



The future of Australia's steel industry

Submission to the Senate Economics References
Committee Inquiry into the future of Australia's
steel industry and its supply chain

Executive Summary

The Illawarra Business Chamber (IBC) welcomes the opportunity to make a submission to the Inquiry into the future of Australia's steel industry and its supply chain.

A domestic steel industry is vital to the overall Australian economy. It creates jobs, employing approximately 100,000 people nationally¹. The multiplier effect is a significant 3-5 indirect jobs for every direct job generated.

Steel is also the backbone of the Illawarra economy. The BlueScope Steel plant at Port Kembla employs more than 3,200 in its raw steel manufacturing business, with an impact of approximately \$2.572 billion per annum, after taking into account all direct, indirect and consumption effects.

In addition to its economic benefits, the Australian steel industry provides a safe, high quality and consistent supply of products for critical infrastructure. Both BlueScope Steel and Arrium produce their products in conformance with Australian Standards.

Steel in Australia has, however, undergone a significant decline. Market factors such as high input costs, price volatility and anti-competitive policies by foreign governments have had a negative impact on the competitiveness of our domestic steel industry.

The IBC is calling on the Federal Government to secure the future of steel in Australia by adopting the following strategies:

- **Recommendation 1:** Require government suppliers to conform to quality standards for steel
- **Recommendation 2:** Enhance local content procurement through better engagement, reporting, and publicising the employment, skills and technology outcomes of public infrastructure projects
- **Recommendation 3:** Encourage State and Territory Governments to use Industry Participation Agreements

This Inquiry is also an opportunity to encourage the Federal Government to further the aims of its *National Innovation and Science Agenda*. While we want the steel industry to continue as an economic force, more needs to be done to develop new, emerging industries.

We therefore recommend the Inquiry:

- **Recommendation 4:** Support economic diversification by building entrepreneurship, boosting small business research and investing in infrastructure

Adoption of the diversification strategies we have proposed will assist the Illawarra to generate new jobs, growth and create a sustainable economic future.

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¹ Australian Bureau of Statistics (2011)

About us

IBC is a regional division of the NSW Business Chamber, the state's peak business organisation. The IBC is also represented on the NSW Business Chamber State Council, and in turn at a Federal level through the Australian Chamber of Commerce & Industry (the Australian Chamber).

We are the leading voice for business in the Illawarra, supporting more than 1,300 unique businesses across the local government areas of Wollongong, Shellharbour, Kiama, Shoalhaven and Wingecarribee. Many of our members are directly or indirectly involved in the steel supply chain.

Part 1: The importance of a domestic steel industry

Economic benefits

Australia's domestic steel industry has two principal centres: Port Kembla, home of the BlueScope Steel plant in the Illawarra, and Whyalla, the location of the Arrium plant in South Australia.

The industry creates a significant number of direct jobs, employing approximately 100,000 people nationally². The indirect impact is still greater, with the multiplier effect estimated from 3 to up to 5 indirect jobs for every direct job generated.

Steel has been the backbone of the Illawarra economy for more than a century. The BlueScope Steel plant at Port Kembla, which produced its first steel in 1928, is the nation's largest, with capacity to make 2.6 million tonnes of raw steel every year. Approximately 3,200 direct employees are involved in the raw steel manufacturing component of BlueScope's business, in addition to its contract workforce.

Analysis conducted by Wollongong City Council estimated the impact of this aspect of BlueScope's business at \$1.916 billion per annum (without taking into effect the multiplier effects)³. This impact would increase to approximately \$2.572 billion per annum, after taking into account all direct, indirect and consumption effects.

The steel industry as a whole is supported by a supply chain of more than 200 distribution outlets, as well as a vibrant fabrication and advanced engineering sector⁴. These businesses service customers in a variety of industries in Australia and in export markets, such as construction, transport, energy and agriculture.

This supply chain is complicated and there are difficulties in accurately assessing its impact. This complexity is demonstrated by the vast difference in estimates of the employment impact of Illawarra's raw steel production operations, which vary from 5,000 to 10,000 jobs⁵.

