



THE HON. GREG COMBET MP
Minister for Defence Personnel, Materiel and Science

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DEFENCE INDUSTRY POLICY AND SMES

**Address to the
Australian Industry & Defence Network – ACT**

Canberra

Check against delivery

SPEAKER: The Hon Greg Combet MP

Mr President, Members of AIDN, Ladies and Gentlemen.

Thank you for your kind welcome.

There is probably no greater responsibility of a national government than to provide for the nation's defence and security.

This is a responsibility to which the Rudd Government attaches the highest importance.

And while each portfolio in modern governments deals with issues of enormous complexity – managing the economy, health, education, climate change to name just a few – Defence is in many respects unique in the challenges it presents.

It is unique because it addresses the profoundly sobering political and moral questions relating to the use of force in pursuit of the national good.

In the Defence portfolio, Minister Faulkner and I are constantly treading the fine line between technologically advanced, and expensive, war fighting capabilities and value for money.

It is the duty of the Defence Ministers to ensure that the weapons that are necessary to deter and defeat an adversary are affordable, that the people who handle them are properly trained and led, and that the full resources of the nation can be brought in behind the national defence effort.

And that final thought needs no elaboration in a group such as AIDN.

Defence White Paper 2009

In May this year, the Rudd Government released its White Paper Defending Australia in the Asia Pacific Century: Force 2030.

That was a watershed document, bringing new focus and direction to the national defence effort after the benign neglect and impetuous spending of the Howard years.

As the White Paper noted, the principal task for the ADF is to deter and defeat armed attacks on Australia by conducting military operations without relying on the combat forces of other countries.

This means that the ADF must be able to control our sea and air approaches against credible adversaries to the extent required to safeguard our territory, critical sea lanes, population and infrastructure.

To help ensure these aims force structure decisions have been foreshadowed that will shape and change the future capabilities of the ADF. This includes the acquisition of new submarines, new anti-submarine warfare frigates, new offshore patrol boats, new Joint Strike Fighter aircraft and greater firepower and mobility for land forces.

Defence Capability Plan 2009

In July, the Minister for Defence and I released the new Defence Capability Plan 2009 that gave substance to building the Force 2030 outlined in the White Paper. Of interest to local industry including the large base of SMEs is that expenditure in Australia is forecast to grow with consequent growth in employment in the defence industry sector.

Both Senator Faulkner and I were at pains to ensure that the DCP contained greater levels of transparency and information to help companies make investment decisions. I am pleased to say that feedback from industry on the details included in the DCP has been mostly positive.

We committed to undertaking an independent review of the information we provide on capability planning. This review has begun and is being conducted by two eminent individuals: Mark Thomson and Leigh Purnell. Both have excellent knowledge of defence and industry and will provide some insightful analysis of this issue.

Obviously, we need to protect the Commonwealth's bargaining position, but on the other hand we need to provide as much guidance as we can so that industry can respond appropriately and in a timely fashion.

Nevertheless, I believe that the current DCP presents great opportunities to Australian Industry.

Funding Force 2030 – the Strategic Reform Program

The Government also committed to a funding model that will underpin growth in the defence sector. We will continue the commitment to 3 per cent real growth per annum through to 2017-2018 with 2.2 per cent per annum after that. In addition, we have agreed to 2.5 per cent fixed indexation out to 2030 to provide greater certainty to budget planning.

However, while the Government has committed to this funding increase, I would like to make it quite clear that there will not be any additional money beyond this. Defence will have to live within its budget.

It is evident that if the White Paper outcomes are to be achieved, it will be essential for Defence to improve its planning, accountability and productivity.

Under the Strategic Reform Program, Defence will need to find \$20 billion over the next ten years for re-investment into current and future capability.

Let me emphasise the fact that this is a Strategic Reform Program, not a Strategic Savings Program. We will only achieve our goals if we reform the way we conduct business, not just try to make cuts here or there.

Working with Industry

There is no doubt that achieving the aims of Force 2030, elaborated through the White Paper, Defence Capability Plan and the Strategic Reform Program will require a significant effort – one that the Government is determined to make.

However, we will need your help and will look to work with you all in a broad partnership to achieve these goals.

The Government will be looking to the defence industry SMEs to play a role in helping achieve these Defence aims.

Firstly, it is well recognised that SMEs within the industry provide the innovation we need to help maintain our capability edge. Through innovative research and development SMEs are often front and centre in our efforts to maintain the edge we have over potential adversaries – a key strategic aim.

