



Inquiry into the establishment of an Australia Fund

AMWU December 2014

Introduction

The Australian Manufacturing Workers' Union (AMWU) represents approximately 100,000 members working across major sectors of the Australian economy. AMWU members are primarily based in manufacturing industries, in particular; metal, vehicle, and food manufacturing, but also in the industries of mining, building and construction, printing and graphic arts, repair and service and laboratory and technical services.

The AMWU has actively engaged in the various processes this government established to forge an industry policy that would enable Australia to retain and grow an advanced manufacturing and engineering capacity. The challenges faced by our manufacturing sector are not isolated to automotive or ship manufacturing but affect the entire sector and as a result the entire economy. Yet our repeated calls for an active government industry policy to meet these challenges has fallen on death ears.

Instead of formulating a policy to deal with the continuing hollowing out of our nation's manufacturing capacity, especially in regional Australia, situation which we believe threatens Australia's status as an advanced economy,¹ this government's actions show its indifference to this situation. Whether we look at an automotive manufacturing policy that through inaction has triggered the announced departure of vehicle manufacturers in this country, or the government's woefully inadequate response to this closure, or its refusal to secure the future of the nation's shipbuilding sector, or its Competitiveness Agenda which represents little more than a fig leaf; the government's record will result in tens if not hundreds of thousands of jobs lost, as well as a much less advanced and balanced economy.

In response to this policy vacuum, the AMWU has proposed through several processes industry policies aimed at ensuring Australia maintains and grows its advanced manufacturing base. These include the Productivity Commission inquiry into the automotive industry, the Government's review into the Victorian and South Australian economies, the Senate inquiry into the shipbuilding industry, the Defence White paper and First Principles review and the Senate inquiry into the Innovation System. Our submissions into these processes outline a detailed innovative approach to industry policy. We commend them to the Committee.²

In light of the significant work that is represented in detail in other AMWU submissions as outlined above, this submission will provide an outline of the most relevant aspects of this work rather than re-present that work.

An integrated growth focused industry policy

¹ A belief that is shared by others, including respected academics such as Goran Roos, Roy Green and John Spoehr.

² These and other submissions are available at: A central proposition
<http://www.amwu.org.au/news/37/research%20reports%20submissions/>

A central component of the AMWU's approach to industry policy is the recognition that in order to build the advanced and competitive industry base we need to safeguard our future prosperity, we need to do everything possible to support:

- Innovation of new technology, both for new products, capital and processes,
- The deployment of new innovation by business through investment,
- The adaptation by business of high performance management and organisational approaches, including giving workers a greater say in decisions as well as listening to worker ideas, and
- The integration of Australian businesses into global supply chains and access to new markets.

These are tasks that require a coordinated industry/innovation policy and cannot possibly be addressed through one single policy innovation. An integrated system wide approach is needed. However as part of this system wide approach, the AMWU argue that a new institution is needed to support otherwise financially constrained firms to develop and deploy new technologies through investment.

That is why the AMWU have and continue to advocate for a Manufacturing Finance Corporation (MFC). Such a corporation would have a similar role to that envisioned for the Australia Fund. The case for such a fund is widely known and well understood, and is based on existing market failures that retard new investment in manufacturing. The case is summarised in our Innovation System Inquiry submission:

“Just 20% of Australian manufacturers are classified as high or medium technology. This is due to sustained underinvestment in the sector, as well as poor management skills and practises.

The ABS data make clear that the most pressing barrier to investment in and deployment of new innovation is access to finance. This is particularly the case for small (fewer than 20 workers) and medium sized businesses (between 20 and 199 workers), of which 19% and 23% respectively report finance as the greatest barrier to innovation. This figure is 16.5% for large firms (over 200 workers) and 20% overall. Finance represents the greatest barriers by far across all size businesses, with cost of development and/or implementation as the third most cited barrier (on average 14.4% of businesses).

However, cost of development and deployment is closely related to access to finance, and it is not clear that businesses are not revealing the same basic pressures when citing access to finance or cost; namely an inability to invest in innovation due to cash flow and other finance restrictions. If we combine these two factors, almost 35% of businesses are not investing in innovation or deploying new technologies, processes

etcetera, due to prohibitive costs or an inability to fund the investment. This is not surprising in the AMWU's experience. When discussing business conditions with firms that employ members, we never hear of levels of required returns on new investments that are lower than 14%. It is clear that in order to maximise the take up of innovation as well new investments, businesses need to access sufficient funding, especially small and medium sized businesses (SMEs).

