



**Australian Government**

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**Department of Foreign Affairs and Trade**  
Economic Analytical Unit





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 **Kimberly-Clark** Australia

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## **ECONOMIC ANALYTICAL UNIT**

The Economic Analytical Unit (formerly the East Asia Analytical Unit) is part of the Department of Foreign Affairs and Trade and is responsible for publishing reports analysing major trade and economic issues of relevance to Australia.

The Economic Analytical Unit is staffed with six economists and has produced 39 major reports since its establishment in 1990. Executive Summaries of the reports and information on how to purchase reports are on the Unit's website.

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<b>ACKNOWLEDGEMENTS</b>	<b>iii</b>
<b>ECONOMIC ANALYTICAL UNIT</b>	<b>v</b>
<b>EXECUTIVE SUMMARY</b>	<b>ix</b>
<b>CHAPTER 1 INTRODUCTION</b>	<b>1</b>
<b>CHAPTER 2 THE AUSTRALIA–UNITED STATES FTA</b>	<b>7</b>
A new dynamic	8
The multinationals and the local economy: growing together	12
The multinationals and exports	17
Australian investors in the United States	18
<b>CHAPTER 3 THE MULTINATIONALS’ INTERNATIONAL ENGAGEMENT</b>	<b>19</b>
Roles within global networks	20
Exports becoming more important	26
R&D imperative	31
<b>CHAPTER 4 THE MULTINATIONALS AS BUSINESS PARTNERS</b>	<b>33</b>
Procurement trends	34
Growing significance of outsourcing and centralisation	40
Strengths and weaknesses of the local supply chain	42
Helping local company participation in procurement	47
Facilitating local company exports	51
R&D partnerships	56
E-commerce: becoming increasingly important	57
International project business	60
<b>CHAPTER 5 GOVERNMENT PROGRAMS</b>	<b>63</b>
<b>CHAPTER 6 IMPLICATIONS</b>	<b>69</b>
<b>APPENDIX TABLES</b>	<b>71</b>
<b>REFERENCES</b>	<b>79</b>
<b>ALSO BY THE ECONOMIC ANALYTICAL UNIT</b>	<b>83</b>

**AUSTRALIA AND THE UNITED STATES**  
**TRADE AND THE MULTINATIONALS IN A NEW ERA**

## EXECUTIVE SUMMARY

US multinationals are important actors in the Australian economy, both in their own right and indirectly, through the business and business practices they bring to their local supply networks. They also are an important avenue for the further internationalisation of the Australian economy.

US multinationals in Australia are heavily involved in international trade and are linked into their global corporation networks. The Australia–United States Free Trade Agreement (FTA) is further deepening bilateral linkages, potentially bringing significant long-term benefits to the Australian economy.

Doing business with the multinationals can create substantial opportunities for Australian companies to grow their businesses. Many local companies, including small-to-medium enterprises (SMEs), have already developed successful business with the multinationals. Many have also been able to develop export business through the overseas networks and connections of the multinationals.

The primary focus of this survey-based study is on US multinationals as drivers of Australia's exports. In particular, given their reach and networks, it examines their role in facilitating access to the US and other overseas markets by local companies, including SMEs. The study has a threefold purpose.

First, it sets out to identify the likely implications of the FTA for US multinationals in Australia, as well as for their local suppliers.

Second, it seeks to gain some insights into the extent to which US multinationals in Australia have a significant role within their corporations' global networks, by considering their responsibilities beyond Australia (their 'mandates'); their export activity; and their involvement in research and development (R&D).

Third, it considers the interactions of US multinationals with local business and institutions. In particular, it looks at their procurement patterns and trends; the ways in which the multinationals help local company participation in their procurement and facilitate local company exports; their R&D interactions; and the impacts of e-commerce.

The report presents statistical findings of the survey, and gives significant emphasis to illustrations of the varied organisational arrangements and roles of the multinationals; some of the ways in which the multinationals are responding to developments and trends; and some of the ways they interact with local business. A number of the case studies included are aimed at identifying a range of relationships between the multinationals and local companies, and exploring factors underlying successful partnerships.

Interviews were held with 54 of the largest US multinational operations in Australia, involved across a broad range of industry sectors. These multinationals account for the bulk of US multinational activity in Australia. Interviews were also held with a number of local companies that are successfully supplying or otherwise working with the multinationals. A small number of Australian companies with significant operations in United States were also interviewed.

## **The Free Trade Agreement**

Australian exporters stand to benefit significantly from the FTA. The dynamic gains from the Agreement, brought about by a closer economic partnership, should also yield significant long-term benefits for the Australian economy.

Given their two-way trade with their US affiliates and their being linked more broadly into global networks, the Australian operations of many US multinational corporations are also in a good position to benefit – through both an expanded level of domestic business activity and a stronger export performance.

The membership of many of the parent corporations of the companies interviewed, as well as some of the companies themselves, of coalitions or business associations which came out strongly in support of the Agreement points to anticipated benefits for their operations in Australia.

Over one-quarter of the multinationals surveyed that are involved in export anticipated that the FTA would lead to a significant increase in their overall exports. This probably represents a conservative indicator of longer-term export gains however, as it takes time for multinational corporations to weigh up the full implications of the Agreement, especially where these might point to major investment decisions and/or shifts in regional/global responsibilities of affiliates. (Most interviews were held in August 2004.) The survey response is also unlikely to capture the effects of the harder to measure dynamic productivity gains on the multinationals' export competitiveness.

The boost the FTA will provide to the Australian operations of the multinational corporations will in turn lead to greater business opportunities for their suppliers and other business partners.

The Agreement will enhance Australia's attractiveness as a destination for US investment. Increased investment will, in turn, spur greater linkages and synergies between firms in the two countries, and encourage best practice in both the private and public sectors as the economies integrate further. The Agreement should also serve as an incentive for US investors to use Australia as a base for operations in the Asia Pacific region, particularly South-East Asia.

If FTAs currently under consideration with regional partners – ASEAN, Malaysia, China – come to fruition, US multinational corporations will come to see still more opportunities for their operations in Australia. A number already centre significant activities in Australia, including regional headquarters functions. Companies from other countries in the region, as well as other regions would also see advantages in servicing the region and the United States from operations in Australia.

## **Multinational integration into corporate structures**

Many multinationals play a significant role within their corporations' global networks, with production/sales responsibilities or else a broad-ranging mandate for the provision of services, beyond New Zealand and the South Pacific. Many also have a significant reliance on exports. These findings are encouraging, as they underline the key role these firms play in integrating Australia into the global economy.

The multinationals with production/sales mandates beyond New Zealand and the South Pacific have a range of circumstances. Some operate fairly independently of their headquarters and have a relatively

free hand in exports. Some exercise their demonstrated competitiveness in exporting to the region or beyond. For others, the markets they are able to enter may be more heavily constrained, with their competitiveness relative to other affiliates the key determining factor. In some cases, arrangements may be highly structured, with so-called 'centres of excellence' for different activities scattered around the globe, including in Australia.

Australia is a favoured location for many US multinational corporations for the provision of services functions to affiliates throughout the Asia Pacific region, particularly information technology and accounting services. Many multinationals also are using Australia as an R&D hub, mostly as a global hub or for the Asia Pacific region.

Mandates need not remain static, however. The mandates of a number of the multinationals have changed over the past five years, some enhanced and some reduced. Australian affiliates need continually to demonstrate their relevance if they are to retain or secure wide-ranging responsibilities.

Most of the US multinationals interviewed are involved in export. The companies surveyed include some of Australia's largest exporters. South-East Asia is a major market for three-quarters of the multinationals involved in export, while North Asia is a major market for over half the exporters.

Over the past five years, exports have become more important for most multinationals. Most expect this trend to continue.

Most multinationals also conduct R&D in Australia that results in product sales into overseas markets.

### **Linkages with local companies**

US multinationals generate considerable business activity and employment through their supply networks.

Multinational corporations are tending to global or regional purchasing decisions as they seek to drive down costs and maintain profitability in the face of increasing global competition. Nevertheless, high levels of local procurement have been maintained in the face of this increasing contestability of purchasing decisions. The local affiliates of many multinational corporations have retained reasonable flexibility in their sourcing and see distinct advantages in local sourcing, notably the avoidance of the shipping costs and delays associated with foreign sourcing. Some multinationals also recognise that nurturing local procurement helps build the capabilities and competitiveness of the local supplier base.

Participation in global or regional supply chains brings new considerations into play. Some local companies are succeeding in getting onto the multinationals' lists of preferred suppliers for global or regional procurements and are winning contracts.

A number of the multinationals interviewed have a procurement role within their global corporations extending beyond the immediate region. This can be to local suppliers' advantage, both for supply to the local affiliate operations and for securing exports to affiliates elsewhere.

In part driven by the trend to global purchasing, a number of multinationals have in recent years moved to rationalise and consolidate their supplier lists.

Local outsourcing of services by US multinationals in Australia is widespread and growing. This presents opportunities for Australian service providers.

While the experience of the vast majority of the multinationals is that the capabilities of local businesses have improved over the past five years, the capabilities and competitiveness of businesses in Asia are also improving. Australian companies therefore need to continually sharpen their competitiveness and move up the 'value chain'.

US multinationals have identified a diverse set of ways in which they have helped local company participation in their procurement. More than one-third of the companies interviewed have developed partnerships and long-term relationships with their key suppliers. Other mechanisms have included inviting and facilitating local involvement in tenders; providing technical assistance; challenging suppliers' ways of doing things; sharing information; and helping suppliers streamline their processes and procedures. Such assistance can help suppliers in their other business activities, both here and overseas.

Many multinationals are also introducing local suppliers to their overseas affiliates and in this way are helping them start or increase exporting. Any business secured with overseas affiliates can in turn lead to introductions to other affiliates or third parties in overseas markets. For their part, the multinationals can benefit to the extent that their suppliers stand to derive greater efficiencies and capabilities as a result of a greater scale of operations and exposure to this export trade.

Most multinationals interviewed are undertaking research and development in Australia, both with Australian companies and with research institutions. Companies generally commented favourably on their linkages with local research institutions, including the calibre of their researchers.

The trend to e-commerce is having implications for local suppliers. They will increasingly need to be able to bid for contracts by electronic means, as well as engage in electronic payments systems. Some multinational corporations are tending to procure more regionally or globally, using e-commerce. E-commerce and the Internet also are fast-changing the way the major US engineering, procurement and construction contractors are conducting their global business.

The Government places importance on attracting productive inward investment. There are also a number of government and government-supported programs to help promote partnerships and links between the multinationals and local industry.

### **Australian multinationals**

Most Australian multinationals that have established affiliates in the United States have done so to supply the US market. Many of the largest investors face high transport costs for their inputs and products and need to be close to their suppliers and customers.

## INTRODUCTION

On 1 January 2005 the Australia–United States Free Trade Agreement (FTA) entered into force. It is the most important bilateral economic agreement ever undertaken by Australia.

The dynamic gains from the Agreement, brought about by a closer economic partnership, stand to yield significant long-term benefits for the Australian economy. The United States is Australia's second largest goods and services export market and largest source of imports. But it is in the area of investment that the gains from the Agreement will perhaps be most significant over time. Already the United States supplies nearly thirty per cent of Australia's foreign direct investment stock, more than any other economy. Australia ranks twelfth among destinations for US direct investment abroad. Conversely, the United States is the biggest destination – 46 per cent – for Australia's foreign direct investment, and Australia is the eighth largest foreign owner of US assets.

The Agreement will enhance Australia's attractiveness as a destination for US investment as it puts in place legal guarantees and other measures that provide greater certainty for investors and significantly raises the threshold for government scrutiny of US investments in non-sensitive sectors. Increased investment will, in turn, spur greater linkages and synergies between firms in the two countries, and encourage best practice in both the private and public sectors as the economies integrate further. The Agreement should serve as an incentive for US investors to use Australia as a base for operations in the Asia Pacific region, particularly South-East Asia.

This study considers the role of US multinationals in furthering the internationalisation of the Australian economy, against the backdrop of the FTA. Its primary focus is on US multinationals as drivers of our exports and integration with global markets, including their role in facilitating access by local companies, including small-to-medium enterprises (SMEs), to the US and other overseas markets given their reach and networks.

The study is based on interviews with 54 US multinationals, plus interviews with a number of local companies that are successfully supplying or otherwise working with the multinationals. Interviews have also been held with 11 Australian multinationals with significant operations in the United States (see Appendix Table 1, page 71).

### Australia and globalisation

Australia has been very successful in meeting the challenges of globalisation. It experienced a very strong turnaround in multi-factor productivity in the 1990s, translating into a pick-up in trend GDP growth (OECD, 2001). The economy's strong performance has continued to the present. Key contributory factors have been the rapid uptake of new technologies and increased labour force skills. Successive economic reform and deregulation programs put in place since the early 1980s have laid the foundations for Australia's improved competitiveness. More recently, the Government has comprehensively overhauled Australia's taxation system, reformed labour and capital markets and introduced privatisation into the transport and telecommunications sectors.

Lower trade barriers and other reforms have led Australian firms to upgrade management practices and workplace arrangements. To improve their competitiveness, companies are also increasingly benchmarking their performance against leading global companies, focusing more on their core skill-sets, investing more in technology, and seeking out new export markets (Economic Analytical Unit, 2003).

### **Multinationals already well-integrated into global markets**

Multinational enterprises have played an important role in Australia's economic growth and development. Historically, their activities have been oriented towards production for the local market behind trade barriers, and distribution of imported products. US companies have been no exception.

However, the multinationals have had to adjust to the new economic environment in Australia just as local companies have done. There have also been some significant changes over recent years in the organisation of international commerce. Notable amongst these, multinational corporations have increasingly been pursuing integrated global strategies and have come to take on a more important role in the world economy, with growing intra-firm and intra-industry trade. Increasing international competitive pressures have also been accompanied by significant global consolidation in a number of industries, resulting in large multinational corporations playing an increasingly prominent role (Department of Foreign Affairs and Trade, 2002).

Multinationals operating in Australia have as a result appreciably re-oriented themselves, and contributed significantly to Australia's increasing integration with global markets, in particular Asia Pacific markets. Australian foreign direct investment abroad has also become more important.

The multinationals are therefore very important to Australia's further enmeshment in the global economy, both through their own activities and for their capacity to assist local companies to become further involved in international commerce.<sup>1</sup>

### **Importance of US multinationals**

US businesses account for over one-third of the operating income of all majority-foreign-owned businesses in Australia – almost double the share of the next largest foreign investor, the United Kingdom (Table 1.1). They account for eight per cent of the operating income of all businesses in Australia.

In 2001, there were an estimated 2352 foreign affiliates from 682 parent corporations based in Australia (UNCTAD, 2003). The largest 200 foreign companies dominate, with close to 80 per cent of revenues of all foreign companies being attributable to them. US companies account for close to one-third of both the numbers and revenues of these 200 largest companies.

### **The US companies surveyed**

All US companies in the top 200 foreign companies were approached for interview. Ten other large US multinationals were also approached. Overall, a 74 per cent response rate was obtained. Adding to the significance of the results obtained, the 47 companies in the top 200 surveyed account for

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<sup>1</sup> The extensive benefits of foreign direct investment to Australia are canvassed in Access Economics (2004).

over 80 per cent of the revenues of all US companies in the top 200 (Table 1.1). In total, the 54 companies surveyed had revenues in 2002 in the order of A\$62 billion.<sup>2</sup> The median revenue was over A\$600 million. The global corporations of around 60 per cent of the top 200 companies surveyed are in the Fortune 500.<sup>3</sup>

Almost half (26) of the companies interviewed were from the manufacturing industry.<sup>4</sup> Around one quarter (14) were from the wholesale industry. Five companies were from the property and business services industry, while the remainder were from other industry sectors. Participating companies were particularly well represented in the information technology field (three in property and business services and two in wholesaling)<sup>5</sup> and pharmaceuticals field (four manufacturers and two wholesalers).

Interviews were based around a standardised questionnaire, with almost all interviews being held in person, mostly in August 2004. Interviewees were for the most part chief executives or chief financial officers/procurement managers. Questions broadly ranged over the multinationals' 'mandates' – defined as a company's responsibilities beyond Australia's shores; exports; procurement policies and practices; and research and development (R&D) activities.

Table 1.1

**Large US multinationals – major players in Australia**  
**Operating income and revenues of US and other businesses**

	A\$ billion
<b>Operating income, 2000-01</b>	
All businesses in Australia	1373
Foreign businesses	311
US businesses	110
<b>Revenues, 2002<sup>b</sup></b>	
BRW top 200 foreign companies	245 <sup>a</sup>
US companies in top 200	75
US companies in top 200 surveyed	61

Notes a. Some adjustments made for companies omitted from the BRW list.

b. There are only relatively minor definitional differences between the BRW revenue measure and the ABS operating income measure.

Sources: ABS, *Economic Activity of Foreign Owned Businesses in Australia, 2000-01*, cat. no. 5494.0 (operating income data) and BRW, *The Top 200 Foreign Owned Companies*, Feb 12-18 2004 (revenue data).

<sup>2</sup> As an indicator of the situation and perspectives of the top 200, a small amount of survey bias would result from the fact that the non-participating companies would overall be somewhat less oriented towards international activities than participating ones. In addition, the 10 other large companies in the survey frame were for the most part selected on the basis of an apparent significant involvement in international activities.

<sup>3</sup> Fortune *Global 500*, Jul 21, 2003.

<sup>4</sup> Industry classification is as per BRW, *The Top 200 Foreign Owned Companies*, and is the industry where the major proportion of revenues are derived.

<sup>5</sup> ABS data indicate that the income of majority-owned US information technology businesses exceeds that of Australia-owned information technology businesses. (ABS, *Foreign Ownership Characteristics of Information Technology Businesses*, published in *Australian Economic Indicators*, March 2003, cat. no. 1350.0)

## The Australian multinationals surveyed

All up, 11 Australian companies with significant activities in the United States were interviewed (a 65 per cent response rate). The companies' interests in the United States cover a range of industry sectors – mining, manufacturing and services. While a small number, their US revenues were over A\$16 billion in 2002-03 (Table 1.2). The companies accounted for around one-third of the revenues of all Australian-owned companies' affiliates in the Americas – and towards 40 per cent of the revenues of all affiliates in the United States, both Australian-owned enterprises and foreign-owned Australian resident enterprises.<sup>6</sup>

Table 1.2

### Australian multinationals are major investors in the United States

#### Revenues of Australian companies' US affiliates

	A\$ billion
<b>Revenues from sales of all companies, 2002-03</b>	
Australian-owned companies' foreign affiliates	126
Australian-owned companies' affiliates in the Americas	53 <sup>a</sup>
Foreign-owned companies' affiliates in the Americas	2.2
Australian affiliates in the United States, both Australian-owned enterprises and foreign-owned Australian resident enterprises	42 <sup>a</sup>
<b>Revenues of Australian companies surveyed, 2002-03</b>	
Approximation of revenues of affiliates in the Americas	18.4 <sup>b</sup>
Approximation of revenues of affiliates in the United States	16.5

Notes: a. News Corporation included in statistic – News Corp had US segment revenues of A\$24.2 billion.

b. Bovis Lend Lease, Amcor, BHP Billiton and Rinker Group account for 81 per cent of the total.

Sources: ABS, *Australian Outward Foreign Affiliates Trade, 2002-03, Experimental Results*, cat. no. 5495.0 (revenues of all companies data) and geographic segment data reported in company annual reports (revenues of surveyed companies data).

## Structure of the study

Chapter 2 considers the Australia–United States FTA and its impact on the Australian operations of US multinational corporations as well as on the activities of Australian multinationals in the United States.

US multinationals' international engagement is considered in Chapter 3, from three perspectives: the 'mandates' they hold within their corporations (production/sales, R&D and 'other services' responsibilities beyond Australia); their exports; and their R&D activities. Their mandates and their exports provide some indication of the degree to which the multinationals are integrated into their corporations' regional and global strategies. R&D undertaken in Australia is another key indicator of the importance of Australian operations to the global corporations.

<sup>6</sup> Around 90 per cent if News Corporation, which has recently changed its place of incorporation from Australia to the United States, is excluded.

