



**Joint Standing Committee On Foreign Affairs,
Defence and Trade**

**Inquiry into Government support for Australian
defence industry exports**

Austal Submission

9 July 2014

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INTRODUCTION

On 19 May 2014, the Senator David Fawcett the Chair of the Joint Standing Committee on Foreign Affairs, Defence and Trade (Defence Subcommittee) announced a new inquiry into Government support for Australian defence industry exports. The Defence Sub-Committee of the federal parliament's Joint Standing Committee on Foreign Affairs, Defence and Trade will conduct the inquiry and is seeking input from stakeholders including the Defence Industry as to how Government can better facilitate export of Australian defence products and services.

The inquiry's terms of reference include examining Government support for Australian defence industry exports, having particular regard to:

- identification of barriers and impediments to the growth of Australia's defence exports;
- how Government can better engage and assist Australian defence industry to export its products;
- the operation of the Defence Export Control Office;
- assessment of the export support given to defence industry by governments of comparable nations; and
- any other related matters.

The Sub-Committee invites public submissions addressing the terms of reference for this inquiry. Austal is pleased to provide this submission and sincerely hopes that our input is helpful to the process.

ABOUT AUSTAL

Austal is a global defence prime contractor, designer, and manufacturer of defence and commercial ships. For more than 25 years, Austal has been a leader in the design, construction, and maintenance of revolutionary ships for Governments, Navies and Ferry operators around the world. More than 250 vessels have been delivered in that time.

Austal's business model for being a competitive shipbuilder is based on being capable of winning domestic and export opportunities, which we believe is the only sustainable model for the long-term future of naval shipbuilding in Australia, and the capability it delivers.

Ships

Defence vessels designed and built by Austal include multi-mission combatants, such as the Littoral Combat Ship (LCS) for the United States Navy, and military high-speed vessels for transport and humanitarian relief, such as the Joint High Speed Vessel (JHSV) for the United States Navy and High Speed Support Vessel (HSSV) for the Royal Navy of Oman. Austal also designs, constructs, integrates, and maintains an extensive range of patrol and auxiliary vessels for government agencies globally, including the Cape Class Patrol Boat Program for Australian Customs and Border Protection. Defence vessels are designed and constructed in Mobile, Alabama and in Henderson, Western Australia.

Austal has been at the forefront of the high-speed ferry market since the early days of the industry. Our market leading designs of high performance aluminium vessels have long been at the heart of Austal's research and development. Today, commercial ship construction is centred on our shipyard in Balamban, Philippines.

Systems

Austal has expertise in integrating complex systems into its ships, including ride control, ship management, and communication, sensors, and weapon systems.

Support

Austal provides a wide range of support services, including through life support, integrated logistics support, vessel sustainment and systems support. These services are delivered through our global support network in the USA, Australia, Asia, the Caribbean, and the Middle East together with partner shipyards worldwide.

AUSTAL'S DEFENCE CONTRACTS

Austal has delivered, or has under contract vessels for the following defence and security customers from around the world:

VESSEL TYPE AND QUANTITY	CLIENT	COUNTRY	YEAR OF DELIVERY
8 x 38m Patrol Boats	Australian Customs Service	Australia	1999
7 x 16m Patrol Boats	New South Wales Police	Australia	2000
2 x 22m Patrol Boats	New South Wales Police	Australia	2000
1 x 101m Theatre Support Vessel	United States Marine Corps	Japan	2001
3 x 22m Patrol Boats	Ministry of Interior	Kuwait	2004
1 x Technology Demonstrator	American Marine Holdings	United States of America	2004
10 x 38m Patrol Boats	Ministry of Defence	Yemen	2004
14 x 57m Patrol Boats	Royal Australian Navy	Australia	2005
7 x 16m Patrol Boats	New South Wales Police	Australia	2006
1 x 16m Patrol Boat	Bermuda Police	Bermuda	2006
2 x 65m High Speed Vehicle-Passenger Support Vessels	The Sultanate of Oman (National Ferries Company)	Oman	2008
1 x 127m Littoral Combat Ship	United States Navy	United States of America	2009
6 x 30m Patrol Boats	Trinidad and Tobago Coast Guard	Trinidad and Tobago	2009
3 x 24m Catamaran Patrol Boats	Queensland Police	Australia	2009

