



Manufacturing Futures

Achieving Global Fitness, April 2006

Australian manufacturers are in the process of transforming their operations to keep pace with rapidly increasing competition from around the world.

Ai Group undertook the *Manufacturing Futures: Achieving Global Fitness* study to highlight how global engagement is requiring business to be lean, make use of global supply chains, become more capital intensive, and be innovative in order to remain competitive. These changes raise questions about whether current policy settings are adequate to ensure Australian manufacturers can prosper in the new global environment.

The study found that globalisation, increasing competition from China and the strong Australian dollar have heightened the need for manufacturing to develop new methods and different approaches to address the challenges it faces.

While these hurdles have shaken industry's perceptions of its future, it is certain that manufacturing remains crucial to the Australian economy going forward.

As one Sydney textile manufacturer said:

"Manufacturing plays a vital role, however, I think we've got to face reality and the reality is that for manufacturing to survive, it needs to think very differently..."

Manufacturing Futures provides a full and clear understanding of the challenges facing manufacturing, what can be done about them, and where industry is heading at this critical juncture.

The report is based on a major, national survey of more than 800 manufacturers, a compilation of previous Ai Group research, consultations with more than 200 business leaders in nine major forums, and in-depth interviews with 20 large manufacturers.

It outlines the strategies being employed by manufacturers to remain competitive, industry's view of government, and sets out recommendations for future policy directions.

Key highlights

- *Manufacturing Futures* addresses the future direction of Australian manufacturing, which in recent times has been subject to intense global competition, the emergence of China and an uncompetitive currency.
- It is not surprising given these dynamics that many manufacturing firms hold a high degree of uncertainty about the future. **One-third of companies indicate they are very concerned about Australian manufacturing prospects.**
- The major sources of concern are:
 - Competition from low cost countries (61% of companies);
 - Insufficient domestic market growth (49% of firms);
 - Inability to secure skilled staff (46% of firms);
 - Insufficient labour flexibility (35% of companies); and
 - Inability to keep pace with regulations (34% of companies).
- **Despite the uncertainty, the overriding message is that manufacturers are building the foundations for a new phase of growth.**
- The study identifies a new level of global engagement by Australian manufacturers. Globalisation has accelerated in pace with the percentage of manufacturing activity derived offshore (either from offshore production or through use of imported materials) expected to increase from 15% to 25% over the next three years.
- **Priority strategies being implemented by companies to remain globally competitive include:**
 - Deriving greater income from new products (19.5% very likely to implement);
 - Using more imported components (17.5% very likely to implement);
 - Outsourcing more offshore (16% very likely to

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- implement); and
- Spending more on skills acquisition (13% very likely to implement).
- Middle order strategies include spending more on capital equipment, R&D and generating greater income from export markets (between 10-13% very likely to implement).
- However, an important one-third of manufacturers have not identified new strategies to meet current challenges.
- Industry recognises competitiveness will be a function of the strategies each company implements, but sees a role for Governments in removing obstacles and facilitating business efforts to improve competitiveness.
- In the view of industry, the highest priorities in relation to action by government (with more than half of firms strongly agreeing) were better company tax and depreciation arrangements and reducing business regulation. Also important was enhancing skill development (with over 38% strongly agreeing).
- Ai Group proposes six objectives for government action:
 1. Building strength through capital investment;
 2. Measures to further globalise Australian industry;

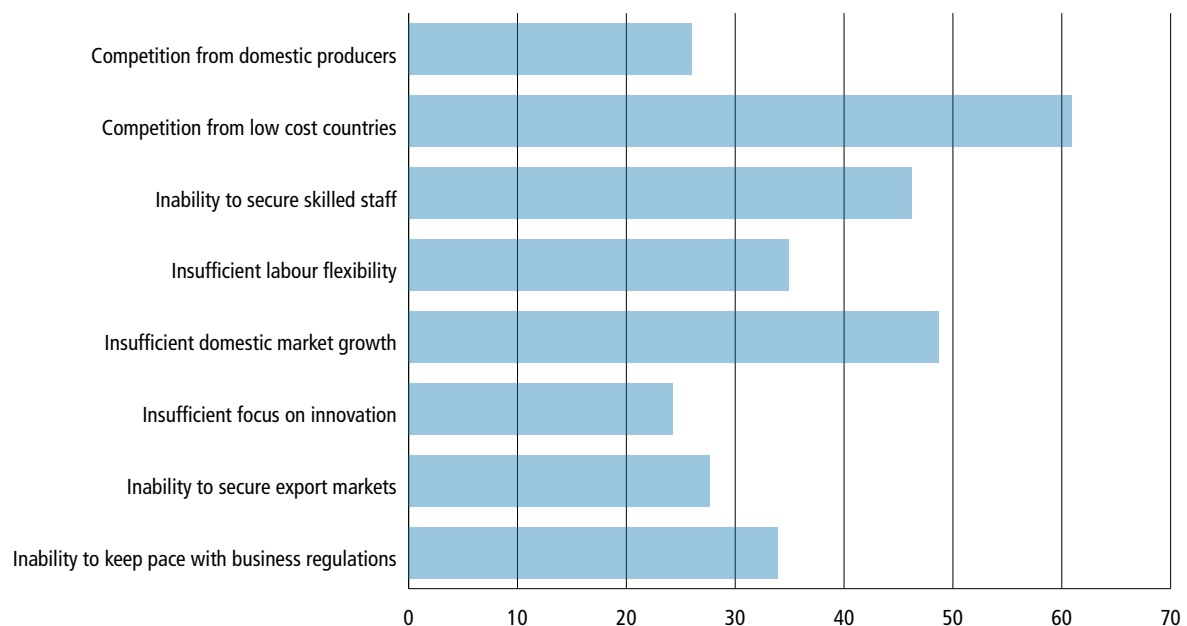
3. Building world class capabilities;
4. Becoming a more skillful global competitor;
5. Loosening the shackles of government red tape; and
6. Becoming a more innovative global competitor.

