If exports increase so will the workload, it will be vital to ensure that the processes and consumption of resources in processing is appropriate.

#### Recommendation/s

Establish realistic timeframes for processing and use processing times as a benchmark of the performance of assessing entities.

Ensure processes are suitable consuming an appropriate level of resources.

#### Validity Period of the Permit/Licence

The validity period for export permits or licenses, can be too restrictive.

Our company has been in situations where we have been issued an MIP, then having secured the contract we have sought to obtain the relevant export permit (some foreign customers, will stipulate this as a contractual and financial milestone), only to be advised that as the system would not be exported within 12/24 months a permit could not be issued.

If Australia is to have a credible defence export industry, the industry must be backed by robust processes which have been prepared in the context of that industry. Is a 12 month validity period long enough to build a combat system for a Frigate?

By comparison, under the US system commercial license authorization<sup>18</sup> to sell is valid for four years.

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<sup>18</sup> One of the two methods available in the US for exporting arms.

As an export permit addresses a specific product, in a specific quantity, to a specific customer the need to time bound it, within reason, is questionable. Whereas an export licence covers a specific product, it enables multiple shipments to a range of customers, which does provide grounds for placing an expiry period on the licence.

Of interest in 2012 there was no requirement for the exporter to inform the State Department details regarding any contract secured under the license authorization, including whether the contract was reduced in scope or cancelled.

Recommendation/s

Establish a mechanism for export permits to have a longer validity period.

## **Review**

Once a decision on the suitability or otherwise of an exportable product has been made, the decision is final, that is there is no mechanism for it to be reviewed by an alternative authority/body. This issue is further complicated by the inability to get advice on the basis of the decision.

Recommendation/s

Consider establishing a mechanism to enable applicants to request a review of export assessments.

## **Assessment of the export support given to defence industry by governments of comparable nations**

The absence of a definition for 'comparable' makes it difficult to ensure the response provided aligns with the committees' expectations. Sonartech is confident this term will be interpreted quite differently, by responding and interested parties.

What would be a comparable nation? What is the best means of determining or identifying a comparable nation? It could be determined in any number of ways, including:

- Percentage of GDP spent on defence/military,
- Defence industry turn over,
- Percentage of defence expenditure on imports,
- Nations Australia naturally aligns with,
- Nations with similar aspirations for their defence industry,
- Nations with a defence industry with the same capabilities.

Australia, generally sees itself as a peer of its 'Five Eye' colleagues, of course the members are quite different on many perspectives, certainly those in relation to military expenditure, [local] defence industry footprints and size of their forces. In many aspects the most comparable to Australia would probably be Canada.

## Canada

The Canadian defence and security related industry contains more than 2,000 companies and employs 70,000 workers, generating annual revenues of roughly CAN \$12.6 Billion<sup>19</sup>, as such it an important segment of the Canadian economy. The Canadian Trade Commissioner also see it as a crucial element of their export sector, with half of its products and services sold abroad, though about 80 percent of them go to the United States.

In the 2010 and 2011 Canada's total exports of military goods and technology was in the order CAN \$1.04 billion<sup>20</sup>. The majority of which, roughly 59%, were supplies to other NATO members. The UK is the single greatest recipient of Canadian military exports each year, and in the 2010- 2011 period received CAN \$261 million in military exports.

Canada is actively trying to stimulate their local industry, with the establishment of programs such as the Industrial and Regional Benefits (IRB) policy. The IRB requires the successful bidder of major defence contracts to engage Canadian industry, in some form, it does not have to be that contract. As at 2011 IRB obligations totalled approximately CAN \$23 billion and amount expected to more than double from the procurements planned out to 2027<sup>21</sup>.