VESSEL TYPE AND QUANTITY	CLIENT	COUNTRY	YEAR OF DELIVERY
4 x 22m Patrol Boats	Armed Forces of Malta	Malta	2009
1 x 103m Joint High Speed Vessel	United States Army	United States of America	2012
1 x 127m Littoral Combat Ship	United States Navy	United States of America	2012
2 x 103m Joint High Speed Vessels	United States Navy	United States of America	2013
2 x 103m Joint High Speed Vessels	United States Navy	United States of America	2014
2 x 127m Littoral Combat Ships	United States Navy	United States of America	2015
2 x 103m Joint High Speed Vessels	United States Navy	United States of America	2015
8 x 58m Patrol Boats	Australian Customs and Border Protection Service	Australia	2013/14/16
2 x 103m Joint High Speed Vessels	United States Navy	United States of America	2016
2 x 127m Littoral Combat Ships	United States Navy	United States of America	2016
2 x 72m High Speed Support Vessels	Royal Navy of Oman	Oman	2016
1 x 103m Joint High Speed Vessel	United States Navy	United States of America	2017
2 x 127m Littoral Combat Ships	United States Navy	United States of America	2018

Austal has a regional sales organisation with Regional Sales Managers responsible for all opportunities within their region. These Regional Sales Managers are supported by

centralised Technical Sales Managers and a design development team located at the Henderson Global Headquarters in Australia. These regions include:

- Asia Pacific
- Middle East and North Africa
- Europe and Central/South America

Sales and Business Development in the United States is managed autonomously with a focus on business with the United States Navy (USN) customer.

Also, Austal has been delivering maintenance and repair services to government-owned aluminium high speed vessels in the Sultanate of Oman and in Trinidad and Tobago since 2009 and 2010 respectively.

As with most international companies, Austal maintains a network of relationships in countries of interest, including agency/consultancy agreements where appropriate.

BARRIERS AND IMPEDIMENTS TO GROWTH OF AUSTRALIA'S DEFENCE EXPORTS

Austal has been a successful manufacturer and exporter of Australian designed and built ships for more than 25 years. In recent years Austal has struggled to compete with our international competitors as a result of various market conditions. This situation has not been unique to shipbuilding and has significantly impacted the broader Australian manufacturing industry.

Currency Exchange Rate Influences

Austal was very successful during the late 1990s and early 2000s in a period when the Australian dollar traded in the range of AUD1 = USD 0.5 to 0.65 and AUD1 = EUR 0.55 to 0.65. During the period from 2011 to 2013, the strength of the Australian dollar had a direct impact on the cost of Australian exports. Austal's products effectively increased in cost by 80% for USD contracts and 50% for Euro contracts when compared with the foreign exchange rates mentioned above. While the Australian dollar has eased against the USD and Euro in the past year, it still remains high when compared with historical foreign exchange rates. This has a very direct impact on the international competitiveness of all Australian exporters.

Manufacturing Efficiency

Austal has spent ten years focussed on manufacturing efficiencies and has developed mature and efficient manufacturing processes to help minimise the manufacturing labour required to deliver each vessel. This process has resulted in the development of a mature and efficient modular construction approach known as the Austal Advanced Shipbuilding (ASB) System. ASB is supported by mature design models driving numerically controlled manufacturing processes, to allow the use of less skilled manufacturing labour to deliver complex systems which are strictly in accordance with the approved design configuration.

While Austal has achieved significant efficiency improvements in our manufacturing processes over time, these efficiency gains are quickly offset by the differences in manufacturing labour costs between Australia and other Asian competitors. It is common for Australian labour costs to be more than ten times those of developing countries such as China and Vietnam.

