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DEFENCE AND TRADE

TRADE SUBCOMMITTEE

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JOINT STANDING COMMITTEE ON FOREIGN AFFAIRS, DEFENCE AND TRADE

Trade Subcommittee

Thursday, 24 February 2000

Members: Senator Ferguson (*Chair*), Mr Hollis (*Deputy Chair*), Senators Bourne, Brownhill, Calvert, Chapman, Cook, Gibbs, Harradine, O'Brien, Payne, Quirke and Schacht and Fran Bailey, Mr Baird, Mr Brereton, Mr Gareth Evans, Mr Laurie Ferguson, Mr Hawker, Mr Jull, Mrs De-Anne Kelly, Mr Lieberman, Mr Martin, Mrs Moylan, Mr Nugent, Mr O'Keefe, Mr Price, Mr Prosser, Mr Pyne, Mr Snowdon, Dr Southcott and Mr Andrew Thomson

Subcommittee members: Mr Prosser (*Chair*), Mr O'Keefe (*Deputy Chair*), Senators Brownhill, Chapman, Cook, Ferguson and O'Brien and Fran Bailey, Mr Baird, Mr Hollis, Mrs De-Anne Kelly, Mrs Moylan and Mr Andrew Thomson

Senators and members in attendance: Senators Brownhill, Chapman and Fergsuon, and Mr Baird, Mr Hollis and Mr O'Keefe

Terms of reference for the inquiry:

To examine and report on Australia's expanding trade and investment relationship with the economies of South America, in particular:

- the nature of Australia's existing trade and investment relationships with the region;
- likely future trends in these relationships, including:
 - the possible impact of financial instability, particularly in Brazil, on Australia's trade and investment interests
 - likely sources of future business opportunities for Australian companies;
- the extent to which services such as transportation, banking and legal systems impact on further expansion of trade and investment linkages;
- the role of Government, particularly DFAT, Austrade and EFIC, in identifying and assisting Australian companies to capture opportunities in South America as they emerge.

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Subcommittee met at 9.01 a.m.**BOLTON, Mr George, Director, Project Financing, Export Finance and Insurance Corporation****BOYLE, Mr Michel, Director, Business Strategy and Analysis, Export Finance and Insurance Corporation****DONNELLY, Mr Roger, Chief Economist, Export Finance and Insurance Corporation****FISHWICK, Mr Stuart, Head of Credit Insurance, Export Finance and Insurance Corporation**

ACTING CHAIR (Mr O’Keefe)—I officially declare open this eighth public hearing of the Trade Subcommittee in its inquiry into Australia’s trade and investment relationship with South America, and I particularly welcome the representatives this morning from the Export, Finance and Insurance Corporation, hereafter known as EFIC by all of us. I think it is timely to state that this inquiry is relevant. It is providing us a valuable opportunity to assess how the Australia-South America trade relationship has developed and is developing. We have become aware that privatisation is an expanding trend in the region, and in some cases it has been quite radical, particularly in Chile, Peru and Argentina. Most South American governments have shown a commitment to creating stable regulatory environments aimed at attracting private capital, and these changes offer major business opportunities for Australia, and we are seeking to explore those.

Could I introduce to you gentlemen the other members of our committee. We have Senator David Brownhill, Senator Grant Chapman, and Bruce Baird, who is a House of Representatives member. They are all members of the government – the ruling party, I think they call them in some countries. Colin Hollis and I are opposition members of the House of Representatives.

We are looking forward to your evidence this morning and an opportunity to chat with you. The subcommittee prefers that all evidence is given in public, but should you at any stage wish to give evidence in private you may ask to do so and we will give consideration to that request.

Mr Boyle—Mr Chairman, thank you very much. On behalf of EFIC and my colleagues at the table, I would like to thank the committee for the opportunity to appear and to explain what we are doing in Latin America and South America in particular. I might just take a moment to introduce the people at the table here. Stuart Fishwick and his team deliver short-term credit insurance products to exporters, to banks, as well as other facilities related to bonds, bond insurance, that type of product. Roger Donnelly provides ongoing advice and analysis to the corporation on issues of political and economic risk. George Bolton works in our medium-term export finance area. His particular expertise is in the area of project finance and, in particular, political risk insurance, and the Alumbraera project is one that is noted and one that George should be patted on the back for. I will be available to answer general questions to the extent that that is necessary.

I might just make a further note that, other than the material that we have left with you, we have tried to provide as comprehensive a picture of our activities as possible. I might just note that, from a general point of view, we have been active in the region, of course, for quite a number of years, even though that profile is only for the past 3½ years, but we have a long history in the market and we note that we have ongoing capacity to take more risk in the market, and we would be happy to talk about that as well.

ACTING CHAIR—Is there anything that anybody would like to throw on the table to start the ball rolling from your point of view, or would you like to move into discussion with us?

Mr Boyle—We will just take questions, if you like, either on the material that you have about us or other issues.

Senator BROWNHILL—Could you take us through how an application process works so we have it for the record? For example, if company A wants to export to Chile or Brazil. What differences would there be between some of the countries if I wanted to export to Chile rather than Venezuela, or Paraguay rather than Brazil, or vice versa? Could you go through the process of that?

Mr Boyle—To begin I might say that, because we have two very distinct businesses, the processes are slightly different in each case. I will ask both Stuart and George to speak to the processes that they deal with, and perhaps Stuart can launch it off.

Senator BROWNHILL—And the speed of the process too, because sometimes people have been a bit critical because they miss out on a deal because of the speed of it.

Mr Fishwick—In terms of the credit insurance business, which is the area that I am responsible for, we are protecting the exporter or the bank against not being paid for goods or services they support. So in my case, the commodity trade and some services trade is usually where the risk arises and it is 180 days or less. What

happens in this situation is that the exporter finds EFIC through maybe discussions with their banker, Austrade or some of our other promotion, and they put a proposal to us of what they would like us to cover. They would nominate the counter parties overseas that they would like us to take a risk on, the level of cover and the payment terms.

We in turn then have to establish if we know those buyers. You can imagine in some countries around the world people do not show themselves too readily and we have to go and track down that information. I suppose the slowest part of the process is tracking down those people, finding their registered address and trying to see if they have the capacity and means to be able to pay. We give the exporter a quote that they accept and from that point on they come to us on a case by case basis on those buyers they would like us to take a risk on. We will give them what we call a credit limit which is the maximum amount we will pay in the way of a claim, and together we try to grow their business from that point.

We have some 1,200 clients that have that type of facility. It supports over \$6 billion worth of business a year. I think today the exposure is just under \$1 billion although it moves up and down depending upon payment terms, activity, et cetera. The criticism of time delays I think is fair, but it does relate to trying to get information about the overseas party. That is probably a thumb sketch presentation of the credit insurance business.

Senator BROWNHILL—Is there any difference between commodities? Let us say if it is a widget importer in Chile or a mining company in Brazil, is there any difference in covers?

Mr Fishwick—If you took our wool trade, typically the buyers are private individuals or private families that run a business and they look the same throughout Europe, North America, et cetera, but each industry centre represents a very different risk. You will find that the industry in the UK at the moment is on its last legs and parts of Italy are up and down in terms of where they are. If you want to sell live animals to another country, Philippines, Indonesia or into the Middle East that represents another sort of risk. So each commodity, each country, each type of exporter we help does represent a unique response that we have to provide. There is not a standard risk assessment.

Senator BROWNHILL—So you do not want to sell underbelly deer at the moment. I think a quarter of all your exposure – if that be the word to use – is in Latin America. It is 26 per cent or \$1.4 billion that is given as the amount.

Mr Fishwick—That includes the medium-term business.

Senator BROWNHILL—And 26 per cent is into South America, is that right?

Mr Fishwick—Into South America the potential maximum exposure EFIC has at the moment for the credit insurance business – the risk of not being paid for good and services shipped on terms less than 180 days – is about 10 per cent of our portfolio. It is a small amount.

Mr Boyle—The balance of that exposure that you quoted would be on the medium-term business for the larger project business.

Mr Fishwick—EFIC has got two businesses – short-term commodity trade and medium-term capital equipment purchases. So there are two types of business.

Mr Boyle—I will just make a distinction, if I may. We make a distinction between the volume of business or export supported that we support during any given period and exposure to risk that we have. That exposure will fall off as debts are repaid, et cetera. The exposure that we had at the end of last year to risk in Latin America was \$253 million. So that is the residual risk at a point in time, but over a period of time, we would have supported far more business than that.

Senator BROWNHILL—Is it harder to get cover for South America than for Europe? Is it easier to get it into Asia? Or is it just individual?

Mr Fishwick—The difference would be access to credit information about the credit standing of that particular counter party in South America. In Europe and North America, there is ready access to databases; people do have a credit profile. In Latin America, people tend not to want to disclose too much about themselves, and that is one of the big issues that we face.

Senator BROWNHILL—How does it compare then to Asia?

Mr Fishwick—Asia will give you information, but not necessarily the correct information.

Senator BROWNHILL—So your private detectives that wander around South America looking at companies and checking them out –

Mr Fishwick—We have a range of options, yes.

Senator BROWNHILL—You would have more of them in Asia than what you have in, say, Europe?

Mr Fishwick—There is more demand for our facilities in Asia than there is in South America, but we use well-recognised mercantile agencies. We use the Australian Trade Commission where necessary, which have posts in various parts of the world, to also provide us with access. We also rely upon the exporter to take some interest in knowing who they are doing business with, so we ask them to tell us about their buyers they are doing business with.

Senator BROWNHILL—We are having an inquiry into our trading opportunities with South America, so what I am trying to find out is whether it is easier to do trade – as far as the export finance insurance side of things – with South America than with Europe, or is it more difficult to do it with South America than with Asia or somewhere else?

Mr Fishwick—In credit insurance, it is easier to do business in Europe than it is in Latin America, yes.

Senator BROWNHILL—So what is the impediment and why is it more difficult to do it in South America?

Mr Fishwick—Access to reliable credit information.

Senator BROWNHILL—So that will gradually improve?

Mr Fishwick—As they open up their information, yes.

Senator BROWNHILL—Or are they, as Latins, people who do not like to divulge as much as, say, the gregarious Australians?

Mr Fishwick—It is not unique to any one country. People are very careful about what they say about themselves because there is a competitive advantage to somebody to know. So it is not unique to Latin America. All I am saying is that the information channels are not as well developed in Latin America as they are in Europe.

Senator BROWNHILL—Do you see an increasing volume of people wanting export finance insurance?

Mr Fishwick—I will comment about credit insurance. At the moment a lot of the trade that we support is a supplement to what the banks do. The banks can provide their support to the export trade into that marketplace. Where they run out of capacity to take the risk, they use EFIC to take the balance, so there are other options before they come to EFIC.

Senator BROWNHILL—What is the interest? Does it vary to every individual? What is the total cost of doing it?

Mr Fishwick—Typically, the banks will help the mineral resource sector, which represents a large volume and lower risk. The cost varies from facility to facility. It is difficult to give you an exact rate, but they are very competitive. Australian trade receivable finance is generally very competitive with overseas.

Senator BROWNHILL—You are very competitive?

Mr Fishwick—In the export finance receivable support that the banks provide, their rates are very competitive with the overseas equivalents.

Mr BAIRD—I suppose I am interested in the general potential of South America. That is what our inquiry is looking at. What is the potential? What are the specific opportunities that we should be pursuing that we are not and vice versa? What are the impediments there? This is what we are trying to pick up on. We know that you guys do an excellent job, and it really is an important part of our marketing opportunities. I notice that on page 3 of your submission you say:

South America is not a natural market for Australian companies, access can be difficult and language barriers are significant.

It does not sound like you are highly enthusiastic about the market. We want to get a flavour of that. We note that on page 8 of your submission under the heading 'Export Working Capital Guarantees and Bonds' you state:

No facilities have been established since July 1996.

Could you explain why that is and on what basis the claim of \$9.35 million was paid involving Stanlite Electronics Pty Ltd in Argentina? Put yourself in our position. Should we be putting, for example, more resources into our traditional markets rather than being spread thinly into South America? You guys are involved with it day by day. What would you be recommending to the government that we do about South America, in short?

Mr Boyle—I will first of all pick up a couple of points that you mentioned in our submission. In the first case, I would not say that we are cold on the region on the basis –

Mr BAIRD—They are your words. Page 3 of your submission says:

South America is not a natural market for Australian companies, access can be difficult and language barriers are significant.

They are your words, not mine.

Mr Boyle—Fair enough. To the extent that Australia has historic ties with Europe and fairly significant economic ties with the United States and more recently in the region of Asia, that is where the focus of the exporting community has been in recent years. These markets tend to be more natural. I guess that was the reason for the words here. Access from a physical point of view has been difficult. There have not been that many flights, and until recently access had to happen in essence through the United States through Los Angeles, which made things awkward and difficult. Beyond that, I think the language barrier probably exists in the region as well.

I think the combination of those things renders this a not so natural market for Australians. The trade flow numbers would probably show that up as well – it is one per cent of trade. There would be other evidence, but the observation that we make about exporters is that their tendency is to be larger and involved in more regions. If they are involved in South America, they also tend to be involved in other regions. It is perhaps an afterthought for them. Having grown their business, they say, ‘Let’s go to South America.’ They already have quite a lot of experience and commitment to being involved as exporters. Those are the kinds of observations that we are making here. As far as the Stanlite case is concerned, it was a case of an exporter being unable to perform a commercial contract and a case where we had provided the buyer with facilities to protect himself against the risk that the exporter would not be able to perform. Those risks came true.

Mr BAIRD—The company went under, didn’t it?

Mr Bolton—Yes.

Mr BAIRD—Generally, in relation to South America, is the risk quite a lot higher as you assess it?

Mr Donnelly—It is a crisis prone region. You cannot get away from that. It is high risk.

Mr BAIRD—High risk in terms of what?

Mr Donnelly—Country or political risk. Let us just go through what happened last year. Six economies went into recession: Brazil, Argentina, Chile, Colombia, Ecuador and Venezuela. Two had currency crises, of course: Brazil, and Ecuador in January this year, and now Ecuador is embarking on this interesting dollarisation experiment which we can go into later if you are interested. One country had a banking crisis. Ecuador again has nationalised all its banks and it has frozen its depositors’ funds. Several Argentine provinces are in arrears to their suppliers and their workers as we speak to the tune of billions of dollars. An Argentine presidential candidate last year, before the elections, was wondering aloud about a debt moratorium. Although we all, I presume, are noticing this trend towards greater commitment to democratic norms, there was a coup in Ecuador in January. It lasted only three hours. The generals bowed to pressure from Washington to restore a civilian government, but that is something else to bear in mind. High opportunities, yes, in places, but you cannot get away from the fact that it is also high risk. There is obviously a spectrum of risk there from the lower risk countries like Chile, but it goes up to what we would call grade 5 risk, which is very high indeed, very highly crisis prone countries – and not just crisis prone, a lot of them are in crisis as we speak.

