

Speech by

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and Trade Committee

to

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Defence Forum

at

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Good morning ladies and gentlemen.

I would like to thank the AI Group for the invitation to talk to you this morning on the government's directions in Defence industry policy.

John O'Callaghan rang me some time ago and asked if I would come to speak with a group in the West.

He said words to the effect 'it won't take too much time Mark.

'Just speak to our members about some developments in the defence area'.

He followed that up with an email late last week and I quote.

"The focus of the forum is on the;

- new Defence White Paper – Force 2030;
- Defence Capability Plan 2009, with reference to the recently released Priority Industry Capabilities (PICs);
- \$20 billion Strategic Reform Program (SRP); and
- The Mortimer Review on defence procurement.
- A strong underlying theme is: the opportunities arising for Australian defence industry, especially SMEs, under Force 2030.

It then goes on to say;

- You could say something about the emerging strategic situation, including China's growing military strength and what that means for defence policy makers;
- Federal Government's approach to defence acquisition policy, with an insight into the priority which the government is giving to upgrading substantially the capability of the Australian Defence Force (ADF), including the commitment to construct a new generation of 12 submarines and acquisition of the Joint Strike Fighter (JSF), among other major programs.;
- the commitment to 3 per cent growth in spending on defence over the next decade, as well as the new indexing of spending.
- what the DCP means for Western Australian companies, including sustainment of the new submarines and other surface vessels.
- you also could say a few words about Defence Materiel Organisation (DMO) and how it works with industry.

That's a fairly brief and easy topic and I'll try and do it justice.

Firstly I would like to say I have worked in this area for the past 7 or 8 years.

I'm Chair of the Senate Foreign Affairs, Defence and Trade Committee.

I'm also active in a range of other defence committees of the parliament.

Thinking about it, Senate Committees have a multipurpose role and they are;

1. a political role;
2. an accountability role;
3. an advisory role to government;
4. an enforcement or oversight role; and
5. an inquiry role.

Firstly the political role in Senate committees is particularly evident in the Senate estimates process which occurs 3 or 4 times a year.

It's a forum for Senators to seek information, examine issues, pursue matters, test public accounts, and question government spending.

It's often a combative and inquisitorial role.

Every policy, every decision, every call of government has to be explained, justified and defended 3 or 4 times a year in a public forum.

It's an effective and tough process.

Secondly, in terms of accountability the role of committees is almost that of a public watchdog.

In terms of accounts, spending, procurement items, and the provision of goods and services to the armed forces.

In particular it overlooks a lot of problems with capability acquisitions.

Witness the fiasco of the Seasprite helicopters.

Thirdly as an advisory role to government Senate committees can be almost an alternative source of private information to government.

Chairs necessarily have access to submissions, information, discussions, and confidences concerning issues or problems.

The fourth facet of Senate Committee work goes to an enforcement or oversight role.

In particular I refer to government policy decisions and their implementation and accountability.

Finally, committees have an inquiry role.

This is a more formal process whereby legislation or references can be examined in considerable detail.

In this area of defence I refer to the obvious example of procurement practices within the DMO.

But to get to Johnno's wish list I will need to start with the 2009 Defence White Paper.

The last Defence White Paper was developed almost a decade ago.

That paper preceded the events of 9/11 as well as our engagement in both Iraq and Afghanistan.

It preceded major natural disasters in our neighbourhood as well as the Bali bombings.

The world has changed and so have the challenges we now face as a global community.

Those challenges include terrorism, people smuggling and maritime security.

At its heart the 2009 White Paper outlines Australia's strategic interests over the next two decades.

Broadly they are security of our country, security in our neighbourhood and the ongoing stability of the Asia-Pacific region.

It also articulates our ongoing commitment to playing our part in international security challenges.

I have seen commentary which describes the focus of the paper as a return to the defence of Australia doctrine of the 1980's.

I think this is too simplistic an argument which discounts our ongoing obligations and responsibilities to our region.

Along with the rise of terrorism, there has been a realignment of global and regional power.

To say nothing of the fragile states in our neighbourhood and the fact that we have the third largest maritime jurisdiction in the world.

Our guiding principle should be one of self-reliance.

By that I mean we have the capacity to engage in independent military operations where we have unique interests.

Force 2030 is about looking forward and not to the past.

It's no surprise the future operating environment of the ADF will be shaped by advances in military technology.

As a result the White Paper, along with the Defence Capability Plan, has outlined significant growth in defence procurement.

In fact the government has committed to the replacement of 80 per cent of all major war fighting equipment.

Replacements will occur over the next 10 to 15 years.

The implication for the DMO is that spending will increase from \$4.5 billion to \$5.6 billion per year over the forward estimates.

It's a massive undertaking and a massive investment.

It will see the replacement of our ageing F-111 and F/A-18 fleets with the purchase of up to 100 Joint Strike Fighters.