The interactions between US multinationals, and to a limited extent the US affiliates of Australian multinationals, and local companies and institutions are discussed in Chapter 4. The primary focus is on procurement issues and supplier relationships. Particular attention is paid to the ways in which US multinationals assist local company, including SME, participation in their procurement and facilitate local company exports. Consideration is also given to e-commerce, which is an important and evolving dimension of supplier relationships. Some discussion of international project business is included.

Government programs which serve to promote partnerships and links between the multinationals and local industry are canvassed in Chapter 5.

Some implications are set out in Chapter 6.



## THE AUSTRALIA–UNITED STATES FTA

### KEY POINTS

- The Australia–United States FTA has the potential to deliver significant long-term benefits to the Australian economy.
- Australian exporters of both goods and services stand to gain appreciably from the FTA.
- While the better access provided for Australian exporters is significant, the investment liberalisation measures as well as the dynamic gains the FTA will provide to the Australian economy more broadly are likely to be far more significant for the Australian economy.
- The Australian operations of US multinational corporations stand to benefit on a number of levels, in turn leading to greater business opportunities for their local goods and services suppliers and R&D partners.
- The majority of the US multinationals interviewed are members of coalitions or business associations that have expressed their strong support for the Agreement.
- Over one-quarter of the US multinationals surveyed which are involved in export anticipated that the FTA would lead to a significant increase in their overall exports.
- A number of large Australian investors in the United States are strong supporters of the FTA. While they do not consider tariffs to be a major issue, they see benefits stemming from the greater certainty and protections afforded to investors and investments in the United States.

The Australia–United States FTA will provide a significant boost to the Australian economy. The Australian operations of US multinational corporations and Australian companies with operations in the United States stand to benefit appreciably.

## A NEW DYNAMIC

The Australia–United States FTA, which came into effect on 1 January 2005, represents a landmark deal for Australia.

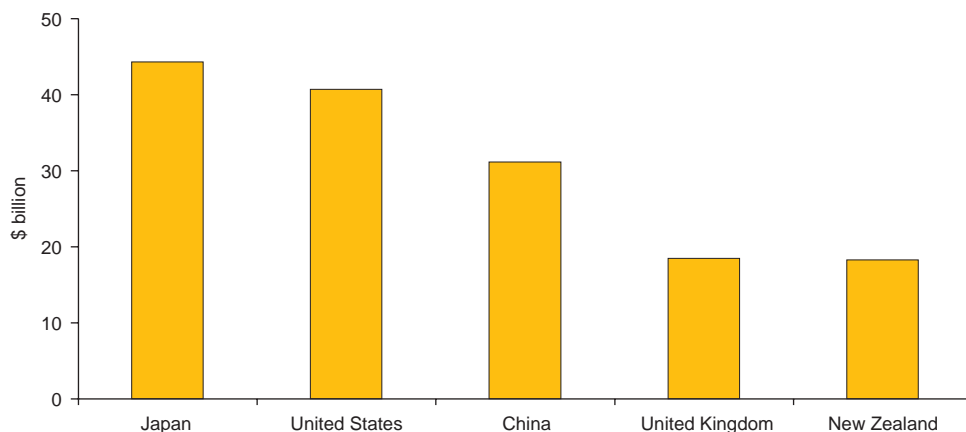
The United States is the world's largest economy, largest importer and largest investor. It is also of key importance to the Australian economy. For the year 2004, the United States ranked a close second to Japan as a trade partner (Figure 2.1). It was Australia's second largest market for goods exports<sup>7</sup>, the largest market for services exports, and the largest source of imports of both goods and services. The United States also ranks as Australia's largest source of direct investment and is by far the most important destination for Australian direct investment abroad (Figures 2.2 and 2.3).

A common language and similar business culture are important factors behind these strong trade and investment ties, and are especially appealing to SME exporters, 19 per cent of which export to the United States.<sup>8</sup>

Figure 2.1

### United States a key trading partner

#### Australia's top five trading partners, 2004



Source: ABS Special Data Service.

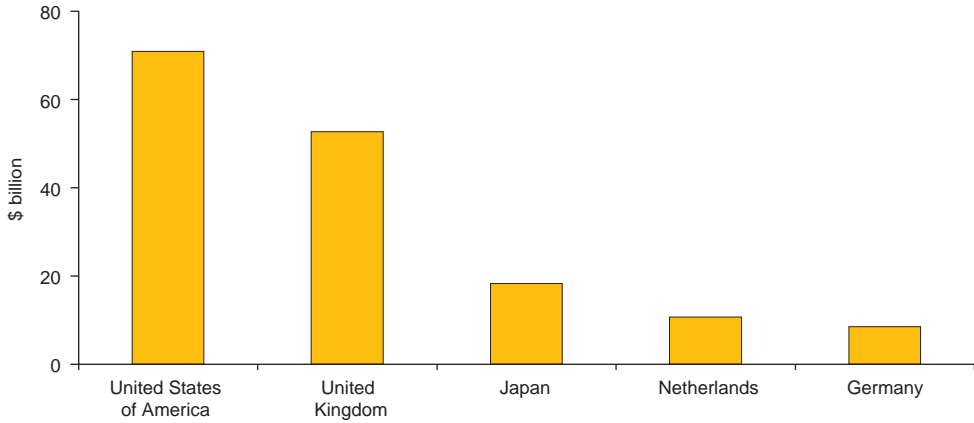
<sup>7</sup> China has since eclipsed the United States as a market for goods.

<sup>8</sup> See BDO Chartered Accountants & Advisers (2005).

Figure 2.2

**Largest direct investor in Australia**

**Australia's top five sources of direct investment, December 2003**

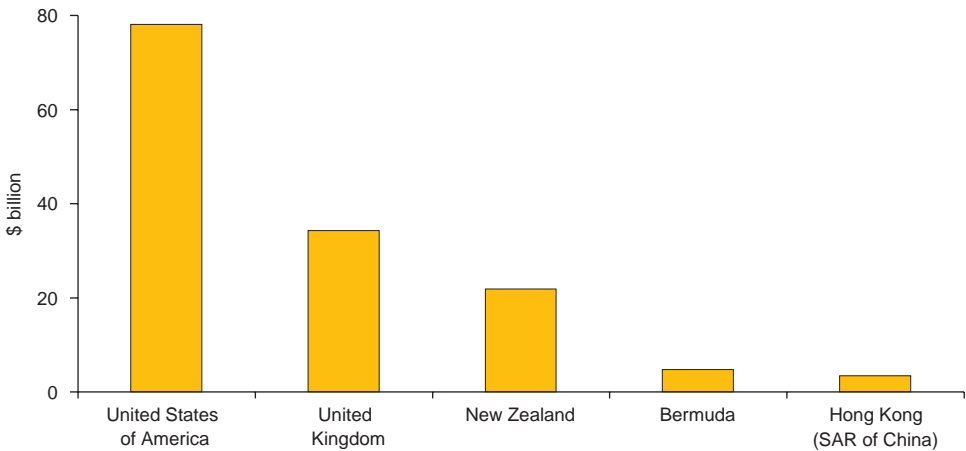


Source: ABS Special Data Service.

Figure 2.3

**Dominant location for Australian direct investment**

**Australia's top five destinations for direct investment, December 2003**



Source: ABS Special Data Service.

Australian exporters stand to gain significantly from the FTA. They have gained immediate, free and open access to the US market for almost all manufactured goods and services. Australian agricultural producers will also enjoy substantially improved access into the US market over time.

Australian service providers in the US market have secured enhanced legal protections that guarantee existing market access and non-discriminatory treatment. Furthermore, the Agreement provides a guarantee against other US preferential agreements as it ensures Australian companies would not be disadvantaged were third-country investors or service providers to secure more liberal treatment in the future. There are also benefits arising from the greater certainty and protection for Australian investors in the United States. Australian goods and services have also gained access to the US government procurement market.

### **THE AUSTRALIA–UNITED STATES FREE TRADE AGREEMENT<sup>9</sup>**

With its entry into force, on 1 January 2005, the FTA is delivering significant new benefits and opportunities for Australian exporters, including:

Elimination of duties on over 97 per cent of US tariff lines for Australia's non-agricultural exports (excluding textiles and clothing);

Improved access for Australian agriculture, with 66 per cent of agricultural tariff lines reduced to zero on day one and a further nine per cent cut to zero within four years;

Full access for the first time for Australian goods and services to the A\$200 billion market for US federal government procurement;

Enhanced legal protections that guarantee market access and non-discriminatory treatment for Australian service providers in the US market, with only limited exceptions; and

Dynamic gains for the Australian economy, including a A\$6 billion boost to annual GDP within a decade as forecast by the Centre for International Economics.

*'The Agreement will provide massive opportunities for Australian companies of all sizes to gain access to the world's largest market... the benefits would be felt in almost every part of our economy, particularly export areas which were vital to Australia's future, including financial and professional services, manufacturing and IT.'* (Hugh Morgan, President of the Business Council of Australia, sourced from Business Council of Australia, 2004b)

While the better access provided for Australian exporters is significant and immediately apparent, the dynamic gains for the Australian economy are more difficult to quantify but are likely to be far more significant over time.

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<sup>9</sup> For extensive documentation on the FTA, see [www.fta.gov.au](http://www.fta.gov.au).

*'Various economists and economic modellers have tried to model the effects of this agreement and they have reached different conclusions. One thing that does not seem to be controversial between them is that they all say, "It is very hard to project the economic effects of an agreement like this because it really depends upon the uptake by Australian and American businesses of the opportunities that the agreement provides." ...'* (comments by Senator Brandis at the Senate Select Committee on the Free Trade Agreement between Australia and the United States, Senate Official Committee Hansard, 2004 [p6])

Dynamic gains will stem from the greater competition that can be expected to ensue with the opening up of the economy to US goods producers and service providers. Increased competition can lead to better use of technology and improved business practices. Production costs will also go down as the costs of business inputs imported from the United States fall, including costs of capital equipment. Likewise, increased foreign direct investment inflows can bring with them new and improved technologies. Companies able to take advantage of greater export opportunities stand to derive greater economies of scale.

*'Trade liberalisation is a critical factor to promoting economic growth and we anticipate that this agreement will facilitate such growth in our two countries and globally...And from the energy sector perspective, we know that energy consumption tracks economic development both as a fuel to growing businesses and to households as the general standard of living increases. With this, yet another benefit of free trade to ChevronTexaco is the opportunity created to produce and sell more energy to fuel the resultant growing economy and its beneficiaries ... In addition, other FTA provisions such as those related to domestic regulation, transparency, local presence, and procurement reinforce existing practices and are all positive for energy services providers.'* (ChevronTexaco submission to Committee On Ways And Means, US House of Representatives, 2004)

Economic analysis undertaken by the Centre for International Economics suggests that a decade after coming into force the FTA will result in an annual boost to the Australian economy of A\$6.1 billion (Centre for International Economics, 2004). The Centre also estimates that the present value of the benefit to the Australian economy exceeds A\$57 billion over the first 20 years of the Agreement. Over 40 000 jobs are estimated to be created and real wages will rise.

The Centre for International Economics has also assessed investment liberalisation, including significant changes to Australia's investment screening<sup>10</sup> and the greater certainty and protection accorded to investors,<sup>11</sup> as likely to make the largest contribution to the overall economic growth and welfare gains arising from the FTA for Australia – ahead of trade liberalisation effects and dynamic productivity gains.

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<sup>10</sup> US investment proposals for acquisitions in non-sensitive sectors are now subject to screening where they involve an investment of A\$800 million or more (up from A\$50 million), while 'greenfields' investments are not screened at all.

<sup>11</sup> Including guarantees on national treatment and prohibition of trade- and investment-distorting performance requirements.

*'The free-trade agreement with the US is an important element of the endeavour to improve our productivity and probably in no area more than investment.'* (Lumsden, 2004)

Some aspects of the FTA which cannot be captured in economic modelling can create their own dynamics. The FTA can, for example, be expected to provide Australia with a better profile in the American market.

*'The [FTA] is a significant step towards providing Australia with the benefits of global economic integration by providing close economic links with the largest economy in the world. The [FTA] will advance Australia's global economic engagement, throughout the twenty-first century. The impact on Australia's economy will be far-ranging, touching most aspects of economic activity and providing dynamic and long-term benefits. Many of the benefits will be immediate, for instance the Agreement has already fostered goodwill between business parties in both countries even before signature...The outcomes on manufacturing, services and investment will create more jobs and increased wealth in the Australian economy. These effects will be on-going and will grow over the long term.'* (Business Council of Australia, 2004a)

The FTA will also lead to enhanced cooperation between the two countries in a range of areas, including customs, mutual recognition of educational and professional qualifications, standards and competition policy. For example, the Agreement establishes a Professional Services Working Group with a specific mandate to investigate ways to promote mutual recognition and other issues relevant to professional services. Further benefits will flow if progress can be made in these areas.

Such benefits could extend to resultant third country involvement. For example, mutual recognition of educational qualifications might be expected to result in additional student numbers from Asian countries as third country student qualifications gained in Australia would also be recognised by the United States. As a result, Australian exports of education services to third countries could increase.

While it did not prove possible to include a chapter on temporary entry in the Agreement, there was recognition by both countries that liberal temporary entry arrangements are important if they are to benefit fully from the commitments contained in the FTA. Following intense efforts by the Australian Government and bipartisan support in the United States, the United States has since created a separate visa category specifically for Australians. This will provide visas for 10 500 Australian business people and professionals, and their spouses, seeking to live and work temporarily in the United States.

## **THE MULTINATIONALS AND THE LOCAL ECONOMY: GROWING TOGETHER**

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The importance of the bilateral investment relationship is underlined by the fact that sales of US affiliates in Australia and of Australian affiliates in the United States are significantly greater than, respectively, US exports to Australia and Australian exports to the United States (Table 2.1).

Table 2.1

**In-country sales larger than exports**

**Affiliate sales as compared with bilateral trade flows**

	A\$billion
<b>Affiliate sales (2002)</b>	
Sales of majority-owned non-bank US affiliates in Australia	112.2
Sales of majority-owned Australian affiliates in the United States	42.4
<b>Bilateral trade (2003-04)</b>	
US exports of goods and services to Australia	26.2
Australian exports of goods and services to the United States	13.9

Sources: US Bureau of Economic Analysis, *Survey of Current Business*, July and August 2004 issues (affiliate sales data) and DFAT, *STARS database* (bilateral trade data).

The Australian operations of many US multinational corporations are in a good position to benefit from the FTA on account of their two-way trade with their US affiliates and their being linked more broadly into global networks.

The Australian operations of US multinational corporations stand to benefit from the FTA on a number of levels. Greater goods and services export opportunities are opening (see further below). Many services sector activities are becoming more attractive to undertake, both for the domestic market and for export.<sup>12</sup> At the same time, they and their customers are benefiting from tariff reductions on the products and production inputs they import from their US affiliates as well as from third parties in the United States. In addition, the dynamic boost the FTA will provide over time to the Australian economy more broadly will lead to higher demand for the multinationals' products and services. In some cases, this higher demand for goods and services could be significant, such as where their key customers secure improved access into the United States. US multinational corporations could also be more inclined to undertake additional investments in Australia.

The FTA can be expected to lead to new investments by some US multinational corporations not presently represented in Australia, and to an expanded presence by other US multinational corporations that have relatively limited operations in Australia at present. Australia should be viewed by some as a more attractive base for operations in the Asia Pacific region, particularly South-East Asia.

*'The MCA [Minerals Council of Australia] supports the recently negotiated Australia / US Free Trade Agreement and considers that it provides an unprecedented opportunity for Australia to achieve closer economic integration with the world largest economy and achieve a significant increase in trade and investment... That the US has concluded an FTA with Australia will enhance Australia's attractiveness as a favourable destination for US investment. Flow on effects to other major trading partners such as China, Japan and India can also be expected to enhance investment opportunities as closer economic and trade relationships are developed with those countries.'* (Minerals Council of Australia, 2004)

<sup>12</sup> In the case of many services sector companies, there is a need to be close to customers so that exports are not an important part of their business.

The boost the FTA will provide to the Australian operations of the multinational corporations will in turn lead to greater business opportunities for their Australian goods and services suppliers and R&D partners. In some instances, the multinationals may also seek to increase their reliance on local suppliers, although most of the US multinationals surveyed are already well-integrated into the Australian economy.

Importantly, the FTA addresses a broad range of issues, in recognition of the strong overlap and interplay between trade in goods, trade in services, the development of e-commerce, government procurement and investment. The FTA goes even further than the WTO in recognising these overlaps, accentuating its relevance to the real world of business. This is a positive for the Australian operations of US multinational corporations in Australia as they seek to enhance their role in global networks, in exporting and in supply networks.

### **Strong US multinational support for an FTA**

The above considerations point to the Australian operations of many US multinationals benefiting significantly from the FTA. Indeed, many of the parent corporations of the companies interviewed, as well as some of the companies themselves, are members of coalitions or business associations that have come out strongly in support of the Agreement.<sup>13</sup> Of the 54 companies interviewed, the parent corporations of 23 are members of the American-Australian Free Trade Agreement Coalition (Appendix Table 2). Many of these are also members of other business groupings supportive of the FTA.

Three parent corporations are members of the Coalition of Service Industries, a leading US business organisation which seeks the reduction of barriers to US services exports.

*'The Coalition of Service Industries (CSI) today announced its strong support for the US–Australia Free Trade Agreement (FTA), noting that the agreement will open up new opportunities for US suppliers in a host of service industries.'* (Coalition of Service Industries, 2004)

Three parent corporations are members of the Business Software Alliance, a member of the International Intellectual Property Alliance.

*'Implementation of the comprehensive obligations in this FTA will strengthen copyright law in Australia, and will also improve the legal tools available there for enforcement of copyright...The beneficiaries of these improvements include creators and consumers of copyrighted works in both countries. This win-win deal will integrate Australia more fully into the global marketplace for copyrighted materials. This is good news for both the Australian and the U.S. economies.'* (International Intellectual Property Alliance, 2004)

The Australian affiliates of seven members of the American–Australian Free Trade Agreement Coalition which were interviewed are also members of the Australia United States Free Trade Agreement Business Group (AUSTA), a coalition of industry groups and companies in Australia established to promote conclusion of a Free Trade Agreement between the two countries.

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<sup>13</sup> While some (post-tax) profits are repatriated, a substantial percentage of US multinationals' profits is reinvested in their Australian operations – in excess of 50 per cent over the five years to 2004 according to unpublished ABS data. Moreover, the bulk of their value added is in the form of wages and salaries paid to their local Australian employees.

*'The [FTA] delivers cutting-edge integration...In both services and investment, AUSFTA provides vital coverage, cutting the cost of doing business, reducing economic distortion and promoting economic prosperity...[The FTA] will make Australia more competitive...(The Agreement) secures Australia's position near the technology frontier, strengthening the Australian economy and to enable it to prosper in the global economy over the next 50 years.'* (AUSTA Business Group, 2004b)

Five of the 54 US multinationals interviewed made individual submissions to the Senate Select Committee on the Free Trade Agreement between Australia and the United States and/or the Joint Standing Committee on Treaties inquiry into the free trade agreement.

Eight multinationals interviewed are members of the Business Council of Australia (itself a member of the Australia United States Free Trade Agreement Business Group). Six are members of the Australian Information Industry Association and a further six are members of Medicines Australia. US companies are a significant force in the Australian information and pharmaceuticals industries, with the companies surveyed being amongst the largest players.

