Australian Government
Productivity Commission

PRODUCTIVITY COMMISSION

INQUIRY INTO AUSTRALIA'S EXPORT CREDIT ARRANGEMENTS

MS P. SCOTT, Presiding Commissioner
DR W. MUNDY, Commissioner

TRANSCRIPT OF PROCEEDINGS

AT SYDNEY ON MONDAY, 26 MARCH 2012, AT 9.27 AM

Continued from 23/3/12 in Perth

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MS SCOTT: Good morning, ladies and gentlemen, welcome to today's hearings. My name is Patricia Scott, I'm the presiding commissioner for this public inquiry and I'm pleased to say that I'm joined by Dr Warren Mundy, who is a commissioner at the Productivity Commission.

We commenced our hearings last Friday in Perth and tomorrow we continue our hearing process in Canberra. The purpose of this round of hearings is to facilitate public scrutiny of the commission's work and to get comment and feedback on our draft report. After the hearings we will be working towards completing a final report to government in May, having considered all the evidence presented at the hearings and in submissions as well as the information we gained through consultations. Participants at this inquiry will automatically receive a copy of the final report once it's released by the government. The government determines the release date.

We would like to conduct all hearings in a reasonably informal manner but I do remind participants that a full transcript is being taken, and for this reason comments from the floor will not be taken but at the end of proceedings for this day I will provide an opportunity for any person wishing to come forward to make a brief comment on the record. So if you've got the internal fortitude to hang around all day and you feel compelled to say something you can do so at the end of the day on the record. Participants are not required to take an oath but should be truthful in their remarks. Participants are welcome to comment on the issues raised in other submissions or in any testimony you hear today. A transcript will be made available to participants from our web site following the hearings. It normally takes two days or so for the transcript to be available. Submissions are also available on the web site.

In the unlikely event of the fire alarms going off we are to get downstairs as quickly as we can and then to turn right at the front door and assemble near the Westpac Bank which is on the corner of Clarence and Market Street. Now, while we're having microphones in front of us and we're having a transcription service, this room is not amplified. So if at some stage during the course of the hearings you find that Warren and myself start to become very softly spoken or you can't hear the testimony of the people at the table can you please alert Annie or Anna or myself at the end of a session. So Anna and Annie - they're going to put their hands up right now. Thank you very much. The reason why I mention it is that often when people are in front of microphones they become quite softly spoken, and it really is important that you hear.

If you haven't already turned your phone to silent or turned it off could I encourage you to think about doing that now, please. If you would like to talk to others in this hearing room - you've heard something that you think is pretty sensational and you'd like to chat about it, could you think about doing that outside, because again because there's no amplification that can mean that other people won't be able to hear the testimony. We will be taking a break for morning tea and for lunch and we hope to finish the day at around 4.30, maybe a little earlier. The bathrooms - head out the door, the women's one is sort of around to the right, got to keep going around a few corners, and the gents' is to the right more directly, follow a few signs.

I now invite Mark Langbein to come forward please, from the Aircraft Support Industries. Just before we start. One last thing, is there any representatives of the press here today? No? Okay. Well, Mark, thank you for coming along. For the purposes of the record could you state your name in full and the name of your company and then would you like to make a short opening statement?

MR LANGBEIN (ASI): My name is Mark Langbein. I'm the managing director of Aircraft Support Industries. Aircraft Support Industries is what you call a - I would say a typical SME. We operate our business out of Manly here in New South Wales and we are a global company working in, I think, every continent in the world.

DR MUNDY: Just for the record I should at this stage declare that I'm the deputy chair of Air Services Australia but I do not believe that ASI has done any work in recent times that ASI has any commercial involvement with Air Services.

MR LANGBEIN (ASI): That's true.

DR MUNDY: I certainly don't recall any, and quite frankly, you may have and I wouldn't have known about it anyway. Mark, could you just give us an outline of the sort of work that you do for your customers?

MR LANGBEIN (ASI): Aircraft Support Industries is a designer and builder of aircraft maintenance facilities. I believe we're the only company in the world that specialises in this business. Projects typically can range from 10 million to hundreds of millions. We work with major airlines. We have done work, obviously, for Qantas, Singapore Airlines, Asiana; currently we're doing Vietnam Airlines, we're working in Russia; basically, as I said, globally. I don't think or I don't believe that we have a competitor globally that does the same work as us.

DR MUNDY: So you basically do the fit-out rather than the physical fabrication of the hanger itself?

MR LANGBEIN (ASI): We do everything from start to finish: design and build, in some cases arrange finance also, basically A to Z.

DR MUNDY: Okay. We've got some data which is publicly available with respect to the transactions you've done with EFIC. They seem to be quite varied in the scope of - the financial size. I mean there's one - there are a couple of a few hundred thousand dollars, less than a million, and there's one at eight and a half. What's the difference between sort of the two ends of the spectrum?

MR LANGBEIN (ASI): Well, basically, the one million is obviously a - roughly a $20 million project and eight million is an 80 million project. They're basically related to performance - - -

DR MUNDY: 10 to one, is that the - - -

MR LANGBEIN: Most of our work with EFIC, or helped with EFIC, has been from performance bonds. You will appreciate that we are actually a relatively small company. We have 16 people in the office in Sydney. We have offices in Singapore and the Middle East that basically are - and project teams on various projects. The majority obviously of the staff are Australians. Basically being a small company some of the competitors we have - like the one recently in Russia was a company called HOCHTIEF, that's the kind of competitors we're up against, but we secure the projects because of our expertise. Ironically I went round - we've done many projects around the world and when Qantas looked a building facilities here they travelled around the world globally looking at facilities and didn't realise they had the expert in the backyard.

DR MUNDY: The company, HOCHTIEF, you mentioned, it's one of the major shareholders of Leightons is it?

MR LANGBEIN (ASI): That's correct, yes.

DR MUNDY: In your submission you indicate that EFIC helped level the playing field. Can you just give us a sense in which, I guess, the playing field was tilted against you. Was it just a scale issue or was it more than that?

MR LANGBEIN (ASI): No, basically it's governmental more than anything. Recently tendered a project for Ethiopian Airlines, for example. We didn't secure that. That was awarded to the Chinese in the end. But if we basically went into a project like that and didn't have some governmental support, whether it's through EFIC or even Austrade et cetera, you don't really stand a very good chance of securing projects. We have seen this also in Russia. It's a very difficult country to go into. To be able to say that you get support from organisations like EFIC is - well, it's very commendable, they highly regard it. There are a few other countries that have similar programs, one that springs to mind is Canada, but many of our - I wouldn't say competitors but construction companies that we work or tender against don't have support from governments, like the French, for example. So they're all centred to - Australian small businesses, I think it's a fantastic idea that they get supported.

DR MUNDY: I presume you're aware that EFIC operates two accounts, a commercial account and a national interest account. I see that in fact two transactions, one in Singapore and the other one in Jordan, were done on the national interest account. Are you able to give us a sense of why there was a national interest component in those two transactions?

MR LANGBEIN (ASI): No, I'm sorry, I can't, no.

DR MUNDY: So that was just - you were dealing with EFIC and there was - did you have any sense at the time that those two transactions were being treated differently by EFIC?

MR LANGBEIN (ASI): Actually, no.

DR MUNDY: Okay I won't ask you any more about that then.

MS SCOTT: I'm going to take this in a different direction. Could you talk about the relationship you have with the financial sector and why in particular you find EFIC support so necessary for your business? You're a long-established company and a successful company. Could you talk about how your success is viewed in the financial sector?

MR LANGBEIN (ASI): Well, basically it depends on the size, as I said, of the projects but for us to tie up working capital we don't have an opportunity to expand. As you're probably aware you used to be able to get bonding through insurance companies et cetera, banks obviously were very stringent on doing it. Construction projects generally require a lot of capital. Predominantly the clients we have are governments or airlines, usually obviously good payers. They might be slow but they're good.

DR MUNDY: Not always.

MR LANGBEIN (ASI): As you say. There's some countries that we look at where EFIC say, "No, we're not interested in looking at those countries." I think they've got sort of a rating of one to seven. Like we looked at a project in Nepal, for example, but it was definitely a no-no; likewise, with Ethiopia, that was also no; then we went to one for Angola and that viewed as a possibility.

MS SCOTT: You've been to your bank before you go to EFIC. What's the sort of relationship that you have now built up with EFIC?

MR LANGBEIN (ASI): Well, it's a case by case basis. I think we've used EFIC probably in my 20-odd years four times: initially in Hainan in China, and recently Abu Dhabi for a company called ADAT, and Vietnam.

MS SCOTT: Okay. We've got a couple of Singapore transactions too on our list.

MR LANGBEIN (ASI): Yes.

MS SCOTT: For transactions - let's say your firm was doing business in New Zealand or somewhere like that, or domestic activity. Would your bank be willing - - -

MR LANGBEIN (ASI): More inclined to help.

MS SCOTT: More inclined to help?

MR LANGBEIN (ASI): Yes.

MS SCOTT: So it's just the risks associated with Jordan, UAE and Vietnam?

MR LANGBEIN (ASI): Yes, in essence. As you know our local banks don't have offices in those locations, which makes it a lot more difficult.

MS SCOTT: What about Singapore? I mean you might - I would think at first blush that Singapore would not represent a inherently large risk?

MR LANGBEIN (ASI): No, Singapore is definitely not a large risk. I think at that particular time for that contract we also had quite a few other projects going and cash flows were, well, of prime importance obviously to make sure the company had enough liquidity to keep trading and growing.

MS SCOTT: Yes. Given that you have projects that are $800 million and so on, is the long-term prospect for your company to in fact become listed as a means to obtain the capital that you need?

MR LANGBEIN (ASI): It's sad but that's sort of what you end up having to do. I'm sort of a bit against that personally, of course, but it's very difficult to - I watched a lot of the larger companies like - you mentioned Leightons before. They obviously don't have any trouble putting up bonds for projects, and poor little SMEs like us sort of get a bit squeezed because a project could be large and yet to get the capacity to bond it is very, very difficult. Quite often you have to also put in a tender bond also. I've got people in Shanghai today, actually, doing a presentation to Boeing but we had to put up a tender bond to even tender that project. Then if you get that the obviously you've got performance bonds et cetera as well.

MS SCOTT: Does the availability of support from EFIC mean that you can delay thinking about going public?

MR LANGBEIN (ASI): No.

MS SCOTT: Okay.

MR LANGBEIN (ASI): No, we are looking at other avenues also, as I say. We can't keep running to EFIC. But I think you probably appreciate also that as your business grows you're on that big wheel that has got to keep expanding. You can't stay still otherwise you basically sink. It's a vicious circle. As I said, now we see projects like for Saudi Arabian Airlines recently come up, the project was 1.2 billion. The competitor was Leightons on that project. They're in a consortium. They become mammoth-sized projects.

That one we probably wouldn't normally talk to EFIC about because we would have to work with a large contractor over there, which we are, but then there are other projects - like, we are currently working on a project for a very large airship hangar for Northrop in Melbourne, Florida. That project is worth around about the $100 million mark, but it is using - once again we couldn't physically bond that by ourselves, we'd need help from someone like EFIC. We've got technology to actually build a facility like that that they don't have in the States. It's obviously a military based program, so there's a lot of synergies between the Department of Defence and what we're doing as well.

MS SCOTT: Thank you. Mark, one of the things that you have objected to in our draft report, and one of the things we are keen to get comment on, is the idea of a cap of $25 million of turnover as the basis for EFIC's attention for support. You didn't agree with the $25 million figure. Do you think there should be any limitation at all, and if you do think there should be a limitation, what sort of size company do you think we should consider in our deliberations?

MR LANGBEIN (ASI): Well, the difficult part I have with this is, like being a design builder contractor, as I said you can have very large contracts. You can have a $500 million contract one year, and next year you're back down to 20 or 30 million dollar projects. I can understand a cap of around about 25 million if you're a manufacturing type organisation, probably even employ quite a lot more people than we employ. So for us I think it's quite unique. It should be based more on the industry rather than just putting a cap overall.

MS SCOTT: Okay. You said you thought we were wrong in the draft report about suggesting that three might be a point where there's a reconsideration about whether a firm should get a fourth line of support, or a fifth or sixth, and on the other hand you just said in your testimony you can't always go back to EFIC for every deal or forever. We were keen to get across the sense that this is about some support but not endless support. What's the right number of transactions in your mind?

MR LANGBEIN (ASI): I think once again it's not the amount of transaction, I suppose it's watching the company to see where the company is growing and expanding, more than the amount of transactions. If I look from the time when EFIC first supported us in China back in the 90s until today, and how our business has expanded, it's substantial, but we couldn't have actually done that without EFIC. It does continue to expand. Eventually we'll get to the point where obviously we won't require funding.

DR MUNDY: How much of your business is roughly either in value or in number of transactions or both does EFIC cover?

MR LANGBEIN (ASI): I'd say 50 per cent. I'd stress though it is only bonding that we look at.

DR MUNDY: Yes, I appreciate that. I guess what our concern is that we're trying to construct a transparent framework but which the government as the owner of EFIC can make sure that there isn't essentially lazy practices. As you say, you don't want to go back to EFIC for everything, and what concerns us, what we're trying to put in place is an arrangement so the government can see clearly that in fact that's not what's happening. It's a governance notion as much as everything, because what we don't want is a relationship of dependency that persists. As you say, you'll grow to the stage at which you're out of that.

But on the other hand we don't want to construct an arrangement which is so intrusive that basically some bureaucrat from the Department of Finance is ticking off every transaction that EFIC enters into. That's what we're trying to achieve with that. Do you have any sense of how we might try and think through that issue?

MR LANGBEIN (ASI): For me I think EFIC's support should be more around SMEs. I have heard and read, obviously, about certain transactions and companies I don't understand why they're getting support, to be honest. But I also know a lot of companies that do and have benefited using EFIC.

DR MUNDY: Obviously the nature of your business is that you have large cash flows because you're a designer contractor with a relatively small staff - and I'm not just talking in the hangar, the aviation space here - but more generally how many companies in Australia would you say have - they might not necessarily be building hangars - but have this similar model on which they're selling these sorts of services overseas, and are they typically the sort of size of your company perhaps, or twice the size, or are they basically a Leightons and the Cloughs of the world?

MR LANGBEIN (ASI): Yes, well, it seems to be more the large ones we hear about, but then there's obviously other ones we hear about for agriculture, for example, that seem to be very beneficial. Some of the industries that we do come across are fantastic that do get the support. As I say, I don't understand the support for the large multinationals. For us also you've got to understand it's quite unusual that you're a company working 99 per cent internationally as well.

DR MUNDY: There are actually a few aviation companies in Australia that do exactly that. I'm just interested in the process that you go through with EFIC. You get a new transaction, is your first act to go and see the bank, or have you got to the stage now where the bank - you know it's a pointless call?

MR LANGBEIN (ASI): No, well, what we are doing currently is we're actually starting to move to a more international banking scene. We're starting to talk more to, like, Hongkong and Shanghai Bank, Standard Chartered et cetera that are more global players. I believe that we'll get more support by doing that.

DR MUNDY: A number of the Australian banks, particularly the ANZ in the submission they have made to the review that Ken Henry is doing for the government on Australia's Future in Asia, have actually indicated that their primary role driver of their corporate development, if you like, is to set up a business bank in Asia essentially to help Australian companies. If you wander around Jakarta or you wander around Hanoi, there's an awful lot of Australian banks around the place. Do you see over time the Australian banks have become more interested in these sorts of transactions, or is it more that the major foreign banks who have a presence in Australia are becoming more interested in businesses like yours?

MR LANGBEIN (ASI): I think it's a bit of both actually. The international banks are approaching us but also banks like National Australia Bank and ANZ. As you said, you do notice ANZ are very strong, especially in Vietnam, the Philippines, Indonesia. I'm sure we can get support from them over there as well.