Labour Costs

In recent years Austal has experienced a decline in our ability to compete for commercial business in the international marketplace. This is particularly the case for smaller commercial vessels which can now be manufactured by competitors in countries with a significantly lower labour cost. It is now common for Austal to compete with manufacturers in Vietnam and China. This was one of the key motivations for Austal to establish a shipbuilding facility in the Philippines. Austal Philippines offers an opportunity for Austal to remain competitive in the international commercial vessel market, due to significantly lower labour costs.

Austal intends to continue building more complex defence platforms from our Australian facility, as these vessels require significantly more design, integration and construction expertise than the vessels currently being delivered from Austal Philippines. The direct material cost of naval combatant platforms is far more significant as a proportion of the total direct cost, due to the complex weapons and sensors which are included in these designs. For this reason, the direct labour cost has less influence on the total system cost.

Protected Markets

Austal's most successful market segment in recent years has been our business in the United States. Our original entry into this market was possible due to the high speed vessel technology offered by Austal, which was not available from existing US shipbuilders. Austal was able to establish a shipbuilding capability at a new facility in Alabama in partnership with an existing US shipbuilder, where we initially constructed high speed aluminium commercial vessels. Austal later partnered with a respected US Defence contractor to pursue US Navy opportunities.

The US shipbuilding market is highly protected by the Jones Act in the commercial sector and the Buy America Act in the defence sector. The Jones Act or the Merchant Marine Act of 1920 is a United States federal statute providing for the promotion and maintenance of the American merchant marine. The law regulates maritime commerce in U.S. waters and between U.S. ports and deals with cabotage, requiring all goods transported by water between U.S. ports be carried on U.S. flag ships, constructed in the United States, owned by U.S. citizens, and crewed by U.S. citizens and U.S. permanent residents. The Buy America Act passed in 1933 by Congress requires the United States government to prefer U.S. made products in its purchases and is applied to all USN ship procurements through reference to the appropriate Defence Federal Acquisition Regulation. As a result of this legislation, all naval vessel construction contracts awarded by the United States Navy are awarded to US shipbuilders, resulting in the continuing success of naval shipbuilding in the US.

Austal is an advocate of the free market and competition across the global market; however in the defence sector a free market approach is becoming less and less common. We have explained the situation in the United States which ensures the domestic supply of ships for the USN. It is also true that many first world countries provide direct support to their shipbuilding industry through mandated in-country supply of assets. This support may take the form of legislation, offset requirements, foreign ownership restrictions, or simple preference in the source selection evaluation criteria. In Europe for example it is difficult to conceive that a naval combatant would be procured in the UK from a supplier other than BAE, or in the Netherlands from a supplier other than Damen or in Germany from a supplier other than TKMS or Lurssen. It is also increasingly true that naval procurements in Asia (Malaysia, Indonesia, Thailand, Singapore, Vietnam and India) are all occurring through Technology Transfer arrangements, where domestic shipbuilders are partnering with European shipbuilders to construct combatant platforms in-country. The strategic importance of a domestic naval shipbuilding capability seems clear to most developed countries.

The Australian situation is fundamentally different. The Australian government has not demonstrated an unambiguous desire to maintain naval shipbuilding as a strategic capability for the future. Recent acquisitions have involved the sourcing of designs, ship construction

(ship modules and entire hulls), combat system integration (combat management system development, weapons and sensors) and in some cases entire program procurements offshore. Recent examples of entire capabilities procured offshore include the 90 m naval aviation training vessel and the Submarine Rescue Gear Ship both being built by Damen Shipyards in Vietnam. It has now also been announced that First Pass approval has been granted for Defence to conduct a limited competitive tender process between Navantia of Spain and Daewoo Shipbuilding and Marine Engineering (DSME) of South Korea for the construction of two replacement replenishment vessels based on existing designs. The economic advantages of these decisions needs to be weighed against the long term strategic implications of the loss of domestic naval ship construction capability and any potential export opportunities that may flow from this capability.