*'The US is the largest ICT [information and communications technology] market in the world, uninhibited access to this market alone would provide the Australian ICT industry significant economic benefits...AIIA and its members support the signing of the FTA with the US.'* (Australian Information Industry Association, 2004)

*'William Sweeney, Jr., [Vice President of government affairs, EDS Corporation], testified (to the US International Trade Commission) that his company's endorsement of the U.S.–Australia FTA reflected the support of virtually every company in every sector of the technology community in the United States.'* (United States International Trade Commission, 2004)

*'The US–Australia Free Trade Agreement has the capacity to attract \$1billion of (pharmaceuticals) research activity to Australia. Medicines Australia said that the greater transparency and improved understanding of the way the Pharmaceutical Benefits Scheme operates, following the FTA, will act as an incentive and provide a greater level of certainty, which underpins investment decisions by the global pharmaceutical industry... We have many advantages in Australia that can make us a major medicinal hub: an excellent medical research infrastructure, high quality clinical research capability, innovative biotech companies and a highly skilled, high-tech, knowledge based workforce. The FTA is a vital catalyst that synthesises these ingredients into greater investment, the creation of skilled jobs, an increase in exports and the development of life saving medicines for Australia.'* (Medicines Australia, 2004)

Seven companies that are not members of the American–Australian Free Trade Agreement Coalition are members of Medicines Australia, the Australian Information Industry Association, or else made individual submissions in support of the FTA.

*'Alcoa has been Australia's leading producer of aluminium since 1963 and has driven the development of Australia's aluminium industry. Australia's exports to the US have been crucial to the growth and development of the aluminium industry... The FTA should underpin future prosperity by promoting greater economic integration and investment between Australia and the US... the FTA would result in benefits as companies such as Alcoa, with a strong base in both Australia and the US were able to serve expanding global markets.'* (Wayne Osborn, CEO Alcoa, sourced from AUSTA, 2004a)

*'By eliminating tariffs on US manufactured goods a free trade agreement between Australia and the United States enhances Caterpillar's competitiveness and strengthens the company's ability to serve Australian dealers and customers. In addition to US manufacturers, other big FTA winners will be consumers in both countries who will gain duty-free access to a wide range of products.'* (Bill Lane, Director of the Washington office of Caterpillar, Inc, sourced from Office of the United States Trade Representative, 2004)

There is clearly strong support in the business communities in both Australia and the United States for the FTA.

It can of course take time for multinational corporations to weigh up the full implications of the Agreement, especially where major investment decisions and/or shifts in regional/global responsibilities of affiliates might be involved. Nevertheless, some multinationals interviewed indicated they had already devised business strategies to take advantage of the openings arising from the FTA. Others may have since moved to develop business strategies.<sup>14</sup> Still others may in time come to identify as yet unforeseen opportunities for wealth creation, including for their supply chains and other stakeholders.

### **Third country investors in Australia**

The FTA can be expected to result in new investments by multinational corporations from third countries. For example, Toyota is reported to be planning to concentrate its manufacturing in those countries party to bilateral free trade agreements.<sup>15</sup> The Australian economy also stands to benefit from an increased attractiveness to investment by third country investors not presently established in Australia.

The generally liberal 'rules of origin' applying under the Agreement benefit non-US investors in Australian manufacturing and local Australian manufacturers alike. In the services sector also, non-US investors have gained enhanced legal protections in view of the liberal 'rules of origin' applying to a service supplier under the Agreement. Similarly, non-US investors in Australia contemplating investments in the United States via their Australian affiliates will be subject to the same investor protection provisions as local Australian companies. In sum, the Australian affiliates of third country investors stand to benefit from the FTA. Foreign investments that might otherwise not take place could also be expected to come to Australia.

The attractiveness of Australia to US investors to service the region would be further magnified if an ASEAN–Australia New Zealand, an Australia–China FTA or an Australia–Malaysia FTA were to come to fruition. Likewise, third country investors would view Australia still more favourably should these FTAs be realised, including as a springboard to service the US market. Arguably, the foundation the Australia–United States FTA provides for a far stronger economic partnership between the two countries makes Australia a more attractive partner for the negotiation of these further FTAs. The United States is after all the largest and most dynamic economy in the world.

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<sup>14</sup> While negotiations on the FTA were finalised in early 2004, the enabling legislation for the agreement was not passed by the Australian Parliament until August, the time at which most of the interviews were undertaken. The final arrangements to allow the Australia–United States Free Trade Agreement to enter into force, on schedule, on 1 January 2005, were completed only in November 2004.

<sup>15</sup> *Australian Financial Review*, 'Free-trade deals can build on car success', 15 July 2004.

## THE MULTATIONALS AND EXPORTS

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The Australian operations of US multinational corporations can expect to secure increased opportunities both within the domestic market, including benefits from the boost the FTA will provide to the local economy more broadly, as well as in export markets. In the process, they will generate more business for their suppliers.

Increased exports by multinationals could be directed to the United States as its tariffs are reduced and eliminated and as better access to the government procurement market and for service providers is afforded. Increased exports could also flow to other countries to the extent that Australia was viewed as a more attractive base for regional operations. Services exports to other countries could also increase in response to the services liberalisation in the FTA, such as in the area of mutual recognition of qualifications.

Over one-quarter of the multinationals surveyed that are involved in export anticipated that the FTA would lead to a significant increase in their overall exports. This is broadly comparable with other survey results. According to the November 2004 survey of exporters undertaken by DHL in conjunction with Austrade, 25 per cent of exporters believed the FTA would have a 'positive' impact on their business (DHL, 2004). Also, 14 per cent of current exporters to the United States believed the FTA would have a 'very positive' impact on their business, up from eight per cent on the May 2004 result, suggesting a groundswell of support for the FTA as companies consider more fully its implications and the opportunities it presents.

The automotive sector is one area where exports are expected to grow significantly, and Holden in particular has been very supportive of the Agreement.

*'In Holden's view, the agreement will strengthen the already significant automotive trade between the US and Australia and provides increased opportunities for both countries to import and export vehicles, engines and components. The flow-on effects from stronger economic growth should benefit the entire automotive industry and drive competition in the marketplace. The agreement will foster closer business relations with the United States and will provide the best possible opportunities for Australian carmakers and component manufacturers seeking to export to the United States. In particular, the agreement will provide flexibility for our business, as opportunities exist for two-way trade in vehicles and components. In addition, opportunities exist for Australian component manufacturers. Several Australian component suppliers have already found niche opportunities in the US and these opportunities may magnify considerably under this agreement.'* (Holden, 2004)

The FTA should also benefit Australia's pharmaceuticals exports. The improved operating environment should also be conducive to increased investment and R&D expenditure being undertaken in the sector. The Australian operations of companies involved in meat and wine exports to the United States also stand to benefit over time as improved access arrangements are phased in.

*'AMH [Australia Meat Holdings] is strongly supportive of the outcomes achieved by the Australian US Free Trade negotiators for beef. The result delivers increased market access resulting in free trade.'* (Australia Meat Holdings, 2004)

*'As the fastest growing export market for Australian wine, the importance of an FTA that achieves the elimination of tariffs, albeit in the medium term, for Australian wine in the United States is clear. The Winemaker's Federation of Australia has costed this tariff elimination at around \$20-25 million in 2015. Importantly, as a global wine company, we recognise that it is important to maintain parity with our major competitors on the United States market, who already have signed preferential trade agreements with the United States in the case of Chile and South Africa, or who are in negotiations (Argentina and the European Union). More significantly, the benefit of signing the FTA will allow a springboard to further reduce barriers to Australian wine trade, in particular those concerning differences in labelling requirements between the two countries.'* (Constellation Wines, 2004)

## **AUSTRALIAN INVESTORS IN THE UNITED STATES**

A number of Australia's major companies that invest in the United States, being members of the Australia United States Free Trade Agreement Business Group, are strong supporters of the FTA. More than half of the Australian companies surveyed are – or their US businesses are – members of the American–Australian Free Trade Agreement Coalition (Appendix Table 2).

*'An FTA that promotes business between the two countries would increase interest of Australian investors in the U.S. marketplace.'* (American–Australian Free Trade Agreement Coalition, 2003)

Many companies would see benefits stemming from the greater certainty and protections afforded to investors and investments in the United States, notably through the national treatment provisions of the Agreement.

Some investors also stand to gain through improved access to the US government procurement market. For example, ResMed, a NSW-based manufacturer with a significant investment position in the United States which specialises in products for the diagnosis and treatment of sleep disordered breathing, now has scope to further extend its business in the United States.

*'This Agreement is fundamentally and hugely important for Australia. It will make things just so much easier for companies like us.'* (Peter Farrell, Executive Chairman, Resmed, sourced from Department of Foreign Affairs and Trade, 2004)

By contrast, tariff barriers are generally not an issue for Australia's large investors in the United States. Their products tend to be manufactured for local markets rather than exported to Australia. The products of companies such as Amcor, Rinker Group, Boral and Bovis Lend Lease are bulky and heavy and so not readily transported, while for the same reason factor inputs can for the most part be sourced more cheaply locally.<sup>16</sup>

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<sup>16</sup> In 2002, goods imports from Australia by non-bank US affiliates of Australian multinational corporations were valued at just US\$150 million out of total sales of US\$22.6 billion (US Bureau of Economic Analysis, *Survey of Current Business*, August 2004).

## THE MULTINATIONALS' INTERNATIONAL ENGAGEMENT

### KEY POINTS

- Australia is being drawn more into the integrated regional and global production strategies of the US multinational corporations.
- Over 40 per cent of the multinationals interviewed have a significant role within their corporation's global network, whether by way of a production/sales mandate, a broad-ranging R&D mandate or an 'other services' mandate at the regional or global level. Many of the multinationals have multiple mandates and the majority have a significant regional headquarters role.
- Australia is a favoured location for many US multinational corporations for the provision of services functions to affiliates throughout the Asia Pacific region, particularly information technology and accounting services.
- US multinationals are major contributors to Australia's overall export effort. In 2002-03, US companies contributed 12 per cent of Australia's total exports of goods and services.
- Over 70 per cent of the US multinationals surveyed are involved in export. Exports are an important source of income for some 40 per cent of these multinationals.
- Exports have become more important over the past five years for more than half the multinationals surveyed that are involved in exporting. A similar number expect exports to become increasingly important over the coming five years.
- US companies account for over one-half of the R&D of all foreign-owned businesses in Australia. This R&D in most instances helps bring about product sales into overseas markets.

Historically, most foreign multinational activity in Australia has been oriented to production purely for the Australian market or the Oceania region, or else the distribution of imported goods and services. In the manufacturing sector in particular, high trade barriers have in the past motivated much foreign investment activity. Despite the major opening up of the Australian economy over the past couple of decades, and the increasing tendency to the organisation of multinational activity on a regional or global basis, concerns persist as to whether multinationals in Australia are integrated into their parent corporations' regional and global strategies (see Nicholas et al, 2003).

The current study provides some insights into the degree of integration of the largest US multinationals with their corporations' regional and global strategies from three perspectives: their responsibilities within the global corporation beyond Australia's shores (their 'mandates'), their reliance on exports,<sup>17</sup> and their involvement in R&D activities.

## **ROLES WITHIN GLOBAL NETWORKS**

Virtually all the multinationals interviewed reported a mandate of one type or another – a production/sales mandate, an R&D mandate and/or an 'other services' mandate. In a number of cases, however, production/sales mandates do not extend beyond New Zealand and the South Pacific. Similarly, a number of companies with R&D or other services mandates do not have a breadth of responsibilities indicative of a high degree of integration.

Nevertheless, over 40 per cent of the multinationals interviewed have a significant role within their corporation's global networks, whether it be a significant production/sales mandate or a broad-ranging R&D or other services mandate at the regional or global level.

This finding is encouraging, and is broadly comparable to the percentage of the multinationals which have a significant reliance on exports (more than 10 per cent of total revenues). (Exports are considered in more detail in the following section.)

### **Production/sales mandates**

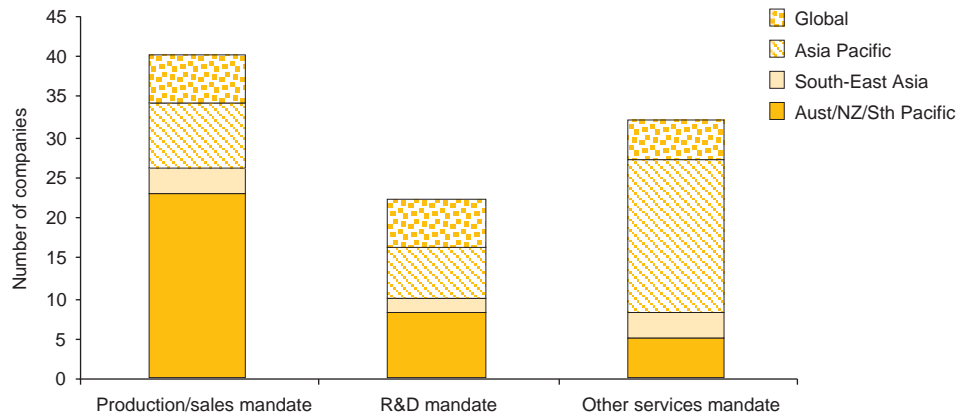
Seventeen of the multinationals interviewed – around one-third – have production/sales responsibilities that extend beyond New Zealand and the South Pacific (Figure 3.1).

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<sup>17</sup> No attempt is made however to distinguish between intra-company exports and exports to third parties. Vertically integrated companies would exhibit high levels of intra-company trade.

Figure 3.1

**US multinationals in Australia: wide-ranging responsibilities**  
**Respondent company mandates**



Source: Survey results.

The nature of companies' production/sales mandates varies. In some instances Australian affiliates face few constraints in their export activities, at least in South-East Asia or the Asia Pacific region. This is more likely where they do not compete with other affiliates, because of clearly differentiated goods and services or because of a clear competitive advantage in supplying to the region. For example:

*An interviewee from a manufacturing company with responsibility for the Asia Pacific region said their business operated relatively independently of headquarters. They had maintained their own brands, strategy and R&D. Their headquarters got involved in matters such as planning, budget and investment approval.*

*Another manufacturing company interviewee said they were the lowest cost sourcing option for supplying Asian markets and in this sense they had a 'mandate'.*

In other instances, the markets that a multinational is allowed to enter may be more heavily constrained, with its competitiveness vis a vis other affiliates the key determining factor. Its ongoing supply into those markets will be subject to its continuing ability to maintain a competitive edge.

In some cases, arrangements may be highly structured, with so-called 'centres of excellence' for different activities scattered around the globe, including in Australia. Such affiliates will tend to be highly integrated into their corporations' global activities.

*Heinz Wattie's has what are recognised within the Heinz corporation as 'Centres of Manufacturing Excellence', adopting world's best practice, for two of its major product lines. Its Echuca site is dedicated to making baby food for Australia, New Zealand and export markets. Its Wagga Wagga plant produces canned meats, with 50 per cent of production exported to over 20 countries.*

## R&D mandates

Reflecting Australia's extensive research capabilities and very good R&D infrastructure, 22 (40 per cent) of the companies interviewed are using Australia as a research hub. In two-thirds of the companies this mandate is global or for the Asia Pacific region or South-East Asia. This is suggestive of a significant degree of integration into their parents' global R&D networks, at least in certain fields of activity.

Some examples of R&D mandates include Alcoa World Alumina Australia, which undertakes R&D on alumina refining technologies on behalf of all Alcoa Inc's operations (see case study). Australia is a global centre for software development within Honeywell. Arnott's is the Asia Pacific regional R&D centre for The Campbell Soup Company.

A number of the pharmaceuticals companies play an important role in R&D within their global corporations, and for some their importance has increased in recent years. Notably, Eli Lilly Australia's R&D role within the global corporation has expanded significantly (see case study). Holden also has an active and growing R&D role within General Motors (see case study).

## Other services mandates

Thirty two (60 per cent) of the multinationals interviewed have an 'other services' mandate. Twenty seven (50 per cent) of the companies interviewed have a mandate that extends beyond New Zealand and the South Pacific, mostly for the Asia Pacific region. In the case of the services sector, seven companies have a broad-ranging regional or global services mandate demonstrating a significant degree of integration within their corporations' global networks.

Reflecting Australian capabilities, a number of companies handle a range of IT functions for affiliates across the Asia Pacific region. Several also provide accounting services for the Asia Pacific region.

*IBM Australia, for example, has an Australian Programming Centre which develops and supports software for IBM mainframe computers around the world; a Computer Processing Centre which forms part of IBM's Asia Pacific data processing centre, servicing IBM's computer processing needs, and those of many large customers, for the countries of the region; an Asia Pacific Regional Accounting Centre which provides ledger accounting services to five countries in the region; a Queensland Call Centre, which provides services to Australia, New Zealand and Japan; and a Multimedia Centre, which has a regional headquarters role for new media. (see [www-8.ibm.com/ibm/au/exportsi.html](http://www-8.ibm.com/ibm/au/exportsi.html))*

Eight companies have a procurement role which extends beyond the immediate region. Such a role can often enable local suppliers to obtain offshore business that might otherwise not be possible (see Chapter 4).

## ALCOA: INVESTING IN PEOPLE AND R&D

Alcoa has been mining bauxite, refining alumina and smelting aluminium in Australia for over 40 years. Its operations include bauxite mines and alumina refineries in Western Australia, aluminium smelters in Victoria, and aluminium rolling mills in Victoria and New South Wales.

Alcoa is a major Australian exporter and employer. Alcoa exported over A\$2.5 billion of product in 2003. Almost 8 million tonnes of alumina is produced by Alcoa each year, accounting for almost half of Australia's total production and 15 per cent of world demand. Alcoa's operations support around 6500 direct jobs and an additional 20 000 indirect jobs, predominantly in regional Australia.

The overwhelming proportion (about 80 per cent) of the A\$1.3 billion Alcoa spent on materials and services in 2003 was spent in Australia. Alcoa works to create opportunities and build skills and expertise among its local suppliers opening up potential for them to compete successfully in global markets.

Research and development is a key priority for Alcoa. Last year, Alcoa invested more than A\$23 million on R&D in Australia. Alcoa's global alumina refining research centre is based in WA and employs 75 staff. The centre has supported Alcoa's WA refineries to become among the most efficient producers in the world.

Alcoa supports research partnerships with government, education and research institutions. Alcoa is contributing more than A\$5.5 million over 7 years to the Co-operative Research Centre for Sustainable Resource Processing. Alcoa also leads the world in mine site rehabilitation research and was the first mining company to successfully return the botanical diversity to its rehabilitated areas.

In addition to R&D, Alcoa invests in the skills of employees and young people. Each year, Alcoa spends more than A\$7 million on apprenticeship and training programs for young people. Alcoa has trained more than 1000 apprentices in Australia. More than 23 000 young people directly benefit from Alcoa's community learning programs each year.

Alcoa is investing to expand its operations in Australia. The company currently has under way a A\$440 million upgrade of its Pinjarra refinery and is seeking approval for a A\$1.5 billion expansion of its Wagerup refinery. The projects have the potential to boost Australia's exports by A\$21 billion and generate thousands of jobs.

An R&D and/or 'other services' mandate is broadly similar to the definition of a regional headquarters (RHQ). The survey findings bear out the expectation that RHQs feature more prominently amongst the larger multinationals than amongst the broader population of multinationals in Australia – three-quarters of the multinationals interviewed have a RHQ role.<sup>18</sup> Sixty per cent of the companies have an RHQ role that extends beyond New Zealand and the South Pacific.

<sup>18</sup> Invest Australia has estimated that there were 848 RHQs or regional operating centres in Australia in 2001-02 (out of some 2350 foreign affiliates in Australia), with 37 per cent of these being US companies.

### **ELI LILLY AUSTRALIA PTY LIMITED: A LEADER IN AUSTRALIAN R&D**

Eli Lilly and Company is one of the world's leading research-driven pharmaceutical companies, bringing to market some of the world's best-known medicines, such as Prozac for depression and Zyprexa for schizophrenia.

The research strength of Eli Lilly and Company is mirrored by the Australian subsidiary, Eli Lilly Australia (ELA). ELA invested approximately A\$44 million in R&D in the 2003-04 financial year, representing 12.5 per cent of sales turnover.

The Commonwealth's Pharmaceutical Industry Investment Program (PIIP) has fuelled this impressive R&D investment. This five year program, which ended in June 2004, facilitated ELA establishment of the Clinical Outcomes and Research Institute (CORI) and the Global Clinical Data Management centre (GCDM), while significantly expanding its traditional clinical trial activity. The successor to PIIP, the Pharmaceutical Partnerships Program (P3), aims to further increase R&D growth.

