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SUBMISSION TO SENATE ECONOMICS REFERENCE COMMITTEE ENQUIRY INTO NAVAL SHIP BUILDING

PART II: The future sustainability of Australia's strategically important naval shipbuilding industry

Forgacs wishes to place on record its support for a rolling build of vessels to deliver a genuine, long term future for Australia's naval shipbuilding industry.

This premise has been widely promoted by the shipbuilding industry, peak bodies, unions and various experts for many decades and there has long been general agreement that when more ships are built the outcomes are significantly better.

By definition a rolling build involves the continuous build and steady delivery schedule of vessels. This approach sustains navy capability as it delivers on-time replacement for ships as they reach the end of their service life. It also offers a predictable pipeline of work for the shipbuilding industry and job security for its workers. This level of certainty improves industry performance through better workforce skills and experience along with increased investment in shipyard infrastructure.

Industry performance over the past 50+ years confirms this thinking: during periods when few vessels were built and there were gaps in demand (the *valley of death*) performance was poor but when the reverse happened successful shipbuilding projects such as the Huon class minehunters and the ANZAC frigates were delivered. Both projects are recognised as high points in Australia's shipbuilding history.

More recently, the Air Warfare Destroyer program has reignited the debate around the capability of local shipbuilders. The early quality and productivity results were below target and have drawn criticism. However, the context, in part, for these performance issues was that the industry in general was gearing up again from a *valley of death* and this takes time, effort and investment.

Forgacs' experience during the AWD program clearly demonstrates this issue.

In simple terms the company has, during the past 18 months significantly lifted its across the board performance, schedule, quality and cost are now either at or ahead of target. A comparison of Ship 3 performance with that of Ship 1, for example, shows an improvement in man hours per tonne of 33%+ between the two ships. There have been similar improvements across all metrics.

This clearly demonstrates the performance improvements attributable to successive build experience – the more you build the better you get!

But the benefits of a sustainable naval shipbuilding industry extend far beyond the actual building of surface combatants and submarines. The ability to carry out indigenous through life support (TLS) of naval vessels is a key issue and largely depends on the knowledge and skills that flow from the actual building of the ships – this is particularly evident as ship complexity increases. It is difficult to have a TLS industry without a successful naval shipbuilding industry.

There are also clearly identifiable nation building benefits for Australia which are focused on future prosperity and security.

These benefits include, but are not limited to:

1. The retention of skills and capability

During the course of the AWD project substantial investment by ASC, BAE and Forgacs has built a workforce with world-class skills and knowledge.

But as the AWD project comes to an end, and if no other projects have come on-stream, these skilled workers, who have come at such a high price, will be lost to the industry and will move off into other potentially more sustainable jobs in different industry sectors, or they will be lost to industry overseas.

As well as losing those skills to the shipbuilding industry they will be lost to the ship maintenance industry. Our strategically important ability to build and maintain ships in this country will be compromised and possibly never retrieved.

Conversely, a rolling build of surface combatants and submarines will provide certainty and will enable industry to retain the skills and capability that deliver productivity and efficiency.

2. Sovereignty

As an island nation Australia's sovereignty relies heavily on its naval strength and its ability to maintain its maritime approaches.

A capable and strategic defence capability relies on this country's ability to build and maintain ships with the help of skilled and dedicated Australians whose first allegiance is to Australia.

Indeed the Senate Economics Reference Committee's Part 1 report for this enquiry concluded that 'National security concerns are central to any consideration about Australia having a naval shipbuilding industry and the priorities should be given to developing and retaining the skill base and experience to support that industry.'

In his 2013 document 'The Future of Naval Shipbuilding' Raytheon's managing director, expressed the view, 'In the current era, the indigenous defence industry is a key component of national defence capability.....it exists as one of the fundamental elements of the national security infrastructure'.

The ability of this country to maintain its sovereign borders is fundamental and unarguable. But this will be more than difficult for Australia's defence forces without an indigenous naval shipbuilding and TLS industry.

Sovereignty and national security are key issues in the naval shipbuilding debate and must be given at least equal consideration alongside the economic factors.

3. Economic advantages

The December 2013 ACIL Allen Consulting report 'Naval Shipbuilding and Through Life Support – economic value to Australia' clearly sets out a number of economic advantages that flow from an indigenous naval shipbuilding industry.

The executive summary says in part (ACIL Allen Consulting, 2013):

Naval shipbuilding is an important contributor to the Australian economy. It directly employs some 6,000 people, and indirectly nearly 15,000 people. The industry makes a contribution to the Australian economy of between (conservatively) \$1.5 billion up to around \$2.3 billion (based on total multipliers) per annum.

