



Australian Government
Productivity Commission

Australia's Automotive Manufacturing Industry

Productivity Commission Position Paper

January 2014

This is a position paper prepared for further public consultation and input. The Commission will finalise its report after these processes have taken place.

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The Productivity Commission

The Productivity Commission is the Australian Government's independent research and advisory body on a range of economic, social and environmental issues affecting the welfare of Australians. Its role, expressed most simply, is to help governments make better policies, in the long term interest of the Australian community.

The Commission's independence is underpinned by an Act of Parliament. Its processes and outputs are open to public scrutiny and are driven by concern for the wellbeing of the community as a whole.

Further information on the Productivity Commission can be obtained from the Commission's website (www.pc.gov.au) or by contacting Media and Publications on (03) 9653 2244 or email: maps@pc.gov.au

Opportunity for further comment

You are invited to examine this position paper and provide written comment or attend a public hearing. The deadline for all written submissions is Thursday 13 February 2014. The Commission will hold public hearings during February 2014.

The final report will be prepared after submissions have been received and public hearings have been held, and will be forwarded to the Australian Government in March 2014.

Further information on how to provide a written submission or register your attendance at the public hearings (as a participant or an observer) is available on the inquiry website www.pc.gov.au/projects/inquiry/automotive.

Public hearing dates and venues

<i>Location</i>	<i>Date</i>	<i>Venue</i>
Melbourne	Wednesday 19 February 2014	Productivity Commission - Rattigan Room Level 12, 530 Collins St, Melbourne
Adelaide	Thursday 20 February 2014	Stamford Plaza Hotel – Boulevard Room 150 North Terrace, Adelaide

Terms of reference

REVIEW OF THE AUSTRALIAN AUTOMOTIVE MANUFACTURING INDUSTRY

Productivity Commission Act 1998

I, Joseph Benedict Hockey, Treasurer, pursuant to Parts 2 and 3 of the Productivity Commission Act 1998, hereby request that the Productivity Commission undertake an inquiry into public support for Australia's automotive manufacturing industry, including passenger motor vehicle and automotive component production.

Background

Australian and State Government support for the automotive manufacturing industry is provided through the current Automotive Transformation Scheme, which provides assistance in respect of production and support for research and development and capital investment, through ad hoc grants provided to vehicle and component manufacturers, through tariffs and through relief from some state taxes.

With the withdrawal of some manufacturers from local production in Australia, recent uncertainty surrounding tax policies affecting the industry, variability in exchange rates and the increasing openness of Australia's automotive retail market, the circumstances under which assistance is provided to the industry warrant review.

Scope of the Inquiry

The Australian Government desires an internationally competitive and globally integrated automotive manufacturing sector and wishes to ensure that any support for the local automotive manufacturing industry is accountable, transparent and targeted at the long-term sustainability of the sector. In consultation with a broad range of stakeholders, and in the context of the Australian Government's desire to improve the overall performance of the Australian economy, the Commission should, in its Review of the Australian Automotive Manufacturing Industry (the 'Review'):

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1. Examine national and international market and regulatory factors affecting:
 - the Australian automotive manufacturing industry’s current structure, productivity, investment, profitability, international competitiveness, exports, workforce structure and practices, skills levels and long-term sustainability;
 - Australia’s attractiveness as an investment location for all phases of automotive manufacturing activity, from research and development through to production of components and vehicles;
 - domestic and international demand for Australian design and engineering services, vehicles and automotive products; and
 - consumer preferences, including consumer demand for new products and technologies.
 2. In examining these factors, take into account the following matters:
 - international automotive industry assistance arrangements, including reporting on and quantifying tariff, non-tariff barriers and budgetary assistance provided by major and emerging automotive-producing countries and the barriers and opportunities for Australian manufacturers and suppliers;
 - the impact of current workplace arrangements in the industry, domestic industry assistance, government vehicle purchasing policies, the Government’s broader deregulation agenda and the taxation environment (noting fair work laws and taxation reform are subject to separate comprehensive review processes); and
 - the spill-over benefits of the automotive sector, such as technology diffusion.
 3. Taking into account all of the above, identify and evaluate possible alternative public support mechanisms that:
 - improve the long-term profitability, sustainability and productivity of the industry;
 - facilitate research into, and the development of, innovative alternative vehicle and component technologies by the industry;
 - contribute to national productivity growth;
 - promote mutual obligation, accountability and transparency; and
 - are consistent with Australia’s international trade obligations.

Including:

- retargeting of assistance, including within the Automotive Transformation Scheme; and

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- introducing more internationally-competitive workplace, regulatory and taxation policies; and
 - identifying any significant transition issues or adjustment costs that may arise from alternative support mechanisms or policy changes and how they might be best managed.
4. Assess the significance of the capabilities within the industry, its direct employment and economic benefits, its secondary impacts on other sectors of the economy, and quantify the costs and benefits, including at the economy-wide and regional level, of existing and alternative assistance mechanisms.

Process

The Commission is to undertake an appropriate public consultation process, inviting public submissions and releasing a preliminary findings report to the public.

The preliminary findings report should be released by 20 December 2013, with the Final report due to the Government by 31 March 2014.

J. B. HOCKEY

Treasurer

[Received 30 October 2013]

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OVERVIEW

Key points

- Australia's automotive manufacturing industry is undergoing significant change.
 - Ford and Holden announced their manufacturing plants will close by 2016 and 2017. Toyota will decide this year on the production of the next generation Camry.
 - A number of component manufacturers and employees will be affected.
- The policy rationales for specific assistance to automotive manufacturing are weak. The community would benefit from the ending of assistance to automotive manufacturing through the Automotive Transformation Scheme (ATS).
 - There is no compelling evidence that spillover and multiplier benefits exceed the costs of assistance to the industry.
 - Decades of transitional assistance have forestalled but not prevented the structural adjustment now being faced by the industry.
 - Assistance imposes costs on the community and dulls incentives to improve productivity, seek export opportunities, and diversify into other industries.
- Current government funding should be reassessed to determine when subsidies should end, and whether to change the timing and amount of funding withdrawn from the ATS.
 - ATS funding for Toyota and other eligible businesses should cease in 2020, and not be extended or replaced with other specific assistance.
 - The closures of the Ford and Holden plants are expected to contribute to an underspend of \$380 million under the legislated ATS funding schedule by 2020.
 - The effect of the uneven profile of funding as outlined in the MYEFO estimates is unclear. It could elevate risks of earlier plant closures by Ford and Holden and might negatively affect investment decisions by Toyota and its component suppliers. A smoother reduction profile would delay the savings benefits, but may reduce adjustment costs.
 - The amount of funding withdrawn from the ATS set out in the MYEFO could result in adjustment costs greater than the savings benefits. Further feedback is sought.
- Firms remaining in automotive manufacturing would benefit from broadly based economic and regulatory reforms and greater workplace flexibility.
- Structural change is often costly for retrenched employees and their families, and may involve job search and training costs, and lead to lower paid or less secure jobs.
 - Some employees of component manufacturing firms may warrant particular consideration if generally available measures appear to be insufficient.
- Loss of employment and economic activity will be concentrated in some regions, with some already having relatively high rates of unemployment and disadvantage.
 - Generally available welfare, employment and training services should be relied on in the first instance, and need to be adequately resourced in the affected regions.
 - Regional adjustment programs can be of limited value. Infrastructure investment and labour adjustment programs, where warranted, need to be designed in ways that generate net benefits for the community as a whole.
- Given the advanced notice of Ford and Holden plant closures, there is time to learn from previous adjustment programs. The Commission is seeking further input.

Overview

Australia's automotive manufacturing industry has undergone considerable structural change over recent decades and further change is occurring. Ford and Holden have announced their intentions to close their automotive manufacturing plants in Australia by 2016 and 2017 respectively. Toyota Australia has indicated that a decision whether to proceed with the Australian production of the next generation Camry will be made in 2014.

The Australian Government has asked the Productivity Commission to undertake an inquiry into the automotive manufacturing industry. The announced closures, and their potential flow-on effects throughout the industry, set the context for the Commission's analysis and its recommendations for future policy settings. The terms of reference for this inquiry require the Commission to:

- assess the significance of the capabilities within the industry, its direct economic benefits, and its secondary impacts on other sectors of the economy
- examine national and international factors affecting the industry
- identify and evaluate possible alternative public support mechanisms
- identify any significant adjustment costs that may arise from alternative support mechanisms or policy changes, and how they might be best managed.

Given the geographic concentration of automotive manufacturing in several regions of Victoria and South Australia, the Commission has also given close attention to the economic and social dislocation facing those particular workforces and regions that may arise as a consequence of structural change in the industry.

The scope of the inquiry

This inquiry will cover the automotive manufacturing industry supply chain in Australia, including:

- motor vehicle producers that manufacture passenger motor vehicles (and engines), light commercial vehicles (including sports utility vehicles) and heavy commercial vehicles (including buses and trucks)
- automotive component manufacturers that supply parts for the production of motor vehicles or the aftermarket

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- providers of services and specialist skills that support the automotive manufacturing industry such as design, research and development, tooling, engineering and production services.

The position paper deals predominantly with the producers of passenger motor vehicles and light commercial vehicles and their associated components and services, not heavy commercial vehicles (buses and trucks) as this latter segment is not a direct beneficiary of industry-specific government assistance.

The Commission's approach

The Commission released a preliminary findings report on 20 December 2013, which examined the local and global factors affecting the automotive manufacturing industry in Australia.

This position paper examines whether there is a case for ongoing industry-specific support to the Australian automotive manufacturing industry, over and above that which is generally available to all industries. This paper also explores the effect of structural adjustment on the workforce, and evaluates options for assistance beyond those provided by the generally available social safety net.

The Commission has taken an economywide perspective when considering the potential costs and benefits of current (and potential future) government assistance to the automotive manufacturing industry.

The Commission has consulted as widely as possible given the compressed timetable for this inquiry. It has met with stakeholders, received submissions, and held public hearings in Adelaide and Melbourne. The Commission is inviting further submissions in response to the draft findings and proposals in this position paper, and will hold further public hearings in February 2014. Also in February 2014, the Commission expects to release the interim results of quantitative modelling which considers the economywide and regional effects of industry adjustment. A technical roundtable on this analysis will be held in early March 2014.

The contributions of inquiry participants and the Commission's further analysis will inform the Commission's final report and recommendations, which will be delivered to the Australian Government by 31 March 2014.

Factors affecting automotive manufacturing in Australia

The Commission's key findings from its preliminary findings report are set out in box 1. The report identified: the global move to production in regions of high demand growth and low labour costs; the importance of scale economies; the high costs of domestic production; the highly competitive domestic market in Australia; and the challenges for firms of competing with affiliates in global companies for corporate investment capital, and for the opportunity to supply export markets.

Structural change in the Australian automotive manufacturing industry

Over recent decades, the Australian automotive manufacturing industry — the manufacture of cars, trucks and buses, as well as automotive engines, automotive components and products for the automotive aftermarket — has undergone significant structural change. This has been in response to changing market and competitive conditions overseas and in Australia, and lower levels of government assistance. Since 2006, Mitsubishi has closed its Australian manufacturing operations and the total number of vehicles produced in Australia has reduced from around 300 000 in 2006 to around 200 000 in 2013. The number of firms that manufacture automotive components has also fallen.

Employment in automotive manufacturing decreased by about 40 per cent over the period 2006 to 2013 — around 44 000 people in Australia were employed in the industry in 2013.

Further industry adjustment will occur

Further reductions in employment in automotive manufacturing will occur over the next few years following announcements by Ford and Holden that they plan to cease vehicle assembly and engine manufacturing in Australia. Their plant closures will directly displace about 1600 employees in South Australia and 2500 employees in Victoria.

The decision by Toyota Motor Corporation in 2014 as to whether Toyota Australia can proceed with plans to produce the next generation Camry model in Australia will be an important factor influencing the scale, timing, and location of further reductions in employment in automotive manufacturing. Around 2500 people are directly employed in manufacturing at Toyota's vehicle assembly and engine manufacturing plant in Victoria.

Box 1 Key points from the Commission's preliminary findings report

- Global forces are driving (and are likely to continue to drive) dramatic changes in both the demand for motor vehicles and the size, scale and location of production.
- At a global level, production capacity exceeds demand for motor vehicles.
 - Demand in a number of developed economies has been slow to rebound from the global financial crisis, and many assembly plants are operating below capacity.
 - Significant rationalisation of production capacity has occurred in the US, and further assembly plant closures have been announced in the UK and Belgium.
 - Vehicle manufacturing capacity is shifting to regions with lower labour costs and high demand growth such as China, Eastern Europe, India, Mexico and Thailand.
 - Many governments provide financial or other support to attract (or retain) an automotive manufacturing industry.
- There is relentless pressure on vehicle producers worldwide to reduce manufacturing costs, particularly in the small to medium size car, high volume, market segments.
 - The selling prices for vehicles in such segments of the new car market are held down by fierce competition from local suppliers and importers.
 - Affiliates within international firms compete for the right to produce models built on global platforms — for supply to both domestic and export markets.
 - Cost pressures extend to component manufacturers throughout the supply chain.
- Production scale and labour costs are key drivers of automotive manufacturing costs.
 - All vehicle manufacturers in Australia are producing well below the 200 000 to 300 000 vehicles needed annually for an assembly plant to be cost competitive.
 - Labour costs in automotive manufacturing are substantially higher in Australia than in countries such as China and Thailand.
 - Despite continuing efforts by vehicle producers and their employees, a substantial cost gap between Australian and many overseas assembly plants remains.
- Increasing vehicle production in Australia, for local supply or export, is challenging. Vehicle producers in Australia have been losing local market share.
 - The Australian new car market is small by global standards. It is highly competitive, to the benefit of Australian consumers, but is fragmented. Top selling models enjoy sales of only a little over 40 000 vehicles a year.
 - Export opportunities are limited by the high costs of production, the sustained high Australian dollar, competition, and continuing barriers to trade.
- Global trends place ongoing pressure on Australian automotive component suppliers.
 - Component manufacturing in Australia is high cost compared to countries such as China and India. Motor vehicle producers in Australia are increasingly sourcing automotive components from overseas.
 - Vehicle producers increasingly require their key component suppliers to have a global presence and be located near major production regions.
 - The greater use of global platforms may lead to opportunities for some Australian component suppliers, but may lead to the closure of others.
- Australian governments have provided capital grants and subsidies to automotive manufacturers, and transitional assistance intended to facilitate industry adjustment.

Structural adjustment pressures go beyond motor vehicle assembly operations

A complex supply chain supports motor vehicle assembly and engine manufacturing. It includes component manufacturers, the suppliers of products such as steel and paint, and providers of automotive research and development, design and engineering services.

As a consequence of changing market conditions, some component manufacturers have already closed or have undergone considerable structural adjustment by diversifying into other industries or into export markets. Others remain reliant on passenger vehicle production in Australia for their business and will be heavily affected by the announced closure of the assembly and engine manufacturing plants. For example, TI Automotive, a subsidiary of a specialist global firm, noted that its Australian operations are entirely dependent on the assembly of passenger vehicles in Australia. Further rationalisation of the number of automotive component firms will occur, which will lead to job losses.

Other segments in the automotive manufacturing industry in Australia are less vulnerable to the announced closures. These segments include the aftermarket parts manufacturers and producers of trucks and buses.

There are an additional 233 000 or so people employed in the repair, maintenance and retailing of motor vehicles and parts (as distinct from the development or production of motor vehicles, engines or automotive components). This workforce is largely independent of, and not significantly influenced by, the degree of automotive manufacturing in Australia.

Is further industry-specific assistance warranted?

A number of inquiry participants considered that governments should provide ongoing industry-specific assistance to automotive manufacturing. Some argued for an extension of the current transitional assistance measures such as the Automotive Transformation Scheme (ATS) (in some cases with changes to their design) and others proposed new initiatives to provide ongoing support to automotive manufacturing.

In part, participants argued that Australia benefits from these assistance schemes through access to ‘spillovers’ from the automotive industry — such as its advanced manufacturing techniques. A further argument is that industry-specific assistance can help reduce or avoid the costs associated with structural adjustment, including those costs arising from lower levels of employment in automotive manufacturing. These arguments are explored below.

Current assistance arrangements for automotive manufacturing

Following a number of earlier transitional assistance plans, the Australian Government announced *A New Car Plan for a Greener Future* (the New Car Plan) in 2008. The plan introduced a number of budgetary assistance measures designed to offer further transitional support to the automotive manufacturing industry over the period from 2008-09 to 2020-21. Current budgetary assistance to the automotive manufacturing industry is outlined in box 2.

Assistance is also provided to the automotive manufacturing industry through government preferential purchasing policies and generally available Australian Government assistance measures, such as tax concessions for eligible research and development activities and export facilitation programs. Other policies affecting the automotive industry include restrictions on the importation of second-hand vehicles and taxation arrangements, such as the luxury car tax.

Automotive manufacturing remains one of the most heavily assisted industries in Australia. The Commission estimates that the equivalent of around \$30 billion (2011-12 dollars) was provided to the industry between 1997 and 2012 in the form of tariffs and various subsidies. The estimated effective rate of assistance provided to the automotive manufacturing industry — the value of assistance as a proportion of a particular industry's (unassisted) value added — was 9.4 per cent for 2011-12. (The effective rate of assistance to manufacturing in total — inclusive of automotive — was 4.1 per cent, and the effective rate of assistance for mining was 0.3 per cent in the same year.) An increasing share of assistance to the automotive manufacturing industry over recent years has been in the form of budgetary (rather than tariff) assistance.

Possible rationales for industry-specific assistance

There are four broad rationales given for assistance to automotive manufacturing. They are:

- spillover benefits
- industry linkages (or 'multipliers')
- the effect of automotive assistance arrangements — in Australia and in relation to assistance offered in other countries — on Australia's attractiveness as an investment location
- the need to counter temporary pressures that threaten the viability of the industry — such as the strength of the Australian dollar.

Box 2 Current budgetary assistance to automotive manufacturing

Current budgetary assistance programs for the automotive manufacturing industry include the following.

- The Automotive Transformation Scheme (ATS) — scheduled to run from 2011 to 2020 — provides assistance in the form of cash payments to registered participants against their eligible automotive production, plant and equipment investment, and research and development expenditure. ATS assistance is divided into a capped part that is subject to annual limits, and an uncapped part. The total amount of legislated capped assistance under the ATS is \$2.5 billion, which is spread across the two stages of the scheme (Stage 1 runs from 2011–2015 and Stage 2 from 2016–2020). The ATS includes a provision that allows for unallocated funding to be rolled forward to the annual caps in future years. However, unallocated funding cannot be rolled forward from Stage 1 to Stage 2 of the ATS. The 2013-14 Mid-Year Economic and Fiscal Outlook included a pre-announced saving of \$500 million from the capped part of the legislated ATS between 2014-15 and 2017-18. It is expected that around \$330 million of uncapped assistance will be provided over the life of this part of the scheme, which terminates in 2017.
- The Green Car Innovation Fund (with an original budget of \$1.3 billion) provides grants for research and development and early-stage commercialisation of projects that reduce the fuel consumption and greenhouse gas emissions of motor vehicles. The fund is scheduled to make its final payments in 2014-15.
- The Automotive New Markets Initiative — scheduled to run between 2012-13 and 2015-16 — was introduced with \$35 million of funding from the Australian and Victorian governments. Funding was increased to \$47 million as part of the two governments' response to Ford's announcement that it would cease manufacturing in 2016. Most of this funding will be allocated through the Automotive New Markets Program, which has a budget of \$42 million and provides grants of up to \$1 million for firms in the automotive supply chain to broaden their customer and product base.

In addition, the Australian Government announced capital subsidies in the form of 'co-investment grants' (with conditions attached) to support future investment plans of the three motor vehicle producers in 2012 and 2013. Under these schemes, \$34 million was paid to Ford, \$29 million was committed to Toyota, and \$215 million was committed to Holden. The Victorian and South Australian governments also made decisions to contribute additional funds for capital investment.

The conclusion drawn from an evaluation of the economywide costs and benefits is that the policy rationales are weak and that ongoing industry-specific assistance to the automotive manufacturing industry is not warranted.

- Although there are spillover benefits from automotive manufacturing, there is no compelling evidence that the benefits to industries outside the automotive industry are significantly greater than those generated by other activities, or that assistance to the industry would yield spillover benefits that would otherwise go unrealised (and that exceed the costs of that assistance). In today's world, information, technology and people are continuously moving between firms, industries and economies, meaning that many of these spillovers would occur through other mechanisms were there to be no automotive manufacturing industry in Australia.
- Claims based on 'multiplier effects' from promoting production through government assistance typically fail to consider the cost of that assistance to taxpayers and the alternative uses of resources in other industries in the economy (which themselves have flow-on effects). For example, a motor vehicle producer might use government funding to buy more parts from component manufacturers, but equally government spending of those resources on health and education (for example) could be used to invest in the health and education workforces — who would contribute to Australia's economic development and social wellbeing, and who would spend their income in ways that also generate economic activity.
- The capacity for governments to use industry-specific assistance to attract and, importantly, retain capital investment that would not have otherwise occurred is limited. Governments should only offer assistance to any industry if it is in the best interests of the community overall. Ultimately it is only a sound business case that will underpin long-term capital investment and reinvestment. As Ford noted when announcing the closure of its subsidised plant, it was 'unable to identify a profitable and sustainable business model' for automotive manufacturing in Australia.
- Competitive pressures of various kinds are never-ending and subsidies or other support for a particular industry to 'ride out' those pressures will not usually transition it to a state of commercial viability. Indeed, the automotive manufacturing industry has been receiving decades of 'transitional' assistance that has forestalled, but not prevented, the structural adjustment now being faced by the industry.

Industry-specific assistance measures risk locking firms and employees into activities that diminish the overall performance of the Australian economy. Further, they can dull the commercial incentives faced by automotive manufacturers to

respond to competitive and adjustment pressures — for example, by reducing their costs, by seeking new business opportunities such as innovative new products, by pursuing export opportunities, by ceasing unsuccessful investments early or by diversifying into other industries.

More generally, although policies that provide industry-specific assistance benefit those who receive that assistance, this comes at a significant cost to taxpayers, and alternative higher-value uses for those funds are forgone.

What does this mean for existing industry-specific assistance arrangements?

The policy rationales for specific assistance to automotive manufacturing are weak, and the community would benefit from the ending of assistance to automotive manufacturing. Assistance provided to automotive manufacturers through the ATS (box 2) is scheduled to cease in 2020. The Green Car Innovation Fund and Automotive New Markets Initiative are scheduled to close in 2014-15 and 2015-16 respectively. The Commission does not support extending these programs or replacing them with other forms of specific assistance, as this would impose net costs on the community.

In the meantime, there is a substantial amount of assistance that is committed to the automotive manufacturing industry until 2020, most of which falls under the capped part of the ATS. In light of the decisions by Ford and Holden to cease manufacturing in Australia, and the Australian Government's pre-announced ATS savings in the 2013-14 Mid-Year Economic and Fiscal Outlook (MYEFO), it is timely to consider the most appropriate funding profile until the closure of the ATS.

The legislated ATS funding profile (set out in the ATS Regulations) provides for \$1.6 billion of capped assistance between 2014 and 2020, progressively phasing down from 2018 to 2020. The closures of the Ford and Holden plants are expected to contribute to an underspend of around \$380 million under the legislated ATS funding schedule by 2020 (box 3).

As noted above, the Australian Government has identified ATS savings of \$500 million in the MYEFO. The resulting funding schedule, however, has an uneven profile — funding would be particularly restricted in 2015, with reductions in 2016 and 2017 also (figure 1). Department of Industry analysis suggests that the MYEFO savings would prevent ATS participants from receiving the full amount of assistance that they are likely to qualify for between 2015 and 2017.

Box 3 Expected capped ATS payments under the legislated funding schedule and with MYEFO savings

Total payments under the legislated ATS funding profile are expected to be \$1250 million between 2014–2020 (see table), taking into account the announced closure of Ford and Holden manufacturing plants. This would result in an underspend of around \$380 million over the life of the scheme (see figure).¹ This underspend is the sum of unallocated funding that has been rolled forward to the end of each ATS stage (box 2).

ATS capped payment projections, 2014–2020

\$ million (nominal)^a

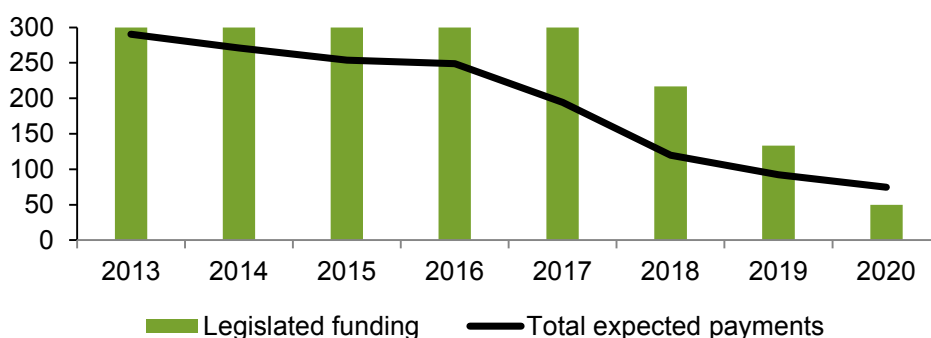
	<i>Legislated funding profile</i>	<i>Funding with MYEFO savings</i>	<i>Difference between funding profiles</i>
Capped assistance ^b	1 630	1 630	—
MYEFO savings	0	500	—
Available assistance	1 630	1 130	500
Expected underspend	380	110	270
Expected payments	1 250	1 020	230

^a All numbers rounded to the nearest \$10 million. ^b Includes estimated rollover amount of \$34 million from 2013.

Source: Department of Industry estimates.

ATS funding profile as legislated and expected payments under that arrangement^a

\$ million (nominal)



^a ATS payments can exceed the yearly cap due to a provision that allows unallocated funding to be rolled forward. Assumes Ford and Holden plants close as announced and Toyota operates at least until 2020.

Source: Department of Industry analysis.

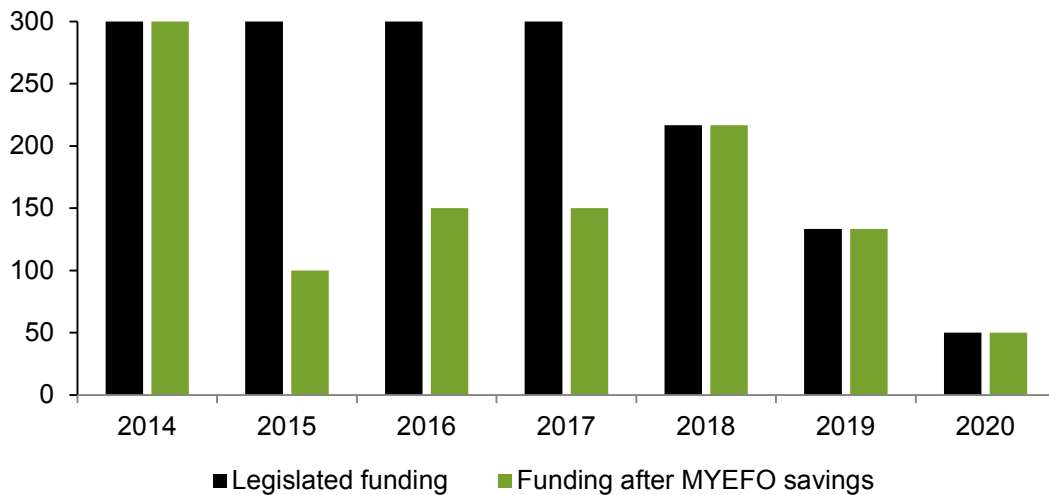
Total payments under the MYEFO funding schedule are expected to be \$1020 million between 2014–2020. It is expected that there will not be any unallocated funds rolled forward between 2015–2017. This will limit the total underspend under the scheme with the MYEFO schedule to \$110 million. Actual total expenditure under the MYEFO schedule is expected to be \$230 million lower than what is now anticipated under the legislated funding schedule. Expected savings are less than the \$500 million reduction in capped funding due to future year expenditure reductions from the Ford and Holden closures.

¹ Also, in 2012 the Australian Government committed \$215 million to assist Holden to make capital investments for manufacturing two vehicle models in Australia until 2022. Holden noted in its submission that this funding is contingent on it making the required investments. However, Holden is no longer committed to manufacturing vehicles in Australia beyond 2017.

In the Commission’s view, and consistent with its above in-principle arguments, there would be benefits to the Australian community from reducing total capped ATS funding as soon as possible. The announced \$500 million saving clearly falls into this category.

However, consideration should also be given to the potential severity and duration of any transitional costs associated with changing the timing and amount of funding withdrawn from the ATS. While the effect of the MYEFO funding schedule on adjustment costs is unclear, the uneven funding profile could elevate the risk of earlier plant closures by Ford and Holden, and might negatively affect investment decisions by Toyota and its component suppliers. The changes to the legislated funding schedule could therefore result in costs greater than the savings benefits by front-loading large, simultaneous adjustment costs throughout the automotive manufacturing industry. The announced savings will potentially elevate policy uncertainty for the automotive manufacturing industry at a time of already major structural change.

Figure 1 ATS capped funding profile as legislated and after MYEFO savings, 2014-2020^a
\$ million (nominal)



^a The \$500 million reduction in capped ATS funding between 2015 and 2017 is subject to the necessary amendment to the ATS Regulations being made and passing a 15 day period in each House of Parliament during which a motion to disallow the amendments can occur. In a given year actual ATS payments can differ from the annual cap due to unallocated funding, and a provision that allows for unallocated funding to be rolled over to future years. The size of each annual cap depends on whether there are any unallocated funds from the previous year carried forward. The Department of Industry has converted the MYEFO financial-year savings schedule to a calendar year schedule to accord with the ATS calendar year caps. These funding schedules do not depend on the announced decisions of Ford and Holden to cease automotive manufacturing in Australia.

Source: Department of Industry.

A smoother reduction profile would delay the savings benefits, but may also reduce adjustment costs.

The Commission is seeking further information on the potential benefits and costs to the community from the ATS funding schedule resulting from the MYEFO savings. Information is sought as to whether the funding profile could be reconfigured such that the net benefits to the community from phasing out assistance over the period to 2020 are maximised, taking efficiency and equity considerations into account. The Commission is also seeking information on whether the amount of funding withdrawn from the ATS as outlined in the MYEFO could result in adjustment costs greater than the savings benefits.

Should Toyota receive extra government assistance?

There have been reports that some interested parties are developing a proposal for Toyota (and its component suppliers) to be provided with additional assistance beyond that currently committed to by governments, so as to encourage it to continue automotive manufacturing in Australia.

Provided Toyota remains as a vehicle producer in Australia, it would receive its full (unmodulated) amount of assistance that it qualifies for in the final three years of the ATS (2018–2020). This outcome holds under both the currently legislated and MYEFO savings funding schedules. (The amount of annual assistance that Toyota receives will still be limited by a cap that prevents an ATS participant from receiving more than 5 per cent of the sales value of its goods and services for the previous year.)

Additional industry-specific assistance to Toyota would exacerbate the economywide distortions already resulting from the current level of assistance to the automotive manufacturing industry. Further, additional budgetary support could encourage other industries to divert management effort towards seeking preferred government treatment. It is also unclear how effective further assistance would be in view of the global trends noted in the preliminary findings report and the associated cost pressures being placed on Toyota. As noted above, ultimately a sound business case is required to underpin long-term capital investments.

In this context, Toyota recognised in its submission that it needs to significantly reduce the cost of its manufacturing operations in Australia to secure future investment from its parent company. Toyota's submission detailed its plans to attempt to achieve this. Toyota also requested a long term, consistent, globally competitive automotive manufacturing industry policy that supports future investment.

Rather than providing extra industry-specific government assistance, in the Commission's view, it would be more efficient to assist Toyota to continue manufacturing in Australia by ensuring that broader policy settings allow it, and its supplier base, to best respond to market and competitive pressures.

Other measures that affect the automotive manufacturing industry

In addition to direct budgetary assistance, there are other policies in place that may influence the automotive industry.

- There are restrictions on the importation of second-hand vehicles through the *Motor Vehicle Standards Act 1989* (Cwlth). These restrictions impose costs, including by potentially increasing the prices of second-hand vehicles and reducing consumer choice, which may exceed the benefits, and thus the rationale for such a policy is weak.
- The Australian, Victorian and South Australian governments have in place fleet purchasing policies that favour Australian-manufactured vehicles. These policies restrict the choice of cars available for government use, which can impose costs on taxpayers. Any benefits of such policies to the automotive industry in Australia appear to be limited. These policies should be removed, particularly if there is only one motor vehicle producer in Australia after 2017.

Enhancing the performance of both the Australian economy and the automotive manufacturing industry

As the Commission has noted on previous occasions, a focus on industry-specific assistance brings with it the risk that attention will be drawn away from the need to improve the broader policy settings that could increase the productivity and competitiveness of not only the automotive manufacturing industry, but also the economy more generally. Some key policy areas include those affecting workplace arrangements (discussed below), taxation, labour market mobility, education and training, infrastructure investment and efficiency, and the broader deregulation agenda.

The performance of all sectors of the economy is influenced by policy settings that affect firms and individuals in terms of:

- their *incentives* to perform well
- the *flexibility* they have to be able to respond to market pressures
- their *capabilities* to develop and implement changes in response to external pressures.

Given that automotive manufacturing firms (in conjunction with their workforces) must become and remain globally competitive in order to be commercially viable, government policies should not dull market signals or inhibit the incentives, flexibility and capability of firms and individuals to respond to those signals.

Workplace arrangements in the automotive manufacturing industry

Some participants and industry commentators have argued that automotive manufacturing workplace arrangements are significantly limiting the flexibility of employers and employees to respond to the current and future challenges facing the industry. These arrangements are commonly set out in enterprise agreements that have been negotiated between employers and employees — these enterprise agreements frequently contain wages for automotive manufacturing employees that are higher when compared to the relevant award and to international competitors. Under some enterprise agreements, entry-level wages can be several hundred dollars per week higher than those provided in the award.

Relatively higher wages can be justified where they are matched by commensurately higher productivity, supported by, for example, flexible workplace arrangements. While some participants have submitted evidence of beneficial productivity improvements, the Commission notes that some conditions previously agreed between automotive manufacturers and their employees significantly reduce flexibility. This includes matters such as rosters (including conditions under which overtime can be worked), changes to production levels and the use of contract and casual staff.

The conditions contained in such enterprise agreements are inevitably a product of the environment in which they were negotiated, from an industry, national and international perspective, and the workplace legislative framework in place at the time. As noted in the Commission's preliminary findings report, the competitive environment in which Australian and global automotive manufacturing companies operate has changed dramatically over recent years (box 1).

The conditions contained in enterprise agreements may also have been influenced by the extent to which automotive manufacturing employers and employees anticipated ongoing government assistance to support continued operations in Australia.

As part of an effort to improve efficiency and cut costs, Holden and its employees undertook a renegotiation of elements of their enterprise agreement during 2013 (although these changes have not taken effect due to Holden's decision not to proceed with the Next Generation vehicle program at its Elizabeth plant). Amongst

the agreed changes were wage freezes, 16 minutes of additional production time per day, reduction of Sunday overtime rates from double time and a half to double time, and greater flexibility through the removal of a requirement for Holden to obtain union agreement on 28 different matters relating to the operation of the business (such as the use of casual labour and contractors).

In late 2013, Toyota sought to vary its enterprise agreement to remove what it now regards as out-dated and uncompetitive practices and allowances that increase its costs. Toyota stated that these changes are a vital part of its cost-reduction program, and may well influence future investment decisions. The move was challenged by four Toyota employees on the basis that a clause in the agreement prohibits further claims before it is due to expire in 2015. This resulted in Toyota being unable to proceed with a planned employee vote on the proposed changes. The Federal Court's decision on this matter is being appealed by Toyota. The Australian Government has announced its intention to 'intervene in support of Toyota's workers being allowed a say as soon as possible on the proposed variation'. Were the Appeal Court's decision to lead to a restriction in the scope for employees to vote on proposed changes to enterprise agreements containing 'no further claims' clauses before the nominal expiry date of the agreements, this would have wide-reaching implications for agreements containing those clauses. Such agreements are widespread throughout the automotive manufacturing sector.

The effect of structural adjustment on the workforce

Displaced employees who are unemployed for any period suffer a loss of income and can incur costs such as job search, training, skills assessment, occupational licensing, and relocation. When displaced employees find new employment, for many their income may be lower and they may have less employment security, relative to their previous job (box 4). The evidence also points to some instances where a person's new work terms and conditions are at least as good as before.

For some employees, retrenchment can lead to prolonged unemployment or joblessness. In such circumstances, the affected individuals can lose some of their vocational skills and find it increasingly difficult to return to work. Unemployed people are also at a higher risk of deep and persistent social exclusion, which encompasses people's reduced participation in educational, work-related, and community activities. Job loss and long-term unemployment can also have adverse consequences for a person's health; for example, increased stress and loss of self-esteem can affect their mental health. Some of these adverse effects can flow on to a person's family and society more generally.

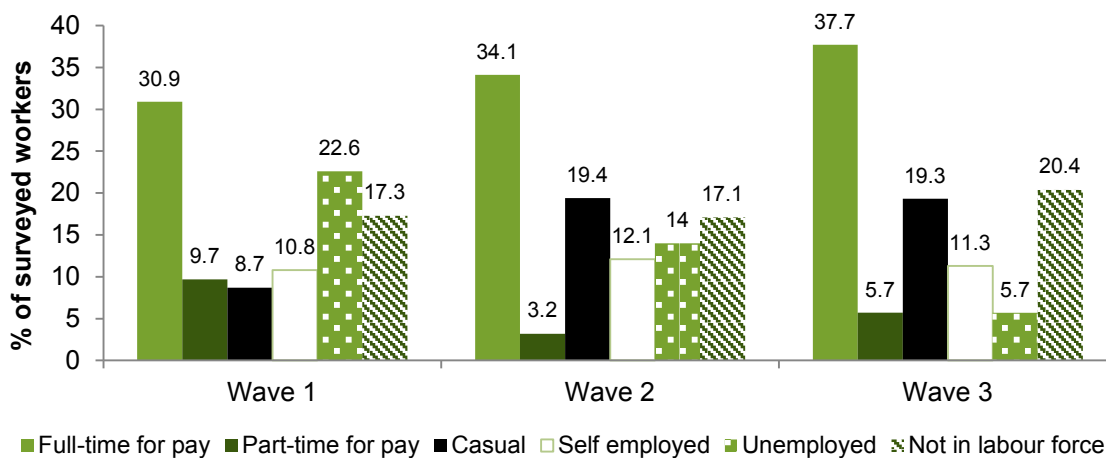
Box 4 Survey of retrenched Mitsubishi employees

In 2004, Mitsubishi Australia announced the closure of its Lonsdale engine manufacturing plant and a reduction in capacity at its Tonsley Park assembly plant, resulting in 700 involuntary retrenchments at Lonsdale and 400 voluntary retrenchments at Tonsley Park. Following the restructure and plant closure, researchers surveyed a sample of retrenched employees in three 'waves'. Wave 1 took place within 6 months of retrenchment, wave 2 took place approximately a year after wave 1, and wave 3 took place approximately a year after wave 2.

The survey results indicate that many respondents experienced a loss of employment security. One third of the previously full-time permanent employees were in full-time paid employment 12–18 months after retrenchment, around a quarter were in casual or part-time paid work, and 12 per cent were self-employed. In wave 2 interviews, many respondents reported that they had struggled to find full-time employment and had to settle for casual or part-time contract positions.

Many respondents also reported a decrease in income. In wave 2 interviews, 72 per cent of respondents reported that they were now earning less than when employed at Mitsubishi. Of those surveyed, 11 per cent reported that they were on the same income, and 15 per cent reported that they earned a higher income. The survey results suggest that the lower earnings partly reflected the shift from full-time to part-time or casual work for many displaced employees, as well as the reality that Mitsubishi paid above the market rate.

Over time there was a progressive increase in the proportion of former Mitsubishi employees who found employment and a decrease in the proportion unemployed (who had not exited the labour force). By wave 3, the unemployment rate among those surveyed was 5.7 per cent. In wave 3 interviews, many of the respondents reported incurring non-financial costs as a result of retrenchment. For example, when asked: 'What has been the most difficult thing about leaving [Mitsubishi]?', the most common response was 'Loss of social interaction' (37 per cent of respondents).



Note: Over the course of the research, 71 of 372 participants withdrew from the study. To the extent those who leave a study are likely to be more or less successful in finding re-employment than those who continue, this attrition might bias estimates of employment patterns from the survey.

The characteristics of affected employees are an important determinant of adjustment costs

The individual characteristics of displaced employees, such as their age, skills, previous occupation, and the extent to which they may be able to, or willing to, work (and possibly live) in a different location, are important determinants of the time taken to find further employment. The automotive manufacturing workforce includes people who are likely to encounter greater difficulties finding re-employment than others (such as those who are older or have limited skills or English language proficiency) (box 5).

Box 5 Characteristics of automotive manufacturing employees that may influence adjustment costs

Studies suggest that people from lower-skilled occupations, with limited qualifications, or with poor English skills are likely to face greater difficulties in finding re-employment. In the automotive manufacturing industry in 2011:

- 34 per cent of employees were employed in lower-skilled occupations (such as labourers and machinery operators), which was similar to manufacturing overall, but about double the average for all industries (at 16 per cent)
- 15 per cent of employees had a bachelor degree or higher (similarly, 14 per cent for all manufacturing), compared to the average for all industries of 26 per cent
- 3.7 per cent of employees reported poor English skills, which was a little higher than the average for the manufacturing sector of 3.4 per cent, but almost three times the level for all industries of 1.3 per cent. Automotive manufacturing employees in Victoria reported higher rates of poor English (5.1 per cent) than those in South Australia (2.1 per cent).

Older people who have been retrenched are less likely to find re-employment. Possible reasons are that they are less inclined to move location while employers prefer to train younger workers who are likely to remain in the job longer.

In 2011, the age profile of the automotive manufacturing workforce was broadly similar to that of manufacturing and all other industries, with about 40 per cent of people employed in the automotive manufacturing industry aged 45 or over.

Redundancy payments are another consideration in assessing the potential effects of retrenchment on automotive manufacturing employees. For example, redundancy payments help to ameliorate immediate financial pressures on displaced employees arising from unemployment.

Some displaced employees, such as those who have worked for motor vehicle producers for a long period of time, are likely to receive large payments relative to the payments that will be received by employees who are reliant on the redundancy

provisions in the relevant award, including employees of some component suppliers. The magnitude of redundancy payments and their timing can influence the behaviour of some employees in terms of their search for other jobs.

The magnitude of adjustment costs also depends on the amount of time between the notification of planned and actual closures. Advanced notice of closures or downsizing is likely to reduce adjustment costs by giving employees time to seek alternative employment whilst still being employed.

The advanced notice that Ford (2016) and Holden (2017) have given in regard to their plant closures is helpful to employees, as are the relatively large redundancy payments that employees will likely receive. Their attempts to help their employees find future employment will assist in easing adjustment pressures. For example, Ford is working with employees and their representatives on transitional arrangements including up-skilling, training and placement opportunities.

However, a number of employees currently working for component manufacturers (many of which are small to medium size firms) that may be forced to downsize or close as a result of Ford and Holden's plant closures may not receive the same degree of notice (or necessarily the same level of help) from their employers. To the extent that these employees rely on generally available services, it will be important to ensure that those services are sufficient. Indeed, some component manufacturing employees may warrant particular consideration if generally available measures appear to be insufficient for their circumstances.

Further consideration of the scope for adjustment for component manufacturing firms and their employees — which for some may occur before the actual exit of Holden and Ford from automotive manufacturing — will form part of the Commission's final report; and public hearings prior to that.

The magnitude of adjustment costs will partly depend on the adaptive capacity of the affected regions

The extent of any contraction in employment arising from industry adjustment — in the automotive manufacturing industry and in the economy more broadly — will depend on a number of factors, including the characteristics of affected regions. Relevant factors include:

- the number of displaced employees — the greater the number of people displaced, the more difficult it will be on average for a displaced employee to obtain a new job. This is likely to be a particularly significant factor where a large number of displaced employees live in a small, local labour market

-
- local labour market conditions — the size of the labour market, its job composition, and its prevailing rate of unemployment. For example, a displaced employee's opportunities for matching with a new job are likely to be highest in a labour market that has a large number and diverse mix of jobs
 - broader factors include the flexibility of labour and credit markets, factors that influence geographic labour mobility including the housing market in the region affected by industry structural adjustment and housing affordability in other regions, and macroeconomic conditions.