Mr BAIRD—So, therefore, if you had to put your bundle of export promotion dollars somewhere it would not necessarily be in South America because of those reasons?

Mr Donnelly—Frequently where the high risks are there are also high opportunities. I am paid to worry, so I am always talking about the dark underbelly of economies. There is, of course, the other side of the coin. As business people looking at the region, they have to balance the opportunities with the risk. Often in well-regulated economies where there is a lot of competition and so forth, all of the opportunities for super normal returns have been competed away: it is in the high risk markets that the high opportunities occur. All I am suggesting is that exporters should go into the region with their eyes open because risk is high in many places.

Mr BAIRD—That is very interesting. What about this dollarisation program? Was it Ecuador?

Mr Donnelly—Yes. This is the equivalent of uncorking the anthrax against the speculators: you take away the object of their speculation. The sucre is the currency of Ecuador. It was speculated against and it forced a very large depreciation and galloping inflation. And because of currency mismatches on the balance sheets of the banks, it caused an enormous banking crisis and forced all the banks, just about, into insolvency. The banking system has been nationalised. So the previous president, the fellow who fell victim to a coup, Mr

Mahuad, said, 'We are just going to withdraw the sucres from circulation and exchange them for US dollars. So in effect we are going to become the 51st state of the United States, monetarily speaking.'

There are some pros and cons to that. It is not going to fix their banking system. It is going to mean that Alan Greenspan is going to run their monetary policy, but he is not going to be taking into mind the needs of Ecuador. But against that, of course, they had a very disorderly financial state of affairs. What having US dollars in circulation means is that they can enjoy, at some point, lower interest rates that key off US interest rates.

Mr BAIRD—So the arrangement is they would only have American dollars. They have not got their own, the sucres are not operating.

Mr Donnelly—There are some legislative and constitutional obstacles to clear at this stage. The plan has not been implemented. The new president, Mr Noboa, the fellow who came in after this three-hour coup in January, has expressed a commitment to the plan. The constitution, as I understand it, needs to be changed and legislation needs to be passed but he is talking about doing it. That is the situation in Ecuador, but again it is one of our most lowly rated countries as far as risk is concerned.

Mr BAIRD—We are told that 'ABC' is important – that is, Argentina, Brazil and Chile. I heard you talking about the problems of Argentina and Brazil. Did Brazil have rapid inflation?

Mr Donnelly—They do not have that any longer. Brazil is an economy that, of course, had their currency crisis at the beginning of last year. I think it was a delayed ricochet effect from East Asia and Russia. The good news about Brazil is that they had one quarter of fairly steep recession following their currency crisis and they have bounced back pretty well. So in fact they only briefly fell into recession last year, which has been a pleasant surprise for everyone. I think the reality is, though, that they are pretty prone to setbacks. They have very high debt – their debt to export ratio is between 400 and 500 per cent. I forget what it is precisely but, typically, alarm bells ring for those people who look at these sort of solvency and financial indicators when it goes above 200 per cent. Australia's ratio is 150 per cent. Their debt service to exports is 50 to 60 per cent. In other words, 50 to 60 per cent of their annual export earnings have to be earmarked to service debt. So when things go wrong and there is some sort of external setback, the economy can be set back. That is why we rate them as 4 on our risk scale, where 1 indicates the most creditworthy countries and 6 indicates the least creditworthy.

If I can get off the pessimism and the risks for a second, there is one opportunity in Brazil from my vantage point as an economist. It relates to a comment that I think you, Mr Deputy Chairman, made earlier that Argentina has gone a long way down the road of privatisation. Brazil has not. They have been doing some stuff in energy and telecoms, but they have a big stock of assets they want to divest and that could present opportunities. Of course, the Spanish, the Europeans and the Americans probably have the jump on the Australians, but the stock of Argentine assets that are privatisable are just about exhausted. In Brazil it is quite different.

Mr BAIRD—What about Chile's economy, as you see it in terms of your risk assessment?

Mr Donnelly—It is the jewel in the South American crown. It has a much lower foreign debt burden, more orderly public finances, quite a diversified export base and a greater application of the rule of law. These are all things that weigh quite heavily in our ratings process.

Mr BAIRD—I find this particularly interesting, Mr Deputy Chairman. Have we got much of this information? Perhaps we could ask Mr Donnelly if he could provide us with the debt to export ratios for the countries that we are looking at in particular. That would be very useful. It really comes to the core of how viable these markets are compared to some of our others. If we are going to spend a lot of money getting in there, there is certainly a high degree of risk.

ACTING CHAIR—I have made a note to ask for exactly that. That assessment that you gave us, Mr Donnelly, is new and different compared with lots of things that have been put to us. It is not necessarily contrary to what has been put to us, but it does flesh that out. I am wondering whether you might have some working papers that flesh out the general points that you have made.

Mr Donnelly—I would be happy to provide something to the committee.

ACTING CHAIR—I will not at this point cut across the questions from the other members, but I will give Mr Bolton notice that perhaps later on I will ask for his political assessment. I have no doubt that, in order to reach your risk table, Mr Bolton is doing his political assessments and you are doing the economic assessments and that is how you got it all. So I would like the matching view.

Mr Donnelly—I would like to make one final observation. There is, I suppose, an apparent disparity between my saying that certain of these countries are risky and Michel, I think, saying that we still have the capacity to cover business there. One of the ways we square that particular circle is that our exposures in a lot of these countries are fairly low already. I think there would be more capacity problems. Michel correct me if I am wrong – if we were already pretty full up on these countries – but that is not the case. Moreover, it is not a monolith in terms of risk to the continent. There are pockets of less risk and ways of managing risk. So that is how you square that particular circle.

Mr BAIRD—I understand that it is more in terms of the role of this committee. How hard we should push the South American market and put our resources into it, highlighting some of the risks involved are important for us to consider.

ACTING CHAIR—I will hand over to Senator Chapman. Perhaps he has some questions.

Senator CHAPMAN—I note your involvement with the Alumbrera mining project and particularly with regard to the political risk insurance aspect. I am just wondering what sort of things that covers. There are a couple of issues that I know have been of importance which relate to the political area in that project. The first of those was the economic stability program which gave a guaranteed tax rate to mining projects. There was some discussion recently in Argentina that that rate might change. Then there was discussion about whether the change would apply to existing projects or any of the new projects and so on. The other issue in relation to that mining project was a dispute with the provincial government over the level of royalties. Are they the sorts of things that you cover in insurance? What sort of things are you actually covering in relation to the Alumbrera project?

Mr Bolton—Political risk insurance generally provides protection to investors or lenders against losses due to three risks: expropriation, war damage or currency and inconvertibility. In the case of Alumbrera we provide that protection to the banks providing the loans to build the mine.

With respect to the two issues that you had mentioned with the economic stability program, if that program is substantially changed – this is my recollection of the transaction at the time – it would take the Congress to change that program. The whole project was awarded, built and constructed on the basis of the fiscal stability or economic stability that was given to the mining industry generally, not just Alumbrera, but the entire mining industry. The fact of life is that Alumbrera represents most of the mining industry in Argentina. If that program were to be substantially changed, it is not a clear black and white area whether that is a political risk or a commercial risk. They could increase taxes and the project could continue to operate quite profitably. It is not a political risk. If that fiscal stability was wiped out across the board and it was directed specifically against Alumbrera, there would be legitimate grounds to have it considered as a political risk. It is not a factor that at this stage I would have concerns about with respect to Alumbrera.

Regarding the royalty issue again, we – and when I say ‘we’, I mean EFIC and all of our counterparts from around the world who share the risk with us – view that strictly as a commercial risk. The amount of money involved is at the end of the day not a large amount of money.

Senator CHAPMAN—I note in relation to the information that you have about export credit agencies from other countries, you say the six largest regional markets for which data is available are Brazil, Peru, Argentina, Venezuela, Colombia and Ecuador, and then you go on to the reported exposure. You have nothing here on Chile. I just wondered why Chile does not feature in that data.

Mr Boyle—The information that we receive is provided through our membership to an organisation called the Berne Union, which is an organisation that includes 41 export credit agencies from around the world. The union members have agreed that they will share information on 64 markets. Typically those markets fall into the category of higher risk. As you heard Roger mention a few minutes ago, Chile does not fall into that category. That presumably is the reason why it was not selected in the first place. The selection of the 64 markets goes back some time. I am not sure to what extent it is reviewed and changed from time to time. I suspect not very often.

The union members have agreed that they will share information on 64 markets. Typically, those markets fall into the category of ‘higher risk’. As you heard Roger mention a few minutes ago, Chile does not fall into that category so that, presumably, is the reason why it was not selected in the first place. The selection of the 64 markets goes back some time, so I am not sure to what extent it is reviewed and changed. I suspect not very often.

Mr Donnelly—It does go back in time. For instance, at the moment it is a bit galling for me that they do not monitor Korea. They simply do not figure amongst the countries on the watch list.

Senator CHAPMAN—Talking about risk, on page 10 of your submission, the current ratings for the principal South American markets indicate that Chile is low risk. You have that graded 2. Why is Argentina up at 4? My ‘seat of the pants’ assessment would have been that Argentina would be a greater risk market than Chile but not at the same level as Peru, Bolivia or some of the others that you raise at 4. Can you perhaps enlarge on your view of Argentina and why it is rated at 4?

Mr Donnelly—Undoubtedly, it is a different economy, a stronger economy and a better managed economy than it was during the 1980s, the days of hyperinflation, the days of constant debt rescheduling, and so forth. Since President Menem came in in 1990 and introduced a convertibility plan, the currency board and the fixed exchange rate, reduced the galloping inflation to OECD norms and implemented a lot of other structural reforms, it has become a stronger economy. But the reality is still that it has a very – I emphasise ‘very’ – high external debt burden.

Its debt to exports ratio is just under 500 per cent. Its debt service ratio is 74 per cent, and this represents a very high burden on the economy and makes it very vulnerable to setbacks in commodity prices and market confidence. When your debt service ratio – in other words, the servicing of your debt – represents 74 per cent of your export income, you are not earmarking every year 74 per cent of your export income to repay that debt. What you are doing, in effect, is going to the capital markets, cap in hand and saying, ‘Can we borrow to pay interest on pre-existing debt?’ That process of servicing the debt, when the debt ratios are that high, leaves you very dependent upon market confidence. Market confidence about Latin America, in general, and Argentina, in particular, is quite skittish. It is constantly under threat of investors giving it the thumbs down and that plunging it into crisis.

Just the other week, they organised a new stand-by line of credit with the IMF of \$7 billion. These are contingency funds that they are hoping will provide them with a cushion if there is such a confidence crisis. For all of those reasons, we have them at a 4. The borderline between our 3 and our 4 broadly corresponds to what Moody’s and Standard and Poor’s would call investment grade versus speculative grade countries. Frankly, we line up quite well with what Moody’s and Standard and Poor’s do. We do not look at all eccentric in giving them a 4 when Moody’s gives them a B1 sovereign credit rating – these are long-term foreign currency ratings – and Standard and Poor’s gives them a BB. We benchmark ourselves against the ratings agencies and see whether we are out of line. According to our ratings concordance, we line up pretty well with what the ratings agencies are doing.

Senator CHAPMAN—One of the claims you had to pay was in relation to Stanlite Electronics. Can you enlarge on what went wrong there and what the problem was?

Mr Bolton—You will find that we supported Stanlite in their bid in a number of different fashions. We provided finance to a company called CTI, which was the buyer of their goods. CTI was building a mobile telephone network in Argentina at a cost of around \$US500 million to \$US700 million. We were part of the banking syndicate helping to finance that project, our involvement being based on what Stanlite was supposed to provide to the project.

At the same time, we provided some support through the working capital guarantee to help Stanlite finance its working capital requirements to fulfil this contract. It was a very large export contract for Stanlite. At that time, Stanlite was extremely active in pursuing opportunities globally and was looking at business in a number of different countries – not just Argentina but other countries in South America, although Argentina was the dominant country in that area; and also other countries in Asia.

It turned out that Stanlite did suffer some cash flow problems. As we acknowledged earlier, the company went into liquidation. At the same time there were some perceived technical problems between the interlink between the Stanlite equipment and some Hughes satellites that were being used for the system. That meant that the buyer, CTI, was reluctant to tick off on certain milestones within the contract which affected Stanlite’s cash flow because they were not being paid under their contract and it was an accumulation of a number of events. When the company went into liquidation, our export guarantee to fund their working capital was called and we paid the claim.

Mr HOLLIS—On page 11 of your submission, you state:

EFIC has taken a number of steps to position itself in the market.

Could you expand on what is a fairly general statement and give us a few practical examples of how you are positioning yourself in the market?

Mr Boyle—The number of initiatives that we have identified are things that are fairly typical for what we do, whether it is in Latin America or otherwise. As a matter of course, we continue to underwrite business in

the region and we continue to take risk. As we mentioned earlier, we have capacity to take more risk than what we have on our books at the present time.

In addition, we are, I suppose, constantly monitoring what our clients are doing and what their needs are. To the extent that we see an opportunity to modify our products to make it easier for them, then we are prepared to do so. Of course, it has to make sense for us to do it. I suppose a couple of examples of changes that we have made recently – not necessarily in the context of Latin America, but more broadly – would be the introduction of the medium-term guarantee program as well as medium-term insurance. That should be particularly useful. In fact, one of the first policies that we issued was in respect of some business in South America. It seems to have worked out for that particular region.

We are in the market periodically. We will typically be motivated by business need rather than, say, generic missionary work, but if there is an opportunity to go into a market, perhaps in association with a trade show or in association with a very specific deal, we will take that opportunity to go and meet with other players in the region and try to identify ourselves to them. In doing so, we are in a position to perhaps help our clients to position themselves with their buyers. So those are things that we do.

Mr HOLLIS—You mentioned trade shows. Have you participated in any trade shows in Latin America recently? I do not know whether what you have put here is a general statement about your role which could apply to Asia, Europe or the Americas, or whether it is a specific initiative that you take in South America. I know you participate in trade shows, but do you particularly target trade shows in South America?

Mr Bolton—Two years ago we participated in a trade show in Chile called EXPOMIN, which was related to the mining industry. We did that specifically because it was South America, we did it specifically because it was the mining industry and we did it specifically because of the opportunities that exist particularly in Peru, Chile and Argentina in relation to the mining industry. That trade show is coming up again in May of this year. We have actually made a conscious decision not to participate this year, because the time, energy and expense that we put into it two years ago has not paid off in opportunities for Australian companies to increase their exports. It was not cost productive.

Mr HOLLIS—Is that the last show you have participated in anywhere in South America – Chile two years ago?

Mr Bolton—I cannot answer that specifically, because I am not aware of other trade shows we may have attended. I did that one.

Mr HOLLIS—That is what we are interested in. It really seems to me, too, that you have hit the crux of the matter in your answer. That is a criticism we get from many people. What people are putting to us, rightly or wrongly, is that it is a long, slow process building business with South America. There are the obvious difficulties with language and distance – all sorts of things like that – and you have to build on any initiative you have shown. I am not an expert – and everyone tells us how difficult it is to do trade with South America – but one area of difficulty that most people who have come before us have identified is mining.

