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For carmakers, end of the road is not far away

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Top 10 selling cars

Model (ranked by cost)	Made	5-year cost*
TOYOTA CAMRY	AUSTRALIA	$56,378.92
HOLDEN COMMODORE	AUSTRALIA	$55,081.59
MAZDA 3	IMPORT	$45,880.39
HOLDEN CRUZE	AUSTRALIA	$44,882.34
VOLKSWAGEN GOLF	IMPORT	$43,355.42
HYUNDAI i30	IMPORT	$42,997.73
TOYOTO COROLLA	IMPORT	$42,704.07
FORD FOCUS	IMPORT	$42,121.50
MAZDA 2	IMPORT	$37,599.64
TOYOTA YARIS	IMPORT	$35,156.66

* 5-year cost includes purchase price plus depreciation, insurance, fuel and maintenance costs

Source: RACQ (2013), drive.com.au

Source: TheAustralian

THE Australian car industry is waiting around to die. With every passing day, analysing its problems becomes less a diagnosis and more a post-mortem. The only question is whether anyone has the courage to sign the death certificate.

The industry's immediate crisis reflects the difficulties confronting our manufacturing industries raised to a power of ten. Under pressure from the resource boom, structural weaknesses that previously led to slow decline have morphed into a sea of red ink.

The numbers are stark. Constrained by the high exchange rate and by ever more intense international competition, the prices Australian manufacturers receive for their products increased by just over 1 per cent a year from 2003-04 to now. That is one-third the rate of producer price inflation for the whole market sector (which covers the commercial, i.e. non-government, parts of the economy) and not even one-tenth the rate of increase in prices that mining has enjoyed. Manufacturing wages, as measured in the national accounts, rose at virtually the same rate as for the entire market sector, and even exceeded wage growth in mining.

With manufacturing wages increasing more than twice as rapidly as labour productivity, real unit labour costs grew while profitability collapsed. Overall, for the market sector, the rate of return on capital rose by about half a per cent a year; for manufacturing, it fell by 5.5 per cent a year. The surprise is not that manufacturing is in strife but that any of it remains.

That it is does largely reflects the durability of its assets. If manufacturers could magically transform their plant and equipment into mines, they would have done so long ago; it hardly needs to be said that they cannot. Yes, hours worked declined by 1 per cent a year; but with manufacturing's share of market sector output falling from 19 per cent in 1999-2000 to 13.6 per cent a decade later, firms have been left with structurally high labour costs and production levels far too low to reap economies of scale.

Nowhere is that clearer than in the car industry. And the reality is that there is no prospect of our car assemblers ever achieving the scale economies that might allow them to absorb the wage penalty. Australia's share of world car production has declined from 1.7 per cent in 1974 to less than one-third of 1 per cent last year. With barely 200,000 cars rolling off our assembly lines, the annual output is not even 30 per cent of Thailand's; an atomic microscope is needed to spot it compared with China's 15 million. Yet the economies of scale dictate annual production runs of at least 250,000 - and that is per plant, and hence far above the industry's total output.

To make matters worse, the environment in which the car industry operates has been transformed in irreversible ways. Not only have consumer preferences moved away from the standard sedan, which has been the industry's mainstay, but lower tariffs, declining transport costs and a high exchange rate have allowed Australian consumers access to the best the world has to offer. As that has occurred, more exacting standards have become the norm, making the Australian industry's conventional products seem uninspiring, if not positively bland.

Rising consumer expectations are a trapdoor: movement only goes one way. That its products don't offer great value makes it all the more difficult for the industry to adjust to that shift. A survey by the RACQ shows the total five-year running costs of an imported Mazda 6 are 16 per cent less than those of a Ford Falcon. But if resale prices now decline 35 per cent more rapidly for Falcons than for Mazdas, it is not simply because of differences in running costs. Rather, it reflects consumers' perceptions that the Australian industry's days are numbered.

Nor is that reckoning far off. The phasing in of the Euro 5 and 6 emissions standards, due to be completed by 2018, will impose further, substantial costs for redesign and retooling; to believe the assemblers' parents will meekly take the hit is delusional. To even contemplate remaining in Australia beyond that point, the firms will demand open-ended commitments to ever-rising subsidies.

Those subsidies are already proving fiscally and politically poisonous. Over the past decade, the industry has received some $19 billion in assistance, an amount equivalent to nearly $30,000 for each of its 50,000 workers each and every year. But even that is an underestimate as it excludes the effects of a host of protectionist measures, including preferential government procurement, restrictions on importing secondhand cars, and unique Australian technical standards. Keeping the industry alive could require retaining all those measures while ramping the other forms of assistance up by more than 50 per cent in exchange for ever shrinking production volumes.

The industry, with energetic backing from the unions, argues that assistance is justified by claimed skill and other benefits to the economy as a whole. Those claims make no sense. Far from being especially skill-intensive, the industry's design capacities pale compared with the range and sheer complexities of the technical challenges dealt with by Australia's major miners. That runs against the myth, endemic in the ALP and the ACTU, that mining is as simple as digging dirt out of the ground, but it is Australian mining, not the car industry, that is pushing the frontier in areas such as complex data analysis, computer aided design, visualisation and robotics.

No surprise, then, that when the RAND Corporation surveyed the Australian supply of the skills needed for the next-generation submarine, its 250-page report did not mention the car industry once - despite so much of that industry being next door to the announced site for the submarine project. Instead, it largely found those skills in the engineering contractors that serve our major onshore and offshore resource projects.

All that is surely obvious: for were the industry a repository of advanced skills, its workers would face few difficulties in shifting to other employers. Rather than having capabilities highly prized in the economy as a whole, nearly half the industry's workers have no post-school qualifications whatsoever. The local labour markets in which it operates are anything but Silicon Valley: they have low rates of school completion, families for whom English is not a first language, and compound sources of disadvantage. And while many of its workers have trained on the job, the skills they have acquired are rarely readily transferred elsewhere.

That is why the adjustment process is so painful. Merely in the past two years, for example, the direct employment associated with GM Holden's South Australian operation at Elizabeth has declined by a third. The results are visible in an effective unemployment rate more than twice the national average. It would be nice to think those are merely transitional problems, but life isn't like that, especially in a country with high minimum wages. And when a full shutdown occurs, the consequences for communities will be grim, as falling property prices lock families into places with few jobs and even fewer prospects.

Yet pouring more subsidies into the industry is no answer. If the goal is to help the communities at risk, it is hard to imagine a less efficient way of doing so than paying for all the inputs consumed in making cars to assemble vehicles people don't want to buy.

And that inefficiency is compounded by futility. Already, the subsidies granted in the past five years have gone largely into wage increases. Sure, the unions know that only accelerates the shrinkage, but they also know high wages mean high redundancy payouts when the end comes, and that those payments will be underwritten by taxpayers.

Ultimately, this is the precipice to which past follies have led. For there is a brute fact the Australian protectionists understood: you cannot both cripple local producers with an industrial relations system incapable of withstanding international competition and allow consumers untrammelled access to the best the world has to offer. Faced with that choice, they had no hesitation in sacrificing consumers, and compromising our prosperity to boot, for the sake of regulating the labour market.

Kevin Rudd and Julia Gillard wanted to have their cake and eat it. They imposed a 19th-century industrial relations system on a 21st-century market in the midst of enormous structural change. When the consequences came home to roost, they threw taxpayers' money they didn't have at a problem they couldn't solve, while making promises they could never keep. As reality bites, local communities will pay the price.