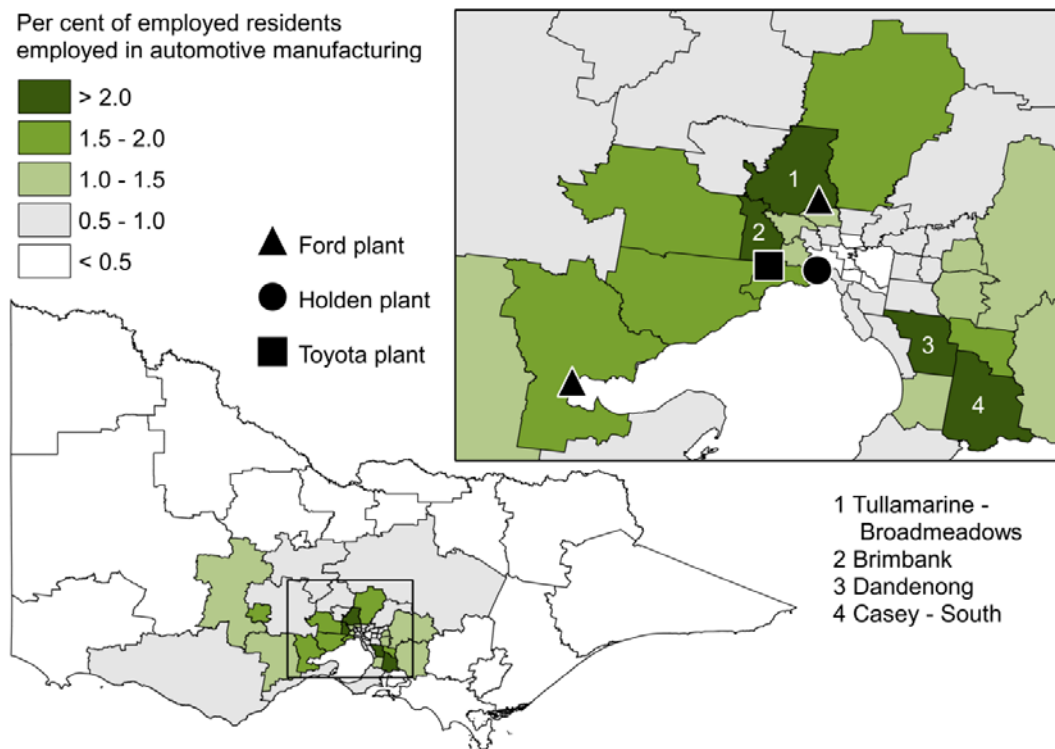
Adjustment pressures are likely to be concentrated within specific regions of Victoria and South Australia

Employment in automotive manufacturing is geographically concentrated in south-east Australia (figures 2 and 3). In 2011, Victoria accounted for about half of all automotive manufacturing employees (54 per cent), while South Australia and New South Wales each accounted for a further 13 per cent.

In 2011, automotive manufacturing employees accounted for less than 2 per cent of employed residents in each region of Australia (with the highest concentrations of automotive manufacturing employees in four regions: Adelaide-North; Melbourne-West; Melbourne-South East; and Melbourne-North West). At the sub-regional level, there were several examples where automotive manufacturing employees accounted for more than 2 per cent of employed residents. Playford, in northern Adelaide, stands out, as 3.4 per cent of employed residents were engaged in automotive manufacturing in 2011.

Regions in Adelaide (Adelaide-North) and Melbourne (Melbourne-West; Melbourne-South East; and Melbourne-North West), and the region of Geelong, will be particularly affected by the Holden and Ford plant closures, and they are most likely to experience significant adjustment pressures. Relatively high levels of unemployment and social disadvantage in some sub-regions, such as Playford in northern Adelaide and Dandenong in south eastern Melbourne, will likely exacerbate adjustment costs.

Figure 2 Concentration of automotive manufacturing employees, Melbourne and Geelong



Adjustment pressures would be exacerbated in some of these regions if Toyota does not proceed with plans to manufacture the next generation Camry model in Australia, particularly in Melbourne (Toyota’s vehicle assembly and engine manufacturing operations are at Altona in Melbourne’s west).

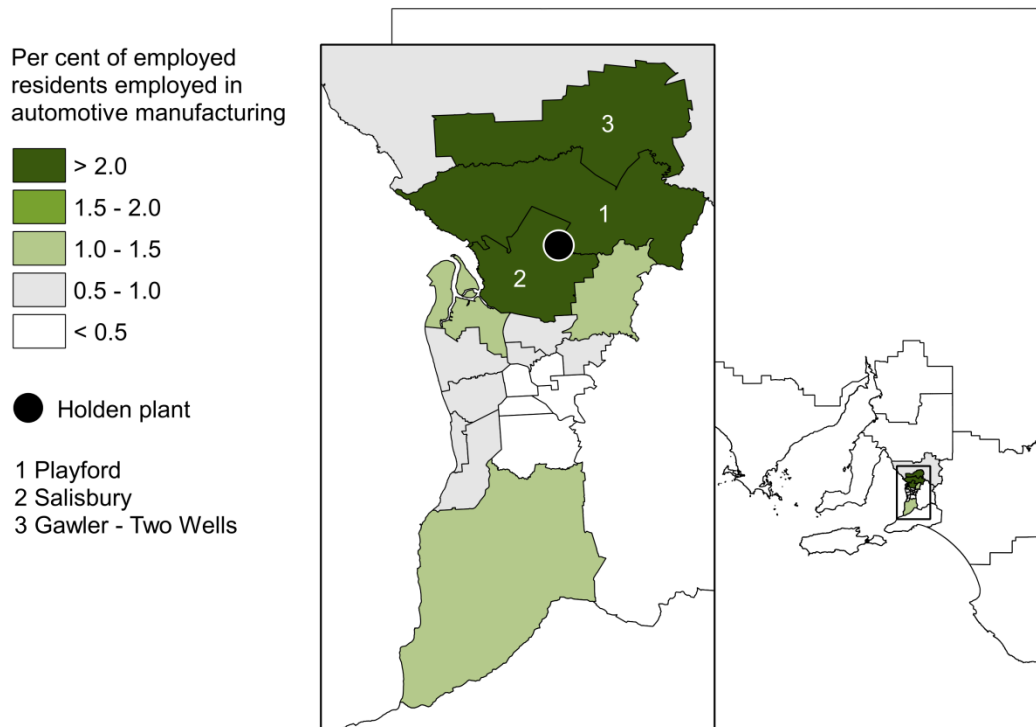
Estimating the costs of adjustment

The Commission is undertaking economic modelling for the final report that will consider the economywide and regional effects of adjustment in the automotive manufacturing industry.

Economic modelling submitted to the inquiry by the Federal Chamber of Automotive Industries estimated the structural adjustment costs associated with a closure of the automotive manufacturing industry. These costs were set against the estimated long-term welfare benefits from the reallocation of resources to more productive uses. This analysis found there would be an overall welfare cost of \$21.5 billion to Australia from closure of the automotive manufacturing industry. This result is sensitive to assumptions about the time taken for the economy to

adjust to the shutdown and the timeframe used to calculate net present values. The Commission will comment further on this modelling work in its final report.

Figure 3 Concentration of automotive manufacturing employees, Adelaide



Facilitating workforce adjustment — a role for government?

Generally available measures have a number of distinct advantages in dealing with adjustment pressures because they seek to:

- treat individuals in similar circumstances equally
- target assistance to those in genuine need, whatever the cause
- address the net effects of the various factors influencing the financial circumstances of individuals and families
- support individuals and families, rather than a particular industry or activity
- minimise the design, administration and monitoring costs of assistance provision.

Generally available measures recognise that there are hundreds of thousands of involuntary job losses every year and that it would not be feasible, equitable or

cost-effective to have a multitude of special arrangements when structural adjustment and labour market changes are so frequent and widespread. In the year ending February 2013, around 355 000 people were involuntarily retrenched across Australia. Of these, 80 000 employees had been with their employer for at least five years. It is important, therefore, that the generally available measures are appropriately designed and resourced to assist all eligible displaced employees through the adjustment process and to moderate potential adverse distributional effects from structural change.

However, the generally available measures are not designed to handle all contingencies. In some cases, there is a role for additional measures to promote equitable outcomes and improve the efficiency of the adjustment process.

Current and proposed special assistance packages for automotive workers

Governments have provided, and continue to provide, special adjustment assistance programs for employees and regions affected by retrenchments across a range of industries. For example, for the automotive manufacturing industry alone, the Australian Government is providing around \$50 million to fund the labour market part of the Automotive Industry Structural Adjustment Program, which provides intensive employment services for displaced employees, including those made redundant as a result of the planned closure of Ford's manufacturing plants.

The Australian and State governments have also funded regional adjustment programs, which subsidise businesses to undertake projects that generate jobs in regions affected by large-scale retrenchments in particular industries (these include two current funds associated with the announced Ford plant closures in Geelong and Melbourne's north).

The Australian, Victorian and South Australian governments have foreshadowed a structural adjustment package in response to Holden's announcement that it plans to cease manufacturing in Australia by 2017. The Australian Government is currently undertaking reviews to inform the design of its proposed assistance package and the South Australian Government released a jobs plan in January 2014. In addition to measures that have typically formed part of previous adjustment packages (such as providing intensive employment services for displaced employees), a range of other options are being canvassed including funding large-scale infrastructure, promoting innovation and investment in selected sectors (such as defence manufacturing and the shipbuilding industry) and relocating public-service functions.

Can special adjustment packages cost-effectively facilitate adjustment?

A range of generally available welfare, training and employment services will assist employees and regions affected by plant closures to adjust to these changes. It is important that these services are adequately resourced and work alongside the efforts of Ford and Holden as part of their announced exit strategy. There may be a case for special adjustment assistance where generally available measures are unlikely to adequately address equity and efficiency concerns related to structural adjustment.

Past special adjustment packages, including regional adjustment funds, have had limited success. Policies that target development of particular regions have often been justified by the desire to retain other local businesses, maintain the rating base of local government and keep schools with sufficient enrolment. However, they can also redistribute employment from one region to another without increasing (and potentially reducing) overall economic activity.

For example, analysis of regional adjustment funds (including those targeting retrenchments in the automotive manufacturing industry) by the Grattan Institute concluded they do not appear to have significantly affected overall long-term unemployment trends, and did not result in the regions performing any better than other regions that lost a major employer but did not receive government assistance.

Targeted public investment and related projects are often developed with the aim of assisting people and regions affected by significant economic change. Infrastructure investments may assist in overcoming bottlenecks to greater economic activity in the affected region. The key issues in this context are whether a proposed infrastructure project provides net benefits to the community as a whole (rather than just to a specific region), and given limited resources, whether it generates the largest net benefits from the available options (regardless of the project's location).

Further, the desire to locate a project (such as a defence or shipbuilding project) in a particular region does not remove the need for a robust assessment of its costs and benefits to the Australian community as a whole.

Evidence on the effectiveness of past policies aimed at encouraging investment in particular industries based on the perceived advantages of those industries in Australia suggests that governments do not have the necessary information or skills to judge which firms or industries will be successful in the future. This raises questions about the ability of governments to successfully 'pick winners', with a frequent outcome being inefficient investment (including the creation of jobs that are reliant on ongoing assistance).

Labour adjustment programs are also often developed, over and above the generally available training and employment services, to improve the skills and general employability of retrenched employees. As noted earlier, automotive manufacturing employees have, on average, an employment history of lower-skilled jobs, lower educational attainment and lower English proficiency compared to the average for all industries.

However, much of the public information that does exist (including information on programs in Australia, such as the program implemented for displaced Mitsubishi employees) suggests that specially targeted programs have had some, but limited, success in assisting displaced automotive manufacturing employees find future employment. It is also important to ensure that these programs do not have adverse effects on other jobseekers who do not have access to the program.

As noted above, the advanced notice of the closures of the Ford and Holden plants gives their employees, and hopefully in most cases their suppliers' employees, a period of time to prepare for change. The Commission is seeking input from participants on the extent to which generally available measures are likely to adequately address equity and efficiency concerns relating to structural adjustment in the automotive manufacturing industry, and whether there are models of providing adjustment assistance more cost-effectively.

Draft proposals, draft findings and information requests

DRAFT FINDING 2.1

The Commission's net combined assistance estimates suggest that about \$30 billion (2011-12 dollars) was provided to the automotive industry between 1997 and 2012. Despite reductions in the absolute level of assistance over time, the automotive manufacturing industry remains one of the most heavily assisted industries in Australia.

DRAFT FINDING 2.2

Governments, in Australia and overseas, use various assistance measures in attempts to encourage automotive manufacturing firms to invest and operate in their jurisdictions. Due to the vast range of measures used, and the lack of transparency in the available information, an accurate comparison of the levels of assistance across countries is extremely difficult to do on a like-for-like basis and is not feasible for this inquiry.

DRAFT FINDING 2.3

The broader policy environment in which the automotive manufacturing industry operates directly affects the productivity and competitiveness of automotive manufacturers, and the capacity for firms and individuals to respond to changing market and competitive conditions. In particular, workplace arrangements are limiting efforts to promote workplace flexibility and increase productivity in some cases.

INFORMATION REQUEST 2.1

The Commission is seeking further information on the existence and nature of any policy or regulatory impediments to adjustment and consolidation in the automotive manufacturing industry, including for displaced employees.

DRAFT FINDING 3.1

The policy rationales for providing industry-specific assistance to the automotive manufacturing industry are weak.

INFORMATION REQUEST 3.1

The Commission is seeking further information on:

- *the potential benefits and costs to the community from the Automotive Transformation Scheme (ATS) funding schedule resulting from the 2013-14 Mid-Year Economic and Fiscal Outlook (MYEFO) savings*
- *whether the funding profile could be reconfigured such that the net benefits to the community from phasing out assistance over the period to 2020 are maximised, taking efficiency and equity considerations into account*
- *whether the amount of funding withdrawn from the ATS as outlined in the MYEFO could result in adjustment costs greater than the savings benefits.*

DRAFT PROPOSAL 3.1

The Australian and Victorian Governments should not provide Toyota Australia with industry-specific assistance that is additional to the current schemes (which are phasing out).

The Australian Government should not extend or replace the Automotive Transformation Scheme after its scheduled closure in 2020.

The Australian Government should not extend or replace the Green Car Innovation Fund after its scheduled closure in 2014-15.

The Australian, Victorian and South Australian governments should not extend or replace the Automotive New Markets Initiative after its scheduled closure in 2015-16.

The Australian, state and territory governments should not provide any further capital subsidies to the automotive manufacturing industry beyond those already committed.

DRAFT PROPOSAL 3.2

The Australian, Victorian and South Australian governments, by 2018, should remove fleet procurement policies that require government agencies to purchase vehicles manufactured in Australia.

DRAFT FINDING 3.2

The policy rationale for prohibiting the large-scale importation of second-hand vehicles into Australia is weak. However, appropriate regulatory measures are required to ensure that consumer protection, community safety, and environmental performance standards are maintained before the restrictions are removed. These concerns are best dealt with directly, through regulatory standards applicable to all vehicles sold in Australia.

The \$12 000 specific duty on imported second-hand vehicles appears to be largely redundant, providing a prima facie case for its removal.

INFORMATION REQUEST 3.2

The Commission is seeking further information on the benefits and costs of removing restrictions on the large-scale importation of second-hand vehicles. In particular:

- what would be the potential benefits of removing these restrictions?*
- what are the potential costs of removing these restrictions and who bears these costs?*
- how could compliance with Australian safety and environmental standards be most efficiently ensured?*
- if the benefits are expected to exceed the costs, how should restrictions be removed and over what timeframe?*

INFORMATION REQUEST 3.3

The Commission is seeking further information on the costs and benefits of allowing importers to apply for tariff concession orders for automotive components.

DRAFT FINDING 4.1

Adjustment pressures in the automotive manufacturing industry, including plant closures announced by Ford and Holden, will result in concentrated reductions in industry employment in specific regions in and around Melbourne and Adelaide. Relatively high rates of unemployment and social disadvantage in some regions, such as in northern Adelaide and in Melbourne's south east, will likely exacerbate adjustment costs.

The individual characteristics of displaced employees will affect adjustment costs. Low skill levels may be an impediment to re-employment for some displaced automotive manufacturing employees and older people who have been retrenched are less likely to find re-employment.

DRAFT FINDING 5.1

Generally available measures have some distinct advantages in dealing with adjustment pressures, relative to ad hoc or special adjustment assistance. These measures:

- treat individuals in similar circumstances equally*
- target assistance to those in genuine need whatever the cause*
- address the net effects of the various factors influencing the financial circumstances of individuals and families*
- support individuals and families rather than a particular industry or activity*
- minimise the design, administration and monitoring costs of assistance provision.*

DRAFT PROPOSAL 5.1

Governments should ensure that generally available welfare, training and employment services are adequately resourced to deal with the effects of structural adjustment in the automotive manufacturing industry.

DRAFT FINDING 5.2

Where governments determine that there is an in-principle case for providing adjustment assistance beyond that generally available, on efficiency or equity grounds, it needs to be demonstrated that such assistance would be cost-effective.

DRAFT FINDING 5.3

There is little evidence that regional adjustment funds have been cost-effective, from a whole-of-economy viewpoint, in addressing the effects of adjustment arising from employment reductions in the automotive manufacturing industry.

DRAFT FINDING 5.4

Available information suggests that targeted labour adjustment programs have had some, but limited, success in assisting displaced employees find future employment. Job search assistance and training appear to be among the more cost-effective options in many circumstances.

Given this, and that labour adjustment programs can have adverse consequences for jobseekers not targeted by the programs, the key issue is whether there is robust evidence that demonstrates that targeted labour adjustment programs would be an efficient and equitable response to the particular adjustment task facing employees from the automotive manufacturing industry.

DRAFT FINDING 5.5

Infrastructure investments may in some cases assist in overcoming bottlenecks to greater economic activity in regions affected by structural adjustment. The key issue is whether a proposed infrastructure project provides net benefits to the community as a whole (rather than only to a specific region), and given limited resources, whether it generates the largest net benefits from the available options (regardless of the project's location).

INFORMATION REQUEST 5.1

The Commission is seeking further information on:

- *specific characteristics and needs of some groups of automotive manufacturing employees that might warrant particular consideration if generally available measures appear to be insufficient*
- *whether there are different circumstances facing employees from the extensive and varied component manufacturing sector as compared to Ford and Holden employees*
- *options for designing adjustment assistance programs for automotive manufacturing employees and regions affected by structural adjustment (together with evidence of the costs and benefits, and the effectiveness, of those options).*

1 About the inquiry

1.1 The Commission's task

The Australian Government has asked the Commission to undertake an inquiry into government assistance for Australia's automotive manufacturing industry, including passenger motor vehicle and automotive component production. The Commission has been asked to:

- assess the significance of the capabilities within the industry, its direct economic benefits, and its secondary impacts on other sectors of the economy
- examine national and international factors affecting the industry
- quantify the costs and benefits of existing assistance mechanisms
- identify and evaluate possible alternative public support mechanisms
- identify any significant adjustment costs that may arise from alternative support mechanisms or policy changes, and how they might be best managed.

1.2 Scope of the inquiry

This inquiry will cover the automotive manufacturing industry supply chain in Australia, including:

- motor vehicle assemblers that manufacture passenger motor vehicles (and in some cases engines), light commercial vehicles (including sports utility vehicles) and heavy commercial vehicles (including bus and truck manufacturing)
- automotive component producers in Australia that supply parts for the production of motor vehicles or the aftermarket
- providers of services and specialist skills that support the automotive manufacturing industry such as design, research and development, tooling, engineering and production services.

This position paper deals predominantly with the producers of passenger motor vehicles, light commercial vehicles and their associated components and services, not heavy commercial vehicles (buses and trucks) as this latter segment is not a direct beneficiary of industry-specific government assistance.

Overview of the Australian automotive manufacturing industry

Around 200 000 vehicles were produced in Australia in 2012; this accounted for one quarter of one per cent of global vehicle production in that year (OICA 2013). There are currently three motor vehicle producers in Australia — Ford Motor Company of Australia (Ford), General Motors Holden (Holden) and Toyota Motor Corporation Australia (Toyota). All are foreign-owned subsidiaries of global companies, with affiliates in many countries.

The three production plants, combined, currently assemble six models of motor vehicles. Production is spread across:

- two states — Victoria (Ford and Toyota) and South Australia (Holden)
- four market segments — small car (Holden Cruze), medium-sized car (Toyota Camry), large car (Ford Falcon, Holden Commodore and Toyota Aurion) and sports utility vehicle (SUV) (Ford Territory).

The three motor vehicle producers in Australia also manufacture engines and undertake vehicle design and engineering in specialty centres located in Victoria.

There is a complex logistical supply chain of about 160 businesses that are involved in the engineering, design, tooling and manufacturing of automotive components (FAPM 2013). Some component manufacturers also supply the aftermarket — in total, there are approximately 260 businesses located in Australia that manufacture components and accessories for the aftermarket (AAAA, sub. 54).

Australia has a comparatively small industry sector that manufactures trucks — PACCAR and Iveco in Victoria, and Volvo in Queensland. There are 15 bus manufacturers throughout Australia (OzeBus 2013).

1.3 The Commission's approach

The Commission has consulted as widely as possible

The Commission has consulted as widely as possible given the compressed timetable for this inquiry. The Commission received the terms of reference for this inquiry on 30 October 2013. An issues paper was released in November 2013 to assist individuals and organisations prepare written submissions.

The Commission held public hearings in Adelaide (2 December 2013) and Melbourne (3 and 10 December 2013), and met with a range of participants including motor vehicle producers in Australia, component manufacturers, industry

bodies, unions and government departments. Consultations with automotive industry analysts and government departments in Japan and the United States have also been undertaken. The full list of visits and consultations is provided in appendix A. Prior to the release of this position paper, the Commission had received 235 submissions; this includes 140 submissions from individual members of the Australian Manufacturing Workers' Union.

A staged approach to the inquiry

The Commission is conducting the inquiry in stages. The first report (the preliminary findings report — box 1.1) was released on 20 December 2013 and examined the national and international factors affecting the competitiveness of the Australian automotive manufacturing industry.

This position paper represents the second stage of the inquiry process. It sets out draft advice on potential options for government assistance to the automotive manufacturing industry, taking into account the benefits and costs of assistance to the community as a whole. The Commission is inviting submissions on the preliminary findings report and this position paper, and will hold a further round of public hearings in February 2014. Also in February 2014, the Commission expects to release the interim results of quantitative modelling which considers the economywide effects of industry adjustment, and will hold a technical roundtable on this analysis in early March.

The contributions of inquiry participants and the Commission's further analysis will inform the Commission's final report, which will be delivered to the Australian Government by 31 March 2014.

Taking account of recent developments in the Australian automotive manufacturing industry

In May 2013, Ford announced its intention to cease automotive manufacturing in Australia by October 2016. In December 2013, Holden announced that it will cease automotive manufacturing in Australia by the end of 2017. Both Ford and Holden have indicated that they intend to maintain a design base in Australia following the cessation of motor vehicle manufacturing.

Box 1.1 Key points from the preliminary findings report

- Global forces are driving (and are likely to continue to drive) dramatic changes in both the demand for motor vehicles and the size, scale and location of production.
- At a global level, production capacity exceeds demand for motor vehicles.
 - Demand in a number of developed economies has been slow to rebound from the global financial crisis, and many assembly plants are operating below capacity.
 - Significant rationalisation of production capacity has occurred in the US, and further assembly plant closures have been announced in the UK and Belgium.
 - Vehicle manufacturing capacity is shifting to regions with lower labour costs and high demand growth such as China, Eastern Europe, India, Mexico and Thailand.
 - Many governments provide financial or other support to attract (or retain) an automotive manufacturing industry.
- There is relentless pressure on vehicle producers worldwide to reduce manufacturing costs, particularly in the small to medium size car, high volume, market segments.
 - The selling prices for vehicles in such segments of the new car market are held down by fierce competition from local suppliers and importers.
 - Affiliates within international firms compete for the right to produce models built on global platforms — for supply to both domestic and export markets.
 - Cost pressures extend to component manufacturers throughout the supply chain.
- Production scale and labour costs are key drivers of automotive manufacturing costs.
 - All vehicle manufacturers in Australia are producing well below the 200 000 to 300 000 vehicles needed annually for an assembly plant to be cost competitive.
 - Labour costs in automotive manufacturing are substantially higher in Australia than in countries such as China and Thailand.
 - Despite continuing efforts by vehicle producers and their employees, a substantial cost gap between Australian and many overseas assembly plants remains.
- Increasing vehicle production in Australia, for local supply or export, is challenging. Vehicle producers in Australia have been losing local market share.
 - The Australian new car market is small by global standards. It is highly competitive, to the benefit of Australian consumers, but is fragmented. Top selling models enjoy sales of only a little over 40 000 vehicles a year.
 - Export opportunities are limited by the high costs of production, the sustained high Australian dollar, competition, and continuing barriers to trade.
- Global trends place ongoing pressure on Australian automotive component suppliers.
 - Component manufacturing in Australia is high cost compared to countries such as China and India. Motor vehicle producers in Australia are increasingly sourcing automotive components from overseas.
 - Vehicle producers increasingly require their key component suppliers to have a global presence and be located near major production regions.
 - The greater use of global platforms may lead to opportunities for some Australian component suppliers, but may lead to the closure of others.
- Australian governments have provided capital grants and subsidies to automotive manufacturers, and transitional assistance intended to facilitate industry adjustment.

Following Holden's decision, Toyota stated that it is reviewing its position to determine whether it can continue operating as the sole motor vehicle manufacturer in Australia. Toyota has indicated that a decision to proceed with the Australian production of the next generation Camry model and its export program will be made in 2014.

The structural changes occurring in the Australian automotive manufacturing industry are not unique to Australia (or to manufacturing more generally). Globally, motor vehicle producers are continuing to make intense efforts to reduce manufacturing costs by rationalising the number of vehicle platforms, closing high-cost assembly plants and requiring greater supply chain efficiencies. In response, production of motor vehicles across the developed economies of the United States, Europe and Japan has declined in both absolute terms and relative to total global production.

The Commission has given careful consideration to the significance of the Ford and Holden decisions for other automotive manufacturing firms in Australia, for component suppliers and related logistics and other businesses, and for employees and regions affected by plant shut downs.

2 The role of government

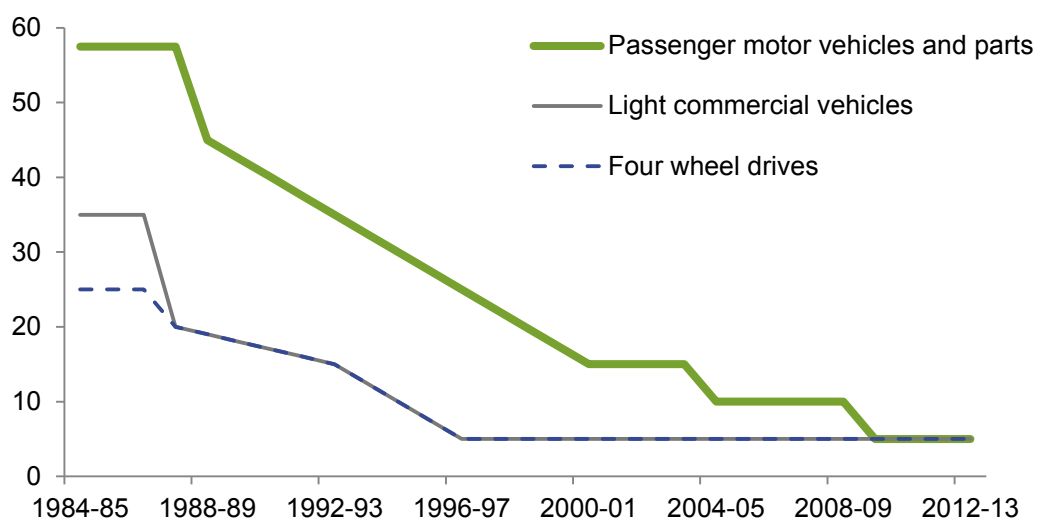
Key points

- Government assistance for Australia's automotive manufacturing industry takes many forms, including tariffs and co-investment grants. The Commission's net combined assistance estimates suggest that about \$30 billion (2011-12 dollars) was provided to the industry between 1997 and 2012. Automotive manufacturing remains one of the most heavily assisted industries in Australia.
- Industry-specific assistance imposes costs on taxpayers and means that alternative higher-value uses for public funds are forgone. Industry-specific assistance dulls the incentive for automotive manufacturing firms to improve productivity, seek export opportunities, cease unsuccessful investments early and diversify into other industries.
- Automotive industry assistance can only be justified where investment and production decisions in the industry are affected by market failure, the market failure is substantial and amenable to government action, and the benefits to the community from providing assistance outweigh the costs. Intervention by governments in the absence of these conditions will come at a cost to the performance of the economy overall. Separately, issues of equity and fairness can justify government assistance to individuals and groups in the community.
- The policy rationales for specific assistance to automotive manufacturing are weak.
 - Automotive manufacturing in Australia can produce 'spillover' benefits. However, these benefits are not unique and are obtainable without industry-specific assistance, either as a consequence of automotive manufacturing overseas, the operations of other industries or generally available assistance measures.
 - Claims based on multiplier effects from promoting production through assistance typically fail to consider the cost of assistance to taxpayers and the alternative use of resources in other industries (which themselves have flow-on effects).
 - Policies to attract investment that would not otherwise have occurred draw resources away from other, more efficient uses, reducing economic performance.
 - Investment in alternative vehicle and component technologies should be driven by commercial factors rather than government assistance.
 - Decades of transitional assistance have forestalled but not prevented the inevitable structural adjustment now being faced by the industry.
- A range of other government policies affect the competitiveness of the automotive manufacturing industry, and the ability of firms and their employees to respond to changing circumstances. In some cases, workplace arrangements are limiting efforts to promote workplace flexibility and increase productivity.

2.1 Past and present assistance arrangements

Historically, much of the assistance received by the automotive manufacturing industry (and more specifically, producers of passenger motor vehicles and light commercial vehicles and their associated components¹), was in the form of tariffs and other trade measures. A series of policy changes, particularly following the 1984 release of the Australian Government's Motor Industry Development Plan (also known as the Button Car Plan), led to a progressive reduction in tariff assistance. The tariff rate on passenger motor vehicles and parts declined 2.5 percentage points annually from 1988 to 2000. Further reductions of 5 percentage points occurred in 2005 and 2010 (figure 2.1).

Figure 2.1 **Tariff rates for the Australian automotive industry**
Per cent



Sources: AAI (2013); Lloyd (2007).

Current general (most-favoured-nation) tariff levels for the Australian automotive industry are 5 per cent. This tariff level applies to passenger motor vehicles, light commercial vehicles and four-wheel drives, as well as original equipment and replacement components. Tariff rates lower than the general rate apply to imports from some countries under bilateral or regional trade agreements. Australia has entered into seven² such trade agreements — with the Association of Southeast

¹ The heavy commercial vehicle (buses and trucks) segment is not a direct beneficiary of industry-specific government assistance.

² Bilateral trade arrangements between Australia and Korea (the Korea–Australia Free Trade Agreement), announced in December 2013, will also remove tariff barriers on motor vehicles and parts. Korea has agreed to eliminate tariffs on manufactured products (DFAT 2013).

Asian Nations, New Zealand, Chile, United States, Malaysia, Singapore and Thailand — and other concessional arrangements, including with developing countries.

As tariff assistance to the automotive industry declined, a series of industry-specific budgetary measures were implemented to assist the industry to adjust. Each package has included a specific end date — the implication being that the industry should not receive ongoing assistance from government beyond that time. The Automotive Competitiveness and Investment Scheme (ACIS) took effect in 2001, and was initially planned to run for five years. The objective of the ACIS was to:

... provide transitional assistance to encourage competitive investment and innovation in the Australian automotive industry in order to achieve sustainable growth, both in the Australian market and internationally, in the context of trade liberalisation. (Minchin 1999)

In anticipation of further tariff reductions, the ACIS was extended to 2015 to provide additional transitional support to the industry.

The post-2005 ACIS, like the pre-2005 Scheme, will be a transitional assistance scheme that will encourage competitive investment and innovation by firms in the automotive industry in order to achieve sustainable growth as tariffs are reduced in line with trade liberalisation. (Hockey 2003)

The Automotive Transformation Scheme (ATS) replaced stage 3 of the ACIS (which had been scheduled to run between 2011 and 2015) in 2011. The ATS is part of a suite of programs (*A New Car Plan for a Greener Future* (the New Car Plan)) designed to offer transitional support to the automotive manufacturing industry over the period 2008-09 to 2020-21. The scheme is intended to:

... encourage competitive investment and innovation in the Australian automotive industry and to place the industry on an economically sustainable footing. ... The object of the Scheme will be achieved in a way that improves environmental outcomes and promotes the development of workforce skills. (Carr 2009)

Additional budgetary assistance is provided to the automotive manufacturing industry through other programs under the New Car Plan, and various capital subsidies in the form of co-investment grants provided by the Australian, Victorian and South Australian governments.

Publicly available information on government assistance to the automotive manufacturing industry is patchy — the Victorian Competition and Efficiency Commission (VCEC 2011, p. 112) observed that there is ‘limited public reporting about the effectiveness and efficiency of particular manufacturing programs’, including measures for the Victorian automotive industry. The limited amount of public information on the costs of administering individual programs was also

highlighted. Data for assistance from the Australian and South Australian governments similarly lack public transparency.

Assistance is also provided to the automotive manufacturing industry through government preferential purchasing policies and generally available Australian Government assistance measures, such as tax concessions for eligible research and development activities and export facilitation programs. Other policies affecting the automotive industry include restrictions on the importation of second hand vehicles and taxation arrangements, such as the luxury car tax.

Assistance is high relative to other industries

‘Net combined assistance’ (also referred to as the ‘net subsidy equivalent’ of assistance) is a measure that quantifies the total assistance provided to an industry by tariff and budgetary support policies. The Commission’s estimates suggest that about \$30 billion (2011-12 dollars) was provided to the automotive manufacturing industry between 1997 and 2012. An increasing share of assistance to the automotive manufacturing industry over recent years has been in the form of budgetary (rather than tariff) assistance.

Notwithstanding reductions in the absolute level of assistance to the automotive manufacturing industry over time, the industry remains one of the most heavily assisted in Australia. While some participants (for example, Australian Manufacturing Workers’ Union (AMWU), sub. 28; Peter Dixon, sub. 112; Troy Mascull, sub. 171; Peter Murphy, sub. 139; Heidi Sutherland, sub. 169; Suzanne Swift, sub. 121; Phillip Toner, sub. 34; Maria Votano, sub. 91) noted that the total budgetary assistance provided to the automotive manufacturing industry is less than for a range of other industries and sectors, this does not take account of the relative sizes of the industries.

In 2011-12, the effective rate of assistance — that is, the value of total tariff and budgetary assistance as a proportion of a particular industry’s (unassisted) value added — for the automotive manufacturing industry was 9.4 per cent, substantially higher than for mining (0.3 per cent) and more than twice that for the broader manufacturing sector (4.1 per cent, inclusive of the automotive manufacturing industry) (table 2.1) (PC 2013d).

Table 2.1 **Effective rate of assistance by industry, 2006-07 – 2011-12^a**
Per cent

	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Primary production	5.9	6.4	4.7	4.4	3.4	3.3
Horticulture and fruit growing	4.1	4.2	4.4	4.0	3.7	3.5
Sheep, beef cattle and grain	5.7	6.3	6.3	5.2	3.4	2.7
Other crop growing	7.6	6.9	2.0	2.1	1.2	1.6
Dairy cattle farming	12.5	13.2	4.5	4.3	2.6	1.8
Other livestock farming	1.8	1.7	1.2	1.0	0.9	1.1
Aquaculture and fishing	12.0	6.9	3.5	3.8	3.9	3.3
Forestry and logging	6.9	6.8	-1.3	4.5	5.5	7.2
Primary production services	-0.1	0.2	0.3	0.1	0.1	0.1
Mining	0.2	0.3	0.2	0.3	0.2	0.3
Manufacturing	4.4	4.4	4.6	4.3	4.0	4.1
Food, beverages and tobacco	3.2	3.2	3.4	3.3	3.3	3.3
Textile, clothing and footwear	12.4	12.2	13.8	11.0	9.0	7.3
Wood and paper products	4.8	4.9	5.2	4.6	4.6	4.6
Printing and recorded media	3.4	3.4	3.5	3.4	3.4	3.4
Petroleum, coal & chemicals	2.7	2.7	2.9	2.8	2.9	2.8
Non-metallic mineral products	2.9	3.0	2.9	2.9	2.8	2.8
Metal and fabricated products	4.6	4.4	4.5	4.3	4.3	4.7
Motor vehicle and parts	12.5	11.9	13.1	11.6	8.7	9.4
Other transport equipment	0.8	0.8	0.9	0.9	0.9	0.9
Machinery and equipment	3.2	3.1	3.2	3.1	3.0	3.0
Furniture and other products	4.8	5.0	4.6	4.4	4.4	4.4

^a The effective rate of assistance is the tariff and budgetary assistance expressed as a proportion of the industry's (unassisted) value added.

Source: PC (2013d).

DRAFT FINDING 2.1

The Commission's net combined assistance estimates suggest that about \$30 billion (2011-12 dollars) was provided to the automotive industry between 1997 and 2012. Despite reductions in the absolute level of assistance over time, the automotive manufacturing industry remains one of the most heavily assisted industries in Australia.

Despite the significant amount of government assistance provided to date, automotive manufacturers and others have argued that ongoing industry-specific assistance is required.

Toyota Motor Corporation Australia (Toyota) (trans., p. 166) has stated that government assistance 'needs to be consistent and it needs to be ongoing' in order for its Australian manufacturing operations to be viable. (Toyota has indicated that a decision on whether to proceed with the Australian production of the next

generation Camry model and its export program will be made in 2014.) Enduring assistance arrangements were also supported by the AMWU (sub. 28, p. 22).

If any given country wishes to retain an automotive manufacturing capacity and the huge economic benefits that it brings, it needs to partner with producers through co-investment and other forms of support.

Likewise, the Federation of Automotive Products Manufacturers (FAPM, sub. 69) and Chassis Brakes International (sub. 53) considered that assistance is necessary to offset the various pressures affecting automotive firms in Australia. Prior to announcing the planned closure of its Australian manufacturing operations, General Motors Holden (Holden, sub. 58, p. 2) submitted:

An ongoing private–public partnership is needed in Australia for the automotive manufacturing sector to compete globally. ... The reality is that countries don't have an automotive industry without some form of government assistance.

Other participants called for changes to the scope and design of existing assistance measures. For example, the Australian Automotive Aftermarket Association (sub. 54, p. 33) argued that eligibility for assistance should be expanded to include aftermarket producers so they are better placed to absorb resources 'displaced' by the decline of domestic automotive manufacturing. The merits of possible changes to existing assistance measures (including the ATS) are discussed in chapter 3.

An economywide perspective is important for evaluating assistance options

Industry-specific assistance measures can benefit motor vehicle producers and automotive component manufacturers in various ways; for example, the ATS allows manufacturers to recover as much as 50 per cent of expenditure on eligible research and development activities (chapter 3). However, this assistance imposes costs on other parts of the Australian economy (box 2.1).

Participants' views on economywide effects

A number of inquiry participants emphasised the importance of taking the economywide effects of automotive industry assistance into account. The Australian Chamber of Commerce and Industry (ACCI, sub. 71, p. 1) considered:

When government raises revenue, either in the form of taxes, levies or fines, to fund specific government industry assistance, it imposes economic costs beyond those directly involved in raising the revenue and negatively affects other non-assisted industries ... [The] government needs to take these costs and impacts into account when considering the policy case for government assistance to a specific industry.

Box 2.1 Economywide costs of industry-specific assistance

Industry-specific assistance can impose costs on taxpayers, consumers and other domestic industries. Any benefits that assistance generates for the assisted industry and the wider community must be set against these costs, which can take several forms.

- **A misallocation of resources:** A well-functioning and productive economy allocates resources to where they can yield the largest payoff. Special assistance to specific industries can lead to significant distortions in resource allocation across the economy, detracting from the performance of the economy overall.
- **Higher input and production costs for other domestic industries:** An assisted industry is likely to invest and employ more than it would in the absence of assistance. This can 'bid up' the price of capital and labour for other industries and may result in reduced investment and employment in those industries. Where unassisted firms are involved in exporting into competitive global markets, their competitiveness is reduced owing to their inability to pass these additional costs on.
- **Higher prices for consumers where assistance is provided through tariffs:** Tariff protection raises the prices consumers face, reducing household income for spending on other goods and services.
- **Higher-value uses of public funds forgone where budgetary assistance is provided:** Provision of industry-specific budgetary assistance precludes alternative uses for these resources; governments cannot fund other initiatives that might deliver a greater net return to the community, such as generally available assistance measures or tax cuts for households and businesses.
 - **Alternatively, there will be costs if additional revenue needs to be raised to fund budgetary assistance:** Raising government revenue to fund production subsidies or co-investment capital grants is not costless; even the most efficiently designed and administered tax will have costs.
- **Demonstration effects:** The provision of industry-specific assistance to one industry can encourage other industries to seek similar treatment. This 'rent seeking' activity (even if ultimately unsuccessful) diverts resources away from more productive uses.
- **Compliance and administration costs:** Assistance measures necessarily involve compliance costs for participants and administration costs for governments.

ACCI (sub. 71, attachment A, p. 55) went on to note that while these 'broader unseen economic costs' can be difficult to measure precisely, they 'are real, of a substantial magnitude and represent a loss to the economy'. Garry White (sub. 1, p. 2) made a similar point:

The Productivity Commission should critically assess claims that the positive externalities associated with the industry are sufficient to offset the large economic costs of the assistance ... Assistance to the motor vehicle industry has its own negative externalities for other industries, consumers and taxpayers.

The Australian Industry Group (Ai Group, sub. 42, p. 34) also highlighted the potential market distortions associated with industry-specific assistance:

As a general principle, Ai Group believes that where there is a case for government

intervention, industry programs aimed at lifting the productivity and competitiveness of industry (e.g., through innovation, global supply chains, improved production techniques or skills enhancement) should be available to all businesses, regardless of the sectors in which they operate, their size or their place in the supply chain. This minimises the likelihood of market distortions that can arise from sectoral support measures or from Government ‘picking winners’ (either in terms of sectors or in terms of stages in a particular supply chain).

In its submission to the National Commission of Audit, the Business Council of Australia (BCA 2013, p. 4) argued that the economywide benefits and costs of industry assistance should be regularly reviewed:

The case for industry subsidies will need to be continually reassessed, to ensure that they are well targeted, temporary in nature and contributing to the enhanced long-term productive capacity of the economy.

The Commission’s approach

The key consideration from a policy perspective is whether providing specific assistance to the automotive manufacturing industry is likely to generate a net benefit for the community as a whole, and if so, whether it represents the highest return available for the funds employed.

The appropriate starting point for this analysis is to identify whether there is an ‘in-principle’ case for government to intervene to alter the consumption and production decisions of Australian automotive manufacturers. Generally, when markets function well, they promote efficiency by allocating resources to their highest value use. In those cases, government intervention to alter consumption or production decisions (by way of a subsidy, for example) will lead to a net loss for the community. Although policies that provide industry-specific assistance provide benefits to those who receive that assistance, the costs imposed on the rest of the community outweigh those benefits. Few, if any, markets conform to the competitive ideal and market failures arise for several reasons (box 2.2) but governments should only intervene when markets have ‘failed’ and transactions that would improve the welfare of the overall community do not proceed.

Establishing that there is an in-principle role for government based on a market failure does not necessarily mean that government should intervene. The market failure must be substantial and amenable to government action, and the expected benefits of government intervention must outweigh the expected costs (discussed further below).

Where market failure is such that policy intervention is appropriate, the benefits and costs of alternative policy options must be considered. As noted in box 2.3, the costs

and benefits of alternative options will depend, in part, on whether good practice policy processes are adopted.

Box 2.2 What is a market failure?

In economic theory, when markets function well, resources are allocated to their highest-value uses and no alternative allocation of resources could make the community better off overall.

In practice, there are occasions when markets do not achieve an efficient allocation of resources, due to a number of potential sources of market failure.