MS SCOTT: How many times has your bank said no to your request for performance bonds or tender bonds?

MR LANGBEIN (ASI): Basically they want 100 per cent collateral, that's what they want. They will say yes but you want 10 million, you put 10 million and lock it up. So that's what sort of destroys your cash flow. Mind you, with EFIC they still have - basically you sign everything over to them anyway and it's still in essence the same scenario if anything went wrong, but yes, it's basically keeping the company with enough financial strength to go through a project.

DR MUNDY: So EFIC still requires collateral, but it doesn't require cash, is that the difference, or it doesn't require as much?

MR LANGBEIN (ASI): No, what particularly - what has happened in the last few transactions is - well, the last two I can think of, Vietnam and Abu Dhabi, is as we have received progress payments they've retained a percentage of cash until we get to the point of - I'm not quite sure what the percentage is but I think it's pushing towards 50 per cent. So if we've got an $8 million facility they hold four million.

MR ....: 70 per cent.

MR LANGBEIN (ASI): 70 per cent, so it's even more, yes.

DR MUNDY: But they take it as the progress payments come in?

MR LANGBEIN (ASI): Yes.

MS SCOTT: Well, I think that's all the questions we have, Mark. Thank you very much for coming along today and thank you very much for making a submission. We appreciate that.

MR LANGBEIN (ASI): Okay, thank you.

MS SCOTT: I now call to the table Jubilee Australia, please.

MS POLCE (JA): Thank you for the invitation to appear today.

MS SCOTT: Just before you go ahead could you just, for the purposes of the transcript, state your full name and your organisation, please?

MS POLCE (JA): My name is Carmelan Polce. I am the deputy director of Jubilee Australia. Jubilee Australia is an independent non-profit research and advocacy organisation established in 2001. Our work draws attention to the policies of government and practices of business that impede the alleviation of long-term poverty, particularly in the Asia Pacific. We have been advocating for reforms to the Australian export credit policy for more than eight years.

MS SCOTT: Thank you very much. Thank you also for your two submissions.

MS POLCE (JA): Should I make my comments?

MS SCOTT: Yes, please.

MS POLCE (JA): Okay, thanks. Thank you. We believe that the commission's inquiry is a considerable step forward in the national assessment of the purpose, methods and impacts of EFIC. We believe the inquiry will generate momentum for reforms that will make export credit arrangements in Australia more responsible and accountable, more aligned with Australia's domestic and international obligations and focused on serving the interests of Australian taxpayers. Jubilee Australia applauds the commission for the reforms and recommendations in the draft report, even as we believe many do not go far enough. Our submission included comments on a broad range of matters. However, my comments today will just focus on the three matters that are of sort of most importance to us. Those are the national interest account, the Freedom of Information Act exemption and the make-up of the EFIC governing board.

Firstly, the national interest account. Jubilee is pleased that in the draft report the commission has challenged the rationale of the EFIC national interest account. We believe that the rationale for the national interest account is flawed. Australian taxpayers are told that in their interest Commonwealth funds are to be appropriated from the budget and used to assist a small number of Australian private corporations to win export contracts. In many cases EFIC assists Australian companies to participate in projects considered excessively risky by private financiers. Any substantive information used to justify this decision, however, is protected by cabinet-in-confidence, and the validity of the decision is not open to debate even by elected members of the federal parliament.

There are no checks and balances in this system and in an environment of minimal transparency, intended or unintended abuses of the policy can occur and go undetected. The case of the PNG LNG project illuminates what is at stake. The Exxon Mobil liquefied natural gas project in the southern highlands of Papua New Guinea represents one of the world's largest project finance transactions. In December 2009 the trade minister confirmed that Australia would become a financier of the PNG LNG project via an EFIC loan of up to 500 million US dollars, 400 million US dollars of which was to be written on the national interest account. In the absence of a parliamentary process to test and review this decision it's not possible to determine the answer to important questions about how the project's risks were assessed and addressed.

Since the signing of the project agreement in late 2009 instances of project-related conflict and unrest have been reported in the project-affected areas, and these were detailed in our submission to the inquiry. Research undertaken this year has found that a majority of people feel that the benefits of the PNG LNG project are not fairly shared, and that if this is not addressed human development is likely to stagnate for many people while the risk of instability and violence is likely to increase.

I would like to note that next month Jubilee Australia is publishing a new report on the PNG LNG project that provides in-depth analysis of its structure and impacts. The paper will culminate in recommendations to the Australian government and the PNG government and the private companies involved to improve project outcomes for the PNG people. In summary, Jubilee Australia recommends that the process for approving exposures under the national interest account include an accommodation for parliamentary inquiry and public scrutiny.

My second topic is the Freedom of Information Act exemption. Jubilee Australia is especially pleased that in the draft report the commission has recognised the risks arising from EFIC's exemptions to the Freedom of Information Act. Under the Freedom of Information Act 1982 all documents relating to anything done by EFIC under Part 4 of the EFIC Act which relates to insurance and financial service products or Part 5 of the EFIC Act which relates to the national interest account and its transactions are all exempt from disclosure. EFIC's business is risk, financial risk as well as risk of environmental, social and human rights impacts. EFIC has a responsibility to inform the public adequately of these risks and to manage them on behalf of the government and taxpayers. The FOI exemptions limit the ability of the public and the government to assess how and how well EFIC is undertaking that responsibility.

Jubilee Australia is in full agreement with comments made by EFIC that documents such as financial statements and cash flows of client companies should be kept confidential. There is a distinction, however, between commercial information and information pertaining to social and environmental issues. We are very pleased at the commission's recommendation that the secrecy and commercial-in-confidence frameworks under which EFIC operates should only apply to financial information of its clients. We are confident that amendments to the Freedom of Information Act can maintain the secrecy of EFIC's client companies' market-sensitive financial information whilst also bringing critical transparencies to matters that are of public concern.

Furthermore, we believe that a distinction should be made regarding EFIC's disclosure requirements in its role as provider of export finance and its role as collector of Australia's sovereign debt claims. With the exception of the tsunami loan agreement with Indonesia, all sovereign debts currently owed to Australia have been generated through the activity of EFIC, predominantly on the national interest account. Yet regardless of how long ago the original EFIC-supported transactions occurred and regardless of the existence of evidence to suggest possible malfeasance or misconduct in the loan or finance contraction process, EFIC is secretive about amounts recovered and outstanding claims. For the most part these are only reported on a highly aggregated level.

Again, we can provide an example to illuminate the importance of resolving this issue. Australia company Tenix is currently being investigated by the Australia Federal Police in response to alleged bribery in its business conduct in Asia. One such deal in question is the 2001-2002 EFIC supported contract with the Philippines coast guard. On the basis that the deal involved bribes to senior officials and that no provision for the purchase had been made in the Philippines national budget the Philippines senate put a stop on making the loan repayments to EFIC, leaving the Australian taxpayers liable. Yet EFIC is able to maintain secrecy about information pertaining to the debt, including the amount that remains outstanding due to the protections under the Freedom of Information Act exemption. Clearly the balance between commercial-in-confidence and public interest must be revisited in the case of Australia's export credit arrangements.

My final topic concerns the EFIC governing board. Jubilee Australia acknowledges the commission's effort to assess the make-up of the EFIC board, although we were disappointed that the recommended reforms did not include the appointment of a board member with expertise in corporate social responsibility. We believe the commitment of EFIC to operate in compliance with international standards of corporate social responsibility and the responsibility to manage the risks of environmental, social and human rights impacts on behalf of the government and Australian taxpayers should be formalised in the governance framework.

Jubilee Australia therefore wishes to reiterate its recommendation that one permanent position on the EFIC governing board be reserved for a member with specialist knowledge and expertise in corporate social responsibility.

Thank you for the opportunity to provide comment and to reinforce the aspects of our submission that we think would make EFIC more responsible and accountable.

MS SCOTT: I'm sorry about my movement of paper around but I wanted to get the right piece of paper in front of me. I was listening intently and I have read your submissions and thanks again for those. Carmelan, EFIC has now made a submission in response to our draft report and we hope it will be up on our web site soon. We draw your attention to the fact that they have now responded - late, but they have now responded to our draft report. In their response, I'm lucky enough to have a copy - in their response they don't support recommendations which are about improved transparency at all, saying that it's just impractical and that their existing obligations more or less are sufficient. Would you like to comment on that? I know you don't have that available to you at this stage, regrettably, but could you say something about that?

MS POLCE (JA): Well, I presume that they're not speaking to the area on which we agree, which is commercial information, they're speaking to our other concern, which is the disclosure of information that exposes the due diligence process undertaken and the process undertaken to assess projects from the perspective of the impact they will have on communities where the projects are - - -

MS SCOTT: So for example, EFIC argues that it's impractical to make a distinction between financial and non-financial information.

MS POLCE (JA): Right, well, I've been a banker for many years and I think I understand the distinction. The due diligence frameworks that suggest best practice for human rights obligations are - they're available in many different spaces. That's one of the issues we raised. There are sort of innumerable protocols that are out there that they could comply with.

These protocols and guiding principles and performance standards - they're asking for disclosure of qualitative, not quantitative, information, to put it simply. They seek to expose risks through an analysis of the behaviour of the project counterparties to the conditions around the project-affected areas. They reinforce the need for action plans that respond to those risks and the need to then maintain an awareness of how those action plans are implemented and how the management and operation of whatever the project is related to the transaction is managed in relation to those action plans. So that's qualitative information, that's not necessarily related to cash flows or revenue streams or even capital, who is providing capital and on what basis and what returns are being generated to the project participants.

MS SCOTT: What about the argument that they have put to us in this late submission that Australian exporters may suffer a competitive disadvantage if there was greater transparency?

MS POLCE (JA): I think that Australian - EFIC would be showing leadership in this area. We're talking about serious allegations of human rights abuses and environmental degradation, and the legacy of projects funded by EFIC is not a good one. So rather than succumb to the lowest common denominator I suppose Australia should be a leader in this space, demonstrating for the rest of the ECAs that standards can be maintained, and that would reflect the true cost of these projects. The other comment I would make is - I'll come back to that.

MS SCOTT: Just staying on this theme, in their response EFIC points to the fact that they have agreed to adhere to international obligations, the common approaches and the Equator Principles and that audits will be undertaken at two-year intervals. What level of confidence do you have about those processes?

MS POLCE (JA): I think that what's missing is guidance by the Australian government. The sort of overriding framework for the management of business and human rights is provided in the UN guiding principles on business and human rights, it's known as the Ruggie Framework. It was endorsed by the Australian government in May of last year, May of 2011, yet the Australian government remains silent on its responsibility to advise government - providing an overarching framework and expectations for Australian businesses to refer to the guidelines and to operate with reference to them. So my comment is that that's what is missing. That's the missing piece here, is the messaging and the leadership from the Australian government in setting the standards for EFIC and for EFIC's clients to comply with.

DR MUNDY: I think just to finish off this issue of FOI you mentioned that you feel that the recent amendments to the overarching FOI legislation would be sufficient to provide the level of transparency whilst protecting the sensitive information of others, of commercial parties with EFIC. Would it be your view that the nature - you obviously had a look at that legislation. Would it be your view that to comply with that act would be, in EFIC's words, impractical to implement? Or do you think, like most other agencies, in fact, virtually all other agencies of the Commonwealth other than security agencies, who are harder to comply, EFIC could comply and not have to bear unreasonable cost?

MS POLCE (JA): I think that it's justified, the cost, if there is a cost. I think that there is an imbalance. I think issues are lurking in the shadows that need to be brought out. I don't think that these broad, sweeping protections are necessary. They hide things that - issues and circumstances that the Australian taxpayers and the Australian government needs to be looking at.

DR MUNDY: Can I just move on to the national interest account. You said that the problem with the NIA there is no opportunity for parliamentary scrutiny, and you alluded to the fact that the moneys are appropriated. So by virtue of the fact that the moneys are appropriated they form part of the senate estimates process. There is an opportunity there. The minister can be examined in question time. The minister in the other chamber can be examined. The parliament can set up inquiries. So you're obviously contemplating something more than the normal process of parliamentary scrutiny for the expenditure of Commonwealth money. So what exactly is it? What is that more that you think needs to be put in place?

MS POLCE (JA): I think that that window only opens after the transaction is already agreed. I think that there needs to be an opportunity in the assessment period. I think that what we recommended was that there be a desktop review of proposals made in advance of signing of an agreement. That would give the trade minister an opportunity to respond when issues are - because if something does arise in the aftermath of a transaction the minister will have already have been exposed to the transaction in advance.

DR MUNDY: Sorry, so this would be?

MS POLCE (JA): Before the signing of the deal.

DR MUNDY: So this desktop review would be undertaken by?

MS POLCE (JA): By DFAT or could be by Treasury, but it needs to be some process, some ministerial process, that then provides an opportunity to examine the transaction before the deal is actually agreed.

DR MUNDY: So you're not proposing any sort of parliamentary process beyond that other than the normal scrutiny of public expenditure, but you think there should be a process within government?

MS POLCE (JA): Within government, a transparent process within government.

DR MUNDY: So it would call for submissions, it would advertise, "EFIC is contemplating" - or the government, because the minister consents to an NIA transaction.

MS POLCE (JA): Yes.

DR MUNDY: So there would be a calling for submissions, a consultation process?

MS POLCE (JA): I think that there needs to be the governmental process that we talked about.

DR MUNDY: Okay.

MS SCOTT: Carmelan, on the issue of bribery you've raised the Tenix matter in your submission and in your testimony today and you've drawn attention to actions by the Philippines government and so on. Are you aware of the processes that EFIC goes through to assure itself that bribery is not an issue when it has dealings or is about to have dealings with a firm, and what do you think of the quality of those processes?

MS POLCE (JA): I don't have any knowledge of those processes.

MS SCOTT: Have you sought to find out about the processes but you were unsuccessful or you haven't made inquiries in that direction?

MS POLCE (JA): As I said, Jubilee Australia has been investigating and raising concerns about the behaviour of EFIC for eight years. I personally have been involved for about the last six months, so I can take your question on notice and respond to you about what consideration Jubilee has made in the past in regards to the safeguards that EFIC employs to ensure that bribery doesn't happen.

DR MUNDY: Perhaps when this late submission from EFIC which we've only just received - perhaps in that response you can also reflect on any material that's in there?

MS POLCE (JA): Yes. I'd be very pleased to. Will the balance of the submissions made in response to the draft report be on the web site as well?

DR MUNDY: They all are.

MS POLCE (JA): Okay.

DR MUNDY: Along with yours.

MS SCOTT: Thanks.

DR MUNDY: Just, I guess a - and this goes both to social policy impacts but also environmental impacts. Do you think it's sufficient - when EFIC is in partnership with other ECAs in other countries do you think it's sufficient for them to rely - say if there's a lead ECA, which there often is. Do you think it's sufficient for EFIC to rely upon the work of others or do you think it should undertake due diligence of its own right?

MS POLCE (JA): I think it should scrutinise the due diligence that has been undertaken by its counterparties and where that's insufficient then it should undertake its own due diligence.

MS SCOTT: Carmelan, in your submission you raised the Tenix matter and other issues related to potential corrupt activity. Is your organisation aware of concerns in the past regarding the Solomon Islands and EFIC, and if so, what light can you shine on that issue?

MS POLCE (JA): Jubilee Australia published a report in 2009 called Risky Business that used a Solomon Islands case study to describe the shortcomings in the process, an EFIC process, and due diligence and environmental issues. So that case study is outlined in our Risky Business report. I can't speak to that case study myself.

MS SCOTT: That's fine. In your submission you refer to difficulties that - I understand difficulties that you've experienced obtaining documentation from AusAID in part because records - and I'm quoting now your submission:

> Records may have been destroyed as part of the routine sorting process of government agencies.