In the AMWU's view, manufacturing businesses face additional barriers to financing, both for diversification projects (especially for auto suppliers facing the loss of their major customer), and for more general investment projects aimed at improving competitiveness, usually through the adoption of some type of innovation. This is supported not just by anecdotal experience of the AMWU. The Australian Industry Group (AIG), recently stated in their submission into Australia's Financial System:³ *"official data and anecdotal reports from Ai Group members indicate banks are still reticent to lend, particularly to manufacturers."* The AIG go on to say:

"Ai Group has been concerned for some time that banks impose especially stringent lending criteria on the manufacturing sector. In a 2011 survey of members, we concluded that financial institutions, responding to the perception of higher risks facing the industrial sector, were downgrading manufacturing industries and making access to finance more difficult and expensive for businesses across the entire sector, regardless of their individual circumstances and risks."

This finding was also reached in the report by non-government members of the Prime Ministers' Manufacturing Taskforce, in August 2012. The report noted that access to finance for the manufacturing sector was one of the major challenges for the sector in the years ahead."

Most recently, automotive supply chain businesses are reporting similar concerns to Ai Group following the recent decisions by the three car assemblers to end local production. The supply chain companies have told Ai Group that difficulties accessing bank finance to invest in new machinery and equipment is one of the main barriers stopping them from transitioning to new markets instead of winding up."

³ Available at: http://fsi.gov.au/files/2014/04/Australian_Industry_Group.pdf

Any attempt to address the ability of our industries to deploy new innovations and move up the value chain, as well re-vitalise our industrial base, needs to address this financing issue.

That is why the AMWU has been advocating for a Manufacturing Finance Corporation (MFC), based on the Clean Energy Finance Corporation (CEFC). The CEFC supports the take up of low carbon technologies across the economy with various publically funded financing products (including concessional loans) based on the fact these technologies are new to the market and financial sector (and are hence treated as very risky), and there is a broader public good reason to support investment in low carbon technologies that exceeds the private returns to these investments (namely combating climate change). The AMWU considers that similar reasons exist for the creation of a MFC.

Advanced manufacturing technologies are also new and their potential and functioning is also little understood by the finance industry. Whether they be additive manufacturing, new forms of computation, design and censoring, new materials and their applications or advanced applications of biological breakthroughs, a large raft of new technological fields are revolutionising manufacturing globally, but Australian financial institutions are understandably reluctant to invest in these technologies, especially when they have the option of investing in mining as an alternative.⁴

In addition, as outlined above, there is a public interest in maintaining and growing Australia's industrial base. Whether couched in terms of economic complexity or diversification or the need to support good high income jobs and a range of skills and abilities across the economy, there is no doubt it is in the nation's long term interest to have a broad economic base that is not reliant on mining and agriculture for our future prosperity.

As outlined above, this public good extends to supporting the maintenance and diversification of existing manufacturing businesses, especially the hundreds of automotive supply chain firms facing a grim future, but also many other in many sectors of the economy.

⁴ Indeed, the AMWU believes there is a broader public good case for government to invest in the application of new technologies for this reason, regardless of the sector involved.

It is worth noting that a MFC would not constitute government spending, but an equity injection by government. As such, it would not add to any government deficit.

Concessional loans would be registered as additional public debt, but only to the degree they are concessional, not to the total value of the loan.

Similar loan programs/corporations exist in the UK, targeting SME businesses⁵ and the Australian Industry Group has suggested government provided 'soft loans' as part of the government's Growth Fund program.⁶ Government provided financial assistance for import and export activity is also commonly provided through financing corporations of the CEFC type. The Export Finance and Insurance Corporation is an example in Australia,⁷ while the Export-Import Bank is the USA equivalent.⁸ In fact, these export credit agencies are extremely common, with at least 40 operating with government backing.⁹

Some details of how such a MFC could work are presented below. In addition to its investment promotion activities, a MFC could link all clients to the relevant Industry Innovation Precinct, Enterprise Connect and the CSIRO industry liaison division, to ensure the each firm enters a network of supportive public institutions, businesses and researchers. Such a network should represent an industry ecosystem, where businesses, researchers, financiers and government agencies cooperate to generate the best business and economic outcomes for the nation. In addition, as has been born out in the CEFC example, often such a corporation can assist in gaining private funds for a project, just by performing due diligence, creating a signal that the project is viable and acting as an intermediary."

The submission goes on to describe how a MFC could be structured and how it could operate:

"The MFC: Structure and governance

⁵ See: <http://www.capitalforenterprise.gov.uk/>

⁶ See the AIG final submission into the Productivity Commission's review into the automotive industry, available at: http://www.pc.gov.au/_data/assets/pdf_file/0005/134186/subpp242-automotive.pdf

⁷ See: <http://www.efic.gov.au/Pages/homepage.aspx>

⁸ See: <http://www.exim.gov/>

⁹ See: http://en.wikipedia.org/wiki/Export_credit_agency

The MFC would be supported by an equity injection from the Commonwealth, and function as a Commonwealth Corporation.