Austal's competitive business model has always been based on our ability to win domestic and export opportunities, which is the only sustainable model for the long-term future of naval shipbuilding in Australia. It follows that strong Government support for Australian defence industry exports is a national security issue that warrants considerable co-ordinated effort across government.

Assistance in this domain is therefore not the sole remit of the Defence Department, rather Defence needs to lead and coordinate activity across whole of government to harness a much more focused effort at senior levels of government. On numerous occasions key ministers from various portfolios visit many countries of interest to defence exporters. There is currently no way of coordinating this visit schedule to harness the potential value of this level of support. This lack of coordination is a significant impediment to publicising potential Australian exports. Industry has been left to its own devices and is often a low priority afterthought, when trying to squeeze into a Minister's busy schedule.

Australian senior military officers also have an ideal opportunity to help support the defence industry, particularly through their counterpart visits and their attendance at trade shows. Many other countries, in particular in the UK and Europe do adopt this approach but regrettably defence exports are unlikely to be an objective for Australian senior military officers.

In a number of markets, in particular the Middle East, it is common for Austal to have a significant offset obligation associated with a construction contract. This obligation requires a significant portion of a contract to be expended in the country where the vessel will be delivered. It requires Austal to develop in-country training and in-service support capabilities and in many instances consider a technology transfer arrangement with an in-country partner. While this approach can lead to an artificially inflated purchase price and unsustainable business expenditure in-country, it does ensure that a portion of government procurement expenditure flows back into the local economy. Easy access to relevant bilateral arrangements occurring across government may assist exporting companies to reduce this offset obligation through activities such military training or other forms of investment and make Australian exporters more competitive.

HOW GOVERNMENT CAN BETTER ENGAGE AND ASSIST AUSTRALIAN DEFENCE INDUSTRY TO EXPORT ITS PRODUCTS

From Austal's perspective overt support by government is important for securing business with foreign government customers. Australian Ministerial representation is of much more importance in some countries than others; and Austal appreciates any direct government representation and support when engaging our international customers.

Australian Government ministers and senior officials travel the globe regularly, often to key defence export markets. This activity provides for an opportunity to highlight Defence Export opportunities at many entry points into various government counterparts, Trade, Diplomatic and Defence to name a few. Co-ordination and awareness of these visits is key. Notwithstanding their busy schedules, and often security related limitations on notification of visits, much could be achieved across Government by having key messages and particular products or bids as an objective of any visit. Companies could provide briefs as required

Targeted trade missions would be another positive step. The UK Trade & Investment Defence & Security Organisation is a good model, working closely with both industry and MOD. This organisation uses all the assets at their disposal such as ships, bases and senior officers as part of a coordinated export package. It's in their culture!

The ADF does not use its senior officers to actively publicise Australian companies and sell exports. Every Foreign Service Chief visit could focus on export opportunities as part of the visit agenda, with feedback provided to highlight updates or potential export opportunities.

The European naval shipbuilders have very effectively used defence exports as a key enabling activity for bilateral defence relationships. This contributes to building local operational capabilities in cooperation with partner nations and enhances inter-operability. This is particularly evident in the Middle East with countries like the UK, US, France and Germany all receiving top support from their respective diplomatic corps and senior defence officials.

Austal enjoys good relationships with the DFAT and Austrade representatives where we are most active (and successful recently), specifically the UAE and Oman. As Austal's presence in the Middle East continues to expand, similarly Austal will seek to work closer with DFAT and Austrade in those countries we seek to target.

A drawback today is that some smaller organisations may be dissuaded from engaging Austrade on a regular basis due to the user pays approach which has become more prevalent.