I was just trying to reconcile that with requirements under the Archives Act for government departments and agencies to retain documents. Could you give us a bit more background on this issue?

MS POLCE (JA): Again, that predates my time but I made an inquiry about that. That note reflects comments to Jubilee Australia when we were making inquiries. So I suppose it was an excuse given that the data may or may not be available, and so there wasn't any acceptance of our request for the information.

DR MUNDY: That was AusAID?

MS POLCE (JA): That was AusAID.

MS SCOTT: It's a very curious answer you've been given.

DR MUNDY: Yes.

MS POLCE (JA): Yes.

DR MUNDY: Very.

MS POLCE (JA): We thought so.

DR MUNDY: Did you follow it up at all?

MS POLCE (JA): No. I can find out what - that was the - - -

DR MUNDY: I guess my other question was was it a general public inquiry or was it by way of an FOI application, would be useful to know as well.

MS POLCE (JA): Okay.

MS SCOTT: Carmelan, just remind me again of your banking background. I think I've read about it in preparation for today but - - -

MS POLCE (JA): So I've been with Jubilee Australia since September but I've had a career in banking and finance. Is there anything further?

MS SCOTT: No, just - you know, your earlier comment that you think it's possible to distinguish between a financial element and a non-financial element, that you can tell the difference apart. You referred to your banking experience.

MS POLCE (JA): Yes.

MS SCOTT: So you think that if you had a series of documents about a transaction you'd be able to distinguish successfully between the two.

MS POLCE (JA): Yes.

MS SCOTT: Okay. All right, well, thank you very much.

MS POLCE (JA): Thank you.

MS SCOTT: Well, we're going to take a break now for morning tea, and we propose to resume promptly at 10.45.

MS SCOTT: Ladies and gentlemen, we will now resume our hearings. As a number of people have joined our hearings I might just elaborate on a few comments I made earlier, just a few housekeeping things. For example, if you haven't turned your phone to silent this would be a great time to think about doing that. This is actually quite a noisy room, between the airconditioning at the back and lots of traffic noise outside. I appreciate that it can be quite hard to hear participants, even sometimes Warren and myself. So if for some reason we suddenly become very softly spoken please can you draw our attention to the fact that you cannot hear, because it's very important the participants, especially people presenting this afternoon, have an opportunity to hear. The microphones are not an optical effect, they're for the transcript purposes but they're not actually for room amplification. So that's why I guess I would suggest - Angus, you might want to take that into account.

Do we have any representatives from the media? Anyone from the media joined us at this stage? Okay. We will be finishing, we think, around 4.30. If you've joined - you've been listening to the testimony say this morning and you wish to make a comment at the end of the day we will give you an opportunity at the end. We'd hope that your comments would be brief, as we're actually anticipating that we will be wrapping up around 4.30, not 4 o'clock as originally in our schedule. If you wish to discuss something with one of your colleagues or someone you've just met we'd encourage you to think about going outside, because again, it's quite a difficult room to hear our participants' commentary. We're expecting to be taking lunch at about 12.30.

Now, for the purposes of the transcript I'd invite the people at the table to state their name, their role in EFIC, and I've got a few introductory comments after that.

MR ARMOUR (EFIC): Angus Armour, Chief Executive and Managing Director of EFIC.

MR HOCKEN (EFIC): Mathew Hocken, Senior Adviser, Government and Industry Relations at EFIC.

MS SCOTT: Well, thank you very much for coming along today, gentlemen, and for the availability of your senior staff. We are very pleased to get your submission - late, but at least we've had an opportunity to read it. We will turn to it at times in our questions but unfortunately you haven't given us sufficient time to fully consider and examine all the points you've made, and as a consequence we are likely to have some follow-up questions. Also it means that participants to this inquiry have not seen your submission, who may well be presenting in our hearing, something we do seek to achieve before the hearings commence.

As we have discussed previously, a late submission increases the likelihood that we will need to have an additional hearing date, but given that we've set aside a quite considerable amount of time to put questions to you today, just how much further questions there will be will depend upon how much progress we can make today. Angus, I understand that you wish to make an opening statement?

MR ARMOUR (EFIC): Yes, commissioner. Firstly, commissioner, I'd like to apologise for my voice, which my colleagues would know does tend to be a little bit softer, so I will not be offended if the commissioners pull me up and ask me to speak a little louder.

DR MUNDY: I suffer from the same affliction.

MR ARMOUR (EFIC): Secondly, commissioner, given the breadth of the inquiry as observed we have some of our senior staff here. There will be times when there will be a brief pause while they may join us at the table. They'll identify themselves when they join us.

MS SCOTT: Well, that will be fine, thank you.

MR ARMOUR (EFIC): As the Commissioner has observed we have tabled today with you - you had it over the weekend - our response to the draft report. I don't intend to go exhaustively through our response. I don't think that's a good use of our time. I would like to present some of our core arguments with the analysis and the findings and the recommendations that are in the draft report.

I'll start by restating from our perspective the core arguments that the Commission enunciated in the draft report, and particularly focusing down on the core premise that there is no evidence of market failure in financial markets or that any failure that may exist might relate to firm size. That core premise drives the Commission's conclusions that EFIC is likely to be competing with private capital, and as a consequence represents a subsidy through our activities; and consequently from the perspective of economic efficiency a mis-allocation of resources. So in summary then, financial markets are perfect and private capital will fund what should be funded optimally. EFIC’s activities are competing with private capital or they represent a subsidy. EFIC is unviable or sub-optimal. That's how we see the conclusions of the report, at least.

The consequences from your findings are recommendations that include - but actually, the recommendations are quite extensive, so again, we'll narrow it down in what we're addressing - include restrictions on EFIC's future activities, and particularly from our perspective an emphasis of establishing a limit against turnover for the support that we offer, so a focus on newly exporting SMEs with a turnover of

$25 million or less; that EFIC support be restricted after three transactions; that it be through a guaranteed product solely; and that, as a consequence really flowing from all that, that there is no onshore or offshore support for large firms. That is how we have read your findings and recommendations, Commissioners.

I would like to start then with the core premise around market failure and our argument. Certainly our response to your report is premised on the belief that your literature review was limited, and the discussion dismissed rather than proved the premise that financial markets are perfectly efficient. Current research embeds concepts of imperfect information, information asymmetry and defective competition into the analysis rather than excluding or dismissing. Experience of the past few years suggests that this is a wise course.

The argument then takes a generalised conclusion about financial markets and applies it to the specific case of project and export finance, again without any further analysis. The commission generalises again that any imperfections in financial markets might relate to firm size. Lehman was a big firm. Big exporters work in frontier and emerging markets. We feel more evidence regarding specific market failures is needed to support your argument that there is some linkage to firm size.

This is a critical point, commissioners, as I think we both agree. There is one thing we can agree on, this is a critical point. The core of the Commission's findings and recommendations flow from this premise, that financial markets are perfectly competitive. On that premise the financial markets are efficient, the commission finds that EFIC is likely to be crowding out, in the words of the finding, the private market. Again, we would emphasise that initial premise is unproven, so we disagree. Regardless, after nearly nine years of operation in our current form a reasonable person would expect to see the Commission provide evidence to support its finding. In fact, the overwhelming evidence from submissions - that EFIC is crowding in. For example, Westpac writes:

> In no case have we seen evidence that EFIC is providing such support inappropriately or in a way that crowds out commercial institutions.

CBA submits:

> There is a clear and consistent focus on filling a market gap on terms and pricing set by the commercial bank sector.

Chartis, from the United States writes in a more colloquial US frame:

> If I thought EFIC were competing with us I would not hesitate to make the case against them. I don't think they are.

So the commission's arguments around market failure and market perfection rely on, in our view, a selective appeal to theory and ignore the evidence that has been provided by the submissions. We urge you to reconsider your conclusions and your analysis.

So flowing from your premise that markets are perfect and efficient, you have concluded that EFIC's activities are a form of subsidy. Now, I can revisit that argument from two perspectives. Firstly, in relation to transaction pricing, and secondly, as you do, in the context of portfolio returns. If I turn first to pricing, I would hope we could agree that EFIC is largely a price-taker. There are commercial benchmarks that we refer to and, if necessary, the OECD guidelines that have been agreed by the Australian Government. Again, any suggestion that we are offering sub-market pricing would presumably draw complaints of competition by the private sector. Secondly, sub-market pricing would similarly affect our ability to obtain reinsurance. Neither of those cases have been shown. As the commission, I think, itself writes, as a price-taker distortions are unlikely to occur.

I would also like to point out that price differentials are not necessarily an indication of subsidy either. Price differentials are not a necessary or sufficient condition to prove the argument that a difference in price is a form of subsidy. Again, in conversation with the commission in the past I've used a number of examples to illustrate that. Why is it not a necessary condition? A very simple rule of thumb that we apply at EFIC: there is no good price for bad risk. The example I have used with you in the past has been when the German export credit agency continued to offer cover into Russia through the financial crisis at very high rates. It was nonetheless, in our mind, a subsidy because the possibility of them recovering those amounts was clearly diminished. There was no good price for a bad risk. Pricing itself is not a necessary or sufficient condition to prove your argument.

I turn then to portfolio return. The commission's argument is simply this: bank returns are about 22 per cent, EFIC's returns are about 8 or 10 per cent pre-tax, the commission would argue EFIC, therefore, is a subsidy. The structure of this argument draws on an irrelevant premise. The commission discusses and then dismisses that banks have a completely different business model than EFIC in drawing its conclusion. EFIC argues in its response that banks have a broader scope and range of products to produce those returns. Equally important, if not more important, is the concept of asymmetric credit selection, which again we have discussed with the commission. It's a function of EFIC's role that we will not chase after good risk, whereas it's in the banks' commercial interest to seek them. Consequently, our credit selection is to choose the least bad risk, if you like, rather than to chase after good risk in order to balance our portfolio. The commission ignores this again.

In summary, EFIC is a price-taker in almost every instance. Its costs are consistent with a broad range of financial service providers and transaction losses have been very low over a very long period. So if price and costs and losses are at commercial levels, then the commission's argument that EFIC’s support represents a subsidy is unsupported by the evidence. The portfolio return comparison is irrelevant. The business models are different. EFIC's capital position is substantially greater than the leverage employed by private financial institutions, that's true. EFIC's profitable operations over a long period have generated its current capital base, which the commission acknowledges but then ignores in its discussion of return on equity. That capital is the basis for EFIC's limits. That's the basis that we offer our support to Australian exporters. It also represents the buffer that protects the Australian taxpayer against the call on EFIC's guarantee. Our return could increase with increased leverage, but that decision has broader implications.

So to sum up our analysis of the findings of the commission's draft report, the commission's essential argument is that financial markets are perfect, and in a perfect market all viable and optimal financing will be provided by the private market. EFIC support is therefore unviable or suboptimal. EFIC's rebuttal is simply this: the premise that financial markets are perfect is unproven. Current research argues that there are a number of market failure issues. The private market is consistently submitted as evidence that not all transactions can be completed in the market. The private market has consistently said that ECAs play a role in filling the gap that results from imperfect markets. As a price taker the private market is consistently submitted as evidence that EFIC is not competing. As a price-taker EFIC has consistently demonstrated the capacity to crowd in private capital. As a price-taker EFIC’s support is unlikely to result in distortions. EFIC's costs and losses are on levels equal to or better than private market experience. EFIC has operated profitably in 19 of the past 20 years. We think this goes to the core of the commission's argument about our viability.

If I turn then to the recommendations, again we would group these. There is a recommendation, a series of recommendations, that focus on narrowing EFIC's business to SMEs with turnover of less than 25 million, new exporters and possibly with limited credit history, by implication then, no support for large firms either offshore or onshore; that there is a limit to the number of transactions that we provide, and that how we provide that support is through only a guarantee model.

The limits are clearly arbitrary. The commission in its report says there is a substantial case to impose a limit but the case is not actually presented. Market failure is independent of size. In the presence of market failure there is no argument to discriminate. The recommendation, we would argue, is incoherent in the sense that you cannot enact those recommendations to limit or narrow EFIC's focus and at the same time seek higher returns.

The recommendation to narrow our support to a guarantee product is particularly troubling given the European experience. European export credit agencies who offer by and large only an insurance product have struggled since the GFC to mobilise the credit capacity, that is, the lending capacity, to deliver their support. They have been seeking EFIC's advice on how to establish a model akin to EFIC's direction. In 2012 we seem to be ignoring the experiences from 2008 and the lesson that having some flexibility in the way a government service is provided is desirable. I would argue, in terms of effectiveness - the commission would appreciate that direct lending is also in many cases a least-cost intervention, where intervention is warranted.

With respect to onshore projects, there has been a clear demonstration that export credit agencies have been an instrumental channel to funnel funding into Australia in the wake of the crisis. More than $6 billion has been provided by export credit agencies globally since the GFC. In some instances we argue there may be gaps that could be considered by EFIC. On this point, however, there is probably an equal concern of EFIC as to the commission, which is this should be a temporary phenomenon. If you look at EFIC's activities prior to 2008 even though we were under our legislation permitted to undertake this activity, we did not. Why not? Because we tested and determined that there was no basis, that there was no market gap. Any funding failures that existed prior to that period were probably due to relevant and reasonable commercial concerns.

When we proposed to the Board in 2008, including the government member, that EFIC respond to the GFC by adopting this pose, adopting this position, my verbal comment at the board was simply, "I'd hope we'd be out of this in three years." That has not proven to be the case. I would still hope we get out of this in three years. I must emphasise to the commission that it's not our desire to build a business around the post-GFC environment. It is our hope that the commercial markets - and our belief, frankly - that the commercial markets will eventually over time be capable of providing the support. But the demand that exists now is apparent to all, as is the need for export credit agency funding at least for the time being, we believe. So we would argue that simply as a precautionary principle this is an acceptable position for EFIC to take.

Commissioners, that's our overview of the response. I would like to take just one minute to emphasise what we think are some of the points that need to be on the record in terms of our approach to providing export credit arrangements. We have supported about $15 billion worth of exports to 65 countries over the past 10 years. We have done so profitably. We have supported both SMEs and large firms. We have worked with the private sector to deliver that support either through $1.6 billion of export finance guarantees or $1.4 billion of reinsurance. We have crowded in the private market in order to achieve these results, and it is a deliberate strategy to achieve those results.

There is a whole section of the report that relates to EFIC's risk management that I have deliberately, in the interests of time, not developed in detail in these introductory remarks, but I would like to observe for the commissioners and for the hearing that our ability to manage risk has been proven through the past 20 years and through many different business cycles and many different crises, by being profitable in 19 of the past 20 years. To have paid to government dividends in excess of $240 million, we think is a demonstration of the integrity of that model, and we would be concerned with any insinuation otherwise.

So that's where we stand, commissioners, in terms of your report. We're very happy to explore our response, acknowledging however that we may need a separate session at a later date to go into some matters in more detail.

MS SCOTT: Well, thank you, Angus. Please call us Patricia and Warren. Well, we've set aside quite a bit of time and you've raised some issues that we will need to return to and explore with you. I'm happy at any stage for you to call to the table any of your people that you wish. This is going to require a bit of forbearance as we address quite a wide range of issues. I certainly want to return to a number of the premises that you think that the commission is holding. We will allow sufficient time for that because they're very important.

But I do want to turn first to human rights issues and our draft recommendation 9.8, which you have responded to in your submission. It's page 63 of 93.

MR ARMOUR (EFIC): Commissioners, I've asked Mr Jan Parsons to join us at the table. Jan, could you state your name and position, please?

MR PARSONS (EFIC): Jan Parsons, Director, Technical and Environmental Review within EFIC.