- **Externalities:** When the actions of an individual or business create a benefit or a cost for others who are not a party to the transaction, and these effects are not reflected in market prices.
- **Public goods:** Goods that are ‘non-rivalrous’ in use (consumption by one party does not prevent others consuming the same good) and ‘non-excludable’ (people cannot be prevented from consuming the good). Producers and consumers cannot capture the full benefits of provision or payments for provision cannot be enforced. Consequently, public goods are likely to be underprovided by the private sector.
- **Imperfect information:** parties to a transaction are unable to obtain all relevant information about the transaction and the parties to it.
- **Information asymmetry:** Where one party to a transaction knows more about key aspects of that transaction than another party. This may result in:
 - ‘adverse selection’, whereby an information asymmetry biases parties towards lower quality or higher risk transactions
 - ‘moral hazard’, which occurs when a party modifies its behaviour to exploit an information advantage and this affects the magnitude of a payment from another party or the probability of that payment being made.
- **Lack of effective competition:** Where there is natural monopoly, or when the market has a small number of firms that are able to restrict output and maintain prices above efficient levels. However, a small number of participants in the market is not sufficient evidence of the exercise of market power, as the threat of new entrants may discourage the use of market power, as may any countervailing power held by customers.

If a market failure exists, it may be possible for government to improve the inefficient market outcome through some form of intervention (for example, a tax, subsidy or regulation). On the other hand, if there is no market failure, government intervention cannot make society better off overall; that is, there is no unrealised transaction that would distribute resources more efficiently. At best, intervention in an efficient market can redistribute the existing gains among market participants; more likely (given the costs of government intervention — box 2.1), the community overall will be worse off.

Source: PC (2012a).

Box 2.3 **Good policy outcomes depend on good policy processes**

The terms of reference for this inquiry state that automotive industry assistance should be 'accountable, transparent and targeted at the long-term sustainability of the sector'. The Commission considers these to be sound principles for public policy processes.

Transparency

Taxpayers should be informed by government on where and how public funds are being spent. Where assistance involves mutual obligation, this should be clear and measurable by all parties.

Businesses that receive assistance should be required to report on a range of key performance indices. Although commercial confidentiality may justify withholding some information in particular cases, governments should carefully scrutinise calls from assistance recipients for limiting disclosure. In all cases, the effectiveness of industry assistance should be independently evaluated over time and the results should be published. As ACCI (sub. 71, p. 1) noted:

... all government assistance and incentives need to be transparent with predictable funding and should have key review indicators and milestones to gauge whether these programs achieve their intended objectives.

Accountability

Governments and the recipients of public assistance should both be accountable to the public for their actions.

In terms of government accountability, the conditions under which industry assistance measures are established should be clearly articulated upfront, and it should be demonstrated to taxpayers that the benefits to the community from government intervention are expected to exceed the costs. This provides the community with greater confidence that 'value for money' should be attained, while enabling recipients of assistance to make commercial decisions with some measure of clarity and certainty. By contrast, ad hoc policymaking erodes community and business confidence in assistance measures, and may deter recipients (current or prospective) from committing to efficient investments. Policy making and program administration that is not transparent has the same effect.

Businesses, in choosing to accept public assistance, should also be held to account and demonstrate that they are generating the net benefits to the community that underpin that assistance.

To uphold accountability, assistance measures will have administrative and compliance costs. The requirements that are most appropriate will vary on a case-by-case basis. However, to maximise the net benefits for the community, governments should design administrative and compliance requirements that avoid unjustified costs.

Autopolis (sub. 10, p. 10) considered that clear objectives had not been a hallmark of automotive manufacturing industry assistance arrangements, and that future initiatives 'must be considerably more transparent and accountable than has been the case'.

(Continued next page)

Box 2.3 (continued)

Long-term sustainability

Where industry-specific assistance can be justified — given the presence of market failure, and the costs and benefits of policy intervention — it should not be regarded as a permanent lifeline. Well-designed assistance measures should seek to provide a sound footing for industries to achieve commercial viability, free of specific government funding or other advantage. The Victorian Competition and Efficiency Commission (2011, p. 66) found that assistance schemes to a manufacturing industry should only be established where:

- the problem that the assistance is intended to address is expected to be very temporary or a one-off permanent restructuring is needed that would result in a viable, and competitive industry
- the industry would be viable in the long-term without further assistance
- supporting the industry would not be at the expense of the competitiveness of other sectors.

The productivity and long-term sustainability of any industry will still partly depend on the overarching policy environment, and on being exposed to competitive pressures that drive innovation and efficiency improvements. This relies on a credible institutional environment and regulatory arrangements that do not unjustifiably impede investments that contribute to community wellbeing.

Governments may also choose to intervene in markets for equity and fairness reasons (for example, to alleviate the consequences of localised economic disadvantage on the functioning of society). This is an especially relevant consideration for the effects of structural adjustment on the automotive manufacturing workforce. (Adjustment issues and associated policy options are discussed in more detail in chapters 4 and 5.)

In this inquiry, a quantitative comparison of all of the costs and benefits of alternative assistance options — to the degree of precision required to inform policy decisions — is not feasible. Any empirical assessment of assistance options requires baseline assumptions regarding the future state of the industry, which is uncertain following the Ford and Holden announcements to cease automotive manufacturing in Australia. This uncertainty is likely to dominate the effect of changes in assistance, making any quantification of the impact of alternative assistance options highly imprecise. Instead, where it is relevant, the Commission has drawn on the evidence presented to this inquiry and its own analysis to examine, in a more qualitative way, the potential benefits and costs of alternative assistance policy options.

Estimating the costs of adjustment

As outlined in chapter 4, the Commission is undertaking economic modelling for the final report that will focus on the potential magnitude and timing of adjustment in the automotive manufacturing industry.

The Federal Chamber of Automotive Industries (FCAI, sub. 30, attachment A) has submitted economic modelling to this inquiry that suggests that there would be a net present value welfare cost of a shutdown of the automotive manufacturing industry in Australia of \$21.5 billion. The shutdown of all automotive manufacturing (including motor vehicle producers and component producers) was linked with ceasing assistance. The FCAI (sub. 30, attachment A, p. 55) stated that:

... modelling was undertaken to examine the potential impacts on the Australian economy if assistance to the automotive industry were to cease entirely (resulting in the three vehicle manufacturers ceasing production in Australia).

The modelling shows the effect of a shutdown of the Australian automotive manufacturing industry, rather than the effect of changes in assistance. No causal link was established in the economic modelling between ceasing assistance and the industry shutting down.

Further, the welfare result from the modelling in FCAI's submission is sensitive to assumptions about the time taken for the economy to adjust to the shutdown and the timeframe used to calculate net present values. Although the report did not provide precise details on assumptions about the adjustment path, the Commission's analysis suggests that assuming a shorter adjustment path, or estimating net present values for a longer time period, is sufficient to lead to a positive net present value welfare effect from the industry shutting down. The Commission will comment further on this modelling work in its final report.

2.2 Is there an ongoing role for government assistance for the automotive manufacturing industry?

A number of participants supported maintaining or increasing government assistance to the automotive manufacturing industry. Several rationales and arguments were advanced. These related to:

- spillover benefits
- industry linkages (or 'multipliers')

-
- the effect of automotive industry assistance arrangements — in Australia and in relation to assistance offered in other countries — on Australia’s attractiveness as an investment location
 - development of alternative vehicle and component technologies or niche market manufacturing operations
 - the need to counter so-called temporary or ‘transitional’ pressures threatening the viability of the industry, such as the relative strength of the Australian dollar.

The remainder of this section considers whether there is an in-principle case for ongoing government assistance to the Australian automotive manufacturing industry (over and above that which is generally available to all industries); that is, whether the aforementioned rationales constitute some form of market failure. (The potential role of governments in facilitating adjustment for employees and regions affected by structural change, including plant shutdowns, is considered in chapter 5.)

Broader policy and regulatory settings also affect the competitiveness of the Australian automotive manufacturing industry, and the ability of the industry to adjust to changing circumstances. These matters are considered in section 2.3.

Spillover benefits

Many inquiry participants emphasised the benefits that flow from automotive manufacturing to the automotive supply chain, non-automotive industries and the wider community. As highlighted in box 2.4, these benefits — usually referred to as positive ‘spillovers’ — include:

- the transfer of skills as employees move from automotive manufacturing firms to other firms in the supply chain, or outside the industry
- the diffusion of management techniques, such as ‘lean manufacturing’ and ‘just-in-time’ manufacturing systems
- automotive industry research and development (R&D), resulting in new products, techniques, skills and knowledge for other businesses and industries.

As discussed earlier in this chapter, governments should only intervene to provide assistance when there is a market failure. Spillovers can be a form of positive externality (box 2.2) when there are benefits resulting from a transaction that accrue to a party not directly involved in that transaction, and these are not reflected in market prices.

Box 2.4 The relevance of spillovers: participants' views

The Government of South Australia (sub. 68) identified spillover benefits as comprising technology transfers, R&D, new product development and skills transfers.

AutoCRC (sub. 39, p. 6) considered:

A key feature of the automotive industry is the leadership role it plays in the broader Australian manufacturing sector in terms of technology uptake — both in relation to products and processes, and in human capital development. ... The main benefits come from the following areas:

- Efficient manufacturing processes, such as just-in-time and lean manufacturing being adopted as the benchmark in other manufacturing and service sectors;
- Lean product development and stage gate processes being adopted across the manufacturing industry as the standard for new product development;
- Design engineering;
- Quality systems;
- Supply chain management processes and systems;
- Diffusion of new technologies;
- Transfer of skilled staff.

BlueScope (sub. 52, p. 13) found:

Working within the automotive industry increases the level of quality and process control as their standards are often higher than what is required by other segments. The benefits achieved in working at the higher standards in automotive then naturally spill over into other segments ... Similarly, significant improvements and spillover effects have been obtained within research and development teams at BlueScope which has been the result of work completed for the automotive industry.

FAPM (sub. 69, p. 27) stated that the spillovers from automotive manufacturing can spread well beyond car production:

Australia's capabilities in automotive manufacturing have significant spillover effects into other parts of the economy. This includes benefits in the form of technology diffusion, skills and management processes which extend to the mining, food processing, aerospace and defence, healthcare and construction industries to name a few.

This theme was reinforced by the FCAI (sub. 30, attachment A), which cited comments by the chief executives of Rio Tinto (mining), Boeing Australia (aerospace) and Coca-Cola Amatil (food processing) on the flow of benefits from automotive manufacturing to their respective industries.

In this regard, some of the identified benefits from automotive manufacturing that flow to other parties are not grounds for industry-specific assistance. Rather, they reflect the gains shared as a result of normal economic activities, including commercial entities entering into contracts to acquire or supply goods and services, companies hiring employees (with remuneration influenced by skill levels and experience), and consumers buying products with higher embedded value due to

technological improvements. Parties already recognise the benefits of these transactions through the exchange of payment — there is no intrinsic market failure.

- Spillovers may occur in the absence of government funding where there are sufficient commercial incentives for a business to undertake the activity that produces the spillovers.
- Spillovers can come from different sources. In today's world, information, technology and people are continuously moving between firms, industries and economies. Many spillovers may still be obtainable in Australia as a result of automotive manufacturing overseas or from the activities of non-automotive industries here and abroad. The adoption of management techniques practised within the automotive industry is a case in point (box 2.5).

From a policy perspective, the relevant consideration is whether government assistance would yield *additional* benefits that would otherwise go unrealised (and that exceed the costs of that assistance). For example, there may be a role for government if the knowledge generated by innovative R&D in automotive manufacturing can be appropriated by other industries without them contributing to the cost of the initial automotive R&D. This is because the community could be made better off if more of that automotive manufacturing R&D, which would not otherwise occur, were undertaken.

However, the same is true of R&D efforts across all sectors of the economy — this being the reason why all industries in Australia have access to generally available assistance measures, such as the R&D Tax Incentive. As one representative of FAPM acknowledged in relation to their own business:

If the support mechanisms for R&D under the automotive industry were to cease, obviously that would mean that all of my R&D activity, whether it be automotive or non-automotive, would be covered by the other programs [such as R&D tax concessions]. So it's not so much a matter that we're being supported specifically because we're automotive. It's just that we've got a choice of two programs, it's one or the other, and if one doesn't exist, we move to the other. (trans., p. 100)

General government support programs also target areas such as vocational education and training, where the resulting gain in human capital benefits not only the individual worker and their employer, but also the wider community (discussed below).

Box 2.5 **Additionality and ‘lean manufacturing’**

The 2008 Review of Australia’s Automotive Industry (the Bracks Review) included a series of case studies that identified different types of knowledge spillovers associated with the automotive manufacturing industry. These were categorised as:

- internal spillovers, whereby a particular company’s non-automotive operations may benefit from its automotive operations through (among other things) transfers of engineering and production capabilities, and management techniques
- spillovers to suppliers, such as by facilitating their entry into new industries or assisting the development of their competencies
- spillovers to others, including by employees moving to non-automotive industries and through industry collaboration with tertiary institutions on training and research.

The Commission considers that many of the examples provided in the Bracks Review do not demonstrate benefits specifically or uniquely attributable to having an automotive manufacturing industry in Australia — and, by extension, industry-specific assistance measures.

To take one example, a key spillover highlighted by a case study of Toyota was the transfer of knowledge pertaining to ‘lean manufacturing’, which Toyota is credited with developing. (Lean manufacturing focuses on eliminating ‘waste’ — such as lost time or resources — while achieving the same or better outcomes. Examples include just-in-time inventory management and using technology to identify and address errors at their source.) Toyota instils the principles of lean manufacturing in its suppliers and these principles have also been adopted in non-automotive industries.

However, lean manufacturing is now practised in many places throughout the world (including in countries where Toyota operates no manufacturing plants), and is the subject of considerable management literature. In addition, other companies — such as Bosch, which was profiled in another Bracks Review case study — have developed their own variations on lean manufacturing and applied them in Australia. This suggests that the benefits of lean manufacturing would likely have reached Australia in the absence of Toyota’s Australian manufacturing operations.

Source: Bracks (2008).

Industry-specific assistance measures will only be justified where any additional spillover benefits that would be obtained exceed the costs of government intervention. However, as the Commission and others have previously identified, quantification of industry spillovers is complex (Bracks 2008; PC 2002, 2007). There is no sufficiently robust method for directly valuing the spillovers from the automotive manufacturing industry, the value added as a direct consequence of industry-specific assistance, or what might occur to replace the provision of these spillovers from the industry in the counterfactual case if there were no domestic automotive manufacturing.

Some quantitative analyses have drawn conclusions about industry spillovers using indirect measures — for example, analysis undertaken for the 2008 Review of Australia’s Automotive Industry (the Bracks Review) used patent citations as an indicator of spillovers. Although that analysis did not estimate the size of the spillovers from automotive manufacturing, it found:

- almost three quarters of the spillovers generated by patents originating in the Australian automotive industry between 1991 and 1999 were retained within the industry itself (38 per cent) or flowed through to the machinery and equipment industry (35 per cent)
- no other industry individually received more than 6 per cent of the automotive industry’s spillovers.

The Bracks Review concluded that automotive industry spillovers are ‘relatively concentrated’ and that the industry ‘serves only a few other industries with large quantities of spillovers from its own technological activities’ (Bracks 2008, p. 134).

The evidence provided by participants to this inquiry (some of which is highlighted in box 2.4) also lends weight to the view that many of the benefits of domestic automotive manufacturing are retained predominantly within the automotive manufacturing industry supply chain.

In the Commission’s assessment, it is unlikely that the spillovers uniquely associated with Australian automotive manufacturing are of sufficient magnitude (relative to those for other industries) to provide strong support for ongoing industry-specific assistance measures. Furthermore, the Commission does not consider that the particular characteristics of the automotive industry render generally available measures (aimed at supporting spillover-generating activities such as R&D) ineffective.

Industry linkages and multipliers

Industry linkage arguments are often advanced alongside discussions of spillovers. Several inquiry participants pointed to the value created by automotive manufacturing in the broader Australian economy. The FCAI (sub. 30, p. 3) submitted:

Automotive manufacturing in Australia receives around \$500 million in direct government funding each year. For this investment, the Australian economy is \$21.5 billion larger. The \$21.5 billion return does not include significant benefits provided to other parts of the economy as spillovers.

Holden (sub. 58) estimated that for each dollar of government assistance it received, it generated \$18 of economic activity in Australia. Likewise, Toyota (sub. 31) reported that each dollar of government assistance it received resulted in \$20 of domestic economic activity. These economic activity ‘multipliers’ include taxes paid to the Australian and state governments, wages paid to employees, and payments to Australian businesses for supplies and services.

Participants also pointed to employment multiplier effects, with claims of up to 200 000 jobs being ‘indirectly’ associated with automotive manufacturing, in addition to the around 45 000 direct employees of automotive manufacturers and their suppliers (Futuris Automotive (Australia), sub. 9; Society of Automotive Engineers Australasia, sub. 43). The Australian Workplace Innovation and Social Research Centre (sub. 8) reported that the closure of Holden’s automotive manufacturing operations would reduce employment across all sectors of the South Australian economy: using input–output modelling, the Centre estimated that 13 200 jobs would be lost across the state (along with \$72 million per year in state tax revenue).

The automotive industry is not alone in relying on multiplier analysis to measure the value created by its activities, and using this information to justify calls for government assistance. Gretton (2013, p. 1) has examined the ‘uses and abuses’ of input–output multipliers and notes that ‘abuse primarily relates to overstating the economic importance of specific sectoral or regional activities’. Recent examples of multipliers documented by Gretton (2013) include:

- the \$50.1 billion in gross state output and 292 000 jobs attributable to the Queensland resources sector
- the \$555 million in gross national output and 4600 jobs attributable to Merck Sharp and Dohme’s pharmaceutical operations
- the \$524 million in gross output for rural and regional communities and 4996 jobs attributable to Charles Sturt University’s operations in 2010.

Gretton (2013, p. 1) considered it ‘likely that if all [multiplier] analyses were to be aggregated, they would sum to much more than the total for the Australian economy’.

Claims based on ‘multiplier effects’ from promoting production through government assistance typically fail to consider the cost of that assistance to taxpayers and the alternative use of resources in other industries in the economy (which themselves have flow-on effects). For example, a motor vehicle producer might use government funding to buy more parts from component manufacturers, but equally government spending of those resources on health and education (for example) could be used to invest in the health and education workforces — people

who would contribute to Australia’s economic development and social wellbeing, and who would spend their income in ways that also generate economic activity. In the Commission’s view, the reported multipliers do not justify dedicated government assistance to the automotive manufacturing industry.

Attracting foreign capital investment in a global industry

The three motor vehicle producers currently with assembly plants in Australia are global companies that operate many plants across a large number of countries. This means that, in addition to competing in the market against other motor vehicle producers, Australian plants compete internally against affiliated operations within their group for corporate investment, and for the right to supply other markets (within or outside their country). As Toyota (trans., p. 162) noted in 2013 in relation to the production of the next generation Camry model:

We are competing against other Toyota plants in both Japan and the US, and a decision will be made next year for this model. So, many other countries are aggressively pursuing this investment and they have access to both transparent and non-transparent support mechanisms such as direct financial grants, long-term taxation and import duty exemptions, accelerated depreciation, tariff and non-tariff barriers.

Competition for globally mobile capital can be distorted if motor vehicle producers in other countries benefit from significant government assistance. (The Commission has compiled a survey of selected countries’ assistance measures — appendix B.) In this context, a number of participants argued that ongoing government assistance is critical for the Australian automotive industry’s ability to attract and retain investment capital (box 2.6).

Many factors contribute to business investment decisions

As appendix B illustrates, foreign governments adopt a wide range of measures that can promote automotive manufacturing, or impede imports of motor vehicles. These include tariffs, excise duties and other vehicle-related taxes, co-investment grants provided by governments, safety and environmental standards, and incentives for consumers to buy new vehicles.

Although decisions about where to locate automotive manufacturing operations may well be influenced by these policy settings, more fundamental market and competitive factors are driving dramatic changes in the demand for motor vehicles and the location of motor vehicle production. As noted in the Commission’s preliminary findings report (PC 2013b), international trends within the global automotive manufacturing industry and other commercial realities are key

determinants of automotive investment decisions. These factors include:

- changing patterns of consumer demand, with considerable growth in motor vehicle demand in developing countries
- ongoing rationalisation of global production capacity, with overcapacity still remaining in many countries
- the economies of scale associated with mass-market vehicle assembly, with the minimum efficient level for annual production per plant of at least 200 000 units (in most cases)
- the shift towards global platforms for vehicles (away from local, market-specific designs)

Box 2.6 Attracting mobile investment capital: participants' views

The Government of South Australia (sub. 68, p. 43) considered:

Government assistance, through the maintenance of tariffs on automotive products (albeit at significantly lower levels) and through the Automotive Transformation Scheme ... has reduced the disparity in attracting investment with [the Australian automotive manufacturing industry's] global competitors which continue to receive government support through a variety of mechanisms, both overt and hidden and often on a much broader scale.

The FCAI (sub. 30, pp. 6–7) noted:

The industry's competitiveness in attracting global capital is strongly influenced by the level of support, including financial, provided by the national government. On this measure, Australia is at the bottom of the league table. Eroding this modest level of assistance ... increases the level of uncertainty in automotive manufacturing policy and decreases the attractiveness of Australia as an investment destination, compared to competing economies.

The AMWU (sub. 28, p. 4) observed:

... in a globalised world with open capital markets ... what is demonised by some as wasteful industry assistance is often necessary to attract significant and important foreign direct investment. This is exactly the case with the automotive industry.

FAPM (sub. 69, p. 33) argued:

Australia must remain an attractive destination for foreign capital. This includes providing an appropriate balance of incentives for foreign investors, and the public and private sectors being proactive in positioning Australia as a destination for footloose investment.

Ford Motor Company of Australia (sub. 65, pp. 21–2) recommended:

... modifications to the present ATS funding parameters to recognise and facilitate investment in the significant research and development activities undertaken by the automotive companies. This is required to retain and attract high value, complex vehicle design work and engineering capability in Australia which may well otherwise go offshore. ... Innovation, coupled with an ability to attract continuous new global investment, are the keys to a sustainable future for the Australian automotive industry. New funding will be competed for in a difficult global industry where investment funds are scarce and increasingly contestable.

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- differences in production costs across countries, with generally lower costs (especially labour costs) in developing economies
 - the availability and scale of suppliers.

Ultimately, a sound business case is required to underpin long-term capital investment and reinvestment — government policy cannot sustainably alter, or compensate for, these fundamental market and competitive conditions. Indeed, the head of General Motors’ international operations, Stefan Jacoby, was recently quoted in media reports as saying:

Our automotive business is driven by scale — of economics, of productivity, of an efficient supply industry, of sufficient and efficient and optimised logistics. ... The decision [to end Holden’s automotive manufacturing operations by 2017] was not made based on any [government] incentives or any reductions of incentives — it was a purely business-driven decision. (Dowling 2014; Hagon 2014; King 2014)

Similarly, when Ford Motor Company of Australia (Ford) announced the closure of its subsidised manufacturing facilities it noted it was ‘unable to identify a profitable and sustainable business model’ for automotive manufacturing in Australia (sub. 65, p. 14).

Broader costs of policies designed to attract investment

The provision of industry-specific assistance to attract investment (that government judges might not otherwise have occurred) detracts from the performance of the economy overall. The consequences of this policy will vary, but the effect can be to:

- increase the rates of return in the assisted industry and thus draw capital away from other domestic industries (rather than increasing Australia’s total capital stock); for example, where private investment funding is directed to the automotive manufacturing industry and away from other industries
- initiate ‘bidding wars’ between states to attract or retain investment, which generally represents a ‘negative-sum game’ for Australia as a whole (Banks 2002)
- encourage rent-seeking by companies, rather than internal productivity improvement
- waste taxpayer funds on attracting investments that would have gone ahead anyway.

These economywide costs can also be magnified by political factors. As noted below, governments can become hostage to permanently subsidising otherwise loss-making investments. What could be promoted as a policy that will generate

employment and economic activity could ultimately prove to be very expensive over time. Banks (2002, p. 7) noted:

A footloose firm need not stop being footloose simply because an initial inducement has been accepted. Once the inducement ends, the business again has the option of relocating, unless a further inducement is provided to remain.

Furthermore, as discussed above, without sound commercial fundamentals, investments attracted by government inducements are unlikely to translate into sustainable sources of employment and economic activity.

In the Commission's view, it is not in Australia's interests to use industry-specific assistance measures in an attempt to attract or retain globally mobile capital investment. Governments should only offer assistance to an industry if it is in the best interests of the community overall.

Notwithstanding this, governments have a vital role in establishing a policy environment that encourages investment on a sustainable basis. In particular, a skilled workforce, competitive taxation arrangements, sound infrastructure, low regulatory burdens and an appropriate and productivity enhancing industrial relations environment can all have a significant bearing on investment location decisions. The effects of the broader policy and regulatory settings on the Australian automotive manufacturing industry are discussed in section 2.3.

International comparisons of assistance arrangements are problematic

In the Commission's view, care should be taken when comparing assistance arrangements across countries. As has been evident from the Commission's research for this inquiry (and its previous work), and from analyses undertaken by others (box 2.7), the feasibility of robustly quantifying and comparing assistance levels across countries is doubtful. There are several significant constraints.

- First, a number of assumptions are required to add and compare diverse forms of assistance across countries. For example, judging the effective assistance provided by a government-backed loan to an automotive manufacturer in one country against a government local procurement policy in another country requires assessment of the terms and conditions of those policies, the extent to which those policies provide benefits to automotive manufacturers (relative to what would occur in the absence of those policies), and the value of those benefits. Results from such analyses are generally not robust to variations in such assessments.

Box 2.7 Analysis of assistance rates across countries

Sapere Research Group was commissioned by the FCAI to examine an OECD (2010) comparison of international assistance to the automotive industry. The Sapere report (Davey 2011) suggested that assistance to the automotive industry in Australia is relatively low by international standards, and was cited in a number of submissions to this inquiry (AMWU, sub. 28; Diver Consolidated Industries, sub. 25; Efron Media Group, sub. 26; FAPM, sub. 69; FCAI, sub. 30; Futuris Automotive (Australia), sub. 9; Government of South Australia, sub. 68; Anna Mortimore, sub. 64). The report presented the level of assistance on a per capita basis.

Autopolis (sub. 224) reviewed and extended the Sapere estimates to adjust for the nature of each country's budgetary assistance. As noted by Autopolis, the Sapere study 'added all forms of assistance together for each country, assuming all schemes operated in an identical manner' (sub. 224, p. 2). Autopolis also noted that Sapere selected an atypical year — 2009, during the global financial crisis — on which to conduct its analysis. To adjust the Sapere estimates, Autopolis applied cash equivalence rates for different types of assistance. For example, Autopolis discounted the value of government loans by 2 per cent to reflect that the actual benefit to recipients is lower than for assistance provided via cash grants.

Autopolis acknowledged that there are limitations to their estimates, including the failure to include all forms of assistance (whether industry-specific or generally available to all businesses). However, Autopolis' analysis indicates that Sapere's findings are sensitive to adjustments for the different ways that assistance is provided internationally (table 2.2). Furthermore, it reveals that the basis on which assistance is reported — whether per capita or per vehicle (for example) — can result in considerable differences in the estimated rates of subsidy. On a per vehicle basis, Autopolis' adjusted figures suggest Australia has by far the highest rate of assistance of the countries studied.

Table 2.2 Estimates of budgetary assistance to the automotive industry vary widely

	<i>Sapere report</i>	<i>Autopolis</i>	
	<i>(Davey 2011)</i>	<i>(sub. 224)^a</i>	
	\$US per capita	\$US per capita	\$US per vehicle
Australia	17.80	17.75	1885
Canada	96.39	2.00	28
France	147.38	2.97	100
Germany	90.37	14.33	206
Sweden	334.18	5.30	297
UK	27.99	0.56	22
US	264.82	5.41	166

^a Autopolis' estimates are based on figures presented in the Sapere report (Davey 2011), but adjusted to account for the different forms of assistance across countries.

Sources: Autopolis (sub. 224); Davey (2011).

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- Second, there is a lack of quality data on all assistance measures in the public domain, with some governments being considerably less transparent about industry assistance arrangements than others.
 - Third, a range of policy measures with varied objectives and purposes potentially affect automotive manufacturing activities. For example, a policy that has been introduced to promote environmental outcomes may also serve as a barrier to international trade (and is in turn, a form of industry assistance). It can be difficult to ascertain which policies influence automotive manufacturing investment and production decisions, and the extent to which these policies (individually and collectively) assist automotive manufacturing firms.

In sum, given that the range of international assistance measures is so varied in character, timing and transparency, the Commission does not consider it possible or advisable to attempt an overall quantitative analysis of comparative assistance levels to the automotive industry across countries. The caveats that would necessarily apply to the results of any such analyses would be of such significance to render the value of the results negligible.

DRAFT FINDING 2.2

Governments, in Australia and overseas, use various assistance measures in attempts to encourage automotive manufacturing firms to invest and operate in their jurisdictions. Due to the vast range of measures used, and the lack of transparency in the available information, an accurate comparison of the levels of assistance across countries is extremely difficult to do on a like-for-like basis and is not feasible for this inquiry.

Alternative and niche-market vehicle and component manufacturing

Some participants considered that the Australian Government (and in some cases state governments) should provide financial incentives to attract or develop specialised vehicle and component assembly operations as an alternative to mass-market automotive manufacturing. For example:

- FAPM (sub. 69) suggested the use of investment attraction programs to facilitate the entry of niche-market automotive manufacturers, such as electric vehicle producers and contract manufacturers (commissioned to produce cars for multiple car brands)
- Allan Robins (sub. 14) advocated reorienting Australian automotive manufacturing to focus on premium-priced models (which could sustain higher production costs) or specialised commercial vehicles (such as purpose-built taxicabs)

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- in their joint submission, Gas Energy Australia and the Victorian Automobile Chamber of Commerce (sub. 76) proposed that automotive industry assistance be used to encourage gaseous fuel technology (liquefied petroleum gas). Similarly, Marsha Foxman (sub. PFR231) supported government funding for development of alternative energy technologies, including hydrogen fuel cells
 - Swinburne University of Technology (sub. 36) recommended that government incentives be offered for ‘knock-down kit’ production (that is, producing and exporting all the components needed for a vehicle, with vehicle assembly occurring overseas) and for development of a modular platform for customisable vehicles that would be assembled close to or at the point of sale.

In some cases, relatively small production volumes have forced Australian automotive manufacturers to adopt different manufacturing approaches and allowed Australian automotive manufacturers to more easily tailor their manufacturing processes for specific applications and conditions, in turn facilitating export opportunities. Toyota (sub. 31, p. 8) observed:

... lower production volumes offer the opportunity for flexibility and agility. Toyota’s Altona plant is the only one in the Toyota world that has all of its operations on the one premises ...

Component and aftermarket suppliers also reported success in niche markets and differentiated products. For example, MTM (sub. 29, p. 1) considered itself a ‘niche global player’ in supplying doorchecks and gearshift assemblies to automotive manufacturers in Australia and overseas.

However, success in niche markets and differentiated products should be driven by the commercial decisions of participants within the automotive sector. As discussed above, unless there is a clear policy based on market failure, industry assistance is not warranted. Where existing automotive manufacturers and capital markets are unable to identify a sound commercial opportunity to warrant the risk of investing in specialised fields, it is highly unlikely that governments will be better placed to identify and back successful ventures.

Moreover, as discussed above, having committed taxpayer funding to specific ventures that turn out to be uncommercial, political pressures can produce conditions where governments continue to invest beyond a prudent level. These factors militate against governments attempting to direct precisely how any industry should operate. Instead of favouring specific technologies, business models and applications, the Commission considers that an emphasis on supporting innovation in general (in recognition of its spillovers, as discussed above) is likely to yield greater returns for the community.

‘Transitioning’ the Australian automotive manufacturing industry

A number of inquiry participants have argued that further government assistance for automotive manufacturing is justified for industry transition purposes — that is, to help the industry:

- withstand various short-term pressures (such as the strength of the Australian dollar), until a ‘business as usual’ position is restored, and/or
- adjust to more permanent changes in market conditions, such as changing consumer preferences.

For example, the Victorian Government (sub. 70, p. 5) argued:

... the most recent transition arrangements (2008) did not foresee the magnitude of the impact of the rise of the Australian dollar and the dramatic changes in global market dynamics brought about by the global financial crisis, the emergence of new car manufacturing nations, changing consumer preferences, and the pace of the shift to global production platforms ... Support should focus on completing the transition to a profitable, globally integrated, sophisticated domestic industry.

Manufacturing Focus (sub. 33, p. 2) similarly considered that rising costs of production in Australia warrant some form of government assistance to help the industry cope:

Australia’s automotive sector is in serious distress. The cost of producing in Australia has increased significantly in recent years. ... A plan is essential to allow time to systematically transition the industry into a globally relevant, high value automotive manufacturing sector.

However, changes in market conditions do not provide a compelling basis for industry-specific government assistance.

First, assistance to help an industry ‘ride out’ market pressures is likely to dull the incentive for businesses (along with their employees and suppliers) to develop adaptive strategies to respond to changing conditions, for example, by improving productivity, pursuing export options, developing new innovative products, ceasing unsuccessful investments or diversifying into other industries.

Second, as discussed in section 2.1, successive (and significant) government funding programs for the automotive industry have been introduced over several decades to facilitate industry transition, following various changes in government policies and market conditions. However, it is clear that assistance has not been able to overcome market conditions and competitive pressures to prevent the industry’s rationalisation over recent decades.

Autopolis (sub. 10, p. 2) questioned whether transitioning the Australian automotive manufacturing industry to long-term sustainability has ever been a realistic objective of assistance policy:

The [Automotive Transformation Scheme] has been nothing of the sort, as it never defined a viable end state to which to transition. In retrospect, the federal and state governments accepted the industry as the industry chose to define it and proffered support which simply attempted to maintain the status quo.

Third, not all aspects of an industry will be affected by changes in market conditions in the same way. For example, while a stronger Australian dollar may make domestically manufactured exports less competitive, it may also reduce costs for automotive manufacturers that import key inputs. Moreover, many of the market pressures facing the automotive manufacturing industry also affect other domestic (export and import-competing) industries, yet many of these industries do not benefit from industry-specific assistance.

Finally, automotive manufacturing is a global industry, with constant pressure to lower costs and innovate with new products. Hence, while the current challenges facing the industry will ease, new ones will inevitably emerge. In this context, the expectation that transitional assistance is strictly short-term in duration is unlikely to hold up in practice, and is not consistent with past experience. Indeed, the long history of automotive assistance for transition purposes demonstrates how ostensibly temporary assistance can turn into a perpetual supply of ongoing government funding adjusted on a ‘made to measure’ basis.

2.3 How do other government policies affect the automotive manufacturing industry?

The productivity, and long-term sustainability, of any industry depend in part on the overarching policy environment, and on being exposed to competitive pressures that drive innovation and efficiency improvements. Governments also have an important role in establishing a policy environment that facilitates firms’ and ‘employees’ responsiveness to changing circumstances. Key policy areas include those affecting workplace arrangements, taxation, labour market mobility, infrastructure provision and efficiency, and education and training, as well as other policies that can impose regulatory impediments to adjustment.

Workplace arrangements in the automotive manufacturing industry

The national workplace relations system is set out in the *Fair Work Act 2009* (Cwlth) and covers the majority of businesses in Australia (FWO 2012b). Within this system, the National Employment Standards provide 10 legislated essential employment conditions, and 122 modern awards set minimum pay and conditions for employees in a particular industry or occupation (PC 2011). Employees in the automotive manufacturing industry are generally covered by the Vehicle Manufacturing, Repair, Services and Retail Award 2010, with some covered by the Manufacturing and Associated Industries and Occupations Award 2010 or other awards.

Enterprise agreements in the automotive manufacturing industry

Instead of relying on the relevant award, employers and employees in the automotive manufacturing sector have generally opted to negotiate enterprise agreements. Enterprise agreements, and variations to enterprise agreements, must be assessed and approved by the Fair Work Commission (FWC). Ford, Holden, Toyota and many automotive component manufacturers have enterprise agreements in place.

In order for an enterprise agreement to be approved by the FWC, employees covered by the agreement must be ‘better off overall’ under the agreement than under the relevant modern award. This does not imply that wages in the agreement must be higher than those in the award. However, enterprise agreements in the automotive manufacturing industry frequently do contain wages that are higher than those in the relevant award. For example, the base wage for an entry-level adult production employee without trade qualifications is \$928.35 per week under the Ford agreement, and \$819.45 per week under the TI Automotive agreement, compared to the award wage of \$622.20 per week (though this differential does not account for any differences in the skills or other attributes of new hires at different workplaces).

In addition to wages, and in common with practice in other industries, automotive manufacturing employees may also receive allowances, including allowances for possessing certain qualifications (such as first aid or trades licences) or for working under particular conditions (such as confined spaces). But again, the allowances may be higher than is provided for in the relevant award. For instance, at Holden, tradespeople who supply and maintain their own tools are paid an allowance of \$24.20 per week (compared to the tool allowance of \$14.71 per week provided in the award).

Relatively higher wages and allowances can be justified where they are matched by commensurately higher productivity, supported by, for example, flexible workforce arrangements. In this regard, several participants commented on the productivity of the Australian workforce, with Holden noting that its ‘line operators [are] among the most productive automotive workers anywhere in the world’ (trans., p. 206). Toyota said that its ‘Altona facility has achieved record efficiency levels and, for the first time in its history, it is performing at or above Toyota’s global target in terms of production efficiency’ (sub. 31, p. 12).

However, many of the conditions and consultation requirements that have been agreed between automotive manufacturers and their employees and enshrined in enterprise agreements reduce flexibility, with particular effect on employers’ decision-making on a range of operational matters (box 2.8). As noted by Ai Group (sub. 42), and discussed below, when unions have a great deal of bargaining power they are able to pressure employers into agreeing to highly restrictive and costly clauses.

Box 2.8 Conditions in enterprise agreements affect flexibility in the automotive manufacturing industry

Enterprise agreements in the automotive manufacturing industry — particularly those of the motor vehicle producers — contain provisions (that in each case were clearly agreed to at the time by the relevant employers) which can diminish flexibility on a range of operational matters. For instance, under the enterprise agreements currently in force:

- Holden has to obtain union agreement before hiring casual personnel. This includes agreement on the number of casual personnel, the tasks that they will perform and the period for which they will be employed. Union agreement will not be unreasonably withheld
- Toyota has to obtain union agreement to ‘significant organisational change including restructuring and outsourcing’.

Other conditions in enterprise agreements that can affect workplace flexibility are leave and attendance provisions. For example, under Toyota’s enterprise agreement, it has to have an annual closedown of 21 consecutive days’ duration. TI Automotive has to ‘deal sympathetically with requests for [a rostered day off] where it has not been possible to give five working days’ notice’. Ford has agreed that its employees receive their first attendance warning on the sixth occasion of being absent from work without appropriate evidence (such as a certificate from a doctor or other health practitioner) within a 12 month period.

Sources: Ford (2012); Holden (2012); TI Automotive (2013); Toyota (2011).

Factors affecting the content of enterprise agreements

The conditions contained in enterprise agreements are inevitably a product of the environment in which they were negotiated, from an industry, national and international perspective.

In part, the fact that wages, conditions and entitlements in the automotive manufacturing industry in Australia are frequently higher than provided for in the relevant award reflects a global pattern. While Australia is among the highest cost countries in terms of labour costs in automotive manufacturing (PC 2013b), automotive manufacturing employees in other countries also receive higher wages and conditions when compared to some other employees in those countries. In Germany and Japan, for example, automotive manufacturing employees have for many years received higher wages than other manufacturing employees (Spatz and Nunnenkamp 2004). This may in part reflect the bargaining power that employees have in an industry where stopping a manufacturing operation can be very costly to the employer. Payment of wages that are higher than those in other industries may also be influenced by the extent to which automotive manufacturing employers and employees anticipate ongoing government assistance.

However, the conditions contained in enterprise agreements also depend on the workplace legislative framework in place at the time. In Australia, this is the Fair Work Act, which sets out rules and obligations about the conduct of the enterprise bargaining process, the content of enterprise agreements and the resolution of any disputes that arise during bargaining, among other matters.

Automotive manufacturers and industry groups suggested that the current framework can limit workplace flexibility and the scope for productivity improvements. For example, Ai Group (sub. 42, pp. 7–8) said:

Despite the obvious challenges facing Australian automotive manufacturers, unions relentlessly push enterprise bargaining claims which restrict flexibility, often under the banner of ‘job security’ ... those claims inhibit the ability of automotive manufacturing businesses to be responsive and adaptable to market changes ... In the real world the only true job security for workers comes from ensuring that businesses remain profitable and competitive. Flexibility is critical if this is to be achieved.

Concerns about inflexibility are of particular importance given that, as noted in the Commission’s preliminary findings report (PC 2013b), the competitive environment in which Australian and global automotive manufacturing companies operate has changed dramatically over recent years. In response to these changes, Holden and Toyota sought to vary their enterprise agreements in 2013 (box 2.9). Formal variation processes must be followed, as once an enterprise agreement is in place, it continues to operate until it is replaced or terminated by application to the FWC,

even if it has passed its nominal expiry date (FWC 2013). The Holden enterprise agreement has a nominal expiry date of 14 November 2014, while the Toyota and Ford agreements nominally expire on 6 March and 31 July 2015 respectively.

Box 2.9 Variations to automotive manufacturers' enterprise agreements

In 2013, both Holden and Toyota sought to obtain the approval of their employees and the Fair Work Commission to vary their enterprise agreements.

Holden (trans., pp. 207–8) reached:

... a landmark agreement to vary an existing enterprise bargaining agreement with a result as follows: a three-year agreement to a wage freeze, 16 minutes of extra productive time every single day, agreements on things like overtime and all sorts of flexibilities.

The variation to the agreement also included the removal of a requirement for Holden to obtain union agreement on 28 different matters relating to the operation of the business (such as the use of casual labour and contractors). The variation 'was approved by a large majority of employees in August 2013 and approved by the Fair Work Commission in September 2013' (Holden, sub. 58, p. 15). Despite being approved, the changes have not been implemented, as it was agreed they would 'only come into effect once the Next Generation vehicle program is confirmed for Holden's Elizabeth plant' (GM 2013b), and this has not occurred.

Toyota also sought to vary its enterprise agreement in 2013, to remove what it now regards as 'outdated and uncompetitive practices and allowances that increase Toyota's labour costs and reduce its global competitiveness' (Toyota 2013b). Toyota claims that these changes are a vital part of its cost reduction program and will affect its future investment decisions (Toyota Australia 2013). This move was challenged by four Toyota employees on the basis that a clause in the agreement prohibits further claims before it is due to expire in 2015. On 12 December 2013 the Federal Court ruled that although the clause 'restricts the current capacity of Toyota and its employees to vary the wages and other terms and conditions of employment contained in the Agreement, there is no restriction on [the clause] being varied or removed in accordance with the variation process provided by the [Fair Work] Act'.³ This resulted in Toyota being unable to proceed with a planned employee vote on the proposed changes. The Court's decision is being appealed by Toyota. The Australian Government has announced its intention to 'intervene in support of Toyota's workers being allowed a say as soon as possible on the proposed variation' (Abetz 2014).

As of 28 January 2014, Toyota's appeal of the Federal Court's decision relating to its proposed variation to its enterprise agreement was still before the Court (box 2.9). Were the Court's decision to lead to a restriction in the scope for employees to vote on proposed changes to enterprise agreements containing 'no

³ *Marmara v Toyota Motor Corporation Australia Limited* [2013] FCA 1351, para. 142.

further claims' clauses before the nominal expiry date of the agreements, this would have wide-reaching implications for agreements containing those clauses. Such agreements are widespread throughout the automotive manufacturing sector.

In addition to issues relating to flexibility and agreement variation, inquiry participants raised other concerns about the workplace relations framework. Ai Group suggested that the Fair Work Act should be amended to more tightly define the matters that are permitted to be included in an enterprise agreement, and to prohibit the inclusion of certain matters. In particular, it raised concerns about the inclusion in enterprise agreements of restrictions on the use of labour hire, independent contractors and casual employees (sub. 42). Ai Group (2012, p. 63) has previously suggested that enterprise agreements should only be permitted to contain 'matters pertaining to the employment relationship between the employer and the employees', because:

... when the unions have a great deal of bargaining power ... unions are able to pressure the employer into agreeing to highly restrictive and costly clauses, the content of which would, in many cases, not be permitted matters.