Summary of the recommendations

While manufacturers understand they carry the main responsibility for change and implementing processes that will increase their productivity, they also recognise that Governments have an important role to play in removing obstacles and encouraging innovation and improvements in competitiveness.

As a result, Ai Group has identified a total of 29 major proposals designed to help build a bigger and more robust economy that will be better equipped to adapt swiftly and effectively to shifts in the economic environment. The recommendations are also aimed at reinforcing the ability of manufacturing to build the capabilities necessary for its future growth.

Sources of industry concerns



Source: Ai Group, Survey on Manufacturing Futures, September 2005

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Specific proposals include:

Building strength through capital investment

- A phased reduction in the company tax rate from 30% to 25% over a five-year period (noting that reform to personal income tax remains the immediate priority);
- A thorough review of Australia's tax regime on investment compared with our trading partners and competitors to be undertaken by Ai Group; and
- Invest Australia should be provided with additional flexibility to support multinational corporations that wish to continue to invest in Australia, insuring that risk of disinvestment is minimised.

Measures to further globalise Australian industry

- Continued pursuit of trade liberalisation at the multilateral, regional and bilateral levels in order to pursue market access for Australian manufacturers;
- Improved visa arrangements to ensure access to foreign markets by Australian skilled workers;
- **Expanding Australia's skilled migration program to assist the growth of Australia's skills base in support of domestic measures to address skill shortages;**
- Doubling the funding for, and implementing changes to the eligibility criteria of, the Export Market Development

Grant (EMDG) Scheme, as well as examination of the reforms to administration that improve access for small and medium-sized enterprises; and

- **Adopt the Board of Taxation's recommendations to remove tax barriers to offshore expansion by Australian companies.**