MS SCOTT: Okay, thank you very much. Thank you for coming along today. In our draft report we were concerned about the lack of clarity regarding Australia's international obligations on human rights. This was something we struggled with. I have to say some of our conversations with other agencies suggested they had a struggle with it, and to be frank we thought that you would likely welcome this because this would actually clarify the obligations to which you are required to comply. So therefore I was surprised that you were actually not after any clarification. You obviously feel that they're perfectly clear. Would you like to elaborate on why you consider them to be particularly clear, what you're referring to exactly and why you consider that any greater articulation by the government would be both impractical and unnecessary?

MR PARSONS (EFIC): I guess the first premise we're working from is that we already address human rights in our environmental and social due diligence work. This is done through a number of different methods but our basic benchmark is something called the IFC Performance Standards. Included within the IFC Performance Standards themselves are human rights issues which are embedded within those standards, like other things such as labour rights, resettlement, rights to clean water, community health and safety. So our basic benchmarks include a majority of human rights issues that most projects will face.

We've also made a commitment - and we also use other things or other benchmarks or other sources of information when we come across a project where maybe the IFC Performance Standards aren't covered off in enough detail; which in our experience is a relatively rare occurrence, but on occasion we've sought advice from various other tools that you can use. There's something called the UNEP FI toolkit for human rights which is guidance for financial institutions on human rights issues. There's also another thing we use, which is the Danish Institute for Human Rights which has a further toolkit. So where we find that maybe the IFC Performance Standards aren't covering those issues in sufficient detail we go to other sources of information. So that's, I guess, basically how EFIC, in a nutshell, addresses human rights.

In terms of guidance from the government about what human rights issues to address, it's a really hard question to answer because ‘human rights’ is not easily defined. It covers a multitude of different issues from labour rights through to rights to clean water through to access to biological or - medicines from natural forests. So for the government to attempt to define that would end up pretty much with what they have already advised us with the treaty database on the DFAT web site. We supplement that with other things. There's recently a report put out by the UN on the guiding principles for human rights in business which we use and which during its preparation we commented on and had some input into. Human rights are currently being considered in a review of the common approaches and the Equator Principles. Again, EFIC is participating in contributing to those discussions. So yes, I mean there's a whole range of different ways that EFIC gains information.

MS SCOTT: Thank you for that answer. How did you establish with the government that the ICF Performance Standards were sufficient to meet their requirements regarding the ministerial directions?

MR PARSONS (EFIC): The IFC Performance Standards are currently considered the best available method for addressing environmental and social due diligence in projects for financial institutions. There are various tools and methods available but of all the methods available the IFC Performance Standards are considered the best standard. So in our advice to government we would recommend to government that that is the best method. When we reviewed our policy a couple of years ago in which the Department of Foreign Affairs and Trade participated in, that was our advice to government at that stage, and we received no dissension from that from government.

MS SCOTT: So essentially you put the proposition to DFAT that the ICF principles should be the principles you adhere to and you effectively got silence back from DFAT and you're taking that silence in the circumstances as an indication that that's the standards you should use?

MR PARSONS (EFIC): I wouldn't say we had silence back from - - -

MR ARMOUR (EFIC): Sorry, I'll just - it's International Finance Corporation or IFC, rather than ICF, and it's an arm of the World Bank.

DR MUNDY: And the World Bank has had some issues in the past with its own standards, and that's why the IFC had to develop these things over time. But sorry, could you just remind me what date did you last do this review?

MR PARSONS (EFIC): Our current policy was adopted by our board in February 2011. We did a review which went over almost two years in doing that - - -

DR MUNDY: When was this last interchange with DFAT?

MR PARSONS (EFIC): Well, DFAT were part of the review.

DR MUNDY: So the review occurred 2009 to - - -

MR PARSONS (EFIC): 2011. We spent a lot of time and effort in making sure that our policy reflected current industry norms.

DR MUNDY: Well, industry norms, whether they're the expectations of government is a different thing. It's a question to you, Mr Armour, I guess, has EFIC communicated these standards to the minister formally, either Minister Emerson or Minister Crean?

MR ARMOUR (EFIC): Well, in the past, as Mr Parsons has indicated, the review process went through a board approval stage involving the government member, and the government member presumably advises the minister on these issues. We have made public - without question, a very public process - to identify if there are other standards available. It's not my impression - I'm not sure what the direction of the questions is going, whether you have identified other standards that are more appropriate or - - -

DR MUNDY: No, we've - - -

MS SCOTT: We've struggled in this area to get clarity, to be frank, from the government about what standards they expect.

MR ARMOUR (EFIC): Right.

MS SCOTT: So that's why we wrote the recommendation, and then to our surprise you've written back saying you don't have any trouble understanding what the government expects of you because - you don't seek any further clarification. But I think I understood Mr Parsons to say notwithstanding your engagement over a long period with DFAT you've never actually ever received a written document or had it confirmed through some other mechanism like a letter that in fact the standards you have decided to apply, which might be perfectly fine, are in fact the government standards.

MR ARMOUR (EFIC): Yes. I accept that point, actually. But I have to assert firstly that we - I'm not conscious of any policy that we've adopted where we've had an explicit approval outside of the board process by government; so for any policy. Secondly, that the Australian government of course is a member of IFC and the World Bank, and they're separate memberships, and therefore presumably the Australian government as a whole has, through that process, approved those standards as being acceptable for the operations of that institution. I know this may be unsatisfactory to you but it certainly is a conventional view that - and widely held conventional view - that these are the best standards. So in the absence of better standards we think it's a reasonable option to adopt.

Of course if - what we haven't perhaps identified for you is there are times we will compare these against Australian standards on occasion because we'll find the IFC has not been required to address a particular issue, and I'm going back over a long period, probably perhaps even before Mr Parsons joined us, but we will consider whether Australian standards are more relevant in some circumstances. But it is reasonable, I think, through this board process, through adopting a policy that has been accepted by the Australian government in a broader international framework - in adopting a policy that has been acknowledged through the OECD process as well. It more or less captures the concerns of the Australian government. If there are particular issues of course we're very open-minded to explore it.

DR MUNDY: But coming back to the question that I asked you, and it wasn't a question about was it approved, it was a question of whether it was communicated, what you're saying to us is that when the board made the decision to adopt that policy, that decision was not communicated with the minister of the day?

MR ARMOUR (EFIC): The policy would - sorry, the outcome from the policy review would have been communicated to the minister in some form, either the annual report or the corporate plan, that would have been quite clear.

DR MUNDY: Okay.

MR ARMOUR (EFIC): How DFAT engages with the minister around these issues is, you know, obviously not transparent to us, because they're offering advice to - - -

DR MUNDY: So what you're saying to us is that communication you would rely upon the government member to do that for you?

MR ARMOUR (EFIC): Correct, to represent the views of government on issues that might be of concern.

MS SCOTT: Thank you for that.

DR MUNDY: Mr Armour, you'll probably need some of your colleagues, and it's not a human rights issue or an environment issue, this one, but we've received a submission from Greyhound Australia which we'd like to ask you some questions about, so you might want to invite some of your colleagues to join us?

MR ARMOUR (EFIC): Do we think we'll need Mr Parsons again around environmental - - -

MS SCOTT: No, I don't think so, not at this stage.

MR ARMOUR (EFIC): He has just flown in from overseas.

MS SCOTT: We may well have questions later but no further ones at this point.

MR PACEY (EFIC): John Pacey, the Chief Credit Officer of EFIC.

MS GOVAERT (EFIC): Andrea Govaert, Executive Director, SME.

DR MUNDY: Thanks very much. We've received a submission dated 20 March 2012 from Greyhound Australia, the long-distance coach operator. It indicates, although not particularly clearly and certainly not on any sort of probative level, that there has been some engagement between EFIC and Greyhound Australia. Can you outline to us what that engagement has been?

MS GOVAERT (EFIC): Well, Greyhound approached us I think about - probably would have been about five months ago for a facility. We've met with Greyhound several times to discuss the actual facility. It was followed, as we normally do, with a more in-depth analysis. I believe, John, you've met them, and I think Jan as well. So the technical due diligence, normally that's separated from the commercial discussions that we have. Then when the facilities are then agreed - because the environmental and the technical due diligence is satisfactory, then we proceed to a final submission which we ask for approval with our credit committee, so that's how it goes in general. If you have any specific questions - - -

DR MUNDY: Well, I have a number of specific questions.

MS GOVAERT (EFIC): Yes, okay.

DR MUNDY: Has the transaction been concluded?

MS GOVAERT (EFIC): No, the final transaction has not been concluded but we've sent the letter of offer, I think about a week ago. But having said that, to bridge - because the company had to issue a bond, as you know so we've issued a bond, which is 100 per cent cash covered, pending the approval for the overall facility. The overall facility was approved, I think, about two weeks ago and the letter of offer was sent - on top of my head I think about a week ago and we're currently in documentation stage.

DR MUNDY: Can you outline for us the nature of the export transaction that's involved with Greyhound Coaches' dealings with yourselves?

MS GOVAERT (EFIC): It is one of the first transactions that we've done in conjunction with our subcontracting initiative which supports SME companies that are forming what we call an integral part to an ultimate export. This company, as you are aware, is involved in transporting staff to the mining site, and the bond was required in favour of - I think it was Bechtel, for the company to deliver on its commitments.

DR MUNDY: Where is the mining site?

MS GOVAERT (EFIC): It's up in the Northern Territory.

DR MUNDY: Whereabouts in the Northern Territory?

MS GOVAERT (EFIC): Sorry, Western Australia.

DR MUNDY: Sorry?

MS GOVAERT (EFIC): Sorry, Western Australia, yes.

DR MUNDY: Whereabouts in Western Australia?

MS GOVAERT (EFIC): Robert - - -

MR DRAVERS (EFIC): The Wheatstone - - -

DR MUNDY: Sorry, we can't take evidence from the floor.

MS GOVAERT (EFIC): It's Wheatstone.

DR MUNDY: It's Wheatstone? Okay, and Wheatstone, for the benefit of Hansard for people unlike me who have a lot to do with Western Australia, it is where? Where is Wheatstone precisely, the town?

MR PACEY (EFIC): It's in the far north-west.

DR MUNDY: Yes.

MS GOVAERT (EFIC): Yes.

DR MUNDY: Okay. So the purpose of Greyhound requiring this bond is so they can successfully bid for a - - -

MS GOVAERT (EFIC): No, the bidding has already taken place.

DR MUNDY: It had already taken place?

MS GOVAERT (EFIC): Yes.

DR MUNDY: Were you in discussions with Greyhound prior to the bidding taking place?

MS GOVAERT (EFIC): Not that I'm aware of.

DR MUNDY: Could you check your records?

MS GOVAERT (EFIC): Yes, I will.

DR MUNDY: If that isn't the case please get back to us.

MS GOVAERT (EFIC): Yes.

DR MUNDY: What's the value - what is Greyhound requiring the bond for, the performance of the transportation service?

MS GOVAERT (EFIC): Yes.

DR MUNDY: Are you aware of whether there was a competitive tender process or not for the contract concerned?

MS GOVAERT (EFIC): It was a competitive tender process. I mean I have to take the actual details on notice because I'm not intimately aware of this.

DR MUNDY: Okay. So it's likely that there would have been other local regional bus operators presumably bidding against Greyhound?

MS GOVAERT (EFIC): Likely, but again, I'll have to take it on notice because I don't know exactly.

DR MUNDY: If you could, yes. It's a bit difficult for us because Greyhound's submission is quite opaque in its details.

MS GOVAERT (EFIC): Yes, it is.

DR MUNDY: So this is the first of these sorts of transactions that you're contemplating entering into?

MS GOVAERT (EFIC): We supported a few other companies. The idea is really to support subcontracting companies with the large natural resources projects. They are generally SMEs, as you know. We've done a few others. Lean Field is another one which we supported in Queensland. More broadly we are definitely planning to help more SMEs if their idea is to - and they deliver a service that is integral to the project.

MR ARMOUR (EFIC): Commissioners, I'm just conscious in fact this is a - well, to me at least, a new line in questioning, and that we haven't really given you a lot of background in terms of - - -

DR MUNDY: Well, now is the first that we knew of it, when we received the submission from Greyhound.

MR ARMOUR (EFIC): Yes, that's right. So perhaps if I get Mr Hocken to explain the government framework that goes around this in terms of the sub-suppliers to large projects.

DR MUNDY: That might be helpful once I finish asking my questions.

MR ARMOUR (EFIC): Okay, and the actual facility that - - -

DR MUNDY: Are you aware - and if you're not, can you get back to us - as to whether Greyhound had existing local coaching operations in that part of north-west WA?

MS GOVAERT (EFIC): Again, I have to take it on notice, I don't know. That's a very, very recent facility, sir, literally two weeks ago.

DR MUNDY: I understand that. Are you also able to inform us as to whether Greyhound intends to use this to provide - as a basis to provide other services within that general region which may not be related to a resources contract?

MS GOVAERT (EFIC): I'm not aware of that.

MS SCOTT: Well, Angus, this might be the right time to get that general introduction to this new initiative, because we're keen to explore it further.

MR HOCKEN (EFIC): Sure. The commission may be aware that there is an initiative which has been announced by government, the Resources Sector Supplier Advisory Forum. It's chaired and headed up by Peter Beattie and has representatives from large, small companies, unions and other associations. It did meet on Friday. It's had a number of meetings over the past months. It's looking at a number of issues which particularly subcontractors and contractors are facing in seeking to get business contracts in some of the large export projects in Australia. So the mandate really is to increase the proportion or the amount of Australian companies who have access to those major projects.

We have had some discussions with the Department of Industry who are running with this initiative, and we are certainly supporting, as Andrea said, with the products that we can provide which do help those subcontractors overcome some of the financing difficulties which they have. There is particularly one subgroup which is focusing on access to finance, and I believe they're developing some initiatives to help address that.

MS SCOTT: Is it the proposition that you're putting to us that Greyhound couldn't obtain this finance from its existing or traditional suppliers of finance?

MS GOVAERT (EFIC): It's in addition, because the idea really is that a lot of these companies they have to provide bonds, performance bonds. They're small companies and - - -

MS SCOTT: And Greyhound fits this category for small companies?

MS GOVAERT (EFIC): Well, it's all in the definition, right?

DR MUNDY: Greyhound is the largest coach - they tell us in their submission that they are the only national coach company; Murrays would probably take exception to that description, but anyway. They've been around for awhile and they're pretty big. So I don't - - -

MS SCOTT: I think they feature in country and western films.

DR MUNDY: They do, and tumbleweeds. But my understanding of this initiative that is being led by Peter Beattie comes out of a debate, particularly in Western Australia, about local content - - -

MS GOVAERT (EFIC): That's right.

DR MUNDY: - - - and the sourcing of product from overseas. Now, I'm not aware of an awful lot of international competition for the provision of bus services in the north-west of WA. In fact, I would suggest that they would probably struggle getting in, they would struggle getting visas for their staff and a whole pile of things. So whilst I understand there is this wider issue about procurement for the resources sector, and it's a difficult and complicated issue, it's not clear to me how the sourcing of these coaching operations, which I understand happen frequently throughout Western Australia, Queensland and New South Wales and South Australia, on this occasion requires intervention by a government agency. So what is different about this and where is the - I mean if the purpose of this is to help Australian firms to compete, where are the foreign competitors?

MS GOVAERT (EFIC): Okay. I have to take your - as I said, the bidding process I'm not intimately familiar with, so I'll have to take that question on notice and I will come back to that. But on the specific financial matter concerning Greyhound, obviously you may or may not know but Greyhound went through some difficulties and the company was turned around and is banked by a number of banks. None of them were prepared to issue the bond, or not under the circumstances. So therefore we negotiated with Greyhound and with - you know, to come to an acceptable solution. The reality is that we have issued the bond currently at 100 per cent cash cover. The bank was only prepared to do that at 100 per cent cash cover. We are looking to release some of that cash throughout the phase of that project. That's what we're currently negotiating with the company. But if you want more detail, which I appreciate, I suggest that I come back to you, because it's much better.