As well as 12 new submarines to replace the Collins Class fleet.

In delivering Force 2030, we've committed to a 3 per cent real growth in the Defence budget until 2017-18

We've projected a further 2.2 per cent in real growth from 2018-2030.

We've also made changes to the 2.5 per cent indexation.

We'll no longer use the Non-Farm GDP Implicit Price Deflator in calculating price indexation supplementation.

The decision was taken to overcome the substantial fluctuations caused by the global economic crisis.

It's previously been a boon for Defence but no longer provides the stability needed for long term project funding.

Instead indexation will be fixed in line with consumer price inflation agreed between government and the Reserve Bank.

There has been some commentary that increases in defence funding are in fact being deferred.

I think this is an unfair criticism as defence spending is not incremental.

Changing strategic environments do have an impact on spending patterns.

However, the most notable problems stem from delays in capability.
There's also the lumpiness of payment schedules.

Also the next few years will be about consolidating our existing plans and inventory.

As we work towards the acquisition of new generation war fighting equipment.

It's important to note however, Defence funding is not just about increases in spending.

It's also about getting the best bang for our buck.

To that end we have laid out an ambitious savings program.

Over the next ten years Defence will be required to finding savings of \$20 billion to reinvest in military capabilities.

As part of this plan there will be an extension of the efficiency dividend of 1 per cent.

The efficiency dividend will apply to administrative activities for the life of the White Paper.

While the fine detail is yet to be released there are three key elements that will inform decisions;

- improved accountability;
- improved planning; and
- enhanced productivity.

The Minister has broadly outlined areas of reform and they include;

- reforming supply chains and inventory management;
- centralising support to the ADF thereby reducing contractor numbers;
- rebalancing the Defence workforce with a focus on military personnel;
- reducing the costs associated with doing business which is code for cutting travel; and
- implementation of the Mortimer Review will also lead to savings over the forward estimates.

As I have said the cost savings are not all targeted upfront.

They are not linear.

They will be implemented over a ten year period.

In some cases they are dependent on further investment in particular practices or procedures.

So, work on the Strategic Reform Program is well underway.

The Defence Strategic Advisory Board will report to the Minister every month.

The National Security Committee of Cabinet will be briefed twice yearly.

The Defence Audit and Risk Committee will also receive regular updates.

I would now like to turn to the broader issue of the government's approach to acquisition policy.

Much of the policy direction has been informed by the Kinnaird Review of 2003 and more recently, the Mortimer Report.

The Kinnaird Review led to a strengthened two-pass process to support planning and approval of major capital equipment projects.

First pass approval is defined as 'the process that gives Government the opportunity to narrow the alternatives under examination'.

Second pass approval is defined as 'the final milestone in the requirements phase'.

The Mortimer Report looked into the effectiveness of reforms implemented as a result of the Kinnaird Review.

This report released in late 2008 brought about further changes to procurement practices.

Essentially the review found deficiencies in the adequacy of project management resources.

It noted a shortage of skilled staff at the DMO and a need for the organisation to become more commercially focused.

The report made 46 recommendations in five principal areas.

- the need for new capability to be initiated on the basis of long-term defence strategy;
- the need to improve the effectiveness of process in the lead up to government approval;
- the need to continue to improve the acquisition process;
- the need to improve the sustainment requirements, definition and management; and
- the need for cultural change in the DMO.

The recommendations have been accepted by the government.

Although I should note a recommendation that the DMO be made an executive agency was not agreed.

However, we have incorporated the spirit of the recommendation in our thinking.

My colleague, Greg Combet as the Minister responsible is now a member of the National Security Committee of Cabinet.

That puts industry participation at the table in procurement decisions.

The intent of the recommendations are also reflected in the Defence Capability Plan.

I'd like to spend some time on the innovations contained in the latest DCP.

I know this is your 'bible' for key strategic planning information.

Primarily it contains two types of projects.

The first are projects scheduled for first and second pass approval over the next four years.

The second are projects scheduled for first pass approval beyond 2013.

It's the first time a schedule for first pass approvals has been given.

It might be worth noting here, there will be six-monthly updates of the web-based version of the plan.

Importantly there's more information on the split between acquisition and sustainment of a project.

This level of detail surpasses the information available in previous 10 year DCP's.

Our new approach will involve five-yearly White Papers and corresponding updates to the DCP.

The purpose of course is to provide you with more detailed information and with more realistic timeframes.

In turn this will give you the ability to make more informed decisions on your investment.

We've also outlined strategically important industry capabilities that need to continue to be available in Australia.

There are 12 broad categories for Priority Industry Capability or PIC's.