We will also be looking to the SME sector to find innovative ways to become more efficient.

For example, the Defence Materiel Organisation will need to find efficiencies particularly in the sustainment area, and will be looking to defence companies with their commercial nous to come up with suggestions where productivity improvements can be made and efficiencies that reduce the overall cost of ownership can be implemented.

The Government will introduce incentives in our maintenance contracts to encourage companies to implement ongoing productivity improvements, enhance their long term business opportunities and share the savings.

I thank the role that I am sure you will be playing in these areas. However, as this is a partnership it is also important that the Government plays its part as well.

Therefore I want to also outline some of the things that we have done, and will do to help support you in your efforts.

Supporting Defence Industry

Firstly, and complementing the most significant DCP in the history of the country are a range of measures the Rudd Government has already announced.

They range from the ePortal to AIC plans. One I want highlight in particular is our new initiatives on training, innovation and productivity. Last year when I spoke to you I acknowledged the challenges SMEs have in investing in training and education. As recognition of this, the Government announced a \$61 million skills package. The fourteen initiatives aim to:

- expand the pool of appropriately skilled people from which the defence industry sector can recruit;
- enhance work and career pathways in the defence industry sector; and
- grow defence industry capability and productivity.

The programs range from school gateway programs in New South Wales, South Australia and Western Australia; the development of a Masters of Systems Support Engineering to the \$21 million Defence Industry Innovation Centre.

We have also launched, or in some cases continued many other initiatives which I want to touch on today, but in the context of the direction we are taking with our Defence industry policy.

The New Defence Industry Policy

You will be aware that the Government is developing a new Industry Policy Statement and I don't want to presage what will or won't be included.

However, it is important I highlight what our thinking is on this important area.

Implementation of recommendations in previous industry policy statements has been varied with little or no coordination. I intend to bring greater coordination to these programs where the sum of the parts will be greater than the individual components.

These programs will plug in to different stages across the gamut of the defence capability acquisition and sustainment cycle.

Just to mention some of these initiatives which are underway, there is the Capability and Technology Demonstrator program and the Extension program that operates in the early capability identification end of the acquisition process by helping companies to bridge the gap between ideas and tangible products.

There is the Rapid Prototype Development and Evaluation program that brings together expertise from different companies to quickly solve capability problems particularly in the network centric warfare area.

There is the Defence Materials Technology Centre and other Centres of Excellence that cooperatively develop state-of-the-art materials for defence applications.

There is the Defence Industry Innovation Centre that runs under the Enterprise Connect banner that helps SMEs become more competitive through assistance with developing business plans and providing access to the latest technologies and research.

There are the AIC and Global Supply Chain programs that maximise opportunities for local companies, especially SMEs, to become involved in our acquisition projects and in international supply chains.

There are the Skilling Australia's Defence Industry program and the Industry Skilling Enhancement Package that helps companies train and up-skill their workforces and helps school and tertiary students to align their studies with defence industry careers.

There is the Defence Export Unit that assists companies that are export ready to market themselves and matches Australian companies and their capabilities with identified overseas opportunities.

These programs and many more like them operate to maximise the opportunities for defence industry. But what has been lacking is a central narrative – recognition of why we are doing all this and where we are trying to head.

Foundations of a New Industry Policy

When discussing how the Rudd Government is supporting jobs in the defence industry it is important to begin by discussing the underlying foundations of defence industry policy.

Firstly, the offset policies or mandated local content requirements that were practiced in the past did not lead to a sustainable defence industry. The Government will not be returning to these policies of the past.

Secondly, the fact is that the domestic defence industry is dominated by the large international defence primes – with a substantial base of Australian-owned SMEs usually operating as tier one and two suppliers.

The fact is therefore that industry shaping investment decisions are often taken overseas, and that our defence industry policy must focus on securing these investments, and ensuring that our SMEs are able to prosper through involvement in the international supply chains.

These two foundations will drive our support for local industry.

From these two foundations I see three key themes that are emerging within the development of our new industry policy. These are:

1. A sectoral approach defined by our strategic needs;
2. A focus on global supply chains; and
3. A new approach to defence procurement.

Strategic Sectoral Approach

For the first time Defence has identified those areas of industry which are most important to the ADF and which provide a logical focus for industry investment and targeted industry support measures.