If we can sort of move away a little bit from the Greyhound example, generally what these SMEs experience, and that's what we've heard from the Australian content and procurement managers for the larger projects, is that they have to come up with bonds, and the bonds are usually under a 100 per cent cash cover requirement, which puts a lot of working capital constraint on these companies. This is where we come in and this is the market gap, if you like.

DR MUNDY: I understand the issue about resource input and the whole debate.

MS GOVAERT (EFIC): Yes.

DR MUNDY: And I understand the purposes for which the Prime Minister appointed Peter Beattie, which was to increase Australian content in supply. In this case and perhaps in other cases we are not aware of, it seems to be the case that we - you and we, the Australian tax payer - are supporting a company whose only competitors could have been other Australian companies, probably local regional ones. You now describe a circumstance where one of the motivations in your consideration was that the company in question had recently suffered an incident of financial distress.

MS GOVAERT (EFIC): I think there are two issues here that you raise. You raise the issue of international competition, which is one issue. We are not involved in the bidding process, so companies come to us after they have won a contract. Maybe there may have been initial discussions: they announce to us that they are bidding for a certain contract in order for us to be prepared. So that is one aspect of it. The second aspect is really the level of collateral. You know, the market gap can emerge in different ways. The market gap, the way we see it here, is a 100 per cent cash cover for a bond, which puts a considerable amount of working capital constraint on a company if they want to fulfil a large contract.

This contract is a large contract: I think it is over - now, before I say anything that is not true, I don't know exactly the size of the contract. But in any event, it will put a lot of working capital constraint on this company going forward. It is true that the company has gone through some rough patches in the past, but they have turned around, and this is where we see this company can make a difference going forward and grow. On that basis, we have actually agreed to support it. Obviously, Greyhound is only one example. There are many, many other companies out there that have gone into bidding for certain contracts. In fact, some of them will not have competition, because typically, SMEs, they bid for very niche activity in a contract and that is why they win these contracts, because they have something on offer that other people don't.

MS SCOTT: If I understand you correctly, Andrea, it may well be the case that you will end up providing support for firms that don't face the challenge of international competition, but you are stepping in to what you consider to be their funding gap issue?

MS GOVAERT (EFIC): I think, yes, there are multiple facets to funding gaps or to market gaps. There are also offshore country risk, and that is the smaller companies that bid for large contracts, as we've seen in Perth.

DR MUNDY: But that is not a case in point here.

MS GOVAERT (EFIC): No.

DR MUNDY: What do you think would have been the consequences if you hadn't proceeded with this transaction?

MS GOVAERT (EFIC): Well, the company would not have been able to fulfil that contract, because they had to issue performance bonds and they would not have been able to do this, because the bank was not willing to step in.

DR MUNDY: So that company would have then defaulted and, presumably, the proponents of Wheatstone would have then got another bussing company to fulfil the contract?

MS GOVAERT (EFIC): I think you have to be careful with the term "default". It's not a default question, it is more that they cannot proceed with the contract.

DR MUNDY: Okay, the contract does not proceed.

MS GOVAERT (EFIC): Yes.

DR MUNDY: So then Wheatstone would then turn to another bus company or perhaps even buy busses themselves and employ bus drivers. Do you think that this transaction, if it had have not proceeded, that the Wheatstone project itself would not have proceeded, so therefore the export transaction was not in jeopardy?

MS GOVAERT (EFIC): I see what you’re getting at, but I think for SMEs it is obviously difficult to say, if they don't do the electric part for that machine, that the project doesn't go ahead. What is important is the Australian content component, and this is why this initiative has been started.

DR MUNDY: But this contract was always going to be performed by an Australian firm for that project.

MS GOVAERT (EFIC): Greyhound in this instance.

DR MUNDY: No, but any other bus company who would have performed this would have been an Australian company.

MS SCOTT: That is something you didn't establish as part of your evaluation process, but in fact the Australian content was at risk. I think that is the point that Dr Mundy is trying to convey.

MS GOVAERT (EFIC): Yes, and I understand that point.

MS SCOTT: Okay. Look, on this new initiative, ‘integral to the overall export resource project’, could you explain to us what those words mean? Integral: how you establish that criticality of this particular initiative, this particular facility, or firm's offering to ensure that it is integral to the overall export resource project?

MS GOVAERT (EFIC): Well, what we normally do when we have a rough, initial outline of a transaction, we seek input from our legal department. In the credit submission it is addressed as well. So we do a test, if you like. Integral is a very difficult legal - well, if you can call it a legal term at all. Yes, so that's what we do. In this particular instance I think we even mentioned this transaction at the Board.

MS SCOTT: So a highway or a tollway to a port in Australia could well be integral to overall export resource projects?

MR ARMOUR (EFIC): In fact, we have had extensive discussion internally about this conundrum that you have identified. We would share your concern that an abuse of this power would be not wise, so the purpose of having that internal discussion, the purpose of commissioning internal advice, is to determine whether a reasonable person would find that an asset or a contract is integral to a project proceeding. You know, at first blush a highway would seem to be just one or two steps removed from that; they would have other purposes, for example. Whereas the Greyhound contract, in this case, was for a specific purpose, and that is just one of the criteria in mind.

DR MUNDY: Are you able to give us written advice as to what those criteria precisely are?

MR ARMOUR (EFIC): We could elaborate even today, I think, on the subject of ‘integral’.

MS SCOTT: Yes. Why don't we have you elaborate today and then you might follow up with the documentation that existed prior to this hearing about your definition of the reasonable person test, okay? So I would be keen to know whether a tourist venture that would have export potential would constitute a venture that you would support, or does this initiative only relate to a resource project?

MR ARMOUR (EFIC): No, tourism is an area where we have debated quite extensively and, again, prior to the GFC, probably more on a different frame of reference. But tourism certainly generates offshore earnings and so does education. Those are legitimate offshore earnings. So the question then falls back on, "Why would we do this and why would no-one else do this?" I must emphasise for the commissioners, we constantly ask this question: why are we doing this and why is no-one else doing this; is this us stepping forward or everyone else stepping back. It is a constant debate within the management team. I have asked Felicity to join us to talk a little bit about the EFIC legislation and use of the word "integral".

MS SHAW (EFIC): Good morning, commissioners. My name is Felicity Shaw, I am a Senior Counsel with EFIC. Under Part IV of the act, Part IV sets out the different financial services and products that EFIC is empowered to provide. As you will be aware, each financial service and product has its own eligibility criteria. It could be export contract, eligible export transaction, Australian benefit. I believe in the case of the Greyhound matter, it was a bonding deal. We looked to section 19 of the EFIC Act and the wording in there allows us to provide bonding support for a contract or in relation to the performance of a contract that would be an export contract, in this case the export of a commodity. So it's those words ‘in relation to the performance of’ in the preamble that led us to develop this test of “is this particular element or component of the transaction integral to the ultimate export contract?”

MS SCOTT: Okay. So I just want to explore that a little bit further, I'm sure Dr Mundy will come in as well. So Felicity, if I've got this right, because it was a bonding contract you felt it was within scope; because the tendering process related to a resource project and the resource project was export orientated, you thought it was in scope?

MS SHAW (EFIC): Correct.

MS SCOTT: But how did you prove the "integral" bit?

MS SHAW (EFIC): Well, I guess you look at each - and it's not only for the Greyhound transaction but you look at transactions in terms of components. One transaction I've been involved in - I wasn't involved in the Greyhound transaction - but it looked at a particular - the supplier provided a particular type of machinery that was required to actually exploit the commodity.

MS SCOTT: Yes, I've got that, because I can see that's directly related to the export opportunity. What about a cleaning contract for that particular resource project? Let's say we had a domestic cleaning company interested in tendering for a process, cleaning contract at the mining facility. Would the cleaning be defined as integral provided it had a - - -

DR MUNDY: Let's assume that the cleaning is necessary to certain occupational health and safety standards in the plant once it's built.

MS SHAW (EFIC): Sure.

MS SCOTT: Would that be in scope, do you think?

MS SHAW (EFIC): Potentially. I mean I guess there's a spectrum of circumstances that can be considered, some obviously less so. I guess this is falling - my view is this would fall into a borderline category.

MS SCOTT: What about cooking, you know, catering services? Do you think that could be integral to the - into the export resource project? I mean workers won't survive continuing their operations - - -

MR ARMOUR (EFIC): The example I use, commissioner, in having these conversations internally is supplying milk, fruit and veg.

MS SCOTT: What's the answer?

MR ARMOUR (EFIC): Well, no. I don't think a reasonable person would see that a relatively low value commodity-type transaction like cleaning or cooking or supplying bread and milk is integral to the project. I think the distinguishing feature for us in Greyhound - and obviously we have to form a judgment on the day, and hindsight may prove that our judgment is subject to challenge, but, you know, evidence and experience show that we normally get it right. We have to form a judgment about whether a project is - or a contract is particularly large or involves particular investment by a firm.

So a cleaning company may have to employ an additional five staff. The actual demand on that company to gear up - sorry, do tell me if I'm speaking too quietly. The actual demand on that company to gear up is very limited, whereas with Greyhound this is a significant contract, this is a significant impact on their business. In that sense you look at it and say, "Okay, what are the conditions that sit around this transaction," or, "How do you assess the relative merits of these transactions?" But it's not an easy judgment, commissioner, and in part because this is a relatively new initiative - well, is a new initiative for us. It reflects a concern by government that SMEs are struggling to either gear up to do these large projects which involve some very large contracts or don't have the same appeal, if I can use that word, to the large engineering firms who were undertaking the contracts because they will tend to default to larger, more established companies they're conscious of.

DR MUNDY: So you're saying this is a significant contract in the scope of Greyhound's business?

MR ARMOUR (EFIC): For Greyhound.

DR MUNDY: How many more people will Greyhound employ?

MR ARMOUR (EFIC): I think it's about - I don't know the precise answer to that.

MS GOVAERT (EFIC): Well, they employ directly all the bus drivers.

DR MUNDY: How many?

MR ARMOUR (EFIC): We'll have to take that on notice and respond to you, commissioner.

MS GOVAERT (EFIC): We'll have to take that on notice.

DR MUNDY: Are they buying any new buses to fulfil this?

MR ARMOUR (EFIC): Again, we'll have - - -

MS GOVAERT (EFIC): Yes, they will.

DR MUNDY: How many?

MS GOVAERT (EFIC): Don't know.

DR MUNDY: Could you find that - - -

MS GOVAERT (EFIC): Yes.

DR MUNDY: So part of the reason why they require this - this is a performance bond for them to perform the contract. So is that in any way related to them needing to source the capital to buy these new buses or are they just redeploying them out of their existing fleet as part of the way that they just rejig their network all the time?

MS GOVAERT (EFIC): I think they partly redeploy their existing, but there is someone in this audience, by that way, that knows this transaction intimately. Would it not be - - -

DR MUNDY: Well, it would be helpful.

MS GOVAERT (EFIC): Yes. But he is - Robert is sitting over there.

DR MUNDY: That would be helpful.

MS GOVAERT (EFIC): Yes.

MS SCOTT: Well, Felicity, maybe if it's all right - I don't mind who exits the scene for a little bit, we can swap chairs as we go through.

MR ARMOUR (EFIC): Would you have any more questions about the legislative basis of what we do?

MS SCOTT: Well, we may. People can come and go as needs require. Thank you for coming to the table.

MR DRAVERS (EFIC): You're welcome. My name is Robert Dravers. I'm a Director in the SME and mid-market business.

MS SCOTT: Thank you.

MR DRAVERS (EFIC): Firstly, I'd like to give you some additional information about this contract. The contract value is $105 million. It is a very significant business for Greyhound. The contract period is six years. The performance bond is for six years. There is no bank in Australia that is willing to take risk on Greyhound for six years. There is just not the slightest question about it. What EFIC has done is provide that bond to Greyhound to enable it to win business.

It was an international tender. There were, according to Greyhound, overseas companies bidding for the business. Greyhound entered into negotiations with Bechtel over a period of about two years to establish their credentials to win this business and demonstrate their ability to perform the contract. Part of that ability centred on what they have done in other places such as Olympic Dam in South Australia. The company has no other business in that part of Western Australia. The company has absolutely no intention of operating a bus service, to the best of my knowledge, in that part of Australia, which is extremely short of people and any commercial viability for a bus service.

So I think, in my view, the EFIC support was essential to this company winning the business and it did go to an Australian company where it need not have done. To answer other questions, the additional employment will be about 100 people. There will be about 70 buses deployed on this contract.

MS SCOTT: Thank you very much, it's useful. Can I go back? You said I think that Greyhound indicated to you that overseas companies were bidding for the business. Do you know how they established that or do you know how you can - - -

MR DRAVERS (EFIC):   Well, I can tell you it was an international tender. The tender was put out by Bechtel and Chevron to an international audience. There was nothing to prevent any company with appropriate transport experience in bidding for that contract, and it is my understanding that there was at least one.

MS SCOTT: Okay, so I just want to check. I mean effectively when governments put a tender on AusTender we could call it an international tender every time. How did you establish to your satisfaction that there was an overseas company bidding for the business?

MR DRAVERS (EFIC):   I cannot demonstrate that without asking Bechtel or Chevron who bid for the business, but we are supporting an Australian company win that business to ensure that that business does eventuate to the benefit of Australians.

MS SCOTT: But just to be clear, I don't want to put words in your mouth, but you talked - I'm trying to work out whose word you took that there was an international bid in play. I'm just trying to establish how you found that out.

MR DRAVERS (EFIC):   I can't say I found that out, but what we did do is work with a company that had been identified by Bechtel as the preferred contractor for the business. We gave them the financial support they needed to ensure that they won that business and it couldn't go elsewhere.

MS SCOTT: So let me see if I've got this right. Bechtel introduced you to Greyhound?

MR DRAVERS (EFIC):   No, as a matter of fact the chairman of Greyhound found EFIC.

MS SCOTT: But would I be right in thinking that there is no documentation, no evidence available to us, which suggested that there was in fact an international bidder for that contract?

MR DRAVERS (EFIC): Well, we don't get told that sort of information by the project principal or the engineering procurement construction manager, so that information isn't necessarily publicly known.

MS SCOTT: No. So for all intents and purposes we could still be looking at an entirely domestic tendering process?

MR DRAVERS (EFIC): I cannot confirm or deny that.

MS SCOTT: Fair enough, I understand.

MS GOVAERT (EFIC): Can I just make one additional comment? It is obviously the working capital and the performance bond, the financing aspect of it as well.

MR DRAVERS (EFIC): Yes, and I would say - sorry. As I said earlier, there is nothing to prevent a foreign company coming in. These are buses that they have to acquire. Greyhound don't have buses lying around. These are new drivers that they have to hire. So a foreign company is just as capable of doing these things as an Australian company. Indeed, the buses will significantly - you know, a number of them will be brought in from overseas. There is no question that there is potential there for foreign competition, and it is my belief that there was one European company bidding for the business, but I don't have that in writing and I can't confirm it.

DR MUNDY: Are you aware of any Australian companies bidding for the business?

MR DRAVERS (EFIC): It's not a question I asked.

DR MUNDY: Well, you're aware of one foreign company. So you're not aware of any Australian companies but you happen to be aware of one foreign company?

MR DRAVERS (EFIC): Yes, correct.

DR MUNDY: There is no sense in which the drivers in question will be recipients of 457 visas or anything like that? As far as you are aware these drivers would be recruited in Australia?

MR DRAVERS (EFIC): They have to recruit drivers with three years minimum coach driving experience - - -

DR MUNDY: With Australian driving licences?

MR DRAVERS (EFIC): No, three years driving experience. It is their intention to deploy some of their staff there and employ others into their existing routes and to recruit as required. Now, "as required" will be to recruit as many as they can within Australia, and if necessary to look overseas.

DR MUNDY: As far as you know the buses will be imported? To the extent that new buses are - I can't remember whether people still make buses - - -

MS SCOTT: Yes, they still make buses.