I am staggered when you say that you participated in a mining trade fair in Chile two years ago – great – but that you are not going to participate in the next one. That is the criticism that people are making: that we go in there with a flourish, we do something once and people never see us again. You are the risk takers, but why wouldn't we go in there and build on those contacts we made in that first show two years ago and say, 'Okay, we didn't do all that well two years ago, we didn't get that many contracts out of it, but maybe we did something wrong or maybe we did not develop this or that?' Why do we just walk away from it and maybe never go back there again? It might have been the time we would have hit the jackpot.

Mr Bolton—Can I make two comments. First of all, historically and under the basis of the EFIC act, the role of EFIC is not to be the entity that pulls exports to a particular area. We follow the exports, but that does not mean we cannot help pull. Point number two, however – and I think this is more crucial – is in relation to the mining industry. I will give you two prime examples. In the case of Alumbra, we, EFIC, and the Commonwealth government put a substantial amount of money at risk in this project, partly with the view of getting the project up and running but also partly as a way of getting additional exports of capital goods, capital services as well as consumables relating to the mining industry into the project. It was a \$US1.2 billion plus project and \$20 million in goods and services out of Australia went into the construction of that mine. Maybe another \$20 million will go into the mine. Some of it already has gone in since it started operating but very little, notwithstanding the fact that we, EFIC, and the government put a lot of money at risk.

Another prime example is a mine in Peru called Antamina. We made it very well known to the sponsors, the financiers and to everybody who would listen, including Austrade, the people who were to promote the trade out of Australia, that we were prepared to put somewhere between \$40 million and \$50 million of our capital,

our money, at risk to help that mine be developed. But our involvement was predicated on, again, capital goods and capital services coming out of Australia.

At the end of the day, we have again a mine with a capital expenditure in excess of \$US1 billion – close to \$US1.5 billion. The amount of capital goods and services going out of Australia into that mine was less than \$10 million. We did not participate because, given the size of it, there was no need to have another party playing in the financing of this mine with \$10 million on the table. We have made it very obvious and clear that we are prepared to help these exporters into the area. We cannot drag them there. We can support them once we are there but we cannot drag them in.

Senator CHAPMAN—Can I intervene and ask where the bulk of the capital goods came from for both Alumbra and the Peruvian mine?

Mr Bolton—In both cases, probably it is fair to say that roughly half of the cost of those mines was what we call ‘local cost’ – in other words costs that would be incurred in Argentina for labour, concrete and things that you cannot import. It would be the same for Antamina, which is currently under construction; it is not up and operating. A substantial portion of the capital goods came from other parts of South America, for example, Chile, which has a very well advanced mining sector. But, more importantly, a lot of it came out of Canada and the United States. It is straight south – very easy.

Senator FERGUSON—I am sorry I was late and if you have covered the area before please say so and I will read it in *Hansard*. A couple of times I have heard you use the phrase ‘we’re in the market’ when you were talking about doing business in South America. Some members of this committee will be visiting Venezuela, Ecuador and Colombia as part of the visit that is going in a couple of weeks. I see from your regional risk table that in fact the highest countries at risk are Venezuela, Ecuador and Colombia. Colombia adjoins a group of four. Would it be fair to say that if our people visit those countries it is unlikely that EFIC is ‘in the market’ in those three countries?

Mr Fishwick—My esteemed colleague, Roger Donnelly, the economist, will grade all the 200-odd countries that we put on our market grades at from one to six. Putting a number alongside that particular country does not mean we are precluded from doing business. It just means it puts us on notice. When we go into that market we take certain care in what type of transactions and what sort of risks we are prepared to take.

Senator FERGUSON—Are you interested in business in those three countries?

Mr Fishwick—We currently have exposures in those markets. We also have problems in those markets but we work through them with the exporters. It is a question of knowing the buyer – knowing the jockey – to see how you do the business. In any country in the world, we will have a look at what is being presented and see what mitigants the exporter brings to participate, to see if we can grow the business over time. We do not take reckless gambles. We take calculated risks.

Could I go back and elaborate a bit more on the question before about when we are in the market. What we are doing at the moment is we are helping people like Austrade in briefings for exporters who want to go and do business in these markets. We give them some sort of advice – some sort of scope – of what to do when you get there and what sort of risk management approach you should take. We go and see the banks who are actively involved in these markets and who have representation there. We talk to them about what we can do to help. We then talk to the major mining houses and tell them what we can do as well. We encourage them. We say, ‘Don’t miss out on an opportunity. If you want to take the plunge, think about it and what we can do – by ourselves, with the banks or a combination.’ We do not necessarily have to be in the country every moment of the day. We can certainly brief the exporters and the group of exporters here to get them equipped and give them some confidence about going overseas and doing it. The question they then have to ask is: businesswise, is it prudent for me to do this? Only they can make that call.

Senator FERGUSON—The reference before this committee is to do with improving trade with South America. We have representatives from eight different countries that have been approaching us. Some of them are quite low risk and some are quite high risk according to your table. It is very easy to talk about doing trade with Chile or Argentina because we already do, but the other countries are the ones that have put a lot of pressures on us as well to look at the opportunities they might have. Some of them are quite small economies. We have got to be careful we do not just have an inquiry talking about trade with Chile and Argentina when there are a number of other countries that are involved in the whole of the reference that we have.

Mr Donnelly—I think to understand the reality about Ecuador and Colombia at the moment you would have to look through the current difficulties their economies are going through to the medium and longer term. It is always difficult to speak in generalities, of course, but I frankly do not see that there are a lot of opportunities in Ecuador at the moment because of the severe political and economic crisis they are going

through. Venezuela has been helped a lot by the oil price rally, but again it is an economy in some disarray. Colombia, as a lot of pundits are saying, is on the edge of a political crisis.

Senator FERGUSON—They are the sorts of things we need to know. There is not much point in us putting a lot of effort into countries and unexpectedly raising their hopes about trade with us if in fact there are a lot of other factors that are going to disturb or distract us.

Mr Donnelly—It also has to be said – and it is something that we have skirted around saying – if the large licks of business were to come to us for those markets, there could be some capacity problems.

Mr Fishwick—Again, it is on a case by case basis. We look at the transaction to see who the players are and what risks we have been asked to take, and we will do the business. In Venezuela, we are helping 10 people at the moment. In Ecuador, we are helping 10. In Colombia, we are helping 11. Throughout South America, we are helping 103 exporting companies. On average, they export to two countries within that region. There are some that are better equipped. A small backyard operator here in Australia may have difficulty making representations to a company overseas, but there are some bigger exporters here with much broader representation in the marketplace that can manage the expansion of an export trade.

Senator FERGUSON—What can we read into that table about working with the banks in South America? There seemed to be a lot of activity in 1997, but since then it has been very minimal.

Mr Fishwick—There were a number of things. Banks come and go with their capacity to take risk. The payment terms, particularly with the coal business into South America and Brazil, went from 180 days to 390 days. The banks were prepared to take that if it was not in a position to take that sort of risk, given our commitment to keeping the credit terms to 180 days or less.

Senator FERGUSON—You sound like insurers. You are all being very careful.

ACTING CHAIR—It is all part of the charm.

Mr Boyle—In addition, in 1997, as far as our activities with the banks were concerned, we also signed the deal for Alumbra. That involved our providing political risk insurance to banks who were lending to the project. That is why the number is disproportionately large.

Mr Donnelly—The banks and the capital markets really do blow hot and cold on South America, particularly since the onset of this East Asian crisis and following the Russian default. When Alan Greenspan first started raising interest rates in the middle of last year, the spreads on the sovereign bonds blew out virtually overnight by 300 or 400 basis points. That is an indication of how sentiment waxes or wanes and creates opportunities or takes opportunities away from the likes of Stuart Fishwick.

Senator FERGUSON—I know opportunities wax and wane, but there are certain interests in Australia that have done reasonably well over that period of time. We had representations from people in Western Australia like WALABAI, the Western Australian Latin American Business Association, who have found a lot of markets, even niche markets, and have actually done very well. That is a group of businesses further away from South America than we are here. There are some people who have done quite well in various countries there.

ACTING CHAIR—They are generally what I would call micro-opportunities versus the sorts of proposals that you become involved in and are asked to facilitate, which are really almost on a national scale, in my view. With time winding down, I might ask a couple of questions myself and then we will do a quick round-up of the other members. It has been a very enlightening session. I have one observation before I ask a couple of questions. Mr Bolton, you gave me the impression that you are pretty disappointed in the tendering performance of the Australian capital industry servicing those opportunities. Don't be. We cannot even get them to bid for Australian mining projects. The Australian content in some of these huge resource projects in Australia is, in my view, quite pathetic. It does not surprise me to find that you set up the opportunity and got such a minimal performance out of them. Don't be too disappointed by it.

Mr Donnelly, I am looking for the long-term view. To go back to the whole landmass of North America, Mexico and Latin and South America, taking the sorts of criteria you use, such as debt-to-export ratios and things like that, how do you see the US as a yardstick for the whole scene? We are hearing that Mexico, given its access through NAFTA, is the place to be now and that, therefore, global companies are positioning themselves both in Mexico and Latin and South America to get into the US market. How are you reading that whole continent in the medium to long term and how are you developing your assessments of all that?

Mr Donnelly—Looking beyond the current noise and some of the setbacks that these economies are suffering, the overall trend since the 1990s – and it I think it is going to continue into this new century – is an upward one. There are grounds for optimism. A lot of the South American countries have put their debt crises

behind them. They have put hyperinflation behind them. They have put their proneness to military coups and all of those military upsets behind them. Democratic norms are pretty well entrenched now and that is a big sea change from the 1980s.

Mexico, certainly in terms of the way we view it and in terms of our ratings process, is benefiting from its close association with the US through NAFTA. In fact it is on our watch list. As well as grading countries, we have a watch list of countries that look prone to downgrade or upgrade. We have got Mexico at a lowish four, but on watch to be upgraded to three thanks to some sea changes that have been going on there and help from NAFTA.

It is not for me as someone who is not a businessman looking at opportunities to say, in some sort of top-down way, 'Go to Mexico. Don't go to Brazil.' It is horses for courses. Investors, exporters and business people could well find a lot of opportunities in places like Brazil. After all, it is the world's number eight economy. Let us not lose sight of that fact. There is an enormous domestic market. Mercosur provides opportunities to jump over the common tariff wall now and produce for the domestic market. I think there are opportunities there. I know I am the guy in EFIC who is paid to worry, so I am always talking about risk, but on the other side of the coin I am sure there are a lot of opportunities.

ACTING CHAIR—It seems to us there is an east-west global trading opportunity; that is, South Africa, Australia and South America. There is the potential of that global direction of trade that has not been explored very deeply and in which we have some opportunity. There is also the trade picture of the US being the great honey pot and the movement is north towards it. How do you rate the US in its debt-to-export ratios for everybody who is planning their strategies around the opportunity there? How do you rate that?

Mr Donnelly—Risk in the United States is not country risk or political risk. Like all of the OECD industrial economies, the US is rated a one. It is in the top category. In other words, it is not an economy where you are going to be tripped up by a sovereign debt rescheduling or by exchange controls that prevent your supplier converting their local currency into foreign currency to pay your invoice. It is not a country where typically a bank is going to fail and dishonour its letter of credit obligation because of some sort of systemic banking crisis. On all of those scores, the US gets high marks and that is what I am involved in, rating the sovereign, the political and the country risk.

However, Stuart will tell you that you still have to keep your eyes open in the US market, because the commercial risk – the risk of your buyer going bankrupt, doing a moonlight flit or whatever – is pretty high there. In fact, our claims people pay out quite big claims for those sorts of reasons. That is one observation I would make about the US. The other observation is that, because it is such a such well-managed and open economy, often the opportunities are not as big there. They have all been competed away; all you can make is a normal rate of return on your capital. Almost by definition – with a hurdle rate of return on capital in Ecuador at 30 per cent or something – anything you are going into will make 40 or 50 per cent. I travel to Port Moresby periodically and it always strikes me that, although a lot of businesses can be sideswiped by all of the political and economic instability that goes on up there, those who manage to avoid being sideswiped are actually sitting on some nice little earners, as you would expect. Again, the US economy is low risk, but in some cases there is lower opportunity. It is a place where there is risk, but it is commercial risk.

Mr Fishwick—Typically, most of our claims are paid in developed countries. The political claims we do have in the credit insurance business are few and far between but when they do occur, they are usually large. But typically in the United States, they have laws which enable a company to go into chapter 11 court protection for two years, come out and maybe even go back in again, and keep doing that until the creditors give up. So it is a very different sort of scenario. But, again going into Venezuela or Colombia, the same reality exists. Companies do refuse to take delivery of goods that were exported to them. They do go insolvent and, in some cases, they just do not pay for what they get. That is a reality that exporters have to be aware of and be prepared for. For that reason, they really have to get to know who they are doing business with.

ACTING CHAIR—Picking up on the point Mr Hollis was making before, if we are to recommend to Australian business that they look to more opportunities in this field, given the facilitation role and the expertise you have, are you available – as you mentioned through the links with Austrade and elsewhere – to the micro and smallish SMEs who need this kind of advice? Are they going to meet you and walk away saying, 'We'll forget about that'? Or are they going to meet you and be given some encouragement to do it, but keep their eyes open for this or that?

Mr Fishwick—The majority of our clients are considered small; not small to large. A few of our clients would dominate 80 per cent of our volume, but we have a large number of clients that are considered very small – somebody with less than \$10 million annual sales a year domestically or export. They come to us. We

give them as much advice as we can. They have access to the country rating system and some market watch information that we circulate via a web site to those clients that register.

Senator BROWNHILL—The advice is that, if you cannot get cover with EFIC, you are better not to touch it. I think you research things pretty well and, if you will not give cover, there is a pretty good reason why you might be better not to deal with that particular company.

Mr Boyle—Mr Acting Chairman, you raised the notion earlier of the flow of trade between South Africa, Australia and South America. This is indicative from our point of view of the kind of business that we look at. If you look at page 7 of the submission, there is a table that identifies the values of the indications of interest that we provide on our medium-term business. Unlike the short-term credit insurance business, the medium-term business is something that we find out about relatively early in the commercial process. Exporters will either want to or have a need to provide a technical and commercial, as well as a financial, solution to their buyer. So we find out relatively early where the business is. If you look at the six months to the end of December 1999 you can see where the demand for letters of interest on the medium term side, capital goods and capital services is coming from: Asia, the Pacific and, to a very limited extent, South America. That might help. This is just a snapshot and it is from our point of view. We are not covering the whole market by any stretch of the imagination, but that is what we are seeing for our relatively high risk part of the market.

ACTING CHAIR—It is a huge fall away from your 1999 figure to your 2000 figure.

Mr Boyle—Keep it in mind that that is only six months.

ACTING CHAIR—Have you got a feel for why the fall away is?