Around 7,400 full time equivalent (FTE) jobs across Australia can be attributed to the production of naval vessels by the five largest prime contractors in the industry. In addition, up to 7,560 FTE jobs can be attributed to the activities associated with through life support of naval vessels.

Thus, the total FTE jobs generated across Australia – and including direct employees, contractors and other flow-on jobs – is nearly 15,000. Because this is based on the sample of the five large contractors only it is a conservative estimate.

Of the potential \$2.3 billion contribution from naval shipbuilding and through life support to the economy, the majority comes from the production side (\$1.3 billion); however, the contribution from TLS is still highly significant (\$975 million).

In addition, there is wide agreement that an indigenous naval shipbuilding industry delivers a significant range of economic benefits including increased gross domestic product from capital investment and reduced pressure on the balance of payments – as well as foreign investment.

Moreover, in the face of a lower exchange rate for the Australian dollar the economic benefits of local shipbuilding increase substantially. In Professor Goran Roos' submission (Submission 25 to the inquiry) he states, 'at a more competitive exchange rate of 70 cents per \$US, the impact of an overseas build could be up to 30 per cent worse.'

The economic benefits of an indigenous naval shipbuilding industry are substantial and nation building.

4. Sustainment and through life support

The symbiotic relationship between naval shipbuilding and through life support (TLS) is well documented – as is the Royal Australian Navy's requirement to have in-country TLS capability.

As stated on page 66 of the Part 1 report from the naval shipbuilding inquiry, it is a commonly held belief that for every dollar spent across the life of a vessel (build and sustainment) approximately \$0.70 is allocated to TLS, hence the necessity to consider the cost of TLS as an integral part of the local naval shipbuilding industry.

In fact, the savings are considered to be so substantial that they will offset any additional costs incurred during the build phase.

It is also widely acknowledged that maintaining and upgrading naval vessels requires extensive information, knowledge and skills and these are most efficiently achieved during the build phase – particularly for more complex vessels.

The issues are:

- TLS must be done – it accounts for around 70% of total vessel cost
- As an independent nation Australia must be able to do this work – there are national security and cost savings
- TLS cost savings are generally sufficient to offset any additional build costs
- TLS requires extensive information, knowledge and skills - it is better to acquire these during the build phase

5. Development of Australian engineers and technicians

The upskilling of Australia's blue and white collar workforces through the construction of complex naval platforms is central to this country's advanced design and manufacturing capability.

Education standards are key to upskilling – especially the extent of take up of maths and science subjects which is fundamental to the future of all Australian industries.

Similarly, the development and retention of engineers and technical staff is a key requirement for Australia.

In this regard trade technicians are as important to the construction process as engineers. The technicians' role is to take engineers' designs and create/build naval vessels or items of infrastructure from them.

The combined skill set of these specialist technicians enables them to provide maintenance and operational support for our most complex marine assets such as the Collins Class submarines.

Shipbuilding provides the opportunity to create and develop these capabilities which are highly transportable to other industry sectors when required.

This country's future will be poorer without this opportunity.

6. Local area– the Hunter region of NSW

Newcastle's shipbuilding industry is a significant contributor to the regional and NSW economies as well as the national GDP.

When the AWD project was at its peak and Forgacs was employing approximately 900 highly skilled workers the wages and labour hire costs accounted for approximately \$90million/per annum – the majority of which was spent locally by families.

In addition to employment the company provided training and development opportunities for its employees – including 80 apprentices.

The number of employees has now dropped to 660 and will continue to ramp down throughout 2015 – unless new projects come on stream.

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This region is experiencing high unemployment levels– having reached 8% in October 2014 (New South Wales - Unemployment Rate by Labour Force Region, Department of Employment). The majority of these job losses have come from the downturn in the coal industry so there are limited local employment opportunities for redundant employees.

The recent close of Hydro Aluminum at Kurri Kurri in the Hunter Valley is a good example of this scenario.

When this company ceased operating in September 2012 and made 330 workers redundant its closure was seen as 'best practice' in that Hydro was very proactive in supporting redundant employees in their quest to find new employment

However, Kurri Kurri Business Chamber now says less than half of the people made redundant have gained comparative employment and most are working in service industries, such as disability services, nursing homes, casual bar work and school bus driving.

The Hyrdo employees who have found work are often now moving from job to job and many have seen their incomes fall form \$100k/per annum to well under \$50k/per annum.

Conclusion

Many naval shipbuilding industry participants have supported the concept of a rolling build of naval vessels in Australia. It is firmly believed that a structured and continuous build of surface combatants and submarines will resolve many of the issues that have plagued the industry in the past.

The benefits of a robust and efficient naval shipbuilding industry range from sovereignty to economic advantages and the ability to provide effective through life support.

All are nation building and all will contribute to Australia's future prosperity and security.

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