DR MUNDY: They still make buses? Okay.

MR DRAVERS (EFIC): Well, they have a contract with Scania to - - -

DR MUNDY: Scania, okay.

MS SCOTT: Can I return to the - it's almost like there's a second layer of criteria in this area, because you mentioned that it has to be significant for the business, it can't be a low value, you didn't think cleaning or cooking sounded like the right area where EFIC would get into. Have you established what the secondary criteria are?

MR ARMOUR (EFIC): Not formally, commissioner, no.

MS SCOTT: No? Okay.

MR ARMOUR (EFIC): We have - because the frequency - it's a new facility and the frequency of applications right now is literally a handful.

MS SCOTT: Right.

MR ARMOUR (EFIC): We are feeling our way through this process.

MS SCOTT: Okay.

MR ARMOUR (EFIC): I expect we will need to respond to conditions in the market. I expect we will need to respond as government policy develops its thinking on this issue.

MS SCOTT: Okay.

MR ARMOUR (EFIC): What we have identified - and I'd like to take a step back from the Greyhound example, I do understand the questions that you're asking there.

But if I look back over a very long period, I will make an observation from that experience, and that is when a large firm like Bechtel (and I don't mean to single them out but it's an easy example) when a large firm like Bechtel considers how to subcontract, they have a process that they have established, from let's say Bechtel US. But again, I don't mean to single out Bechtel, this relates to any of the major companies, large engineering companies, multinationals that are working here. They have a process that understandably reflects the scope of their global operations. There are certain ticks - certain boxes that have to be ticked, there are certain processes that have to be followed. It is a business that has operated globally on scale. So they tend to work with people they tend to work with, if I can be colloquial about it. So they're quite comfortable re-contracting with people from other countries on the basis that they have a proven record of delivery.

Now, there is, in my view, a certain logic to that, a certain commercial logic to that, but there is also undeniably what you might term an information asymmetry there, because they don't have the protocols that go back into head office to say, "Look at this small Australian firm." The local manager for these operations - and this is - I see your look, commissioner, but - - -

MS SCOTT: I'm just trying to characterise Greyhound as a small - - -

MR ARMOUR (EFIC): No, I'm stepping back from Greyhound, commissioner, sorry - - -

DR MUNDY: Hardly a name that's not familiar to American television.

MR ARMOUR (EFIC): Yes, indeed. Point taken, commissioner, and again, I'm stepping back to look back over the past 10 years of why this issue has been - I think it has been accentuated by the resource boom but this is an issue that has persisted for a very long period of time, and that is, large multinational companies working in Australia will tend to subcontract to recognised names they've worked with in other markets. There is a certain flow of business that has increased as a consequence of the resource boom that is perhaps opening the door for Australian firms to compete. Now, the question is whether they can overcome this information asymmetry.

One of the efforts that we've made - and again, repeatedly, commissioner, I don't want to come back to this point but I can recollect sitting with Bechtel over the years saying, "I don't understand why" - and again, not to single them out, "But I don't understand why you don't contract with more Australian SMEs." Basically their answer is, "We have a big process. We have a big process that has a bias towards big firms." Well, the challenge for us is to get the judgment right about whether we've identified the right firms and whether they have the capability of actually entering into this market in competition with established players.

DR MUNDY: I've had some experience in contracting for major infrastructure developments, and there is a degree of truth in what - particularly in highly specced technical componentry. But the circumstances being described to us here is that Greyhound had actually won the contract before they came to you. That's what your colleague said. So the fact that they weren't - the issue about contracting with Australian firms had actually been gotten over.

MR DRAVERS (EFIC): Sorry, can I just clarify that? They had been identified as the preferred contractor - - -

DR MUNDY: Okay.

MR DRAVERS (EFIC): - - - but they had not signed on the dotted line, because one of the things that they needed to put up was a performance bond. That is critical to them then being able to sign the contract. So at the point where somebody becomes the preferred contractor, we can look to provide the bonding that is required to enable them to win the contract.

DR MUNDY: So it is possible that if they did not proceed the next preferred contractor would have stepped into the breach?

MR DRAVERS (EFIC): More than possible.

MR ARMOUR (EFIC): Commissioner, I think rather than build a case around hypotheses we should come back with the facts.

MR DRAVERS (EFIC): Yes.

MR ARMOUR (EFIC): I think rather than generalise from one specific example you should step back and look at the body of work that we're doing. I have informed the commission that this is a relatively new initiative. I can't say we've got it perfect yet because we're trying to find our way. I can identify there are information asymmetries that concern us, and that's what we're trying to address. But this line of questioning I think is unproductive from the perspective that we need to actually go back and develop the argument.

MS SCOTT: That's a good point, Angus. So in some ways because it's such a recent initiative, you're effectively learning by doing. I mean each proposal comes forward, you think about it, and you're in effect developing criteria as you go along. Is that a reasonable characterisation of this?

MR ARMOUR (EFIC): Right.

MS SCOTT: Okay. So you're developing criteria as you go along. When did this go to the board? Is this going to be in a board paper at some point? Sorry, I didn't mean Greyhound, I mean the initiative.

MR ARMOUR (EFIC): Yes, that's right, we understand.

MS GOVAERT (EFIC): We've covered it in the SME business development report and in the board presentation, but we didn't put up a separate product paper, if you like, because it is just then - if it fits within our mandate, and it is just an extension of what we do normally. The product is not any different, it's performance bonds or working capital or a combination of both.

MS SCOTT: So I just want to clarify here - - -

MR ARMOUR (EFIC): But the specific example we talked about we actually did discuss that at the board.

MS GOVAERT (EFIC): Yes.

MS SCOTT: Okay, all right.

MR ARMOUR (EFIC): Greyhound was discussed at the board.

MS SCOTT: Okay, let's see if I get it right. This particular initiative, which is hot off the track - that's not the right phrase, but it's newly-developed and developing. While an individual example has been discussed at the board, Greyhound, and while you see it as an extension of your existing work and you're confident that it fits within your legal framework, we're not going to find a piece of paper which says, "Board, this is where we're going to go. This is how much money we've set aside. This is the criteria, subject to further clarification." We're not going to find something like that which sets out all the things?

MR ARMOUR (EFIC): Well, as Andrea says, in her business development report there will certainly be a paragraph that says, "Board, this is the direction we're going."

MS SCOTT: So you've got a paragraph which says - well, Andrea, I don't want to put words into your mouth. What would be sort of the sign-off that you got from the board on this initiative?

MS GOVAERT (EFIC): There is no formal sign-off on the proposal as such. As a marketing initiative, as a business development initiative, it was addressed in a board paper and it was underpinned by the fliers that we've designed which was shown to the board and which set out the criteria in a nutshell, for exporters. We can send you the - - -

MS SCOTT: Okay, well, we'll - - -

MR ARMOUR (EFIC): But the board would have turned to your question precisely, the board would have noted.

MS SCOTT: Look, we would be keen to see that documentation.

MS GOVAERT (EFIC): Yes.

MS SCOTT: And I guess what I'm interested in - we've had a look at your credit manual and documentation that goes around your larger initiatives - is what documentation exists. Given that things are happening a little on the fly, you're learning as you're doing, and this is a new initiative, you wouldn't really have a manual on this now, would now?

MR ARMOUR (EFIC): No, and, commissioner, the manuals that you have in your possession and the credit manuals are directly relevant to this initiative, as are the product descriptions we have given you in the past. As Andrea says, there are actually no new products associated with this, there are no new credit guidelines. The question is - and we tease out - is this integral, what are the competitors circumstances, what are the issues that are being confronted.

MS SCOTT: Okay.

MR ARMOUR (EFIC): We start with the normative question of why should we do this, and explore that. So that is really the area of where we're learning as we're doing it, as you put it. But in terms of the actual financial implications for the corporation, in terms of the actual risk management of products, et cetera, it would be completely consistent with the material you have already.

MS SCOTT: That's good, that's very helpful. Angus, what money have you assigned to this new initiative; you know, the contractors and subcontractors?

MR ARMOUR (EFIC): It would be within existing limits, commissioner. It would be by company, for example, in terms of a credit counterparty limit, and, again, you have the information on that.

MS SCOTT: So you haven't earmarked a particular amount?

MR ARMOUR (EFIC): No. Commissioner, we don't tend to headline amounts like that. I mean, we tend to - - -

MS SCOTT: No, all right. But I'm not asking you to publicly indicate what the amount is; I would like to know whether you have earmarked a particular amount for this initiative. I mean, you have got flyers out there. I've got that right?

MR ARMOUR (EFIC): Yes.

MS SCOTT: You have got flyers out there. You have got, you know, "We're interested in doing this business." I guess, Matt, in your interactions with the Department of Industry or indicating that you are open to this sort of work. I am interested what initial quantum of business you think you will be doing in this area.

MR ARMOUR (EFIC): It's a very important point you raise, commissioner, because at the end it is a matter of having a dialogue to understand better how we think. We think in terms of limits rather than objectives, so it's not our purpose to go out and do 200 million of this facility if 5 million is all that's required. It is our objective to stay within prudent risk limits for the companies we're working with. If we were to run this program for the next two years and end up with a portfolio of $20 million, given that it is a very marginal cost to promote and still consistent with government policy, from our perspective that would be a good outcome; we would be participating in something that is a whole-of-government concern, we were doing that prudently and financially self-sustaining. This is the asymmetric credit selection I described earlier: we're not actually seeking to grow that portfolio, but it is in response to a problem that may be emerging from the market.

MS SCOTT: So if you're more comfortable with the word "limit", has there been a decision either by the board or by management, or has Andrea made a decision, which would be something like, "We would be keen to see a limit of X in relation to this contracting or subcontracting?"

MR ARMOUR (EFIC): Again, the existing limits still apply. So the limits that you're contemplating - or that I think you're seeking, in a sense of a consolidated revenue context, you're seeking an envelope that we're spending from, whereas we're saying we will contemplate applications for individual companies but they will need to pass our current tests, and the amount that we provide will need to be consistent with our current limits. So there is no envelope we're seeking to spend. As I say, as the market gap falls, that is where we should fall. So if the market gap is five million, we should be at five million; if the market gap is 100, we should be at 100, subject to prudential limits. Again, I think we're slightly at cross-purposes, but I am trying to impart that we don't actually seek to achieve a portfolio of a certain size.

MS SCOTT: All right, I think I've got that. This new initiative, in effect you are hanging out your shingles and saying to contractors and subcontractors working with the resource sector, "Come to us and we may well be interested in your business." That is effectively how it works?

MS GOVAERT (EFIC): It is a bit more subtle than that, because we also work with the banks in this. So the major banks - ANZ, Westpac, but also the others - have established specific natural-resource supply-chain finance groups and we have spoken to the banks as well, because although technically we can issue performance bonds ourselves, as you know, we prefer to work through the banks.

MS SCOTT: Okay, and the research that went on before this, could you comment about that; that is, the evaluation you undertook beforehand or the research you undertook to establish the need for this initiative. Could you talk about that?

MS GOVAERT (EFIC): Well, there are two aspects to it, and I think one of them is really mainly driven by the government - maybe, Mat, do you want to elaborate? We have had extensive discussions with the government on this issue.

MS SCOTT: Okay.

DR MUNDY: Sorry, can we ask who those discussions with the Commonwealth were with?

MR HOCKEN (EFIC): Yes, sure. That's the Department of Industry: it's with Deb Anton at the Department of Industry, Murray Fearn, Katherine Smith; the main people who are particularly working on the Resources Sector Supplier Advisory Forum. Other state governments are obviously involved in inputting into that process; state and territory governments.

DR MUNDY: No discussions with the Commonwealth Resources Department?

MR HOCKEN (EFIC): Sorry?

DR MUNDY: No discussions with the Commonwealth Resources, Energy, and Tourism Department?

MR HOCKEN (EFIC): I expect so within the Department of Industry.

DR MUNDY: But in - - -

MR HOCKEN (EFIC): No, not with - - -

DR MUNDY: But your organisation hasn't.

MS SCOTT: Mat, in those discussions, I imagine it works like this, having been in the policy space previously, is that people would be very interested to hear that EFIC has got this capability and within what you see as your remit. But I won't be surprised that they think there is some quantum that is likely to be available. There haven't been discussions about potential quantums at all?

MR HOCKEN (EFIC): They are looking to establish that. It is one of those things which it is difficult to get good data on the quantum that is out there.

MR ARMOUR (EFIC): I think you are talking about - they are asking how much we will spend. Is that your question, commissioner?

MS SCOTT: Yes, that's right.

MR HOCKEN (EFIC): No, that question hasn't been asked.

MS SCOTT: Okay, good, that's clear. Thank you.

MR ARMOUR (EFIC): Mat was talking about them identifying - - -

MS SCOTT: Yes, I understand. I just want to check, this initiative reflects public statements by the government, overtures to EFIC to become involved. Have I got that right? You have had overtures from government departments to become involved in this initiative?

MR HOCKEN (EFIC): They have sought our advice on some of the issues which are coming out from the forums, so they are obviously in contact with industry, as I said, with unions, with other governments who are raising these issues. So they have sought our advice with - you know, we see those issues occurring as well.

MS SCOTT: And then you were able to say, "Actually, we have got this capacity." Is that how it has worked?

MR ARMOUR (EFIC): If I can say that, that is exactly right, commissioner, and it also reflects the initiative we took with Screen Australia. That literally came about from a conversation where the chairman of Screen Australia was speaking with a film producer and identified the issues that, for smaller-budget features, there was simply a gap that the commercial market wasn't filling, that it was very restricted in the Australian domestic context. So EFIC as a statutory authority does have the ability to be more flexible in taking up these policy concerns and trying to respond to them. We do keep people informed, and I don't think Mat mentioned it, but we actually met with the minister's office to brief them on what we were doing and, again, we got very supportive feedback in the sense of what we were doing.

MS SCOTT: Okay. So, Mat, you're confident that the minister's office understands the direction that you are heading in?

MR ARMOUR (EFIC): That is the minister of industry.

MS SCOTT: The minister of industry.

DR MUNDY: So you haven't had these discussions with Minister Emerson's office?

MR ARMOUR (EFIC): We may well have; but, again, it certainly would have been noted by the board that we were going in this direction. So, again, we rely to some degree on the conversations that exist between the Department of Industry - - -

DR MUNDY: Just to be clear about this, because we have had an awful lot of industry ministers in the last few months, which minister was the minister for industry at the time?

MR HOCKEN (EFIC): That would have been Minister Carr.

DR MUNDY: Minister Carr, okay.

MS SCOTT: Thank you, that's good. Angus, given that we're in Sydney, would it be possible for your team to be in contact with your office and be able to make available to us before we leave today - in fact, it would be great if we could do it straight after lunch - some of the flyers; a hardcopy of the flyers. If it's possible to get that paragraph from your board paper, that would also be most welcome. If you have already now made decisions - I don't know how soon it is in your development progress; but, Angus, if there's half a dozen companies, a dozen companies, 20, I don't care, if you have already made decisions in relation to a number of these arrangements, we would be keen to get a list of what the size of the transactions are and who they are with.

MR ARMOUR (EFIC): I am only conscious of two.

MS GOVAERT (EFIC): Yes.

MS SCOTT: Okay, that's fine.

DR MUNDY: What's the other one?

MR ARMOUR (EFIC): The one we cited - Lean Field.

DR MUNDY: Okay, yes, we're aware of that.

MR ARMOUR (EFIC): Commissioner, there is no question we can get the flyers to you. The issue with the board paragraph might simply be that anyone who has access to those papers is currently in the room, so that might be a tomorrow-morning thing, if that's okay.

MS SCOTT: I'm trying to remember my geography of Sydney. What would it be, Angus, about a 10-minute walk?