Toyota also commented on the need to address risks posed by industrial action. It considered that 'changes to the industrial relations framework should be contemplated to, among other things:

- require industrial laws including those surrounding bargaining to be based, at least to some degree, on productivity and flexibility gains
- set a more reasonable threshold for the definition of 'significant harm' in the context of preventing damaging industrial action' (sub. 31, p. 16).

Proposals to place greater restrictions on the ability of employees to take industrial action or on the matters that may be included in an enterprise agreement raise complex issues. They may also be difficult to enact without affecting other sectors of the economy.

For the final report, the Commission will seek to examine the role that the workplace relations framework may have on competitiveness and productivity in the auto manufacturing industry through further consultations and public hearings. Proposals for changes to the workplace relations framework will also be considered as part of an inquiry into workplace relations that the Commission will soon be asked to undertake (Abbott 2013).

Other policies affecting the automotive manufacturing industry

Taxation

Like every other industry, the automotive manufacturing industry is subject to a range of taxes. It is important for the industry that these taxes allow government revenue to be raised in ways that minimise burdens and distortions. As the Victorian Government (sub. 70, p. 26) noted:

It is imperative that Australia's tax system is efficient and supports business investment and growth. Competitive taxation is also critical for attracting foreign investment. The automotive industry is subject to a number of tax measures including company tax, payroll tax, GST and the Luxury Car tax. Given that the automotive sector is particularly trade exposed, efficient tax design is vital.

Previous reviews of the tax system have found that reducing the overall tax burden, particularly company tax, could have a range of benefits. For example, the Business Tax Working Group (2012, p. 2) noted that 'a lower corporate tax rate could attract foreign investment in industries that are currently struggling with difficult domestic and international economic conditions as well as providing a better environment for investment in the longer term'. Citing these potential benefits, Australia's Future Tax System Review (the Henry Review) recommended that the company income tax rate be reduced from 30 to 25 per cent (Treasury 2010).

The luxury car tax and fringe benefits tax are considered in chapter 3.

Training

The vocational education and training (VET) system is important in providing skills to people employed in the automotive manufacturing industry, and in facilitating firms' and employees' responsiveness to changing circumstances. In many cases, these skills will be transferable to other industries.

Within the VET system, there is a dedicated automotive manufacturing training package that contains seven qualifications and over 100 units of competency (Autoskills Australia 2013). Nationally accredited training — from the automotive manufacturing training package and from other training packages — is provided by a range of registered training organisations. Ford, Holden and Toyota are all registered training organisations, as are other firms such as PACCAR Australia (sub. 61) and DENSO Automotive Systems Australia (sub. 72).

The Australian and state governments provide funding for VET, including VET in the automotive manufacturing sector. For instance, the South Australian Government noted that 'over \$13 million has been invested into this sector to

support more than 4500 people in training and skills development activities’ (Government of South Australia, sub. 68, p. 42).

Government policies can affect the quality and accessibility of training and the responsiveness of the training market. Through the National Agreement for Skills and Workforce Development, governments have undertaken to pursue reforms designed to improve the quality, responsiveness, equity and efficiency of training and training outcomes (COAG 2012). The effectiveness of these reforms will be of particular importance for employees displaced from the automotive manufacturing industry who undertake further training (chapter 5).

The Fair Entitlements Guarantee

The Fair Entitlements Guarantee (FEG) is a legislative scheme that provides financial assistance to employees who have lost their employment due to the liquidation or bankruptcy of their employer and who are owed certain employee entitlements. It was created in 2012 to replace a similar, non-legislated scheme (which was known as GEERS — the General Employee Entitlements and Redundancy Scheme). A range of conditions and caps apply to the assistance that will be provided under the FEG — for example, up to 13 weeks of unpaid wages and a maximum of four weeks redundancy pay per year of service (Department of Employment 2013).

FAPM expressed concern that, because the FEG can only be accessed following the liquidation or bankruptcy of a business, ‘it is often in the interests of acquiring companies for a target to become insolvent or bankrupt so that the employee entitlements including the redundancy liability would not be their responsibility’ and that such liquidation can cause ‘substantial dislocation for the industry’ (sub. 6, p. 51). Other participants expressed concern that the FEG may encourage employers to agree to enterprise agreements containing generous redundancy benefits, on the assumption that such benefits would not be paid by the employer and could instead be provided by the FEG were the firm to go into liquidation.

However, the existence of the FEG and the caps and conditions that currently apply to FEG payments do not appear to warrant any specific policy changes at this time.

- Allowing a firm to become insolvent and cease production in order to avoid paying employee entitlements is a relatively extreme measure that is only likely to be contemplated in limited cases where the ongoing viability of the firm was already in question.

-
- To the extent that such behaviour constitutes fraudulent ‘phoenix’ activity (deliberate liquidation of a company to avoid paying liabilities) (and noting that automotive manufacturing is not among those industries identified as being at high or medium risk of such activity), a range of prevention and enforcement mechanisms are already in place, and more have been proposed (FWO 2012a).
 - The FEG addresses a legitimate community concern to protect the entitlements of employees who would otherwise stand to lose them. The benefits of this protection need to be considered alongside any concerns about the incentives the FEG creates.

Other policies

A wide range of other government policies can affect the automotive manufacturing industry, and also affect industry and labour market adjustment. For example:

- government policies can affect the geographic mobility of labour that is an important element of a well-functioning labour market (box 2.10)
- though Australia already has a national system of qualifications in higher education and vocational education and training — a system that allows skills to be recognised across firms, industries and jurisdictions — differences in occupational licensing may present a barrier for licensed individuals who are considering working interstate (PC 2013c).

The Commission is seeking further information on whether these or any other policies or regulations pose impediments to adjustment and consolidation in the automotive manufacturing industry, and the nature of those impediments.

DRAFT FINDING 2.3

The broader policy environment in which the automotive manufacturing industry operates directly affects the productivity and competitiveness of automotive manufacturers, and the capacity for firms and individuals to respond to changing market and competitive conditions. In particular, workplace arrangements are limiting efforts to promote workplace flexibility and increase productivity in some cases.

INFORMATION REQUEST 2.1

The Commission is seeking further information on the existence and nature of any policy or regulatory impediments to adjustment and consolidation in the automotive manufacturing industry, including for displaced employees.

Box 2.10 **Geographic Labour Mobility**

The Commission is currently undertaking a study into geographic labour mobility. The draft report of that study included the following key findings.

- By improving matches between employers and workers, geographic labour mobility can contribute to economic efficiency and community wellbeing. The main impediments to geographic labour mobility relate to personal factors, and in particular family circumstances.
- Geographic labour mobility has been an important mechanism for adjusting to the demographic, structural and technological forces shaping the Australian economy. It has been assisted by the considerable flexibility shown by employers and employees in overcoming the effects of impediments to mobility. The increase in long-distance commuting and temporary immigration has been particularly important, and should not be impeded by excessive regulation.
- Poorly designed policies, in areas such as taxation, housing and occupational licensing may reduce geographic labour mobility. Reforming these areas would lessen impediments to mobility and have broader benefits to the community. Potential areas of reform include:
 - removing or significantly reducing housing-related stamp duties, and increasing reliance on more efficient taxes, such as broad based land taxes
 - reviewing the level, indexation and eligibility for Commonwealth Rent Assistance to assist the mobility of low income workers in rental accommodation
 - encouraging job services providers to work directly with employers to identify new opportunities for job seekers, including opportunities outside their immediate labour market region where relevant.

The final report of the study will be provided to the Australian Government by 21 May 2014.

Source: PC (2013c).

3 Implications for assistance schemes

Key points

- The policy rationales for specific assistance to automotive manufacturing are weak. The community would benefit from the ending of assistance to automotive manufacturing through the Automotive Transformation Scheme (ATS) and other budgetary assistance schemes, such as the Automotive New Markets Initiative.
 - There is no compelling evidence that spillover and multiplier benefits exceed the costs of assistance to the industry.
 - Decades of transitional assistance have forestalled but not prevented the structural adjustment now being faced by the industry.
 - Assistance imposes costs on the community and dulls incentives to improve productivity, seek export opportunities, and diversify into other industries.
- Current government funding should be reassessed to determine when subsidies should end, and whether to change the timing and amount of funding withdrawn from the ATS.
 - ATS funding for Toyota and other eligible businesses should cease in 2020, and not be extended or replaced with other specific assistance.
 - The closures of the Ford and Holden plants are expected to contribute to an underspend of \$380 million under the legislated ATS funding schedule by 2020.
 - The effect of the uneven profile of funding as per the Mid-Year Economic and Fiscal Outlook (MYEFO) estimates is unclear. It could elevate risks of earlier plant closures by Ford and Holden and might negatively affect investment decisions by Toyota and its component suppliers. A smoother reduction profile would delay the savings benefits, but may reduce adjustment costs.
 - The funding withdrawn from the ATS set out in the MYEFO could result in adjustment costs exceeding the savings benefits. Further feedback is sought.
- Policies that require government agencies to purchase vehicles that are manufactured in Australia for their fleets restrict the choice of cars available for government use, which can impose costs on taxpayers. Any benefits to the automotive manufacturing industry are limited and are unlikely to exceed the costs.
- Restrictions on the import of used vehicles cause distortions in the market and raise the price of used vehicles in Australia.
- Bilateral and regional trade agreements should be pursued where they improve the welfare of Australians overall. However, these agreements may not benefit each individual industry. Some agreements may not reduce export market restrictions facing the Australian automotive manufacturing industry, and may lower barriers to competitive imports.

In 2008, the Australian Government introduced the *New Car Plan for a Greener Future* (New Car Plan) — a suite of programs designed to offer transitional support to the automotive manufacturing industry over the period 2008-09 to 2020-21. While some of the programs in this plan have since concluded, the Automotive Transformation Scheme (section 3.1) and some smaller schemes (section 3.2) remain in operation. The industry is also influenced by mechanisms such as preferential government procurement policies, taxation policy and restrictions on the importation of second-hand vehicles (section 3.3).

The Commission has found that there is no compelling case for governments to provide assistance to the automotive manufacturing industry on an ongoing basis (chapter 2). However, there is a range of possible approaches to withdrawing existing assistance — over various timeframes — and the benefits and costs associated with those approaches vary. This chapter sets out the Commission’s examination of the alternatives and discusses possible approaches to reducing, and eventually removing, prevailing industry-specific assistance measures, taking into account the benefits and costs to the community as a whole.

3.1 The Automotive Transformation Scheme

Overview of the Automotive Transformation Scheme

The Automotive Transformation Scheme (ATS) (and its predecessor the Automotive Competitiveness and Investment Scheme) was put in place to operate as a transitional support measure to assist the industry to adjust to reductions in tariff assistance (chapter 2). To receive assistance under the scheme a person must first meet the requirements to be a registered participant (box 3.1). Registered participants can then apply to receive assistance in the form of cash payments against eligible investments in research and development and plant and equipment, and in the case of motor vehicle producers, eligible production (box 3.2).

ATS assistance is divided into capped assistance, which is subject to annual limits, and uncapped assistance.

- *Capped assistance* is available under the ATS from 2011 to 2020. All ATS participants can apply to receive capped assistance for eligible investments in research and development (at a rate of 50 per cent of the maximum claimable value of research and development) and plant and equipment (15 per cent). In addition, motor vehicle producers can claim capped assistance against the value of eligible production of motor vehicles, engines and engine components (1 per cent). The legislated funding schedule under the ATS (set out in the ATS Regulations) provides for \$2.5 billion of capped assistance, which is spread

across the two stages of the scheme (Stage 1 runs from 2011 to 2015 and Stage 2 from 2016 to 2020). Motor vehicle producers can claim up to 55 per cent of each annual cap, with the remaining 45 per cent available to other eligible ATS participants. If demand for assistance exceeds the cap in a given year, payments to participants are modulated to prevent the total amount of payments from exceeding the cap. The ATS includes a provision that allows for unallocated funding to be rolled over to the annual caps in future years. Unallocated funding is divided between motor vehicle producers and other eligible ATS participants on the same 55:45 basis. Unallocated funding cannot be rolled forward from Stage 1 to Stage 2 of the ATS.

- *Uncapped assistance* is available under the ATS from 2011 to 2017. Uncapped assistance, which is only available to motor vehicle producers registered under the scheme, is paid against the value of eligible production of motor vehicles, engines and engine components. The rate of assistance under the uncapped part of the scheme is scheduled to decrease from 1.5 per cent of the maximum claimable value of production in 2011 to 0.15 per cent in 2017. Commonwealth Department of Industry analysis suggests that \$328 million of uncapped assistance will be provided over the period 2011 to 2017.

Future ATS funding and payments

There is \$1.6 billion of legislated capped assistance still committed to the automotive manufacturing industry under the ATS (as set out in the ATS Regulations) over the period 2014 to 2020, progressively phasing down from 2018 to 2020. The Australian Government included in the 2013-14 Mid-Year Economic and Fiscal Outlook (MYEFO) its pre-announced intention to change the legislated ATS funding schedule. The Government has identified ATS savings of \$500 million in the MYEFO. The resulting funding schedule, however, has an uneven profile — funding would be particularly restricted in 2015, with reductions in 2016 and 2017 also (figure 3.1).

For uncapped assistance, Department of Industry analysis suggests that around \$98 million will be paid to motor vehicle producers between 2014 and 2017.

Box 3.1 Who is eligible to receive assistance under the ATS?

The ATS is open to eligible motor vehicle producers, component producers, machine tool and tooling producers, and service providers. The ATS Regulations outline the requirements a 'person' (meaning an actual or potential ATS participating firm or other entity) must meet in the 12 months preceding an application to be a registered participant under the scheme, and thus be eligible to receive assistance. To apply for registration as:

- a *motor vehicle producer*, a participant must have produced in Australia at least 30 000 motor vehicles or engines
- an *automotive component producer*, a participant must have produced in Australia at least one kind of component used as original equipment in at least 30 000 motor vehicles or engines and the value of the component produced must have been at least \$500 000; or the value of all original equipment components produced in Australia by the participant must have been at least \$500 000 and must have comprised at least 50 per cent of the value of all components produced by the participant
- an *automotive machine tool or tooling producer*, a participant must have produced in Australia machine tools and tooling with a value at least \$500 000 and at least 50 per cent of that value must have been for machine tools and tooling used to produce original equipment for motor vehicles or engines
- an *automotive service provider*, a participant must have provided automotive services in Australia with a value at least \$500 000 and at least 50 per cent of that value must have been for services related to producing motor vehicles or original equipment for motor vehicles or engines.

If the above requirements are not met, a participant can still apply for registration if: (a) they can prove that the above requirements will likely be met in the 12 months following the application; or (b) the relevant Minister is satisfied that registration would be in the national interest. The Regulations outline the matters the Minister must have regard to when deciding whether registration would be in the national interest. While registration is necessary to receive assistance under the ATS, it is not sufficient. Registered participants can only receive assistance if they undertake eligible investments or production.

Source: Automotive Transformation Scheme Regulations 2010.

Box 3.2 What activities attract assistance under the ATS?

Under the ATS, payments are provided to registered participants for eligible investments in research and development and plant and equipment, and the production of motor vehicles, engines and engine components.

- A participant can claim *research and development* activities that are: (a) directly related to the design, development, engineering or production of motor vehicles, engines, engine and other components, machine tools or tooling; and (b) undertaken for the purpose of acquiring new knowledge or creating new or improved materials, products, devices, production processes or services.
 - While this definition applies to all ATS participants, motor vehicle producers may not claim research and development activities that are directed at any production or provision of automotive services for their own use.
- Various types of *plant and equipment* investments can be claimed for assistance. This includes plant and equipment that is used for, or directly supports, the manufacture, assembly, design, development or engineering of motor vehicles, engines, engine and other components, machine tools or tooling. Plant and equipment must be for use in Australia.
 - Motor vehicle producers may not claim plant and equipment used to produce automotive components (other than engines or engine components) for their own use, to produce machine tools or tooling for their own use, or to facilitate the provision of automotive services for their own use.
- Motor vehicle producers can claim the *production of motor vehicles, engines and engine components*. Assistance amounts are based on total sales revenue from each motor vehicle producer's production.

Source: Automotive Transformation Scheme Regulations 2010.

The Department of Industry has provided the Commission with projections of capped ATS payments under two different funding scenarios (table 3.1):

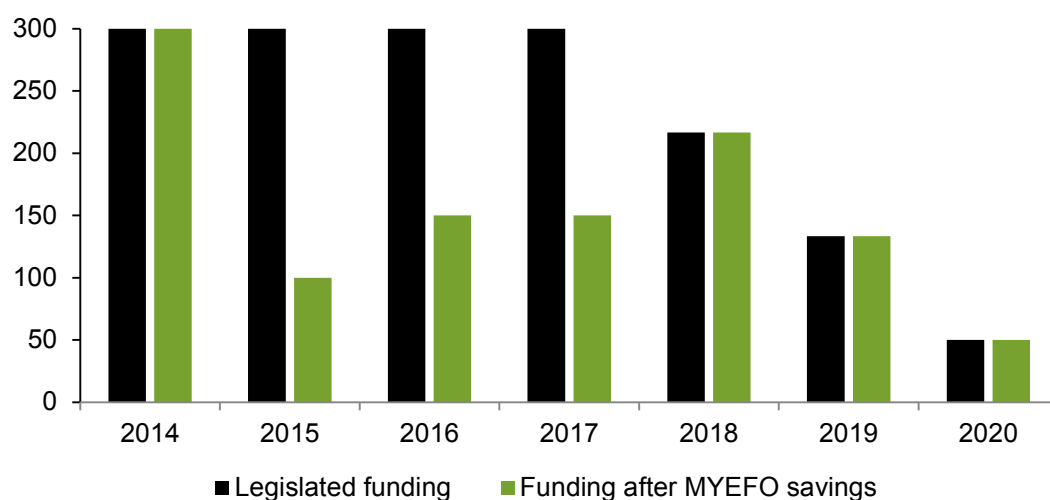
1. the legislated capped funding profile
2. the savings outlined in the 2013-14 MYEFO.

This analysis takes into account the announced closure dates for both Ford Motor Company of Australia (Ford) (October 2016) and General Motors Holden (Holden) (the end of 2017), and assumes that Toyota Motor Corporation of Australia (Toyota) continues to manufacture until at least 2020. The Department has also assumed that Ford and Holden do not receive ATS assistance for any design activities once they cease automotive manufacturing in Australia.¹

¹ Any research and development associated with Holden and Ford design activities conducted under contract for another party would not attract ATS assistance (Department of Industry, pers. comm., January 2014). While Holden or Ford could potentially receive assistance for plant and equipment expenditure, this scenario has not been used for projecting ATS payments.

Figure 3.1 ATS capped funding profile as legislated and after MYEFO savings, 2014–2020^a

\$ million (nominal)



^a The \$500 million reduction in capped ATS funding between 2015 and 2017 is subject to the necessary amendment to the ATS Regulations being made and passing a 15 day period in each House of Parliament during which a motion to disallow the amendments can occur. In a given year actual ATS payments can differ from the annual cap due to unallocated funding, and a provision that allows for unallocated funding to be rolled over to future years. The size of each annual cap depends on whether there are any unallocated funds from the previous year carried forward. The Department of Industry has converted the MYEFO financial-year savings schedule to a calendar year schedule to accord with the ATS calendar year caps. These funding schedules do not depend on the announced decisions of Ford and Holden to cease automotive manufacturing in Australia.

Source: Department of Industry.

Table 3.1 ATS capped payment projections, 2014–2020^a

\$ million (nominal)^b

	Legislated funding profile	Funding with MYEFO savings	Difference between funding profiles
Capped assistance ^c	1 630	1 630	—
MYEFO savings	0	500	—
Available assistance	1 630	1 130	500
Forecast underspend ^d	380	110	270
Forecast expenditure	1 250	1 020	230

^a MYEFO — 2013-14 Mid-Year Economic and Fiscal Outlook. ^b All numbers rounded to the nearest \$10 million. ^c Includes estimated rollover amount of \$34 million from 2013. ^d Comprised of unallocated funds rolled forward to the end of Stage 1 of the scheme (2015) and Stage 2 (2020).

Source: Department of Industry estimates.

Under the currently legislated capped funding scenario, the Department of Industry's analysis suggests that there would be sufficient funds to meet demand for ATS assistance without modulation in every year. Further, the announced exit of Ford and Holden is expected to generate an underspend of around \$380 million over

the life of the scheme (figure 3.2).² This underspend is the sum of unallocated funding that has been rolled forward to the end of each ATS stage. Total payments under the legislated ATS funding profile are expected to be \$1250 million between 2014 and 2020.

Under the \$500 million MYEFO saving scenario, the Department of Industry's analysis suggests that participants would not receive the full amount of assistance that they are likely to qualify for between 2015 and 2017. Thus, there is not expected to be any unallocated funds rolled forward between 2015 and 2017. This will limit the total underspend under the scheme with the MYEFO schedule to \$110 million. Total payments under the MYEFO funding schedule are expected to be \$1020 million between 2014 and 2020. Thus, actual total expenditure under the MYEFO schedule is expected to be \$230 million lower than what is now anticipated under the legislated funding schedule. Expected savings are less than the \$500 million reduction in capped funding due to future year expenditure reductions from the Ford and Holden closures.

The withdrawal of Ford and Holden will have little effect on total uncapped payments, given that this part of the scheme is scheduled to end in 2017.

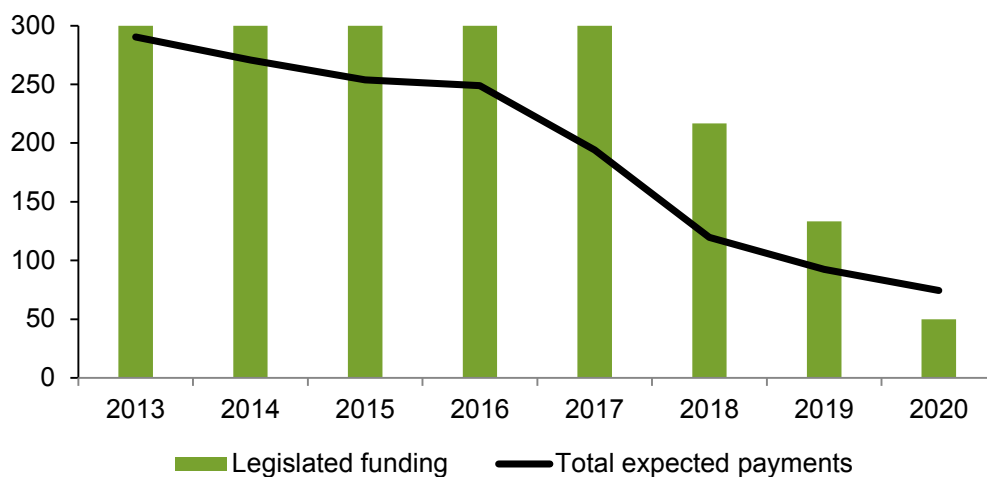
Participants' views on the ATS

Participants expressed a range of views on the ATS. Some participants viewed the ATS as flawed, for example:

[The Australian Government has been determined] to support the national industry by means of a considerable injection of public funds, through [the Automotive Competitiveness and Investment Scheme] and then ATS, even as import tariffs were taken down to negligible levels. This strategy has clearly failed. 2012 production was down almost 50 per cent from the peak and share of world production fell by well over half, as growth accelerated in the emergent markets. Mitsubishi abandoned production in Australia, Ford is now to follow. The Automotive Transformation Scheme has been nothing of the sort, as it never defined a viable end state to which to transition. (Autopolis, sub. 10, p. 2)

² Also, in 2012 the Australian Government committed \$215 million to assist Holden to make capital investments for manufacturing two vehicle models in Australia until 2022. Holden (sub. 58) noted that this funding is contingent on it making the required investments. However, Holden has announced its intention to cease manufacturing vehicles in Australia beyond 2017.

Figure 3.2 ATS capped funding profile as legislated and expected payments, 2013–2020^a
 \$ million (nominal)



^a In a given year actual ATS payments can exceed the yearly cap due to a provision that allows for unallocated funding to be rolled over to future years. The analysis assumes that the Ford and Holden plants close as announced, the legislated funding schedule applies and Toyota continues to operate at least until 2020. The Department of Industry has converted the MYEFO financial-year savings schedule to a calendar year schedule to accord with the ATS calendar year caps.

Source: Department of Industry analysis.

However, many participants were supportive of the ATS and expressed concern about a possible reduction in ATS assistance, for example:

We believe that the immediate priorities for the Federal Government are to confirm as soon as possible the continuation of the ATS, undiminished in value, to confirm continued funding (ROH Automotive, sub. 49, p. 5)

Many participants highlighted the need for policy certainty:

We cannot overemphasize the need for long-term policy certainty. Industry funding cannot be linked to government election or financial cycles. It must be in line with at least the industry’s investment cycle. This is because the automotive industry has long development lead times and requires long-term certainty from government to support product development. If funding is cut in the middle of this process, companies cannot be expected to invest in new vehicle production or design with confidence. (FCAI, sub. 30, p. 7)

Policy stability is especially crucial to programs such as these, that are aimed at fostering long-term investment and innovation. Long-term certainty is all the more important when applied to automotive production, due to the very long lead-times in its investment, planning and decision-making cycle. (Australian Industry Group, sub. 42, p. 41)

... longer term certainty [will] encourage the existing car manufacturers to commit to the local market beyond current model cycles. Additionally, this would provide a

framework to support the investment attraction activities outlined above by ensuring potential investors saw a long term alternative in the Australian market. (FAPM, sub. 69, p. 50)

Some participants proposed changes to the design of the ATS.

- Some participants supported increasing ATS funding above budgeted levels and/or extending ATS funding beyond 2020 (AMWU, sub. 28; FAPM, sub. 69; Futuris Automotive, sub. 9; Holden, sub. 58). For example, Holden (prior to their announced closure) supported perpetual ongoing assistance and at an annual rate above the currently legislated ATS, while the Federation of Automotive Products Manufacturers recommended that assistance arrangements be extended to 2025 and that the assistance package for 2015–2020 be expanded to \$1.5 billion.
- Some participants proposed changes to the eligibility rules for firms providing services to the automotive manufacturing sector (APV Australia, sub. 5; Ford, sub. 65). For example, Ford (sub. 65, p. 21) considered that modifications were required ‘to retain and attract high value, complex vehicle design work and engineering capability in Australia’.
- The Australian Automotive Aftermarket Association (sub. 54) called for extending access to ATS funding to aftermarket suppliers.
- BlueScope and Chassis Brakes International sought changes to key definitions, which would broaden the eligibility requirements. BlueScope (sub. 52) sought a change in the definition of ‘automotive component’; while Chassis Brakes International (sub. 53) sought a change in the definition of ‘automotive company’.
- Other participants saw a need to reconsider how assistance was allocated (participants did not specify how these changes should be funded, but as mentioned above, some supported increased ATS funding overall). For example the Auto CRC (sub. 39) and the Federation of Automotive Products Manufacturers (sub. 69) called for increases in the tooling grant under the ATS. Futuris Automotive (sub. 9, p. 11) suggested lifting the R&D grant to 75 per cent for activities assessed to be strategically aligned ‘towards [Australia’s] natural advantages’ and the Federation of Automotive Products Manufacturers (sub. 69, p. 47) suggested that the rate of assistance for plant and equipment investment ‘in the ATS program be increased from 15 per cent to 35 per cent’.

The Commission's view

The ATS should not be extended or replaced

Industry-specific assistance provided under the ATS subsidises the costs incurred by motor vehicle producers and automotive component suppliers. However, this assistance is not without considerable costs for taxpayers and other parts of the Australian economy (chapter 2). Further, the ATS's objectives appear to be inconsistent with several features of the scheme.

First, the support afforded by the ATS (and its predecessor scheme, the Automotive Competitiveness and Investment Scheme) dulls the commercial incentives faced by automotive manufacturers in Australia. Motor vehicle producers and automotive component manufacturers have had access to considerable industry-specific assistance for adjustment purposes since 2001; the ongoing nature of this assistance partially shields firms from competitive pressures, and may result in firms making decisions that are not based on a sound business case.

Second, to be eligible for ATS assistance, component manufacturers must demonstrate that their components are produced for use in motor vehicles or engine production (box 3.1). This may have reduced the incentive for component manufacturers in Australia to diversify into supplying other industries. Submissions from the Victorian Government (sub. 70) and the Government of South Australia (sub. 68) note that many firms in the automotive supply chain are still heavily reliant on sales to motor vehicle producers in Australia to remain viable. This is notwithstanding Ford's earlier announcement of its intended exit by 2016, as now compounded by Holden's announced 2017 exit.

Any move to increase or extend the ATS would also risk:

- providing negative demonstration effects, whereby other industries are encouraged to seek government funding assistance. As noted by the Commission in its 2002 Review of Automotive Assistance:
... the provision of ad hoc assistance to one firm can create expectations by other potential beneficiaries for similar treatment. This has been shown to lead to unproductive diversion of entrepreneurial effort towards seeking preferred treatment — a phenomenon known as 'rent seeking'. (PC 2002, p. 153)
- drawing attention away from the need for better government policy in areas that could increase the productivity and competitiveness of the economy more generally, as well as in the automotive manufacturing industry.

The policy rationales for industry-specific assistance to automotive manufacturing are weak. The community would benefit from the ending of assistance to

automotive manufacturing through the ATS. The Commission does not support extending the ATS or replacing it with other forms of specific assistance, as this would impose net costs on the community.

DRAFT FINDING 3.1

The policy rationales for providing industry-specific assistance to the automotive manufacturing industry are weak.

Withdrawing legislated ATS funding prematurely has drawbacks

There is a substantial amount of assistance that is committed to the automotive manufacturing industry under the capped part of the ATS. In light of the decision by Ford and Holden to cease manufacturing in Australia, and the Australian Government's pre-announced \$500 million saving in the 2013-14 Mid-Year Economic and Fiscal Outlook (MYEFO), it is timely to consider the most appropriate funding profile until the closure of the ATS.

In the Commission's view, and consistent with its above in-principle arguments, there would be benefits to the Australian community from reducing total capped ATS funding as soon as possible. The announced \$500 million saving clearly falls into this category.

However, consideration should also be given to the potential severity and duration of any transitional costs associated with changing the amount and timing of funding withdrawn from the ATS. While the effect of the MYEFO funding schedule on adjustment costs is unclear, the uneven funding profile could elevate the risk of earlier plant closures by Ford and Holden and might negatively affect investment decisions by Toyota and its component suppliers. The changes to the legislated funding schedule could therefore result in costs greater than the savings benefits by front-loading large, simultaneous adjustment costs throughout the automotive manufacturing industry. The announced savings will potentially elevate policy uncertainty for the automotive manufacturing industry at a time of already major structural change.

A smoother reduction profile would delay the savings benefits, but may also reduce adjustment costs.

The Commission is seeking further information on the potential benefits and costs to the community from the ATS funding schedule resulting from the MYEFO savings. Information is sought as to whether the funding profile could be reconfigured such that the net benefits to the community from phasing out assistance over the period to 2020 are maximised, taking efficiency and equity

considerations into account. The Commission is also seeking information on whether the amount of funding withdrawn from the ATS as outlined in the MYEFO could result in adjustment costs greater than the savings benefits.

INFORMATION REQUEST 3.1

The Commission is seeking further information on:

- *the potential benefits and costs to the community from the Automotive Transformation Scheme (ATS) funding schedule resulting from the 2013-14 Mid-Year Economic and Fiscal Outlook (MYEFO) savings*
- *whether the funding profile could be reconfigured such that the net benefits to the community from phasing out assistance over the period to 2020 are maximised, taking efficiency and equity considerations into account*
- *whether the amount of funding withdrawn from the ATS as outlined in the MYEFO could result in adjustment costs greater than the savings benefits.*

Should Toyota receive extra assistance?

There have been reports that some interested parties are developing a proposal for Toyota (and its component suppliers) to be provided with additional assistance beyond that currently committed to by governments, so as to encourage it to continue automotive manufacturing in Australia.

As noted above, provided Toyota remains as a vehicle producer in Australia, it would receive its full (unmodulated) amount of assistance that it qualifies for in the final three years of the ATS (2018–2020). This outcome holds under both the currently legislated and MYEFO savings scenarios. (The amount of annual assistance that Toyota receives will still be limited by a cap under the scheme that prevents an ATS participant from receiving more than 5 per cent of the sales value of the participant's goods and services for the previous year.) It is also likely that other ATS participants, including component manufacturers, will also receive the full (unmodulated) amount of assistance that they qualify for in the final three years of the ATS (again, this holds under both scenarios).

Additional industry-specific assistance to Toyota would exacerbate the economywide distortions already resulting from the current level of assistance to the automotive manufacturing industry (chapter 2). Further, additional budgetary support could encourage other industries to divert management effort towards seeking preferred government treatment. It is also unclear how effective further assistance would be in view of the global trends noted in the preliminary findings report (PC 2013a) and the associated cost pressures being placed on Toyota. As

noted above, ultimately a sound business case is required to underpin long-term capital investments.

In this context, Toyota (sub. 31) has recognised that it needs to significantly reduce the cost of its manufacturing operations in Australia to secure future investment from its parent company, and its submission detailed its internal cost reduction plans that attempt to achieve this. Toyota also requested ‘a long term, consistent, globally competitive [automotive manufacturing industry] policy suitable for the Australian context to attract future investment’ (sub. 31, p. 3).

Rather than providing extra industry-specific government assistance, in the Commission’s view, it would be more efficient to assist Toyota to continue manufacturing in Australia by ensuring that broader policy settings allow it, and its supplier base, to best respond to market and competitive pressures.

Modifications to assistance rates and eligibility requirements are not supported

The Commission does not consider that there is a compelling case for:

- altering the rates of assistance under the ATS, such as by increasing the rate of assistance available for eligible research and development or investment in plant and equipment
- extending ATS assistance to aftermarket producers.

As the ATS currently operates at or close to its funding cap, the effect of changing assistance rates between different parts of the scheme, without changing the overall amount, would be to reallocate funding among participants. For example, if the rate of assistance for research and development were raised, those participants who have most of their assistance tied to research and development would receive more assistance, at the expense of those participants who have most of their assistance tied to investment in plant and equipment.

As noted above, the Commission considers that the policy rationales for assistance to the automotive manufacturing industry are weak. In light of this, the Commission considers that there is little benefit to be gained from redesigning the scheme to increase the rate of assistance provided, or to provide assistance to a new set of participants.

Similarly, extending ATS assistance to aftermarket producers would transfer ATS funds away from original equipment component manufacturers toward aftermarket firms. Extension of the ATS to another sector of the market could induce a level of

dependence by that sector and run counter to the intention to phase out this transitional scheme.

Should Ford and Holden receive ATS assistance for design services once they cease manufacturing in Australia?

Ford and Holden have stated their intention to maintain automotive design operations in Australia (Ford 2013; GM 2013a). The Department of Industry has advised that, without changes to the scheme, Ford and Holden would not receive assistance for research and development as automotive service providers once they cease manufacturing operations in Australia (Department of Industry, pers. comm., January 2014).

There would be costs and benefits associated with providing assistance for Ford and Holden design services. On the one hand, if these firms were to receive assistance under the non-motor vehicle producer component of the ATS, this could have the effect of reducing the assistance received by the component manufacturers and other firms receiving assistance under this part of the ATS. Such a result may heighten uncertainty during an already difficult period for component manufacturers. On the other hand, providing assistance to Ford and Holden design service activities for the remaining years of the ATS following their planned closure of plants in Australia could assist with the transition for those activities and reduce adjustment pressures during this period.

A relevant issue is that all of the design and engineering work undertaken by Ford and Holden, once they cease manufacturing in Australia, will be for their affiliates overseas. This limits the value of the potential spillovers available to the Australian economy as a result of this work.

On balance, the Commission does not consider that there is sufficient evidence that there would be net benefits to Australia from altering the ATS to provide assistance for Ford and Holden design services once these firms cease manufacturing in Australia.

3.2 Other budgetary assistance programs

In addition to the ATS, the New Car Plan (DIISR 2008) includes several other programs — some of which have concluded. There remain two other New Car Plan schemes that provide direct budgetary assistance to the industry.

- The Green Car Innovation Fund was implemented with a budget of \$1.3 billion (although this was later reduced), and provides grants for research and development and the early-stage commercialisation of projects that reduce the fuel consumption and greenhouse gas emissions of motor vehicles. The government closed this scheme for new entrants in 2011, ahead of the 2018 scheduled end date. Final payments under this scheme are due in 2014-15 (Department of Industry, pers. comm., 5 November 2013).
- In 2012 and 2013, the Australian Government announced capital subsidies in the form of ‘co-investment’ capital grants to support future investment plans of the three motor vehicle producers (subject to these companies proceeding with the relevant investments). These packages include a \$34 million payment made to Ford, and a commitment to pay \$29 million to Toyota, and \$215 million to Holden. The Victorian and South Australian governments also contributed to these packages, although in some cases the value of state government assistance is not publicly available.

In addition, in 2012 the Australian, South Australian and Victorian governments introduced the Automotive New Markets Initiative (ANMI), which is scheduled to run until 2015-16. The ANMI was introduced with \$35 million of funding from the Australian and Victorian governments, and increased to \$47 million as part of the two governments’ response to Ford’s announcement that it would cease manufacturing in 2016. The ANMI consists of three components (Australian Government, Victorian Government and South Australian Government 2012).

- The bulk of the funding (\$42 million) is provided through the Automotive New Markets Program, which provides grants of up to \$1 million for firms that supply automotive components, machine tools or tooling productions, or automotive services. Grants are payable on projects that assist firms in the automotive supply chain to broaden their customer and product base. Around \$13 million has been allocated under the Program to manufacturers such as Australian Precision Technology (to produce components for the defence, aerospace and mining sectors) and Hella Australia (to produce lighting for the military and heavy industry) (Department of Industry 2013a, 2013b).
- The Business Capability Support Program provides support to firms to develop capabilities and improve productivity.

- An Automotive Envoy was appointed to introduce automotive suppliers to new markets within the global supply chain.

Other schemes were included in the New Car Plan but have already concluded, including the Automotive Supply Chain Development Program, which was budgeted to provide \$20 million to component manufacturers between 2009-10 and 2012-13.

The total budgetary assistance available to automotive manufacturers under these schemes between 2013-14 and 2017-18 is estimated to be \$280 million — although a large proportion of this is the Holden co-investment capital grant (table 3.2).

Other assistance schemes under the New Car Plan include the liquefied petroleum gas (LPG) vehicle scheme, which provides payments to purchasers of new vehicles that use LPG technology (section 3.3) and the Automotive Industry Structural Adjustment Program, which provides support for displaced employees (chapter 5).

Table 3.2 Australian Government budgetary assistance to the automotive industry (in addition to the ATS)

\$ million (nominal), 2013-14 – 2017-18.

	<i>Automotive New Markets Initiative</i>	<i>Green Car Innovation Fund</i>	<i>Holden investment incentives^a</i>	<i>Toyota investment incentives</i>
2013-14	11.6	6.1	36.0	6.9
2014-15	10.1	1.1	50.7	18.7
2015-16	7.1	0.0	112.7	1.0
2016-17	0.0	0.0	15.6	1.0
2017-18	0.0	0.0	0.0	1.0
Total^b	28.9	7.1	215.0	28.6

^a This funding is contingent on Holden implementing its 'Next Generation Plan' (Holden, sub. 58, p. 9). ^b Totals may not add due to rounding.

Source: Department of Industry (pers. comm., 5 November 2011).

Participants' views

The Federal Chamber of Automotive Industries (sub. 30) noted that the early closure of the Green Car Innovation Fund had affected policy certainty within the industry. Holden (sub. 58) suggested that the Fund was successful in attracting foreign investment, and the Australian Manufacturing Workers Union (sub. 28) considered that the Fund should be reintroduced in a modified form.

The Australian Manufacturing Workers Union (sub. 28) also supported the ANMI, and suggested the governments should give strong consideration to recommitting to this initiative. AutoCRC (sub. 39, p. 13) considered that business diversification

was a ‘particularly difficult and challenging’ process for most component manufacturers, and recommended that the programs under the ANMI be extended. The Australian Automotive Aftermarket Association (sub. 54) noted that while the Automotive New Market Program had been effective for original equipment component manufacturers, it should not exclude aftermarket producers. The Association also suggested that the Business Capability Support Program was poorly targeted, and that the funds under this program should be diverted to a diversification program that was better targeted.

The Commission’s view

The New Car Plan schemes are likely to have benefited some industry participants, for example, by lowering the cost to automotive firms of research into low-emission motor vehicles. However, the Commission does not consider these benefits are sufficient to outweigh the direct and indirect costs of assistance to the community as a whole.

While there are legitimate spillovers associated with particular types of research and development activity, these are best addressed through generally available measures (chapter 2). Likewise, although product or market diversification is an important part of industry adjustment (and there are examples of such diversification taking place — box 3.3), government intervention is not justified unless there is a market failure impeding this diversification (chapter 2). If efforts to diversify cannot attract market interest then this could simply reflect commercial decisions about allocating scarce resources given the costs, benefits and risks relative to other investment opportunities.

Notwithstanding this, the arguments for retaining the ATS until its scheduled closure date (as outlined in section 3.1) equally apply to other committed budgetary assistance measures. Accordingly, the Commission is proposing that the ANMI continue to operate until the 2015-16 end date, and any committed co-investment packages be honoured, provided that the pre-conditions for such government co-investment (such as proceeding with a new model investment program) are met by the firms concerned. These schemes should not be extended or replaced upon their conclusion.

The Australian and Victorian Governments should not provide Toyota Australia with industry-specific assistance that is additional to the current schemes (which are phasing out).

The Australian Government should not extend or replace the Automotive Transformation Scheme after its scheduled closure in 2020.

The Australian Government should not extend or replace the Green Car Innovation Fund after its scheduled closure in 2014-15.

The Australian, Victorian and South Australian governments should not extend or replace the Automotive New Markets Initiative after its scheduled closure in 2015-16.

The Australian, state and territory governments should not provide any further capital subsidies to the automotive manufacturing industry beyond those already committed.

Box 3.3 Examples of diversification in the automotive supply chain

Many submissions from component manufacturers illustrated examples of component manufacturers diversifying their business away from reliance on the motor vehicle producers in Australia — including via export contracts.

Australian Arrow commenced actively seeking new diversified business in 2011 and we see our new business program as being critical to the long term continuation and targeted growth of Australian Arrow. This program will assist in mitigating some of the risk from the changing Australian automotive landscape and will lessen our dependence on automotive OEM supply. (Australian Arrow, sub. 17, p. 3)

Of critical importance to [Diver Consolidated Industries'] revenue stream over the past four (4) years has been export business attained due to our relationships with local vehicle manufacturers GM-Holden and Ford. ... [Diver Consolidated Industries] has won export contracts ... for products to countries such as Canada, China, South Africa and Brazil for use in the construction of motor vehicles in those countries.

In 2004 [Diver Consolidated Industries'] dependency on the Australian automotive industry was in the order of 99%. With our diversification and new business development efforts this has reduced to ~72% today. That change has taken 9 years. (Diver Consolidated Industries, sub. 25, pp. 6 and 9)

MTM moved into finding non automotive business approximately 8 years ago and is seeing success in 3 key products of Tomcar, Steelsafe, [and] H20 PurePlus ... (MTM, sub. 29, p. 1)

3.3 Other policy relevant arrangements

Government vehicle purchasing policies

The Australian, Victorian and South Australian governments each have fleet purchasing policies that preference vehicles that are manufactured in Australia over imported vehicles (box 3.4). No other state or territory government has such a policy in place (Smartfleet 2013; Victorian Government, sub 70). In July 2013, Salisbury Council in South Australia became the first local government to implement a preferential fleet purchasing policy (Weatherill 2013c). While these preference policies vary in design, the broad purpose is to provide a form of support to the Australian vehicle manufacturing industry.

In 2012-13, Australian-manufactured vehicles accounted for 56 per cent of fleet purchases by the three governments with an Australian-made purchasing policy (the Commonwealth, Victorian and South Australian governments), and 21 per cent of fleet purchases by the remaining state territory and local governments combined (box 3.5 and figure 3.3).

The remaining state, territory and local governments purchased a little over 7000 vehicles that were manufactured in Australia. Using 2012-13 figures, if all governments purchased vehicles manufactured in Australia in the same proportion to total sales as applies to those jurisdictions with a preferential purchasing policy (56 per cent as compared to their current proportion of 21 per cent), the additional number of Australian-manufactured vehicles sold would have exceeded 11 000 (around 5 per cent of Australian vehicle production in 2012). This is broadly consistent with the Victorian Government estimate that if all governments supported fleet procurement that favoured vehicles manufactured in Australia, it could ‘increase sales of domestic made cars by 8000 to 10 000 units per annum’ (sub. 70, p. 36).