Government support through consular representation and defence attachés (DA) does vary dramatically from region to region depending on the perceived priorities of the particular individuals. For a DA to be effective in support of export opportunities, they need to recognise that representation of Australian industry is a fundamental element of their job description and forms part of the officer's performance appraisal. Specific guidance is required in this regard, lest it be left to individual interpretation. This also requires a sound knowledge of the capabilities of Australian exporters in order to effectively promote those capabilities. This knowledge can only be gained by engagement with industry and ideally

some direct exposure to industry products and services. Some ambassadors visit Austal's yard as part of preparation for their Post. Future Defence Attaches (and senior officers) should also visit industry, not only as part of their own professional development, but to better understand Australian export capability.

Effective marketing can be achieved through advocacy. The Defence Export Unit and Team Defence Australia (TDA) were formed to provide exposure for companies wishing to export. TDA is now an element of the new Australian Military Sales Office (AMSO), and is focussed on supporting exhibitors at various trade shows. Whilst this provides companies a welcome opportunity to exhibit in shows they may not otherwise attend, an increased advocacy role would be a valuable addition to support that activity.

Austal was very encouraged by the recent gifting of Bay Class Patrol Boats to Sri Lanka and Malaysia. Gifting of aging assets needs to be included as a fundamental element of the capability life cycle decision process and can lead to ongoing support contracts for Australian industry. The C130 model, whereby this gifting created in-country support partnerships for Australian companies is a good concept. It also develops stronger regional diplomatic and strategic partnerships between governments. Government support to win an ongoing support contract should therefore be an integral part of any significant gifting program. The risk of not requiring a level of through life support, or technology transfer, is that the products themselves will deteriorate and tarnish not only the company's reputation, but also the governments. Gifting is a very powerful diplomatic and confidence building tool, and needs to be considered as a system. It is also an opportunity to increase Australian industry support opportunities.

THE OPERATION OF THE DEFENCE EXPORT CONTROL OFFICE

The role of DECO from an Austal perspective is to efficiently support the licensing and approval of defence exports. It is noted that the on-line DECO application processes have recently improved and appear to better support the expeditious processing of applications.

The only time where Austal has experienced delays as a result of the DECO process, has related to a request for an Approval-In-Principle to export to a jurisdiction which presented a policy challenge for the Australian Government (Taiwan). DECO relies on inputs from a range of different Commonwealth authorities to process export applications and do not always have visibility or control over the timing of responses. It would be useful for DECO to be able to provide better information regarding the likely time line for approvals and the probability of a successful approval being realised.

The US ITAR licensing process presents its own challenges and in many parts of the world represents a trade barrier for the US defence industry. It is often far cheaper and quicker to avoid US sourced systems due to ITAR restrictions. Australia needs to ensure that DECO remains an enabler to exports.

ASSESSMENT OF THE EXPORT SUPPORT GIVEN TO DEFENCE INDUSTRY BY GOVERNMENTS OF COMPARABLE NATIONS

For a company such as Austal bidding on high value defence opportunities, the support of the Australian Government can be vital and indeed the difference between winning and losing. Many governments view the award of their strategic defence contracts as an opportunity to strengthen relationships, and seek agreements and concessions from the host government.

This is well understood, particularly in Europe and the US, and political capital is often brought to bear in support of business. Many of our competitors particularly the British, French, Italian, Dutch and German organisations receive direct support and representation from all levels of government from their Royal family to Prime Ministers in support of defence sales. This level of support sends a powerful message to prospective customers regarding the level of government faith in the product and support of that product. In the Middle East and North Africa and in Asia this level of government support has led to export success by several European manufacturers.

It is fair to say that since the recent Australian federal election that Austal has enjoyed government support particularly in the Middle East, from the Prime Minister through to travelling Ministers and Parliamentary delegations, however awareness of some of these visits was serendipitous rather than orchestrated. Similarly, the local Embassies and DFAT/Austrade have been supportive of Austal's activities to secure business.

