GERARD WALDRON

Reverse tariffs on Australian manufacturing

I have been retired from ARRB for a few years now and so my knowledge of the heavy vehicle industry isn't up to date, but I think I have spent my time wisely in the related field of RV manufacture, at TRACK.com.au. The insights I will share are that international competitiveness is not only based on, clever design, cost of materials and productive labour, but also relies on taxes and regulation being applied without disadvantage to local manufacturers.

This article is based on a letter I sent to Victorian treasurer, Tim Pallas, some weeks before the recent budget. Subsequently, the budget has demonstrated that my letter had no influence! Nonetheless I will make the case here again, because I believe all Australian manufacturing has some issues in common with RV manufacture, that really need a policy and taxation response.

COVID has given us insights into the fundamentals of internationally competitive manufacturing and as they say, 'you should never waste a crises'. Like many businesses TRACK is enormously grateful for Job Keeper and the State Government reimbursement of Payroll Tax, which helped us through nearly three months of nil production in 2020.

Competitive Taxation

One of the telling insights came to us simply because of the payroll tax reimbursement. TRACK was paying >$1000/unit manufactured, in payroll tax!!!

The second insight came as we were renegotiating our factory lease, when the landlord pointed to the significant increases in land tax and similar charges over the previous five years which would have to be recovered going forward and so our rent has increased by around $400/unit manufactured.

This $1400/unit is based on production levels we hope to exceed in 2021, but in common with many other manufacturers we have supply chain constraints, despite a pleasingly full forward order book, so the net outcome will likely be incrementally lower State Government charges/unit, as we incrementally increase production.

Meanwhile

The recent history of the RV industry in Australia demonstrates why these taxes are so important. Firstly, around 90 per cent of Australian RV production is in Victoria, so state taxes, regulations and lockdowns impacted most Australian-made product.

The RV market until 2015 was roughly 40 per cent Jayco, 40 per cent all other Australian manufacturers and 20 per cent imports including EU, UK, USA and China.

In 2015 Australia signed a free trade agreement with China. By pre-COVID 2020 the market was in thirds, with equal shares from Jayco, all other Australian manufacturers and China. Notable also, the volumes in the 2/3 Australian share were unaltered, but Chinese imports had grown to >10,000/year, so all the growth in the sector had been taken up by imported product!

As the Victorian manufacturing lockdowns were coming to an end in October 2020, the Chinese manufacturers had already been out of lockdown for some months and in the last quarter of 2020 their Australian RV market share rose to >40 per cent.

Significantly Australian manufacturers returned to work with depleted supply chains, parts shortages, and increased lead times, especially on the many Chinese made parts that go into a locally built RV. So even with buoyant sales, ramping up production in response is a 'difficult opportunity'.

While we can easily see the lower production costs of Chinese manufacturing creates a competitive advantage, it is probably less obvious that Australian taxation further enhances the competitiveness of imports, relative to Australian manufactured RVs.

Compared with local manufacturers, generally, importers have a much smaller local footprint and so attract much lower payroll tax and land tax per unit. Indeed, for many, these charges ($1400/unit at TRACK) would be nearer zero. This is a perverse outcome when COVID so recently demonstrated that retaining and reinvigorating Australian manufacturing was critical to our economy and security.

In some cases this is compounded by business structures, where an importer might be an Australian Pty Ltd company, which is wholly owned by the overseas manufacturer. Clearly in addition to its other advantages, it can decide the import (transfer) pricing and ensure any income tax paid is 'modest', in the time-honoured traditions of larger multinationals.

In reality the only tax area where local and imports are on an equal footing, is GST. Local manufacturers would be far more competitive with imports if we raised GST and deleted the abovementioned state taxes. Simple and as difficult as that!

State Regulation

The light trailer industry (up to 4.5t) has not been included in the federal regulatory system that has historically

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applied to cars, trucks, and heavy trailers. It will be included with the introduction of the RVSA on 1 July 2021 with all manufacturers required to be in the system by July 2022. This will substantially level the playing field between those who have always been compliant (or at least tried) and those who haven't, except in those areas where States regulate such as in plumbing, gas and electrical.

The state-regulated aspects, plumbing, gas and electrical are subject to interpretations that vary not only state to state, but also inspector to inspector, within states. Noting again that the majority of our national RV manufacturers are based in Victoria, while the majority of imports come into Queensland and so obtain local approvals under a different regime to the majority of Australian-made RVs.

Examples abound but here's a couple:

Watermark - a classic example

Watermark certifies water plumbing fittings, to performance standards in domestic situations. Watermark is only called up in Victorian and South Australian legislation, but it is only enforced in Victoria for RVs.

In my opinion (and so are the authorities in all states but VIC) that it adds no value to RV customers. What it does do is restrict the RV manufacturer's options for supply of hot water plumbing fittings, to fittings that are not designed for RVs. RVs generally use, lighter and more compact components than those used in houses.

In TRACK's case the enforcement of watermark required significant redesign and added parts cost, that applied to none of our competitors.

So, we were not only immediately disadvantaged in comparison to other Australian manufacturers in our segment, but also the lion's share of imports, which do not land in Victoria!

Gas Ventilation - another specific issue

TRACK sells into the 'serious off-road' market segment. We have interstate competitors, whose RVs are sold into all states including Victoria. The ability to keep dust out of these RVs is a significant customer requirement, but the gas regulations demand permanent ventilation. Despite the market disadvantage, TRACK complies, while competitors close the permanent vents, while the RV is in travel mode. TRACK has asked Energy Safe Vic to approve a similar arrangement for us, but they have emphatically disallowed this strategy. By the way, we agree with the Victorian rules, but the lack of national consistency is costing us business.

Levelling the regulatory playing field, starts with recognition that RV manufacture is a national industry and should be nationally regulated. The easiest option would be to have the Commonwealth include all the relevant parts of Plumbing, Gas and Electrical standards in its RVSA type approval process. As manufacturers we are required to produce and have approved compliant designs and we are then subject to audit — which carries significant penalties for failure and provides for national recall of defective product. This could be a policy decision of national cabinet and I'm sure its principles would be welcome in other national industries.

Australian RV manufacture is a national industry that is subject to serious international competition. It needs to be in an environment of regulation and taxation that levels rather than tilts the playing field against it. With imports growing rapidly there isn't a lot of time to fix this, but it should be fixed for all manufacturing in any case.

Gerard Waldron
Life Member,
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