- Electronic Warfare;
- High Frequency and Phased Array Radars;
- 'High end' system and 'system of system' integration;
- Through-life and real time support of mission and safety critical software;
- Anti-tampering capabilities;
- Signature management;
- In-service support of Collins Combat System;
- Acoustics technologies and systems;
- Ship dry docking facilities and common user facilities;
- Selected ballistic munitions and explosives;
- Infantry weapons and remote weapons stations; and
- Combat clothing and personal equipment.

Government intervention or assistance may vary to these industries.

It may include assistance in skills development.

It may also include decisions that ensure there is enough work available to maintain the specific capability.

As I have said, the government's main concern will be to maintain these capabilities in Australia.

However, competitiveness will remain the key to successful tendering.

If an overseas company moved their operation to Australia in a specified PIC area, they'd compete with locally based companies.

Therefore the PIC's policy is not a guarantee of return on investment.

We're not in the business of picking winners.

What it's designed to do is to make sure we have the capability we need when we need it.

So what does this all mean for defence industries in Western Australia?

The DCP shows the electronics and maritime sectors will grow significantly over the next four years.

The maritime sector in particular has an annual growth projection of over 8 per cent over that time.

This will mean increased employment opportunities.

Australia wide its estimated 29,000 people work in defence industries.

The expectation is that figure will increase by 5,000 positions over coming years.

To be competitive we will need to up-skill our workforce to take advantage of the opportunities on offer.

The Government announced last year a \$61 million defence industry skills package.

Of particular interest for Western Australia is the Maritime Industry Schools Pathway Program.

This \$2.4 million initiative will provide high school students with greater awareness of careers in the local defence maritime industry.

Essentially it will provide information on how to shape their studies to pursue such a career.

This will be achieved by developing and delivering a school curriculum for years 9 to 12.

The curriculum will be centred on the maths, science and technical studies students will need.

The skills package also includes \$21.2 million for the Enterprise Connect Defence Industry Innovation Centre.

The Centre, based in Victoria will assist Australian defence sector businesses to respond to the unique challenges they face.

Further support to industry will be provided by Specialist Defence Industry Business Advisers.

These advisors will be located in each major city including Perth and will work one-on-one with local companies.

The aim is to help local business compete against the international defence industry in terms of local and international contracts.

Of course it's all about the contracts.

In this area the continuing support for the ANZAC Frigates will be central to the WA maritime industry.

It will involve work on the ANZAC Anti-Ship Missile Defence Upgrade (ASMD).

This is a comprehensive upgrade of the ANZAC frigates.

It includes the addition of innovative phased array radar technology.

This technology is designed and built by an Australian company, CEA Technologies.

Western Australia is also providing ongoing support to the Collins Class Submarines at the ASC West site at Henderson.

Obviously industry will continue to support key ADF bases such as HMAS Stirling, Campbell Barracks and RAAF Pearce.

As to future opportunities for WA industry they will involve:

- Sea 1000 – The Future Submarine which is projected to commence construction after 2016;
- Sea 1180 – Patrol Boat, Mine Hunter Coastal and Hydrographic Ship Replacement Project, with a timeframe of around 2020; and
- Sea 5000 - The future Frigate program which will be under consideration around 2019.

I understand that WA companies have also expressed an interest in the JSF project.

I know industry has some concerns about the increasing emphasis on military off-the-shelf solutions.

Obviously the government is looking to maximise our defence dollars.

It's true to say our domestic defence industry is dominated by large international primes.

I think with the sole exception of the ASC all Australian based primes have now been absorbed by international companies.

However, Australian-owned Small and Medium Enterprises (SME's) usually operate as tier one and two suppliers.

Let me say, that Australian SME's are developing a growing reputation internationally.

The government is keen to build upon this by promoting your expertise and technological know-how.

We are seeking to build partnerships' with companies to create a more competitive Australian defence industry.

Last month the Minister launched the Defence Industry Innovation Centre.

This is a joint project of DMO and the Department of Innovation, Industry, Science and Research.

Its aim is to assist defence industry and in particular SME's.

Your work with the primes should be considered stepping stones.

As ultimately, prosperity for defence industries will come from increased involvement in international supply chains.

Both Boeing and Raytheon have signed on for the *Australian Industry Capability* deed initiative.

This project involves primes setting up dedicated Australian offices.

The purpose is to encourage Australian SME involvement in any Defence contract with a value of more than \$50 million.

It should also assist SME's in winning supply-chain business and compete in offshore markets.

In conclusion, we have a vibrant SME sector and we want to encourage that innovation and expertise.

Today's defence planning and the capabilities needed are both sophisticated and complex.

We recognise the partnership required between military and industry to match military capability to strategic demands.

We've put the roadmap for sustainable Australian defence industries in place.

The proof of our commitment and the success of our roadmap will be determined by you into the future.

The White Paper and DCP require an expansion in both the capacity and capability of the defence industry sector.

You will need to play your part by taking advantage of all the opportunities that are available.

I would urge you to continue to broaden your horizons and look to exporting your technological expertise.