CORI was established as a regional centre of excellence to provide solutions for an unmet need - namely capability for the design, development, management and analysis of clinical trial data for Australia and the Asia Pacific region. Since its opening in February 2000, the scope of CORI continues to grow, with CORI now supporting the development and analysis of clinical trial activity in Australia, Asia, Africa, Eastern Europe, Middle East, Latin America and Canada.

GCDM provides data management capabilities for trials throughout the world. This group works very closely with the CORI team, particularly in the development and application of new technologies to support this key area of ELA's business. Significantly, GCDM is one of only three regional centres within Eli Lilly and Company managing Lilly clinical trial data worldwide.

ELA has also expanded its R&D activity in basic drug discovery via collaborations and partnerships with local biotechnology companies. One example is a collaboration between Lilly Research Laboratories, Indianapolis, and Acrux Ltd, a Melbourne biotechnology company, to develop drug delivery technology. Such activities are a clear recognition by ELA and Lilly headquarters of the value of Australian biotechnology, and the opportunities that exist for establishing global win-win collaborations.

In addition to biotechnology companies, ELA has sought to establish local collaborations with Australia's leading medical research institutes, exporting the innovation and expertise throughout the world. The Lilly Melbourne Academic Psychiatry consortium (known as Lilly MAP) showcases such collaboration. This was established in 2002 as a multidisciplinary collaboration between ELA and the University of Melbourne Department of Psychiatry, the Mental Health Research Institute and the Alfred Psychiatric Research Centre.

### **HOLDEN: CARVING OUT A GROWING GLOBAL ROLE**

The automotive marketplace is today both highly competitive and globally focused. Holden continues to maintain its competitive edge and works closely with its best performing suppliers to develop new opportunities.

Holden has won access for large rear-wheel drive vehicles to a range of export markets as part of General Motors' plans, based on its ability to supply the product competitively. Holden now sends its vehicles to the United States, Middle East, United Kingdom, South Africa, Brazil and across the Asia Pacific region under General Motors brands including Chevrolet, Pontiac and Vauxhall. Most recently, exports to the Republic of Korea and China are due to commence in 2005.

Holden is one of Australia's leading exporters of automotive products and services. In 2003, it exported 36 000 vehicles and 137 000 engines and earned a total of A\$1.24 billion including vehicles, engines and components. In 2004 Holden celebrated its 50th anniversary export year and set a new all-time vehicle export record for the company, breaking through the 50 000-vehicle barrier. It is hoped that engine exports will be buoyed by sales of its V6 engines produced at its Global V6 engine plant, which was commissioned in November 2003 as the second GM facility producing these engines.

Holden has one of a small number of GM R&D Centres worldwide, and provides engineering and design services for GM operations in the Asia Pacific region.

Holden Innovation has recently been established to undertake collaborative work with its parent on future automotive technologies, and works with local institutions such as CSIRO and Monash University. For example, Monash University Accident Research Centre has recently expanded its road safety research program for Holden into the Middle East (separate case study refers).

### **Mandates can expand or contract**

Local affiliate mandates are not static. In a competitive and fluid operating environment, global corporations restructure and rationalise in the constant pursuit of competitive advantage. The mandates of one-third of the companies interviewed have changed over the past five years. The challenge for Australia is to maintain, and if possible further enhance, their importance within their corporations. Australia's sound economic fundamentals and improved competitiveness make the task easier. The communications revolution and lower transport costs diminish the significance of geographic location. Lower trade barriers in the region and, more importantly, Australia's FTA arrangements – with New Zealand, the United States, Thailand and Singapore and potentially also with Malaysia, ASEAN and China – also make Australia a more attractive base for regional operations.

Holden is one company that is now playing a more significant role within its global corporation compared with five years ago.

Bechtel is another. It moved its Mining & Metals business unit headquarters to the company's Brisbane office in 2002. The Brisbane office has global responsibility for Mining & Metals procurement and also serves as the business unit's 'Centre of Excellence' for alumina and bauxite projects. Bechtel Mining & Metals maintains Centres of Excellence for copper and gold (in Santiago), as well as aluminium (in Montreal).

Other instances include:

*A US multinational in the manufacturing industry in Australia has recently assumed overall responsibility for their ASEAN operations – whereas previously they had just Australia/New Zealand responsibilities. Their accounting and IT group also now provides some services for the entire Asia Pacific region.*

*Another interviewee said there had in recent years been a global rationalisation of manufacturing undertaken within their corporation. As a result, there were now a limited number of manufacturing sites for a given product ('centres of excellence'). For some products, the Australian affiliate was now the sole supplier throughout the world.*

While some multinationals located in Australia now have an increased mandate, others have a significantly reduced role within their organisations. Two companies now report to headquarters through regional headquarters.

*The Asia Pacific headquarters of a company in the wholesaling industry has recently moved from Australia to Hong Kong, to be closer to its markets.*

Three manufacturing companies have lost their production operations over the past five years or so, although two of these have managed to secure a much enhanced R&D role within their corporations.

In spite of their acquisition by US interests in recent years, Arnott's (acquired by the Campbell Soup Company in the early 1990s – see case study) and ACI Packaging (acquired by Owen-Illinois in 1998) have retained major responsibilities for Asia Pacific operations, and also have part- or wholly-owned businesses in Asia.

## **EXPORTS BECOMING MORE IMPORTANT**

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US multinationals are significant contributors to Australia's overall export effort. In 2002-03, majority US-owned major exporters contributed A\$17.6 billion in exports – representing 13 per cent of Australia's exports of goods and services. This is appreciably higher than their eight per cent share in Australian businesses' operating income, although the difference is more marked in the case of non-US foreign-owned businesses (Figure 3.2).

Over 70 per cent of the US multinationals surveyed are involved in export. All but one of those in the manufacturing sector are exporters. All three mining companies export. Ten of the fourteen companies in the wholesaling industry export. A number of other services sector companies are also involved in export, in some instances through services exports to their overseas affiliates.

## CAMPBELL ARNOTT'S ASIA PACIFIC

The acquisition of Australia's leading biscuit company, Arnott's, by The Campbell Soup Company in 1997 secured the future for some iconic Australian products; provided new capital for Australian manufacturing; and gave impetus to Arnott's vision to build a global brand. Campbell Arnott's now employs 4300 Australians nationally.

In addition to maintaining Arnott's icon brands including Tim Tam, Shapes and Jatz, the company has also been able to invest in other Australian brands such as Wagon Wheels and Quattro, which might otherwise have disappeared. Innovative snack, biscuit and soup products have been developed by Campbell Arnott's Australian research and development teams, including the Snack Right 'Better For You' range, Campbell's Asian Soups and Kettle Sensations premium snacks.

A capital upgrade program worth A\$238 million for Campbell Arnott's seven manufacturing plants across four States has increased productivity, reduced wastage, and facilitated new product development for the local market and for export.

Arnott's Australian-made biscuits are exported to more than 40 countries, including Japan, the United States, Canada, United Kingdom, Indonesia and New Zealand. Arnott's Asia Pacific headquarters in Sydney is the base for Arnott's push into Asian markets, including its November 2004 entry into China. The company is pursuing acquisitions and joint ventures with local brands in some markets in tandem with increasing exports of Australian-made products to other markets in Asia.

Australian companies, rural and regional businesses and farmers benefit from more than A\$360 million spent by Arnott's and Campbell's each year purchasing Australian raw materials and services. For example, potatoes are sourced along the entire east coast of Australia from Bundaberg to Victoria, sugar from Queensland, dairy products from Victoria, and corn from New South Wales. Some farmers – like those in the Riverina growing soft wheat – can sell their entire crops to Campbell Arnott's. As product volume has increased so has the Company's spend on local produce and services.

Over the long term, Campbell Arnott's has developed supply partnerships with major Australian companies including Allied Mills, Visy and Amcor. In 2004 the company established another significant partnership with Linfox in a logistics outsourcing agreement valued at A\$75 million annually.

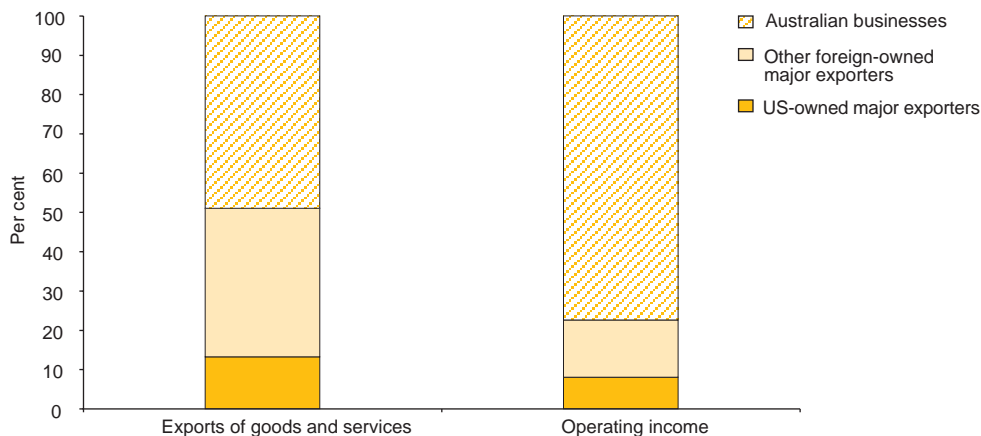
These relationships also provide broader opportunities for growth. For example, Australian company Amcor has leveraged its supply relationship with Campbell's in Australia to open up new opportunities for sales to Campbell's in Europe and North America.

As Campbell Arnott's continues to expand in the Asia Pacific region there is strong potential for some of its Australian partners to grow in parallel.

Figure 3.2

**US multinationals in Australia are significant exporters**

**Shares in Australian exports and operating income**



Note: Major exporters are defined as businesses exporting A\$1 million or more of goods or services; they accounted for 95 per cent of total exports in 2002-03. Personal travel and government services excluded from export data.

Sources: ABS, *Foreign Ownership of Australian Exporters and Importers, 2002-03* (cat. No. 5496.0.55.001); ABS, *Australia's Exporters, 2002-03*, Feature Article in *International Trade in Goods and Services, Australia, 2003* (cat. No. 5368.0); ABS, *Economic Activity of Foreign Owned Businesses in Australia, 2000-01*, cat. no. 5494.0.

Additionally, some interviewees who said their companies were not involved in exporting do in effect have some exports. One manufacturer has a subsidiary business which exports. Two services sector companies provide services to other affiliates. Another provides call centre services globally, while another has a headquarters role for the provision of a range of services.

Some companies are also involved in export indirectly, to the extent that their product is sold to customers some of whom might export. Some companies have also facilitated exports by local Australian companies and institutions (see Chapter 4).

Exports are an important source of income (more than 10 per cent of total revenues)<sup>19</sup> for 60 per cent of the multinationals involved in export – or some 40 per cent of all the multinationals surveyed. Nine companies are focused primarily on export markets (that is, exports contribute more than 50 per cent of their total revenues). The surveyed companies include some of Australia's largest exporters.

South-East Asia is a major market for some three-quarters of the multinationals (29 companies) involved in export (Figure 3.3). New Zealand and the South Pacific is a major market for around 60 per cent (the sole major market for a quarter of these). North Asia is a major market for over half the companies. The United States is a major market for just over one-third of the companies. Around one in five of the exporters export worldwide.

<sup>19</sup> Based in a few instances on an estimate of market prices where transactions are between affiliates.

**SOME OF AUSTRALIA'S LARGEST EXPORTERS**

Alcoa World Alumina Australia's revenues from exports of alumina and aluminium in 2003 were A\$2.6 billion. It supplies 15 per cent of the world's demand for alumina.

Australia Meat Holdings is the largest food processor and meat exporter in Australia. In the year to May 2004 its sales were A\$3.5 billion, with exports accounting for 85 per cent of production.

Holden is one of Australia's leading exporters of automotive products and services. In 2003, it exported 36 000 vehicles and 137 000 engines and its total exports were worth A\$1.24 billion. In 2004, Holden exported over 52 000 vehicles.

Pfizer's annual exports from its three Australian manufacturing plants have a market value in excess of A\$600 million.

Over the past five years, Boeing has exported from Australia A\$1.25 billion worth of aerospace components and high technology services.

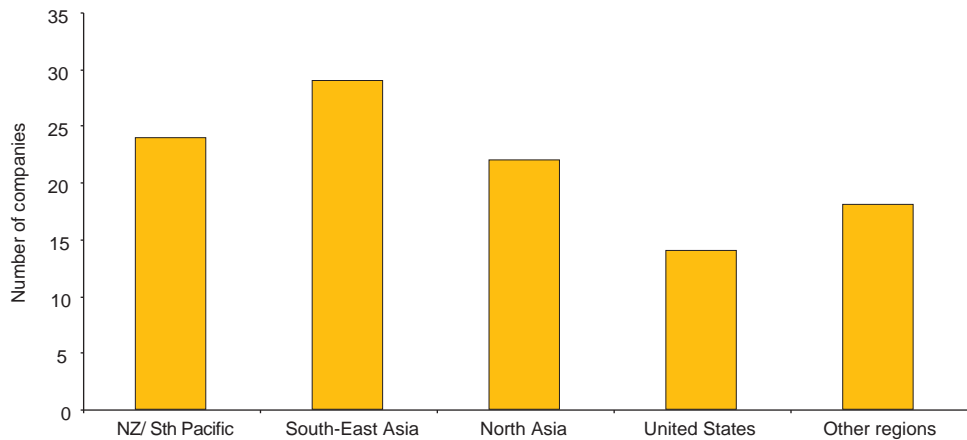
Over the past ten years, Kraft Foods (Australia) have earned export sales of A\$1.2 billion.

Sources: [www.alcoa.com/australia/en/home.asp](http://www.alcoa.com/australia/en/home.asp) (*Alcoa in Australia: 2003 Sustainability Report*), [www.holden.com.au](http://www.holden.com.au), [www.pfizer.com.au](http://www.pfizer.com.au), [www.kraft.com.au](http://www.kraft.com.au), accessed 9 November 2004, and unpublished information provided by Australia Meat Holdings and Boeing Australia.

Figure 3.3

**South-East Asia key export market**

**Respondent companies' major export markets**



Source: Survey results.

Encouragingly, exports are becoming more important for many multinationals. Over the past five years, exports have become more important for over one-half of the companies surveyed that are involved in export – compared with just three companies for whom exports have become less important. Similarly, looking ahead to the coming five years, one-half of the interviewees from companies involved in export expected exports to become more important for their business (Figure 3.4). For the most part, these companies are the same as those for which exports have become more important over the past five years.

US Bureau of Economic Analysis data also point to a dramatic increase in the importance of exports for US manufacturing industry multinationals in Australia since the mid-1980s – with exports doubling their share of sales over the period since the mid-1980s to just over one-quarter today.

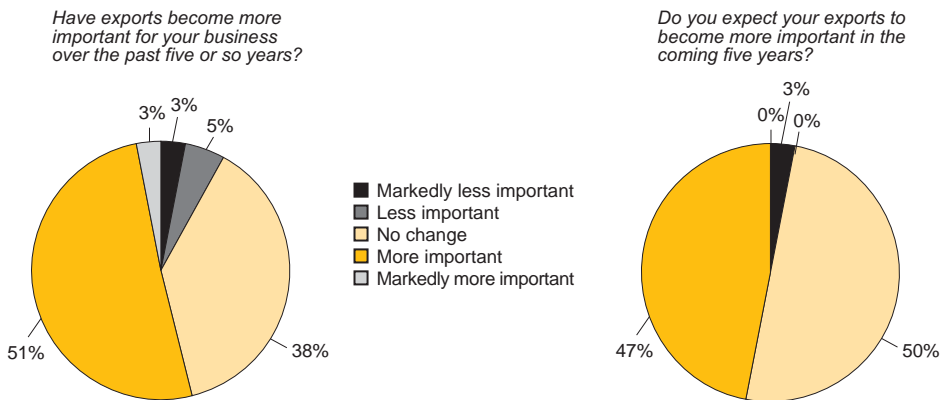
The increasing importance of exports – mainly to the Asia Pacific region – is consistent with Australia being drawn more into the integrated regional and global production strategies of the multinationals. The improved competitiveness of Australian industry, linked to the substantial dismantling of trade barriers and other economic reforms over the past couple of decades, is a driver of such trends. For example:

*A manufacturing company interviewee said the increasing importance of their exports reflected a trend to specialisation of manufacturing plants within the corporation around the world.*

Figure 3.4

**An increasing export profile**

**Changing importance of exports for respondent companies**



Source: Survey results.

## R&D IMPERATIVE

Innovation is a critical driver of economic growth. A study undertaken by the Department of Industry, Tourism and Resources (2002) underlines the significant contribution multinational enterprises make to the national innovation system, through their own R&D activities in Australia, through technology diffusion from their parent corporations, and through their interactions with local firms and institutions.

Over 40 per cent of total business R&D expenditure in Australia is undertaken by foreign-owned businesses.<sup>20</sup> This is almost double their share in industry value added. US companies have a disproportionate share – over one-half of the R&D of all foreign-owned businesses.

At the same time, the intensity of R&D undertaken in Australia by US multinationals is more modest by comparison with that undertaken by US affiliates in many OECD countries. In 2001, R&D expenditures by US affiliates in Australia were 1.5 per cent of their value added – which is less than that of US affiliates in Belgium, Finland, Switzerland and the Republic of Korea for example.<sup>21</sup>

Similarly, based on survey responses from 169 affiliates of nearly 50 multinational manufacturing corporations from the United States and five other countries, Harzing and Noorderhaven (2004) found that Australian affiliates had lower capabilities in R&D compared with affiliates in other countries. However, they found few significant differences between Australian and other affiliates in the extent of two-way knowledge transfers, although Australian affiliates were less likely to be 'global innovators' (characterised by high knowledge outflows and low knowledge inflows) and more likely to be 'local innovators' (low knowledge outflows and inflows).

The extent of R&D undertaken in Australia by US multinationals varies considerably from company to company. Holden headed the list of corporate spenders on R&D in 2002-03, with outlays of A\$227 million, followed by Ford Motor Company of Australia at A\$93 million (Intellectual Property Research Institute of Australia, 2004).

Around 30 per cent of interviewees said their companies spend three per cent or more of their revenues on R&D, with a handful reporting spending of over five per cent.<sup>22</sup> At the other end of the spectrum, over 40 per cent of the companies surveyed spend less than one per cent of their revenues on R&D. In half of these companies, R&D tends to be highly centralised in their organisations, with no R&D undertaken in Australia.

Some companies' R&D activities in Australia are focused on product modification for the Australian market.<sup>23</sup> At the same time, some two-thirds of interviewees said their companies conduct R&D in Australia that results in product sales into overseas markets. In some instances, this R&D is incorporated into customers' overseas product sales. Some companies also have a significant R&D mandate within their organisation. Many companies also undertake R&D in collaboration with local companies and institutions (see Chapter 4).

<sup>20</sup> ABS, *Foreign Ownership Characteristics of Businesses Undertaking Research and Experimental Development Activity in Australia*, published in *Australian Economic indicators*, August 2002 (cat. no. 1350.0).

<sup>21</sup> US Bureau of Economic Analysis *Survey of Current Business*, November 2003.

<sup>22</sup> Based on a comparison with IBISWorld data on R&D expense incurred, there was some observed tendency to over-reporting of R&D intensity at interview.

<sup>23</sup> Studies by Thorburn et al (2002) and Nicholas et al (2003) identified modification of products or services for the local market as a key, if not principal, focus of R&D undertaken by the broader set of (not just the largest) multinationals in Australia.

Some interviewees noted the excellent quality of Australian R&D but pointed to a shortage of researchers and a lack of critical mass to support extensive R&D. A number of companies commented favourably on the Government's R&D tax concession. One interviewee also said they had benefited from the R&D Start program (a grants and loans program that supports businesses to undertake research and development and its commercialisation). However, two companies in the pharmaceuticals sector made specific mention of the fact that they were unable to access the 125 per cent R&D tax concession because their patents were held overseas. Another manufacturing company interviewee expressed concern that the 175 per cent Premium (Incremental) R&D Tax Concession did not suit the cyclical nature of their industry.