The Canadian view is:

*"Even in the absence of a major increase in defence spending, it would be in the national interest to have a strong domestic defence industrial base, one that goes well beyond the basic capability of maintenance and repair to the actual sovereign production of key goods and services. In addition to a sovereignty rationale, defence-related industries are important sources of technological dynamism and innovation. They are leading-edge participants in global value chains, and generators of high-value exports and well paying jobs. Accordingly, they should be supported as drivers of long-term growth and prosperity".<sup>22</sup>*

## United States

The United States is a major international trading entity and the largest supplier of arms globally, holding 39% of the global market in 2012. In 2012 the total value of US exports was US \$2.2 Trillion, of which military exports totalled US \$73 Billion. The Government has established a range of mechanisms and programs to facilitate export, with support at the highest levels. In 2010 President Obama launched the National Export Initiative, one element of a strategy to double US exports (across all sectors) by the end of 2014.

The US Government's Advocacy Center is an office established to support US companies in their marketing to foreign governments, this includes defence companies. Their mission is:

*"...to coordinate U.S. Government resources and authority in order to level the playing field on behalf of U.S. business interests as they compete against foreign firms for specific international contracts or other U.S. export opportunities. In doing so, the Advocacy Center helps create and retain U.S. jobs through exports."*

A primary means of implementation is the coordination and engagement of federal government Agencies throughout the Advocacy activity. One example being the Department of State's assistance with more than US \$2.5 billion worth of deals quarter four of 2012. The International Trade Administration claims that in 2012, their advocacy activities resulted in

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<sup>19</sup> Canada First: Leveraging Defence Procurement Through Key Industrial Capabilities

<sup>20</sup> Deliveries to the US are not contained in these figures as they are handled via different mechanisms.

<sup>21</sup> Canada First: Leveraging Defence Procurement Through Key Industrial Capabilities

<sup>22</sup> Canada First: Leveraging Defence Procurement Through Key Industrial Capabilities p xiii

success for US companies in the order of \$36.6 billion, which is almost double the result of 2010. By the end of 2012 the Center was handling 657 active advocacy cases.

The US has two distinct mechanisms for supply of weapons, the Foreign Military Sales (FMS) program, a government to government means of supplying equipment and the licenced commercial export system. The FMS program is the most prevalent means of export of US arms and probably the most well known. The US considers it to be a form of security assistance and a fundamental tool of U.S. foreign policy. It could be considered a joint program, whereby the Secretary of State determines which countries have access to an FMS program and the Secretary of Defense is responsible for executing the program. Supply under the FMS program can occur under funding from the recipient nation or via the US Foreign Military Financing (FMF) program; these may be provided in the form of a loan or as a Grant where the funds are not required to be repaid.

## UK

The UK is also quite active in promoting defence exports, probably more so in the face of the cuts to the military budget and the need to sustain a defence industry which holds many capabilities deemed to be of strategic importance. For context in 2013, from figures released 8 Jul 14, UK defence and security exports totalled £13 billion, and increase of 13% over 2012.

The UK has a variety of programs to support their defence industry both in local development and in export. What is worth noting is how the Government has demonstrated it's recognition of the importance of the defence industry to the UK, the Defence Industrial Policy 2002 was signed by both the Minister for State for Defence Procurement and the Minister for State for Employment Relations, Industry and the Regions<sup>23</sup>. The importance of the industry goes beyond the direct benefit to the UK's Armed Forces and as such it deserves attention from other interested government departments/agencies.

Support and promotion of military exports used to be handled by, the Defence Export Service Organisation (DESO), which was a department within the Ministry of Defence. In 2007 the then Prime Minister Gordon Brown announced DESO would be shut down the following year<sup>24</sup>.

From April 2008 the responsibility for support of defence exports transferred to the newly established a Defence and Security Organisation (DSO), by both civilian and military personnel, within UK Trade & Investment (UKTI).

Of note there are parallels between most of the services and assistance the DSO provides to UK industry to what is provided in Australia. One distinct difference is the promotion and representation of UK military equipment by uniform personnel and the facilitation of military specialists for UK industry enabling them to gain access to objective advice and support regarding military doctrine, equipment and services.

The UK's view of their defence industry and the role it plays is nicely summarised by Sir Gerald Howarth in 2011, when he was the Minister for International Security Strategy from May 2010 to September 2012. *"Over the past year in office, led by the Prime Minister, my ministerial colleagues and I have travelled to a number of countries to strengthen our bilateral ties while promoting British defence industry. Selling equipment can help to achieve our defence diplomacy objectives by enabling countries to participate in joint military operations, or help a nation defend itself against mutual potential adversaries. It can also*

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<sup>23</sup> Defence Industrial Policy, London, Ministry of Defence, 2002, p. 4.