Assessing whether impacts are direct or indirect is a particularly difficult exercise. For example, one of IBC's members employs 100 people who are 100% reliant on BlueScope continuing raw steel operations as they form a part of the actual raw steel operations. Whether this equates to a direct jobs impact, or indirect, is unclear.

While Wollongong is transforming into a more service-based knowledge economy, manufacturing as a whole remains the most important sector in terms of output, contributing approximately \$7.9 billion in annual revenue toward the total gross regional product (GRP) for the Illawarra of \$18.6 billion⁶.

² Australian Bureau of Statistics (2011)

³ REMPLAN (2015)

⁴ Australian Steel Institute (2015), Capabilities of the Australian steel industry to supply major projects in Australia, p. 3.

⁵ There have been two assessments of the impact. Research by the University of Wollongong (2015) assessed the employment impact of 10,000 jobs and \$3.3 billion loss to gross regional product. In August 2015 BlueScope estimated withdrawal from direct steel supply at Port Kembla would result in approximately 5,000 direct and indirect job losses.

Manufacturing is also the second largest employer regionally, with more than 8,500 people engaged in the industry. This equates to approximately 12% of the region's total workforce⁷.

Strategic benefits

There are several strategic reasons why the Federal Government should take steps to retain a domestic steel industry in Australia:

Quality

Purchasers of steel products must have assurance that they have been manufactured to a high quality standard, and are safe for use. This is particularly the case given their use in applications with high-stakes safety concerns, such as building and construction.

The most effective way to gain this assurance is to procure steel products that have been manufactured by a supplier with a robust quality management system in place, and complies with the relevant Australian Standards. Rigorous standards have been developed for each process in the steel supply chain.

Both BlueScope Steel and Arrium, the two steel manufacturers in Australia, produce their products in compliance with these standards. BlueScope's steel products have also been certified by the two primary organisations which audit the quality of steel processes and products⁸.

High volumes of non-compliant imports from China, however, are placing pressure on these domestic manufacturers. Australian steel companies are often locked out of lucrative contracts due to an undue emphasis on upfront costs, rather than whole of life costs. Competitors are able to offer a lower price point, in many cases due to savings achieved through not meeting the rigorous requirements of Australian Standards⁹.

Yet poorly manufactured, nonconforming steel products place significant cost burdens on the purchaser. Failed products, components and infrastructure:

- cause project delays due to the need to rework steel components
- substantially increase the whole of life cost, due to the burden of increased maintenance and repairs¹⁰.

Where the purchaser of low quality steel products is the Australian Government, the cost is to the economy – and the public – as a whole.

Skills retention

The Australian manufacturing industry is innovative, contributing more than 25% of its business expenditure to research and development¹¹. Data concerning research and development expenditure by steel manufacturers was not available at the time of writing, however it is expected that it is in line with the industry average.

Steel is a particularly skilled sector, employing engineers, highly trained tradespeople and scientists. The loss of these skills and the opportunities they bring for further innovation could be a significant negative.

⁶ REMPLAN, (2015)

⁷ Ibid.

⁸ The Australasian Standards Certification & Verification of Reinforcing, Prestressing & Structural Steels (ACRS) and the Australian Technical Infrastructure Committee (ATIC).

⁹ Ryan, D. and Cairns, I. (2015). *Non-Conforming Product Submission*, Australian Steel Institute, p.9

¹⁰ Ibid, p. 13

¹¹ Department of Innovation, Industry and Science. (2015). *Manufacturing Industry Report Card*, p. 2.

Part 2: The current situation

Despite its strategic and economic importance, the future of steel in Australia is uncertain.

The global economy is increasingly competitive, and steel markets have been volatile. World steel consumption and production declined in 2015. Consumption fell by 1.7% to 1.6 billion tonnes; while production declined by 1.9%, mainly due to lower output by China, the United States and Japan¹². The outlook for 2016 is subdued, with consumption expected to increase by 0.9% globally, and production to remain at current levels. The forecast for Australia is more sobering, with steel production expected to reduce by 6.2% due to global competition¹³.