## THE MULTINATIONALS AS BUSINESS PARTNERS

### KEY POINTS

- Most US multinationals generate considerable business activity and employment indirectly through their supply networks and other linkages.
- The reliance on local materials and goods suppliers by most US multinationals interviewed has not changed noticeably over the past five years. For many multinationals, their level of business with local suppliers is however growing as the scale of their business operations in Australia increases.
- High levels of local procurement have been maintained in the face of an increasing contestability of purchasing decisions arising from the trend to global or regional purchasing decisions by multinational corporations.
- Local outsourcing of services by US multinationals in Australia is widespread and growing. For almost half the multinationals interviewed, local outsourcing has become more significant over the past five or so years. And this trend is expected to continue, presenting further opportunities for Australian service providers.
- The focus for some other multinationals has been less on outsourcing but more on the centralisation of services functions within the corporation, at either the regional or global level.
- US multinationals are assisting local companies to participate in their procurement in diverse ways. More than one-third of the US multinationals surveyed have purposely set about developing partnerships and long-term relationships with their key suppliers.
- Around half of the US multinationals surveyed have helped local suppliers to export.
- US multinationals have significant linkages with other companies and institutions in the national innovation system.
- There has been a rapid uptake of e-commerce by US multinationals. Local suppliers need to embrace e-commerce to become part of the supply chains of the multinationals.

In addition to their direct contribution to the Australian economy, US multinationals generate considerable business activity and employment indirectly through their supply networks and other linkages. While the multinationals interviewed have varying degrees of interaction with local business, collectively they are very important 'business multipliers'. For example:

*While Merck Sharpe & Dohme (Australia)'s direct employment in 2000 was 850 people, Access Economics has estimated its expenditure was responsible for creating an additional 4600 jobs through its supplier relationships (Merck Sharp & Dohme, 2002).*

*Economists ACIL Tasman have estimated that in 2001 The Boeing Company's direct and indirect contribution to Australia's employment was in the order of 5400 jobs. Its direct employment was approximately 3000 (www.boeing.com.au, accessed 14 December 2004).*

## **PROCUREMENT TRENDS**

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The reliance on local materials and goods suppliers by most US multinationals interviewed has not noticeably changed over the past five years, nor do they expect it to do so over the coming five years.

It needs to be recognised however that most already rely very significantly on local suppliers. As a group, manufacturing companies indicated that almost 60 per cent of their total inputs – of materials/goods, services, technology and capital equipment – are sourced locally.<sup>24</sup> Mining, petroleum and metals companies and food manufacturers tend to be particularly reliant on local suppliers.

While local suppliers may not have increased their share of overall procurements by the multinationals, a significant number of multinationals noted that their business with local suppliers had nevertheless grown as the scale of their business operations in Australia had grown, and also pointed to anticipated further strong growth in their businesses over the coming five years.

In the resources area, local procurement is likely to grow strongly as a result of the number of projects in Australia currently under development or in prospect. Involvement in these projects will present opportunities for Australian companies to grow and globalise.

### **Global supply chains**

High levels of local procurements have been maintained in the face of an increasing contestability of purchasing decisions arising from the trend to global or regional purchasing decisions by multinational corporations.

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<sup>24</sup> Two-thirds of manufacturers answered this question. Note that this estimate may include an element of overseas sourcing to the extent that local suppliers may source some of their inputs from overseas.

The trend, evident in the case of some of the multinationals interviewed, stems from the fact that it is now much easier than before to purchase supplies from around the globe. Enabling factors include:

- information technology and communications advances, such as near real-time information exchange as well as the growing role played by e-commerce;
- lower trade barriers;
- improved and cheaper international freight and logistics, partly as a result of miniaturisation of some products; and
- technology advances which make possible mass 'customerisation' of products.

Global supply chains and supply chain management are an increasingly important part of the strategies and policies of many multinational corporations as they seek to drive down costs and withstand intensifying global competition.

#### SOME GENERALISED CHARACTERISTICS OF DIFFERENT TYPES OF SUPPLY CHAINS\*

Multinational supply chains might broadly be considered in four fairly distinct groups:

**Commodity supply chains** – companies will seek out the best price provided the quality is right. They will tend to change readily between suppliers where there is a cost advantage.

**Production line manufacturers** – supply chains are highly engineered, but options tend to be fairly well-defined. Companies will tend to develop long term relationships with suppliers and engage in critical information exchange with them. For example, if a company sees a need to shave its price to stay competitive, it will look to see where it can make savings in its supply chain and work with suppliers to achieve that end.

**Technology supply chains** – supply price tends not to be such an issue as suppliers will be seen as part of the technology solution. Existing suppliers are less likely to be displaced, provided they keep innovating.

**Other non-technical supply chains** (eg building and construction) – as in the case of commodity supply chains, companies tend to be price-focused, and prepared to change quite readily between suppliers – being able to deliver to a particular price is part of the pre-qualification process.

\* Based on discussions with Jim Box, CEO Industry Capability Network Queensland (see also Box, J.E., 2004).

One reason for the trend to global and regional procurements not impacting in a major way on local procurement levels is that local affiliates have often retained reasonable flexibility in their sourcing. For example:

*A manufacturing multinational interviewee said 'There is some emphasis now on ensuring that the group optimises its buying potential through collective purchasing of inputs. So we talk to suppliers on a global basis, but will only deal with those who can supply competitively to the local market. So there has not been a lot of impact on the Australian operations.'*

Local supply has the advantage of avoiding shipping costs and delays associated with foreign sourcing, and shipping delays can be important where just-in-time manufacturing is being undertaken, product life cycles are short or demand responsiveness is important. Relationship building is also easier in the case of suppliers close at hand – as is legal recourse in the case of non-fulfilment of contract terms.<sup>25</sup>

Some multinationals also recognise that nurturing local procurement helps build the capabilities and competitiveness of the local supplier base.

Any trend to global or regional sourcing also stands to have a lesser impact on local activity to the extent that multinational corporations with a local presence in Australia secure contracts that are let.

As the Committee for Economic Development of Australia (2004) points out however, Australian companies may need to look to getting into global or regional supply chains if they are to achieve appropriate scale. Some local companies are succeeding. Hofmann Engineering is one company that has worked hard to secure global or regional contracts, in recognition of the scale advantages that stand to be derived (see case study).

Participation in global or regional supply chains brings new considerations into play. Suppliers need to:

- adapt their products or services;
- provide regional or global product and service support; and
- work or partner with other supply chain participants, both in Australia and overseas.

The sharing of risks is also a much more important dimension of these supply chains compared with the traditional arm's length contractual relationships that have existed between supplier and customer.

Australian suppliers are likely to be advantaged where the Australian affiliate has a procurement role extending beyond the immediate region. For example:

*An interviewee in a manufacturing company with a global procurement role said they could foresee continued offshore opportunities for their Australian suppliers as they moved to broaden their global sourcing.*

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<sup>25</sup> Braithwaite (2003) argues however that companies can take certain measures to mitigate the risks associated with global sourcing.

### **HOFMANN ENGINEERING: A PROACTIVE APPROACH TO GLOBAL BUSINESS**

Hofmann Engineering, a 100 per cent Australian owned company, is one of Australia's largest engineering companies, with comprehensive gear manufacturing facilities. It has been working with the Australian mining industry for over 34 years.

Hofmann's experience is that it is hard work building up relationships with the multinationals. It has proactively pursued and won a number of tenders let by the multinational mining, and engineering, procurement and construction houses, most of which are now conducted via on-line auctions.

Hofmann has developed a reputation for delivering high quality products on time. It benchmarks its operations and processes against the best gear manufacturers in the world. It has an R&D company which undertakes product development and has a complete design facility utilising the latest gear and gearbox design software. It has a competitive edge in the area of heat treated gearboxes and parts.

Hofmann recognises the possible benefits in partnering with original equipment manufacturers, which invariably are multinational companies. In their sub-contracting, Hofmann will choose Australian suppliers if the price is only slightly more expensive than the imported product. That said, to be competitive it has had to rely on import sourcing for some raw materials and castings.

Hofmann was winning most of Alcoa's tenders in Australia for valves for both operations and project builds and so was recently awarded a global contract for three years. Hofmann has since provided valves for the upgrade of Alcoa's Jamaican refinery, as well as follow-up orders. The main benefit for Hofmann has been the efficiencies brought about by the increased scale of production the global contract has enabled.

### **Other drivers of change**

In part driven by the trend to look more to global purchasing options, a number of multinationals have in recent years moved to rationalise and consolidate their supplier lists. To the extent this becomes an increasing trend, supplier companies that wish to stay small stand to lose out, although they may still be able to secure business on a sub-contracting basis.

There is an increasing trend amongst multinational corporations to focus more narrowly on core competencies, whether these be production processes, technology development or marketing. At the same time, they are looking more to developing partnerships with key suppliers and also to contracting out some operations. Such operations are being spread internationally, with location decisions dependent on costs and logistics (UNCTAD, 2002).

Some multinationals interviewed have recognised increasing local industry capabilities and have taken strategic decisions to outsource some manufacturing.

*PACCAR Australia is one multinational that has come to rely significantly more on local suppliers. It now outsources the assembly of truck sub-assemblies which was previously undertaken in-house (see case study).*

Some multinationals have extended their business by working with local suppliers with complementary skills sets to provide 'packaged' or integrated solutions.

*Cummins Engine Company is another multinational which has considerably increased its reliance on local suppliers. It has started to do more 'packaging' work – bidding for contracts that involve inputs beyond its core products. In particular, Cummins Engine are drawing in local suppliers to provide an engine, generator and cooling systems package for Bombardier Transport, who are building fast trains for Victoria (see Air Radiators case study).*

### **PACCAR AUSTRALIA – A CLOSE AND EVOLVING RELATIONSHIP WITH SUPPLIERS**

PACCAR entered the Australian truck market in 1970 with the establishment of a Kenworth Truck assembly plant near Melbourne. Over the years, PACCAR Australia has designed and developed trucks to suit the often harsh and demanding local operating conditions and to ensure they meet the local Australian Design Rules regulations. Today, PACCAR Australia is enjoying market leadership in Australia, and also exports to New Zealand and Papua New Guinea.

PACCAR Australia imports major components such as engines, transmissions and chassis rails from its overseas affiliates but, otherwise, is able to source most components from Australian suppliers. It used to make various sub-assemblies in-house but has started to outsource some of this work. This has enabled it to speed up the assembly process to meet fast-growing demand.

PACCAR worldwide has in recent years adopted the 'Six Sigma' methodology. Six Sigma is an approach to analysing quality issues aimed at identifying and addressing 'defects' (anything outside of customer specifications) in any process.\* PACCAR Australia has applied the methodology both internally as well as with key suppliers. PACCAR Australia spends time with those key suppliers, reviewing their manufacturing processes. It also engages in benchmarking – showing suppliers how they are performing in comparison with other suppliers. This has helped ensure more consistent product quality and delivery from suppliers, and also encompasses the 'just in time' approach where that makes business sense.

With the ramping up of its truck production over recent years, PACCAR Australia's suppliers have become better placed to invest in new capital equipment and hence further improve their capabilities and efficiencies.

\* See <http://www.isixsigma.com>

### AIR RADIATORS: AN EXPANDING BUSINESS LOOKING MORE TO OVERSEAS CONTRACTS

Air Radiators is a market leader in the design and manufacture of industrial heat transfer and air movement solutions. It manufactures products engineered to withstand the harshest conditions. The company employs more than 140 people, and is one of the largest manufacturing employers in the Geelong region.

Air Radiators is an approved supplier to world-leading manufacturers of trucks, buses, earthmoving equipment, agricultural machinery, power generation, rail and other major capital equipment. Its major clients include Cummins Engine Company, Kenworth, Iveco Trucks and Caterpillar Elphinstone.

Air Radiators has been an active exporter for over 25 years to Asia, the Pacific, Europe and the United States, and now has a broad global customer base. Its proven track record supplying to major multinational companies, including those from the United States, has helped it secure significant export business over the years. It has also gained some business through referrals. For example, its reputation with PACCAR Australia (builders of Kenworth trucks) for radiators suited to harsh conditions has led to its securing some ongoing export business with KenMex (PACCAR Mexico).

Air Radiators' supplier relationship with cane harvester manufacturer, Austoft, has led it to supply cooling packages to the Austoft sister company, Brastoft, in Brazil.

Two major contracts have enabled Air Radiators to grow even stronger over the past two years. It is supplying cooling packages to Cummins Engine Company for the Victorian regional fast train project, being managed by Bombardier Transport. It is also supplying cooling packages direct to United Goninan for the Hunter Valley fast train project in New South Wales.

Air Radiators is now seeking to leverage off these two local contracts to get into overseas markets and so maintain its higher level of business activity. In September 2004, it displayed its world-leading technology in the supply of integrated engine cooling systems at Innotrans 2004, International Trade Fair for Transport Technology in Berlin, Germany.

Product ranges have also tended to increase compared with just a few years ago, while product life cycles have shortened.

*One manufacturer had come to rely on a greater number of imported inputs as it had extended its product range. Sometimes this reliance on imported inputs was maintained until a local capability had been achieved. However, its experience was that sometimes local suppliers seemed unwilling to make the necessary investments, and they may not pick up the business even over time as life cycles of products can be short.*

### Australian multinationals

Reflecting the bulky and heavy nature of the products they produce, the factor inputs of many of Australia’s large investors in the United States can for the most part be sourced more cheaply locally in the United States. Not surprisingly, therefore, the US affiliates of the Australian multinationals interviewed buy-in products or services from Australian suppliers only to a minor extent.<sup>26</sup> Nevertheless, three companies cited specific examples of local companies supplying inputs to their US operations on an ongoing basis.

### GROWING SIGNIFICANCE OF OUTSOURCING AND CENTRALISATION

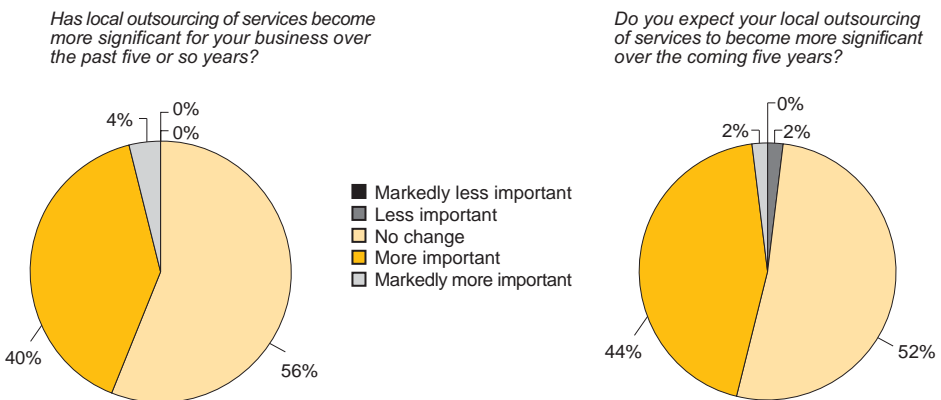
Local outsourcing of services by US multinationals in Australia is widespread and growing. For almost half the multinationals interviewed, local outsourcing has become more significant over the past five or so years. And local outsourcing is expected to become still more significant for just as many over the coming five years (Figure 4.1).

This presents opportunities for Australian service providers, including the local affiliates of other multinationals. In some sectors, outsourcing for others is a core business activity of US multinational service providers, and a number of these companies have seen their outsourcing business grow.

Figure 4.1

#### Outsourcing becoming more important

#### Changing importance of local outsourcing of services for respondent companies



Source: Survey results.

<sup>26</sup> US Bureau of Economic Analysis data (*Survey of Current Business*, July 2004, Table 16 addenda columns) indicate that virtually all imports by Australian multinationals in the United States are intra-firm.

Services that are outsourced will tend to be related to a multinational's non-core activities. Two prominent examples of services outsourced because they are considered to be non-core competencies are warehousing and distribution. Information technology services is another.

Outsourcing is also considered by some multinationals to offer the advantage of flexibility.

Some multinationals are also looking to rationalise their outsourced services in order to secure efficiencies and better control. For example:

*One interviewee said 'we are always looking at our processes and, if it makes sense, we will outsource. The trend is to move away from contracts with lots of small suppliers and instead develop supply contracts with just one supplier who can then subcontract.'*

For some multinationals, the focus has been less on outsourcing but more on the centralisation of services functions within the corporation, at either the regional or global level. They have sought to drive efficiency gains through standardising and streamlining business processes throughout their organisations, and moving towards shared service centres. Where centralisation of service functions is to affiliates in other countries, this can detract from local outsourcing possibilities. Conversely, centralisation of functions to Australian affiliates can generate related outsourcing activity.

The Australian affiliates of a number of multinationals have been beneficiaries of this centralisation trend in some services areas (see Chapter 3). Prospectively, others stand to benefit also, for example:

*One respondent flagged a significant focus on centralisation: 'The global company is looking into the possibility of centralising call centre services, accounting services, payroll services and some information technology functions. The company would be willing to consider Australia as a site for some of these.'*

*Another company said that all transaction processing for information technology, human resources and finance would shortly become a shared service regionally. For this purpose, Singapore, Australia, New Zealand and the South Pacific will become one region. As the Australian operations were the largest of these, the people performing this shared service role would be located in Australia (but reporting elsewhere in the organisation).*

A number of multinationals said that some functions were now handled by affiliates in Asia, although these tended to be lower-skilled functions such as payroll processing.

Travel services was commonly cited as an area where multinationals are moving towards centralised services and engaging service providers with global scale such as American Express. Travel services have previously been handled in a decentralised way and involved local travel agents.

Where functions are centralised elsewhere, there may still be openings for local business:

*One services sector respondent said 'Global players in the services sector will only pick up the very big deals. There is therefore potential for local services SMEs to step in and fill the gaps below this level where there is a need for decisions close to the customer.'*

## STRENGTHS AND WEAKNESSES OF THE LOCAL SUPPLY CHAIN

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The general view of the multinationals interviewed was that the capabilities of local companies have improved over the past five years, driven in large part by competitive pressures.

Being a supplier to the multinationals, with their exacting requirements, will generally require good capabilities, continuous improvement, being customer-focused and cost competitive. For example:

*One multinational interviewee stated that they set high standards and their suppliers respond.*

*Another interviewee said they were continually having to move forwards when it comes to technology, and their Australian suppliers have had to keep up with the demands placed on them.*

*Another further extended the connection: 'Suppliers who are also working for other globally oriented companies are more than likely to have been continually pushed to innovate and increase their value added, and as a result their capabilities have improved and continue to improve. They understand the nature of strategic sourcing and what adds to value (expertise, ideas and skill sets) rather than just dwell on the cost aspect. Other companies by contrast (mainly smaller companies) will tend to start to move 'up the curve' but then plateau – as they are not continually pushed.'*

Pax Australia has achieved a significant market presence in Asia through the relationships it has built up with multinationals and believes that other Australian manufacturing companies can also achieve success (see case study). They need to focus on products where they are competitive, place an emphasis on technologies, continually look for smarter ways of doing things, and take a long term view.

While the experience of the overwhelming majority of the multinationals is that the capabilities of local businesses have improved over the past five years, the capabilities and competitiveness of businesses in Asia are also improving. They therefore point to the need for local suppliers to stay ahead of the competition by continually sharpening their competitiveness and moving up the 'value chain'.

*For example, one manufacturer said they had moved to source more from overseas – both ingredients and packaging – at the expense of local suppliers. The change had come about as the capabilities of, and reliability of sourcing from, South-East Asia had improved. The exchange rate also had been a factor. The Internet had also played a role in bringing about change – they do a lot of reverse auctioning on-line.*

### PAX AUSTRALIA: COMMITMENT CAN PAY OFF

Pax Australia is a contract manufacturer, with manufacturing facilities in Ingleburn, NSW. It produces 40 million aerosols and 30 million liquids a year. It is a family-owned, private company, and is a major local employer, with around 300 employees.

Pax produces 700 different products and has 20 clients across 16 countries. Around one third of its production is exported.

Pax's main clients are Procter & Gamble Asia (Hong Kong, Singapore, Malaysia, Japan, Taiwan, Korea) and Gillette (Australasia, Hong Kong, Korea, Philippines, Vietnam, Singapore, Taiwan, Indonesia). Other clients include Johnson & Johnson, Colgate Palmolive and Revlon.