Accordingly when we released the DCP, we also released the list of Priority Industry Capabilities, which are those capabilities that provide strategic advantages to Australia by being available locally. These form a sub-set of the Strategic Industry Capabilities that were identified in the White Paper 2009, and provide guidance to industry on the sorts of capabilities and technologies that we think are important.

The Priority Industry Capabilities (or PICs) are not individual companies, nor are they restricted to the primes. SMEs can and do operate in the PIC areas, and indeed, the PICs themselves will change over time with changes in our strategic environment. That is why we will regularly update the White Paper outlook and the Defence Capability Plan.

The challenge for Government in defence industry policy and PICs in particular will be implementation. Government must match its rhetoric with actions. A good example of this is the ANZAC Anti-Ship Missile Defence Project. Learning from the lessons of troubled past procurements such as the FFG upgrade, we decided to install the ASMD upgrade on one ANZAC ship before installing it on the other seven.

This is a prudent move to reduce risk; however it also places pressure on the supplier of the innovative phased array radar at the heart of the upgrade: CEA Technologies and CEA's supply chain. Phased Array Radar is a Priority Industry Capability, so Government needed to consider the PIC implications when managing this project. That is why significant funding was allocated to manage issues around radar obsolescence, supply chain pressures and skills retention.

I've already highlighted today a range of other initiatives that will help maximise opportunities for industry. These policies will be focused, but not

exclusively, on supporting the growth of defence industry in areas Defence has decided offer Strategic Industry Capabilities.

Global Supply Chains

A second theme I would expect to see in the industry policy is a focus on export through integration into global supply chains. This Government has great confidence in the design and manufacturing skills of Australian defence industry. We therefore seek to actively encourage large international corporations to identify opportunities for Australian industry to bid for work on a competitive basis in the company's global supply chains.

Adopting this policy creates a more competitive Australian industry which is not solely reliant upon local Defence projects while facilitating the transfer of skills from the original equipment manufacturer to Australian industry.

It also means that the Australian company may be able to provide support services and products (for example spares) on a competitive basis, for new capabilities that we are acquiring from overseas. That is, it facilitates the transfer of skills and knowledge from large offshore corporations to Australian companies so that they can compete for opportunities in a global support chain.

The Global Supply Chain initiative, under the Australian Industry Capability program, funds large offshore corporations to identify opportunities for competitive Australian companies in their supply chains and those of their suppliers. The initiative also provides Australian companies with marketing assistance and management and technological training to prepare them for export opportunities.

This initiative will mostly take the form of establishing an Office of Australian Industry Capability (OAIC) similar to the Boeing OAIC.

A DMO review of the operation of this office has found that in the period it has been operating, approximately \$26.5 million worth of contracts with Boeing has been won by Australian industries in competition with US and international suppliers.

The second prime to establish and sign a deed was Raytheon who has established an Australian Industry Development Unit. This Unit has already helped two Australian SMEs win major contracts in Raytheon's supply chain. SMA recently won a \$13 million contract, while Micreo won an \$8 million contract to supply components to Raytheon's ALR67 radar warning receiver on F/A-18's in Australia, the United States and elsewhere.

While these arrangements are only now gaining momentum, reaction from Australian industry and prime contractors has been very favourable. The result is that Australian companies can improve their commercial viability and be better able to manage variations in local demand.

A new approach to defence procurement.

The third theme I would expect to see in the policy statement is around a new approach to defence procurement. This will be driven by the Mortimer Reforms and the Strategic Reform Program.

These reforms envisage a new partnership between defence and industry based on innovative contracting methods and a shared risk-reward model. The use of alliance based contracting and contracting for availability are but two examples of this.

These reforms also envisage an empowered Defence Materiel Organisation being involved earlier in the capability development cycle.

I am keen to see a reform focused and more business-like DMO. I want to see a DMO that is run along commercial lines and critically a DMO that injects commercial realities into acquisition decisions much earlier.

I intend making some further comments on this new approach to defence procurement in the coming weeks.

Conclusion

We want better outcomes for industry and defence, because our national security depends on it.

Both Defence and industry will need to work together to deliver Force 2030, and I look forward to continuing the cooperative relationship that we have developed.

Thank you and I am happy to take questions.

Media contacts:

Rod Hilton (Greg Combet):	02 6277 4771 or 0458 276 619
Defence Media Liaison:	02 6127 1999 or 0408 498 664