Fleet purchases by all governments, of both Australian-produced and imported vehicles, are small in the context of total Australian vehicle production and the sales of Australian-produced vehicles (figure 3.4).

Box 3.4 Government procurement policies

The Australian Government's Fleet Vehicle Selection Policy applies to Commonwealth agencies operating under the *Financial Management and Accountability Act 1997 (Cwlth)* and to those that have 'opted in' under this Act. To comply with the policy, relevant agencies are required to select passenger and light commercial vehicles that are manufactured in Australia, unless it can be demonstrated that no suitable vehicle is available. Moreover, all passenger vehicles (whether made in Australia or imported) purchased by these agencies must have a five-star Australasian New Car Assessment Program (ANCAP) safety rating and all light commercial vehicles purchased must have a minimum four-star ANCAP rating.

A Commonwealth agency that purchases an imported passenger vehicle must provide a business case detailing the operational requirements that precluded the selection of a vehicle that was produced in Australia (Department of Finance 2012a, 2012b). (A business case is not required to justify importing a light commercial vehicle.) Cost is not to be used as an operational reason for purchasing an imported passenger vehicle — the Fleet Vehicle Selection Policy notes that:

When considering an imported passenger vehicle some factors that may not be considered operational requirements include:

- vehicles with similar size, load capacity and clearance to an Australian-made passenger vehicle;
- environmental considerations, such as fuel efficiency; and
- cost of the vehicle. (Department of Finance 2012a, p. 1)

The Victorian Government's standard motor vehicle policy requires that only passenger motor vehicles that are 'substantially manufactured in Australia'³ may be leased or purchased by all Victorian Government departments and selected agencies (the motor vehicle policy is a guideline only for remaining government agencies) (Victorian Government Department of Treasury and Finance 2012, p. 11). Light commercial vehicles must be Australian-made unless there are no suitable Australian-made vehicles that would meet requirements. Executive vehicles must also be Australian-made (Victorian Government Department of Treasury and Finance 2013). Except in certain cases (such as emergency services and police vehicles), Victorian government departments or agencies requiring an exemption to the Australian-made requirement must demonstrate (in writing to VicFleet) a 'clearly defined operational need' to choose an imported passenger vehicle (Victorian Government Department of Treasury and Finance 2012, p. 11).

The South Australian Government Financing Authority (SAFA 2013, p. 21) has noted that:

The purchase of motor vehicles is outside the scope of the State Procurement Act 2004. However, where practicable, the South Australian government supports Australian based manufacturers, purchasing Australian made passenger vehicles where possible.

³ A vehicle is defined as 'substantially manufactured in Australia' if 'the body is assembled and painted in Australia and the compliance plate is fitted at the point of manufacture in Australia'.

Box 3.5 Fleet purchases by governments with and without a preferential purchasing policy

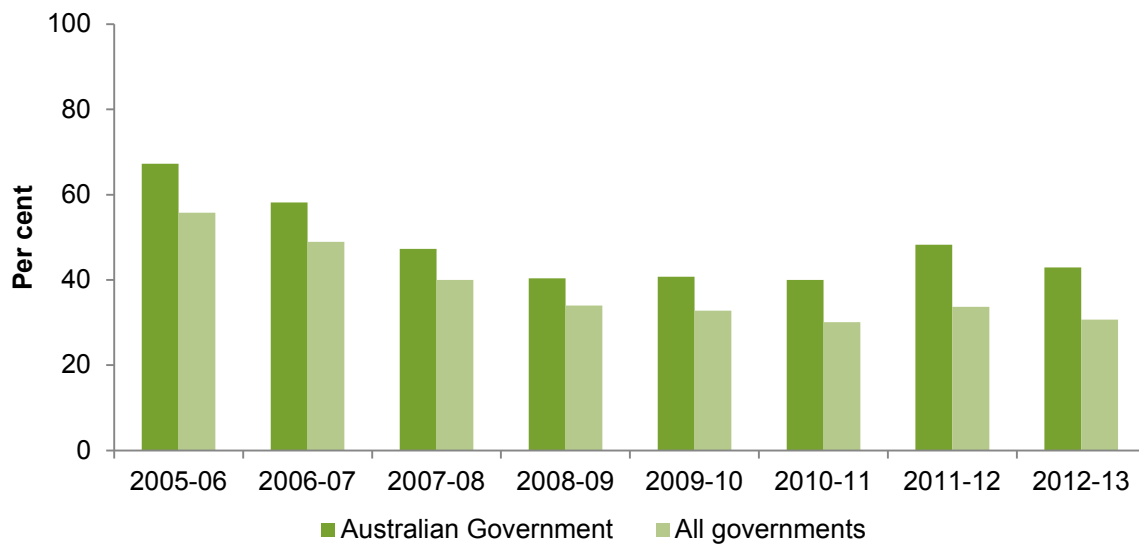
In 2012-13, around 56 per cent of passenger and commercial vehicles purchased by the three jurisdictions with a preferential purchasing policy (the Commonwealth, Victoria and South Australia) were manufactured in Australia, compared to 21 per cent of the fleet purchases of the remaining jurisdictions combined. While this may suggest that preferential purchasing policies are effective in increasing sales of vehicles produced in Australia, the absolute numbers of vehicles purchased by governments are small. All governments together purchase less than 50 000 fleet vehicles annually, limiting the scope of fleet purchasing policies as an avenue for achieving substantial increases in Australian production scale.

<i>Jurisdiction</i>	<i>Total vehicles purchased^a</i>	<i>Imported^a</i>	<i>Manufactured in Australia^a</i>	<i>Proportion of vehicles purchased that are manufactured in Australia^a</i>
	Vehicles	Vehicles	Vehicles	Per cent
All governments	46 232	32 028	14 204	30.7
Governments with a preferential purchasing policy				
Australian Government	2 291	1 308	983	42.9
Victoria	6 701	2 714	3 987	59.5
SA	3 447	1 435	2 012	58.4
	12 439	5 457	6 982	56.1
Governments without a preferential purchasing policy				
NSW	10 622	7 719	2 903	27.3
Queensland	3 872	2 728	1 144	29.5
WA	4 117	3 347	770	18.7
Tasmania	1 373	1 129	244	17.8
ACT	334	277	57	17.1
NT	948	804	144	15.2
Local governments	12 527	10 567	1 960	15.6
	33 793	26 571	7 222	21.4

^a Includes passenger and commercial vehicles. Figures are for 2012-13.

Source: Department of Industry (pers. comm., 4 November 2013).

Figure 3.3 Australian manufactured vehicles as a proportion of government fleet purchases
2005-06 to 2012-13, per cent



All governments: Australian, State and Territory and local governments. Data include all vehicles purchased by government agencies, whether or not they adhere to a preferential purchasing policy, and include privately-plated vehicles such as those 'purchased' by executive staff.

Sources: Department of Industry (pers. comm., 4 November 2013; pers. comm., 15 January 2014).

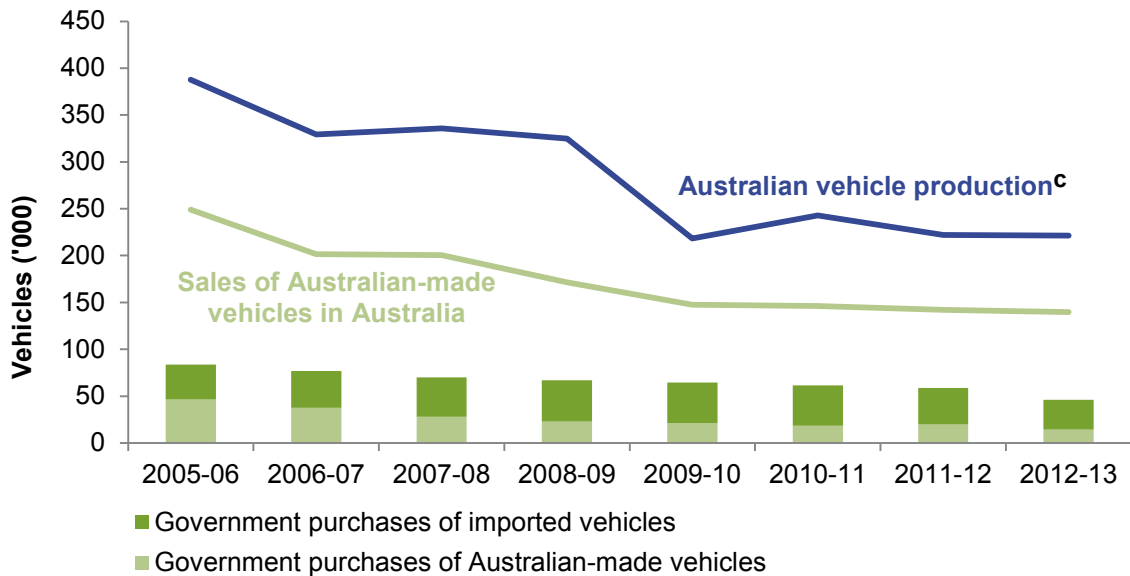
Participants' views

Several participants proposed wider adoption of government purchasing policies that give preference to vehicles manufactured in Australia, as a contribution to help stimulate the sales and production of vehicles manufactured in Australia (AMWU, sub. 28; Diver Consolidated Industries, sub. 25; FAPM, sub. 69; Futuris Automotive, sub. 9; Victorian Government, sub. 70).

For example, the Federation of Automotive Products Manufacturers (sub. 69) recommended that all levels of government, government agencies and publicly-funded organisations adopt fleet procurement policies that require the purchase of vehicles manufactured in Australia unless operational reasons preclude such a choice. The Australian Manufacturers Workers' Union (sub. 28) argued that policies favouring Australian-produced government fleet purchases could be used to support the Australian automotive manufacturing industry while still complying with Australia's World Trade Organization commitments.

Figure 3.4 **Government vehicle purchases^a and Australian vehicle production and sales in Australia^b**

All governments, 2005-06 to 2012-13



^a Commonwealth, State and Territory and local governments. Data include all vehicles (including passenger, light and heavy commercial vehicles) purchased by government agencies, whether or not they adhere to a preferential purchasing policy, and include privately-plated vehicles such as those 'purchased' by executive staff. ^b Fleet purchases data are for all governments and are by financial year, as shown. Australian production data are by calendar year (2005 to 2012). ^c Includes vehicles manufactured in Australia and exported.

Sources: AAI (2013); Department of Industry (2013b; pers. comm., 4 November 2013; pers. comm., 15 January 2014).

The Commission's view

Government fleet purchasing requirements effectively act as a subsidy to producers with a manufacturing presence in Australia. They can impose costs on governments (and in turn, taxpayers), which may include:

- the administrative costs of running the policies
- the regulatory burden on an agency or individual to explain why they did not purchase a vehicle manufactured in Australia, if no suitable vehicle manufactured in Australia is available
- restrictions on the choice of vehicles available to government departments. Government departments and agencies must forgo the potential benefits of purchasing lower-cost, better-suited or better-quality imported vehicles, unless they can justify the decision to choose an imported vehicle on the basis of operational requirements. As noted earlier, the Commonwealth's Fleet Vehicle

Selection Policy explicitly disallows the citing of vehicle cost as an operational requirement.

The benefits of government fleet purchasing policies to the Australian automotive manufacturing industry appear to be limited. Commonwealth, state and territory, and local governments together purchased about 14 200 Australian-manufactured vehicles in 2012-13. This is less than 7 per cent of the approximately 220 000 vehicles produced in Australia in 2012. In addition, once vehicles exported from Australia are taken into account, it is about 10 per cent of the approximately 140 000 Australian-made vehicles sold in Australia. As a result, government purchases are not a substantial contributor to the scale of production for assembly plants in Australia. Looking at this in another way, were there no government procurement policy in place, and assuming that all governments then purchased the same percentage of vehicles manufactured in Australia that applies now to those governments with no preferential policy, the loss of production in Australia would amount to around 4300 cars (box 3.5).

Consideration should also be given to the possible effect of fleet purchasing requirements if Toyota were the only vehicle producer with an Australian manufacturing presence post-2017. Toyota would benefit as the only producer that could meet the requirement that the car must be manufactured in Australia and this may increase its sales of Australian manufactured vehicles. As the only manufacturer eligible under the scheme, there would be no competitive pressures on Toyota in terms of its pricing of vehicles that were essentially ‘required’ to be bought from them. However, this may not be an issue if the scheme were designed in such a way that it provided for benchmarking against the price and performance of imported vehicles. Ultimately, removing this cost and complexity makes sense. Manufacturers in Australia, government agencies, and the community will arguably be better off with no preferential procurement policy and with sales to government being won by manufacturers in Australia on merit.

Overall, the Commission considers that the distortions imposed by government purchasing requirements can impose costs on the community and these are unlikely to be offset by the benefits to motor vehicle producers that manufacture in Australia. Removal of these requirements would be expected to yield net benefits to the economy as a whole.

DRAFT PROPOSAL 3.2

The Australian, Victorian and South Australian governments, by 2018, should remove fleet procurement policies that require government agencies to purchase vehicles manufactured in Australia.

Barriers to importing second-hand vehicles

Second-hand vehicle import duty

In addition to the general 5 per cent tariff applying to all automotive imports, imported second-hand vehicles are notionally subject to a specific customs duty of \$12 000. However, following changes to the *Motor Vehicle Standards Act 1989* in 2000, this duty is now ‘essentially redundant’ (Australian Customs and Border Protection Service, pers. comm., 10 December 2013). Vehicles cannot be imported without a Vehicle Import Approval, and importers may claim exemption from the \$12 000 duty if they obtain such approval prior to importation (Australian Customs and Border Protection Service 2013; DIRD 2013).

Imported used vehicles may otherwise be exempt from the duty under other concessional arrangements as detailed in the Customs Tariff (Schedule 4) — for example, concessional arrangements can apply for vehicles that are 30 years or older, or that have been exported from and subsequently returned to Australia. Based on a sample of imported second-hand vehicles during the period March to November 2013, about 98 per cent of the imports were granted concessional treatment under Schedule 4 provisions (Australian Customs and Border Protection Service, pers. comm., 10 December 2013). (The remainder did not seek concessional entry under Schedule 4, but might have received it under other provisions of the Customs Tariff.)

The effective barriers to importing second-hand vehicles therefore arise from the process of, and requirements for, obtaining a Vehicle Import Approval (discussed below), rather than from the specific \$12 000 duty.

Regulatory requirements for importing second-hand vehicles

The *Motor Vehicle Standards Act 1989* (Cwlth) regulates the importation and supply of road vehicles to the Australian market. (The Department of Infrastructure and Regional Development is currently reviewing this Act.) Although there are several pathways for second-hand cars to be imported into Australia, there appears to be no pathway for the import of a significant number of recently built second-hand vehicles that would meet Australian Design Rule standards. Under the Motor Vehicle Standards Act, applications for approval to place a used import plate (or to supply to the market a used imported vehicle without such a plate) ‘can only be made in respect of a single used imported vehicle’ (sections 13C(2), 16(3)). The Motor Vehicle Standards Regulations 1989 (as amended up to 2012) also prohibit automotive workshops from importing more than 100 used vehicles in each vehicle category in a 12-month period (Part 3 (6a)).

These restrictions have primarily been justified on a consumer protection and road safety basis, as a way of ensuring all vehicles meet minimum safety standards (DIRD 2013). These regulatory arrangements have also been justified as a mechanism to restrict the expansion in used vehicle imports:

The changes made by this bill are intended to ... prevent unchecked growth in the importation of used vehicles that are very similar to vehicles already marketed in full volume [in Australia]. (Commonwealth of Australia 2001, p. 3)

The Commission's view

Restrictions on the importation of second-hand vehicles, particularly the barriers to large-scale importation of such vehicles, reduce competition from this source. Experience from New Zealand (box 3.6) suggests that the importation of second-hand cars may have put downward pressure on second-hand car prices and increased consumer choice in the second-hand vehicle market.

One inquiry participant argued that non-tariff restrictions on second-hand vehicle imports have allowed car companies selling new cars in Australia (particularly premium vehicles) to charge far higher prices in the Australian new vehicle market than they do in other countries, over and above the effect of the luxury car tax (Chop Wood, sub. 2).

The Commission expects that, in the long term, the removal of unjustified restrictions to the large-scale importation of second-hand vehicles would benefit the community as a whole. This does not mean there should be free, unregulated entry of all used imported vehicles. Careful attention should be directed to ensuring that consumer protection and community safety, and environmental performance standards are maintained. These concerns are best dealt with directly, through regulatory standards applicable to all vehicles sold in Australia.

It may also be necessary to allow a lag between any announcement of policy changes and implementation as it will take time to ensure that appropriate regulatory arrangements are in place. Further, consideration (particularly in terms of timing and advanced notice of such changes) should also be given to individuals and businesses that have made investment decisions under the existing regulatory framework. (For example, those involved in vehicle leasing arrangements would need to take account of any effects on estimates of vehicle residual values that underpin lease contracts.)

Box 3.6 Second-hand vehicle imports in New Zealand

New Zealand reduced its vehicle import tariffs from the mid-1980s, as part of a comprehensive program of economic reforms, and removed all tariffs on passenger and light commercial vehicles (excluding motor homes and ambulances) in 1998.

Vehicle imports grew strongly, and most of all, imports of second-hand vehicles. By 2002, used imports represented about 68 per cent of all vehicle registrations in a year, compared with 'well less than 10 per cent' before 1986. Most of these used imports were from Japan, which supplies a large international market for used vehicles as a result of its car registration system. (In Japan, new vehicles are sold with a fitness warranty that is valid for three years, and the costly and time-consuming process of warranty renewal leads many Japanese consumers to replace their vehicles after the three-year period.)

Pawson (2012) reported that the entry of vehicle imports from Japan 'gave New Zealanders access to well-priced late model cars, further increasing the country's high level of car ownership'. A survey by Tunny (2011) of prices for second-hand Toyota Corollas (2006 automatic hatchback model) in Australia and New Zealand found that vehicles of similar mileage were on average almost 20 per cent cheaper in New Zealand than in Australia. (The survey data were taken from online car advertisements, and so might differ from actual sale prices. The survey was also of limited sample size, consisting of five observations for each of Australia and New Zealand for this model.)

Vehicle import assessment

All new and used imported vehicles entering New Zealand must be certified as compliant with relevant approved vehicle standards before they can be registered for road use. Certification is undertaken by NZ Transport Agency-approved certifiers, and the applicable standards depend on vehicle type and date of manufacture or first registration. The certification process includes a physical vehicle inspection as well as the sighting of documentary evidence provided by the importer, showing compliance with New Zealand legal requirements. From 2002, class MA passenger vehicles (those with nine seats or fewer) must also meet an approved frontal impact standard.

Safety performance

In 2005, researchers at the Monash University Accident Research Centre investigated the relative safety of imported used vehicles and vehicles sold new in New Zealand. They found that the used imports were as safe as those sold new when compared on a year-of-manufacture basis, and that the difference in crashworthiness performance between an average used imported vehicle and an average new vehicle was attributable to the date of manufacture of the used vehicle rather than its previous use in its country of origin. More recent (2013) research from the same centre found that improvements in crashworthiness have slowed since 2008, suggesting that the gap in crashworthiness performance between new vehicles and used imported vehicles may be narrowing.

(Continued next page)

Box 3.6 (continued)

Odometer fraud

Tampering with odometer readings of imported used vehicles — so as to show a falsely lower mileage — was a noted problem in New Zealand following removal of second-hand vehicle import barriers. The New Zealand House of Representatives Commerce Committee (2002, p. 3) reported in 2001 that there was ‘little doubt that substantial proportions of used Japanese imported vehicles have their odometer tampered with’. Estimates by industry and consumer groups of the extent of such tampering mostly ranged from 10 to 30 per cent of all imported used vehicles, and as high as 60-70 per cent according to some assessments.

The New Zealand Government subsequently passed the *Motor Vehicle Sales Amendment Act 2010* to increase consumer protection and promote ‘informed purchasing decisions’ in relation to motor vehicle sales (Ministry of Business, Innovation and Employment 2010, p. 1).

Sources: Clerides (2008); House of Representatives Commerce Committee (2002); Ministry for Culture and Heritage (2012); Ministry of Business, Innovation and Employment (2010); Newstead and Watson (2005); Newstead, Watson and Cameron (2013); New Zealand Customs Service (2013); Pawson (2012); PC (2009); Statistics New Zealand (1999).

The Commission is seeking further information on the likely effects of removing restrictions to the import of second-hand vehicles, and any regulatory arrangements that should be put in place before such a policy change is implemented.

DRAFT FINDING 3.2

The policy rationale for prohibiting the large-scale importation of second-hand vehicles into Australia is weak. However, appropriate regulatory measures are required to ensure that consumer protection, community safety, and environmental performance standards are maintained before the restrictions are removed. These concerns are best dealt with directly, through regulatory standards applicable to all vehicles sold in Australia.

The \$12 000 specific duty on imported second-hand vehicles appears to be largely redundant, providing a prima facie case for its removal.

INFORMATION REQUEST 3.2

The Commission is seeking further information on the benefits and costs of removing restrictions on the large-scale importation of second-hand vehicles. In particular:

- *what would be the potential benefits of removing these restrictions?*

-
- *what are the potential costs of removing these restrictions and who bears these costs?*
 - *how could compliance with Australian safety and environmental standards be most efficiently ensured?*
 - *if the benefits are expected to exceed the costs, how should restrictions be removed and over what timeframe?*

Industry-specific tax and subsidy arrangements

Luxury car tax

The luxury car tax (LCT) is a 33 per cent tax levied on the GST-inclusive value of luxury cars over a specified threshold. The LCT was introduced in 2000 at the time of the introduction of the GST and the abolition of the wholesale sales tax. Luxury cars were subject to a substantially higher rate of wholesale sales tax than non-luxury cars. The LCT was designed to maintain this higher rate of taxation, so that the price of luxury cars did not fall dramatically (Costello 1999).

In 2013-14, the LCT thresholds are \$75 375 for fuel-efficient cars (defined as fuel consumption not exceeding seven litres per 100 kilometres) and \$60 316 for other cars. Some cars — including non-passenger commercial vehicles, motor homes, campervans and emergency vehicles — are exempt from the LCT, regardless of their value (ATO 2013b, 2013c). The LCT currently raises around \$400 million a year (Treasury 2013a).

Participants' views

Several participants expressed concern about the structure or effects of the LCT. The Australian Automobile Association noted that 'the Henry Review of Taxation considered the LCT to be an inefficient and discriminatory form of taxation and recommended its abolition' (sub. 77, p. 4). Australian Performance Vehicles (sub. 5) considered that the LCT should not apply to Australian-made vehicles. Toyota characterised the LCT as a 'punitive and inequitable tax' and noted that it 'is *not* a form of protection for local car makers' (sub. 31, p. 2).

The Australian Automobile Association (sub. 77, p. 4) also suggested that the LCT may have adverse effects on the safety of the vehicle fleet:

The LCT severely constrains consumer choice by pricing a significant portion of buyers out of the market for vehicles priced at the higher end of the market. ... the base model of vehicle which falls under the LCT threshold may not include ground breaking safety technologies. The cost of adding safety enhancing features, such as adaptive

cruise control, a lane departure warning system or a blind spot monitor, may push the price of vehicle over the LCT threshold, potentially affecting a buyer's decision whether or not to include such features.

Futuris Automotive pointed out that since 2007, there has been a large increase in the proportion of cars on the market that attract the LCT (sub. 9).

The Commission's view

The choice and design of taxes is important for productivity, in the automotive industry and more broadly. As the Henry Tax Review noted:

Tax and transfer policy should support productivity through the efficient allocation of investment and productive resources to their most highly valued uses. When products are taxed at the same rate, relative prices will be unaffected and there will be less impact on the decisions of individuals and businesses. A broad base also enables a lower rate of tax for a given revenue objective, which results in smaller distortions to people's and businesses' choices. Broadly-based taxes are, therefore, more consistent with an allocation of resources in the economy that supports a high rate of economic growth and individual satisfaction. (Commonwealth of Australia 2009a, p. 18)

Because it is levied on a narrow base, the LCT is a higher-cost and less efficient method of raising revenue than more broadly based taxes. The LCT is also arbitrary in its effect, in that it leads to taxpayers with the same economic means paying different amounts of tax depending on their tastes. It 'falls on people with a preference for relatively expensive cars, but not on those with a preference for diamonds, fur coats or yachts' (Commonwealth of Australia 2009b, p. 475).

The Henry Tax Review found that the LCT was one of the taxes that should, in time, 'be abolished and their revenues replaced by taxes applying to the four robust and efficient tax bases' (Commonwealth of Australia 2009a, p. xviii).

However, given the effect on government revenue if the LCT were not replaced by another revenue source, it is important that its removal be considered as part of a broader package of taxation reform measures. The Australian Government has announced that a Taxation White Paper will be prepared (Hockey and Sinodinos 2013), and this may provide an appropriate opportunity to consider the removal of the LCT, alternative revenue sources and associated transition issues.

Exemptions from fringe benefits tax for certain commercial vehicles

Certain benefits provided by employers to employees in place of salary or wages are subject to fringe benefits tax (FBT). Employers who make a car available for an employee's private use are generally taken to be providing a car fringe benefit,

which is subject to FBT (ATO 2009). However, a FBT exemption is available for an employee's private use of a taxi, panel van, utility or other commercial vehicle if such use is generally limited to travel between home and work and to other infrequent or incidental use (ATO 2013a). Estimates of the cost to the Australian Government of this exemption are not available (Treasury 2013b).

Several participants considered that the FBT exemption for commercial vehicles should be changed in some way.

- Chassis Brakes International advocated removing the FBT exemption from imported vehicles in order to increase sales of vehicles manufactured in Australia (sub. 53).
- Diver Consolidated Industries suggested that the FBT exemption is being used for work vehicles 'that are not true work vehicles, i.e. 4-door pick-up trucks and utilities, effectively passenger car substitutes' (sub. 25, p. 6). Futuris Automotive expressed similar concerns (sub. 9).
- Diver Consolidated Industries (sub. 25), the Federation of Automotive Products Manufacturers (sub. 69) and Futuris Automotive (sub. 9) suggested that the FBT exemption should be available for 'environmentally friendly models including hybrid and factory fitted LPG vehicles' (FAPM, sub. 69, p. 53).

In making these suggestions, participants were advocating the use of the FBT exemption to support Australian manufacturing or promote purchases of motor vehicles or improve environmental outcomes. However, the rationale for using the FBT exemption instead of more targeted policies to promote these aims is unclear, particularly as the FBT exemption only affects a small proportion of the vehicle fleet. As discussed in chapter 2, the policy rationales for industry-specific government assistance to automotive manufacturing are weak. If government intervention is warranted to improve environmental outcomes, it should be undertaken using policies designed specifically to achieve those environmental objectives, rather than through changes to the FBT exemption.

Bilateral and regional trade agreements

The removal of trade impediments by other countries could potentially facilitate access to export markets and benefit exporting firms in Australia's automotive manufacturing industry. Recognising this, the Bracks Review of Australia's Automotive Industry recommended the expansion of bilateral and regional trade agreements (BRTAs) with a focus on the Gulf States, the Association of South East Asian Nations and South Africa (Bracks 2008).

Some participants in this inquiry similarly suggested that the removal of trade barriers and/or the use of BRTAs could aid the automotive manufacturing industry in Australia (Australian Industry Group, sub. 42; BlueScope, sub. 52; Diver Consolidated Industries, sub. 25; FAPM, sub. 69; Government of South Australia, sub. 68; PolyPacific, sub. 44; Victorian Government, sub. 70).

BRTAs do not necessarily equate to 'free-trade'

It should be noted that the removal or reduction of tariff barriers in some export markets may not necessarily deliver the desired access to those markets, as sought by Australian automotive manufacturers. Although BRTAs are often termed 'free trade agreements', in reality these agreements entail the exchange of 'concessions' between partner economies with the aim of advantaging trade between those partners (PC 2010). The result is that while some trade barriers are removed, many remain in place, creating uneven access to the partner markets depending on the terms of the BRTA in question.

In addition, many countries block importer access by imposing non-tariff barriers such as excises, taxes, quality standards and certification or registration programs (appendix B). For example, despite the presence of a BRTA between Australia and Thailand, Thailand's excise on motor vehicles according to engine size disadvantages particular Australian car exporters, such as Ford:

Even if published tariff rates under negotiated Free Trade Agreements appear to be reasonable, many non-tariff barriers come into play to effectively reduce the potential for significant or worthwhile export opportunity. For example, despite the terms of the trade agreement negotiated with Thailand (TAFTA), Ford Territory diesel vehicles exported to Thailand incur a 40 per cent domestic excise tax (71.4 per cent in actual practice), impacting its relative cost competitiveness and making it a luxury, niche market entrant and limiting its volume potential. (Ford, sub. 65, p. 9)

Participants highlighted that these non-tariff barriers can be significant and should be taken into consideration when negotiating further BRTAs (AAAA, sub. 54; Australian Motor Industry Federation, sub. 74; David Baker, sub. 16; Toyota, sub. 31).

BRTAs may not benefit automotive manufacturers

Even were the non-tariff barriers to Australian exports to be addressed, it is not clear that the automotive manufacturing industry will benefit from a BRTA. Although BRTAs may yield net benefits for Australian consumers and Australia as a whole, they typically create groups of 'winners' and 'losers' in industry (PC 2010). Accordingly, the outcome for automotive manufacturers is mixed.

Firms may gain through the trade arrangement if they get improved access to an export market. For example, Toyota (sub. 31) noted that a BRTA with Gulf Cooperation Council nations would help it compete with vehicles produced in the United States — many of which enter those nations free of tariffs due to US negotiated BRTAs. Other firms that could be expected to benefit are those that gain access to cheaper imports due to a reduction in tariffs. As discussed below, Toyota (sub. 31) noted that the general tariffs that it and its component suppliers in Australia pay — around \$300 per vehicle on imported parts — are particularly challenging given the severe cost pressure on the industry.

Firms that are likely to lose from a BRTA are those that are disadvantaged by increased competition arising from reduced tariffs on imports. For example, some participants highlighted that the BRTA between Australia and Thailand had encouraged a significant increase in imports of cars from Thailand which now enter Australia duty free (Diver Consolidated Industries, sub. 25; FAPM, sub. 69).

Whether or not a particular BRTA results in a net benefit to the automotive manufacturing industry depends largely on the balance of firms that gain versus those that lose, and on the particular conditions agreed to during the negotiation of the agreement. Some participants in this inquiry expressed the opinion that past BRTAs had disadvantaged Australian automotive manufacturers (Australian Performance Vehicles, sub. 5; BlueScope, sub. 52; Government of South Australia, sub. 68; John Lyons, sub. 12; Murat Kiremitciyan, sub. 6; PolyPacific, sub. 44; ROH Automotive, sub. 49).

The Commission's view

Given these concerns, the Commission is sceptical that BRTAs are a solution to the challenges faced by the automotive manufacturing industry. As a matter of principle, BRTAs should be negotiated with the overall welfare of Australia in mind, but this may not necessarily benefit individual industries (such as automotive manufacturing). In addition, the Commission reiterates its caution that '[w]hether any particular BRTA generates net benefits, and the extent of those benefits, depends crucially on its design' (PC 2010, p. 231). Agreements that exclude particular sectors or do not account for behind the border measures, can create distortions and entrench protection and special treatment. Furthermore, the benefits of agreements can be eroded by transaction costs if negotiation is prolonged or if there are complex administrative processes, such as rules of origin, tied to the agreement (PC 2010).

Tariff concession arrangements

A five per cent tariff applies on vehicles and automotive components imported into Australia. However, there are some measures in place that allow for the duty-free or concessional entry of goods into Australia. One such measure is the tariff concession system. This system allows for importers to apply for a tariff concession order on goods, if substitutable goods are not produced in Australia. If a tariff concession order is granted, all importers of the good subject to the order can import the good at a duty-free rate (Australian Customs and Border Protection Service 2010).

Some goods, including original equipment components, are on the ‘excluded goods schedule’ (schedule 2 of the Customs Regulations 1926), and are ineligible to be the subject of an application for a tariff concession order. Toyota (sub. 31) raised concerns with this provision, noting that it and its component suppliers pay around \$300 tariff per vehicle on components either directly imported by Toyota, or imported by its component suppliers. As a result, automotive components would first need to be removed from the excluded goods schedule before an application for a tariff concession order could be lodged.

Removing automotive components from the excluded goods schedule would have costs for some automotive manufacturers and benefits for others. On the one hand, motor vehicle producers and some component manufacturers could benefit from receiving a concessional duty on selected imports. On the other hand, there may be differential effects on component suppliers (depending on whether they import components or compete against importers), and there would be administrative costs associated with applying for, and processing, tariff concession orders (some of which may be unsuccessful). The Commission is seeking further information on the costs and benefits of concession arrangements for those seeking to import automotive components before determining whether policy reform is necessary.

INFORMATION REQUEST 3.3

The Commission is seeking further information on the costs and benefits of allowing importers to apply for tariff concession orders for automotive components.

ANCAP vehicle safety ratings

The Australasian New Car Assessment Program (ANCAP) undertakes safety testing and safety assessments on new vehicles in Australia, and ‘provides consumers with independent and transparent advice and information on the level of occupant protection provided by vehicles in serious crashes and ... on the fitting of advanced

safety assist technology ...’ (ANCAP, sub. 18, p. 1). The ANCAP rating system provides information to consumers by awarding vehicles a rating from one star to five stars. The scheme is not binding on manufacturers or importers — a separate set of standards (the Australian Design Rules) regulates the design of vehicles sold in Australia, including required safety features.

Several participants suggested the use of ANCAP safety ratings as a tool to assist the Australian automotive industry. Futuris Automotive (sub. 9), the Australian Manufacturing Workers Union (sub. 28) and the Federation of Automotive Products Manufacturers (sub. 69) all suggested discouraging the purchase of vehicles that are less than 5 star rated, such as by requiring consumers to pay higher registration fees for such vehicles. Futuris Automotive (sub. 9) noted that, as all vehicles manufactured in Australia are 5 star ANCAP rated, such a policy would lead to people moving to safer, and perhaps Australian-manufactured, vehicles.

The Commission considers that linking registration fees to ANCAP safety ratings is unlikely to have any substantial influence on the motor vehicle producers in Australia. While all vehicles manufactured in Australia are 5 star rated, the majority of imported vehicles are now also 4 or 5 star rated. Of the 474 vehicles tested by ANCAP since 1993, 252 vehicles (53 per cent) have been given a 5 star rating and 164 (35 per cent) have been given a 4 star rating (ANCAP 2013). The policy could also have the effect of raising motor vehicle prices for Australian consumers.

There may be benefits to vehicle safety from linking registration fees to ANCAP ratings. In particular, motor vehicle producers would have an incentive to ensure their vehicles for import into Australia met the requirements of the new policy. However, such a scheme would have only marginal, and possibly short-lived, effects on the sale of motor vehicles produced in Australia.

The costs and benefits of proposals to increase safety should be assessed in their own right, prior to the implementation of such a policy. This issue is beyond the scope of this inquiry.

Gaseous fuelled vehicles

The Australian Government currently provides support for the LPG sector through the LPG Vehicle scheme, which began in 2006. This scheme initially provided a grant of up to \$1000 for consumers to purchase a new vehicle fitted with LPG capabilities, or to convert an existing vehicle to use LPG. This grant was doubled to \$2000 for new LPG vehicles in the New Car Plan to ‘make new LPG vehicles more affordable to Australian families [and] encourage the early adoption of new technologies’ (DIISR 2008, p. 11). The scheme has provided just under

\$600-million in grants since it commenced. Around 3500 grants have been made for the purchase of new LPG vehicles, and around 310 000 have been for the conversion of an existing vehicle to LPG (AusIndustry 2013b). The scheme is scheduled to close to new entrants on 30 June 2014.

Some participants suggested that further support should be granted to the LPG industry, pointing to Australia's large reserves of gaseous fuels as a competitive advantage in this area. Futuris Automotive (sub. 9) suggested that there should be a government rebate for the purchase of gaseous fuelled vehicles, and that these vehicles should be exempt from FBT. The Federation of Automotive Products Manufacturers (sub. 69) also suggested that a FBT exemption should apply for the purchase of such vehicles. Gas Energy Australia and the Victorian Automobile Chamber of Commerce (sub. 76) suggested a range of support measures for the gaseous fuel industry, including an extension of the LPG Vehicle Scheme and amending the ATS to enable greater access to the scheme for the LPG industry.

The Commission does not consider that government support for the gaseous fuels industry is warranted beyond the scheduled conclusion of the LPG Vehicle Scheme. The choice of fuel type for a vehicle should not be distorted by differential tax or excise arrangements for that fuel, or by government subsidies which favour one fuel over another, unless such a policy was based on a clearly defined market failure, such as environmental externalities arising from vehicle emissions. If motor vehicle producers in Australia were to switch to manufacturing more LPG vehicles, or natural gas powered vehicles, this should reflect a commercial decision, which would take into account any advantage granted by Australia's reserves of gaseous fuels, and should not require support from the government (chapter 2).

4 Adjustment costs for automotive manufacturing employees

Key points

- The Australian automotive manufacturing industry has undergone significant structural change in recent years, resulting in a reduction in employment of about 40 per cent over the period 2006 to 2013.
 - The decisions by Ford and Holden to cease manufacturing in Australia by 2016 and 2017, respectively, will lead to further reductions in employment.
- The extent of any further contraction in automotive component manufacturing, and consequent reduction in overall employment, will depend on a number of factors, including:
 - the extent to which component manufacturers choose to, and are able to, diversify into international automotive markets and other products
 - Toyota’s decisions about its future manufacturing operations in Australia.
- Retrenchments can be costly for affected employees and their families.
 - Displaced employees who are unemployed for any period suffer a loss of income and can incur costs such as job search, training, skills assessment, occupational licensing, and relocation.
 - When displaced employees find new employment, their income may be lower and they may have less employment security, relative to their previous job.
 - Prolonged periods of unemployment or joblessness also involve non-financial costs (such loss of vocational skills and adverse effects on mental health).
- The magnitude of adjustment costs will partly depend on the characteristics of affected employees and regions, the level of redundancy payments, and the time that employees and regions have to prepare for change.
- Adjustment pressures in regard to automotive manufacturing closures are likely to be concentrated within regions of Victoria and South Australia.
 - Relatively high levels of unemployment and social disadvantage in some sub-regions, such as Playford in northern Adelaide and Dandenong in south eastern Melbourne, will likely exacerbate adjustment costs.
- The individual characteristics of displaced employees will also affect adjustment costs.
 - Low skill levels may be an impediment to re-employment for some automotive manufacturing employees.
 - Older people who have been retrenched are less likely to find re-employment.

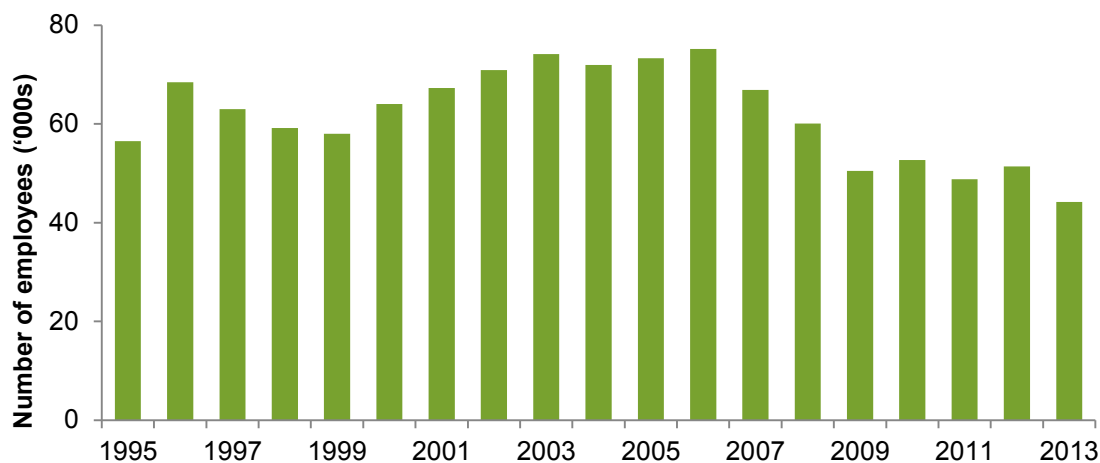
4.1 An industry in transition

The automotive manufacturing industry has undergone significant structural change

As noted earlier, the Australian automotive manufacturing industry has undergone significant structural change. This has been in response to changing market and competitive conditions overseas and in Australia, and lower levels of government assistance (PC 2013a). Since 2006, Mitsubishi has closed its Australian manufacturing operations and the total number of vehicles produced in Australia has reduced from around 300 000 in 2006 to around 200 000 in 2013. The number of firms that manufacture automotive components has also fallen (IbisWorld 2013a, 2013b, 2013c, 2013d).

Employment in automotive manufacturing decreased by about 40 per cent over the period 2006 to 2013 — around 44 000 people in Australia were employed in the industry in 2013 (figure 4.1). For perspective, employment in automotive manufacturing comprised 4.7 per cent of total manufacturing in 2013. Employment in manufacturing (excluding automotive manufacturing) decreased by 5.7 per cent over the period 2006 to 2013 (ABS 2013a).

Figure 4.1 **Employment in automotive manufacturing**
1995 to 2013^a



^a Employment figures are based on quarterly employment, averaged to the November quarter of each year, for ANZSIC06 Group 231 (Motor vehicle and parts manufacturing). This includes business units mainly engaged in motor vehicle manufacturing (class 2311), in motor vehicle body and trailer manufacturing (class 2312), in automotive electrical component manufacturing (class 2313), and in other motor vehicle parts manufacturing (class 2319).

Source: ABS (Labour Force, Australia, Detailed, Quarterly, November 2013, Cat. no. 6291.0.55.003).

Further industry adjustment will occur in the short to medium term

Motor vehicle producers

Further reductions in employment in automotive manufacturing will occur in the next few years, following the announcements by Ford and Holden that they will cease manufacturing in Australia by 2016 and 2017, respectively. These closures will directly displace about 2500 employees in Victoria and 1600 employees in South Australia (table 4.1). Some of these employees might leave before the closures, such that the reduction in employment will be spread over time.¹

Table 4.1 Closures announced by Ford and Holden in 2013

	<i>Timing</i>	<i>Directly displaced employees</i>
Ford	<ul style="list-style-type: none"> motor vehicle and engine manufacturing operations to cease in October 2016 	<ul style="list-style-type: none"> 1 200 Broadmeadows (northern Melbourne) and Geelong, Victoria^a
Holden	<ul style="list-style-type: none"> motor vehicle and engine manufacturing to cease by end of 2017 	<ul style="list-style-type: none"> 1 600 Elizabeth (northern Adelaide), South Australia^b 1 300 Port Melbourne and Lang Lang, Victoria^c

^a Ford's assembly plant and head office is located in Broadmeadows and its engine plant is located in Geelong. ^b Holden's vehicle assembly plant is located in Elizabeth. ^c Holden's design and engineering, engine plant, and head office are located in Port Melbourne and its proving ground is located in Lang Lang, near Melbourne.

Sources: Ford (2013); GM (2013a).

Following Holden's announcement in December 2013 of its plans to cease manufacturing in Australia, Toyota indicated that it was reviewing whether it could continue operating, as it would become the sole passenger motor vehicle manufacturer in Australia (Toyota 2013a).

Toyota has indicated that a decision whether to proceed with the Australian production of the next generation Camry model will be made in 2014. The outcome of this decision will be an important factor influencing the scale, timing, and location of further reductions in employment in automotive manufacturing. Around 2500 people are directly employed in manufacturing at Toyota's vehicle assembly and engine manufacturing plant in Victoria (table 4.2).

¹ For example, employment at BHP was around 2800 when it announced in 1997 that it would close its plant in Newcastle in 1999. With retirements and those leaving over the subsequent two years, there were around 900 needing assistance to find further employment when the facility finally closed (PC 2012b).

Table 4.2 Toyota's Australian manufacturing operations, 2013

<i>Activities</i>	<i>Main locations</i>	<i>Direct employees</i>
Manufacturing	Melbourne (Altona)	2 500
Supporting activities (corporate, R&D, marketing and sales)	Melbourne (Altona, Port Melbourne, Notting Hill) and Sydney	1 900 ^a
Total		4 400

^a Includes 200 employees at Toyota Australia's sister company, Toyota Technical Center Asia Pacific Australia, which undertakes R&D and supports Toyota Australia's manufacturing operations. The facility is located in Notting Hill, Melbourne.