Pax had Procter & Gamble's Asian business some years back but lost it in 1995. It recognised that if it was to supply multinationals in Australia it also needed to be in a position to supply all of Asia, and set about developing a strategy aimed at gaining a sustained presence in Asia. It had found that the multinationals were all seeking to rationalise their presence in Asia by reducing the duplication of facilities and were wanting to deal with just one supplier for the whole region, thereby giving them greater leverage. Pax started regular visits to Taiwan, Korea, Hong Kong, Singapore and Thailand, and sought to influence planners in multinationals in the region. Its first success came with the regaining of Procter & Gamble's Asian business. Subsequently it secured all of Gillette's Asian business.

Critical to Pax's success has been the formation of a strategic alliance with a Japanese company, Daizo, and their creation of the 'One Asia' network to manufacture aerosols and liquids to client requirements for sale across Asia. Daizo has two factories in Japan and one in each of Thailand and China.

Pax commenced working with Daizo in the mid-1990s – at the insistence of one its customers – sending its engineers to help with the design and building of Daizo's Shanghai factory. This led to the development of a long-term relationship based upon trust and mutual respect, and the formation of One Asia in the late 1990s.

Today, One Asia provides a seamless supply chain to multinational customers across all of the Asia Pacific region utilising its five manufacturing facilities. It is a well-known and well-regarded business amongst all targeted customers, and is experiencing strong growth.

Pax considers it would be very difficult for an Australian company to realise a region-wide manufacturing business in the absence of an alliance such as theirs. In addition to adopting a common approach to marketing, the partners have been able to leverage their respective strengths – in technical, R&D, purchasing and general administration. In essence, One Asia is emulating the behaviour of a large multinational company whilst still being able to retain its individual and private company status.

Characteristics that can set successful companies apart from other suppliers include innovativeness, responsiveness, keeping up with technology, and benchmarking against competitors. Local suppliers also need to be prepared to take on a share of the risks if they are to retain and extend their business dealings with the multinationals.

*One manufacturing company interviewee said their local suppliers did not seem to realise that they needed to look to some offshore sourcing to stay competitive, just as they had done. They could also foresee a number of SMEs dropping off their supplier lists because they lacked the technology and confidence, and did not seem to be prepared to take risks and invest in new plant and equipment. The SMEs had unrealistic expectations that they would help them run their businesses and shoulder all the risks. This was in contrast to many Asian SMEs who were prepared to share in the risks. These shortcomings were resulting in many SME suppliers not keeping pace with the local operations of multinationals and larger Australian companies who had by contrast improved their supply capabilities. There needed to be a paradigm shift in many SMEs – to date they had been able to get by just by focusing on supplying companies locally, whereas they needed to be looking for business opportunities globally if they were to remain viable and grow their businesses.*

Ferra's involvement in the Joint Strike Fighter program<sup>27</sup> underscores the costs and risks involved for SMEs to secure offshore business with US multinational corporations (see case study). Companies need to be both serious and capable of supplying at the required quality in the required time frames and in the required volumes at competitive prices. This usually involves additional capital expenditure. At the same time, becoming involved in projects such as this can lead more readily to spin-off work with project partners as well as other parties.

Multinationals can also be demanding customers, requiring for example up-front savings as well as annual price reductions for multi-year contracts in the expectation of productivity improvements over time.

Australian companies have undoubted strengths in the resources sector, and foreign investment and multinational involvement in the development of the sector over the years has underpinned the growth of many local businesses. For example, as the profile of the oil and gas industry in Western Australia has increased, there has been increased involvement by overseas interests – which has brought more technology and expertise to Western Australia, which has also helped local suppliers to improve their international competitiveness.

Some multinationals identified skill shortages, lack of scale, and lack of competition as weaknesses in the local supply chain. In the resources sector, with a number of large projects currently under development or in prospect, concerns were raised as to the availability of a sufficient pool of skilled labour to meet the impending demand. In some sectors, US multinationals have been active players in efforts aimed at addressing the education and training needs of Australian employers.<sup>28</sup>

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<sup>27</sup> The Government's investment in the Joint Strike Fighter program as a 'level Three Partner' provides, amongst other things, the opportunity for Australian companies to bid for development and manufacturing work, as well as associated support and maintenance.

<sup>28</sup> For example, a number of multinationals are members of the IT Skills Hub, which is focused on information and communication technology skill development (see [www.itskillshub.com.au](http://www.itskillshub.com.au)).

A lack of scale was seen by some multinationals to impact on the pricing and competitiveness of local industry. Lack of scale might be addressed by local companies looking for opportunities to grow their businesses through exports, perhaps by getting into the multinationals' regional or global supply chains or otherwise securing contracts with the multinationals' overseas affiliates. However, without a proven track record it can prove a challenge to win such business. An alternative approach to gaining some scale economies is to look to supplying export-oriented multinationals locally as Hook Plastics has done (see case study).

A few companies raised the issue of the lack of competitive supplier pricing, resulting from the existence of just one or two suppliers in some industries.

### **FERRA: CONTRACTOR TO THE JOINT STRIKE FIGHTER PROJECT**

Ferra, an SME, is one of Australia's leading precision engineering and high-pressure die-casting companies. It has state-of-the-art plant, equipment and computer design services, all of which are underpinned by a considerable depth of experience and dedicated employees.

Ferra has built a solid reputation as a world-class supplier of precision light metal components to exacting quality standards, delivered anywhere in the world. Ferra is quality assured to QS9000, ISO9001. It prides itself on supplying to such demanding industries as aerospace, high-end automotive, telecommunications, medical industries and many major manufacturers.

Ferra has recently won seven contracts out of the 21 let in Australia for Lockheed Martin's Joint Strike Fighter (JSF) Project. These long term contracts will result in significant company growth. Ferra also supplies other international companies such as Hewlett Packard (United States), Filtronic Comtek (United States) and Celestica Inc (Thailand). It is also an approved supplier to Boeing and supplies Boeing Australia.

The JSF business has not come easily. Ferra has had to expend considerable effort and money over an extended period of time.

A trade mission to the United States organised by the Department of Industry, Tourism and Resources helped establish Australian involvement in the JSF project. But this mission was just the start of efforts to build ongoing relationships and confidence that Australia had the expertise to accommodate the needs of Lockheed Martin and its sub-contractors. These needs included reduced costs at 'best value', high quality on a repeat basis, real time resource tracking, e-commerce, annual 'cost downs' (continuous improvement), and an understanding of global logistics.

Ferra's experience is that repeat visits overseas to continually develop relationships with potential clients are critical to success. Clients will also need to be convinced to come to Australia to view, and be reassured by, a company's capabilities. Ferra was also prepared to invest in increased machine capability to put it in a better position to win JSF contracts.

## HOOK PLASTICS: TAPPING INTO GLOBAL MARKETS THROUGH THE MULTINATIONALS

Hook Plastics is a family owned SME with no licence agreement with any other company either foreign or domestic. The company manufactures international-standard injection moulded components and finished assemblies for the automotive, electronics, telecommunications and appliance industries.

Management has placed particular emphasis on building up the business's engineering skills. It works closely with designers and engineers of major clients with a view to continual improvements in product quality, aesthetics and function. The business has faced a number of challenges in recent years.

**Why Change?** Hook Plastics realised manufacturing for the domestic market offered little in the way of growth opportunities. Moreover, its engineering costs per unit of production were relatively high because of low domestic volumes. Hook Plastics' customers had also encouraged them to participate in the global market.

**Strategy** The company decided to position itself as a supplier of world-class plastic mouldings and assemblies to local divisions of export-oriented multinational companies. In this way it has avoided the costs and strains of setting up foreign offices or agencies. In some instances, it exports to the overseas affiliates of its customers, but through arrangements with the local affiliates. The company had previously been supplying mouldings to a local division of Siemens for supply to Telstra and also to meet Siemens's export contracts. It therefore had some experience in meeting the requirements and expectations of foreign customers. Hook Plastics' people had also worked with toolmakers and development departments of some companies in Europe.

**Prices** The resulting higher production and sales volumes have increased Hook Plastics' material price bargaining power and allowed introduction of more automated manufacture to reduce and control costs. This has put the company in a much better position to meet the demanding requirements of its multinational customers, especially in the auto industry.

## HELPING LOCAL COMPANY PARTICIPATION IN PROCUREMENT

While the multinationals can be demanding customers, their financial strength, technical capabilities and extensive networks can assist local companies. US companies have identified a diverse set of ways in which they have helped local companies, including SMEs, to participate in their procurement (see for example Boeing Australia, Textor, Baxter Healthcare and Collins Foods Group case studies).

More than one-third of companies indicated they have purposely set about developing partnerships and long-term relationships with their key suppliers.<sup>29</sup> Some have entered into long-term contracts with suppliers even when it may not particularly suit them. Other mechanisms used by US multinationals to support suppliers include:

- inviting and facilitating local involvement in tenders;
- providing technical assistance;<sup>30</sup>
- challenging suppliers' ways of doing things;
- sharing information;
- helping suppliers to streamline their operational processes and procedures, including quality aspects, environmental and safety standards;<sup>31,32</sup>
- sponsoring suppliers to attend international conferences and forums with a view to expanding their horizons; and
- procuring inputs at a cost cheaper than suppliers could otherwise obtain.

Assistance provided by US multinationals to local companies to participate in the multinationals' procurement can lead to improved operational effectiveness. This happens both through extending their technical competence and capacities and improving, and bringing discipline to, their processes and procedures. All these improvements can be applied by local companies to their other business activities, both here and overseas – with their other existing customers, with their potential customers and with their own suppliers. The 'spillover' benefits multinationals can bring to the broader economy – in the form of such enterprise spin-offs, as well as demonstration effects, competition effects, and the mobility of trained labour – can be substantial (UNCTAD, 2001).

<sup>29</sup> Such long-term cooperative relationships typify the Japanese system of subcontracting, to which a greater willingness on the part of suppliers to make customised investments is often attributed. This can in turn lead to productivity and quality improvements (Purcell and Nicholas, 2002).

<sup>30</sup> A survey of 270 multinationals operating in Australia, reported in Nicholas et al (2003), revealed that more than one-third of the companies 'sometimes' transferred technical know-how, while a further one-sixth 'usually' transferred technical know-how (source: unpublished data provided by Nicholas).

<sup>31</sup> A study by Thorburn et al (2002) of 56 SMEs supplying to both multinational and Australian customers found that the suppliers' multinational customers in Australia were more likely to train or certify them to meet product quality and service standards than were their local Australian customers.

<sup>32</sup> A UK study of the effects of foreign investment similarly found significant effects on business practices and performance of local firms. Nearly two-thirds of the suppliers surveyed considered that their relationships with foreign companies had led to positive impacts on their business practices, with the strongest and most widespread effects being on quality assurance systems, product development activities, production organisation and cost control (PA Cambridge Economic Consultants, 1995).

## BOEING AUSTRALIA – ENCOURAGING SME PARTICIPATION IN PROCUREMENT

The Boeing Company has been involved in the Australian aircraft and defence businesses for more than 75 years. In the last five years, Boeing has invested A\$579 million in facilities, plant, equipment, and employment and training of Australians and technology transfer, A\$265 million (1997-2001) in local R&D and has exported aerostructure components and high technology services worth some A\$1.25 billion.

Boeing Australia Limited, a wholly-owned subsidiary of The Boeing Company, is a high technology company specialising in design, development, manufacture and installation of complex defence and commercial systems. Boeing Australia is headquartered in Brisbane and employs nearly 2000 staff at 19 locations around Australia, supporting defence and other customers.

Boeing Australia has progressively increased levels of local content, and actively encourages and facilitates SME involvement in purchasing programs. Overall, some 10-20 per cent of the company's procurement needs are met by SMEs, with SME involvement in 'life cycle support' contracts for defence systems being nearer to 60 per cent.

Boeing Australia recognises that engaging local suppliers enhances local industry capability, which in turn enhances Boeing Australia's ability to develop its own business over the long-term. Defence contracts also demand a significant amount of local Australian industry involvement, and the emergence of South East Queensland as a significant aerospace hub allows Boeing Australia to draw on a greater pool of local companies to meet contractual requirements.

There is significant benefit for local companies too. Local suppliers gain access to Boeing Australia's knowledge, procedures, and protocols, and are often mentored by experienced Boeing Australia procurement professionals to rapidly mature their processes and procedures, to meet the company's demanding quality standards. Boeing Australia supports this by providing quarterly feedback through its supplier assessment program, which measures suppliers' performance on criteria such as quality, on-time delivery and affordability.

As an example of the support that Boeing Australia provides for many of its contractors, the company at present has 26 engineers deployed to help contractors with program delivery.

Further examples of Boeing Australia's relationships with SME suppliers are:

- Boeing Australia was instrumental in the development of a 'virtual factory' which brings together a variety of SMEs with differing capabilities into a collaborative group, providing a capability Boeing Australia can leverage off. The group has formed an electronics manufacturing outsourcing centre, which is now a certified supplier to Boeing Australia.
- Rosebank Engineering is working closely with the Boeing Aerospace Support Centre at Amberley, supporting the F1-11 strike aircraft providing hydraulic, pneumatic, fuel and mechanical component maintenance.

### **TEXTOR: A PRODUCTIVE PARTNERSHIP WITH KIMBERLY-CLARK AUSTRALIA**

Textor is a leading producer of non-woven textiles, offering an array of needle punched and chemical or thermal bonded products for use in healthcare and hygiene, cleaning, filtration, food packaging, agribusiness, environment and promotions. It became an Australian-owned company in 2000, headquartered at Tullamarine.

Textor approached Kimberly-Clark Australia (KCA) seeking to supply nappy components. KCA had been relying on an overseas supplier, and was keen to have a local source of the components. To secure the business, however, Textor had to be able to trim its margins, which it was able to do by undertaking substantial capital investments and working its machinery intensively.

KCA opened up its technology to Textor and worked with Textor in the development of products for KCA, and helped Textor install a new production line. It brought in some of its technicians from the United States to help the company improve its equipment and also invited Textor to view its US plants. Through its buying power, KCA also secured more favourable rates on some items.

KCA has been a tough, demanding customer. KCA has demanded guaranteed qualities and getting its production processes accredited to KCA has proved a challenge for Textor. KCA has been precise, professional and engineering-focused in its dealings with Textor. At the same time, it has been prepared to support Textor to ensure targets are met. In turn, Textor has developed a similar approach in its dealings with its suppliers, thereby helping to ensure standards are raised down the line.

Textor now has 100 per cent of KCA's business in Australia. The relationship with KCA has helped turn Textor around into a profitable business looking to expand further. KCA has introduced Textor to its affiliates in Singapore and Taiwan, and Textor expects to be able to secure their business also.

### **BAXTER AUSTRALIA'S RELATIONSHIP WITH LOCAL SUPPLIERS**

Baxter Healthcare Australia and New Zealand is a provider of healthcare products, technologies and related services.

Building relationships with local suppliers is an integral part of Baxter Australia's business success. An example of this is reflected in the 'Plastic Pour Bottle' range. This range has evolved from a product with an aluminium cap and paper label, to a fully recyclable unit made completely from polypropylene. Suppliers played a central role in the redesign of the empty bottle and the tamper evident seal. When a Baxter joint venture company in Turkey launched their own polypropylene bottle, they chose to source caps from Baxter Australia's local supplier, due to competitive cost and outstanding quality. Designed Mouldings, the cap supplier, has since been awarded the Baxter Turkey 2003 Best Supplier award, based on quality, delivery and service criteria. Designed Mouldings continue to supply Baxter in Turkey with over two million caps each year.

Baxter Australia has been sourcing bottles from Plaspak-Steriplus for over 15 years. When Baxter Australia approached Plaspak-Steriplus to reduce costs, so that it could expand its market opportunities, they responded with a design that met the challenge. Baxter Australia's current export volume is over two million units each year, or approximately a third of total production.

The close proximity of local suppliers also allows Baxter Australia to take advantage of 'just in time' daily deliveries. For example, empty bottle stock held on site does not exceed four hours of manufacturing time. Baxter Australia is heavily reliant on its suppliers for consistent quality and delivery. The close relationship Baxter Australia maintains with Plaspak-Steriplus allows this system to work very effectively.

The cap and bottle suppliers have been classified as 'Certified Suppliers' by Baxter Australia's quality assurance team. This means that their internal quality checks meet Baxter Australia's required standards, eliminating the need for Baxter Australia to inspect each delivery. This reduces costs.

It is through such close relationships with local suppliers that Baxter Australia has been able to produce a better designed quality product and increase its export sales opportunities in very cost competitive markets.

### **COLLINS FOODS GROUP: A WIDE REMIT BENEFITS SUPPLIERS**

Collins Foods Group operates 112 KFC outlets in Queensland and 28 Sizzler restaurants in Australia. It is responsible for support to Sizzler in Thailand, Taiwan, Japan, Korea and New Zealand. It is presently overseeing the setting up of operations in China.

Collins Foods supports Australian manufacturers and service providers, and purchases Australian made products wherever possible. It sources the freshest, quality product from all across Australia to guarantee Sizzler and KFC customers receive only the best. For many years it has worked closely with Australian suppliers to ensure they all meet the stringent specifications Collins Foods demands.

Collins Foods has a written code of conduct governing the way it does business with suppliers. It will often seek to build up relationships with existing suppliers rather than put business out to tender. Where a supplier would need to make a significant investment of a depreciable nature, Collins Foods will let contracts over an appropriate period.

Sizzler and KFC are regularly adapting their products to suit customers' demands. With the assistance of suppliers, new tastes, styles and flavours are introduced to their menus on a regular basis.

Collins Foods has assisted meat producers to supply product to Sizzler operations in Korea and Thailand. It will take on a facilitating role, and disengage once an arrangement is in place. The R&D undertaken with suppliers aimed at developing new meat products has helped get suppliers' products into offshore markets.

### **FACILITATING LOCAL COMPANY EXPORTS**

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Over 70 per cent of the US multinationals surveyed are exporters. Many of these companies depend on inputs from local suppliers and in this sense these suppliers are also exporters.

Established links with multinationals can help suppliers and contractors enter or expand export markets through the multinationals' overseas networks. Multinationals may refer their proven suppliers to their overseas affiliates. Moreover, export-oriented multinationals will have a good knowledge of overseas market conditions and preferences, which they may be willing to share with their suppliers. They may also be able to provide marketing channel assistance.

Any offshore business generated may be one-off, intermittent or more regular. Ongoing business opportunities can arise if a local supplier is able to gain pre-qualification or 'preferred supplier' status for affiliate business.

Any business secured with overseas affiliates can in turn lead to introductions to other affiliates or third parties in overseas markets. Australian companies gaining overseas consulting business may

also be able to draw in other local people. This trade facilitation role can be mutually beneficial. The multinationals can benefit to the extent that their suppliers stand to derive greater efficiencies and competencies as a result of a greater scale of operations and exposure to this export trade.

However, very little study has been undertaken to date on these market access 'spillovers', or the channels of transmission (Blomström et al, 2000). One study by Raines et al (2001) of the Scottish oil and gas, and electronics sectors, both of which are dominated by foreign-owned multinationals, found that multinationals had been instrumental in initiating and extending the export business of a number of their key suppliers. Nearly half of these suppliers in both sectors followed their multinational business partners into overseas markets or else secured business with the multinational's overseas affiliates through referrals or the credibility they had gained in supplying the multinational locally.

Around half of the US multinationals in Australia canvassed in the present study – both manufacturers and non-manufacturers alike – have helped local suppliers to export in their own right. This assistance has been provided in various ways, with numerous examples included in the case studies. In the majority of cases, the multinational has introduced local suppliers to their overseas affiliates or otherwise facilitated trade with their overseas affiliates or their clients (see Yum! Restaurants case study). In a couple of instances, multinationals have facilitated trade or on-the-ground business with overseas operations directly under their control or in which they are involved (see Honeywell case study). One multinational has introduced a local company to an Australian client leading to technology exports to that client's overseas operations. Some multinationals have also helped their customers to export.