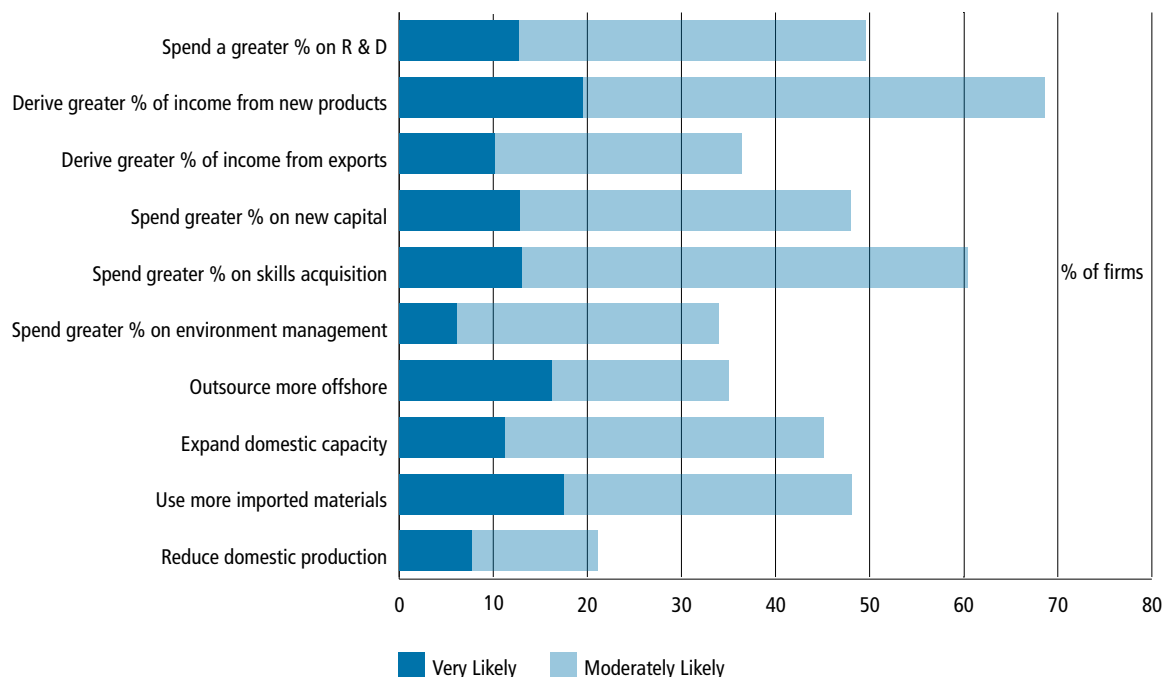
Building world class capabilities

- **Implementation of a whole of government strategy to lift business capability by providing advisers who are able to assist business with growth strategies and link them to industry and government initiatives available to support their business plans;**
- The Building Capability Initiative being also charged with assisting enterprises to develop skill development strategies; and
- The development of regional and industry collaboration networks.

Becoming a more skillful global competitor

- **Increase the focus of the training system on the upskilling of existing workers;**
- Increase the overall spending on education and training;
- Improved access to recognition of skills for existing employees;
- Extend and refine incentive payments to employers;

Strategies likely to be pursued by companies over the next three years



Source: Ai Group, Survey on Manufacturing Futures, September 2005

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- **Make Science and Engineering undergraduate programs a National Priority for concessional HECS eligibility; and**
- **Broaden tax eligibility for self-education expenses for learning beyond current career.**

Loosening the shackles of government red tape

- Building on the principles agreed at the Council of Australian Governments (COAG) meeting in February 2006, all governments adopt improved and consistent measures of:
 - The impacts of compliance burdens (including private and public sector administrative costs);
 - The effectiveness of regulations in achieving explicit goals; and
 - The opportunity costs of regulation-induced behavioural changes.
- **Commitment to reducing the compliance burden by 15% over three years;**
- Streamlining the application process for all government grants through a two-tier approval process with a greater focus on performance outcomes;
- Introduction of an annual Regulatory Implementation Bills/Ordinances by all tiers of government to facilitate an annual regulatory reduction process;
- Establishment of a Regulatory Review Unit operating with an independent Board to oversee the implementation of targets for review of institutional arrangements;
- Regulation Impact Statements should be revitalised and expanded; and
- **A uniform national premium and national standards to be established for workers' compensation through the new Australian Safety and Compensation Council with a commitment to implement by 2010.**

Becoming a more innovative global competitor

- The Commercial Ready program is too recent to review, however, support is provided to the Australian Government's decision to review the R&D tax concessions;
- **Making the R&D tax concession more effective by allowing companies to credit their franking accounts by the amount of company tax saved as a result of the concession;**
- Improving linkages between business and public sector research including addressing barriers to public/private research collaboration;
- **Improving access for Australian companies to tax concessions and grants for offshore research and development activities that benefit the national economy; and**
- A grant scheme should be introduced to support small and medium enterprises in meeting the professional costs associated with intellectual property protection, particularly in overseas markets.

Conclusion

Finally, the report raised important questions about what it means to be an Australian manufacturer, and how success and failure will be judged in the future.

The totality of Australian manufacturing can no longer be defined as Australian sourced production given a greater share of production and inputs will be sourced from offshore.

A metal manufacturer from Wollongong summed it up:

"We are no longer an Australian company, but a global company based in Australia."

According to the information gained during the compilation of *Manufacturing Futures*, **Australia's new breed of manufacturers will have several or all of the following characteristics:**

- A belief in their capacity to compete against overseas companies in Australia and overseas;
- A global outlook to their business with a desire to be world class operators;
- A focus on ongoing business improvement, with every effort being made to be lean, strip out wasteful operations and improve productivity;
- A focus on building the capital intensity of production through automation and the rapid adoption of new technology;
- An emphasis on lifting the skills capabilities of staff through both apprenticeships and training to upskill;
- A well-developed supply chain, seeking out the most competitive suppliers whether they be, for example, in Australia, Mexico or China;
- A focus on product design and innovation that will deliver quality products at world competitive prices; and
- A focus on developing niche markets supported by strong customer relations and after-care services.

In conclusion, the future of Australian manufacturing will be strongly influenced by the degree to which we are able to integrate into the global economy and keep pace with the necessary actions and investments to achieve global fitness.

Further Comment:

Heather Ridout, Ai Group: 02 9466 5504

Media Inquiries:

Tony Melville, Ai Group: 02 6233 0700