Sources: Victorian Government (sub. 70); Toyota (sub. 31, p. 4).

Structural adjustment pressures go beyond motor vehicle assembly operations

A complex supply chain supports motor vehicle assembly and engine manufacturing. It includes component manufacturers, the suppliers of products such as steel and paint, and providers of automotive research and development, design and engineering services.

As a consequence of changing market conditions, some component manufacturers have already closed or have undergone considerable structural adjustment by diversifying into other industries or export markets (box 4.1). Others remain reliant on passenger vehicle production in Australia for their business and will be heavily affected by the announced closure of the assembly and engine manufacturing plants. For example, TI Automotive, a subsidiary of a specialist global firm, noted that its Australian operations are entirely dependent on the assembly of passenger vehicles in Australia (TI Automotive, sub. 62).

The extent of any contraction in automotive component manufacturing, and any consequent reduction in overall employment, will depend on a number of factors. These include the extent to which component manufacturers choose to, and are able to, diversify into other markets (such as exports, aftermarket products and non-automotive products).

Other segments in the automotive manufacturing industry in Australia are less vulnerable to the announced closures. These segments include the aftermarket parts manufacturers and producers of trucks and buses (AAAA, sub. 54; Australian Industry Group, sub. 42; CNH Industrial ANZ, sub. 60).

There are an additional 233 000 or so people employed in the repair, maintenance and retailing of motor vehicles and parts (as distinct from the development or production of motor vehicles, engines or automotive components). This workforce is largely independent of, and not significantly influenced by, the degree of automotive manufacturing in Australia.

Box 4.1 The extent and regional nature of component suppliers' dependence on motor vehicle producers

The level and regional distribution of employment losses in the component sector due to the planned Ford and Holden plant closures depend on the extent to which component suppliers rely on these motor vehicle producers for sales, and their ability to diversify sustainably into other markets.

Domestic production of components for use by motor vehicle producers within Australia is heavily concentrated in Victoria and South Australia. Of motor vehicle producers' total purchases of components manufactured in Australia, it is estimated that around 70 per cent are sourced from firms in Victoria and around 20 per cent from firms in South Australia (Productivity Commission estimates using FCAI sub. 30, attachment A).

Further, each of the motor vehicle producers appear to source the majority of their Australian-produced components from within the state in which it is located. Around 70 per cent of Holden's purchases of Australian-produced components are estimated to be sourced from South Australia where it carries out assembly operations, and around 30 per cent from Victoria where it manufactures engines (Productivity Commission estimates using Australian Workplace Innovation and Social Research Centre, sub. 8; Holden, sub. 58).

Despite this regional concentration, some component manufacturers have diversified into other markets to a significant extent. Industry reports indicate that on average around 30 per cent of component manufacturers' revenue is from sales to the Australian aftermarket, and around 20 per cent is from exports (IbisWorld 2013d).

The Commission's approach to evaluating adjustment costs

The Commission has examined the nature and incidence of possible adjustment costs in the automotive manufacturing industry to inform its evaluation of adjustment assistance options (chapter 5). To gain insights into these adjustment issues, the Commission has examined evidence from other large-scale retrenchments in Australia (table 4.3). The Commission is undertaking quantitative analysis to provide further insights into the potential scale of effects on employees, regions and the economy, arising from adjustment pressures in the automotive manufacturing industry. In February 2014, the Commission expects to release the interim results of quantitative modelling, and will hold a technical roundtable on this analysis in early March 2014.

Table 4.3 Examples of other large-scale retrenchments in Australia

<i>Company</i>	<i>Timing</i>	<i>Location</i>	<i>Directly displaced employees</i>
Nissan	• assembly plant closed 1992	Clayton, Melbourne	1 800
Ansett	• collapsed in September 2001	Australia-wide	16 000
Mitsubishi	• engine foundry closed and downsizing at assembly plant 2004	Lonsdale and Tonsley Park, Adelaide	1 100
	• assembly plant closed March 2008	Tonsley Park, Adelaide	930
Holden	• closed third shift at assembly plant in 2005	Adelaide	1 400
BHP Steel	• steelworks closed 1999	Newcastle	2 800
Electrolux	• closed two factories in 2006/2007	Adelaide	500
	• announced closure for 2016	Orange	500

Sources: ABC (2008); Electrolux (2013); Beer et al. (2006); Hutton (1992); Pankhania and Farrell (2013); PC (2012b); Valadkhani (2003).

4.2 Costs of industry adjustment for employees

Retrenchments resulting from industry adjustment can be costly for affected employees and their families. For example, displaced employees who are unemployed for any period suffer a loss of income and can incur costs associated with seeking alternative employment, such as job search, skills assessment, training, occupational licensing (from changing occupation or jurisdiction), and relocation (Francois, Jansen and Peters 2011; PC 2001). When displaced employees find new employment, for many their income may be lower and they may have less employment security, relative to their previous job (OECD 2013) (box 4.2).

For some employees, retrenchment can lead to prolonged unemployment or involuntary joblessness². In such circumstances the affected individuals can lose some of their vocational skills and find it increasingly difficult to return to work (Haynes et al. 2011; PC 2001). Unemployed people are also at a higher risk of deep and persistent social exclusion, which encompasses people's reduced participation in educational, work-related, and community activities (McLachlan, Gilfillan and Gordon 2013). Job loss and long-term unemployment can also have adverse consequences for a person's health; for example, increased stress and loss of self-esteem can affect their mental health (Bartley 1994; Beer et al. 2006; PC 2001). Some of these adverse effects can flow on to a person's family and society more generally (Beale and Nethercott 1985; McLachlan, Gilfillan and Gordon 2013; PC 2001).

² Involuntary joblessness includes discouraged job seekers (people who want to work but are not actively looking because they do not believe they would find a job).

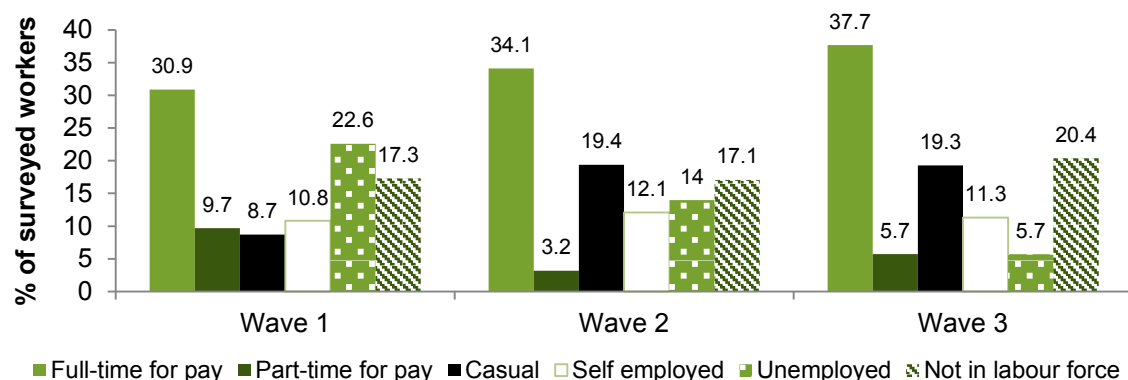
Box 4.2 Survey of retrenched Mitsubishi employees

In 2004, Mitsubishi Australia announced the closure of its Lonsdale engine manufacturing plant and a reduction in capacity at its Tonsley Park assembly plant, resulting in 700 involuntary retrenchments at Lonsdale and 400 voluntary retrenchments at Tonsley Park. Following the restructure and plant closure, researchers surveyed a sample of retrenched employees in three 'waves'. Wave 1 took place within 6 months of retrenchment, wave 2 took place approximately a year after wave 1, and wave 3 took place approximately a year after wave 2.

The survey results indicate that many respondents experienced a loss of employment security. One third of the previously full-time permanent employees were in full-time paid employment 12–18 months after retrenchment, around a quarter were in casual or part-time paid work, and 12 per cent were self-employed. In wave 2 interviews, many respondents reported that they had struggled to find full-time employment and had to settle for casual or part-time contract positions (Armstrong et al. 2008).

Many respondents also reported a decrease in income. In wave 2 interviews, 72 per cent of respondents reported that they were now earning less than when employed at Mitsubishi. Of those surveyed, 11 per cent reported that they were on the same income, and 15 per cent reported that they earned a higher income. The survey results suggest that the lower earnings partly reflected the shift from full-time to part-time or casual work for many displaced employees, as well as the reality that Mitsubishi paid above the market rate (Armstrong et al. 2008).

Over time there was a progressive increase in the proportion of former Mitsubishi employees who found employment and a decrease in the proportion unemployed (who had not exited the labour force). By wave 3, the unemployment rate among those surveyed was 5.7 per cent. In wave 3 interviews, many of the respondents reported incurring non-financial costs as a result of retrenchment. For example, when asked: 'What has been the most difficult thing about leaving [Mitsubishi]?', the most common response was 'Loss of social interaction' (37 per cent of respondents).



Note: Over the course of the research, 71 of 372 participants withdrew from the study. To the extent those who leave a study are likely to be more or less successful in finding re-employment than those who continue, this attrition might bias estimates of employment patterns from the survey.

Sources: Armstrong et al. (2008); Beer (2008); Beer et al. (2006); Pieters (2013).

A number of papers draw on the surveys of retrenched Mitsubishi employees (Beer 2008; Beer et al. 2006; Pieters 2013) to evaluate employment and other outcomes for displaced automotive manufacturing employees. Further studies could inform policy decisions on adjustment options when workforces and regions face structural adjustment challenges. The Commission's draft report on Geographic Labour Mobility highlighted the potential benefits of a longitudinal study of retrenched Ford workers for understanding the long-term effects of structural adjustment (PC 2013c).

The magnitude of adjustment costs will partly depend on the adaptive capacity of employees and regions

The magnitude of adjustment costs is a direct reflection of the speed at which the economy manages to redirect resources (Francois, Jansen and Peters 2011). Labour adjustment costs will depend on the extent to which other industries are able to absorb displaced employees and the length of time it takes those employees to find re-employment.

The characteristics of affected employees and regions will influence the magnitude of adjustment costs (Borland 1998; PC 2001). Relevant factors include:

- The number of displaced employees — the greater the number of people displaced, the more difficult it will be on average for a displaced employee to obtain a new job. This is likely to be a particularly significant factor where a large number of displaced employees live in a small, local labour market (Borland 1998).
- Local labour market conditions — the size of the labour market, its job composition, and its prevailing rate of unemployment. For example, a displaced employee's opportunities for matching with a new job are likely to be highest in a local labour market with a large number and diverse mix of jobs (Borland 1998).
- Individual characteristics of displaced employees, such as age, skills, previous occupation, and the extent to which they may be able to, or willing to, work (and possibly live) in a different location. For example, displaced employees that are older will generally face greater difficulties finding re-employment.

There are also broader factors that can influence adjustment costs, including the flexibility of labour and credit markets (chapter 2), factors that influence geographic labour mobility including the housing market in the region affected by industry structural adjustment and housing affordability in other regions, and macroeconomic conditions. With respect to the latter, the South Australian

Government (sub. 68) noted that Mitsubishi closed its manufacturing operations at a time when the economy was relatively buoyant, and argued that it is much less likely that people who stand to lose their jobs through the closure of Holden's Elizabeth assembly plant will be able to find alternative manufacturing jobs.

The magnitude of adjustment costs will also depend on the time that employees have to prepare for change

The magnitude of adjustment costs will also depend on the amount of time between notification of planned closure and the actual time of closure. Advanced notice of closures or downsizing is likely to reduce adjustment costs by giving employees time to seek alternative employment while still employed and increasing the likelihood they move directly into new employment without any period out of employment (Addison and Blackburn 1997; Fallick 1996; Friesen 1997). In this respect, Ford and Holden have announced their intention to cease manufacturing between three and four years ahead of their planned closure dates. This is a substantially longer notification period than in some other large-scale retrenchments in Australia, such as when Ansett Airlines was placed in voluntary administration in September 2001 and ceased passenger airline operations two days later (Weller and Webber 2004).

A number of employees currently working for component manufacturers (many of which are small to medium size firms) that may be forced to downsize or close as a result of Ford and Holden's plant closures may not receive the same degree of notice from their employers as those working for Ford or Holden.

4.3 Preliminary evaluation of adjustment costs in the automotive manufacturing industry

Adjustment pressures are likely to be concentrated within specific regions of Victoria and South Australia

Employment in automotive manufacturing is geographically concentrated in south east Australia. In 2011, Victoria accounted for about half of all automotive manufacturing employees (54 per cent), while New South Wales and South Australia each accounted for a further 13 per cent (figure 4.2). Most of the reduction in automotive manufacturing employment since 2006 has occurred in Victoria and South Australia, partly reflecting the closure of Mitsubishi in Adelaide and downsizing at facilities in Melbourne, Geelong, and Adelaide by Ford, Holden and

Toyota (figure 4.2 does not reflect changes in employment since 2011, such as the retrenchment of 350 employees at Toyota’s Altona Plant in 2012).

Figure 4.2 Employment in automotive manufacturing, by state and territory

2006 and 2011^a



^a Employment figures for ANZSIC06 Group 231 (Motor vehicle and motor vehicle part manufacturing). This includes business units mainly engaged in motor vehicle manufacturing (class 2311), in motor vehicle body and trailer manufacturing (class 2312), in automotive electrical component manufacturing (class 2313), and in other motor vehicle parts manufacturing (class 2319).

Source: Productivity Commission estimates using ABS (*TableBuilder Pro*, 2011, Cat. no. 2073.0), ABS (*TableBuilder*, 2006, Cat. no. 2065.0).

In 2011, around half of all automotive manufacturing employees in Australia lived in one of ten regions³ in Melbourne and Adelaide (table 4.4). This reflects these regions’ close proximity to Ford, Holden and Toyota manufacturing plants and/or automotive component manufacturers. Melbourne South East, for example, contains a large number of automotive component manufacturing establishments (Victorian Government, sub. 70) as well as IVECO Truck’s manufacturing facilities.

Outside of Melbourne and Adelaide, the regions with the highest number of automotive manufacturing employees in 2011 were Geelong and Ballarat in Victoria. As noted above, Ford’s engine plant is in Geelong. The Australian Industry Group recently suggested that Ford and Holden’s decisions to cease manufacturing in Australia would have a limited effect on Ballarat:

³ ‘Regions’ refers to ABS Level 4 Statistical Areas (SA4) and ‘sub-regions’ refers to ABS Level 3 Statistical Areas (SA3).

Most [component manufacturers] have said [Holden's exit] won't have a huge effect on them because it is not their main customer ... Most of the component manufacturers who supplied to Ford are not here any more. (Kay Macaulay, Australian Industry Group regional manager, quoted in Dixon (2013))

In 2011, automotive manufacturing employees accounted for less than 2 per cent of employed residents in each region of Australia (with the highest concentrations of automotive manufacturing employees in four regions: Adelaide North; Melbourne West; Melbourne South East; and Melbourne North West). At the sub-regional level, there were several examples where automotive manufacturing employees accounted for more than 2 per cent of employed residents. Playford in Adelaide North stands out, as 3.4 per cent of employed residents were engaged in automotive manufacturing in 2011 (table 4.4, figure 4.3, figure 4.4).

Given that regions in Adelaide (Adelaide North) and Melbourne (Melbourne West; Melbourne South East; and Melbourne North West), and the region of Geelong, have the highest concentrations of automotive employees, and will be particularly affected by the Ford and Holden closures, they are most likely to experience significant adjustment pressures. Adjustment pressures would be exacerbated in some of these regions if Toyota does not proceed with plans to manufacture the next generation Camry model in Australia, particularly in Melbourne (Toyota's vehicle assembly and engine manufacturing operations are at Altona in Melbourne's west).

The Commission will undertake regional economic modelling for the final report to better understand the potential scale of these adjustment pressures on regions, and therefore the pressures facing those made redundant in those regions.⁴

⁴ Regional modelling results will be based on Statistical Divisions under the Australian Standard Geographical Classification, rather than Statistical Areas as referred in this chapter (ABS 2011a). Statistical divisions generally cover a broader geographic area than ABS Level 4 Statistical Areas. For example, there is one statistical division for each of metropolitan Melbourne and Adelaide.

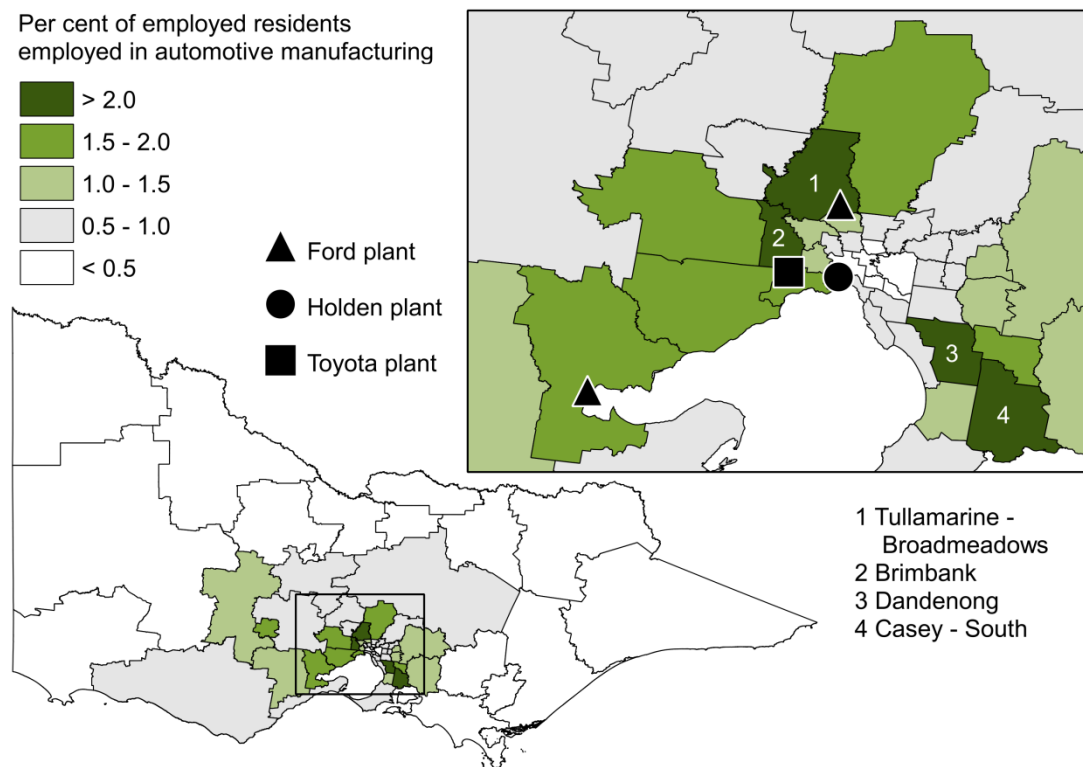
Table 4.4 Automotive manufacturing employment, selected regions, 2011
Based on usual place of residence^a

<i>Regions and sub-regions</i>	<i>Number of residents employed in automotive manufacturing</i>	<i>Share of Australian automotive manufacturing employment (%)</i>	<i>Share of employed residents that are employed in automotive manufacturing (%)</i>
Adelaide			
Adelaide - North	3 408	7.0	1.9
Playford	1 043	2.1	3.4
Salisbury	1 284	2.6	2.3
Gawler - Two Wells	301	0.6	2.0
Adelaide - South	1 564	3.2	1.0
Onkaparinga	1 036	2.1	1.4
Selected regions (Adel) total	4 968	10.1	
Melbourne			
Melbourne - South East	5 329	10.9	1.8
Dandenong	1 638	3.3	2.3
Casey - South	1 392	2.8	2.3
Casey - North	1 067	2.2	1.8
Cardinia	516	1.1	1.4
Melbourne - West	5 114	10.4	1.8
Brimbank	1 769	3.6	2.4
Wyndham	1 390	2.8	1.8
Melton - Bacchus Marsh	930	1.9	1.6
Hobsons Bay	585	1.2	1.6
Maribynong	440	0.9	1.3
Melbourne - Outer East	2 702	5.5	1.1
Yarra Ranges	887	1.8	1.2
Melbourne - North East	2 527	5.2	1.2
Whittlesea - Wallan	1 483	3.0	1.9
Melbourne - North West	2 209	4.5	1.6
Tullamarine - Broadmeadows	1 302	2.7	2.5
Melbourne - Inner	1 372	2.8	0.5
Melbourne - Inner South	1 258	2.6	0.7
Mornington Peninsula	1 176	2.4	0.9
Frankston	831	1.7	1.4
Selected regions (Melb) total	21 689	44.3	
Geelong			
Geelong (region)	1 694	3.5	1.5
Geelong (sub-region)	1 355	2.8	1.7
Barwon - West	119	0.2	1.5
Ballarat			
Ballarat (region)	964	2.0	1.5
Ballarat (sub-region)	748	1.5	1.7

^a The twelve selected regions (SA4 census areas) had the highest number of residents employed in automotive manufacturing in Australia in 2011. The twenty selected sub-regions (SA3 census areas) had the highest share of employed residents employed in automotive manufacturing in Australia in 2011.

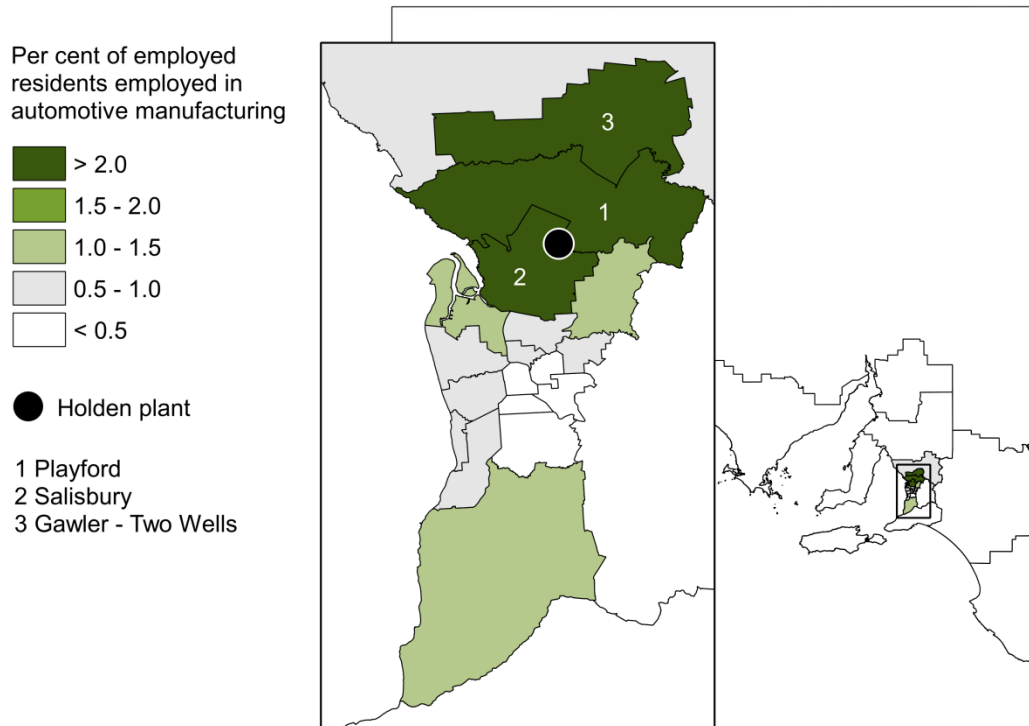
Source: Productivity Commission estimates using ABS (*TableBuilder Pro*, 2011, Cat. no. 2073.0).

Figure 4.3 Sub-regional concentration of automotive manufacturing employees, Melbourne and Geelong



Source: Productivity Commission estimates using ABS (*TableBuilder Pro*, 2011, Cat. no. 2073.0).

Figure 4.4 Sub-regional concentration of automotive manufacturing employees, Adelaide



Source: Productivity Commission estimates using ABS (*TableBuilder Pro*, 2011, Cat. no. 2073.0).

Relatively high unemployment and social disadvantage in some regions will likely exacerbate adjustment costs

Some participants noted that high unemployment and social disadvantage in some regions (and some sub-regions in particular) will likely exacerbate adjustment costs. The Government of South Australia (sub 68, pp. 5–6) noted:

the regional impact of a closure of GM Holden’s Australian operations will be ... compounded by the high incidence of unemployment and socioeconomic disadvantage in Adelaide’s northern suburbs, particularly in the City of Playford.

The ABS produces a range of socio-economic indexes — one of the more commonly used is the Index of Relative Socio-economic Disadvantage (IRSD) (Byron 2010). The IRSD ranks areas according to their rate of relatively disadvantaged people.⁵ For example, if a sub-region is in the 16th IRSD percentile,

⁵ The IRSD is made up of a number of variables with different weightings. Heavily weighted variables include: the proportion of people with stated annual household equivalised income between \$1 and \$20 799; the proportion of families with children under 15 years of age who

15 per cent of sub-regions in Australia have a higher proportion of relatively disadvantaged people. Thus, a low percentile indicates a relatively high level of disadvantage.

ABS data indicate that rates of unemployment and social disadvantage (based on the IRSD) vary across regions and sub-regions.⁶ Sub-regions with already relatively high levels of unemployment and social disadvantage include Playford in northern Adelaide and Dandenong in south eastern Melbourne (table 4.5).

In 2011, manufacturing jobs accounted for nearly 21 per cent of all jobs in Playford compared to around 11 per cent of all jobs in Greater Adelaide as a whole (Government of South Australia, sub. 68). Entrenched unemployment is also relatively high in the area, with almost 6 per cent of Playford's residents in 2009 having been on an unemployment benefit for more than 180 days, compared to 3 per cent in Greater Adelaide (Government of South Australia, sub. 68).

live with jobless parents; the proportion of occupied private dwellings with no internet connection; the proportion of employed people classified as 'labourers'; and the proportion of people aged 15 years and over whose highest level of education is year 11 or lower (ABS 2011b).

⁶ Up to date unemployment rates are not available for the regions and sub-regions in table 4.4. Given this, we have examined recent unemployment rates for the Labour Force regions and Local Government Areas that most closely align to the relevant regions and sub-regions.

Table 4.5 Unemployment rate and Index of Relative Socio-economic Disadvantage (IRSD)

Based on usual place of residence

<i>Labour Force regions and Local Government Areas^a</i>	<i>Unemployment rate (%), 2013^b</i>	<i>IRSD percentile, 2011^c</i>
Adelaide		
Northern Adelaide	8.4	
Playford	15.5	9
Salisbury	8.9	23
Gawler	6.6	43
Southern Adelaide	5.1	
Onkaparinga	5.9	64
Melbourne		
South Eastern Melbourne	6.8	
Greater Dandenong	9.4	11
Casey	5.9	72
Cardinia	5.9	81
Outer Western Melbourne	7.1	
Brimbank	8.8	18
Wyndham	8.7	75
Melton	9.0	70
Hobsons Bay	5.1	70
Maribyrnong	7.6	48
Outer Eastern Melbourne	4.6	
Yarra Ranges	4.2	85
North Eastern Melbourne	5.6	
Whittlesea	7.8	60
North Western Melbourne	7.0	
Hume	8.0	34
Inner Melbourne	5.5	
Southern Melbourne	5.4	
Mornington Peninsula	6.1	
Frankston	7.0	67
Geelong		
Barwon - Western District	5.7	
Greater Geelong	6.6	63
Golden Plains	4.4	83
Ballarat		
Central Highlands - Wimmera	5.0	
Ballarat	6.4	53

^a Up to date unemployment rates are not available for the regions and sub-regions in table 4.4. The selected Labour Force regions and Local Government Areas are those which most closely align to the regions and sub-regions in table 4.4. ^b Reported unemployment rates for Labour Force regions are a 12 month average of monthly unemployment rates to November 2013. Unemployment rates for Local Government Areas are as at September 2013. ^c The ABS does not publish IRSD percentiles for Labour Force regions.

Sources: Productivity Commission estimates using ABS (Labour Force, Australia, Detailed, Quarterly, November 2013, Cat. no. 6291.0.55.003); Productivity Commission estimates using Department of Employment (Small Area Labour Markets, Australia, September quarter 2013); ABS (Census of Population and Housing: Socio-economic Indexes for Areas (SEIFA), Australia, 2011, Cat. no. 2033.0.55.001).

Low skill levels may be an impediment to re-employment for some displaced automotive employees

Studies suggest that people from lower-skilled occupations, with limited qualifications, and/or with poor English skills, are likely to face greater difficulties in finding re-employment (Murtough and Waite 2000; OECD 2013). With respect to former Mitsubishi employees, for example, Beer (2008) notes that displaced employees with fewer formal qualifications were particularly likely to report difficulties in finding work and poorer working conditions once they found work.

In the automotive manufacturing industry in 2011:

- 34 per cent of employees were employed in lower skilled occupations (such as labourers and machinery operators), which was similar to manufacturing overall, but around double the average for all industries (16 per cent) (table 4.6)
- 15 per cent of employees had a bachelor degree or higher, compared to 14 per cent for all manufacturing and 26 per cent for all industries (table 4.7)
- 3.7 per cent of employees reported poor English skills, which was a little higher than the average for the manufacturing sector (3.4 per cent) but almost three times the level for all industries (1.3 per cent). Automotive manufacturing employees in Victoria reported higher rates of poor English (5.1 per cent) than those in South Australia (2.1 per cent) (table 4.8).

There was a decrease in the proportion of the automotive manufacturing workforce from lower-skilled occupations and with limited qualifications from 2006 to 2011, mirroring a broader trend in the manufacturing sector as a whole.

Table 4.6 Occupations by selected industries, 2006 and 2011

Percentage of workforce

	<i>Automotive manufacturing</i>		<i>Manufacturing sector</i>		<i>All industries</i>	
	2006	2011	2006	2011	2006	2011
Managers and professionals	21	23	21	23	33	34
Technicians and tradespersons	28	30	26	26	14	14
Clerical, administrative and sales employees	10	11	15	16	25	24
Machinery operators and drivers	15	13	15	15	7	7
Labourers	24	21	20	18	10	9
Other	2	2	2	3	11	12

Sources: Productivity Commission estimates using ABS (*TableBuilder Pro*, 2011, Cat. no. 2073.0), ABS (*TableBuilder*, 2006, Cat. no. 2065.0).

Table 4.7 Educational attainment of employed persons, selected industries, 2006 and 2011

Percentage of workforce

	<i>Automotive manufacturing</i>		<i>Manufacturing sector</i>		<i>All industries</i>	
	<i>2006</i>	<i>2011</i>	<i>2006</i>	<i>2011</i>	<i>2006</i>	<i>2011</i>
Bachelor degree or higher	13	15	11	14	22	26
Diploma/certificate	37	40	36	39	31	33
Year 12	17	17	18	18	19	18
Year 11 or below	27	26	33	28	27	22
Not stated	5	2	2	2	2	1

Sources: Productivity Commission estimates using ABS (*TableBuilder Pro*, 2011, Cat. no. 2073.0), ABS (*TableBuilder*, 2006, Cat. no. 2065.0).

Table 4.8 Employed persons with 'poor English'^a, 2006 and 2011

Percentage of workforce

	<i>Automotive manufacturing</i>		<i>Manufacturing sector</i>		<i>All industries</i>	
	<i>2006</i>	<i>2011</i>	<i>2006</i>	<i>2011</i>	<i>2006</i>	<i>2011</i>
Victoria	5.3	5.1	3.9	4.1	1.4	1.5
South Australia	1.4	2.1	1.5	2.1	0.7	0.9
Australia	3.7	3.7	3.0	3.4	1.2	1.3

^a A person with 'poor English' is defined as someone who reports speaking a language other than English at home, and reports that they speak English 'not well' or 'not at all'.

Sources: Productivity Commission estimates using ABS (*TableBuilder Pro*, 2011, Cat. no. 2073.0); Productivity Commission estimates using ABS (*TableBuilder*, 2006, Cat. no. 2065.0).

Age-related adjustment issues may also affect some employees

Studies suggest that older people who have been retrenched are less likely to find re-employment (Borland and Johnston 2010; Carroll 2006; Murtough and Waite 2000). This might reflect a range of supply and demand factors including the reduced likelihood that people will move to find re-employment as they get older (PC 2013c) and the preference of employers to train younger employees who are likely to remain in the job longer (PC 2005). Analysis of former Ansett employees, for example, found that age was a strong predictor of the likelihood of relocation, with employees over 45 years of age less likely to relocate (Weller 2009).

The age profile of the automotive manufacturing workforce has changed over time, with the proportion of people aged 45 or over increasing between 2006 and 2011. Nonetheless, in 2011, its age profile was broadly similar to that of manufacturing and all other industries, with about 40 per cent of people employed in the automotive manufacturing industry aged 45 or over (table 4.9).

Table 4.9 Age profile of employed persons, by industry classification
Percentage of workforce

	<i>Employment distribution by age</i>									
	2006					2011				
	< 25	25-34	35-44	45-54	55+	< 25	25-34	35-44	45-54	55+
Automotive manufacturing	11	25	28	23	13	10	22	28	25	15
Total manufacturing	13	22	27	24	15	12	20	25	25	17
All industries	17	21	24	23	15	15	22	23	22	18

Sources: Productivity Commission estimates using ABS (*TableBuilder Pro*, 2011, Cat. no. 2073.0), ABS (*TableBuilder*, 2006, Cat. no. 2065.0).

Redundancy payments

Redundancy payments are another consideration in assessing the potential effects of retrenchment on automotive manufacturing employees. For example, redundancy payments help to ameliorate immediate financial pressures on displaced employees arising from unemployment. Some displaced employees, such as those who have worked for motor vehicle producers for a long period of time, are likely to receive large payments relative to the payments that will be received by employees who are reliant on the redundancy provisions in the relevant award, including employees of some component suppliers. The magnitude of redundancy payments and their timing can influence the behaviour of some employees in terms of their search for other jobs.

Ford has indicated that they are in the process of negotiating a ‘Social Plan’ agreement with employee representatives, which is intended to define key exit arrangements such as early release, redeployment opportunities, redundancy payments and retraining. The Commission understands that Ford and its workforce have yet to reach agreement on the details of the plan.

DRAFT FINDING 4.1

Adjustment pressures in the automotive manufacturing industry, including plant closures announced by Ford and Holden, will result in concentrated reductions in industry employment in specific regions in and around Melbourne and Adelaide. Relatively high rates of unemployment and social disadvantage in some regions, such as in northern Adelaide and in Melbourne’s south east, will likely exacerbate adjustment costs.

The individual characteristics of displaced employees will affect adjustment costs. Low skill levels may be an impediment to re-employment for some displaced automotive manufacturing employees and older people who have been retrenched are less likely to find re-employment.

As noted in chapter 5, the Commission is seeking further information on specific characteristics and needs of some groups of automotive manufacturing employees that might warrant particular consideration if generally available measures appear to be insufficient. In particular, it seeks information on whether there are different circumstances facing employees from the extensive and varied component manufacturing sector as compared to Ford and Holden employees.

5 Adjustment assistance for employees and regions

Key points

- Generally available welfare, training and employment services have distinct advantages in dealing with adjustment pressures.
- However, generally available measures are not designed to handle all contingencies. In some cases, there is a role for additional measures to promote equitable outcomes and improve the efficiency of the adjustment process.
- Where governments determine that there is an in-principle case for providing special adjustment assistance, on efficiency or equity grounds, it needs to be demonstrated that such assistance would be cost-effective.
- Past special adjustment packages, including regional adjustment funds, have had limited success. For example:
 - Regional adjustment funds do not appear to have resulted in the targeted regions performing any better than other regions that lost a major employer but did not receive government assistance.
- There is limited public information on the effectiveness of labour adjustment programs for displaced automotive manufacturing employees. The public information that does exist (particularly information on programs for displaced Mitsubishi employees) suggests that specially targeted programs have had some, but limited, success in assisting displaced automotive manufacturing employees to find future employment.
- Infrastructure investments may, in some cases, assist in overcoming bottlenecks to greater economic activity in regions affected by structural adjustment. The key issue is whether a proposed project provides net benefits to the community as a whole (rather than to a specific region), and given limited resources, whether it generates the largest net benefits from the available options (regardless of the project's location).
- The Commission is seeking input from participants on the extent to which generally available measures are likely to adequately address equity and efficiency concerns related to structural adjustment in the automotive manufacturing industry, and whether there are models of facilitating structural adjustment more cost-effectively.
 - In particular, the Commission is seeking input on whether the circumstances facing employees in the extensive and varied component manufacturing sector are different to those facing Ford and Holden employees.

5.1 The role of generally available safety net measures

Governments provide a range of generally available safety net measures to help people manage adverse circumstances, including:

- Welfare assistance, such as social security payments and tax concessions for people with low or no income. For example, someone who has lost their job may be entitled to income support, such as the Newstart allowance, or financial support to lower their living costs, such as rent assistance.
- Employment, training and counselling services. If a person is retrenched and is seeking re-employment, for example, they will generally have access to employment services provided through Job Services Australia (Department of Human Services 2013).

Generally available measures have distinct advantages in dealing with adjustment pressures relative to ad hoc or special adjustment assistance. For example, they:

- treat individuals in similar circumstances equally
- target assistance to those in genuine need whatever the cause
- address the net effects of the various factors influencing the financial circumstances of individuals and families
- support individuals and families rather than a particular industry or activity
- minimise the design, administration and monitoring costs of assistance provision (PC 2001, 2012b).

Generally available measures recognise that there are hundreds of thousands of involuntary job losses every year and that it would not be feasible, equitable or cost-effective to have a multitude of special arrangements when structural adjustment and labour market changes are so frequent and widespread.

In the year ending February 2013, around 355 000 people were involuntarily retrenched across Australia. Of these, 80 000 employees had been with their employer for at least 5 years (ABS 2013b). As noted in chapter 4, the Ford and Holden closures will directly displace about 2500 employees in Victoria and 1600 employees in South Australia. A number of retrenchments will occur in the component manufacturing sector and automotive services sector.

In some cases the line between special assistance and generally available measures can become blurred. For example, where the closure of a manufacturing plant and related businesses results in large-scale retrenchments in a particular region, generally available welfare, employment and training services need to be adequately resourced to meet increased demand. This might involve temporarily increasing

resources available to deliver these services in certain regions. Similarly, service providers will often tailor generally available measures to the needs of people in the area.

In addition to generally available safety net measures, broader economic policy settings have an important role in increasing the resilience of regions to structural change. For example, the Commission is conducting an inquiry into subsidies for Tasmanian shipping and freight. The Commission's draft report found that:

... approaches that are designed to make the region concerned more attractive to business generally — such as improving selected infrastructure, upgrading labour force skills, removing inefficient taxes and improving administrative efficiency — are preferable to sponsoring selected firms or encouraging businesses to locate (or remain) there through subsidies. (PC 2014)

DRAFT FINDING 5.1

Generally available measures have some distinct advantages in dealing with adjustment pressures, relative to ad hoc or special adjustment assistance. These measures:

- *treat individuals in similar circumstances equally*
- *target assistance to those in genuine need whatever the cause*
- *address the net effects of the various factors influencing the financial circumstances of individuals and families*
- *support individuals and families rather than a particular industry or activity*
- *minimise the design, administration and monitoring costs of assistance provision.*

DRAFT PROPOSAL 5.1

Governments should ensure that generally available welfare, training and employment services are adequately resourced to deal with the effects of structural adjustment in the automotive manufacturing industry.

5.2 Rationales for special adjustment assistance

Adjustment pressures can arise from a number of sources, of greater or lesser significance at different points in time, including:

- changes in underlying market and competitive forces faced by businesses and their employees — for example, changing consumer demands, international competitive pressures, and technological innovations

-
- population growth or decline, or changes in its composition — arising from, for example, changes in the level or composition of a region’s economic activity
 - changes to economic, social or environmental policy — such as those caused in recent decades by tariff reductions
 - changes in the natural environment — such as the consequences of prolonged drought.

As discussed in the preliminary findings report, changes in market conditions in Australia and globally have been a key source of recent structural change in the automotive manufacturing industry (PC 2013a).

Generally available measures will usually be appropriate for assisting the adjustment process and moderating adverse distributional effects from structural change (PC 2001). However, these measures are not designed to handle all contingencies. In some cases, there is a role for additional measures to promote equitable outcomes and improve the efficiency of the adjustment process.

Rationale for special adjustment assistance on efficiency grounds

From an efficiency perspective, the main rationale for special adjustment assistance is to address sources of market failure (chapter 2) which inhibit the adjustment process and increase transitional adjustment costs for the broader economy. Where special adjustment assistance can reduce adjustment costs attributable to market failures (that cannot be addressed through changes to the generally available measures), such as imperfect information on alternative employment opportunities, there is an in-principle case to intervene. Similarly, where existing broader government policies — such as housing policies and occupational licensing measures — seem likely to impede the adjustment process, and constrain labour mobility in particular, there is a case for examining the possibility of modifying the relevant policy to remove or lessen the impediment (see chapter 2).

Rationale for special adjustment assistance based on equity and fairness grounds

Structural adjustment can have adverse distributional effects on people employed in particular industries and/or living in particular regions, which may in turn raise equity concerns. As noted in chapter 4, for example, some participants suggested that high unemployment and social disadvantage in some sub-regions (such as Playford) will likely exacerbate adjustment costs. Similarly, some displaced automotive manufacturing employees may face greater difficulties finding

employment due to limited skills, lower educational attainment, lower English proficiency, or older age.

The Commission has previously argued that the case for special adjustment assistance on equity grounds is likely to be strongest where a government proposed a policy change, and that change:

- imposes a clear and sizeable burden on a specific group in the community (particularly if the affected group is already relatively disadvantaged)
- delivers benefits mainly to relatively advantaged groups in the community, at a cost to others, and/or
- involves a largely unanticipated and material change to a well-defined and defensible property right (PC 2001, p. XIX).¹

Underlying such arguments is the proposition that governments should be accountable for significant adverse distributional impacts arising from deliberate, clear and transparent policy decisions.

The case for providing special adjustment assistance in response to changes in market conditions is more contentious. For example, firms in all industries and individuals win or lose from market-based changes every day, and this is usually considered part of the normal operation of markets.

The Government of South Australia observed that ‘while it is often argued that there is a stronger rationale for additional assistance where the adjustment pressure is a result of policy change, the case is not clear cut’ (Government of South Australia, sub. 68, p. 50). The Government of South Australia further noted that drawing a distinction between market-based changes and those resulting from government policy raises a number of equity issues:

‘Many kinds of phenomena produce losses. These include natural disasters, as well as wars, the discovery or exhaustion of natural resources, technological discoveries and changes in preference sets – and changes in public policy. On grounds of equity, it does not seem warranted to select isolated public policy changes from this set as a trigger for making transfer payments.’ (Rottenberg 1986, cited in Government of South Australia, sub. 68, p. 50)

Although the Government of South Australia was arguing against relying on a change of public policy as being a sufficient trigger for providing additional

¹ The Commission’s study on structural adjustment (PC 2001) examined the case for special adjustment assistance in response to policy-induced structural change and market-related structural change. It did not cover the case for assistance in response to other sources of adjustment, such as natural disasters.

assistance, its argument applies equally to whether there is any equity in drawing a distinction between the hundreds of thousands who are retrenched annually across the economy and those who are retrenched from particular industries. As noted in its submission, ‘the existence or intensity of suffering is independent of the cause’ (sub. 68, p. 50).

Other matters when considering special adjustment assistance

Where governments determine that there is an in-principle case for special adjustment assistance, on efficiency or equity grounds, it is necessary to demonstrate that such assistance would yield a better overall outcome than relying on generally available measures. In particular, it is necessary to show that the proposed measure would target the problem effectively (that is, it provides assistance to those who are adversely affected) and would be cost-effective (taking into account additional financing costs, administrative costs, behavioural costs, and interactions with other programs/policies).

The following sections examine current and proposed special assistance packages and evidence on their effectiveness in achieving equity objectives and/or overcoming market-based impediments to adjustment.

DRAFT FINDING 5.2

Where governments determine that there is an in-principle case for providing adjustment assistance beyond that generally available, on efficiency or equity grounds, it needs to be demonstrated that such assistance would be cost-effective.

5.3 Current and proposed special assistance packages for automotive manufacturing employees

Governments have provided, and continue to provide, special adjustment assistance programs for employees and regions affected by retrenchments in a wide range of industries, including the automotive manufacturing industry. Special adjustment assistance programs for the automotive manufacturing industry include the Australian Government’s Automotive Industry Structural Adjustment Program (AISAP) and assistance provided by the Australian and Victorian governments in response to Ford’s announcement that it will cease manufacturing in Australia in 2016 (table 5.1). The Australian, Victorian and South Australian Governments have foreshadowed a structural adjustment package in response to Holden’s announcement that it will cease manufacturing in Australia by the end of 2017.