#### **YUM! RESTAURANTS: ASSISTING LOCAL EXPORTERS**

Yum! Restaurants is the largest restaurant business in Australia measured in terms of numbers of stores, both owned and franchised. It is the franchisor for the brands of KFC and Pizza Hut.

Virtually all Yum! Restaurants' raw materials are sourced from Australia. R&D is undertaken in conjunction with local suppliers. Most R&D is focused on the local market, but some is also incorporated into offshore affiliate products.

Yum! Restaurants has helped Australian suppliers secure business with Yum! franchisees in Asia and the Middle East. It provides supplier introductions and sometimes proactively assists suppliers secure contracts. Given the issues of scale associated with the limited Australian market, this facilitating role, coupled with the Yum! Brand reputation, has helped ensure the ongoing financial viability of some suppliers. At least two suppliers have now factored exporting into their business plans and managed to develop significant export markets with the potential to exceed in importance their sales to the local market.

Yum! Restaurants expects to help secure exports by suppliers into Asian and Middle East affiliates in the order of A\$20 million this year, up from just A\$1 million in 2000.

Once suppliers have met Yum! Restaurants quality and safety standards, they are able to meet any other standard across the region. Conversely, if they can succeed in exporting into Yum! affiliates in Asia, suppliers will be well placed to expand exports to other customers across the region.

### **HONEYWELL AUSTRALIA: DRAWING SUBCONTRACTORS INTO OFFSHORE PROJECTS**

Honeywell Australia's core activity is the provision of business automation and control systems for industrial and commercial customers. Software is central to this activity, and Australia is now a global centre for software development within Honeywell. In addition, the Perth office is the head office for Honeywell's work with Alcoa globally.

The installation of automation and control systems involves large expenditure on procurement, notably for sub-contracting local contractors.

Honeywell Australia is an accredited supplier and it helps bring its subcontractors up to the required performance standards. Subcontractors can in turn apply these same standards in their contracts with the businesses they engage.

The knowledge and expertise which some key subcontractors have acquired in the process of working with Honeywell Australia has been instrumental in their obtaining work in connection with Honeywell projects in Asia.

Honeywell Australia engineers quite often work with their suppliers in overseas projects, in a contractor-subcontractor relationship. In the case of their work with Alcoa, Honeywell Australia engineers have drawn large numbers of Australian suppliers who worked with them on projects in Australia, into overseas projects with Alcoa.

It would seem reasonable to posit that multinationals with a significant offshore mandate are in a better position to facilitate exports by their Australian suppliers, not least because they are more likely to be closely linked into their global organisations in terms of two-way knowledge and other information flows. However, there was not a marked difference in the extent to which multinationals with a significant mandate have facilitated exports by their suppliers compared with the other companies interviewed. Nor was there a marked difference in the extent to which multinationals involved in export have facilitated exports by their suppliers compared with the non-exporting companies interviewed. But, almost all (seven of the eight) companies with a procurement role beyond the immediate region have helped their local suppliers to export.

A few multinationals, notably in the information, communication and technology sector, have gone into export with local companies (see CMC case study). This may involve the sharing of technologies to create an attractive solution for the export market, or alternatively the local company might develop a process or technology which works for one of the multinational's local clients but which might equally work for an overseas affiliate's clients. The multinational can provide customers the local company would otherwise not access, and can offer the local company backing by way of its financial strength and the credibility it can lend.

### **COMMERCIAL METALS COMPANY: PARTNERING FOR DOMESTIC SALES AND EXPORT**

Commercial Metals Company (CMC) is a listed corporation on the New York Stock Exchange. CMC and its subsidiaries manufacture, recycle and market steel, metal products and raw materials through a worldwide network of over 140 locations. Group revenue exceeds US\$4 billion, with over 30 per cent generated outside the United States.

In Australia, CMC processes and value adds steel, markets and distributes steel, and markets raw materials to the steel, foundry, smelting and metals industries.

CMC Tomago Heat Treatment Plant sources alloy steel bar domestically from OneSteel and Smorgon, as well as import. This bar is heat-treated and cold finished and this value added steel product is sold for sophisticated engineering steel applications. Prior to this investment (1998) most of this steel grade was imported.

CMC subsidiary Coil Steels Group is a national distributor and processor of BlueScope sheet and coil in Australia.

CMC also assists SMEs through the provision of working capital as part of the raw material supply package. An example is Pacific Coal Processing, a start up business in Newcastle. Pacific Coal Processing shareholders own the coke production facilities while CMC provides the working capital to purchase the coal, and funds the marketing cost and accounts receivable. Coke is sold domestically but also through CMC international marketing offices. This new venture has recently developed sales to New Zealand and Korea. As acceptance of the product grows, further investment will be needed for working capital and to expand production.

While CMC does not trade directly with the United States, it provides an important service and plays a role in the Australian steel and metals industry.

### **Australian multinationals**

Only one of the Australian multinationals interviewed, Mincom, has helped one of their suppliers export to other parties in the United States (see case study). Another company said they had helped some of their clients in Australia extend their involvement in the United States. In another case, a multinational's business dealings with suppliers in Australia have given rise to those suppliers securing supply contracts to their operations in other parts of the world, but not the United States. These contracts have sometimes led to their securing business with non-associated companies in these countries.

## MINCOM: BORN OF THE GREAT AUSTRALIAN CHALLENGE

Australian companies have developed a broad range of skills in software and technology to help large enterprises, like mining companies, that are dependent on assets for their revenues. The main competitive advantage of Australian companies like Mincom is their ability to respond quickly and effectively to service operations in remote and often inhospitable areas. With 25 years in mining technology, Mincom is a leading technology partner for asset-intensive industries worldwide.

The company produces software in areas such as maintenance, schedules and logistics, designed to ensure the efficient running of plant and equipment. Established in Brisbane in 1979, the company employs 1100 people; it services clients in the mining, oil and gas, utilities, transportation, defence and government industries in more than 40 countries.

### Mincom goes to America

Mincom's first export was the sale of Miner2, a mine-mapping product, to Louisiana miner Dollet Hills in 1984. By 1988 Mincom employed 33 staff in the United States and BP America became a customer. After the business's flagship software MIMS was introduced to the US market, Union Pacific Railroad was next in a series of major American companies to use Mincom's technology, fuelling the company's growth across Latin America, Africa and Asia.

Mincom's North American business now accounts for some 40 per cent of the company's total revenues. Mincom Inc. is a major reseller of Mincom's software and services to US clients.

### Collaboration with local and global partners

Like groundbreaking technology, partnerships have been central to Mincom's success. In 1997 Caterpillar Inc signed a deal with Mincom to develop 'whole of enterprise' solutions for the mining industry. Today Caterpillar has a 12 per cent shareholding in Mincom, an investment made to fund the development of technology complementary to Caterpillar's equipment. Mincom has since developed software for Caterpillar. Another alliance, with Newmont Mining, now extends to its operations in Russia.

Technology partnerships and resellers include Computer Associates, IBM and Oracle. Development partners include Hewlett-Packard, Microsoft, and Sun Microsystems.

Mincom relies on its partnerships with global giants and local companies to create world best practice business solutions for customers. This collaboration has extended to Mincom providing avenues for other Australian companies to gain a foothold in the US market. Mincom has provided an Australian SME, Oniqua, which produces a complementary product, with a channel to some of its US clients, and has also provided them with some office space in the United States. Melbourne-based learning company Parviva is another local partner providing their products and services to Mincom's client base out of the headquarters in Colorado.

## R&D PARTNERSHIPS

Survey results indicate US multinationals have some significant linkages with other players in the national innovation system.

Just over half of the US multinationals interviewed undertake R&D with other companies in Australia. Still more collaborate in R&D with institutions such as universities and the CSIRO, or else undertake R&D as part of a government program (e.g. in Cooperative Research Centres or the Government's Pharmaceuticals Partnerships Program).

This is broadly consistent with the findings of a study by the Department of Industry, Tourism and Resources (2002) of some 40 multinationals in Australia. In that study, most multinationals had R&D links with institutions such as universities, the CSIRO or Cooperative Research Centres. Strategic alliances with local companies were far less common however.<sup>33</sup>

The R&D collaboration with other companies undertaken by the surveyed multinationals is mostly with suppliers, but some is also with customers or clients. Some is with specialist R&D companies.

Several manufacturing multinationals collaborate in R&D with local suppliers, aimed at new product development. A number of companies in the food manufacture or retail sectors work with other companies to develop new products including products intended for export. Instances were also cited of collaboration with other companies in the area of production technology. Some pharmaceuticals companies undertake R&D with biotechnology companies.

*Merck Sharp & Dohme (Australia) recently entered one of the largest biotechnology collaborations in Australian history with the Melbourne-based biotechnology firm Amrad Corporation. With a potential value of US\$112 million plus royalties, the collaboration could lead to the development of significant new therapies for asthma.<sup>34</sup>*

Companies interviewed generally commented favourably on their links with local research institutions, and on the calibre of their researchers. However, some were concerned by the complexities associated with securing R&D projects and funding; two of the companies maintained that institutional arrangements were too fragmented.

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<sup>33</sup> A survey of Australian manufacturing companies undertaken by Basri (2001) found that over half of the companies that undertook product innovation had a 'foreign collaboration partner'. However, the study did not distinguish whether the partner was an overseas parent or subsidiary, a local affiliate of a multinational, or an unrelated overseas partner.

<sup>34</sup> Sourced from [www.msd-australia.com.au](http://www.msd-australia.com.au), news release 15 October 2003, accessed 24 November 2004.

## **MONASH UNIVERSITY ACCIDENT RESEARCH CENTRE AND HOLDEN IN MIDDLE EAST ROAD SAFETY PUSH**

Monash University Accident Research Centre is expanding its research program investigating vehicle crash and injury risk for Holden into the Middle East.

In a Memorandum of Understanding with the United Arab Emirates University signed in March 2004, Monash University, a world leader in road safety research and initiatives, is assisting the United Arab Emirates University to establish the UAE Research Centre for Transportation and Traffic Safety at its main campus in Al Ain.

After a successful 10-year relationship with Holden in Australia, Monash University Accident Research Centre will carry out car accident investigations involving Holden vehicles exported to the United Arab Emirates and sold locally as Chevrolet vehicles.

Monash University Accident Research Centre's research in the United Arab Emirates will provide valuable assessment of the occupant protection of Commodore based-models under Middle East road and traffic conditions. (The Middle East is Holden's largest export market, with exports of 22 000 cars in 2003.)

Monash University Accident Research Centre will assist the United Arab Emirates University set up the cross-faculty research institute, provide training for investigators, supply equipment for conducting crash inspections, and monitor the process and quality of the data received.

## **E-COMMERCE: BECOMING INCREASINGLY IMPORTANT**

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The Internet and e-commerce are reducing operating costs and facilitating the entry of new players to the marketplace. As a result, the trading environment is becoming more competitive. At the same time there can be 'first mover' advantages given the propensity for establishing ongoing trading relationships on the back of the new technologies.

There has been a rapid uptake of e-commerce by US multinationals over recent years, and most of the multinationals interviewed have implemented e-commerce systems to undertake procurement. Some multinational corporations are also procuring more regionally or globally, using e-commerce. Many multinationals also have e-commerce arrangements with their customers and distributors. The majority of companies that do not yet have e-commerce are looking to develop such arrangements. A number of companies have also moved to upgrade their existing systems.

The sophistication and coverage of the multinationals' e-commerce systems varies significantly. They include EFT-only systems; direct e-commerce links with selected key suppliers; and other quite extensive systems. For some, e-commerce is already a vital part of their way of doing business. For others, e-commerce is expected to become a more integral part of their business.

Business activities increasingly being undertaken on-line include requests for quotation, the handling of tenders, the raising of purchase orders, invoicing, bill payments and on-line auctions. E-commerce

systems can yield considerable business efficiencies, particularly if they are integrated with a company's internal financial systems. They can provide the means for a company to standardise the way it does business with a large base of suppliers.

E-marketplaces and private business-to-business trading exchanges are becoming an increasingly important tool for multinationals to do business with their suppliers and customers. For example, large resource companies such as Newmont increasingly use an online procurement system called Quadrem (see case study).

The trend to e-commerce has implications for local suppliers. They increasingly need to be able to bid for contracts by electronic means, as well as to engage in electronic payments systems. Procurement from them becomes easier for their customers if they have e-catalogues setting out their product range, specifications and prices.

Typically suppliers need to go through a pre-qualification process to be able to supply electronically. Pre-qualification will generally involve an appraisal across a range of areas including due diligence, quality assurance, and environmental compliance. There is often a rigorous pre-qualification process for major or critical procurements. A technical evaluation of suppliers will be important where there are major safety issues.

Suppliers therefore need to take pre-qualification seriously. It can bring eligibility to bid for all work with a particular line of expertise.

Generally, suppliers have adapted well in implementing systems compatible with those introduced by the multinationals, although some are still at the 'starting blocks'. Larger companies, with their greater resources, have tended to demonstrate more adaptability than smaller companies. One area where a number of multinationals said that local suppliers were generally not up to the mark was logistics.

Prospective suppliers will often be told early on in discussions that they will need to conform to the multinational's way of doing business, including e-commerce. However, in some instances key supplier relationships have been maintained in spite of the supplier not having e-commerce capabilities.

Be that as it may, suppliers need to be up-to-date with business practices if they are to be good business partners. Most companies recognise the advantages of e-commerce and need no encouragement to get involved via pre-qualification.

Previously, considerable gaps in awareness between large and small firms about the evolving use of e-commerce and the Internet in supply chains have been identified (Department of Industry, Tourism and Resources, 2001). Encouragingly, Australian SMEs are increasingly becoming involved in on-line buying and selling activities. In 2004, 39 per cent of SMEs took orders on-line (up from 19 per cent in 2001), while 44 per cent received payments on-line (up from 13 per cent) (Sensis, 2004). Australia's e-commerce sector ranks highly amongst developed countries on most indicators of Internet access and cost and has a strong legal environment and security infrastructure to support e-commerce (Economic Analytical Unit, 2002).

### NEWMONT: E-COMMERCE WITH QUADREM

Newmont acquired Normandy Mining in February 2002, making Newmont Australia the largest gold producer in Australia with an interest in five mining operations. Newmont Australia (together with all of Newmont's major global operations) participates in Quadrem, an on-line business-to-business procurement entity owned by 21 of the world's largest natural resource companies, including Newmont (see [www.quadrem.com](http://www.quadrem.com)).

Quadrem, based in Dallas in the United States, offers many services to Newmont and its suppliers globally. Quadrem's core business is a transaction processing engine that allows the transfer of electronic documents from buyers to suppliers (e.g. purchase orders) and also from suppliers to buyers (e.g. purchase order acknowledgements and invoices). Quadrem maintains standards for each document so buyers and suppliers connect once to the marketplace and are connected to all Quadrem enabled business partners. Quadrem also offers value added services including electronic auctions, electronic tendering and electronic content management.

Most of Newmont Australia's procurement is done locally in Australia. Many mining consumables are sourced from global suppliers, through their local subsidiaries. Newmont encourages suppliers to join Quadrem and has said to suppliers that there will come a time when all their business will be done via e-commerce. Participation in electronic commerce is a criterion in selection of preferred suppliers.

Major benefits can be realised if the information systems of both buyers and suppliers are integrated into Quadrem. Electronic documents flow from one system to another without any data entry. The reduction in rework due to errors is a benefit to both parties. Quadrem standards for orders compel buyers to input high quality orders which results in streamlined processing across the 'procure-to-pay' value chain.

Newmont's smaller suppliers can participate at a reasonable cost through facilities hosted by Quadrem. Orders are picked up at the Quadrem web site and other electronic documents can be generated at Quadrem based on the data in the order. Data still need to be entered into the supplier's system.

Once connected to Newmont through Quadrem, suppliers have the opportunity to promote themselves globally as e-enabled to other members of the electronic marketplace. Most companies recognise the advantages and need little encouragement to become involved with e-processing through Quadrem.

A number of companies have provided suppliers with assistance and encouragement to become e-commerce enabled and link up to their systems. Some provide training. For example, one said they had 'supplier enhancement programs' involving the sharing of information with, and provision of advice to, suppliers.

*One company had just reached the pilot phase stage for the implementation of an e-commerce system which included the approvals process, created purchase orders that were electronically despatched to suppliers, and did receipting of goods and payment. Their systems would grow as suppliers connected. The consolidation of their developing supplier base was linked to the implementation of their e-commerce systems. As part of their tender processes, there was now an expectation that suppliers would be linked into the system. The company was working closely with its suppliers to get them e-commerce enabled, and was keen to ensure small companies were able to implement e-commerce systems.*

The Office for the Information Economy is actively working to promote the uptake of e-commerce by industry, particularly SMEs.<sup>35</sup> Austrade also provides information on e-commerce and the adoption of e-commerce tools in export marketing and transactions.

## **INTERNATIONAL PROJECT BUSINESS**

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E-commerce and the Internet are fast-changing the way the major US engineering, procurement and construction contractors such as Bechtel, Kellogg Brown & Root and Fluor are conducting their global business. Recent consolidation and rationalisation within the engineering sector worldwide is also contributing to global sourcing trends as are reductions in trade barriers and increasing modularisation of process plants.

With the development of global web-based intelligence systems, e-commerce is a pre-requisite to becoming visible to the big engineering houses. Local companies therefore need to embrace e-commerce if they are to become part of supply chains for major projects.

Many Australian companies are succeeding in supplying major projects undertaken locally – often through the matchmaking efforts of the Industry Capability Network. Some, however, may miss out on contracts by not being on global engineering firms' lists of preferred suppliers for global procurements. This can happen in spite of their clearly being competitive and having overseas project experience.

Industry Capability Network Western Australia has been seeking to address the issue of why some Australian companies are not on global supplier lists (Industry Capability Network Western Australia, 2004). It has identified various reasons, including the fact that information on Australian suppliers to Australian projects has not been retained and hence is lost sight of when the global lists have been constructed. In addition, many engineering firms have been looking to consolidate their supplier lists as they develop their web-based systems. As part of its efforts, Industry Capability Network Western Australia is introducing key offshore personnel of several EPC contractors to Australian suppliers who have worked with the EPCs' local affiliates. Their work indicates that EPC contractors are willing to increase the number of suppliers on their emerging web-based supplier systems.

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<sup>35</sup> See [www.dcita.gov.au/ie/ebusiness](http://www.dcita.gov.au/ie/ebusiness).

## **INDUSTRY CAPABILITY NETWORK – WINNING BUSINESS FOR LOCAL INDUSTRY**

Industry Capability Network (ICN) is an Australia-wide network that facilitates business partnerships by helping industry and government buyers identify competitive local supply chain solutions in areas of import replacement and export, and introducing local companies' products and services to buyers. (see [www.icn.org.au](http://www.icn.org.au)).

Industry Capability Network Limited is the coordination office for the ICN national network of offices located in every state and territory of Australia. The ICN offices are independently managed, with a staff of around 80 technical people across all industry sectors. The offices are financially supported by the Australian and state and territory governments.

ICN is in a good position to assist Australian and international buyers identify the capabilities of Australian industry and individual companies with its national database of over 36 000 companies.

While its traditional focus has been on import replacement, a number of the state arms of ICN are looking to help get Australian industry better linked in to global supply chains for major overseas projects and contracts. Various approaches are being trialled.

One notable example in Victoria concerns a major investment in new rolling stock undertaken by transport franchisees, National Express, Yarra Trams and Connex. Contracts were awarded to Siemens, in the case of National Express, and Alstom, in the case of Yarra Trams and Connex. No local content provisions existed in the contracts.

Nevertheless, ICN Victoria worked with Siemens, and then Alstom, to secure significant local industry involvement in the projects. They organised several trade missions to showcase the skills and competitiveness of Australian industry, taking senior executives from thirty Australian companies to Siemens in both Austria and Germany and to Alstom in France. ICN Victoria benefited through funding under the Australian Government's Supplier Access to Major Projects Program and the Victorian Government's Export Program.