Mr Bolton—I will have the specifics here, but a large chunk of that \$300-odd million will relate to high speed catamarans transactions. Ultimately, we did support one or two of them.

ACTING CHAIR—As distinct from an Incat, or is that an Incat?

Mr Bolton—It would be an Incat or an Austal.

ACTING CHAIR—I think I read that you had staked about seven Incats so far into the region. Have they all gone okay?

Mr Bolton—Yes. Sometimes some of our people stay awake a little longer than necessary but, by and large, okay.

ACTING CHAIR—Developing from the things you have been talking about, there are specific business experiences, specific companies and there are more details – as you said, you have the information with you – behind some of the general observations you have made. I am wondering whether Jane Vincent, the committee secretary, could perhaps be in touch with you later so that you can provide some more of that detail for us on the understanding that it is business-in-confidence information. I think it will give us a much better briefing. We are going to visit the region in two or three weeks time, so it would be very useful if you would not mind doing that.

Mr Boyle—If you would like to direct some questions to me I would be delighted to see what we can provide.

ACTING CHAIR—Is there anything that you would like to throw in as a final comment?

Mr Boyle—No, other than thanking you for the opportunity to appear. We hope that our answers have been helpful. If you have additional questions that might come up later on either before your trip or after your trip feel free to contact us and we will see what we can do to provide whatever information we can.

ACTING CHAIR—On behalf of the committee I would like to thank you, gentlemen. It has been very enlightening and it has given us another perspective, and we needed it. Thank you.

[10.20 a.m.]

WEEMAES, Mr Warwick Eduard (Private capacity)

ACTING CHAIR—Welcome. The subcommittee prefers that all evidence be given in public, but should you at any stage wish to give evidence in private you may ask to do so and the subcommittee will give consideration to your request. Would you like to make any opening statement?

Mr Weemaes—Yes, thank you very much. As you know, I have not made a written submission to the committee, but I am extremely happy that you have asked me to appear because I think there are opportunities for Australian business in Latin America. I am a consultant. I guess you would call me an SME. My job is to identify and develop business opportunities in Latin America, with a particular focus on Argentina. I also come with a perspective of having been a public servant, serving as ambassador in the region to Brazil and Argentina, with accreditations to Peru, Uruguay and Paraguay.

Apart from the major commodity type exports, which have been traditional, Australia has opportunities in the areas of services, systems and innovative manufactures. If you look at Argentina, for example, you can see that there is a theme running through what the Australian companies there now, which are the new entrants in the field, do. P&O is there basically with a system with logistics; two Australian cinema companies are there, once again with systems with know-how; HIH is there with workers compensation insurance, which is once again a system; Prime Television is there, once again with a system. You could probably say that our mining investment there is, once again, a demonstration that Australian developed systems are applicable. And an area I have had something specific to do with – the health area – is one more illustration of that. All of that shows that there are things and systems developed in Australia which are applicable to Latin America and successfully exportable. So I would think that, if there are any Australian exporters already in the field, they should have a look at South America. They may or may not find a market, but at least they should look at it.

On the question of the role of government, I believe very strongly that government, along with business and other actors, has a very important role to play. If I could summarise that, I would say that the first element is the overall bilateral relations framework. People often tend to be sceptical about that, but I believe it does count. In countries such as Argentina, Brazil, Chile and Uruguay, for example, our Cairns Group relationship is an important backdrop for a general attitude about and image of Australia. The fact that the government deals with those and other governments over a wide range of fields makes it easier for business. That is in the general sense.

There is another obvious role, which is raising awareness in those markets of what Australia has to offer as an exporter and also raising awareness within Australia that there are prospects in Latin America. Business is done by business but my impression is that, for example, a lot of the publicity and the lead which was given by government in relation to Asia did encourage business to look at the Asian market. Although Latin America is far from being Asia, I think that sort of profile from government does assist.

Then there is the question of information which the government can provide to the public and private sectors. I remember when I was ambassador in The Netherlands I visited the Dutch archives and was interested to see that, up until the Napoleonic invasion, all Dutch diplomatic reports were unclassified and were distributed automatically to the chambers of commerce around the country. The government's attitude apparently was that diplomacy was very much to do with commerce and information was valuable to commercial sources. I think, from my observation, the Australian government system is doing that and doing a good job.

Finally – and this should not be underrated in any way – the government can help specific business efforts. In two areas that I have had personal knowledge of and involvement in – for example, the interest in exporting Australian plastic note technology and the successful bid for a health consultancy in Argentina's principal university hospital – the fact that the Australian government was seen to be behind the projects was, I think, quite a helpful factor. I should mention that on both of those occasions the Minister for Trade gave specific assistance both in talking to ministers and, in the hospitals project, making a speech in Argentina about Australia's capacity in the health field. Thank you, Mr Chairman. If there are questions, I would be very happy to answer them.

ACTING CHAIR—Thank you, Mr Weemaes.

Mr BAIRD—Yes. Thanks very much for your input. These guys seem to know you personally, which I have not had the opportunity to do. Where else have you been as ambassador?

Mr Weemaes—My last post was as ambassador in Argentina. Before that I was ambassador in Saudi Arabia accredited to all the Arabian peninsula countries. Before that I was ambassador in the Netherlands. Prior to that I was ambassador in Brazil accredited to Peru.

Mr BAIRD—I suppose the time in The Netherlands is a good reference point. One of the things catalysed by the comments that were provided by EFIC is the degree of risk, et cetera. It keeps occurring to me in terms of this inquiry that we have a small amount of trade which, considering the volatility of the markets, is good work that we have. But in terms of getting benefits from the market, are we really better to concentrate on our existing markets?

One of the reasons this influences me is that I had a few years involvement in the tourism industry. There were examples of different states doing different things. Some wanted to be all things to all people and spread their resources thinly around the world. They seemed to have lagged behind. Others have said, 'We are going to concentrate on these markets and put our resource into them,' and it seems to have paid off. Given your experience both in Europe and South America, should we be decreasing our resources in South America and putting them where there are better opportunities elsewhere, staying where they are at the moment, or increasing them because of the opportunities that are not being taken advantage of as you would see them?

Mr Weemaes—It is the sixty-four dollar question. I do not believe I can give you the sixty-four dollar answer. I agree that logically you should place your efforts where you are most likely to get returns. But I suppose it is also true that you can get incremental returns in other areas which surprise you and which are welcome. For example, looking at the export of Australian plastic note technology, I believe they will be looking at a number of non-mainstream markets because they see opportunities there. Looking at the health consultancy area, I believe the group that got together to go for and execute that contract found an opportunity which was valuable.

ACTING CHAIR—Probably the final comment made by the EFIC people – and I noticed you sitting in the gallery listening – was about whether you will you get paid. Regarding the sorts of businesses you have been developing, which have been in the services field, how have you felt about recommending to your clients: 'This is worth a run and I am confident we will get paid'? How have you made that judgment?

Mr Weemaes—Essentially we went into it on the understanding that we were reasonably sure we would get paid. But I have to say that we nevertheless needed to put in a lot of effort to make sure that we were paid.

Senator FERGUSON—How enthusiastic are South American businesses to do trade with Australia or to allow Australian investment to become involved in South American business? I ask that because I wonder what have we got to offer as Australians that they cannot get from other countries that are closer, that have had traditional closer links with them, that offer the same price or are cheaper or that offer more opportunities for investment. What is it that is attractive about Australia that would make them want to do business with Australia, or Australians to do business with South America, unless there is a good investment opportunity? It is all right for the ambassadors to say how keen they are for us to go and do business with South America, but that is part of their job in Australia. What we really need to know is how keen the actual business people are to do business with Australia.

Mr Weemaes—Just as here people would not normally think of Latin America, over there people would not normally think of Australia; their principal focus would be North America, Europe or Asia. That having been said, we do have a certain image there and in the areas that I am familiar with we have won business because we have had high quality and better product and we have been price competitive. In a way, we are seen as non-threatening. We come from a country which they believe is of similar economic size to them and perhaps with a similar economic history and therefore that is a positive thing. But in the end you have to interest the client in what you have to offer and the client will only buy what you have to offer if it is good and competitive. From what I know of Australian business in Latin America and the companies that have put in submissions, all of them have had product which is competitive.

Senator FERGUSON—If that is the case, the answer to Mr Baird's first question really might be that perhaps we need more resources to make people aware of what we do have to offer. Mr Baird's question was whether we have enough resources, too much or not enough. If in your opinion there is a product that we have to offer which is price competitive, of better quality and attractive for a lot of other reasons, then maybe we are not making them aware enough in a strong enough manner of the products that we have to offer.

Mr Weemaes—I guess this is an issue of government resources, business resources and the question Mr Baird put, which really is the sixty-four dollar question, as to where both should put their resources. I do not think there is a clear answer.

Senator FERGUSON—But we had a situation where EFIC said that they were going to have their exposure in South America by attending trade fairs. They went to one two years ago and it was a mining fair when in most cases mining companies are big enough to be able to do their own promotion. It would appear as though it might be better if somebody were to attend a trade fair where we were looking at more of the microbusinesses that Mr O’Keefe was talking about. I do not know whether our emphasis is in the right place. That is what worries me.

Mr HOLLIS—I also wish to go back to what Mr Baird asked. You have been an ambassador in several of the countries there and also in other countries, and in your experience people must come to you as an ambassador for assistance or when they are doing business. As we had EFIC before us, what sort of role do you think that they play in assisting Australian business to gain credit in insurance? Did you have any experience of this?

Mr Weemaes—I do not have direct experience in assisting Australian business to get credit in insurance but I do believe that the ambassador, the staff and DFAT can provide valuable assistance to business. They can provide general information on the economic and political environment, which is always essential. They can facilitate access to senior levels of business and government decision makers and, in a more general way, they can in effect act as salespeople for Australia in general and for the sector from Australia in particular.

Mr HOLLIS—But that is all very general, isn’t it? We all know that. I was trying to get a little bit more out of you. We had EFIC here talking to us about their role in cover and about short-term and long-term business things. Obviously, they have to be careful although they seemed to say that they were prepared to take risks. I wondered if you could enlighten us, given your time in South America, particularly as ambassador there, and in the Argentine and Brazil and accredited to other countries; if there was a business project, for instance, that you must have had knowledge of. Given the role of EFIC, I was wondering whether they carried out a role or not in insurance, or didn’t anyone ever see you about these things?

Mr Weemaes—When I was with DFAT as an ambassador, I kept in contact with EFIC and on briefing and consultation visits I always visited EFIC. But I have to say that I had never been involved in a direct case with EFIC, so unfortunately I cannot help you on that.

ACTING CHAIR—I will ask the question in a different way. EFIC tend to need to come into the game as a last resort provider of finance when no-one will touch the deal and where an Australian business opportunity looks like it is going nowhere unless EFIC does it. Along with EFIC, comes a bit of a sense that government is behind it in one way or another. In the business opportunities that you have facilitated, have you found resistance among the financial institutions to getting involved with Latin and South American business, like the banana republic kind of imagery, or are they quite sophisticated and open about assessing the deals on a merit by merit basis?

Mr Weemaes—I have not had to face an issue of financing a project, but my general experience, both when I was with DFAT and even more particularly now that I am looking for business and trying to encourage business to look at Latin America, is that there has to be quite an education process to combat the banana republic image. You have to overcome that.

ACTING CHAIR—So in your case, if you have identified an opportunity, and you are looking for a provider for it, is the difficulty in getting the provider interested, or once the provider is interested, in getting the financing interested?

Mr Weemaes—The first difficulty is to get the provider interested and that can be quite difficult. For example, in this hospital project, in the end those that were involved were very satisfied with the project and the outcome although initially sceptical.

ACTING CHAIR—And they would now want to continue to tender for further business of that kind in South America.

Mr Weemaes—Certainly.

Senator FERGUSON—You have been asked the question about EFIC and the role that they might play. I guess one of the real questions is that, during your time as ambassador, how many projects, companies or businesses either ran into defaults or actually were involved in businesses that failed? Because if there was a risk there, generally it is because somebody has failed or credit has been withdrawn or they have not been paid, or some of those issues. As ambassador, if things like that happened in either Brazil or Argentina, you surely would have known if they had Australian connections. What was the rate of lack of success?

Mr Weemaes—Forgive me; I am trying to recall.

Senator FERGUSON—No, that is all right. It is hardly a fair question off the cuff.

Mr Weemaes—Nothing initially jumps out at me as such a case. I am certainly aware of companies that had experienced difficulties with late reimbursement of taxation – difficulties with getting payment. But they were seen as the normal operational factors in Brazil and Argentina. I cannot remember a business that failed during my time.

Senator FERGUSON—You cannot remember any business failures?

Mr Weemaes—I would not want to make an affirmation that there were not, but I cannot recall any.

Senator FERGUSON—In your current role as a consultant, do you detect any reluctance of Australian companies to want to do business in South America?

Mr Weemaes—Certainly, there is an image problem. There is the problem that Mr Baird mentioned of companies concentrating on markets they know, and easier markets, and the question is: why should we try an unknown or something which seems to us to be difficult or tricky?

Senator FERGUSON—It seems to us that, apart from mining, where you actually have to go to where the resources are, you have not got much choice unless there are options in various places in the world. Apart from mining, there seems to be some difficulty. We might hear from other witnesses that it is not.

Mr Weemaes—The difficulty is a difficulty in perception and attitude towards Latin America on the part of Australian business. I would argue that Australian business has gone into a number of difficult, tricky and unfamiliar markets around the world and has done so as, first-up, an adventure. Asia, at one stage, was considered extremely exotic and difficult. The Middle East was always thought to be a difficult market. Yet these are now considered as normal markets.

ACTING CHAIR—So why is there reluctance? Is it a mixture of political instability and economic instability? Is it the mixture of both that makes them reluctant, or just an unknown of the market?

Mr Weemaes—I would say that, firstly, it is a misguided perception that these are unstable, banana republic type places. Secondly, it is a lack of awareness of what those markets are really like – their sophistication, the opportunities that are there, the size of the markets and the fact that it is possible for an Australian company to do successful business there. During my time as ambassador in both Argentina and Brazil, I continued to hear, from Australian business representatives who were there and doing business, this very point: that people in Australia were timid. These businesses had proved that it was a rewarding market and that the government should be doing more to get this message across.

ACTING CHAIR—Is there a distinction to be drawn between Australian businesses that are simply exporters of goods or services – in other words, that are just marketing goods and services – and those that, because of the nature of the business, have to invest in the South American country? Senator Ferguson mentioned the mining industry as an example where, because the resource is there, it is an investment activity rather than simply a marketing activity. I know there is some involvement in primary industry in Argentina on the part of some Australian investors. I am talking about those sorts of things. Is there a distinction to be drawn there as to which is harder and in which area there is more interest on the part of Australian business, from your experience?

Mr Weemaes—My impression is that big projects are investment projects, and there is quite a range of those. For the newcomer, I think it is possible to get into those markets without making significant investment, by marketing services or manufactures which are innovative.