It would be governed by an independent board of governors, comprising leaders in the fields of finance, industry (manufacturing), science and technology, and unions.

It would be headed by a CEO, who would be a high profile Australian of exceptional caliber and integrity and be responsible for the running of the Corporation on a day to day basis.

The MFC would be brought into existence by an Act of parliament, establishing its functions and responsibilities in legislation.

It would be expected that the Corporation would apply commercial rigor when making its investment decisions, focusing on projects and technologies at the later stages of development. By adopting a commercial approach, it would be expected that the Corporation would invest responsibly and manage risk so it is financially self-sufficient and achieves a benchmark rate of return. This benchmark rate of return would be expected to be met across the whole portfolio of the Corporation's assets, not by any specific asset.

The benchmark rate of return would be set by legislative instrument, and would be equivalent to the average 5 year government bond rate.

The MFC: Function

The government would have the expectation that the Board will take a long-term outlook when setting the investment strategy for the Corporation.

The Corporation would be the government's primary mechanism to help mobilise investment in the Australian manufacturing sector, to improve its competitiveness through the deployment of new technologies, and over the long term to transform the sector into an 'advanced manufacturing' sector.

An advanced manufacturing sector is one that entails the rapid transfer of science and technology into manufacturing products and processes. Its competitive advantage is based on the use and coordination of technologies like IT, automation, nanotechnology, computation, sensing, and networking, and materials in either processes or products.

The Corporation will invest at the demonstration, commercialisation and deployment stages of innovation. The Corporation will be established to finance the renewal of Australia's manufacturing industrial base using financial products and structures to address the barriers inhibiting investment.

The Corporation will have regard to its potential effect on other market participants when considering investment proposals. In line with its policy intent, the Corporation should have regard to positive externalities and public policy outcomes when making investment decisions and when determining the extent of any concessionality for an investment."

As discussed above, in order to be as effective as possible, a MFC would need to work in conjunction with other institutions such as universities, the CSIRO, Austrade, Enterprise Connect and Commercialisation Australia (or their scaled down replacement, the Entrepreneurs' Infrastructure Program) as well as the Clean Technology Finance Corporation and the Export Finance Insurance Corporation.

At a minimum, the establishment of an Australia Fund should be aimed at the same policy goals that are outlined above for the MFC. The MFC can also serve as a basis for part or all of the functioning/design of any Australia Fund.

Industry policy to minimize damage

Policy is needed to mitigate the impacts of the closure of the automotive manufacturing industry, especially policy to assist in the transition of supply chain firms to new products and markets. Only through active policy intervention can the employment, social and community impacts of closure be minimized.

To date, the government's response to this task has been so inadequate as to be laughable. The \$155 Growth Fund announced in response to the industry's closure includes a \$20 million diversification fund to help supply chain firms diversify. In addition, only \$3 million of this represents new funding for diversification support, as \$17 million of the fund has been transferred from the now closed Automotive New Markets program, which was also aimed at assisting auto supply chain diversification.

As outlined in the AMWU submission to the inquiry into the Automotive Transformation Scheme (ATS) Amendment Bill,¹⁰ the AMWU believes that rather than cut \$900 million from the ATS, the government should be using this funding to assist industry transition and diversification. Our proposed approach is to reform the functioning of the ATS program to broaden its scope, in particular into industry diversification.

As a goal of any Australia Fund, strong consideration should be given to the fund providing auto supply chain diversification support, as well as broader industry development support. As such any approach needs to consider how best to incorporate the ATS, its funding and its role into any future Australia Fund.

One option, which would receive the support of the AMWU, is to establish an Australia Fund that has two components; a MFC based industry growth role, focused on new businesses and existing SMEs, and an industry transition role focused on supporting businesses facing almost certain closure due to broader factors such as the closure of the automotive manufacturing operations. This second role could be supported by winding in the ATS into a broader grants based program to support supply chain businesses, as well as key advanced manufacturing sectors currently under extreme pressure such as automotive manufacturing, food processing and shipbuilding.

Conclusion

Regardless of the form of a Future Fund, the AMWU strongly supports any move to re-animate industry policy towards ensuring Australia's industrial base grows both in terms of size and in terms of capability. This inquiry represents an acknowledgement that Parliament recognises the government does have a central role to play in supporting industry development, even if the current government is reluctant to make the same acknowledgement, especially through actions rather than words.

However, any Australia Fund cannot work in isolation and to truly be effective in ensuring Australia maintains a technologically advanced and diverse economy, needs to be complimented by a raft of policies aimed at supporting skills, work and fair competition for Australian industry.

¹⁰ Available at:

http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/ATS_Amendment_2014/Submissions