These efforts resulted in \$400 million in local involvement – not just for Victorian industry, but also for industry in New South Wales, Queensland and Western Australia – out of a total contract value of approximately \$1 billion. This business has also led to other offshore business for the companies involved. For example, Air International Transit secured contracts to supply air conditioning units to Siemens and Alstom. Innovonics are supplying CCTV security systems to the London Underground Train System and castings are being exported from Austcast in Queensland to Austria.

With the coming into effect of the Australia–United States Free Trade Agreement, ICN Victoria has taken steps to build on Australia's supply chain strengths in the marine and rail components industries, including leading a strategic trade mission into the United States.

If Australian companies are to secure and maintain involvement in global supply chains for projects undertaken in Australia and overseas, they need to demonstrate capabilities beyond delivering competitively priced, quality products to site within tight project schedules. A number of factors take on greater importance, such as:

- sophisticated business systems (including e-commerce capabilities);
- an ability to take on some project risk;
- relationship-building with key players; and
- innovation.

Australian suppliers might find they can compete more effectively by forming joint ventures and alliances to supply a package of expertise, components, plant and equipment (Hatch, 2001).<sup>36</sup>

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<sup>36</sup> See also Deborah Wilson Consulting Services (2002).

## GOVERNMENT PROGRAMS

The Australian Government places importance on attracting productive inward investment. There are also a number of government and government-supported programs to help promote partnerships and links between the multinationals and local industry.

Invest Australia seeks to build on Australia's industry competitive strengths, through its targeted foreign investment attraction program. Its investment promotion, attraction and facilitation efforts are focused on securing projects that fit with the Government's economic and industry development priorities. In recognition of the 'spillover' benefits of foreign investment, Invest Australia has among its priorities the development of clusters and supply chains in certain industries and the development of the national innovation system.<sup>37</sup> Invest Australia works with the Industry Capability Network to ensure that Australia's capital equipment and services capabilities are promoted in the design and development phases of major investment projects.

The Industry Capability Network facilitates business partnerships for the purpose of local supply, access to global supply chains and local business growth. It has an extensive national network of offices (see box, page 61).

Austrade has a worldwide network of offices helping Australian companies win overseas business for their products and services. Both organisations promote Australian expertise and have databases of Australian suppliers.

AusIndustry manages a number of programs on which multinationals have drawn.<sup>38</sup> The Enhanced Project By laws Scheme is aimed at encouraging increased Australian industry participation in major investment projects, both in Australia and overseas, through targeted duty concessions. Project proponents are required to provide and implement an Australian Industry Participation Plan to demonstrate that they intend to provide full, fair and reasonable opportunity to Australian industry to participate in all aspects of the project.

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<sup>37</sup> Government initiatives aimed at catalysing the development of networks and clusters of research and industry include the Cooperative Research Centres Program and the two 'centres of excellence', National ICT Australia and The National Stem Cell Centre (see <http://backingaus.innovation.gov.au>).

<sup>38</sup> See [www.ausindustry.gov.au](http://www.ausindustry.gov.au).

### **INVEST AUSTRALIA\***

Invest Australia is Australia's national inward investment agency, and promotes productive foreign direct investment into Australia to support sustainable industry growth and development. It achieves this by promoting Australia's competitive advantages as an investment destination and actively facilitating investment projects into Australia.

Its efforts in the United States are focused on the Government's high technology priority sectors of ICT, biotechnology and nanotechnology.

Invest Australia facilitates new investment by providing prospective investors with a single contact point within the Australian Government. Through the Major Projects Facilitation service, Invest Australia provides prospective investors with information, advice and support to assist with necessary government approvals.

Through the Strategic Investment Coordination process, there is scope for giving investment incentives to attract to Australia projects with significant net economic and employment benefits that would otherwise have located offshore.

Under the Supported Skills Program, companies that make a significant investment in Australia are allowed to bring out from within the company group key expatriate managerial and specialist employees who are essential to establish operations in Australia.

As well as its promotion, attraction and facilitation efforts aimed at seeking out new investors, Invest Australia cooperates with the States and Territories to assist local affiliates of multinationals to make a case to their parent companies when they are competing on a global basis with other affiliates for new investment. It is well positioned to assist local companies that are making a case for re-investment through its overseas network's links with the head offices of international companies located in Australia, including US companies.

\* See: [www.investaustralia.gov.au](http://www.investaustralia.gov.au)

The Supplier Access to Major Projects program provides funds for specialist consultants to work directly with project developers to identify supply opportunities for capable and competitive Australian companies.

The Pharmaceuticals Partnerships Program (P3) is aimed at increasing R&D activity throughout the entire value chain including biotechnology, originator and generic medicines. It is also aimed at encouraging partnerships and links between multinational firms and local players. P3 will provide A\$150 million over the five years from 1 July 2004 to support more than A\$500 million of new high quality pharmaceutical R&D in Australia. A number of US multinationals in the pharmaceuticals sector are either participating or seeking to participate in the Program.

**AUSTRADE: HELPING EXPORTERS\***

Austrade provides a range of trade-related services for exporters, including the Export Market Development Grants (EMDG) Scheme, assistance through TradeStart, the organisation of trade events, and a range of forms of in-market assistance. It also promotes Australian expertise and capabilities internationally.

Financial assistance is available under the EMDG scheme to encourage small and medium sized Australian businesses to develop export markets.

TradeStart, a national network of export assistance offices, forms a key plank in meeting the Government's target set in 2002 of doubling the number of Australian exporters by 2006. It is a partnership between Austrade, state and territory governments, industry associations and regional development organisations. TradeStart's focus is on helping new exporters on a one-to-one basis.

Austrade and TradeStart offer a package of free services through the New Exporter Development Program (NEDP) which is designed to assist SMEs develop their business overseas and make their first export sale.

Austrade coordinates, promotes and participates in a range of international and local trade events in all major industry sectors. The types of trade events include local seminars for exporters, international trade shows and exhibitions, and trade missions to targeted export markets.

Austrade has expanded its capacity to help Australian exporters – in particular SMEs – identify opportunities and gain market access into the United States, and has been proactively seeking to facilitate small business uptake of trading opportunities arising from the Australia–United States FTA. In particular, it:

- is engaging 30 new export facilitators to provide specialist advice on the US market to Australian exporters – 23 to be located in the United States and seven located in Australia;
- is appointing five business development managers and has established a Selling to Government Office in Washington to pursue government procurement opportunities;
- has expanded its presence in the United States and engaged expert staff to identify particular areas of opportunity;
- has run seminars across Australia to give advice to local businesses about the most effective market entry strategies; and
- has established a database allowing organisations seeking contacts with a view to doing business with the United States to register their interest online.

\* See [www.austrade.gov.au](http://www.austrade.gov.au)

The Government seeks to promote local industry development through its own procurement programs in the area of information and communications technology. The Government's approach is aimed at the generation of substantial industry development outcomes from information and communications technology procurement, particularly SME participation, and encourages multinational engagement with the Australian information and communications technology sector. The objective is to have a vibrant, globally competitive and internationally recognised information and communications technology industry that can take advantage of international opportunities and contribute to economic growth in Australia.<sup>39</sup> EDS Australia (see case study) and other US multinationals in the sector have been supportive of the industry development aspects of the Government's approach to procurement.

Many of the Australian Government's Action Agendas, which have been developed for a number of industries to enable industry and government to work together to realise opportunities and overcome impediments to growth, have identified the importance of global supply chains and developed supply chain strategies for local industries.<sup>40</sup>

Notable is the Heavy Engineering and Infrastructure Action Agenda, the overriding objective of which has been to increase the level of Australian participation in major engineering and infrastructure projects. The Action Agenda has provided a platform that, amongst other things, enables the heavy engineering industry to explore the dynamics of global supply chains for the benefit of Australian SMEs (Department of Industry, Tourism and Resources, 2004). The National Infrastructure & Engineering Forum, an industry-based organisation, was created to monitor the implementation of the Action Agenda's recommendations directed at industry.<sup>41</sup>

The Australian Government is also working to promote and accelerate the uptake of e-commerce tools and practices in recognition of its importance in lifting the productivity and productive capacity of the Australian economy. The Office for the Information Economy administers a number of programs to help promote the take-up of information and communications technology.<sup>42</sup>

State and territory government agencies also undertake targeted foreign investment attraction programs and activities in support of local procurement by multinationals in Australia.

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<sup>39</sup> See [www.dcita.gov.au/ict](http://www.dcita.gov.au/ict).

<sup>40</sup> See [www.industry.gov.au](http://www.industry.gov.au).

<sup>41</sup> See [www.nief.com.au](http://www.nief.com.au).

<sup>42</sup> See [www.dcita.gov.au/ie/business](http://www.dcita.gov.au/ie/business).

**EDS AUSTRALIA GLOBAL PARTNER SOLUTIONS PROGRAM**

EDS Australia is a subsidiary of EDS Corporation, the world's largest independent IT outsourcing company, based in Plano, Texas. IT outsourcing accounts for the majority of EDS Australia's business, although business process outsourcing currently represents the fastest growth area.

EDS Australia actively facilitates the export efforts of Australian IT companies through its Global Partner Solutions program (see [www.gps.eds.net.au](http://www.gps.eds.net.au)). This program reflects its local industry development commitments, made as a result of successfully bidding for government business. This follows EDS' graduation from an earlier Australian Government initiative, the Partnerships for Development program. The States have put similar programs in place.

The aim of the Global Partner Solutions program is to support local information, communications and technology SMEs by helping them with the marketing of their products and services throughout the EDS global network of clients and industries. The program provides these companies with an ability to generate export income, to expand their client base and to raise their profile in the global marketplace. To date, the program has brought more than A\$100 million in export sales growth to these companies. For EDS, the program introduces innovative and differentiated solutions to broaden and complement its portfolio of service offerings.

Some of the program successes include:

- **Maxamine**, a South Australian company which has signed a multi-million dollar license and reseller agreement with EDS USA for their enterprise wide 'Web Analytics' software, both for internal EDS use and for facilitating EDS' e-business sales.
- **NeoProducts**, a Victorian company producing touch screen data kiosks, has, jointly with EDS, installed 10 000 'self service' kiosks for a major UK Government department.
- **Proxima Technology**, a New South Wales-based company which has delivered significant operational and cost reduction benefits with their 'service level management' software to major banks, government departments and telecommunications companies in Australia, Europe and the United States – and to a number of other key EDS accounts globally.
- **Tower Software**, a Canberra-based company which has won a A\$30 million plus contract for the installation of TRIM electronic document and records management software on 300 000 desktops for a major US defence agency, as part of EDS' multi-billion dollar outsourcing contract.

EDS has elected to continue the GPS program beyond its current 'sunset' this year, as part of the voluntary industry development initiatives sought by the Australian Government under its current IT procurement policies.



## IMPLICATIONS

The Australia–United States Free Trade Agreement brings the prospect of expanded business activities by the US multinationals in Australia and, for many, a stronger export performance. The FTA should also lead to more direct investment from the United States as well as increased interest in the US market on the part of Australian investors. Opportunities for US companies, as well as companies from third countries, stand to be heightened should regional and other bilateral FTAs – notably with ASEAN, Malaysia and China – come to fruition.

This study has found that many local companies and institutions, including SMEs, have developed successful business with the multinationals. Many have also been able to develop export business through the overseas networks and connections of the multinationals.

As well as providing direct business opportunities for their suppliers, multinationals can be a force for bringing about the improved competitiveness of suppliers. This can lead to business openings with other companies, both in Australia and overseas.

The survey results show that the multinationals help their suppliers to participate in their procurement in a diverse set of ways. Many have developed partnerships and long term relationships with their key suppliers. Some multinationals are also prepared to assist their suppliers improve their operational processes and procedures. Such assistance can be leveraged by suppliers in their other business activities, both here and overseas with their other existing customers, with their potential customers and with their own suppliers.

Some important changes are taking place in the way the multinationals are conducting their business, which present both challenges and opportunities for Australian suppliers.

Most notably, e-commerce and competitive forces are leading to many multinational corporations looking to, and implementing, global or regional purchasing arrangements.

With the multinationals increasingly turning towards e-commerce, local companies also need e-commerce capabilities. The multinationals are increasingly expecting their suppliers to bid for contracts by electronic means, as well as to engage in electronic payments systems. Suppliers need to work hard to get themselves on global engineering firms' lists of preferred suppliers for global procurements, particularly for international projects.

Ongoing business opportunities can arise if local suppliers are able to gain pre-qualification or 'preferred supplier' status for business with the multinationals and their overseas affiliates.

An increasing tendency to focus on core competencies is leading many US multinationals in Australia to look to local outsourcing of a range of services functions, leading to opportunities for Australian service providers.

In the face of the increasing capabilities and competitiveness of businesses in Asia, local companies need to constantly sharpen their competitiveness and move up the 'value chain' if they are to continue to secure business with the multinationals.

The multinationals can be demanding customers. To secure their business generally necessitates good capabilities, continuous improvement and cost competitiveness.

Characteristics that can set successful companies apart from other suppliers include innovativeness, responsiveness, focusing on core areas of expertise and skill sets, keeping up with technology, and benchmarking against competitors here and overseas. Local suppliers also need to be prepared to take on a share of the risks if they are to retain and extend their business dealings with the multinationals.

Australia and the United States have entered a new era in their trade and investment relationship. The bilateral free trade agreement has opened up new opportunities for large and small Australian companies. The Australian Government has committed additional resources to help exporters take advantage of these new opportunities.

This study has focused on working with established multinational companies. The multinationals will play a large part in the expansion of trade and investment between Australia and the United States under the favourable environment created by the free trade agreement. Doing business with them can be demanding, but also rewarding for those Australian companies keen to grow their businesses.

## APPENDIX

## APPENDIX TABLES

Table 1

## Multinationals Interviewed

US companies in list of top 200 foreign companies in Australia <sup>a</sup>	
3M Australia	Hewlett-Packard Australia
Alcoa World Alumina Australia	Holden
Apache Energy	Honeywell Holdings
Arnott's Biscuits Holdings	IBM Australia
Australia Meat Holdings	John Deere Australia/New Zealand
Baxter Healthcare	Johnson & Johnson
Bechtel Australia	Kimberly-Clark Australia
Boeing Australia	Kraft Foods (Australia)
Bristol-Myers Squibb Australia	Manpower Services (Australia)
Cargill Australia	Masterfoods Australia New Zealand
Caterpillar of Australia	McDonald's Australia Holdings
Cisco Systems Australia	MCI Worldcom Australia
Citigroup Australia	Merck Sharp & Dohme (Australia)
CMC (Australia)	Millennium Inorganic Chemicals
CSC Australia	Newmont Australia
Cummins Engine Company	Owens-Illinois (Australia)
Dow Chemical (Australia)	PACCAR Australia
DuPont (Australia)	Pfizer Australia
EDS (Australia)	Philip Morris (Australia)
Eli Lilly Australia	Sun Microsystems Australia
ExxonMobil Australia	Tyco Services
GE Australia & New Zealand	Wyeth Australia
Hardy Wine Company	Yum! Restaurants Australia
Heinz Wattie's	
Other large US multinationals in Australia	Australian multinationals
Abbott Australasia	Ancor
ChevronTexaco Australia	BHP Billiton
Collins Foods Group	Boral
Dunavant Enterprises	Bovis Lend Lease
Lucent Technologies Australia	Cochlear
Monroe Australia	Computershare
Sara Lee (Household & Body Care)	Foster's Group
	Mincom
	Orica
	ResMed
	Rinker Group

Note: a. BRW, *The Top 200*, Feb 12-18 2004.

Table 2

**Free Trade Agreement Coalition Members**

**US multinationals interviewed whose parent corporations are members of the American-Australian Free Trade Agreement Coalition**

3M Australia	ExxonMobil Australia
Alcoa World Alumina Australia	GE Australia & New Zealand
Baxter Healthcare	Hewlett-Packard Australia
Bechtel Australia	Holden
Boeing Australia	IBM Australia
Cargill Australia	John Deere Australia/New Zealand
Caterpillar of Australia	Masterfoods Australia New Zealand
ChevronTexaco Australia	Merck Sharp & Dohme (Australia)
Citigroup Australia	PACCAR Australia
DuPont (Australia)	Pfizer Australia
EDS (Australia)	Sun Microsystems Australia
Eli Lilly Australia	

**Australian multinationals interviewed who are – or whose US affiliates are – members of the American-Australian Free Trade Agreement Coalition**

BHP Billiton	Orica
Rinker Group	Computershare
Foster's Group	Resmed

Table 3  
**US Multinationals Survey Results**

**1. Mandates**

1. Do you have a 'mandate' (responsibilities beyond Australia)?		2. Has your mandate changed substantially over the past five years or so?		3. Productions/sales mandate			
				Aust/NZ/ Sth Pacific	South-East Asia	Asia Pacific	Global
50 (yes)	4 (no)	18 (yes)	36 (no)	23	3	8	6
4. R&D mandate		5. Other services mandate					
Aust/NZ/ Sth Pacific	South-East Asia	Asia Pacific	Global	Aust/NZ/ Sth Pacific	South-East Asia	Asia Pacific	Global
8	2	6	6	5	3	19	5

Table 3 (cont.)

2. Exports

1. Do you export?	39 (yes) 15 (no)
-------------------	---------------------

Exporting businesses

	2. How important are exports to your business? Please express as a percentage of your total revenues	3. Please identify your major export markets:	4. Have exports become more important for your business over the past five or so years?	5. Do you expect them to become more important in the coming five years?
Scale	1 = 0-10% 2 = 10-20% 3 = 20-30% 4 = 30-40% 5 = 40-50% 6 = >50%	1 = NZ/Sth Pacific 2 = South-East Asia 3 = North Asia 4 = United States 5 = Other regions	1 = Markedly less important 2 = Less important 3 = No Change 4 = More important 5 = Markedly more important	1 = Markedly less important 2 = Less important 3 = No Change 4 = More important 5 = Markedly more important
1	16	24	1	1
2	9	29	2	0
3	3	22	15	18
4	1	14	20	17
5	1	18	1	0
6	9			
Total no. of respondents	39	39	39	36

Table 3 (cont.)

**3. Research and Development**

	1. What proportion of your total revenues do you spend on R&D?	2. Do you conduct R&D in Australia that results in product sales into overseas markets?	3. Do you do R&D with other companies in Australia?	4. Do you do R&D with Cooperative Research Centres, CSIRO, or universities?
<b>Scale</b>	1 = <1% 2 = 1-2% 3 = 2-3% 4 = 3-4% 5 = 4-5% 6 = >5%			
1	21	36 (yes) 18 (no)	30 (yes) 24 (no)	12 (CSIRO) 17 (unis.) 6 (CRCs)
2	9			
3	3			
4	7			
5	3			
6	6			
Total no. of respondents	49	54	54	54

Table 3 (cont.)

4. Procurement

	1. Has local outsourcing of services become more significant for your business over the past five or so years?	2. Do you expect your local outsourcing of services to become more significant over the coming five years?	3. Have you come to rely more on local materials/goods suppliers over the past five years?	4. Do you expect your procurement of local materials/goods to become more significant over the coming five years?
	<b>Scale</b> 1 = Markedly less important 2 = Less important 3 = No change 4 = More important 5 = Markedly more important	1 = Markedly less important 2 = Less important 3 = No change 4 = More important 5 = Markedly more important	1 = Less 2 = No/little change 3 = More	1 = Markedly less important 2 = Less important 3 = No change 4 = More important 5 = Markedly more important
1	0	0	9	2
2	0	1	36	5
3	29	27	9	38
4	21	23		9
5	2	1		0
Total no. of respondents	52	52	54	52

Table 3 (cont.)

4. Procurement (cont.)

	5. Is the presence of capable suppliers in close proximity to your operations important to your business?	6. In your experience, have the capabilities of local businesses improved over the past five years?	7. Can you give an example of where you have helped one of your local suppliers export?	8. Have you gone into export together with any of your local suppliers?	9. Have you established e-commerce systems to undertake procurement?
<b>Scale</b>	1 = Unimportant 2 = Moderately important 3 = Important 4 = Very important 5 = Crucial				
1	8	40 (yes) 8 (no)	27 (yes) 27 (no)	8 (Yes) 45 (no)	39 (yes) 15 (no)
2	9				
3	18				
4	8				
5	7				
Total no. of respondents	50	48	54	53	54



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