ACTING CHAIR—Thank you. The observations you have made are very consistent with quite a stream of submissions that have been made to us – that there is a strong role for government to play because, culturally in South America and Latin America, the role of government is significant in encouraging these trade relationships, and we need to be aware of that. Secondly, a constant theme is that there is little awareness of Australia over there, and there is little awareness of opportunities here. There has to be a breakthrough in that to create these opportunities. What you are saying – as I pick it up – is that the opportunities are particularly in skills, services and products, every bit as much as major commodity investments of one kind or another.

We have also been told quite consistently that there is a much better established business culture, albeit perhaps coming off a Spanish or Portuguese language base. But the European business culture is identical to the one that has evolved here, and we ought to understand those opportunities. They are not any more difficult than Asia was to get into, if you get the focus. I think that is a fair summary of what we have been hearing, and it is your experience too, both professionally as a diplomat and as a consultant. We are trying to pick our way through the ways in which we might report to give emphasis to those things, but what you have said has reinforced that, and I thank you for that. Is there anything you would like to say in conclusion?

Mr Weemaes—No. As I said at the beginning, I am very grateful you have asked me to come. I think that what you are doing is part of the important effort to publicise the opportunities that there can be in Latin America. But, basically, it is up to business to take them.

ACTING CHAIR—I thank you once again. You will be sent a copy of the transcript.

Proceedings suspended from 10.51 a.m. to 11.03 a.m.

O'SULLIVAN, Mr Neil Edward, Vice President, Marketing, Sales and Services, Nu-Lec Pty Ltd

ACTING CHAIR—Welcome, Mr O'Sullivan. As you know, this is the Trade Subcommittee of the federal parliament's Joint Standing Committee on Foreign Affairs, Defence and Trade. We are focusing, in particular, on investment and trade opportunities in Latin and South America. As I have already informed you informally, we prefer that all evidence be given in public, but should you at any stage wish to give evidence in private you may ask to do so and we will give consideration to that request. Do you have any comments to make on the capacity in which you appear?

Mr O'Sullivan—Nu-Lec Pty Ltd is a Brisbane based manufacturer of high voltage switch gear.

ACTING CHAIR—For the benefit of members of the committee, Mr O'Sullivan has prepared a statement that he would like to read to the committee and table for incorporation into the *Hansard*. That should then generate its own discussion with us. Mr O'Sullivan, we invite you to proceed with your statement.

Mr O'Sullivan—Thank you.

Senator BROWNHILL—I would like to make a comment, Mr O'Sullivan. If you are going to spend all the time reading that, it is not going to give us a lot of time to ask questions. Whereas, if you precis it—and it becomes part of the record if it is incorporated anyway – it will save a lot of your time and it will still go into the *Hansard*.

Senator CHAPMAN—We could take five minutes and read it more quickly than you could read it to us.

Mr O'Sullivan—Yes. Nu-Lec Pty Ltd started in 1981. We are a wholly owned Australian company and we are still a private company today. We currently export to 52 countries around the world. That has been achieved since 1992, when we first started to export. We currently successfully export, in particular, to South America – to Brazil, Argentina, Chile, Peru, Colombia and Venezuela. We make a range of products that are considered leading edge technology in the world today. They were researched and developed in Australia. The research and development was totally funded by Nu-Lec Pty Ltd, but we did get some assistance from some government research and development programs. I would like to recognise that. We first started to export in 1992 and we got some assistance, again, from federal government export market development grants. That certainly made it a lot easier for us to get into the export business.

To date, our South American business is probably considered, on a regional basis, our second strongest market behind the United Kingdom, which would be our strongest market today. There are a lot of reasons why we have been successful in South America, but the one reason we have been successful, more than any other, is that South American countries and the people in South American countries are prepared to embrace new technology far more quickly than is the case in other parts of the world. They look for new technology and they embrace it. I think that is one of the reasons why we have been successful.

I have tried to list some of the barriers which I perceive that the Australian federal government might be able to help us with. The first one is associated with Australian citizens travelling to South America. I am not sure if you are aware that if you go to the Brazilian embassy and make application for a visa to visit South America or Brazil – a business visa – and you apply to go there on a sales mission to promote your products, you are granted a visa by the Brazilian embassy. If you say that you want to go there and service your products then you are not. There is a very detailed process that requires Brazilian government application and approval from the local people that you are going to service for. I have actually attached a copy of that. In the past, we have put together programs because we actually execute supply-install types of contracts in South America. We have had deadlines to meet with local electricity utilities and have made application for visa for our service staff to go there and carry out service, installation and commissioning work, and they have been denied.

My understanding of the visa system is that much of the visa system is based on reciprocal arrangements between countries. If there is something that can be investigated there to help us get visas for not only our sales staff but also our service staff that would be of vast assistance. It is specific to Brazil. We do not have that same amount of trouble in the rest of South America.

The committee is probably well aware of duties and taxes with exporting to South America, but I would like to present a specific case here. In our particular case, we manufacture a range of high-voltage switch gear. It is used by the electricity utilities, many of which are being privatised in South America these days. There is a 19 per cent import duty to start off with. It is applied on the CIF value. After that is added, there is a five per cent industrial product tax; then there is 0.38 per cent bank tax. This is followed, depending on which area we are delivering into, a circulation merchandise tax that varies between 17 per cent, 12 per cent and seven per cent.

There is an additional three per cent federal social tax and a 0.65 per cent social security tax. All in all, our actual declared CIF value, by the time we add all the taxes, has actually been increased by 70 per cent.

Senator FERGUSON—What is CIF?

Mr O'Sullivan—CIF is cartage, insurance and freight. It is the value of the goods, including cartage, insurance and freight, when it arrives in the port in their location. Australia is certainly a member of the World Trade Organisation. We are not currently a full signatory of the GPA, and I know that does not necessarily affect South America but it does affect other parts. We are certainly discriminated against, even in the United Kingdom, because we are not a full signatory to the GPA. My understanding is that we actually fully comply but we do need some legislation changes before we can –

ACTING CHAIR—What is the GPA?

Mr O'Sullivan—There is a separate section of the World Trade Organisation called the Government Procurement Agreement, the GPA. We are not currently a full signatory to the GPA. As a result of that, Australian manufacturers exporting into some parts of the world are discriminated against against other members who are full signatories of the GPA, in particular the United States.

ACTING CHAIR—Without cutting across what you are saying here, are you talking about supplying to non-privatised government instruments that are buying from you?

Mr O'Sullivan—Where we have actually come across it – and I know I am getting off the South American scene here a little bit, but while I have a ministerial audience I would like to share some of our problems with you – is in the specific instance where the European Union purchases equipment in accordance with European Union regulations. Most of our customers are electricity utilities. Some of them are privatised; some of them are still government entities. But in all cases there is a utilities directive in the European Union which requires even the private ones to purchase their goods in accordance with the Government Procurement Agreement of the World Trade Organisation. Right now, because Australia is not a full signatory, if we have a US based competitor, they receive preferential treatment importing into Europe over the top of us. There is actually a five per cent preference applied to a US based manufacturer when we are selling into Europe because we are not a signatory to the GPA.

Senator FERGUSON—Why aren't we a signatory? Do you have any idea?

Mr O'Sullivan—Some of our embassies in Europe have actually helped us with this. My understanding is that there is currently some government purchasing legislation that needs to be changed before we can become a signatory. In fact, because of the way that our Australian government goes about its purchasing and procurement, we actually comply with the requirements, but there is a piece of legislation that has to be changed before we can sign. That is my understanding. That comes from advice from one of our embassies when they looked into it.

Senator FERGUSON—Have you ever made any request to the government to change that? Obviously, it affects your ability to tender.

Mr O'Sullivan—Yes, I have. We have certainly made requests through AusIndustry. They are following it up at the moment, but I would certainly like to highlight it here today.

Senator BROWNHILL—Mr Chairman, I agree with Senator Ferguson. I think we should follow that up.

ACTING CHAIR—We will follow that up. You have landed on the right zone with that one.

Mr O'Sullivan—Thank you very much.

Mr HOLLIS—I think we also should note that when we do follow it up we get back in contact with Mr O'Sullivan and tell him what we are doing about it.

ACTING CHAIR—Does that flow, given what you just said related to EU? Is the behaviour in South America the same in that they follow that general approach? If we were a signatory, would you be better off going into South America?

Mr O'Sullivan—I do not think it actually affects our business in South America because, as you can see, about 70 per cent of our import price is taxed. There is a 70 per cent tax in total applied with those varying taxes. Quite clearly, that is not in accordance with what the World Trade Organisation is trying to do in creating a global marketplace and removing these barriers. There are certainly enormous barriers associated with import duties and taxes that exist right now in South America.

The next item that I would like to highlight to you is company tax. The reason company taxes are an issue is that, because of the very large duties and taxes associated with importing fully assembled product, it makes perfect sense to look at local assembly. You can get significantly reduced taxes associated with local assembly.

The next thing that you then start to look at is, 'Okay, if I have a local assembly plant there and I am making profits there, what are the taxes associated with doing that?' The company tax rate is currently 34 per cent, which does not necessarily make it unattractive to set up local assembly plants there, but there is no tax treaty between Australia and Brazil or between Australia and Argentina. That is something else that I would encourage you to look at. If we developed tax treaties between those countries, it would make it more attractive for Australian industry to set up there and repatriate profits.

Language is a barrier, but clearly you have been told that several times before. We overcome that by converting everything to Portuguese and Spanish. Despite the great pain associated with getting visas and things, we tend to offer incentives, through our distributors, to bring their engineers to Australia to study at our university that we fund. They work at our factory and so we get those skills as well as their gratitude forevermore. They then go back to their markets with masters degrees and continue to promote the Nu-Lec name, which is our company name, and products. It is always very difficult to get those visas.

Mr BAIRD—Student visas or visitor visas?

Mr O'Sullivan—They are typically student visas, with a work component. They are able to do work experience in my business. We try and set them up so that they are contributing to our business quite significantly. Quite often their masters degrees are studied by thesis. We actually want them at the factory all the time and they do a thesis topic that is associated with our products and our business. That is very hard to get across to visa organisations because most of these visas limit the student working hours to 20 hours a week. They are coming here and their reward is a masters degree. The reward for us is that they learn more about our products. They become knowledgeable about our products and are grateful to us so they go back and promote our products and services in their markets. It is very difficult to get across to a visa section that that is what we are trying to do.

ACTING CHAIR—How many of those have you done?

Mr O'Sullivan—Three, so far, and on every one of them I have a file this thick associated with achieving it.

ACTING CHAIR—But you got there.

Mr O'Sullivan—Yes.

ACTING CHAIR—Has it been successful?

Mr O'Sullivan—Extremely successful.

Senator FERGUSON—But it is true that student visa requirements in most cases are that they cannot work while they are under a student visa. It is a blanket rule. It is not exceptional.

Mr O'Sullivan—Whenever you are doing business it has got to be a win-win situation, and what we are doing is creating a win-win situation. They are getting a formal qualification from an Australian university. Our universities are winning. They are winning because they go home with an Australian masters degree, and we are winning because we get their Spanish skills and their Portuguese skills and they know an enormous amount about our product by working at the factory. So we are creating a win-win situation but our current visa restrictions are making it difficult for us to achieve that.

ACTING CHAIR—That point is understood.

Mr O'Sullivan—The next one is the InterAmerican Development Bank. Australia is not a member of that bank. The InterAmerican Development Bank provides significant funding for projects in South America and because the source country for our equipment is Australia, we are discriminated against, we are not allowed to bid. We only have two competitors in the world – one is US based, the other is UK based. They can both bid for these projects but we cannot. Through the Australian Industry Group we have made previous submissions to the federal government to consider becoming a member of the InterAmerican Development Bank. Again, I would encourage you to investigate that.

The next matter is Merco Sur. You have probably heard that several times in your investigations. 'Merco' stands for merchandise and 'sur' stands for trade, so it is a merchandise trade agreement in South America. The members are Argentina, Brazil, Chile, Uruguay and Paraguay. There are absolutely no taxes whatsoever associated with trade in that zone. So again, for us to set up local manufacturing in Argentina or Brazil, immediately we are 30 per cent or 40 per cent more competitive in those other countries.

ACTING CHAIR—Are you doing that?

Mr O'Sullivan—Can I go off the record?

Senator BROWNHILL—Forget about it. Leave it for now

Mr O'Sullivan—Foreign currency is the next issue. Australia has a wonderful thing called an Australian dollar, but unfortunately in most of the world it is seen to be like monopoly money. In saying that I mean no disrespect to our currency or our policies associated with our currency.

One of the problems that we have globally is that, if we tender in Australian dollars and our competitors are tendering in some other currency – normally their currency is US dollars or British pounds – the local exchange rates, which do not necessarily reflect the world market exchange rates that are applied to the levelling or the equalisation to be able to then do an evaluation, make us uncompetitive. I believe a lot of this is associated with our banking industry and the way they trade in foreign currencies. To give you an example, if we tender in Australian dollars in Brazil and one of our competitors tenders in US dollars, when they convert them both to real, the exchange rate that is applied against ours is normally the local exchange rate that has been nominated in Brazil and the real to Australian dollar exchange rate normally does not reflect a world market value for the Australian dollar. So we are far better off tendering in US dollars so that we are actually evaluated on a level playing field.

I do not have a ready solution for this. I do not even know what I am asking you to do, but I am just trying to make you aware that quite often the Australian dollar is not a favourable currency for us to be tendering in. But, clearly, we are an Australian manufacturer, so if we tender in any other currency, there is some foreign exchange risk that we are taking.

Senator FERGUSON—The only problem is the exchange rate risk, isn't it?

Mr O'Sullivan—Which is not insignificant.

Senator FERGUSON—I understand that.

Mr O'Sullivan—The real, for instance, devalued by 50 per cent over 1999. If we are tendering in the real, there is an enormous risk there.

Senator FERGUSON—You have asked us lots of other things that we have some influence over. I am not sure that we can have too much influence over the last issue.

Mr O'Sullivan—I do not have a ready solution, but there may be some encouragement for our banking industry to look at foreign currencies, in particular the currencies in South America – being non-foreign tradeable does not help either. If we set up local manufacturing in Brazil, we will sell in real. The parts will still be made in Australia. We will send parts in. So we have Australian costs associated with manufacturing those parts. We are tendering in real. If we went to our bank, which is actually technically impossible, and tried to get forward cover on real or forward sell real at a guaranteed Australian dollar exchange rate, we cannot do that. However, US banks can. US banks will do that. So our US competitors have an advantage over us there.

Certainly, since the significant devaluation of the real, specifically in Brazil, most contracts are now written in US dollars anyway. No-one will touch real right now. Prior to the devaluation, a lot of companies – particularly our customers, the electricity utilities, because their revenue is in real – sell their electricity and they get paid in real, so they want to write contracts in real. In the past it was difficult to get a contract in anything else except real. Today, it is the accepted norm that all contracts are in US dollars.