Many governments also offer financial assistance in support of export contracts in the form of gifting of defence assets, low interest or zero interest loans or other government-to-government assistance arrangements. Examples of this direct government support have been seen in Morocco (with the delivery of Damen Sigma Corvettes), Egypt and Iraq (with US foreign military finance assistance) and currently in Israel (with discussion proceeding over the gifting of German F100 frigates). While Austal has worked closely with EFIC in the past, this support tends to be largely on commercial terms without any consideration of the strategic importance of better government-to-government relations with particular potential customers. More could be made of EFIC's offer, including easing limitations on the level of Australian content of a particular product to enable a customer to qualify for financial support. In the case of Austal, EFIC support available to customers for ships built in our Philippines yard is not as attractive as ships built in Australia. However the strategic impact of selling an Australian branded product can be the same, and profits are returned to Australia and reported through ASIC.

Training opportunities are often sought by customers as part of high value contracts. Many customers value the training by high quality Armed Forces. The UK is a good model for this sort of activity. With our own high quality armed forces, any training offered by the ADF as part of a user pays sales package would be highly valued, and would provide a tangible benefit to a prospective customer. Whilst the Services are not sustained to provide external training, Defence has a strong record of international attendance on many of its courses, and opportunities can be met with the right resolve. Such training would not only support industry, it would also enhance government relations bilaterally, and build confidence and understanding between the defence forces. An article highlighting the UK model (RUSI

Defence Systems Autumn/Winter 2011) is attached (Appendix A) as an example of the level of government support the UK defence industry enjoys from its government.

The United States also has a very effective Foreign Military Sales organisation supported by their Defence Security Cooperation Agency (DSCA), with dedicated representation within each US Embassy. DSCA is the central agency that synchronizes global security cooperation programs, funding and efforts across Office of Secretary of Defence, Joint Staff, State Department, COCOMS, the services and US Industry. DSCA is responsible for the effective policy, processes, training, and financial management necessary to execute security cooperation within the US Department of Defence. US Foreign Military Sales opportunities are typically initiated directly with the US government who then manage the procurement of US Defence articles on behalf of the end user. This process ensures that the non-recurring cost of US government programs is amortised across a broader base and that the US suppliers are able to generate export revenue and maintain jobs within the US for the benefit of the broader economy. This role is similar to the objectives of the Australian Military Sales office but it does not appear to have the critical mass to facilitate exporting in a timely manner on a regular basis

OTHER RELATED MATTERS

Austal's defence platforms are often procured by foreign defence organisations well before consideration of the merits of the capability by the ADF. It is worthwhile noting that the export of Australian technology is far more easily achieved when the Australian Government has demonstrated their operational experience and faith in a capability.

Austal's range of platforms for Navy, Coast Guard and Police applications are well suited to high speed intra-theatre security and defence operations. Requirements for patrol, border protection, drug interdiction, fisheries protection and the security of offshore assets are becoming more prevalent in many acquisition programs around the world.

In addition to these security and patrol missions, many navies have recognised the advantage of modular mission capabilities. These mission packages can be exchanged depending on the particular mission requirement, providing a more cost effective and capable platform for a variety of roles. This approach is a key premise for the Littoral Combat Ship program for the USN, where Austal is the prime contractor for a ten ship program.

There is also an increase in the need for high speed logistics vessels for both security and humanitarian missions. The March 2014 award of a contract for two (2) x 72m High Speed Support Vessels for the Royal Navy of Oman, similar in concept to the Austal Joint High Speed Support Vessel (JHSV) being delivered to the USN from Austal's Mobile shipyard, is indicative of the relevance of this type of capability.

From Austal's perspective, our defence products have evolved from our experiences in meeting similar operational requirements for maritime security and border protection, and our commercial products have a strong pedigree in quality, high speed passenger transport which is at the forefront of aluminium shipbuilding technology. We are also continuously broadening of our offering in support of our vessels through life. We hope that the capability of our products will be recognised by the ADF in the same way they have been embraced by the US Navy and other reputable navies.