Table 5.1 Current labour and regional adjustment programs for the automotive manufacturing industry in Australia

<i>Program</i>	<i>Description</i>	<i>Duration</i>	<i>Total funding</i>	<i>Funding source</i>
Automotive Industry Structural Adjustment Program	Provides intensive employment services to employees made redundant from eligible manufacturing firms in the automotive industry	2008-09 to 2016-17	\$51.9m ^a	<ul style="list-style-type: none"> • Australian Government
Assistance for Ford employees	Funding is mostly for career advice and training to supplement employment support services	na	\$15.1m ^b	<ul style="list-style-type: none"> • Australian Government
Geelong Region Innovation and Investment Fund	Support investment by businesses leading directly to new jobs in the Geelong region	2013-14 to 2015-16	\$24.5m ^c	<ul style="list-style-type: none"> • Australian Government • Victorian Government • Ford
Melbourne's North Region Innovation and Investment Fund	Support investment by businesses leading directly to new jobs in Melbourne's north	2013-14 to 2015-16	\$24.5m ^c	<ul style="list-style-type: none"> • Australian Government • Victorian Government • Ford

^a Relates to the labour market adjustment support element of the Automotive Industry Structural Adjustment Program. The Automotive Industry Structural Adjustment Program included another element to help firms with legal, relocation and other merger costs, which commenced in January 2009 and is now closed. ^b Comprises funding for: Auto Skills Australia to provide career advice and training to supplement employment support services (\$10 million); designation of Geelong as one of 21 priority employment areas and the appointment of a local employment coordinator (\$0.74 million); a regional industry coordinator to support employees from downstream businesses and to work with industry and employee organisations (\$3.3 million); Federation of Automotive Parts Manufacturers to assist businesses (\$0.47m); and an Australian Jobs and Skills Expo and four Jobs Marts to be held in Geelong (\$0.6 million). ^c The Australian Government will contribute \$30 million; the Victorian Government \$9 million; and Ford Australia \$10 million.

Sources: AusIndustry (2013a); Carr (2013); DoE (2013); DoI (2013a); Shorten (2013).

Automotive Industry Structural Adjustment Program

The AISAP provides intensive employment services to employees made redundant from eligible manufacturing firms in the automotive manufacturing industry (employees made redundant would not normally be entitled to this type of employment service due to income support waiting periods and their recent work experience). Intensive employment services are provided through Jobs Services Australia, and include job search and career advice, a comprehensive skills assessment, and skills development and training relevant to the needs of the local labour market. Job seekers also receive additional assistance such as employment subsidies, equipment and training through the Employment Pathway Fund (DoE 2013). The AISAP is administered by the Commonwealth Department of

Employment and is scheduled to run from 2008 to 2017 (\$18.7 million of funding has been allocated for the financial years 2012-13 to 2016-17) (DIICSRTE 2013).

Assistance in response to Ford's announced departure

The Australian and Victorian governments established the Melbourne's North Region Innovation and Investment Fund (MNRIIF) and the Geelong Region Innovation and Investment Fund (GRIIF) in July 2013 in response to the announcement by Ford that it plans to cease automotive manufacturing in Australia. The MNRIIF and GRIIF will each provide \$24.5 million in grants to businesses for projects in Melbourne's northern suburbs and the Geelong region. AusIndustry and the Victorian Department of State Development, Business and Innovation will allocate grants to projects that 'generate sustainable jobs' in the affected regions. Businesses will be required to match grant funding one-to-one (AusIndustry 2013a). The Australian Government also committed \$15.1 million to assist displaced Ford employees (in addition to the support already available under the AISAP) (Shorten 2013).

Assistance in response to Holden's announced departure

Following Holden's announcement that it that will cease automotive manufacturing in Australia by 2017, the Australian, Victorian and South Australian governments indicated that they intend to put in place 'a comprehensive structural adjustment and co-investment package to support affected auto industry employees, their families, businesses and regions' (COAG 2013).

There is currently limited public information about the package and uncertainty remains over the final design and level of the assistance. The Australian Government has indicated it plans to establish a \$100 million 'growth fund' to support initiatives in regions facing pressure in their manufacturing sectors, with funding expected from the Commonwealth (\$60 million), Victorian (\$12 million) and South Australian (\$8 million) governments and Holden (\$20 million) (Abbott and Macfarlane 2013). However, the response of state governments to the Australian Government announcement has been mixed (Naphthine 2013) (Weatherill 2013b) and the South Australian Government recently announced a \$393 million 'Jobs Plan', to which it committed \$60 million and sought \$330 million from the Australian Government (Weatherill 2014) (box 5.1).

Box 5.1 **South Australian Government ‘Jobs Plan’**

The recently announced South Australia Government ‘Jobs Plan’ contains a range of measures designed to assist workers, their families, businesses and regions affected by Holden’s announced closure. The measures include:

- support and retraining for displaced workers
- funding for infrastructure projects and businesses in affected regions
- funding to encourage the diversification of automotive supply businesses
- a range of programs to encourage the development of ‘advanced manufacturing’ industries, through support for business precincts and collaboration
- funding to businesses within certain industries (including defence, resources and energy, premium food and wine, health and biomedical, education and business services, tourism, and creative industries)
- working with the Australian Government to bring forward a number of infrastructure projects.

Many of the proposed programs require a contribution from the Australian Government.

Source: Government of South Australia (2014).

The Australian Government announced a ‘wide-ranging industry initiative comprising targeted support for regions impacted; reviews of the South Australian and Victorian economies; and development of a National Industry Investment and Competitiveness Agenda which will focus on our strengths, create jobs and exploit our competitive advantages’ (Abbott and Macfarlane 2013). It noted the reviews of the South Australian and Victorian economies would look at ways to boost the competitiveness of each state’s economy by:

- encouraging investment and innovation in high growth sectors in the affected regions
- further investing in infrastructure to boost productive capacity
- where appropriate and cost effective, relocating Commonwealth public service functions to the affected regions
- considering the most pressing concerns of the shipbuilding industry
- supporting the diversification of automotive supply chain companies
- supporting the training and redeployment of employees displaced by closures.

The reviews of the South Australian and Victorian economies will inform the design of the growth fund.

In addition, the South Australia Government has appointed former Federal Government Minister Greg Combet to the role of Automotive Transformation

Coordinator. Premier Jay Weatherill has indicated Mr Combet would initially be supported by the South Australian Advanced Manufacturing Taskforce and be responsible for coordinating assistance provided to automotive industry workers and automotive suppliers (Weatherill 2013a).

5.4 Can special adjustment packages cost-effectively facilitate adjustment?

There is a range of possible options that could form part of a new or enhanced structural adjustment assistance package for the automotive manufacturing industry. Current and previous special adjustment packages for the automotive manufacturing industry have typically included two types of programs:

- regional adjustment funds (sometimes referred to as industry and innovation funds), which subsidise businesses to undertake projects that generate jobs in regions affected by large-scale retrenchments
- labour adjustment programs, which provide retrenched employees in the industry with access to additional assistance beyond what retrenched employees would normally receive (such as intensive employment services).

As discussed above, governments are canvassing additional options for creating jobs in areas affected by retrenchment by Ford and Holden and by a number of component manufacturers and related businesses. These include funding large-scale infrastructure projects, promoting innovation and investment in selected sectors (such as defence manufacturing and the shipbuilding industry) and relocating public service functions.

As the Australian and State Governments are yet to finalise their proposed adjustment packages, the Commission has considered evidence on the effectiveness of possible measures, to help guide the development of the programs.

Regional adjustment funds

Previous regional adjustment funds

Since 2004, there have been five regional adjustment funds targeting regions affected by retrenchments in the automotive manufacturing industry. In addition to the two regional adjustment funds relating to Ford's announcement that it will cease manufacturing in Australia (MNRIIF and GRIIF), these regional adjustment funds include (table 5.2):

- the Structural Adjustment Fund for South Australia, which was in response to the closure of Mitsubishi's Lonsdale site in southern Adelaide in 2004
- the South Australian Innovation and Investment Fund, which was in response to the closure of Mitsubishi's site at Tonsley Park in northern Adelaide in 2008
- the Geelong Investment and Innovation Fund, which was in response to Ford's announcement that it would close its Geelong engine assembly plant in 2007 (The Geelong Investment and Innovation Fund continued despite Ford later announcing it would continue to operate the plant) (PC 2012b).

Table 5.2 Previous regional adjustment funds related to closures and downsizing in the automotive manufacturing industry

<i>Fund</i>	<i>Period</i>	<i>Announced fund size</i>	<i>Value of grants made</i>	<i>Anticipated full time equivalent jobs created</i>
		\$m (nominal)	\$m (nominal)	no.
Structural Adjustment Fund For South Australia	2004-05 to 2008-09	45 (\$40m Commonwealth, \$5m South Australia)	37.1	1 198
South Australia Innovation and Investment Fund	2008-09 to 2011-12	30 (\$25m Commonwealth, \$5m South Australia)	24.0	895
Geelong Investment and Innovation Fund	2008-09 to 2010-11	24 (\$15m Commonwealth, \$6m Victoria, \$3m Ford)	18.8	1 120

Sources: AusIndustry (2012a, 2012b, 2012c, 2012d, 2012e, 2012f); Beer (2006); PC (2012b).

Regional adjustment funds have typically been administered as competitively funded grants of up to 50 per cent of the capital costs of each job creation project. The evaluation criteria for these grants have included the number of jobs created and the level of economic benefit, such as contributions to diversification of the regional economy or the introduction of innovations or technology. Between 2004 and 2013, \$148 million was announced for regional adjustment funds in South Australia and Victoria in response to announced automotive manufacturing industry redundancies.

Effectiveness of regional adjustment funds

Several studies have questioned the effectiveness of regional adjustment funds in generating new employment. For example, Daley and Lancy (2011) examined a selection of regional adjustment funds that were introduced in Australia between 2004 and 2010, including the three funds relating to closures in the automotive manufacturing industry (table 5.2). They concluded that these regional adjustment

funds did not appear to have significantly affected overall long-term employment trends in the relevant regions, and did not result in the regions performing any better than other regions that lost a major employer but did not receive any government assistance.

More recently, it has been reported that the \$30 million Illawarra Region Innovation and Investment Fund — that was set up in late 2011 following large-scale redundancies at BlueScope Steel’s Port Kembla works — will not create as many jobs as initially expected. The government initially estimated that the fund would generate 888 full time positions by mid-2014 (to replace the 800 jobs that were lost at BlueScope). In May 2013, however, the New South Wales Industry Minister indicated that it would create 200 fewer full-time jobs than initially estimated (Atkin 2013).

Similarly, international evidence suggests that the effectiveness of regional adjustment funds in generating new employment has been limited. For example, Swedish firms that received regional investment grants did not generally hire more employees (Ankarhem et al. 2010). In Britain, the Regional Selective Assistance program, which provides grants to firms for investment in economically disadvantaged areas, led to an increase in employment in small firms but not in large firms. This may be due to ‘larger firms being more able to “game” the system and take the subsidy without changing their investment and employment levels’ (Criscuolo et al. 2012, p. 2).

A related concern about regional development policies, such as regional adjustment funds, is that they might fund activity that would have occurred anyway or crowd out or transfer activity from elsewhere. Daley, for example, argued that there is ‘no evidence that [regional development policies] have increased activity by more than they have reduced it elsewhere in Australia’ (Daley 2012, p. 11). Given the potential for regional development policies to simply redistribute economic activity across regions or businesses, Daley and Lancy suggested that they are ‘subsidies that can only be justified on equity or social grounds rather than because they are likely to drive long-term sustainable economic growth’ (2011, p. 7).

Design of regional adjustment funds

In some cases, poor design or targeting of regional adjustment funds can make them more costly and less effective than they otherwise would be. The Structural Adjustment Fund for South Australia, for example, included funding for projects outside the southern region of Adelaide where the Mitsubishi plant was located and beyond where many retrenched Mitsubishi employees lived. Beer (2008) argued

that this approach did not take into account the fact that the retrenched employees looked for work locally.

Ex post evaluation of regional adjustment funds

As previously noted by the Commission (PC 2012b, 2013c), analysing the effectiveness of regional adjustment funds is made more difficult by the absence of ex post evaluation. For example, the new Geelong Region Innovation and Investment Fund is very similar in its design to a previous program, the Geelong Investment and Innovation Fund, which operated in 2007-08 in response to a Ford restructure. It appears that no formal evaluation of the effectiveness and efficiency of this fund has been publicly released since it operated. Undertaking formal evaluations of regional adjustment funds and publishing the results is important for demonstrating that they deliver net benefits to the Australian community.

DRAFT FINDING 5.3

There is little evidence that regional adjustment funds have been cost-effective, from a whole-of-economy viewpoint, in addressing the effects of adjustment arising from employment reductions in the automotive manufacturing industry.

Labour adjustment programs for automotive manufacturing employees

Previous labour adjustment programs

Recently, employees displaced from the automotive manufacturing industry have been given immediate access to levels of intensive assistance that are otherwise reserved for the disadvantaged and long-term unemployed. This has typically included a mixture of job search assistance, training, relocation assistance, and wage subsidies. (The programs listed in table 5.3 generally included these elements.)

Table 5.3 Australian labour adjustment programs in the automotive manufacturing industry

<i>Program</i>	<i>Date</i>	<i>Closure/ downsize</i>	<i>Budget</i>
Passenger Motor Vehicle Labour Adjustment Package	1991-na	Passenger motor vehicle manufacturing	na
Mitsubishi Labour Adjustment Package ^a	2004-2010	Mitsubishi (Lonsdale and Tonsley Park)	\$10m (\$7.5m Commonwealth, \$2.5 SA Government)
Holden Labour Adjustment Package	2005-2009	Holden (north Adelaide)	\$10m (\$7.5m Commonwealth, \$2.5 SA Government)
Mitsubishi Labour Adjustment Package ^b	2008-2011	Mitsubishi (Tonsley Park)	\$10m (\$7.5m Commonwealth, \$2.5 SA Government)
Automotive Industry Structural Adjustment Program ^c	2008-09 to 2016-17	Passenger motor vehicle manufacturing	\$51.9m Commonwealth

^a Implemented with Structural Adjustment Fund for South Australia. ^b Implemented with South Australian Innovation and Investment Fund. ^c Relates to the labour market adjustment support element of the Automotive Industry Structural Adjustment Program. The Automotive Industry Structural Adjustment Program included another element to help firms with legal, relocation and other merger costs, which commenced in January 2009 and is now closed.

Sources: Beer and Evans (2010); Carr (2008); DEET (1995); DEWR (2006); HRSCWWRP (2006); Government of South Australia (2006); Department of Employment (pers. comm., 24 January 2014).

Effectiveness of labour adjustment programs

International literature provides mixed evidence on the effectiveness of labour market programs that have typically made up automotive labour adjustment packages. For example, international surveys on labour market programs have found job search assistance programs generally yield positive results and are usually cost effective compared to other labour market programs. Training programs are successful in some circumstances, particularly for the long-term unemployed, but less successful for employees that have been laid off en masse (Card, Kluve and Weber 2010; Dar and Tzannatos 1999). Wage subsidies are unlikely to have a positive impact as they often have high ‘deadweight costs’ (that is, they pay for outcomes that would have been achieved without the subsidy (Dar and Tzannatos 1999).² However, there is still very little knowledge on what makes an optimal labour market program (O’Neil and Neal 2008).

In some cases, labour adjustment programs can have impacts on other jobseekers through displacement effects. Displacement (sometimes referred to as ‘shuffling the

² In Australia, DEEWR (2012) found that more than three quarters of wage subsidy recipients it surveyed would have hired the same job seeker even if they had not received a wage subsidy.

queue’) occurs where jobseekers targeted by a particular program simply substitute for non-targeted jobseekers in filling existing vacancies (Boockmann et al. 2012; Crépon et al. 2013). Although displacement is difficult to measure where present these effects decrease the change in aggregate employment due to the program. Also, there can be distributional consequences from displacement, particularly where programs target one group of jobseekers over others with similar levels of labour market disadvantage (Brown and Köttl 2012).

Design of labour adjustment programs

In some cases, poor targeting of automotive industry related labour adjustment programs has decreased their effectiveness (Armstrong et al. 2008; Beer and Thomas 2007). For example, Armstrong et al. observed:

It would appear that the Job Network agencies did not have the resources to deal with skilled workers and that placing redundant Mitsubishi workers on an existing scheme designed to assist the long-term unemployed was an inappropriate response by government ... Given the skills shortage the state was facing, together with the considerable growth in mining and defence industries, it would have been more appropriate if [Labour Adjustment Package] funding had been redirected to further training or re-skilling opportunities for redundant workers. (2008, p. 348)

The authors contrast the Mitsubishi Labour Adjustment Package with, what the authors considered, the ‘more successful’ labour adjustment package for MG Rover in Birmingham (UK). The MG Rover package involved greater funding assistance and targeted support available for employees, and a greater emphasis on re-training needs, to assist adjustment. For good long-term employment outcomes, it is important that training is focused on the needs of industry and of employees (some former MG Rover employees reported having undertaken training that led to jobs that that they subsequently found they did not like or want to do (Bentley, Bailey and de Ruyter 2008)).

Ex post review of labour adjustment programs for automotive employees

While there have been studies examining labour market outcomes for displaced automotive employees following retrenchment (including the study of retrenched Mitsubishi employees), there is limited public information on the effectiveness the labour adjustment programs themselves. The information that is available often relates to the percentage of displaced employees participating in the program who had found re-employment. In 2006, for example, the Department of Employment and Workplace Relations noted that the Mitsubishi Labour Adjustment Program had achieved ‘good outcomes’ for displaced employees and that as of January that year,

74 per cent of employees who registered for Job Network assistance had been placed into work (DEWR 2006, p. 24). However, Armstrong et al. provide a different view on the program:

... Given that the majority of redundant Mitsubishi workers did not use a Job Network agency and that very few of the individuals who did use them actually managed to find employment through the Job Network agencies it is evident that the Labour Adjustment Package was not effective in assisting these displaced workers to regain employment. (2008, p. 348)

Assessments of automotive labour adjustment programs have been conducted in the absence of a control group, such that it is not possible to compare the employment outcomes of displaced employees with access to the programs relative to the outcomes of similar jobs seekers without access to the program. Consequently, it is difficult to establish whether these labour adjustment programs led to better employment outcomes for automotive manufacturing employees, relative to what would have occurred if they only had access to generally available measures.

As mentioned above with respect to regional adjustment funds, undertaking formal evaluations of labour adjustment programs and publishing the results is important for demonstrating that the programs deliver net benefits to the Australian community.

DRAFT FINDING 5.4

Available information suggests that targeted labour adjustment programs have had some, but limited, success in assisting displaced employees find future employment. Job search assistance and training appear to be among the more cost-effective options in many circumstances.

Given this, and that labour adjustment programs can have adverse consequences for jobseekers not targeted by the programs, the key issue is whether there is robust evidence that demonstrates that targeted labour adjustment programs would be an efficient and equitable response to the particular adjustment task facing employees from the automotive manufacturing industry.

Other proposed measures targeting affected regions

A number of publicly funded infrastructure investment and related projects have been suggested as a means of assisting employees and regions affected by announced retrenchments in the automotive manufacturing industry. For example, the Australian Manufacturing Workers' Union (AMWU) suggested that 'defence manufacturing could fill part of the gap left by Holden's closure' (AMWU 2013). The City of Salisbury advocated 'public sector investment in economic

infrastructure that ... lays a foundation for regional economic diversification' (sub. 227, p. 1). In addition, as noted above:

- the South Australian Jobs Plan contains a broad range of different measures to 'support industries to change and grow and to keep South Australians in work' (Government of South Australia 2014, p. 1)
- the Australian Government's reviews of the South Australian and Victorian economies are considering a range of measures to 'boost the competitiveness' of those economies, including by encouraging investment and innovation in high growth sectors, investing in infrastructure, relocating Commonwealth public service functions and 'considering the most pressing concerns of the shipbuilding industry' (Abbott and Macfarlane 2013).

Public investment in large-scale infrastructure

Efficient provision of infrastructure services is crucial for productivity and economic growth, as well as to promote social and environmental objectives. The costs and efficiency of transport, communication, energy, water and other infrastructure services bear strongly on firms' competitiveness and on community wellbeing in any region, and bottlenecks in infrastructure investment can have an adverse effect on wellbeing. (Infrastructure Australia (2008) has noted that bottlenecks may arise in major urban infrastructure due to poor planning and concerns about public criticism of infrastructure projects.)

However, there is little evidence, and what is available is mixed, on the effectiveness of targeted investments in infrastructure in promoting the development of regions affected by structural adjustment in Australia.

The little information that is available tends to focus on the employment effects of investment in one type of infrastructure. For example, Leigh and Neill (2011) found that expenditure on road construction through the Roads to Recovery program led to a reduction in local unemployment rates in the short term. However, Daley and Lancy (2011) found that over a longer time period the same program had no effect on employment.

At the international level, the OECD found that:

Polices targeting infrastructure are not usually the most effective tools for strengthening growth in underdeveloped regions, as infrastructure does not appear to be the binding constraint for the great majority of regions ... there is a need to revise development strategies that view infrastructure investments as the pre-eminent tool for regional development. In some instances, such investment may be better used for other purposes. (2012b, pp. 16, 22)

Infrastructure investment in targeted regions is just one part of the equation needed to promote growth:

Infrastructure is a necessary, but not sufficient, condition for growth. It is only relevant if human capital and innovation are also present in a region. (OECD 2009, p. 69)

In addition, a focus on seeking infrastructure investment or other financial support from external sources may be an impediment to growth.

How policy makers frame the challenges they face does matter. The case studies [of growth factors and bottlenecks to development in 23 regions] suggest that a self-conscious shift towards a growth-oriented policy framework is very often a part of the recipe for success. As long as policy makers focus on exogenous sources of support for a region, growth is unlikely to take off (OECD 2012b, p. 25).

More broadly, infrastructure investment decisions are best guided by efficiency considerations, rather than particular social objectives (PC 2008). Public investment decisions should involve a transparent analysis of the costs and benefits of all options prior to any major public infrastructure investment proceeding. The key efficiency issue in this context is whether a proposed project provides net benefits to the community as a whole (rather than to a specific region), and given limited resources, whether it generates the largest net benefits from the available options (regardless of the project's location).

Without such cost–benefit analysis, public investments are prone to ‘optimism bias’ and a confusion between political and economic objectives (Banks 2012). If poor infrastructure decisions are made, this can have a high opportunity cost and can be a long-term drag on the economy's productivity.

DRAFT FINDING 5.5

Infrastructure investments may in some cases assist in overcoming bottlenecks to greater economic activity in regions affected by structural adjustment. The key issue is whether a proposed infrastructure project provides net benefits to the community as a whole (rather than only to a specific region), and given limited resources, whether it generates the largest net benefits from the available options (regardless of the project's location).

Other targeted policies

Investment in ‘high growth’ sectors

In addition to infrastructure projects, governments have at times funded programs designed to encourage investment in particular industries based on the perceived advantages of those industries. This has typically included industries that are seen as

being ‘innovative’ or ‘advanced’ and industries that are forecast to grow quickly. However, evidence on the use of such policies in Australia suggests that governments do not have the necessary information or skills to judge which firms or industries will be successful in the future, and raises questions about the ability of government to successfully ‘pick winners’ in this way (PC 2012a). Without sound commercial fundamentals, investments attracted by government inducements are unlikely to translate into sustainable sources of employment and economic activity.

The drawbacks of regional adjustment funds (such as redistributing employment from one region to another without increasing overall economic activity) also apply to other policies that target development of particular industries. These adverse effects arise because:

... the subsidised project will draw capital and labour, particularly skilled labour, from other local firms. This will mean either that the wage rates of such employees increase, raising the costs of other firms within the local economy; or that some other potential projects will be stymied. At the extreme, there may be little or no change in employment in the local economy — that is, old jobs will be ‘crowded out’ by the new ones. (Banks 2002, p. 7)

Because of this crowding out, government funding of otherwise uneconomic investments in selected sectors will result in an inefficient allocation of resources and is likely to create jobs that are reliant on continued assistance.

Attracting public services or major projects

Policies that target development of particular regions (such as relocating public service functions) have often been justified by the desire to provide skilled employment, retain other local businesses, maintain the rating base of local government and keep schools with sufficient enrolment.

However, they can also redistribute employment from one region to another without increasing (and potentially reducing) overall economic activity. The likelihood of there being little effect on overall economic activity is magnified where different regions end up engaged in a bidding war to attract desired projects. As Van Biesebroeck noted:

If an investment project is expected to generate local benefits over and beyond its resource costs, it is likely to be pursued by many. Jurisdictions will engage in a bidding war to attract the project, offering competing incentive packages to increase the relative attractiveness of their locality. As a result, some of the potential benefits (externalities) will be competed away. (2008, pp. 219–20)

In addition, in bidding wars:

... a State or Territory that wins today could lose tomorrow, so that over time no jurisdiction is better off than it would have been simply competing on its merits ... From a national perspective, inter-State competition for investment conducted via selective assistance is a negative-sum game. (Banks 2002, p. 12)

Further, the desire to locate a project (such as a defence or shipbuilding project) in a particular region does not remove the need for a robust assessment of its costs and benefits to the Australian community as a whole.

Community development and regeneration

Investment in local infrastructure has been suggested as a means of promoting community building and regeneration in disadvantaged regions affected by closures in manufacturing and other industries. For example, the South Australian Government has announced a fund for projects, such as upgraded recreation facilities and new community centres, that ‘generate activity and rejuvenate local areas most affected by automotive industry restructuring’ (2014, p. 13).

Similarly in Victoria, the Revitalising Central Dandenong initiative is designed to address the poor connectivity, high unemployment and minimal economic growth in Dandenong (Places Victoria 2013b). The initiative commenced in 2005 and will take place over a period of 15 to 20 years (Places Victoria 2013a).

Evidence of the cost-effectiveness of regeneration projects is limited. Where such projects have contributed to regional growth, it has been on the basis of a clearly identified need. For example, in Bordeaux in France, regeneration of the city centre and investments in public transport were needed to accommodate projected population increases, and are seen as having contributed to regional growth and development (OECD 2012b). As with all investments, investment in regeneration and community building should only occur when it provides net benefits to the community as a whole.

The Commission’s view

In light of the limited evidence that targeted policies can cost-effectively facilitate structural adjustment in targeted regions, the need for more effective policy responses becomes apparent. As noted at the start of this chapter, broader economic policy settings have an important role in increasing the resilience of regions to structural change. By removing barriers that constrain firms and individuals in raising productivity and responding to market and competitive pressures,

broad-based economic and regulatory reforms would assist regions affected by structural change, as well as promote the wellbeing of the community more broadly.

The announced staged closure of the Ford and Holden plants gives all of those affected a period of time to prepare for change and there is time to ensure that any further assistance, if needed, is well-designed.

However, as noted in chapter 4, it is possible that a number of employees currently working for component manufacturers (many of which are small to medium size firms) that may be forced to downsize or close as a result of Ford and Holden's plant closures, may not receive the same degree of notice (or necessarily the same level of help) from their employers. To the extent that these employees rely on generally available services, it will be important to ensure that those services are sufficient. Indeed, some component manufacturing employees may warrant particular consideration if generally available measures appear to be insufficient for their circumstances.

The Commission is seeking input from participants on the extent to which generally available measures are likely to adequately address equity and efficiency concerns related to structural adjustment in the automotive manufacturing industry, and whether there are models of facilitating structural adjustment more cost-effectively. The limited availability of good evaluations of past structural adjustment assistance programs also places a high premium on designing a post program evaluation methodology and allocating funding for this sort of longitudinal evaluation at the time any new programs for the automotive industry are initiated.

INFORMATION REQUEST 5.1

The Commission is seeking further information on:

- *specific characteristics and needs of some groups of automotive manufacturing employees that might warrant particular consideration if generally available measures appear to be insufficient*
- *whether there are different circumstances facing employees from the extensive and varied component manufacturing sector as compared to Ford and Holden employees*
- *options for designing adjustment assistance programs for automotive manufacturing employees and regions affected by structural adjustment (together with evidence of the costs and benefits, and the effectiveness, of those options)*

A Conduct of the inquiry

The Commission received the terms of reference for this inquiry on 30 October 2013. Following receipt of the terms of reference, the Commission placed notices in the press and on its website inviting public participation in the inquiry. Information about the inquiry was also circulated to people and organisations likely to have an interest in it.

The Commission released an issues paper in November 2013, inviting public submissions and indicating particular matters on which it sought information. Following consultation with stakeholders and the receipt of submissions, a preliminary findings report was released on 20 December 2013. This report examined the local and global factors affecting the automotive manufacturing industry in Australia, and is available at www.pc.gov.au/projects/inquiry/automotive/preliminary. In total, 235 submissions were received in response to the issues paper and the preliminary findings report (table A.1). All submissions are available online at www.pc.gov.au/projects/inquiry/automotive/submissions.

The Commission has held meetings with a range of stakeholders, including motor vehicle producers, component manufacturers, industry bodies, unions and government departments (table A.2). The Commission also undertook consultations with automotive industry analysts and government departments in Japan and the United States (table A.3).

Public hearings were held in Adelaide on 2 December 2013 and in Melbourne on 3 and 10 December 2013. Participants in the public hearings are listed in table A.4.

The Commission is inviting further submissions in response to the draft findings and proposals in this position paper, and will hold further public hearings in February 2014. Also in February 2014, the Commission expects to release the interim results of quantitative modelling which considers the economywide effects of industry adjustment, and will hold a technical roundtable on this analysis in early March 2014. The contributions of inquiry participants and the Commission's further analysis will inform the Commission's final report, which will be delivered to the Australian Government by 31 March 2014.

The Commission would like to thank all those who have contributed to the inquiry.

Table A.1 Submissions received^a

<i>Individual or organisation</i>	<i>Submission number</i>
Abbott, Bonnie	154
Amato, Cosmo	204
ANCAP Australasia Limited	18
Angwin, Elicia	144
Australasian Fleet Management Association (AFMA)	41
Australian Arrow Pty Ltd	17
Australian Automobile Association	77
Australian Automotive Aftermarket Association (AAAA)	54
Australian Chamber of Commerce and Industry (ACCI)	71#
Australian Industry Group	42#
Australian Manufacturing Workers' Union (AMWU)	28
Australian Motor Industry Federation	74
Australian Performance Vehicles	5
Australian Productivity Council Pty Ltd	13
Australian Workplace Innovation and Social Research Centre	8
AutoCRC Limited	39
Autopolis	10, 224#
Backwell IXL	21
Baker, David	16
Bannwart, Robert	198
Beggs, Anthony	205
Bell, Adrian	82
Bernasconi, James	67
Berry, John	106
Bettinzoli, Roberto	220
Birch, Cheryl	119
Bisset, Jane	222
Bittmann, Tony	PFR233
Black, Simon	206
Blackwell, Judi	180
Blackwell, Simon	210
BlueScope	52
Bond, Geoffrey	185
Breen, Lyndal	197
Brokenbrough, Matthew	178
Brown, Chrissy	194
Bryant, Carole	209
Bus Industry Confederation	73
Business SA	46
BuyAustralianMade	40
Carmichael, Benjamin	167
Carroll, Julie	196
Carter, Susan	215

(Continued next page)

Table A.1 (continued)

<i>Individual or organisation</i>	<i>Submission number</i>
Centre of Policy Studies	7
Chassis Brakes International (Australia) Pty Ltd	53
Chop Wood Pty Ltd	2
City of Salisbury	227
ClimateWorks Australia	63
CNH Industrial ANZ	60
Confederation of Australian Motor Sport	59
Connell, Neil	186
Connor, Michael	147
Corcoran, Daniel	182
Coupe, Mark	166
Cowling, Diane	120
Crouch, Dean	110
Crowe, Robert	202
Crundwell, Shannon	157
Dalkie, Danielle	160
Darmody, Rod	124
Delaney, Alex	109
Dempsey, Peter	221
Denso Automotive Systems Australia Pty Ltd	72
Deviesseux, Shirley	130
DeVries, Timothy	3
Dewar, Stephen	127
Diver Consolidated Industries	25
Dixon, Peter	112
Docklands Science Park Pty Ltd	11#
Dunn, John	168
Dymmott, Geoffrey	126
Eagles, Andrew	207
Efron Media Group	26
Elisabeth	153
Engineers Australia	38
Excellent Plating Works Pty Ltd	4
Federal Chamber of Automotive Industries (FCAI)	30#
Federation of Automotive Products Manufacturers (FAPM)	69
Firehock, Andrea	149
Fitzgerald, John	183
Ford Motor Company of Australia Limited (Ford)	65*
Fordyce, David	133
Foxman, Marsha	PFR231
Frith, Matthew	214
Futuris Automotive (Australia) Pty Ltd	9
Gas Energy Australia (GEA) and Victorian Automotive	76

(Continued next page)

Table A.1 (continued)

<i>Individual or organisation</i>	<i>Submission number</i>
Geelong Manufacturing Council	24
Gellie, Christopher	228
Gilbert, Graham	226
GM Holden Ltd (Holden)	58
Government of South Australia	68
Gralton, James	150
Greg Marks Consultant	23
Griffiths, Brett	216
Grotty, Adam	187
Haden, Andrew	136
Hargreaves, Den	93
Harkness, Peter	83
Harness, Jennifer	200
Harrison, Colin	223
Hatchard, Kylie	115
Healey, Earl	179
Hella Australia Pty Ltd	45
Heraud, Peter	148
Hewetson, Mark	105
Hill OAM, Helga	140
Hill, Kent	132
Hofmann, Michael	114
Hooper, Brad	98
Houston OAM, Rev James	89
Hunter, Patrick	92
Hutchinson, John	141
Hutchison, Robert	184
Jeffress, Ross	188
Juric, Ivan	135
Kerr, David	75
Kerrigan, Wayne	116
Kiremitciyan, Murat	6
Kooiman, Lee	203
Land Values Research Group	PFR234
Law, Valerie	191
Le Clerc, Tony and Anne	165
Leblanc, Nicholas	146
Levis, Mike	129
Lim, Joseph	175
Lubin, Jean-Jacques	145
Lyons, John	12
Macintosh, Stuart	113
Maguire, Timothy	156

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<i>Individual or organisation</i>	<i>Submission number</i>
Mainstream Party	225
Manning, Phil	95
Manufacturing Focus	33
Marguin, Ariel	159
Mascull, Troy	171
Masson, Rod	190
Matthews, Roy P	79
May, Barrie	211
McLachlan, Daniel	100
McLean Management Consultants	57
McLean, Wayne	151
McLeish, Amelia	143
Merridew, Christopher	80
Meyers, Janis	199
MHG Asia Pacific Pty Ltd	27
Miller, Lee	173
Mortimore, Anna	64
MTM Pty Ltd	29
Murphy, Peter	139
Murray, Luke	104
Mushalik, Matt	PFR232
Naumovski, George	163
Nesbitt, Michael	122
PACCAR Australia Pty Ltd	61
Palm Products	56
Papanicolaou, Dorothy	84
Patrick, Brad	125
Pedersen, Jacqui	88
Peperkamp, Ben	103
Perez, Luis	164
Pitcher, Shirley	87
Pitt, Lincoln	111
Plastic Products	35
Podger, Geoff	193
PolyPacific Pty Ltd	44
Porter, Matthew	101
Powell, Anthony	217
PPB Advisory	55
Professionals Australia	22
Quinlan, Alan	174
Rebbeck, Adam	158
Reed, Karl	47, 138
Reynolds, Mark	108

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Table A.1 (continued)

<i>Individual or organisation</i>	<i>Submission number</i>
Richardt, Kevin	170
Robert Bosche (Australia) Pty Ltd	78*
Robins, Allan	14
Robinson, Gertrude	131
ROH Automotive	49
Rutherford, Lesley	123
Sardelis, Bill	86
Schafer, Bruce	161
Seccombe, Roger	176
Seymour, Michael	107
Shearer, Sandy	155
Sherwin, Erik	117
Shields, Glenn	192
Sipma, Christine	195
Smith, John	37
Smith, Mark	81#
SMR Automotive Australia Pty Ltd	51
Society of Automotive Engineers Australasia	43
Spencer, Gwenda	189
Spittle, Joan	97
Stephens, Shaun	152
Stewart, James	PFR230
Stokes, Kristen	137
Storrar, Brian	142
Struben, Colin	162
Sutherland, Heidi	169
Swain, Sam	208
Swift, Suzanne	121
Swinburne University of Technology	36
Thomas, Graham	96
Thurgood, Peter	201
TI Automotive Australia	62
Tomcar Australia Pty Ltd	32
Toner, Phillip	34
Toyota Motor Corporation Australia Limited (Toyota)	31
Trevethan, Howard	128
Trindall, Lyn	181
Tucker, Lorrella	219
Turner, Peter	118
TXM Lean Solutions Pty Ltd	48
VCAMM Ltd	19
Victorian Government	70#
Votano, Maria	91

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<i>Individual or organisation</i>	<i>Submission number</i>
White, Nathan	213
Warrilow, Andrew	85
Watson, Max	94
Watson, Wayne	218
Wheatley, Irene	102
White, Garry Martin	1
White, Peter Graham	PFR229
White, Peter	20, 90
Will, Dr. Frank	50, PFR235
Williamson, Maree	212
Wilson, Anthony	172
Wilson, Jason	99
Women in Adult and Vocational Education	66
Wylie, David	15
Wylie, David	134
Zakaria, Jack	177

^a An asterisk (*) indicates that the submission contains confidential material NOT available to the public. A hash (#) indicates that the submission includes attachments.

Table A.2 Visits and consultations — Australia

Individual or organisation

ACT

Australian Chamber of Commerce and Industry
Australian Industry Group
Department of Foreign Affairs and Trade
Department of Industry
Department of Prime Minister and Cabinet
Federal Chamber of Automotive Industries
Treasury

South Australia

Futuris
South Australian Government
TI Automotive

Victoria

Australian Automotive Aftermarket Association
Australian Council of Trade Unions
Australian Manufacturing Workers' Union
AutoCRC
Automotive Supplier Excellence Australia
Federation of Automotive Products Manufacturers
Ford Motor Company of Australia
General Motors Holden
Toyota Australia
Victorian Department of Premier and Cabinet
Victorian Department of State Development, Business and Innovation
Victorian Department of Treasury and Finance

Western Australia

Professor Goran Roos

Table A.3 Visits and consultations — Japan and United States

Individual or organisation

Japan

Austrade
Bloomberg News Corporation
Department of Foreign Affairs and Trade
European Automobile Manufacturers Association (ACEA)
Fujitsu Research Institute (FRI)
Japan Automobile Importers Association (JAIA)
Japan Automobile Manufacturers Association Inc. (JAMA)
Japan Society for The Promotion of Machine Industry
Meiji University, School of Business Administration
Ministry of Economy, Trade and Industry (METI)
Mizuho Bank, Industry Research Division
University of Tokyo, Faculty of Economics

United States

Brookings Institution
Congressional Research Service
Terry Barr Sales
University of Michigan, Transportation Research Institute
United States Treasury, Office of Financial Stability
United States Department of Commerce

Table A.4 Public hearings

<i>Individual or organisation</i>	<i>Transcript page numbers</i>
Adelaide — 2 December 2013	
Australian Workplace Innovation and Social Research Centre, The University of Adelaide	3–12
South Australian Government	13–25
Australian Manufacturing Workers' Union (AMWU)	26–37
Australian Automotive Aftermarket Association (AAAA)	38–47
Professor Goran Roos	48–68
Melbourne — 3 December 2013	
Australian Industry Group	72–82
Palm Products	83–89
BuyAustralianMade	90–94
Federation of Automotive Products Manufacturers (FAPM)	95–112
Diver Consolidated Industries	113–117
MTM Pty Ltd and Tomcar Australia	118–128
Australian Productivity Council	129–134
Society of Automotive Engineers Australasia	135–140
Australian Manufacturing Workers' Union (AMWU)	141–151
Federal Chamber of Automotive Industries (FCAI)	152–160
Toyota Australia	161–173
Frank Will	174–180
Australasian Fleet Management Association	181–187
PolyPacific Pty Ltd	188–193
Melbourne — 10 December 2013	
GM Holden Australia	196–217

B International assistance arrangements

As outlined in chapter 2, automotive manufacturing industries in many countries benefit from a wide range of government assistance measures (often from all levels of government), including:

- tariff and non-tariff barriers, such as quotas, taxes and excise duties
- direct government assistance to the domestic automotive industry, such as co-investment capital grants, loans and loan guarantees, investment in equity, investment in relevant infrastructure, incentives to motivate retirement of older vehicles, and subsidies (direct and indirect, including subsidies to lower the price of inputs)
- regulatory barriers to trade or potential barriers, such as excessive safety, fuel efficiency, emissions or quality standards and certification programs, and other forms of assistance, such as fleet procurement policies
- assistance measures that are broadly available and can be accessed by the automotive manufacturing industry, including export financing, wage subsidies, research and development (R&D) support and tax concessions or exemptions.

Further, it is at times alleged that some countries have intervened in financial markets with a deliberate strategy of lowering or suppressing the value of their national currency, which among other effects could have a benefit to their domestic automotive manufacturing industry.

In line with the terms of reference for this inquiry, the Commission has conducted a desktop survey of the government assistance measures in nine major and emerging automotive-producing countries or regions.

The Commission faced a number of challenges when undertaking this survey. Evidence on assistance measures often lacks transparency, is dispersed and difficult to verify and covers different time frames across countries. Moreover, for many forms of assistance, it has been possible to only give examples of what was committed by governments as being available to firms, rather than its budgetary cost, disaggregated by industry.

Some government policies have a broad objective, such as promoting environmental outcomes, rather than the specific objective of providing assistance to automotive

manufacturing. The Commission has erred on the side of including the broader policies where it considered they could provide assistance to the automotive manufacturing industry.

The Commission is grateful for the assistance of the Department of Foreign Affairs and Trade in locating some of the information contained in this appendix.

B.1 Tariff rates

Tariff rates on motor vehicles and components imposed by selected countries (including Australia) are given in table B.1.

It should be noted that tariff rates vary according to each country's tariff schedule, with different rates applicable under different circumstances (often highly specific in definition). As such, the rates below should be taken as indicative of the range of generally applicable tariff rates in the selected countries shown. The figures do not account for the bilateral and regional trade agreements in force between countries that can have complex effects on the *actual* tariff rates applied to automotive products under various conditions.

Table B.1 **Applied tariff rates, selected countries**
2013

<i>Country or region</i>	<i>Tariff rate on passenger vehicles^a</i>	<i>Tariff rate on commercial vehicles^b</i>	<i>Tariff rate on automotive components^c</i>
	%	%	%
Australia	5	5	5
Brazil	35	35	0–18
China	25	6–25	3–25
European Union	10	22	3–4.5
India	60–100	10	10
Japan	0	0	0
Mexico	20	20	0–5
Korea	8	10	8
Thailand	80	40	10,30
United States	2.5	0–25	0–2.5

^a Based on HM Code 8703 — motor cars and motor vehicles principally designed for the transport of persons.

^b Based on HM Code 8704 — motor vehicles for the transport of goods. ^c Based on HM Code 8708 — parts and accessories of motor vehicles.

Sources: Advice from DFAT (11 December 2013); US Department of Commerce (2011); WTO (2013).