In my front statement, I actually talked about a company called Light. Light is the electricity utility for Rio de Janeiro. We have actually become quite famous in Light. They were fined severely by the regulator a few years ago, so they contracted us to put an automation system in for the whole of Rio, particularly Copacabana Beach and places like that where they wanted to make sure that the electricity supply was very reliable. We actually took their minutes of supply from 40 minutes – which is a measure of how continuous the supply is in the industry – down to three minutes. It is a significant improvement. We actually had that contract in real, but we got an exchange rate variation towards the end of it to conclude it. I was there last month. We have just signed a new contract to extend this system and we signed that in US dollars. For the first one, they would not entertain anything except real; the second one, we would not entertain anything except US dollars but, because of our reputation and the fact that they wanted us, we were able to do that.

Senator BROWNHILL—Can I just make a point here. Most of those currency fluctuations are something that you as a business will hedge two ways. Most of the trade is done in American dollars, so you will just hedge in American dollars. If they want you to go into real, you then have to do a double hedge, I guess.

Mr O'Sullivan—You can hedge real against the US dollar locally, but with the banking industry there, there is normally quite a large cost associated with doing that.

Senator BROWNHILL—I think Senator Ferguson made the point that something that can be done with the InterAmerican Development Bank situation and the visas. I think that, as far as those hedges are concerned, it is a detriment to trade with South America, but it is something that I do not think we can handle.

Senator CHAPMAN—It is a consequence of the current relatively low level of trade, isn't it? If there were a high level of trade, then you would have more interchangeability between real and Australian dollars directly.

Mr O'Sullivan—Yes.

ACTING CHAIR—Assuming that you are doing this business profitably and very successfully, despite all these barriers and despite having to, in effect, double hedge your currency estimates, it is all going very nicely. So move on.

Senator FERGUSON—Did you use the people that you have had out here – the guys that you brought out here as students – or who do you use? You said language is a barrier, but it does not seem to have been much of barrier if you do not speak Portuguese.

Mr O'Sullivan—My personal responsibility is a global responsibility for the company, so I cannot speak every language that we trade in. What we do is we look for distributors that have English language skills and they generally act as our interpreters locally. Personally, I have spent a lot of time in South America, so I have picked up some of it, but I do not speak it fluently.

Senator FERGUSON—Then language is not the barrier that you say it is if a company like yours can trade successfully. It might be more of a barrier to people who are trying to actually start up without any contacts, but language is not the barrier that I perceived it might be in your instance.

Mr O'Sullivan—Provided you develop a discipline associated with using an interpreter. I have a very quick story. In one of our first export markets, Vietnam, I was explaining the impulse integrity of our device. They actually go out on electricity poles. Quite often the electricity network is the highest thing in the area and, therefore, it is most susceptible to lightning. I was explaining in English all of the lightning impulse integrity that is built into our equipment to withstand these lightning strikes. It was actually interpreted as, 'The Nu-Lec is so strong it can withstand a typhoon.' So interpretation is a barrier. Typically, you will only ever get 70 per cent right. You have to understand the limitations on your interpreter and you have to work within those limitations. You also have to demand that private conversations do not go on. At the start of a meeting I say, 'I am sorry; I do not speak your language. This is my interpreter. They will interpret everything that is said.' Provided you can control the room so that you do not end up with private conversations going on in other languages and you get them into the discipline that everything everyone says get interpreted, then you can effectively do business, I believe. There is a real skill to develop there to be able to do that.

Senator FERGUSON—Your real danger is when the guy that is getting things interpreted actually understands your English but you do not understand any of his language. That is the real danger.

Mr O'Sullivan—The Australian accent is not readily recognised. Most people that do speak English speak it with more a US based type accent. You have to be aware of that. Certainly, when you are in those sorts of countries, slowing down what you are saying and speaking with as much clear diction as possible is also necessary.

Senator BROWNHILL—The other thing is having a technical knowledge of what they are talking about too. Because if you have an interpreter that does not have any technical knowledge of what they are talking about –

Senator FERGUSON—You get typhoons.

Mr O'Sullivan—Yes, exactly. The very last item that I had on my list is government to government. We are very lucky in Australia. We do not necessarily have any natural enemies or natural rivals. Globally we are recognised as a nation that does not have anyone that does not want to trade with us for past historical reasons, and we are very lucky like that. Unfortunately, in the majority of countries around the world, we are known for our lovely beaches and our kangaroos, not necessarily our technology. There is an enormous amount of technology that is developed in Australia, particularly in our case. We have more than eight world patents on our product range now and it is considered leading edge technology in the world today. It is the best there is in our industry and that is why we continue to be extremely successful in our export ventures. Government to government promotion of our technology – and not only our tourism – is another thing that I would encourage you to consider.

Senator BROWNHILL—How can you not afford to set up your business in one of those countries and be a part of Merco Sur? That is really the first question, by the way.

Mr O'Sullivan—Yes. In order to increase our level of competitiveness, it is basically mandatory.

ACTING CHAIR—We all have to face facts that in every developing country and now in modern countries, the government is always under pressure to try to get as much done at home as it can. As your

relationship evolves there, joint ventures and local manufacture work backwards and forwards at both ends of the spectrum. That will obviously be your corporate plan, and should be.

Mr O'Sullivan—Yes. There is always a lot of local value adding with our product anyway. It goes out on the pole and connects back to a central computer system to control and monitor the network and reconfigure it when there are faults. There is a lot of local value adding with communications companies. Most of our distributors have skills in what we call integration capability. There is already a lot of local value adding and in order to ensure that we maintain our competitiveness, it is important that we try to eliminate some of those taxes. From a government to government point of view, if and when South American countries become part of the world trade and we can start to get those barriers reduced, that would be good, too.

Senator FERGUSON—I have a question particularly on your last paragraph about government to government activity. I asked Mr Williams who was here before – and you might not have been here when he answered – why do people want to do business with us? What is there about Australia that would attract them to do business with us, rather than the United States or the United Kingdom? I notice in your last paragraph you said:

... most countries in South America are eager to do business with us.

Is that only the reaction because of your company's involvement in a particular industry sector, or do you through your visits there believe that South American business people, governments and others are actually eager to do business with us?

Mr O'Sullivan—I believe so. This not only applies to South America, but Central America and the rest of the world. Australia is really in my opinion – and I am widely travelled – considered a very friendly nation. We have no natural enemy. In South America in particular, not everyone in South America looks favourably on North America. There is a lot of historical reason why that is the case. There is no history here in Australia; we do not have any history with any of the South American nations as to why there would be grudges held or why they would not want to trade with us. Absolutely. I consider it a distinct advantage to be an Australian manufacturer trying to take our products globally for that reason.

Senator FERGUSON—When did your company, Nu-Lec, start?

Mr O'Sullivan—We were founded in 1981.

Senator FERGUSON—And you are now employing 200 people and have distributors in 34 countries?

Mr O'Sullivan—We actually have product and service in 52 countries. We have our own offices in the United States, United Kingdom and South Africa. Our corporate office and factories are in Brisbane. I think those figures you gave are a little bit out of date. We have 200-plus people at the factory in Australia as well as the employees around the world.

Senator FERGUSON—It is a pretty big move in seven years, isn't it?

Mr O'Sullivan—Yes. We were actually founded in 1981, so we are almost 20 years old, but our export business started in 1992.

Senator FERGUSON—You have raised a lot of issues that are important to this inquiry² because you have got some practical history and dealings with South America. It is different to talking to departmental officials or others that are not actually involved. You have given us some good information. Thank you.

Senator BROWNHILL—Carrying on from what Senator Ferguson said, what could you advise people who want to trade with South America to do? Or have you just been successful because you have got a niche market product?

Mr O'Sullivan—We are successful because we get focused and we solve the problems. Every market has a different barrier. You get in there and solve those problems rather than say, 'That is all too hard'. You get in and find a way. With the visas, we end up with files this thick. There are the people who are here studying. Some other people might have given up before that.

Mr BAIRD—Visas which way – into Australia or going into South America?

Mr O'Sullivan—The people coming here. The ones going the other way as well are just as difficult.

ACTING CHAIR—Predominantly you are talking about that student's masters visa?

Mr O'Sullivan—Yes. Getting our service staff into Brazil requires an enormous process. We have to have the end user that we have sold to make application to the government to get our staff visas to go there and assist them with training and service work. Again there is a large process that other people might give up. We just do not in any market. That is why we continue to be successful.

Senator BROWNHILL—You have got a good product. It is a niche product. It is high tech, close to the cutting edge product and you are in the top three of the world. We cannot even discuss that side of it. You are obviously a pretty smart company. You have said that you are persistent. You obviously do not leave a stone unturned and you knock down a door if you cannot find the key to it; is that right?

Mr O'Sullivan—That is basically it. We probably unscrew it off its hinges rather than knock it down.

Mr BAIRD—I notice you have got an exclusive agent in South America. Has that been an important factor?

Mr O'Sullivan—I think exclusive distributorships are the only way to go. You have got to show them loyalty and they will show you loyalty.

Senator BROWNHILL—Have you used the Export Market Development Grant and EFIC? Any good? Any problems?

Mr O'Sullivan—We have used the Export Market Development Grant very effectively. I think we are deemed to be big enough and successful enough to stand on our own two feet now. That is fine, too. I will tell you a very quick story on that. As I mentioned before, Vietnam was one of our first markets that we had to go to. Particularly marketing in Asia, typically you drop about \$US10,000 per person per week on air fares, accommodation and local in-market costs. For us, back in 1992, that was an enormous amount of money. Our president and I got on an aeroplane and went to Vietnam. We took \$US30,000 cash with us because there was no credit cards or anything else that could be used in Vietnam at that time. We had that strapped around us under our seat. That was an enormous amount of money. We did presentations to all three-power companies there and we had no idea whether we were going to be successful or not. The Export Market Development Grant made that possible. We probably would not have done that without the Export Market Development Grant. As a result of those visits, less than two months later we signed contracts for \$US2 million. That was our second export market ever. I would really encourage the Export Market Development Grant to continue because it certainly was one of the major reasons for our success.

Together with that are the research and development grants that have also been provided to us. We can spend up to \$20,000 or \$30,000 a day in laboratories around the world to type test our equipment. There is a set of Australian standards, which you would be aware of. There are also what are called 'ANSI' standards, which are American standards, and 'IEC' standards, which are the European standards. We have to go to independent laboratories and type test our equipment to prove that it is capable of meeting those standards, and that can cost \$20,000 or \$30,000 a day. There are only two or three laboratories in the world that are capable of doing it, and the research and development grants, again, helped us initially to get our products over there to get them type tested so that we could put them on the world market stage. We have never used EFIC successfully. I have tried to on several occasions, but we have not been able to use them successfully, to date.

Senator BROWNHILL—What was the barrier? The cost?

Mr O'Sullivan—I think EFIC thought it was a good deal. We had one particular case in Malaysia where we were awarded a contract for several million dollars. Between the time that we were awarded it – actually, our local distributor was awarded it, and they did not take exchange cover – and the time that the letter of credit was raised, the Malaysian ringgit dropped significantly during the Asian crisis period. So our distributor had a contract in Malaysian ringgit, had a contract with us in Australian dollars, did not have exchange rate cover and could not afford to raise an LC on us in Australian dollars, because it would have cost them money to execute the contract. So I tried to get EFIC involved and to go directly to the end user – T&B, the utility – to do a deal and just could not put it together.

Senator BROWNHILL—So EFIC has not been of use to you, but it is not for lack of trying?

Mr O'Sullivan—It is not for lack of trying. We did not get it together then. I think EFIC provide a useful service, we just have not been able to get it together with them yet.

Senator CHAPMAN—On a global stage, how many competitors do you have? Is your product relatively limited in terms of the number of people that produce it?

Mr O'Sullivan—Yes, it is. There are two major competitors; there are basically six in total.

Senator CHAPMAN—Would you be the only Australian?

Mr O'Sullivan—We are the only Australian manufacturer. We are the only manufacturer in the Southern Hemisphere.

ACTING CHAIR—Do you have a strong domestic market?

Mr O'Sullivan—We have about 90 per cent of the domestic market, and it was from that base that we started to export.

Senator CHAPMAN—I am just trying to get a feel for how important your product was, in terms of your capacity to penetrate South America, as distinct from how important your marketing effort was. Can you give us a feel for that?

Mr O'Sullivan—They both factor – and you will notice my title is 'Marketing, Sales and Service', so I may give you a biased opinion. They are both very important. If our research and development manager were here, he would tell you it was features and functionality, and I will tell you it was marketing effort, but you cannot do it without both.

ACTING CHAIR—With all three?

Mr O'Sullivan—Yes.

Mr BAIRD—Was the fact that you have 90 per cent of the Australian market a significant help in penetrating the South American market?

Mr O'Sullivan—Absolutely. Australian electricity utilities are world-class. When you look at benchmark figures that are more and more readily available these days with the privatisation of the industry, Australia is always right up there. For us to be the supplier to those utilities, allowing them to achieve that, is recognised globally. There is no doubt about it.

Mr HOLLIS—More generally about doing business in South America, you obviously carried out market research. There was some reason you went there. What sort of assistance did you get or did you need from the Australian officials there? For example, did you make contact with Austrade or our embassies? Were they able to assist you? Were they able to recommend interpreters?

Mr O'Sullivan—I think Austrade plays a very good role until you have actually established your own structure in the market. For instance, if we are trying to go to a new market, we may place some local advertising to attract potential distributors, they make application and there is a survey that we give them. Then rather than our expending the cost and the resources associated with going around and looking at everyone of them, we will often pay Austrade or contract Austrade to go and visit those organisations to make sure they are real, and it gives us an in-market report of those distributors and we will then short-list them. At that point Austrade is not going to help you close business; you have got to go and do that yourself and, provided you recognise that and use it for the service that, I believe, it is very useful for, it does a good job doing that. Austrade used to actually do it very economically but it is becoming more and more cost conscious all the time so we tend to pay for it these days – but, again, it is worth it.

Mr HOLLIS—But you reckon that the intelligence gathering and assisting that they do is value for money?

Mr O'Sullivan—Yes, it is, provided you give them a clear brief on what you want. You cannot expect them to be an expert in your industry.

Mr HOLLIS—Did you deal with only Austrade? You did not deal with the ambassadors or anyone like that? You did not go through the missions; you just went through Austrade?

Mr O'Sullivan—I have in the past used ambassadors at a high level to help us. Certainly, for this GPA that I was mentioning before, some of the European ambassadors helped us there. They actually wrote letters to the utilities and asked them to stop discriminating against us, so that helped. So we have used ambassadors for that role.

Mr HOLLIS—How did you latch on to South America? Did you get an inkling? Was it in a trade journal or did they approach you or you approach them?

Mr O'Sullivan—Our first contact with South America was at a conference in Los Angeles, and we developed the relationship.

Senator FERGUSON—You were in other countries before you went to South America?

Mr O'Sullivan—Yes. We were in North America before we went to South America.