On the assumption that the Australian home grown product is competitive and suits the need, this serves to increase the prospects of Australian exports as it is in use by a reputable Defence force. Total cost of ownership for the ADF can also be reduced through successful sale of export versions. Importing capability does not achieve these objectives.

Austal is in contract with the Australian Customs and Border Protection Service (ACBPS) for the provision of 8 patrol boats. This submission has been focussed on Defence exports only however that particular contract reveals that other government departments with international relationships can also benefit from export sales opportunities. This scenario reinforces the need for a whole of government co-ordinated approach to defence industry exports. It's bigger than Defence, and requires leadership and accountability across government.

CONCLUSION

Austal enjoys a strong and cooperative working relationship with the Australian government, the ADF and with DFAT and Austrade and are grateful for the role they have played in Austal's success. There are a number of key issues summarised below which would lead to more effective support for Australian defence industry exports:

- Austal's business model for being a competitive shipbuilder is based on being capable of winning domestic and export opportunities, which we believe is the only sustainable model for the long-term future of naval shipbuilding in Australia.
- From Austal's perspective overt support of our products and opportunities through a ministerial level co-ordinated and whole of government approach is important for securing business with foreign government customers.
- The Australian Defence Force does not tend to use its senior officers to actively sell exports, as is the case with some other export competitors. However some of the most effective marketing of Austal's products has been as a result of advocacy by Australian Defence Force (ADF) personnel.
- In order to effectively support Australian defence exports it is essential to have an engaged, educated and enthusiastic diplomatic corps that are willing to represent Australian Industry as a key part of their broader job description.
- There is benefit in offering ADF training as part of a potential export contract.
- The export of Australian products and technology is more easily achieved when the Australian Defence Force has demonstrated their operational use of that capability.

Finally, Austal appreciates the opportunity to present this submission to Trade Sub-Committee and looks forward to reading the outcomes of the inquiry.

Appendix A – UK Ministry of Defence Support to Defence Exports

DEFENCE ACQUISITION

Ministry of Defence Support to Defence Exports

Gerald Howarth, minister for international security strategy, outlines the coalition government's latest work to help cut the deficit through its support to increased defence exports

The UK presence at September's DSEI exhibition in London had considerable ministerial support



When this government came into office, we undertook the Strategic Defence and Security Review, in which we took stock of the changed international scene, reviewed the UK's place in the world and adjusted our Armed Forces to meet these challenges. The task was exacerbated by a £38 billion departmental black hole and a £150 billion national budget deficit spiralling out of control.

The world has moved on from Cold War certainties, making it increasingly important to enhance existing alliances while fostering new ones in the wider interests of promoting regional stability. In my view, defence leverages more influence in bilateral relations than any other area of intergovernmental activity, and defence exports represent a key component in that activity. That is why we announced our coalition policy to increase the level of support to defence exports, which can contribute to regional stability by helping other nations to build up their defence and security capabilities.

Defence exports also bring prosperity to the nation in terms of profits, employment and intellectual property. The defence industry contributes around £6 billion to the economy and employs around 300,000 people, tens of thousands of whom are in highly skilled jobs. They provide our Armed Forces with some of the best equipment on offer. There is also a clear benefit to the public purse, as defence exports also reduce the cost to the taxpayer of Ministry of Defence (MoD) acquisition projects by extending production runs.

Supporting defence exports is a cross-Whitehall endeavour. I have responsibility for defence exports in the MoD, working in harmony with the Defence & Security Organisation (DSO) – part of UK Trade & Investment (UKTI), overseen by Lord Green in the Department of Business, Innovation and Skills (BIS). BIS also leads on export licensing in close consultation with the Foreign & Commonwealth Office (FCO) and MoD. Over the past year, the MoD has sought to provide DSO with comprehensive support.

DEFENCE ACQUISITION

Over the past year in office, led by the Prime Minister, my ministerial colleagues and I have travelled to a number of countries to strengthen our bilateral ties while promoting British defence industry. Selling equipment can help to achieve our defence diplomacy objectives by enabling countries to participate in joint military operations, or help a nation defend itself against mutual potential adversaries. It can also serve to increase influence by building up a trusting relationship with nations that can last for generations.