B.2 Brazil

Table B.2 **Examples of government assistance to the automotive manufacturing industry in Brazil**

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	<i>None identified.</i>
Tax concession	<p>The Brazilian Government's 'Inovar Auto' policy increases the federal industrial products tax on vehicles by 30 per cent, offset by a 30 per cent tax concession to eligible automotive manufacturers. Eligibility for the concession is contingent on:</p> <ul style="list-style-type: none"> • average vehicle fuel efficiency • the number of manufacturing processes that are undertaken in Brazil (Inovar Auto identifies 12 specific processes) • local investment in research and development, engineering, industrial technology and/or components suppliers • participation in standardised labelling for vehicle emissions (ICCT 2013; Tavares 2012). <p>A tax concession is also available to foreign automotive manufacturers that import vehicles into Brazil (subject to local investment requirements), although only for a maximum of 4800 vehicles per year (PwC 2012).</p> <p>The Brazilian Government has temporarily reduced the rate of the industrial products tax on vehicles since May 2012 as a stimulus measure. Initially, the tax cuts were to last for only three months, but they have been extended multiple times — most recently in April 2013 until December 2013 at a forecast cost of BRL2.2 billion (Government of Brazil 2012; SECOM 2013).</p>
Loans and other financing programs	<p>The Brazilian Development Bank provides support to automotive manufacturers in the form of low interest rate loans. Recent examples include BRL2.4 billion in financing for a new Fiat car plant, BRL373.5 million to expand Renault's engineering program, and BRL342 million for Volkswagen to design and develop new vehicles (BNDES 2012a, 2012b, 2013).</p> <p>During the global financial crisis, the Brazilian Government directed the Brazilian Development Bank and state-owned commercial banks to provide automotive manufacturers and components suppliers with easier access to credit (ILO 2010).</p>
Input price subsidy	<p>Petrol and diesel prices in Brazil are indirectly regulated, with the pricing policy of oil producer Petrobras subject to the approval of the Brazilian Government — the company's major shareholder. Petrobras's pricing methodology is not publicly disclosed, however, a stated objective of the policy is to prevent 'volatile' international oil prices from being passed on to consumers. Consequently, retail prices for petrol are lower than the cost to Petrobras of importing refined fuel. In November 2013, Petrobras announced increases in the refinery gate price of petrol and diesel of four and eight per cent respectively (Petrobras 2013a, 2013b).</p>
Rebates to consumers	<i>None identified.</i>

(Continued next page)

Table B.2 (continued)

<i>Policy type</i>	<i>Policy description</i>
Technology standard	<p>Brazil's emissions standards for new vehicles are based on those adopted by the European Union, with some variation (IBAMA 2011; UNEP 2012).</p> <p>Since 1976, all petrol in Brazil must be blended with ethanol. The current standard is a fuel blend of 25 per cent anhydrous ethanol to 75 per cent petrol, although fuel blends with as little as 18 per cent ethanol are permitted. The Brazilian Government's championing of biofuels has encouraged the development of flexible-fuel engines, which are capable of switching between fuel blends and 100 per cent ethanol fuel (UN-Energy 2011).</p>
Government procurement	<i>None identified.</i>
Other assistance	<p>Under a modified protocol to a bilateral trade agreement between Brazil and Mexico, the Brazilian and Mexican Governments will apply export quotas until March 2015 on vehicles traded between the two countries. As part of the protocol, the governments also required manufacturers to increase the proportion of vehicle components sourced locally from 30 to 35 per cent in 2012, and to 40 per cent by 2016 (Ministry of Economy (Mexico) 2012).</p>

B.3 China

Table B.3 **Examples of government assistance to the automotive manufacturing industry in China**

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	<p><i>Key government programs</i></p> <p>China's <i>Twelfth Five-Year Economic and Social Development Plan (2011–2015)</i> designates the 'new-energy automobile industry' (encompassing electric hybrid cars, pure electric cars and fuel cell cars) as one of seven strategic industries for support and development into leading pillar industries. The plan states that the Government will set up special funds for the development of these strategic industries and expand the size of government start up investment (National People's Congress (China) 2011).</p> <p>Specific assistance measures were detailed in supplementary sectoral plans, such as the <i>Energy Saving and New Energy Vehicles Industry Development Program (2012–2020)</i>.</p> <ul style="list-style-type: none"> • Under the Energy Saving and New Energy Vehicles Industry Development Program, the Government has allocated funds for R&D, engineering, standard making and market applications of energy-saving (efficient internal combustion engine cars) and new energy vehicles (National Energy Administration (China) 2012). It has been reported that China plans to invest US\$18 billion over the period of the plan in the development of electric and hybrid vehicles and their key components (Stewart and Stewart 2012). • On 8 November 2013, the Ministry of Industry and Information Technology made remarks re-affirming the Government's intention to further expand development of new-energy vehicles, and that China had provided subsidies for this development by RMB 5.7 billion as at the end of the 2012 (translation provided in advice from DFAT, 24 January 2014).

(Continued next page)

Table B.3 (continued)

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	<ul style="list-style-type: none"> The Australian Trade Commission (2013) notes that China's Ministry of Finance intends to invest over RMB 1 trillion in further research on energy efficient and new-energy technologies.
Input price subsidy	Subsidies have been provided for a number of inputs (land, coal, electricity, natural gas, automotive glass, and cold-rolled steel) used by Chinese automotive and component manufacturers (Haley and Haley 2013; Stewart and Stewart 2012).
Rebates to consumers	<p>The Chinese Government offers subsidies of RMB 3000 for the purchase of vehicles of 1.6 litres or less (Ministry of Finance (China) and National Development Reform Commission (China) 2013). In 2013, the Chinese Government together also announced a national subsidy scheme for consumers in 28 specified cities of up to RMB 60 000 for the purchase of listed new-energy vehicles. Many local municipal agencies offer subsidies to augment the national scheme (advice from DFAT, 24 January 2014).</p> <p>Subsidies for the retirement and update of old vehicles have also been used (Stewart and Stewart 2012). For example, Beijing offers scrappage payments (until 31 December 2014) of between RMB 2500 to RMB 14 500 to vehicle owners who scrap vehicles made in 1995 or earlier (Automotive News China 2013).</p>
Capital subsidy or grant	<ul style="list-style-type: none"> Some provincial governments have implemented measures to support their local automotive industry in accordance with the policies and directives issued by the central government, including the Twelfth Five-Year Plan and the Energy Saving and New Energy Vehicles Industry Development Program. These measures include preferential tax treatment, loan interest subsidies and credit support, and discounts on land prices (Stewart and Stewart 2012). <p>There have been some public estimates of assistance to the automotive industry in China.</p> <ul style="list-style-type: none"> Haley and Haley (2013) reported that the Chinese central and seven local (provincial) governments distributed about US\$18.4 billion in subsidies to the auto-parts industry through technology-development and industrial restructuring policies from 2001–2011. <p>In September 2012, the United States raised a World Trade Organization (WTO) dispute challenging Chinese export subsidies to its automotive and automotive parts manufacturers. The Office of the United States Trade Representative argued that these subsidies, including cash payments for exporting, R&D grants, financing assistance and preferential tax treatment, contravene WTO rules (which prohibit subsidies based on export performance), and amounted to at least US\$1 billion over the period 2009–2011. It noted that despite having joined the WTO more than a decade prior, China had still not provided a complete notification of its central, provincial and local government subsidies (USTR 2012a, 2012b).</p>
Tax concession	<p>The High and New Technology Enterprise qualification is an incentive available to automotive parts manufacturing companies that grants a 15 percent preferential corporate income tax rate to companies that meet the criteria (KPMG 2014). Also, under the <i>Automotive Industry Development Policy</i> (2004 and updated in 2009) R&D expenses are tax deductible (KPMG 2004).</p>

(Continued next page)

Table B.3 (continued)

<i>Policy type</i>	<i>Policy description</i>
Loans and other financing programs	<p>The Twelfth Five-Year Plan states that the Government will make comprehensive use of preferential financial policies, such as risk compensation, and encourage financial institutions to strengthen credit support for the seven strategic industries identified in the plan (National People's Congress (China) 2011).</p> <ul style="list-style-type: none"> • There are also reportedly a range of government measures to promote exports from China, including export targets, export financing and insurance support, and restrictions on export of raw materials aimed at increasing their relative domestic supply and restricting world supply (Stewart and Stewart 2012). For example, the authors reported that China ExIm Bank extended a RMB 5 billion export credit to Chery Automotive in 2005 and a further RMB 10 billion export credit in 2008. The bank also contributed an undisclosed portion of financing toward a US\$2.7 billion Geely Auto takeover of Volvo in 2010 (Stewart and Stewart 2012).
Technology standard	<p>The Energy Saving and New Energy Vehicles Industry Development Program sets goals for improved fuel efficiency. For example, a target average fuel consumption of 6.9 litres per 100km for all passenger vehicles by 2015 and 5.0 litres by 2020 (Australian Trade Commission 2013; National Energy Administration (China) 2012).</p> <ul style="list-style-type: none"> • It has been reported that some provincial governments have passed laws that favour their local manufacturers, for example by setting vehicle specifications for taxis to match those of locally manufactured vehicles (Haley and Haley 2013).
Government procurement	<p>In 2012, 11 Chinese Government departments started using domestically made electric vehicles as their official business vehicles (Government of China 2012). Foreign made and joint-venture made cars were excluded from the Chinese Government's 2012 draft public procurement list for government vehicles (China Daily 2013; Global Trade Alert 2013). While a final list does not appear to have been adopted, a recent report suggests that Volvo Car Corporation (Chinese owned) was added to the list this year (Murphy and Zander 2013).</p>
Other assistance	<p><i>GDP target</i> — The Twelfth Five-Year Plan states that the proportion of the value added of new strategic industries (of which the new energy automobile industry is one) should comprise about 8 per cent of GDP by 2015 (National People's Congress (China) 2011).</p> <p><i>Production target</i> — The Energy Saving and New Energy Vehicles Industry Development Program sets an objective for China to produce and sell annually 500 000 battery electric and plug-in hybrid electric cars by 2015, 2 million by 2020 and a cumulative sales total of 5 million between 2015 and 2020 (European Chamber of Commerce in China 2013).</p> <p><i>Foreign ownership and local content requirements</i></p> <ul style="list-style-type: none"> • Wholly foreign-owned enterprises in vehicle assembly are not permitted in China (ownership is restricted to 50 per cent through joint ventures with domestic companies). • Wholly foreign-owned enterprises are permitted for automobile parts manufacturers, with the exception of new energy vehicle battery manufacturing facilities for which ownership is restricted to 50 per cent (USTR 2011, 2012a). • Foreign investors are limited to no more than two joint ventures with Chinese partners for producing passenger motor vehicles and two joint ventures for commercial vehicles (European Chamber of Commerce in China 2013). • In January 2012, the Chinese Government amended its list of priorities for foreign investment, removing vehicle manufacturing from the 'encouraged' category and placing it in the 'permitted' category in view of current overcapacity and the large amount of foreign direct investment in vehicle manufacturing. Instead, China is encouraging investment in R&D and 'new energy' vehicles (Australian Trade Commission 2013).

B.4 European Union

Table B.4 **Examples of government assistance to the automotive manufacturing industry in the European Union**

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	<p>'Regional aid' enables EU member states to support development in specified economically disadvantaged regions (subject, in most cases, to the approval of the European Commission). Regional aid has been used by various governments to help finance the establishment or expansion of car manufacturing plants (EC 2006b). For example, the German Government has undertaken to contribute €43.7 million towards the €521.6 million expansion of a Porsche facility in Leipzig (although this aid is the subject of a European Commission investigation as to whether it complies with the regulatory framework for allowing regional aid) (EC 2012b).</p> <p>Under the <i>Framework for State aid for Research and Development and Innovation</i>, EU member states may grant aid to manufacturers for:</p> <ul style="list-style-type: none"> • R&D projects for cars (including for 'green' technology) • technical feasibility studies in preparation for R&D projects • process and organisation innovation in services (but not for 'routine or periodic changes' to production lines and manufacturing processes) • establishing and operating innovation clusters to support open research, including for training and research facilities and information and communications technology infrastructure (EC 2006a). <p>Examples of funding for research, development and innovation include:</p> <ul style="list-style-type: none"> • €20.5 million in aid from the French Government to Renault for the development of diesel hybrid commercial vehicles (EC 2013a) • €24.2 million in aid from the French Government to Valeo (a car component manufacturer) for the development of a hybridisation system for petrol engines (EC 2013b). <p>Separate from grants to any individual manufacturers, general research programs may also benefit the automotive industry. For example:</p> <ul style="list-style-type: none"> • the German Government committed €500 million between 2009–11 for R&D under the National Development Plan for Electric Mobility. A further commitment of €1 billion from the Government's Energy and Climate Fund extended these efforts until 2013 (BMW 2012) • the UK Government announced in 2013 that it was committing £500 million over ten years to a new research centre for advanced engine technologies, to be matched by a further £500 million investment by industry partners (Cable 2013). <p>The European Commission may also authorise member states to provide assistance for worker training, where there is an underinvestment in training that contributes to market failures (European Parliament 2009; Foecking and Majcher-Williams 2010).</p>
Tax concession	<p>Many member states offer tax concessions for consumers to purchase electric, hybrid and/or other alternative fuel vehicles. In several cases, owners of eligible vehicles may be fully exempted from paying vehicle-related taxes (such as vehicle registration charges, road taxes and fuel consumption taxes). In other cases, vehicle-related taxes are applied at a discounted rate, or are waived for an initial registration period (ACEA 2013a).</p>

(Continued next page)

Table B.4 (continued)

<i>Policy type</i>	<i>Policy description</i>
Loans and other financing programs	<p>The European Investment Bank (EIB) has provided loans to car manufacturers across Europe, including to sponsor investments in 'green' technology. During 2009 and 2010, as part of the European Clean Transport Facility, the EIB reported lending €3.1 billion to car manufacturers (Srejber 2010). In November 2012, the European Commission and EIB announced further cooperation on financing innovation in Europe's automotive sector as part of the 'CARS 2020 Action Plan' (EC 2009, 2012a).</p> <p>Under the <i>Community guidelines on state aid for rescuing and restructuring firms in difficulty</i>, the European Commission permits member states to offer loans or loan guarantees to companies that require urgent assistance to avert otherwise inevitable financial collapse. To be approved under the guidelines, any state aid must be restricted to the minimum amount necessary, not impose undue adverse spillover effects on other member states, and adhere to the principle of 'one time – last time' — that is, troubled companies cannot be repeatedly bailed out by governments. On this basis, the European Commission authorised £6.5 million in loans from the UK Government to assist MG Rover in 2005 (EC 2004, 2005).</p> <p>During the global financial crisis, the European Commission permitted member states to subsidise interest repayments and/or offer state guarantees on loans. These temporary provisions, which expired at the end of 2010, were intended to facilitate car companies' access to credit (EC 2009). As one example, restructuring aid from the French Government to PSA Peugeot Citroën included a state guarantee to cover the company's bond issues (an estimated subsidy equivalent of €486 million) (EC 2013c). More generally, in that period:</p> <ul style="list-style-type: none"> • the French Government provided €6 billion in loans to Peugeot Citroën and Renault, €2 billion to the financial services operations of these two firms and €600 million to automotive industry suppliers (AFP 2009) • the German Government loaned €1.5 billion in bridge financing to the Opel automotive manufacturing firm in 2009 (Government of Germany 2009) • the Swedish Government gave SEK 20 billion (about US\$3 billion) in credit guarantees to automotive manufacturing firms (AFP 2008), which were used in loans of approximately SEK 4 billion each to Volvo and Saab. The Volvo loan was repaid to the Government in 2012, but the Saab funds were lost when the company went bankrupt in 2011 (advice from DFAT, 24 January 2014) • the UK Government provided £2.3 billion in loans and loan guarantees during 2009–2010 to automotive manufacturing firms under the Automotive Assistance Program (House of Commons Business and Enterprise Committee (UK) 2009).
Input price subsidy	<i>None identified.</i>

(Continued next page)

Table B.4 (continued)

<i>Policy type</i>	<i>Policy description</i>
Rebate to consumers	<p>During the global financial crisis, various EU member states adopted scrappage programs for old vehicles ('cash for clunkers') to boost demand for new vehicles.</p> <ul style="list-style-type: none"> • In France and Italy, consumers were only eligible for a rebate where the vehicle they were purchasing met carbon dioxide emissions targets. • The Portuguese and Spanish Governments initially operated scrappage programs without emissions targets for vehicles, but later amended their schemes to include such targets for some vehicles. The Portuguese Government included emissions targets from January 2009 to December 2010 (when the program was suspended), and the Spanish Government included such targets from September 2008. • The Dutch, German and UK governments did not apply emissions targets in their scrappage programs at any stage (although in the Netherlands, a more generous rebate was available for diesel-engine vehicles) (Leheyda and Verboven 2013). <p>None of the programs discriminated between domestically (or European) produced and imported vehicles.</p>
Other assistance	<p>The German state of Lower Saxony holds approximately 20 per cent of voting rights in Volkswagen. Under the federal German Government's 'Volkswagen Law', some decisions for consideration at an annual general meeting of Volkswagen's shareholders require a majority of more than 80 per cent of the decision-making capital of the company. This provides the Lower Saxony Government with veto powers over major corporate decisions at Volkswagen (Court of Justice of the European Union 2013).</p>

B.5 India

Table B.5 **Examples of government assistance to the automotive manufacturing industry in India**

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	<p>The Indian Government has contributed around INR 22.9 billion in funding to the National Automotive Testing and R&D Infrastructure Project, which involves establishing and upgrading automotive testing and research facilities around the country. Additionally, state governments that host project facilities have granted land at concessional rates (NATRIP 2013).</p>
Tax concession	<p>The Indian Government applies reduced excise duty rates for small and fuel-efficient vehicles, as well as hybrid engine systems. Custom duties concessions for specified components for electric and hybrid vehicles are also available until March 2015 (Government of India 2013; Haugh, Mourougane and Chatal 2010).</p> <p>Some state governments also offer tax concessions for vehicle purchases. For example:</p> <ul style="list-style-type: none"> • the Delhi Government provides a refund on value added tax, road tax and registration charges for purchases of new electric vehicles (Delhi Government 2012) • state governments in Madhya Pradesh, Kerala, Gujarat and West Bengal have reduced excise taxes on electric vehicles (Perdiguero and Jiménez 2012).

(Continued next page)

Table B.5 (continued)

<i>Policy type</i>	<i>Policy description</i>
Loans and other financing programs	The Indian Government provides funding to state-owned banks in order to boost their capital adequacy ratios, with a stated intention that this should enable banks to extend more credit to households — including for (but not exclusive to) automotive financing. The Indian Government committed to capital infusions totalling INR 140 billion as part of the 2013-14 budget, and in October 2013 announced ‘in principle’ support to provide additional bank funding to further stimulate consumer demand (Ind-Ra 2013; Ministry of Finance (India) 2013).
Input price subsidy	Diesel, kerosene and Liquefied Petroleum Gas fuels are subsidised, while many oil marketing companies still set retail prices at below-market levels and claim the difference between global market prices and local prices from the Ministry of Finance at a favourable rate (Lang and Wooders 2012).
Rebates to consumers	Between November 2010 and March 2012, the Indian Government provided a rebate of up to 20 per cent on the ex-factory prices of electric vehicles with 30 per cent of their parts manufactured in India, up to a maximum of INR 100 000. Manufacturers were expected to claim the rebate from government, and pass the lower prices on to consumers. INR 950 million was budgeted for the scheme (MHIPE 2012). State governments have also introduced subsidies. For example, the Delhi Government provides a 15 per cent rebate on the base price of electric vehicles. The rebate is partly funded by a levy imposed on the sale of diesel fuel in Delhi (Delhi Government 2012).
Technology standard	India’s emissions standards for new vehicles are based on those adopted by the European Union, with lagged implementation (Urdhwareshe 2013).
Government procurement	The Indian Government maintains a list of approved vehicle models that can be used by ministers and senior public servants as staff cars (Ali 2004; Arora 2003). All approved models are manufactured in India. Central public sector enterprises are permitted to purchase any new model of small-engine car manufactured in India, with consideration given to fuel efficiency and environmental impact (Dongre 2013).

B.6 Japan

Table B.6 **Examples of government assistance to the automotive manufacturing industry in Japan**

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	The Japanese Government does not specifically fund programs for the automotive manufacturing industry. Its industry assistance programs are generally targeted at small and medium enterprises, and so Japanese car makers are usually ineligible (advice from DFAT, 21 January 2014).
Tax concession	The Japanese Government offers vehicle-related tax incentives to encourage businesses and households to purchase electric, hybrid, natural gas and fuel-efficient petrol/diesel vehicles. Depending on what environmental standards the vehicle meets, the owner may be eligible for exemptions or reductions on acquisition and tonnage (registration) taxes (JAMA 2013).

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Table B.6 (continued)

<i>Policy type</i>	<i>Policy description</i>
Tax concession	<p>Light cars ('kei' cars), defined as those with engine displacement below 660 cc and meeting certain height, width and length restrictions, receive preferential tax treatment (they can pay as little as 25 per cent of the weight tax of a non-'kei' similar vehicle). Foreign automotive manufacturers have complained that the specifications of 'kei' cars have been designed to favour Japanese car makers. The Japanese Government is considering changing the tax treatment of 'kei' cars to bring it closer in line with the taxation of other small cars, but has not yet made a final decision (advice from DFAT, 21 January 2014).</p> <p>Japan's 'Special Measures for Industrial Revitalization and Innovation' provides the government with scope to support business efforts to restructure and innovate. The special measures available include government subsidies, debt guarantees and tax concessions. The policy has had limited application in Japan's automotive industry.</p> <p>In 2012, the Japanese Government approved measures that entitled Mazda Motor Corporation to a concession on the registration and license tax for a proposed capital raising. The capital raising by Mazda was to facilitate a restructuring of the company, which the government deemed to be a 'resources productivity innovation', and eligible for support under the legislation (METI 2012).</p>
Loans and other financing programs	<i>No examples identified.</i>
Input price subsidy	<p>The Japanese Government offers an Employment Adjustment Subsidy, which provides employers with a time-limited subsidy of up to 80 per cent of workers' wages (67 per cent for large companies) as an incentive to maintain employment levels during production downturns. Subsidies may be paid to employers for workers to take leave, to be temporarily transferred to another job, or to undertake education and training (Hirashima 2013; Soble 2009; Steinberg and Nakane 2011).</p>
Rebates to consumers	<p>In June 2009, the Japanese Government introduced two forms of consumer subsidy to encourage purchases of fuel-efficient vehicles — a scrappage program for replacing old vehicles with more fuel-efficient models, and a direct grant (without requiring that an old vehicle be traded in) for new cars that met high fuel-efficiency and emissions standards. Initially, few foreign cars were eligible for the subsidy, as they had not been certified as meeting the necessary standards. After complaints from the United States Trade Representative, the Japanese Government modified the program to allow more foreign cars to qualify for subsidies (Cooper 2010). Both streams of the consumer subsidy program ended in September 2010 (Canis et al. 2010). Following the 2011 Tohoku earthquake, a second round of 'eco car' subsidies — for which JPY300 billion was budgeted — was made available from December 2011 until September 2012 (IEA 2013; Waschilowski 2012).</p>

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Table B.6 (continued)

<i>Policy type</i>	<i>Policy description</i>
Technology and safety standards	<p>The Japanese Government imposes fuel economy standards for all vehicle manufacturers selling in the Japanese market — those that fail to comply are subject to official warnings and, subsequently, financial penalties. All vehicles must also be certified for safety and greenhouse gas emissions, with a higher standard ‘four-star status’ available for the most environmentally friendly models (JAMA 2009). Foreign automotive manufacturers, such as in the US and EU, have argued that the Japanese Government’s refusal to recognise similar internationally-based testing imposes a cost burden on imported vehicles (ACEA 2013b; Marantis 2013).</p> <p>For low-volume imported vehicles (where less than 5000 vehicles per year per vehicle type are to be brought into Japan) an alternative to full assessment by Japanese regulators is available under a ‘Preferential Handling Procedure’. Under this procedure, the certification of the exporting-country regulator is recognised as sufficient to accredit a vehicle for sale in Japan (Canis et al. 2010; JAMA 2009; USTR 2013).</p>
Government procurement	<i>None identified.</i>
Other assistance	<p>The New Energy and Industrial Technology Development Organization (NEDO) is an independent administrative agency that receives funding from the Japanese Government. NEDO coordinates R&D efforts in industry, academia and government, focusing on industrial, energy and environmental technologies. In relation to Japan’s automotive sector, recent research by NEDO has focused on battery and fuel technologies for vehicles. Some projects include:</p> <ul style="list-style-type: none"> • basic research, since 2009, into lowering the costs and improving the performance of electric vehicle batteries (NEDO 2013) • a 2008–12 research project into hydrogen supply infrastructure to support commercialisation of fuel cell vehicles (NEDO 2012). <p>Requirement for the biennial inspection and testing of vehicles that have been in use for at least three years provides some incentive for Japanese consumers to purchase new vehicles, rather than incur costs to maintain older vehicles to the requisite safety and environmental standards. This effect was more pronounced prior to reforms to the inspection and testing regime in the mid-1990s — in 1993, the average car age was 2.93 years; by 2009, it had risen to 7.49 years (Kitano 2013; Smitka 2002, 2013).</p> <p>Devaluation of the Japanese yen through monetary easing by the Japanese Government resulted in a depreciation of about 25 per cent against the US dollar between December 2012 and May 2013 (McKinnon and Liu 2013).</p>

B.7 Korea

Table B.7 **Examples of government assistance to the automotive manufacturing industry in the Republic of Korea**

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	<p>The Korean Government has committed to supporting the development and adoption of alternative fuel technology for vehicles, including investments in:</p> <ul style="list-style-type: none"> • R&D into improving mileage for electric vehicles • commercialisation of hydrogen fuel cars • establishment of electric vehicle charging infrastructure (OECD 2012a; PCGG 2011). <p>The Korean Government provides approximately US\$100 million (roughly KRW 100 billion) per year to support R&D (advice from DFAT, 28 November 2013). Examples of assistance to R&D include:</p> <ul style="list-style-type: none"> • a program to develop replaceable batteries for electric buses, supported by about KRW 17.2 billion of government funding over the period 2010–2013 (Ministry of Land, Infrastructure and Transport (Korea) 2012) • programs to develop natural gas vehicles (including buses), to be supported by about KRW 10 billion of government funding per year over the period 2012 to 2015 (unofficial translation of Korean Ministry of Environment press release supplied in advice from DFAT, 28 November 2013).
Tax concession	<p>The Korean Government applies lower consumption and vehicle tax rates for small-engine vehicles. For the smallest category of engine (capacity less than 1000 cc) most taxes applied on the purchase of a vehicle are waived (KAMA 2013).</p> <p>Hybrid vehicles attract a tax exemption up to a maximum of KRW 3.1 million (this exemption replaced a previous subsidy program in 2009). In 2012, 35 830 such vehicles were sold, giving a maximum possible support value of KRW 111 billion in that year. Electric vehicles receive tax exemptions of up to KRW 4.2 million per unit (estimated maximum support value of KRW 3 billion in 2012) and compressed natural gas vehicles, of between KRW 16 million and KRW 42 million per unit (no estimated support value available) (advice from DFAT, 28 November 2013).</p> <p>Additionally, the Korean Government has announced a ‘bonus–malus’ system to take effect (if legislated) from 2015. When in place, tax concessions will be provided for low-emission vehicles, while increased tax rates will be levied on high-emission vehicles (Jones and Yoo 2012).</p>
Loans and other financing programs	<p>During the global financial crisis, the Korea Development Bank provided liquidity support to Daewoo (at the time, a subsidiary of GM) and Ssangyong (Stanford 2010).</p>
Input price subsidy	<p>The Korean automotive industry, together with other industries, benefits from low energy prices due to government-regulated prices and major government participation in the sector (advice from DFAT, 21 January 2014).</p>
Rebates to consumers	<p>As of 2013, the Korean Government provides a subsidy of up to KRW 15 million to each buyer of an electric vehicle. Municipal governments may also operate their own rebate schemes for consumers — for example, Seoul provides an additional KRW 15 million subsidy for electric cars, while Jeju Island offers KRW 8.7 million (Sojung 2013).</p>

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Table B.7 (continued)

<i>Policy type</i>	<i>Policy description</i>
Technology standard	<p>Korea has adopted emissions standards for petrol and gas-fuelled vehicles used by the US Government of California (the Non-Methane Organic Gases Fleet Average System), and European Union emissions standards for diesel-fuelled vehicles (KAMA 2013).</p> <p>The Korean Government is progressively introducing combined fuel economy and greenhouse gas emission targets, with car manufacturers to achieve 100 per cent compliance by 2015. Testing of fuel economy is aligned with processes under the Corporate Average Fuel Economy standards used in the United States (An, Earley and Green-Weiskel 2011).</p> <p>As a consequence of the bilateral trade agreement negotiated between Korea and the European Union, a five-year plan for harmonising vehicle safety standards commenced in 2009. Where inconsistency between Korean and European standards remains, Korea will be required not to apply its standards in a way that limits market access (KAMA 2013; Stangarone 2009).</p> <p>Despite the above evidence of international standardisation and harmonisation, reports suggest Korea still has many technical vehicle requirements that are 'just different enough' from international standards to impose an additional burden on imported vehicles, and that have drawn complaints from US and EU automotive industries (advice from DFAT, 28 November 2013).</p>
Government procurement	<p>The Korean Government has established a target for 50 per cent of vehicles purchased for the public fleet to be alternative fuel vehicles (OECD 2012a). The municipal Government of Seoul has committed to replacing all vehicles in its public fleet (including taxis and buses) with either electric or hybrid engine systems by 2020 (Seoul Metropolitan Government 2011).</p>
Other assistance	<p>Regulated automotive insurance premiums are higher for imported car models compared to most domestically produced models. At least in part, this appears to be due to relatively higher repair costs associated with imported cars (including sourcing replacement components). The Korea Insurance Development Institute reported that the average insurance payout in 2012 was around KRW 1 million for a domestically produced vehicle, but nearly KRW3 million for an imported vehicle (KIDI 2013a, 2013b).</p>

B.8 Mexico

Table B.8 **Examples of government assistance to the automotive manufacturing industry in Mexico**

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	<p>Mexico's federal and state governments invest in public research centres that can benefit the automotive sector. For example, the Center for Research and Technical Assistance of the State of Querétaro was built with both federal and state government funding, along with private sector investment. The Center provides facilities for vehicle and component testing, and has contributed to the development of parts and machinery used within the automotive sector (ProMexico 2013).</p>

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Table B.8 (continued)

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	<p>Automotive manufacturers are eligible for capital grants through Mexico's trade and investment agency, ProMexico, for projects that generate economic development (Trani 2012). Small and medium sized enterprises may also be eligible for a share of MXN 350 million in federal funding provided through the National Enterprise Institute, which is intended (among other things) to reduce automotive industry demand for imported components in favour of domestic suppliers (ProMexico 2013).</p> <p>Local and state governments may also provide incentives for manufacturers to locate in their territories. For example, the Querétaro state government offers financial support for worker training and relocation (Government of Querétaro 2013).</p>
Tax concession	<p>Since 2003, the Mexican Government has offered tax concessions to support automotive manufacturing under a federal Automotive Decree. A key benefit of the decree is that a carmaker may import foreign-produced cars duty free, subject to achieving local production targets (ProMexico 2013).</p> <p>The Mexican Government provides general tax incentives for exporting manufacturers, including in the automotive sector. Examples include:</p> <ul style="list-style-type: none"> • Sectoral Promotion Programs, which entitle companies in specified industries (such as vehicle and auto-parts manufacturing) to access preferential tariff rates both for imports (for goods to be used in local production) and exports • the <i>Decree to Promote Manufacturing, Maquila and Export Services Companies</i>, which provides various exemptions or limits on import duties paid by export-oriented companies in producing exports. Additional concessions for corporate income and value added taxes also apply — although tax reforms legislated in 2013 will remove some of these • the High Volume Exporting Companies Registry, which provides exporters (where exports exceed US\$2 million annually, or account for at least 40 per cent of the company's sales) with streamlined tax processes and opportunities to recover import duties paid • the Return of Import Taxes to Exporters program, which refunds eligible exporters for import taxes paid on goods used as inputs into exported goods (EY 2013b; PwC 2013). <p>State governments may also offer additional tax concessions to manufacturers. For example, the Querétaro State Government offers discounted property taxes for eligible companies that create jobs through the construction of new manufacturing facilities (Government of Querétaro 2013).</p>
Loans and other financing programs	<i>None identified.</i>
Input price subsidy	<p>Fuel prices are subsidised, with Pemex (the state-owned oil company) importing petrol and diesel and reselling it domestically at a price set by the Mexican Government each month. Since 2010, the Mexican Government has sought to increase retail prices gradually to reduce overall losses associated with the subsidy (Plante and Jordan 2013).</p>

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Table B.8 (continued)

<i>Policy type</i>	<i>Policy description</i>
Input price subsidy	During 2009, the Mexican Government operated a Job Preservation Program — a scheme to subsidise businesses, including in the automotive industry, to retain workers during the economic downturn. In exchange for agreeing to work shorter hours, workers were compensated by the government for lost earnings (subject to a cap of MXN 5100 per worker). MXN 217 million was provided to workers in the automotive industry (Galhardi 2009; Messenger and Rodríguez 2010).
Rebates to consumers	Between July 2009 and March 2010, the Mexican Government operated a Vehicle Renewal Program — a MXN 500 million scrapping scheme, providing subsidies for consumers who traded in old vehicles (at least ten years old) for new vehicles worth no more than MXN 160 000. To attract the MXN 15 000 rebate, new vehicles had to be manufactured in Mexico or in a country with which Mexico had signed a bilateral trade agreement (Calderón 2009).
Technology standard	Mexico's fuel economy and emissions standards for new vehicles are based on those adopted by the United States, with some variation (SEGOB 2013; UNEP 2012). Mexico also gives consideration to the safety and environmental standards established by the World Forum for the Harmonization of Vehicle Regulations (ProMexico 2013).
Government procurement	<i>None identified.</i>
Other assistance	<p>ProMexico provides non-financial assistance to companies seeking to develop export markets. Under its transactional business accompaniment program, ProMexico assists with connecting Mexican companies to overseas partners — for instance, to integrate Mexican components manufacturers into global supply chains (ProMexico 2013).</p> <p>Under a modified protocol to a bilateral trade agreement, the Brazilian and Mexican Governments will apply export quotas until March 2015 on vehicles traded between the two countries. As part of the protocol, the governments also required manufacturers to increase the proportion of vehicle components sourced locally from 30 to 35 per cent in 2012, and to 40 per cent by 2016 (Ministry of Economy (Mexico) 2012).</p> <p>To improve air quality in Mexico City, local authorities regulate which days cars can be used under a scheme known as <i>Hoy no Circula</i>. Tighter restrictions apply to vehicles that are at least ten years old or exhibit poor environmental standards, while the best rated vehicles are not subject to any usage restrictions (Ministry of Environment (Mexico City) 2013).</p>

B.9 Thailand

Table B.9 **Examples of government assistance to the automotive manufacturing industry in Thailand**

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	<i>None identified.</i>
Excise tax regime	<p>Thailand currently imposes vehicle excise duties based on the size and type of engine. The lowest rates of duty are applied to pick-up vehicles with engine capacity equal to or less than 3250 cc, and the highest rates to any vehicles with engine capacity over 3000 cc.</p> <p>Under a new excise tax structure, to take effect from 1 January 2016, the schedule of duty rates varies by engine size, fuel type and CO₂ emissions, with hybrid vehicles emitting no more than 100 g/km of CO₂ emissions attracting the lowest rates of duty for passenger motor vehicles (PMVs). The new excise tax structure, will reduce the excise duty on eco-cars from 17 per cent to 14 per cent if CO₂ emissions are equal to or less than 100 g/km (BOI 2013; Pramualcharoenkit 2013). However, PMVs with engines over 3000 cc (which are traditionally imported) will still be charged the maximum rate of 50 per cent, regardless of fuel type or CO₂ emission. By contrast, pickup passenger vehicles up to 3250 cc (mostly locally manufactured) will be charged excise duty of no more than 30 per cent and as little as 3 per cent if they are pickup vehicles that emit no more than 200g/km (advice from DFAT, 28 November 2013).</p> <p>The Thai Government's rationale for the excise regime is to support fuel-efficient and alternative-energy vehicles.</p>
Tax concession	<p><i>Producers</i> — Thailand's Board of Investment provides tax incentives for different parts of the Thai automotive industry.</p> <ul style="list-style-type: none"> • Car manufacturers that invest at least THB 15 billion in a facility that will, within five years, produce more than 100 000 units (per year) of a passenger car model can be exempted from corporate income taxes for five years. • Manufacturers participating in Thailand's 'eco-cars' scheme are eligible for: exemption from corporate income taxes for up to eight years, exemption from import duties for machinery and equipment, a 90 per cent reduction in import duties on raw materials and components (where they cannot be produced locally). • Manufacturers of tyres and high-tech vehicle components are also eligible for corporate income tax holidays and import duty exemptions and reductions. • Manufacturers of natural-gas vehicles face reduced import duties for natural-gas fuel tanks and control system components. • Several other specified automotive activities (where they occur outside Bangkok) are eligible for a 50 per cent reduction of corporate incomes taxes for five years, with additional tax deductions allowed for costs associated with transport, utilities, construction, and infrastructure installation (BOI 2013; UNESCAP 2012). <p>Companies are eligible to claim a 200 per cent deduction on their corporate income taxes for eligible R&D expenses (EY 2013a; TAI 2012).</p> <p><i>Consumers</i> — Tax incentives are available to owners of alternative-fuel vehicles, such as reductions in the road tax for vehicles powered (entirely or as a hybrid) by natural gas (IISD 2013). Lower excise taxes are applied to eco-cars than for conventional passenger cars (as mentioned above).</p>

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Table B.9 (continued)

<i>Policy type</i>	<i>Policy description</i>
Loans and other financing programs	The Small and Medium Enterprise Development Bank of Thailand can provide loans, guarantees and other financial service support to small and medium enterprises (such as Thailand's automotive component suppliers). In 2012, the bank signed a Memorandum of Understanding to provide support for initiatives to improve the environmental standards in Thailand's automotive and automotive components manufacturing industries (SME Bank 2012).
Input price subsidy	Compressed natural gas, liquefied petroleum gas, diesel and biofuels are subsidised at different rates, depending on the particular fuel type (IISD 2013).
Rebates to consumers	The Thai Government introduced an excise tax rebate scheme for first car buyers who purchased vehicles between September 2011 and December 2012. Eligibility for the rebate (capped at THB 100 000) was contingent on the vehicle having an engine capacity not exceeding 1,500 cc or being pick-up vehicles manufactured in Thailand, and worth no more than THB 1 million. The excise tax rebate was paid to qualifying owners within one year of purchase, although recipients are required to retain ownership of the vehicle for at least five years (BOI 2011).
Technology standard	Thailand has adopted European Union emissions standards for new vehicles (Srisurapanon and Wanichapun 2001).
Government procurement	<i>None identified.</i>
Other assistance	Import licences are required to import used vehicles and automotive components, and are available only for imports that are intended to be re-exported or used for non-commercial purposes (Marantis 2013). 'Non-tax incentives' are available to foreign vehicle and vehicle parts manufacturers to establish operations in Thailand, including land ownership rights and streamlined procedures to facilitate work permits and visas for employees brought in from abroad (Asawachintachit 2012; BOI 2013).

B.10 United States

Table B.10 **Examples of government assistance to the automotive manufacturing industry in the United States**

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	Various state governments provide investment grants and job training grants to automotive manufacturers. For example: <ul style="list-style-type: none"> • Michigan's business development program provides grants, loans or other economic assistance of up to US\$10 million to businesses that create jobs and/or provide investment. In 2012-13, the program provided grants to a number of automotive design, component and manufacture companies (Michigan Economic Development Corporation 2013) • Kentucky provides matching grants for industry-specific workforce training programs. Grants have been provided to a number of automotive manufacturers and component manufacturers (Kentucky Cabinet for Economic Development 2013)

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Table B.10 (continued)

<i>Policy type</i>	<i>Policy description</i>
Capital subsidy or grant	<ul style="list-style-type: none"> Mississippi provided US\$363 million to Nissan toward the cost of building an assembly plant in Madison County in 2003, followed by US\$7.3 million for infrastructure in 2011 and US\$7.5 million for plant expansion in 2012 (Nave 2012).
Tax concession	<p>The Federal Government provides a tax credit of between US\$600 and US\$1000 against excise tax imposed on the purchase of qualified plug-in electricity vehicles (US Department of Energy 2013b).</p> <p>Various states provide state tax concessions to automotive and automotive component manufacturers, including in relation to property taxes and income taxes. For example:</p> <ul style="list-style-type: none"> Michigan provided a credit against its state business tax to Chrysler in 2010 (valued at US\$1.3 billion over 20 years), and to Ford (valued at US\$909 million over 15 years). These credits were provided to encourage the companies to expand in Michigan over competing states and countries (Michigan Economic Development Corporation 2010). GM received a tax credit valued at US\$1.1 billion in 2008-09 (Michigan Economic Development Corporation 2009) Indiana and Ohio provide job creation and job retention tax credits against various state taxes (including commercial activity tax and corporate income or franchise tax). The credits are performance based and are subject to the creation or retention of jobs. Ford, Chrysler, and GM have received both job creation and job retention tax credits (Indiana Economic Development Corporation 2013b; Ohio Development Services Agency 2012a, 2012b) Indiana provides an alternative fuel vehicle manufacture tax credit of up to 15 per cent of qualified investment in the manufacture of alternative fuel vehicles (Indiana Economic Development Corporation 2013a) Mississippi granted Toyota US\$296 million in tax incentives to build a manufacturing plant near Tupelo (MDA 2010) Georgia provided Kia Motors with US\$76 million in tax credits in 2006 to establish its first US manufacturing plant in that state, as part of a total of US\$410 million in support (Birmingham Business Journal 2006) Kentucky granted Toyota US\$146.5 million in tax incentives to expand its Georgetown manufacturing facility in 2013 (Automotive News 2013), after having committed US\$240 million in incentives to Ford to expand its Louisville plant (City of Louisville 2010).
Loans and other financing programs	<p><i>Automotive Industry Financing Program</i> (part of the Troubled Asset Relief Program). In response to the global financial crisis, in 2008-09 the US Government provided around US\$80 billion in loans and other forms of support (such as the purchase of automotive company stocks and securities) to Chrysler and GM and their respective finance arms. Both Chrysler and GM had filed for bankruptcy protection in 2009, and received the loans to continue operating during company restructuring. As of 31 December 2013, the US Treasury Department had recovered approximately US\$63.2 billion of the funds dispersed through the program (US Department of the Treasury 2014).</p> <ul style="list-style-type: none"> The <i>Automotive Supplier Support Program</i> provided government-backed protection on money owed to automotive suppliers for products shipped to automotive companies participating in the Automotive Industry Financing Program (valued at US\$5 billion) (US Department of the Treasury 2013). Automotive suppliers also permitted to sell their receivable commitments from automotive manufacturers to the Treasury (at a discount) to receive money immediately (US Department of Commerce 2010).

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Table B.10 (continued)

<i>Policy type</i>	<i>Policy description</i>
Loans and other financing programs	<ul style="list-style-type: none"> • The <i>Automotive Warranty Commitment Program</i> provided loans to protect warranties on new vehicles purchased from GM and Chrysler during their restructuring period (valued at US\$1.1 billion) (ILO 2010; US Department of the Treasury 2013). • The <i>Advanced Technology Vehicles Manufacturing Loan Program</i> provided loans to support the development of the manufacture of advanced technology vehicles and associated components in the US — for example, over the period 2009-10, US\$5.9 billion was loaned to Ford, US\$1.45 billion to Nissan and US\$456 million to Tesla (US Department of Energy 2013a).
Input price subsidy	<i>None identified.</i>
Rebates to consumers	<p><i>Consumer Assistance to Recycle and Save</i> (also known as ‘cash for clunkers’). Credit to consumers who trade in old, fuel-inefficient vehicles when buying or leasing new, more fuel-efficient vehicles. The credit was US\$3500 or US\$4500 depending on the type of vehicle purchased and was non-discriminatory, applying equally to the purchase of domestic and foreign vehicles. The program provided support totalling US\$2.85 billion and has now ended (US Department of Transport 2009).</p> <p>Various states provide incentives for the adoption of hybrid and plug-in electric vehicles. State rebates or tax credits range from US\$1000 in Maryland to US\$6000 in Colorado (National Conference of State Legislatures 2013).</p>
Technology standard	Greenhouse gas emissions standards and corporate average fuel economy standards require new cars and light trucks to achieve 35.5 miles per gallon by 2016. In 2011, the US Government announced an agreement with thirteen large automotive producers to increase fuel economy to 54.5 miles per gallon (163 grams per mile of CO ₂) by 2025 (NHTSA 2012; US EPA 2012). From August 2013, US Customs will refuse any consumer products that are noncompliant with US energy conservation standards (GPO 2013).
Government procurement	In 2011, the Federal Government announced that by the end of 2015, all new light duty vehicles leased or purchased by government agencies be alternative fuelled vehicles, such as hybrid or electric, compressed natural gas, or biofuel. Executive fleets are also required to achieved maximum fuel efficiency (The White House Office of the Press Secretary 2011). The policy does not discriminate between US and foreign made vehicles.

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