
BACKGROUND NOTES ON STRUCTURAL ADJUSTMENT IN AUSTRALIA'S AUTOMOTIVE INDUSTRY

The Transformation of Australia's automotive sector

The Australian automotive industry has undergone a major transformation in recent years — from a highly protected inward looking industry relying almost exclusively on the domestic market, to one increasingly looking to exports to secure its future. While many factors have contributed to this transformation, reductions in the previously very high levels of government support for the industry, and changes to the nature of that support, have clearly played a key role.

Twenty years ago, the industry was protected by nominal tariffs of up to 57.5 per cent; quantitative import restrictions on passenger vehicle imports with a tariff equivalent of over 100 per cent; and local content rules providing similarly high levels of support to local component production. Within this cocoon, five vehicle assemblers, purchasing from a plethora of component suppliers, produced 13 models at low volumes, almost solely for the small domestic market. The industry's productivity and quality performance was poor and industrial disputation rife. However, the 'made-to-measure' nature of the assistance provided by quotas and local content protection greatly diminished the incentives for the industry to address its progressively worsening competitiveness.

The unwinding of this regime began in the mid 1980s, as part of a general push to 'internationalise' and improve the performance of the Australian economy. By the end of the 1980s, quantitative restrictions and local content rules had been removed and the phasing down of tariffs was well underway. While tariffs on passenger vehicles were paused at 15 per cent in 2000, they will be cut to 10 per cent in 2005, with a further cut to 5 per cent in 2010. This latter reduction will align automotive tariffs with the general manufacturing tariff.

Not surprisingly, these reductions in protection have provided significant benefits to consumers in lower prices and greater choice. For example, there are now 250 vehicle models available in Australia, compared to just 70 before the removal of quotas.

The reforms have also contributed to considerable rationalisation in the industry. The number of locally produced passenger vehicle models has fallen from 13 to 5, and the number of significant 'original equipment' and raw material suppliers has more than halved.

This rationalisation has contributed to a large increase in the industry's productivity. For example, the number of vehicles assembled per employee has increased by 50 per cent since 1990. Product quality has also improved markedly. In combination with a much greater focus on innovation and customer service engendered by the more competitive environment, these performance improvements have allowed the industry to offset the impacts of a surge in vehicle imports through strong export growth. Exports now account for more than 30 per cent of production compared to less than 10 per cent a decade ago.

Moreover, while an inevitable consequence of strong productivity growth and stable total output has been a marked decline in employment — down 38 per cent in the 1990s — these reductions have occurred in a reasonably orderly fashion.

The industry's largely successful adjustment to much lower levels of protection has been helped by other elements of the reform program. For instance, the fall in the value of the Australian dollar in the mid-1980s following the floating of the currency, cushioned the effects on the industry of the removal of import restrictions and local content protection. Labour market reforms in the 1990s — especially the introduction of enterprise bargaining — have been instrumental in facilitating the uptake of just-in-time production methods, an essential part of modern automotive manufacture. And, the industry's competitiveness has been improved by reforms that have led to more efficient provision of infrastructure services, such as electricity and transport.

Aspects of the industry's assistance package have also been designed to facilitate orderly transition. Apart from reducing protection gradually to give the industry 'breathing space' to increase its competitiveness, many firms have had access to transitional budgetary support. This support, which is oriented towards encouraging new investment and innovation, will continue until 2015, with more generous levels of funding than were recommended in the Productivity Commission's review (PC, 2002).

The industry still faces some significant challenges. Industrial disputation remains a problem. Production volumes remain low by international standards. As in other countries, large investments are likely to be required to enable automotive producers to meet more stringent environmental standards and to incorporate new technologies into their vehicles. Also, fluctuations in the value of the Australian dollar will obviously impact on the industry's competitiveness in both domestic and export markets.

Nonetheless, and notwithstanding future reductions in tariffs and the eventual cessation of budgetary support, much of the industry is optimistic about the future. The strong performance of the Australian economy has seen the domestic vehicle market grow strongly, a trend expected to continue. And growing recognition internationally of the industry's capabilities, together with prospective trade agreements with countries such as the USA and Thailand, are seen as providing a platform for further export growth.

Such optimism in the face of the prospective removal of the industry's special treatment would have been inconceivable when the reform program began. Moreover, the transformation in the industry has been achieved without the disruption seen in some other highly assisted sectors (such as textiles, clothing and footwear). The measured nature of the reform program — giving the industry both time to adjust and incentives to improve its performance — has clearly contributed to the successful outcome achieved. But wider economic reforms have also been important in enhancing the industry's capacity to compete successfully with lower levels of assistance.

REFERENCE

PC 2002 Inquiry Report No. 25, *Review of Automotive Assistance*, December 2002
(<http://www.pc.gov.au/inquiry/auto/finalreport/auto.pdf>)

**All reports are on the Productivity Commission's website at
www.pc.gov.au**