MR ARMOUR (EFIC): It's more the getting in and finding the paper. I can't off the top of my head tell you which day the exact report - - -

MS SCOTT: Sorry, I thought it was a recent thing. This happened some time back, did it?

MR ARMOUR (EFIC): Three, four, five months ago. You have a conversation with the board - and certainly the Greyhound conversation was December, so we would have talked to the board prior to that about our thinking around this facility. But that is the length of time, the gestation period, for reflecting on whether this is appropriate and having conversations around particular transactions.

MS SCOTT: Okay. In terms of the market gap, Andrea, or maybe this is for Robert, if a firm identifies to you that they have not had a success in obtaining the support they require from their financial institution, would that represent the sort of evidence that you require to then think, "Right, we're dealing with the market gap." Would that be - - -

MS GOVAERT (EFIC): No. Generally, as I said earlier on, though we can issue performance bonds - technically we can do it ourselves - but we normally have a direct conversation with the bankers. Because all our products are contingent, you end up issuing a guarantee through a bank, so you would have that conversation.

MS SCOTT: Okay, that's clear.

DR MUNDY: So there's a bank involved in the Greyhound transaction?

MS GOVAERT (EFIC): Greyhound has bankers, but in this instance we have issued performance bonds ourselves.

MS SCOTT: In the other instance of Lean Field?

MS GOVAERT (EFIC): I think it is a combination of working capital and a bond.

MS SCOTT: Okay.

DR MUNDY: That has been done through a bank rather than directly?

MS GOVAERT (EFIC): That has been - the working capital is done through the bank, yes.

DR MUNDY: Okay.

MS SCOTT: Okay, thank you. That's useful. We are keen to probably have a break now and resume in three quarters of an hour. That would have it as half past 1. Would that be all right with you?

DR MUNDY: Otherwise we will have to start a discussion and then stop and start again, so it is probably easier if this is a natural break for where we want it to go.

MS SCOTT: Yes. All right, I think that's what we'll do. Ladies and gentlemen, we will break now and resume promptly at 5 past 1 with EFIC. We will continue our questions then. Thank you very much.

(Luncheon adjournment)

MS SCOTT: Good afternoon, ladies and gentlemen. I'm pleased to say that we're going to resume the hearings now. Angus, any opportunity to produce that flyer?

DR MUNDY: Yes, they're there.

MS SCOTT: Great, thank you.

DR MUNDY: Angus, the Brookfield transaction, which has now entered information which is in the public domain, one of the issues that has concerned us with that is it's a very large project being undertaken by one of the world's largest infrastructure companies. We are just interested to understand and just clarify whether it is EFIC's view that, without its assistance, the credit enhancement that was required by Brookfield could not have been obtained; and I guess we're also interested in how is it that you ascertain or separate an issue between the particular credit preferences of individual corporations, which may reflect their corporate strategy or their own desires, and something which might be more systematic of a problem, requiring intervention by a government agency such as yourselves.

MR ARMOUR (EFIC): Commissioners, I might ask Mr Peter Field to join us.

MR FIELD (EFIC): Good afternoon, commissioners. Peter Field, Executive Director of Origination and Portfolio Management at EFIC. Commissioners, is there a particular way you would like me to address that broader statement?

MS SCOTT: The way I would paraphrase Dr Mundy's question is that Brookfield is a very large enterprise. Is it your assessment that the project would not have gone ahead without your involvement, given the considerable resources available to Brookfield?

MR FIELD (EFIC): At the end of the day, we have to satisfy ourselves that we believe there is a gap to be filled here. In that case we went through a process of understanding the drivers behind Brookfield's investment in that rail upgrade; we had to take a view of the commercial circumstances surrounding the transaction; we had to look at the risk that they might have to consider taking with respect to, effectively, taking project-related risk on that rail line. Because if that upgrade had been completed and the project subsequently failed, then that money spent on that rail line would effectively had been wasted. So we had to look at the broader structure that they sought to implement and then respond to the issues that they identified in the shortcomings of actually implementing that financing plan.

MS SCOTT: I just want to clarify again, is it your view, Peter, that the project would not have gone ahead without your support?

MR FIELD (EFIC): I think it is difficult to make that clinical analysis as to whether it would or it would not. The issues that they were dealing with at the time, there was a clear hesitation on their part to proceed. In fact, the delivery of the upgrade arrangements was substantially delayed as they found a way to finance it in a way that would minimise a risk.

MR ARMOUR (EFIC): If I can elaborate, commissioner, stepping back to Commissioner Mundy's question, it is our job on a day-to-day basis to test what is happening in the market. That is why we are involved in the market; we have to test what they are telling us. We wouldn't accept at face value what we might be told; we have to go out and determine whether it has some veracity. So on a general level we will always test why we are involved and what the basis is that we are being asked to provide support. In this case I think the reference to Brookfield as an institution is misplaced, because the question is how do the banks fund this project as a whole.

I mean, there is an ideal, optimal structure for any project in a balance of debt and equity, but suggestions have been made in the past that they are substitutes and that is not true. So in the context of what was needed for the financing as a whole, which Peter describes, there was a representation to us that there was a gap, and we tested that and we found the logic compelling. But I think our decision is best judged by the evidence, and the evidence - again, these are received from the banking sector, from the private market - is that there are gaps that we do need to fill.

MS SCOTT: Okay. But I just want to be quite specific, your professional judgement was this project would not proceed without your support?

MR ARMOUR (EFIC): On the day.

DR MUNDY: Is it also your judgement that there were considerations around that, about whether it would not proceed, which go significantly beyond the credit preferences of Brookfield itself.

MR ARMOUR (EFIC): Again, I don't think it's so much an issue of Brookfield's credit preferences; it is what Brookfield's syndicate of financiers expect. Again, you're seeking to transfer to the risk onto the Brookfield balance sheet; whereas, we are more broadly speaking about the financiers of Brookfield, not just Brookfield as an entity on its own.

DR MUNDY: So what you are saying is that - I mean, I think this is an important threshold issue. You make the statement that debt and equity aren't substitutes. They're not, but they're fungible at the margin. I guess the real question we're trying to get to here and part of the issue is are these gaps that you're perceiving a function of the business choices that are being made by companies like Brookfield and their financiers, or are they symptomatic of something that requires policy intervention by yourselves.

MR ARMOUR (EFIC): Again I would caution against generalisation, but in this particular case the underlying risk that the commercial market was concerned with was an unnamed Chinese bank, and we have been asked not to name the Chinese bank. Now, your observation is on the rating in that bank, I understand that. But the concern of the private market is whether they, the private financiers, are willing to take a 10-year exposure to this Chinese bank versus, let's say, a two-year or a three-year exposure. At that rating there is more appetite for a short-term limit of two or three years. For a project of this dimension, an infrastructure project, there is a requirement for some level of certainty, some level of term funding. The financiers look through that and say, "Well, hold it. I'm being asked to take a risk on a Chinese bank, whatever rating, for a 10-year time frame. Is that something I'm comfortable doing." I can say pretty categorically that, no, there is not a great deal of bank capacity appetite for that structure of transaction. It's not a preference, that is simply the nature of how an infrastructure project would be funded. So I think that is an issue that needs to be recognised.

MS SCOTT: Thank you.

MR ARMOUR (EFIC): Sorry, if I could just elaborate for a second, commissioner. The other element I would like to just highlight - it may not be relevant to your question, but I think it is important to say that our involvement did help EDC of Canada - Export Development Canada, another export credit agency - provide actually substantially more than they might have otherwise in supporting this transaction. So we have a crowding-in impact that I think is important to acknowledge as well.

DR MUNDY: In your submission to the review being conducted by Dr Henry for the Asian Century white paper, or whatever it is called, mention is made of your involvement or potential involvement in the Ichthys natural gas project. Can you outline to us what that involvement is or is likely to be and where it is up to?

MR FIELD (EFIC): Yes. EFIC was selected as one of six export credit agencies to form what was described as a pathfinder group.

DR MUNDY: Selected by who?

MR FIELD (EFIC): By the sponsors.

DR MUNDY: And they are?

MR FIELD (EFIC): They are Total, 24 per cent, and Inpex Corporation of Japan, 76.

MR ARMOUR (EFIC): Total are French.

MR FIELD (EFIC): That selection was based on our ability, effectively, to catalyse the support of those other five export credit agencies. So they wanted to provide a framework, establish it amongst the six export credit agencies that would start this process, which would then roll into the balance of the financing at which we would include a syndicated bank piece. So our function was to, effectively, negotiate the terms and the conditions of the project financing for the project.

DR MUNDY: You will be providing some financing or guarantees?

MR FIELD (EFIC): That is the implication of being within the pathfinder group, yes. They are intended to be participants in the debt financing.

DR MUNDY: So you will be a participant in the provision of the debt?

MR FIELD (EFIC): At this point, that is our intention, to pursue an approval from our board to participate in this financing, yes.

DR MUNDY: So you will be providing debt?

MR FIELD (EFIC): We will be providing finance. It is undecided whether it will be in the form of debt or in the form of a guarantee.

DR MUNDY: Okay.

MR FIELD (EFIC): And it has not been approved.

DR MUNDY: No, that's fair enough. Is it expected that it will be all on the Commercial Account or is there an expectation there may be some on the National Interest Account?

MR FIELD (EFIC): There is no expectation of referral to the NIA, so Commercial Account only.

DR MUNDY: Just moving on. There was an article in the Financial Review on a date which I have just mislaid. It was a couple of weeks back, 14 March. Talking about the financing of the Roy Hill mine rail and infrastructure. Roy Hill is being developed by Hancock and the article says, and I quote, "But it is understood that

Hancock will avoid a bond rating, preferring to procure some commercial bank project lending backed by export credit agency finance." The context of this is difficulties about the transparency of the Rinehart family trust or otherwise. Is EFIC one of the export credit agencies mentioned in this article?

MR FIELD (EFIC): I couldn't tell you whether it was their intention to implicate EFIC or not, but I can tell you that we are not in any meaningful discussions with anybody with respect to Roy Hill.

DR MUNDY: Okay, thank you.

MS SCOTT: Angus, I am interested in exploring why resource projects in particular are your area of onshore interest and not, for example, general infrastructure. Could you explain why particularly the resource sector?

MR ARMOUR (EFIC): I might start by giving some background to our involvement in resources and I'll come back to - - -

MS SCOTT: No. I'm pretty conscious of time here, Angus. If you could keep your answer quite contained to the question I asked, that would be good.

MR ARMOUR (EFIC): Then the most concise answer would be that has been our perception of the demand at this stage; that we have not been approached by commercial financiers with an issue regarding projects as you describe. So as I said previously, we are out testing the market. We have deep linkages with and an understanding of the market. We have relationships with the banks and the project and infrastructure groups. Our assessment at this point - and I can't recall a project in the nature that you have described.

MS SCOTT: What about power generation or power distribution? We know there is going to be very considerable investment in future years in these two areas and it may be the case that the people that you test the market with are - banks may come forward to you and say there is a considerable opportunity for EFIC in supporting power generation or power distribution. What would your attitude be towards these two areas?

MR ARMOUR (EFIC): In the first instance I would find it hard to argue it was integral in terms of our act, if you're talking about developing a large-scale power project that serves the grid. I'm not sure how that would relate to our legislation, whether it would be integral. Is that the question?

MS SCOTT: Yes, that's what I'm asking.

MR ARMOUR (EFIC): Okay. Now, that is my initial response. Now, commissioners, I have to say we have been approached by other parts of government to talk about our experience in this area, both Clean Energy Group, et cetera.

MS SCOTT: Yes, I understand.

MR ARMOUR (EFIC): To talk about our experience and capabilities in this area. But that's not, from my perspective, with the outcome that EFIC provides the support to government, but simply seeking our advice on how it might be done.

MS SCOTT: So integral to a resource project wouldn't be, for example, a power generation facility at Mount Isa?

MR ARMOUR (EFIC): Well, a small-scale one, if it links in to a particular project, is arguably integral. I'm sorry, commissioner, that is why I was trying to clarify what you were asking about. Talking on a big scale, because I had in my mind the discussions we had with the Clean Energy people and the financing of Victorian brown coal, et cetera. That is one end of the scale. It is large, like a large resource project, that is not something that is integral.

MS SCOTT: So brown coal, no.

MR ARMOUR (EFIC): Well, any large - - -

MS SCOTT: Black coal, yes?

MR ARMOUR (EFIC): No, it's scale, commissioner.

MS SCOTT: It's scale, right.

MR ARMOUR (EFIC): So in this case we would say - unless you can correct me, I don't see a large power project serving the grid having that necessary relationship to an export purpose; it serves many reasons. It is a bit like the question you asked earlier about highways and other forms of infrastructure. We put that in a particular category. If you are talking about a firm that is supplying componentry or expertise for a small power plant that is dedicated to a particular mine that is exporting, then there is an argument, certainly, to be contemplated for integral.

DR MUNDY: For example, there have been some suggestions about network augmentation projects to link Mount Isa up with the backbone spine grid that runs up and down the great divide. I think it's called the Copper River?

MR FIELD (EFIC): CopperString.

DR MUNDY: CopperString, motivating primarily an argument about development of processing facilities and potentially up into the Gulf of Carpentaria. So if there was a strong export resources flavour to a project like that, would that - or do you actually need to really tie it down to one plan?

MR FIELD (EFIC): I think we have to look at the substance of the circumstance. We did look at CopperString - sorry, we were brought CopperString as a proposition and we rejected it.

DR MUNDY: On what basis?

MR FIELD (EFIC): I think it was seriously underdeveloped when it was shown to us in the first place. We had questions about its economic viability.

MS SCOTT: Peter, have you gone with the alternative though, in supporting the alternative project?

MR FIELD (EFIC): I'm sorry, I don't follow- - -

MS SCOTT: Has EFIC provided support for the alternative proposal that was around?

MR FIELD (EFIC): The alternative being?

MS SCOTT: A facility at Mount Isa fed, I understand, by gas.

MR FIELD (EFIC): A gas-fired [power-station]- - -

MS SCOTT: Yes.

MR FIELD (EFIC): Yes, there was.

MS SCOTT: Are you supporting that project?

MR FIELD (EFIC): No, we are not.

MS SCOTT: Okay.

MR FIELD (EFIC): Again, there was an approach from one of the engineers in relation to that project, but in the end no support was required.

MS SCOTT: Angus, when it comes down to it, not articulated anywhere on paper, but in your mind you can see a distinction between projects that should be within your remit and those that are outside on the basis of - and I think you have mentioned scale, you have mentioned closeness to export. So it doesn't have to been resource; I mean, a resource project is not good enough, is it?

MR ARMOUR (EFIC): It has to be "integral", is the word that we focus on in terms of our legislation.

MS SCOTT: No, but it can't be a brown-coal project for domestic consumption. That would not pass muster in your mind. Provided it is directly linked to an export project, then that is okay?

MR ARMOUR (EFIC): Well, it is open to discussion. I don't want to say it's okay.

MS SCOTT: Okay, open to discussion. So that's why a coal loader is open to discussion but a toll road to a port would not be within the remit?

MR ARMOUR (EFIC): I think because the coal loader has a very clear dedication, whereas the toll road could serve many purposes.

MS SCOTT: Okay, so one is scale, one is dedication, one is closeness to the export. Are there other characteristics that we - - -

MR ARMOUR (EFIC): I would reflect on the discussions we had with government with 2006; I think those are still relative guidance. But for most of the projects that you're contemplating with your question, it is actually a discussion we had with the board, given the scale involved. So there would be a need for us to test pretty rigorously with departments and with the board before we proceeded in anything.

DR MUNDY: There have been discussions from time to time in central Queensland and in parts of Western Australia about, dare I say, fly-in fly-out workforces and the desire to build fairly substantial aviation facilities for the general enhancement and development of what is essentially a resources region. Not tied to any particular projects; just there to support the general activity. I guess what I'm trying to tease out here Angus, is there in your mind a particular nexus that needs to be drawn with a particular project; or could you conceive of a circumstance where it may be, you know, this is what happens in this region and this will support the export activities of the region?