Mr HOLLIS—Just on a general overview of, say, South America, what do you think the potential for trade between Australia and South America is? Is it always going to be a niche market, or is there a general market there? You have been successful. What do you think are the handicaps or the shortcomings of Australians doing business there? If I can hit you with a third one: is it worth the effort? One of the things that has been put to us is that Asia is so close and we have broken into Asia. This is a difficult market: is it worth the effort?

Mr O'Sullivan—I think each business has got to do its own analysis of that. Market prices around the world vary dramatically from country to country for any particular commodity. The thing that I would

recognise is that the way that people live in South America is very similar to the way we live. The food they eat is very similar; the clothes that they wear are very similar; our climates are very similar; lifestyles are very similar. There is an enormous affinity between the commodities, goods and services that we are using, and the goods and services that are used in those countries. So clearly, there must be a market there for our local manufacturers in just about all areas for that reason.

From a market price point of view, it is my experience that the market price there for the majority of things is not vastly different from the market price in Australia. Clearly, there are all sorts of import restrictions and barriers applied there, so it is difficult to fully import in all circumstances. But it is really, I believe, a case of people having to have a look at the market price and decide whether they can make money there. But, certainly, there would be very few industries in Australia that could not trade effectively there provided the market price will allow them to do that.

Mr HOLLIS—Why are we not there in more volume then? Why is it such a small market for Australia currently?

Mr O'Sullivan—Perhaps because there has been a significant focus at government level in the Asian region. A government level focus in all sorts of areas encourages people to go to Asia and trade in Asia. Most of our government trade missions and things are focused on the Asian region. I quite often get invited to go on trade missions and very rarely do I ever see one to South America. I think government can definitely take a role here and start to encourage people to turn their attention in that direction because I think there is definitely a market there.

Senator FERGUSON—In your submission you say to us that from June last year to December sales from the South American region were 15 per cent of your total turnover when it could have been double that. What factors would have to be in place for you to double it?

Mr O'Sullivan—Start to look at more local value adding to reduce some of the import tariffs.

Senator FERGUSON—That is not something that we, as a government, can do; that is something that you would have to do?

Mr O'Sullivan—Yes, it is something that we would have to do.

Senator FERGUSON—When you said that it could be double that, I wondered whether we have any impediments.

Mr O'Sullivan—What you can do is to put a tax treaty in place.

Senator CHAPMAN—What capacity is there for the Australian government, through the world trade negotiations, to get some of those tariffs down? Are they pretty much fixed in cement or is there capacity for them to be reduced?

Mr O'Sullivan—I cannot say that I am an expert on that. I do not know what status most of the South American countries have with the World Trade Organisation, but the World Trade Organisation is clearly focused. There are a lot of working groups and government entities involved in bringing down trade barriers globally, and that is happening. Again, any push we can have to the World Trade Organisation to get those barriers dropped in South America will allow more trade to be developed.

Mr BAIRD—I, like Senator Ferguson, am impressed to have someone here who is involved in the marketplace and getting orders and contracts in South America. We can learn very directly from you. I notice you mentioned the double tax agreement. That would be number one on the priority list that should be addressed to assist you and others to develop in the market. Other things to be included would be participation in the inter-American investment group and the visa issue. That would be it? Obviously our role is to take back recommendations to government as to what we should be doing to remove some of the impediments to trade with South America.

Mr O'Sullivan—Those three issues, plus a consideration towards a government-to-government marketing campaign associated with promoting the capabilities of Australia, particularly in the area of high technology. Everyone knows that this is a wonderful tourist destination – and, again, that attraction helps us – but it does not necessarily tell people that we are high tech. Any sort of promotional campaign associated with our ability to produce high-tech products would certainly help our manufacturing sector.

Senator BROWNHILL—Are the air flights going to be a boost and a boon to more trade? For example, the argument is given that if people know more about a country – having students here and that sort of thing – they will go back and sell the country. That is what has happened in Asia. Another argument that is given is that if people come here as tourists, they then pick up business interests. If we have more people going the

other way as tourists – and it will be a much more affordable tourist destination with direct flights – is that going to make a difference?

Mr O’Sullivan—Of course there were direct flights before Qantas started to fly. It is good to have Qantas flying there, because they have a 747-400 which goes directly from Buenos Aires to Auckland without having to stop in Rio Gallegos and there are not the concerns about very old aircraft. Any type of social exposure to other countries has to develop our industry, both tourism and other industries, I believe. It is great to have Qantas flying there.

Senator BROWNHILL—What about cost effectiveness?

Mr O’Sullivan—I still do not know how airlines price their different sectors, but it is reasonably cost effective.

Senator BROWNHILL—This is my last question. Have you been invited by trade ministers to do anything to try to help sell furthering trade to South America? Has Austrade asked you or the minister?

Mr O’Sullivan—No. I had one contact in the embassy in Buenos Aires who tried to get together a bit of a trade evening and asked for some contributions. I committed to do that, but it fell over and did not get enough interest.

Senator BROWNHILL—Do you think that peer group pressures are the best way to sell this? If you can say that you have done it with your type of product, could other people do it with other types of product just as effectively by taking on some of the lessons that you have learnt?

Mr O’Sullivan—I think so.

ACTING CHAIR—I have just a couple of quick questions before we wind up this segment with you. With regard to the Masters students’ fees, when you decide, ‘Right, there is one for us; we will give this a go’ and embark on the process, about how long does it take for you to finally close that file?

Mr O’Sullivan—It takes in excess of six months.

ACTING CHAIR—All three of them have taken that time?

Mr O’Sullivan—Yes.

Mr HOLLIS—Did you ever see your local federal member on that issue?

Mr O’Sullivan—No, we tend to do things on our own.

Mr HOLLIS—I know that, and that is good. Sometimes federal members of parliament are not a lot of assistance, but in a case like that – I do not know what your electorate is –

Senator FERGUSON—Present company excepted, of course, Mr Hollis.

Mr HOLLIS—The problem with visas is that they are blanket, but if you had a specific case, you could go through the federal member and see the minister. I am not trying to give any member of parliament more work, but if you went and actually explained to the minister exactly what was involved, it might only be this much instead of that much. That is a decision that you should make and it does not matter what side of the political fence you are on. Next time I would give it a go anyway and see if that could reduce it.

Mr O’Sullivan—Yes, that is good advice.

ACTING CHAIR—You have brought some focus to something that is about to become a bit of a problem for us because of student overstays and the student visa issue. We know there are several institutions that are providing genuine work experience for business degrees of this kind. They have been producing terrific results for the company, Australia and the students. I am starting to hear similar experiences where we have been caught up in the blanket, solved the overstays and now our kids cannot work either. It is going to have to come up and you have given us a very good concrete example of a company that is doing it properly and creating big opportunities from it. That is fine, and take Mr Hollis’s advice because the local member is worth a call. It might cut your six months down to two months next time on that one. I wanted to ask you about something else very briefly. This matter has not come up much during our inquiry, but Captain Pocock from P&O will be speaking to us after you. A couple of our presenters have made observations about delivery and transport systems, and in aviation the air links have been raised as an issue. What has your experience been with the distribution network once you have sales in there?

Mr O’Sullivan—Our experience is that we can generally put a 20-foot container anywhere in the world for about \$US3,000– and not quite double that for a 40-foot container. The freight times to South America tend to be about eight weeks and it generally requires some trans-shipment. But, again, it is because of the demand. If the demand increases, then there would be more motivation from the shipping lines to perhaps look at direct sailings that do not require trans-shipment, and we could get that down. It is an issue. Whenever you are

tendering for work, lead-time is always an issue associated with securing a business. If we can get that lead time down by reduced shipping times, then it would be an advantage.

ACTING CHAIR—That is either dealt with by carrying more stock over there or dealing on a just-in-time system that is at least eight to 10 weeks or more.

Mr O'Sullivan—Yes.

ACTING CHAIR—But you find that it is reliable enough in that form?

Mr O'Sullivan—Yes. Our shipping very rarely goes off the rails. It is preferred not to trans-ship because, as I am sure your next speaker will tell you, when goods are trans-shipped, there can often be delays.

ACTING CHAIR—So direct services appeal where you can get them?

Mr O'Sullivan—Yes.

ACTING CHAIR—Fair enough. No-one else has any further questions. I thank you on behalf of the committee, Mr O'Sullivan. It has been a very enlightening discussion with you. I move:

That the Trade Subcommittee receives as evidence and authorises for publication the submission from Mr Neil O'Sullivan to the inquiry into Australia's trade and investment relationship with South America.

ACTING CHAIR—I would also like to suggest that, rather than us going into in camera to discuss the issue of local production that we skipped through earlier, with your permission, we will ask our secretary, Ms Vincent, to perhaps have a private chat to you about that, and she can brief us on some of those points in confidence, because we are interested in that too. On behalf of the committee, thank you again.

Mr O'Sullivan—Thank you for the opportunity to present some of our barriers.

ACTING CHAIR—Thank you.

[12.07 p.m.]

POCOCK, Captain Richard Wolf Lamoral, International Projects Manager, P&O Australia

ACTING CHAIR—I would like to resume our activities this morning and formally welcome Captain Richard Pocock. Have you done this exercise before?

Capt. Pocock—No.

ACTING CHAIR—I will just brief you then that the committee prefers that evidence generally be given in public but, if at any stage you wish to do so in private, you may ask that and we will give consideration to the request. The way you conduct affairs is entirely up to you. If you would like to make a brief opening statement, you are welcome to do that.

Capt. Pocock—Would you like to know something about P&O before we talk about what we are doing in South America?

ACTING CHAIR—Yes, in the general sense. We are pretty well informed of the company in broad terms, but go to it as you see fit.

Capt. Pocock—It often confuses people as to where we fit into the bigger picture. P&O is a London based, transport based conglomerate. In 1998 it consisted of 11 operating divisions, including cruise ships, ferries and bulk ships; Earl's Court was owned by P&O; Bovis Homes was owned by P&O; and there was a division called P&O Australia, which was wholly owned by P&O London but managed and operated out of Sydney.

P&O Australia has five operating divisions, of which the chairman is Richard Hein and, as I say, it is managed from here in Sydney. There is a division called the Cold Storage Division, which is the equal largest cold storage business in Australia and the seventh biggest in the world, managed here from Australia. There is a business called Maritime, which has offshore rig supply vessels, a shipping agency, a ship charterers and the supply vessel which goes down to the Antarctic. There was a business, before it was sold late last year, called P&O Services that cleaned and managed government and private buildings. There is a business called P&O Holidays, which operates four or five islands in the Barrier Reef. And there is a business called P&O Ports.

The genesis of P&O Ports was in the early 1960s when P&O Australia was initially set up as an agency business for its ships here, but it grew to take advantage of other business opportunities, one of which in this country was stevedoring. By last year we had a little over 50 per cent of the business in Australia and we work in that market with Patricks. In the mid-1980s, it was apparent to P&O Australia that stevedoring in Australia was a mature business. There was not a lot of growth available and we extended our business overseas.

Against international competition in 1984, we won the right to manage a container terminal in Port Kelang, and that was the world's first port privatisation won by P&O Ports in Australia. That was judged at one stage by the United Nations to be one of the two most successful privatisations in the world in terms of the benefits that it brought to the community, the government and the citizens of that country. Since then we have gone on growing. We now have 26 large facilities in 18 countries around the world. We have an additional 40 operations here in Australia. We have an additional 19 in North America and we operate in four ports in South Africa. Our business is spread all the way from Russia to China, throughout Asia, through India to South Africa, up to Europe and over to North America. In terms of turnover at the moment, P&O Ports has a turnover of \$A1.2 billion which is its contribution to P&O Australia's total turnover of \$1.75 billion. We have assets worth \$A1.5 billion. We have in excess of 11,000 employees worldwide of the total of 40,000 that P&O Australia has.

So that is the nature of our business. P&O is in a state of change at the moment. It has divested itself of a number of its businesses in the UK. It has floated a number off and has joint ventured a number. It is slimming down to its core businesses which will be: a large ferry business with 48 ferries trundling around the North Sea, north Europe; the Ports Division, which is us in Australia; and a logistics business. The largest of its businesses is about to be floated off as a separate company – that is, P&O Cruises which has 17 cruise ships with another seven on order at the moment. Amongst those cruise ships, until only two months ago, was the largest ship in the world, the *Grand Princess* of 109,000 tonnes. We have seven ships on order: five were ordered just before Christmas for a total cost of \$US2 billion. That business will be floated off. The company at the moment is in the process of change, but it does recognise that P&O Ports is one of its core businesses. In 1993-94 the Argentinian government put five container terminal operations on the market for tender. We successfully bid for the largest of those but not without a certain amount of problems. We won the bid and then an injunction was taken out against us by our Argentinian competitors, and we lost the bid. Then there was an

amount of dialogue at ambassadorial, very high commercial levels and at government level and we won the tender. The Australian ambassador in Argentina at the time was of enormous help to P&O Ports in that process. We advised the Argentinian government that five tenders were far too many for the business that was available. Despite that, they would not change their minds. Within only a matter of months, one of those companies went out of business and went bankrupt. Within the first three years there, we lost a total of \$US25 million. We struggled very hard but we hung in and now, six years later, the business is successful.

We have learnt a lot about doing business in South America. We are content to be there. We would invest more money if there was the opportunity there. We have, I have to say, an excellent relationship with our work force in Argentina which is generally transmitted throughout businesses around the world. They are highly efficient businesses and we enjoy good relations with our labour.

Since then, we have bid for two more port operations in Latin America – one in Brazil and one in Chile. We are interested in and are currently pursuing three other opportunities in Brazil, one in Peru, one in Ecuador and one in Venezuela. So we are still very active in that part of the world and hopeful that we will be able to put our feet down again. I think that is all I can tell you and, of course, I am happy to answer any questions.

ACTING CHAIR—Thank you, Captain Pocock. Senator Chapman will begin the questioning.

Senator CHAPMAN—Thank you for that outline of your activities, Captain Pocock. I actually had the privilege of visiting your port in Buenos Aires when I was there in November and was given quite an extensive briefing and tour, so I probably will not have a lot of questions because I have that background. Can you give me some comparison of the efficiency of your operation in Buenos Aires – and I guess crane lifts is probably the measure generally used – compared with Australia?

Capt. Pocock—I can tell you that in most of our operations overseas we look to between 25 and 30 containers an hour per crane. Last month we got just over 15 in Sydney and I think it was just over 18 in Melbourne.

Senator CHAPMAN—How do manning levels compare per quantity of containers?

Capt. Pocock—Manning is better than it was here because we have now got access to casual labour, but there is certainly far more access to casual labour overseas and in South America. There we are able to say that we want these men to be specialists and we want to employ them because they will work for the company and they drive the cranes that are worth \$US7½ million each. We want those people to work for us. But we do not want the people who drive the trucks and do the less technical work to be part of us and we will hire them on an as needs basis. We are able to do that in most places we operate in the world so we do not have to carry a huge work force.

Senator CHAPMAN—As I recall, the actual docks you took over there were warehouse type docks originally, weren't they?

Capt. Pocock—Yes.