Australia has been rated one of the world's freest economies: an assessment the IBC welcomes¹⁴. At the same time, the low barriers to entry into Australian markets mean that global pressures have had a significant impact on the domestic steel industry's competitiveness:

- **High input costs:** The high Australian dollar has driven increased production costs, including for key input commodities such as iron ore and coal.
- **Market distorting policies:** Market distorting policies by governments in competitor countries have also had a negative impact on the domestic steel industry. China, the main global supplier of steel products, has been a net exporter of steel since 2005 and its production capacity has only recently peaked. Chinese producers have been supported by policies designed to increase their market share. These include favourable tax treatment, generous subsidies, as well as targeted research and development incentives designed to retain specialist manufacturing skills onshore.
- **Price dumping:** Dumping involves exporting a product for a price below its cost of production, or price in the location of manufacture, with the intention of rapidly driving down prices in competitor markets and rapidly increasing market share. There is evidence that foreign steel companies, including competitors in China and South Korea, have engaged in illegal dumping. The recent introduction of anti-dumping legislation by the Federal Government is a welcome remedy to this issue.
- **Volatility in the price of hot rolled coil:** Dramatically increased steel output (particularly from China) has driven down the price of hot rolled coil from \$US300 per tonne in 2010 to approximately \$200 per tonne in 2015.

In combination, these factors have dramatically eroded profit margins. BlueScope Steel reported in July 2015 that its steel exports were making a loss. While BlueScope decided in October 2015 to continue raw steel production, this was achieved through cost savings including the reduction of 500 jobs.

The job losses at BlueScope are very concerning. Unemployment in the Illawarra is a disproportionate 7.6%, well above the national average, while workforce participation is only 51.2% below a national rate of 61.4%.

A continued decline in steel could cement already high levels of unemployment and disadvantage, unless alternate industries develop a presence.

¹² Office of the Chief Economist. (2015). *Resources and Energy Quarterly - December Quarter 2015*. Department of Innovation, Industry and Science, p. 12.

¹³ Ibid, p. 13.

¹⁴ World Economic Forum. (2015). *Global Competitive Index – Australia*

Part 3: Recommended response from Government

The IBC believes that manufacturing is a vital segment of the Australian economy, and should remain so. This view has been affirmed by our members in a recent policy survey.

We are nevertheless committed to the free market. We believe this provides the best environment for innovation, opportunity and growth.

Action by the Federal Government to retain this industry and secure its supply chain should, therefore, be guided by these principles:

- The market should remain **competitive**
- The steel industry should operate on a **level playing field**
- Steel products used in Australian public projects should be **high quality and safe**.

We recommend the Senate Economics Committee consider four strategies that align with these principles.

Recommendation 1: Require government suppliers to conform to quality standards for steel

As mentioned in Part 1 of this submission, Australia has a strong and well developed standards and conformance framework for the range of processes involved in the steel supply chain. Compliance with this framework is, however, not mandatory and inferior steel imports continue to be used, even in public infrastructure initiatives.

Allowing optional non-conformance puts products that choose to meet Australian standards at a competitive disadvantage, and exposes Government initiatives to safety and quality risks. Using non-compliant products increases the whole-of-life cost, placing an unacceptable burden on the economy.

The South Australian Government has sought to remedy this disparity, announcing in December 2015 that every government procurement activity involving steel would be required to demonstrate the steel had been independently certified as meeting the relevant Australian Standard.

To build confidence in the system and ensure steel manufacturers who comply with the Australian Standards are not disadvantaged, the Inquiry should recommend that all Federal Government procurement initiatives mandate the use of steel meeting Australian quality standards. This must be complemented with a strong system of auditing and policing to ensure conformance.

These measures will ensure that new infrastructure projects meet the public's expectations concerning safety, quality and risk mitigation.

Recommendation 2: Enhance local content procurement through better engagement, reporting, and publicising the employment outcomes of public infrastructure projects

The Government should maximise opportunities for Australian firms, including those in the Illawarra, to participate in public projects. Steel is a critical input for infrastructure projects ranging from road and rail initiatives, to schools, hospitals and energy projects.

Some stakeholders have proposed mandatory local content procurement targets. The IBC is of the view this would be anti-competitive.