<sup>24</sup> Defence Industry Daily "UK's DESO Done In" 2 Apr 08

*serve to increase influence by building up a trusting relationship with nations that can last for generations.”<sup>25</sup>*

## **Other ‘Comparable’ Nations**

### **Turkey**

Turkey has an ambitious plan for growing their defence industrial base, which has a strong focus on export. For this reason they warrant consideration in the context of defence exports.

Turkey’s defence [and security] budget in 2014 was USD \$25.356B.

The Undersecretariat for Defence Industries (SSM), the equivalent of the DMO, is responsible for providing capabilities to the armed forces, as well as the development of the country’s defence industry and its technologies.

The Turkish Government has a goal of reducing reliance on arms imports and growing its exports, setting a target of US \$8B by 2016. Last year the countries Defence and Aerospace Industry Exporters Union are seeking to have 5% of the countries total exports to be in the areas of defence, systems, platforms and services.

The Government has launched policy, established processes and made commitments to support these goals, these include:

- Commitment of 5% of the defence budget towards R&D.
- Defence procurement should provide the stimulus for industrial development,
- Increasing the offset requirement to 70%,
- Establishment of co-production deals involving transfer of important technology to Turkey,

Whether you agree or disagree with their model, the program is working with ‘defence’ exports reaching a total of \$1.4B in 2013, which represented a 43% increase over the total of defence exports in 2008.<sup>26</sup>

From the 2012-2016 Strategic Plan, SSM’s vision is “Making Turkey superior in defence and security technologies” their mission is “Management of industrialization, technology and procurement programs that assures the continuous improvement of Turkey’s defence and security capabilities.”

## **Recommendation/s (from this section)**

Recognise the importance of defence exports beyond those that directly benefit the ADF. Establish a joint responsibility for Australian defence industry between the Department of Defence and the Department of Industry.

Recognise the value Australia can obtain in international relationships from defence exports and address it appropriately.

Proactively seek to procure equipment from Australian defence industry.

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<sup>25</sup> RUSI Defence Systems “Ministry of Defence Support to Defence Exports” Autumn/Winter 2011 p 23

<sup>26</sup> Defence News “Turkish Defence Exports Hit \$1.4B Record in 2013” 13 Jan 14

## **Any other related matters**

### **Offset and Local Industry Content Mandates**

Australia has moved away from the concept of mandating 'offset' or local industry content in defence, and broader Government, procurement on the basis of valid reasons. In fact the very mention of it these days brings scowls and derogatory comments. They should however be understood and understood in context.

Whilst Australia is operating in the realm of a 'free market', all nations have not adopted the same approach. In fact the majority of our potential export customers have offset programs in place. The aim may be to protect Australian taxpayers from carrying an inefficient industry and rightly so, however what impact does or will this have on the ability of Australian Industry to export.

Whether we like them or not previous local content policies were the foundation that established the in country support capabilities Australia has today. So they did deliver benefits.

### **Sovereign Capability**

Defence industry is somewhat unique in that governments, domestic or foreign, are the only [legal] customers. It is largely seen as a sovereign capability and as such Governments, even when having signed a Free Trade Agreement, will retain flexibility to favour their own local suppliers. In developed nations governments tend to encourage development of their domestic defence industry, seeing it not just as a means of enhancing their ability to protect their nation but also as a vital avenue for stimulating innovation and growth.

In the context of supportability the benefit of using Australian developed products is clear, concern regarding cost of sustainment can be defrayed through the establishment of a larger user base. The impact and importance of having Australian developed products in service with the ADF should not be underestimated in the context of exporting.

The reality is that Australia's defence industry is linked to the governments' policies and practices. If defence exports are deemed important then the policies and practices must be adjusted to reflect this importance. If this is to be done it should be done proactively, at a pace appropriate for the maturity of the exports yet cognisant of accessibility of the targets markets now and into the future.

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11<sup>th</sup> July 2014