We also assist UKTI DSO through the loan of military and civilian staff. Some of those military personnel form an Export Support Team in UKTI DSO, who can demonstrate capability to potential customers or provide specialist advice and guidance to industry and overseas buyers. MoD provides demonstrations by the Armed Forces on large, complex platforms, such as Typhoon. In addition, experts from the single Services or Defence Equipment and Support often provide independent information and advice on UK capabilities on behalf of industry. Demonstrating the potential of a capability by our highly skilled Armed Forces is a huge selling point for UK industry, and such support is of vital importance if we are to maintain an edge in an increasingly competitive global market. The reputation of its Armed Forces is undoubtedly a plus factor in helping the UK to win.

Many overseas governments want British military training as part of an export package... It is imperative that we maintain the ability to offer this facility

That is demonstrated by the fact that many overseas governments want British military training as part of an export package. International defence training is something that the MoD offers as part of defence diplomacy initiatives to strengthen cooperation and international partnerships. As Britain's Armed Forces reduce in number, it is imperative that we maintain the ability to offer this facility to our friends and allies, many of whose decision-makers today were trained at Sandhurst, Dartmouth or Cranwell.

I know there is recurring criticism that MoD equipment requirements tend to exceed potential customers' needs or budgets, but we are working to address this issue by embedding exportability into the early phases of the MoD's acquisition cycle. By doing this, we are looking to set requirements that are sufficiently flexible for potential customers, while ensuring that we do not compromise our ability to deliver what the UK needs. For the successful implementation of exportability into the MoD acquisition cycle, we must ensure that industry is conducting robust market research, so we can identify capability gaps within the international market and invite these countries into capability partnerships early on, potentially saving both sets of taxpayers money on research and development and reducing the unit cost by increasing production runs.

Since we have come into office, we have also seen the need for high-level strategic thinking, bringing together all of government to work towards promoting defence exports. That is why the Secretary of State for Defence set up the Defence Exports Support Group. Chaired by him,



the group consists of ministers from the MoD, BIS, UKTI, and FCO, as well as senior officials from UKTI DSO. The group will also be expanded to include ministers from the Home Office for security exports, as security is increasingly seen as the other side of the defence coin. The Group is examining how each of our departments can provide support to exports, as well as addressing some of the barriers that are preventing this government from supporting exports to its maximum potential. This has not been easy in the face of budget cuts and stretched resources, but we recognise the importance of defence exports in reducing our national deficit.

The government is committed to supporting exports, but we are also committed to ensuring that the UK exports responsibly. Government support

DEFENCE ACQUISITION



An AgustaWestland AW159 Wildcat helicopter on display at the DSEI exhibition in September

to specific industry campaigns is set in the context of the Consolidated European Union and National Arms Export Licensing Criteria being in place.

We are encouraged by the progress made in the first year since we took office. We have extended our focus beyond our traditional markets in the United States and the Middle East, and have invested considerable effort in engaging with emerging markets, such as Brazil and India. The Defence & Security Equipment International (DSEI) exhibition in September was a great success, showcasing what UK companies can deliver, supported by an outstanding DSO commitment and a substantial ministerial presence.

We will soon be publishing the Technology, Equipment and Support for UK Defence and Security White Paper, which will contain an export section

that outlines the way in which the MoD will provide support to UKTI DSO in the promotion of defence exports.

While we believe that it has been a good year, we shall not rest on our laurels. As well as serving the interests of Britain's Armed Forces and defence industry, we believe that defence exports can play a major role in helping to generate the growth-led economic recovery that we need. Our defence industry has a world-class capability that is able to contribute to that recovery. In the UK's historic ties around the globe, often dating back centuries, we enjoy an unrivalled network of friends and allies that we can support in terms of exports and in offering partnership and technology. Let us capitalise on these twin advantages. ■