However, we propose the Federal Government consider the adoption of measures that will promote greater communication and transparency on the use of local content by its agencies. These include:

- identify and communicate potential opportunities to local businesses throughout the supply chain;
- annual reporting on the levels of local content and employment procured; and
- publicising the anticipated training, skills development and technology transfer outcomes of major infrastructure initiatives.

These strategies would help promote local business and employment growth by amplifying their market access, while ensuring that the involvement in Government infrastructure initiatives remains competitive.

Recommendation 3: Encourage State and Territory Governments to use Industry Participation Plans

We also recommend the Federal Government encourage State and Territory Governments to adopt Industry Participation Plans for initiatives of more than \$100 million, particularly for joint Federal-State projects.

Under this approach, prime contractors would develop plans in collaboration with the Industry Capability Network, in accordance with the following principles:

- Local small and medium enterprises should be provided with a full and fair opportunity to compete for government contracts;
- Local industry engagement should extend to all levels of the procurement supply chain, not just lead contractors;
- Information on the procurement pipeline should be freely available and communicated, so that local industry can plan ahead and be involved; and
- All government tendering mechanisms should be open, clear, accountable and minimise tendering costs.

As with the local content procurement strategies we have recommended for the Federal Government (**Recommendation 2**), Industry Participation Plans increase the effective participation of manufacturers in Government procurement opportunities by outlining:

- measures for identifying and communicating with local businesses in the supply chain;
- anticipated levels of local content and employment, including apprentice/learning workers; and
- skills development and technology transfer outcomes.

Industry Participation Plans create an incentive for prime contractors to commit to the use of competitive local suppliers. By encouraging the utilisation of the ICN, the process should minimise regulatory burden and be easy to comply with. The quality of the plan and its outcomes should also be part of the tender evaluation and monitoring criteria.

In undertaking this initiative it is imperative that the principle of maximising value for money over the life of the product or infrastructure be calculated and form a strategic component of the evaluation by Government of any relevant tender. Both the initial contract cost and whole of life costs including training, operation, equipment and facility downtime, ongoing maintenance, disposal and ongoing administration costs should be fully evaluated to justify tender selection.

Recommendation 4: Supporting economic diversification into new industries

The IBC has long advocated with the Federal Government for measures to diversify the Illawarra economy. While the steel industry will remain a mainstay, new industries must develop if we are to have a sustainable economic future.

In September 2015, when the continuation of BlueScope Steel's operations at Port Kembla was uncertain, we partnered with Ai Group in a submission offering a comprehensive suite of strategies to support this transition (**Appendix A**).

Further advocacy with the Federal Government in the following months led to the announcement of a \$972,000 structural adjustment package to reskill retrenched workers and assist them to find and transition to new employment. The Federal Government also announced in December its *National Innovation and Science Agenda* (the Innovation Agenda).

More needs to be done, however, to grow new sectors, build skills and foster innovation. While the Innovation Agenda is an ambitious plan, further work is needed to encourage start-ups, entrepreneurs and creative business ideas in regional centres.

We advocate the following:

- **Restore the three Entrepreneurial Advisors** which were withdrawn from the Illawarra in June 2015. These resources would empower local businesses to explore new products and services, serving as critical supports for the diversification process. (See attachment 2).
- **Invest in a Small Business Innovation Research program** to encourage collaboration between SMEs and research providers to develop solutions to meet the needs of Government agencies. We are seeking an initiative similar to that being undertaken in South Australia.
- Invest in and commit to timeframes for key infrastructure, including:
- Gateway to the South - M1 (F6) Extension
 - Complete the extension of the freeway between Waterfall and St Peters by 2020
- Mainline Acceleration Program 60 minute travel time on the Illawarra Rail Line
 - Complete engineering upgrades to resolve structural issues on the Wollongong to Sydney rail line
 - Invest in targeted works on speed restriction and pinch points by 2019
 - Commit to \$1 billion in capital works by 2024

A priority for the Federal Government is to create an environment where businesses continually identify new, creative products and services. Investment in these resources would strongly align with this objective – equating to a hand up, not a hand out for business.