Senator CHAPMAN—And you sort of flattened those and produced container docks?

Capt. Pocock—They were old derelict facilities and we have spent \$100 million in building it into a world-class container terminal. A feature of our business is that we have to spend large amounts of money to start with and we do not do very well for the first few years. In the case of Argentina, as I just told you, we lost \$US25 million in the first three years. So we are in a high-risk business.

Senator CHAPMAN—You provide the stevedoring facilities and the storage and you actually run the container port. Do you provide tugboat facilities and those sorts of things as well, or is it just purely the container facilities?

Capt. Pocock—The answer to that is that in very few places do we provide tugs. I think we do in Pakistan, but that would be unique. Our business is often container terminals where we lease the container terminal from the government for a period of 30 years. There are a number of mechanisms for financing that – either we put a lot of money down in the first place or we have to pay an annual rental. We buy all of the equipment. We employ all of the labour. We operate that for, as I said, up to 30 years. Most of our facilities are container terminals. In the case of Manila, we operate the whole of the north harbour, which is 26 berths and 18 anchorage points. That is a huge operation that employs nearly 3,000 people. Then we have an operation in Indonesia where we do all of the logistics, including maintenance of the trucks and employing the truck drivers to get gold and concentrate from Freeport mine down to the ships and loaded into the ships. So it is a very diverse business.

Senator CHAPMAN—Of your worldwide operations, where would you rank the Buenos Aires port in terms of (a) its efficiency in comparison with the others and (b) its profitability?

Capt. Pocock—It is certainly amongst our most profitable and in terms of efficiencies, if it is not the most efficient, it is up there in the top three or four.

Senator BROWNHILL—You have just said that it is one of the most profitable. Obviously you are not positioning yourself in South America because it is not going to become a busier part of the world. What growth projects you are working on in that area? Obviously Australia is not going to get all the trade which we would like. As their economies improve and the countries become more stable there is going to be an increase in trade. What does your graph say there?

Capt. Pocock—Do you mean the market as a whole?

Senator BROWNHILL—Yes, the market as a whole – because you are part of the transport chain.

Capt. Pocock—As a market as a whole, the shipping container generally follows GDP. In Argentina at the moment their share is forecast at 3.8 per cent and last year it was a negative 3.3. That, in fact, materialised volumes throughout the port. The whole port handles 1.1 million. We are anticipating the growth rate of GDP which is 3.8 per cent.

Senator BROWNHILL—And that is a worldwide trend?

Capt. Pocock—There are a number of factors. If you go to less developed economies where containerisation has not made a high penetration, then there is going to be growth there. All of that has happened in Argentina. The only growth now is GDP.

Senator BROWNHILL—What about outward trade from those countries? There is refrigerated transport, obviously.

Capt. Pocock—There is but, of course, their market has collapsed as ours did when the European Union came into existence. They are not well supported by North America in terms of their refrigerated cargoes and produce, nor by Europe.

Senator BROWNHILL—Our opportunities for trade in South America are there but are we going to be gazumped? In the past it was, maybe, Europe, but is there going to be a north-south axis now? This is not going to affect you that much but I am just asking for a more general visionary view of the situation. If there is an increase in trade with North America there is still going to be the same amount of shipping and transport of containers. What is your view of that? We are having an inquiry to look at trade opportunities with South America. Have you got a personal view that says that there is a great opportunity for us or do you think we are going to gazumped by North America?

Capt. Pocock—Our experience is that it is the locals that gazump us. The South Americans are passionate about keeping their own businesses. Whilst they have not got the money to compete with people like Spanish Telecom and other big companies, in our business they are passionate about keeping their business. Their ports are their crown jewels, as they see it, and their port authorities, labour and political constituencies want to keep the ports in local hands.

We have had that twice now. In Brazil we bid for a business for US\$159 million but it went to Brazilians. And that was an auction system. It was quite interesting. It was like going to a weekend auction for a house here. We sat in the stock exchange in Rio de Janeiro and just raised our hands every time we wanted to up the bid by \$500,000. The Brazilians would have taken that business regardless of how much they had to pay for it.

In Chile, at the end of last year we bid US\$17 million for a business and the Chileans bid US\$126 million. In another business in Chile, we bid US\$42 million; the Chileans bid US\$96 million. They are passionate about keeping their businesses.

Senator BROWNHILL—Does that follow through with all businesses? Obviously, yours is the one you know more about. I am just wondering whether we are dealing with a culture here that says, ‘Well, we like to do things ourselves. Therefore we will have import replacement ourselves, rather than actually having the import.’

Capt. Pocock—I have no real idea.

Senator BROWNHILL—I am not trying to lead you, Captain. I am trying to get more out of your evidence than just the fact that you have got port facilities, container facilities and that sort of thing, so as to learn more about the psyche of the country.

Capt. Pocock—South America competes with us and North America for the Asian market. There are a lot of things that we produce that they produce far more cheaply than we do: wood pulp, paper – all of those forest products. They produce copper concentrate far more cheaply than we do. My whole feeling about South America is that it is just so underdeveloped. There is just so much opportunity there.

ACTING CHAIR—The point that flows is that you are making a business assessment that these ports are worth getting into, given the Australian expertise and ability you can take there?

Capt. Pocock—Yes.

ACTING CHAIR—They are worth getting into because the business is going to grow. Providing you can get in – and it is hard fought to get in – you have made assessments along the lines you talked about with Senator Brownhill of the way that the business may grow. I guess what we are asking is: what directions do you see the business growing in and what opportunities are there for Australian business to be in that growth?

Capt. Pocock—There are two questions. Firstly, what direction do we see it growing in? There is a huge consumer market there. There are 154 million people in Brazil, et cetera. As their own internal economies pick up, there is going to be higher and higher demand for consumption. It is one of those places that we believe can only grow because it is so far behind the Western world.

Senator BROWNHILL—Where I came from in my questions was that you are actually on the ground, in the country, providing a facility for the country. We have had a previous witness today that says the next step most probably will be to set up a manufacturing base within the country and use the benefits of Mercosur. Is that really going to be the biggest opportunity for Australian companies: to set up a manufacturing base or whatever, within those countries, to make use of Mercosur, rather than trying to pop our stuff in from Australia in a manufacturing product – because of the psyche of the country and that sort of thing? It would not affect you, obviously, because the ships are still going to be coming in out from other countries. It goes back to another question. Earlier today, we were talking about direct transport and direct shipping. A previous witness made the comment that the eight weeks does not really worry him that much. But it does worry some people if they want to put a product into those countries. Maybe the biggest opportunities are going to be with manufacturing bases being situated there and repatriating profit.

ACTING CHAIR—The way the senator has explained that sort of clarifies it. We have had people come to us and say, ‘If the shipping services were better, we would be able to do better.’ That is fine. In a sense, we have drawn the link that P&O’s interests in the region can be seen as being an indication that P&O sees more business between Australia and the region. But what you are really saying to us is that you have got a product to sell them – whether they are our education services, professional expertise, manufacturing expertise or whatever – that you can do well with. You are there because of the business opportunity, not necessarily to grow the trade between Australia and South America. I do not even know whether you see much growing trade.

Capt. Pocock—The trade between South America and Australia is not a part of our equation when we go into a business. Trade between South America and the rest of the world is our part of the equation. I heard the previous witness talk about Australians in South America. We are non-threatening. We are not caught up in Euro-politics, or North American politics. We are absolutely non-threatening. As a company and as individuals, we see ourselves as ambassadors for Australia when we go there. I have a personal philosophy what whenever you tender for a big business you need to be the preferred winners. It will not always, if ever, make you the winners, but in order to leave your footprint on the business in that country you need to leave having been the preferred winners.

ACTING CHAIR—Whereas, by comparison, when Qantas make a decision to try some weekly flights to South America, they are doing it because they believe the business flow, the tourist flow or whatever will be there. They believe the business is going to be there. We should not draw the same parallel with shipping. Your investment is a global business local opportunity.

Mr HOLLIS—Almost as an aside, you mentioned that you have been there six years and you said that you learnt a lot about doing business in South America. Share what you can with us.

Capt. Pocock—South America is a different place. All of the countries are different, and they all relate back to their different histories. They all have different ethics, different methods of behaviour in approaching business and different values. It is a highly legalistic society. It is quite frustrating legally, in most respects. That has been my personal experience. I had to fly over to Chile at the end of last year for a meeting with 15 people from port authorities. There were two of us. There were 15 of them, seven of whom were lawyers, two of whom had flown down from New York. It is a highly legalistic society.

I will read you something, if I may, from the man who runs our Buenos Aires operation. He says ‘the bureaucracy in Argentina is not easy, and it is not easy to obtain decisions and agreement from authorities; it is ponderous, and it could take months on simple issues’. That is true. It is said that corruption is widespread. However, we are unable to comment on that because P&O has a strict policy that it does not involve itself in that. After an early period in Argentina where people tried, they quickly understood where we were coming

from. We are not asked anymore. There is always the suspicion that it is there in Argentina. In Chile, I suspect no. Chile is a well-governed and well-disciplined country, made so because the people are different. They went to Chile. There was little attraction for the Spanish to go to Chile. They went there, and they fought with the Indians for 300 years. In fact, the Spanish never got south of the Biobio River in Chile. They were fighters and tough, committed and resolute people. They are different now in the year 2000. It is a good place to do business. It is again legally difficult, but what you see is what you get, and generally they mean what they say.

Brazil is Portuguese. Brazil is different altogether. Nothing is as it seems to be. My own view is that there is little loyalty in the society in Brazil. It is a lovely place. They all get on with each other. You see all colours of people playing football on the beach at Rio de Janeiro. It is a marvellous place, but it is a very difficult place to do business because, again, it is not as we are. What we say is generally what we mean and what we do. That is not the case there.

Peru is a very dignified, closed and autocratic society with a few Spanish people very much at the top. In Ecuador, 80 per cent of the people live in poverty, and that is the same as Peru. Just a few people control the country. We have learnt a lot about what to do there. The most important thing in our business is always our local partner. It is very hard to get rid of a bad partner. The local partner will enable you to do what you want or will destroy it for you. We spend a lot of time working out who we are prepared to work with and spelling out to them what our culture is, what our ethos is, what our expectations are and what the requirements of them will be – they would have to find \$30 million or \$40 million in a few months time if we win – so that we all understand each other. I think that is what we have learnt about South America.

Mr HOLLIS—Yes, so I am a little bit puzzled. What would it be? I guess it would be having a good local partner, having immense patience and having a product to sell.

Capt. Pocock—Patience. Yes, and credibility. That is where I say that being Australian helps, because we are not involved in anybody else's politics. We are completely neutral. I know it is an old chestnut, but it is all about people, and it is all about representing yourself, whatever your company stands for and what Australia stands for.

ACTING CHAIR—Even though P&O is globally known as an old, longstanding British company, have you been able to establish on the basis of them accepting that they are doing business with the Australian component?

Capt. Pocock—Yes.

ACTING CHAIR—And that you are a global player as an Australian stevedoring company?

Capt. Pocock—Yes.

ACTING CHAIR—That is good.

Capt. Pocock—We had to do that particularly in Chile last year, with all of the Pinochet troubles happening in the UK. Society was very polarised on that issue.

ACTING CHAIR—It has come up in a lot of submissions to us that, as anywhere, you have to have good local partnerships. To win those tenders, you have had to have the local content in the form of a submission that it is going to involve a quality local partner. That has been part of the whole deal put to the government?

Capt. Pocock—Different tenders require different things. Some tenders demand a local partner, some tenders demand that, as an operator, we have 35 per cent of the equity – or whatever – and others make no such demands on us and are completely ambivalent when it comes to ownership.

ACTING CHAIR—Corporately, finance has not been a problem? You have not had to go to EFIC or anyone else. You are well capitalised. You make your bid, and you know whether you can stake it or not.

Capt. Pocock—Yes. Funding is not an issue for us. On that, I should add that in all of our operations we have equity, varying from 100 per cent down to 32 per cent, which is the least we have. We never buy into a business that we cannot operate ourselves. That is partly to protect our own reputation and partly because the financiers require that of us anyway.

ACTING CHAIR—I have had the airlines telling me for years that if the landing charges at a certain airport are better then more planes will fly there, and I have never really accepted that as a premise. They go where the people want to go, and vice versa. In your case, you are establishing independent shipping operations that have their own measures of efficiency, their own labour costs and their own structures. Do the relative costs – for instance, of shipping in and out of Australia versus shipping in and out of London versus shipping in and out of somewhere else – make any difference as to that volume of business?

Capt. Pocock—Do you mean whether our facilities will attract business or not?

ACTING CHAIR—Yes. For instance, in Australia it is a judgment to make between using yourselves or Patrick. Is it the same situation in other places too? Or are people saying that they will go and use Australia or South America as a base because they can get a good deal at a port?

Capt. Pocock—The whole dynamics of shipping are changing. Ships are getting bigger and costing more money and, therefore, the shipowners want them to stop in fewer places. The picture that is almost here is large ships – they already carry 6,500 containers whereas, in the seventies and eighties, the biggest was 3,500 – just going around the world. In actual fact, they will stop at Panama and then to go back the other way; it is a pendulum service, because they cannot get through the Panama Canal. They will probably stop at five or six ports around the world. They go fast and have enormous economies of scale. From those five or six ports, the rest of the world will be fed. That is the pattern that is beginning to emerge there.

In terms of our costs, whether we can attract business or not, we bid for, as I have said just now, business in Brazil, which is one of the most, if not the most, expensive ports in the world but it still the second largest port in South America. Shipowners continue to go there. There are all sorts of things that come into play. If you have one port in a country, then you can charge high prices, as Santos does in Brazil, although Rio competes with it – but there are other issues there. We try to determine all of that when we do our market study into these places, but you can get it very wrong. One of our big competitors is a Filipino company that paid for the Port of Rosario at the River Plate in Argentina two years ago. They paid \$170 million odd for the port, which was a derelict backwater, and the next highest bid was \$30 million. The Filipinos now are warning their shareholders that they may well have to walk away from it and lose up to \$40 million. So you can get it very wrong. After you have got it and you think you have got it right – for example, in Argentina – things can still go wrong for you. We at P&O Ports are passionate about our business. All we do is run ports. A lot of us are ex-seafarers and are really married to the concept of ports and seas and we are passionate about it. I think that is probably why we do it so well from Australia.

ACTING CHAIR—I would like to thank you, Captain, on behalf of the members of the committee. Please do not take the fact that members have been leaving while you have been presenting as a signal of the interest in your submission. It is not so – this happens. It has been a very interesting presentation from you. As you would have picked up when you were in the audience a little earlier, it flows very nicely from the other information that has been coming to us. If there is anything you would like to clarify for the benefit of *Hansard*, you may do that when we finish the proceedings. I formally thank you on behalf of the committee.

Resolved (on motion by **Mr Hollis**):

That this subcommittee authorises publication of the proof transcript of the evidence given before it at public hearing this day.

Subcommittee adjourned at 12.43 p.m.