MR ARMOUR (EFIC): Commissioner, I confess I'm completely unaware of the facilities that you talk about there, so I don't really have a point of reference to draw a conclusion.

DR MUNDY: Let me put it in tourism assets, and the same question applies. A major tourism region, it has often been talked about the need for an international airport on the Whitsundays. No particular project; it would just help export earnings from tourism. I'm just trying to see where the link is. Is it a particular export activity generally or specific projects?

MR ARMOUR (EFIC): We tend to look at specific projects, because that gives us a better assessment of the risk that we're being asked to undertake and it also gives us a clearer picture of what is the shortfall in capacity and what is driving the shortfall in capacity. The further away you get from that linkage the more difficult it is for us to represent what is happening in the market and what are the risks we are being asked to adopt.

DR MUNDY: So the linkage with Wiggins Island is there is this set of coal mines which you know about?

MR ARMOUR (EFIC): Well, the full risk around that project is derived from the ownership of those mines.

DR MUNDY: Okay.

MS SCOTT: This is a series of short questions. I just want to confirm for the record, Angus, that EFIC doesn't provide subsidies?

MR ARMOUR (EFIC): Correct.

MS SCOTT: That you achieve a commercial return on your facilities?

MR ARMOUR (EFIC): We price at or above market, which implies a commercial rate of return on a transaction.

MS SCOTT: You indicated today that you were a price-taker. Would that potentially entail, in some cases, undertaking a transaction or a facility at a loss?

MR ARMOUR (EFIC): Not that I can think of in 20 years. As a matter of fact, we reject transactions on the basis of - - -

MS SCOTT: There is quite a discussion in our draft report and in your response to our draft report about rates of return. On page 154 or thereabouts we have a discussion about return on equity for EFIC after tax. We say, taking a long view, that appears to be just over the bond rate, on average. Do you have trouble with that statement?

MR ARMOUR (EFIC): I'd ask our Chief Financial Officer to join us on this section, commissioner.

MS SCOTT: Thank you, yes.

MR NEILSON (EFIC): Stuart Neilson, Chief Financial Officer at EFIC.

MS SCOTT: Thanks. In this case I'm not actually asking you about what's the right point of comparison, I just want to seek your view on whether you agree that after-tax rate of return on equity for EFIC is, on the long term, around the 10-year bond rate?

MR NEILSON (EFIC): I think the information we have provided shows that we report our numbers on a pre-tax basis, and the pre-tax return is above the bond rate. I think you have got a table that shows, if you apply tax rate to that, then it would be at or above the 10-year bond rate, yes.

MR ARMOUR (EFIC): Ceteris paribus.

MR NEILSON (EFIC): Yes.

MS SCOTT: So I just want to check. You don't have trouble with the statements we have got in there regarding the - sorry, I just had trouble hearing then.

MR NEILSON (EFIC): Sorry.

MS SCOTT: I just want to confirm that you don't have any concerns regarding our characterisation that EFIC's after-tax return is around the bond rate?

MR NEILSON (EFIC): You're saying after-tax return?

MS SCOTT: I am.

MR NEILSON (EFIC): We don't pay tax.

MS SCOTT: Yes, I know that.

MR NEILSON (EFIC): So the after-tax return that we would generate would be probably around, on average, 4 per cent, if you apply an arbitrary tax rate of 30 cents in the dollar.

DR MUNDY: Would there be any reason to expect that there might be things that would lead to lower effective tax rates, by anything material?

MR ARMOUR (EFIC): I wouldn't rule it out. I think that is the point we're making is, commissioner, based on your assumptions around a tax rate, you can construct that graph. But I can't warrant to the assumptions and I can't say at this point what activity would - - -

DR MUNDY: Sorry, Mr Armour, you probably didn't have the opportunity to see your Chief Financial Officer, as you were facing us. But I got the impression he was suggesting that it might be a per cent - perhaps there might be something, but not an awful lot. Or you would need to go and do some work to form a view?

MR NEILSON (EFIC): All I'm suggesting is that we know what the corporate tax rate is, we don't pay tax. So to imply a particular tax rate would require some work on our behalf to actually calculate what the after-tax return would actually be.

DR MUNDY: What your effective tax rate would be, allowing for any - - -

MR NEILSON (EFIC): Yes, so in order to respond to the question I would be having to make some assumptions.

MS SCOTT: Okay. One of the conclusions we make in this draft report is that the rate of return, given the nature of the risks of the activities you're involved with, doesn't seem commensurate compensation for risk for the Australian government for the tax payers. That is effectively what one of our conclusions is in the draft report. I would be interested in your comment on that.

MR NEILSON (EFIC): I think when you look at the return on equity for banks, if that is the reference point - - -

DR MUNDY: No.

MS SCOTT: No, I'm not actually saying that. I'm actually making it clear that I'm not using the banks as a reference point. I'm using the reference point to be the 10-year bond rate as almost risk free. Given that your activities involve a risk, how does your risky activity compare in terms of rates of return to the risk-free rate of return. I'm saying they don't appear to be very different.

MR NEILSON (EFIC): We would expect to earn a rate of return above the risk-free rate.

MR ARMOUR (EFIC): I think from our perspective it is the shareholder who determines what rate of return is appropriate for our activity and our function, and I know you have a view as expressed in the report. Our conundrum in responding, if you like, is that for as long as I can recall we have presented our three-year forecasts to our minister, and have shared these with central agencies, and have said, "This is the activity we are undertaking and these are the returns that we expect." At no stage has it arisen in those conversations with central agencies and with the minister that they had a different expectation in terms of risk.

MS SCOTT: I think what we're suggesting in this draft report is that expectations don't seem to be very high, given the risk sector that you're operating in.

MR ARMOUR (EFIC): I'm not sure how the word "risk" is being used in lots of different contexts here. But I think if you look at our consistent performance over a very long period, when some financial institutions have lost a great deal of money, I think you need to balance off, with respect, our shadow rating and the performance. The government says - you know, we're not in a position to dictate to the government what their philosophy should be around return. They look at what we do and they look at broader benefits to society and they strike a compromise.

DR MUNDY: So you would have no difficulty in principle with the minister, in his statement of expectations, saying, "Across the scope of your business, I expect you to earn X per cent over the bond rate," whether that be one, whatever. The notion that he might do that is not problematic?

MR ARMOUR (EFIC): I think as long as the minister has made an informed choice. Again, firstly, it's not my role to tell the minister what to think.

DR MUNDY: No.

MR ARMOUR (EFIC): So standing back and looking at it from a broader policy perspective, as long as people involved in formulating the policy understand the implications of what they're saying, that is the role of government. So for example, if we are currently pricing to the market - that is, we are not subsidising but we are pricing the market - if our costs are comparable to most financial institutions - and they are - and our losses are very low for a very long period of time, then the implication of what you're suggesting is we need to charge above market prices. The minister and the government would need to reflect on the implication for Australian exporters if we do charge above market prices, whether it is above the commercial market or whether it is above the OECD. That is the only observation I would make.

DR MUNDY: Let me ask for a simple response to my second question. You would not have a difficulty with a recommendation that said the minister, through the statement of expectations, as the shareholder's representative, should determine the rate of return that EFIC should earn across its business as a whole and, obviously, over a long period; we're not talking about year on year.

MR ARMOUR (EFIC): I think I've answered that question. It's not yes or no; it's a question of considering the policy dimensions.

DR MUNDY: Assuming the minister deals with those matters properly, which we can assume he will.

MR ARMOUR (EFIC): Then it's not my role to tell the minister what to say in their statement of expectations.

MS SCOTT: I think you indicated, Angus, that the disposition of EFIC, the modus operandi, is that you would charge market prices.

MR ARMOUR (EFIC): Correct. We would charge to market or OECD; we would find, where we can, relevant benchmarks to establish our pricing. We are a price-taker.

MS SCOTT: That's all right. And you don't subsidise?

MR ARMOUR (EFIC): Correct, not from our perspective, at a transaction level.

MS SCOTT: On page 87 of your submission. Page 87, the last box on that page reads, "EFIC has a legitimate role to play in supporting transactions and projects where risks are large, long-term, and positively correlated. Thanks to the government's superior capacity to bear and pool these risks, it is also legitimate for government to earn a lower return on equity it has invested on EFIC on behalf of tax payers that private shareholders are entitled to demand of private companies." Just trying to fit that in with your statement that you charge market prices and you do not offer subsidies.

MR ARMOUR (EFIC): I think they're two different things. The point you refer to there is a return on equity.

MS SCOTT: Right.

MR ARMOUR (EFIC): Which is a conversation around, for example, however your report has portrayed it, our return on equity versus the banks'. Then there is a question about pricing and our position on pricing, I think I have stated it quite clearly, is as a price-taker. Our return on equity may be lower than a shareholder in the CBA but not for the reason that we're subsidising price, and this is the important distinction I'm making. Your perspective, as I see it from the report, is the subsidy arises because of a discrepancy between the bank return and our return. In the first case we argue it's not a relevant comparison given their business model and our business model.

MS SCOTT: In some ways the bank point that you make in the submission very frequently is a distraction and a red herring. I want to characterise, if you are charging market prices consistently, why is it that we're going to end up and you think it is acceptable for EFIC to achieve a lower return on equity than private investors would receive.

MR ARMOUR (EFIC): And the answer I gave in my opening statement, commissioner, was our return on equity may be relatively lower because we are holding more capital. So if the argument is to return capital and therefore to achieve a higher return on equity, that is possible. But, again, from a policy perspective you need to consider the implications of a financial institution with a higher degree of leverage and a smaller capital buffer.

DR MUNDY: And every other possible use the Commonwealth may have of that capital.

MR ARMOUR (EFIC): Correct, and we acknowledge that point in our response to you. It is just unclear from your draft report what opportunity costs you have identified; this is what we struggle with in our response. There are different ways the Commonwealth might consider the alternative use of that capital. In considering that alternative use of that capital, they might also need to consider whether a lower capital base, implying that EFIC cannot provide as much support on a literal level, also has implications that a number of offs and ons, if you like, need to be worked through to determine the outcome.

MS SCOTT: Just on the buffer, you would also be seeking to earn a market-price return on that as well, wouldn't you? It's not like you're sitting - so I'm just trying to work, if you were trying to earn market return on the buffer, you're earning market return on all your transactions, how you would end up being then below market return on the total?

MR ARMOUR (EFIC): In the first instance, commissioner, we actually have very little latitude about how much money we make on the buffer, as you say, as the capital, because that's very prescribed by CAC Act, so the purpose of investing our reserves, which I think is your question, is to protect capital, not for the purposes of profit. That's very much a conservative platform that has been instituted through the CAC Act, so that's one dimension.

Secondly, the point we made repeatedly is that we do not have the options available to us to diversify and expand our income in order to generate higher returns. We have asymmetric credit selection, we have a very narrow window. So in the perspective of a finance institution they may seek to have a very homogenous, high-volume product that is very profitable. This is a concrete example, so homogenous, high-volume product that is very profitable. From our perspective, a homogenous and high-volume product is intellectually inconsistent with market gap. If there is such a large gap is it really failure? What is driving that circumstance?

I think we provide in some detail the other avenues that commercial financial institutions have in order to generate better returns, but even taking your point in terms of, "Why can't you do it?" and the answer is very clearly because it's a different business model. Secondly, if you were to look at our return against the level of capital that we require just for the risk we currently have on our book, we work it out to be roughly 22 per cent, which is comparable to what the banking sector provides. So there are choices to be made in this, and the choice that we made is to have the capital buffer that allows us to provide more support to Australian exporters and to protect the Australian taxpayer. You can increase leverage but it comes with attendant risks. Higher return, no question, but attendant risk.

DR MUNDY: This proposition about governments pooling risk and earning lower returns on equity, is this a proposition you think applies to all government business enterprises or EFIC in particular?

MR ARMOUR (EFIC): No, I don’t think there is an implication in the report that we would argue this for every enterprise - no. I'm not even prepared to say it applies to EFIC, given the discussion we just had about our return environment, but it is a legitimate economic argument.

DR MUNDY: One which was generally rejected in the mid-90s when we had competitive neutrality introduced.

MS SCOTT: We might move on. I'm just conscious of time.

DR MUNDY: Yes. There has been some discussion in the media, and I think some of it has possibly been attributed to you, but I can't quite remember, so I won't hold it - I've read an awful lot of material in the last couple of days. But there has been suggestion that there is a need - there have been increasing levels of ECA involvement, other ECAs, in the Australian - particularly in the resources sector, and that that might of itself, and left unaddressed, lead to Australian producers being disadvantaged because their offshore competitors presumably are getting finance from other ECAs. Is there any evidence that you're aware of of this sort of activity?

MR ARMOUR (EFIC): Sorry, commissioner, I'm not aware of that report and I don't quite follow the statement.

MS SCOTT: This is the idea of the strings attached, that I think you're quoted as saying that it was important for EFIC to be in this space because otherwise there would be lost opportunities to other ECAs and that the other ECAs' activities came with strings attached. Do you want me to find the article?

MR ARMOUR (EFIC): No, I understand that now, thank you. The implication, and I don't want to put too much stress on this point but it is the simple fact that when US Ex-Im Bank provides funding for a project in Australia they do so on the basis that it will create US jobs. Now, to the extent that there is a gap, to the extent that we feel the gap is one that EFIC could profitably address, there is the possibility that our involvement will result in Australian jobs at the expense of a US Ex-Im Bank facility. It's a very broad conceptual approach to it, that's why I don't want to put too much emphasis on it, I would say that Commissioner Mundy's comment about the media is probably about right there, but it is a simple fact that they have a reason to provide it and they provide it to generate US jobs. To the extent that those jobs come at the expense of Australian equipment supply, for example, that's possibly an issue the government wants to - - -

DR MUNDY: Much in the same way that in support of Austal's development in Alabama, I think it is - - -

MR ARMOUR (EFIC): US Ex-Im?

DR MUNDY: No, in your support of all the fast ferry builders, for example, or their activities in the United States, presumably that's creating jobs in Australia which might have otherwise been created in the United States?

MR ARMOUR (EFIC): Well, that's certainly creating additional jobs in Australia, which was the purpose of putting forward that proposal.

MS SCOTT: In some cases they could also be creating jobs in America as well, I mean to the extent that they're offshoring as well?

DR MUNDY: Yes.

MR ARMOUR (EFIC): No, there would be no - it's prohibited by US legislation for Austal to construct a vessel in Australia to move to the US.

MS SCOTT: No, we're familiar with that.

MR ARMOUR (EFIC): You know that?

DR MUNDY: Yes.

MS SCOTT: Yes.

MR ARMOUR (EFIC): I don't need to go there. So there is no suggestion they will be at the expense of Australian jobs, in that context.

DR MUNDY: Okay. The "strings attached" I suspect is a bit of a media furphy, because they're promoting their exporters into other markets, that's what they do, that's the nature of what they do.

MS SCOTT: Generally you don't have an objection to that.

MR ARMOUR (EFIC): No.

MS SCOTT: Because you were talking about crowding in the other ECAs.

MR ARMOUR (EFIC): Absolutely. We are a capital importer.

MS SCOTT: In fact you would like to see other ECAs involved?

MR ARMOUR (EFIC): Sorry, it's not our judgment about whether they should or they shouldn't be involved, but it's a question that - sorry, the simple fact is we are a nation that imports capital. The simple fact is there is a clear shortfall in the bank capital available to develop some of these projects, and the sponsors have accordingly gone to the export credit market to provide for that shortfall.

DR MUNDY: You're satisfied that at all times foreign ECAs are acting in accordance with the relevant OECD standards and relevant World Trade Organisation standards?

MR ARMOUR (EFIC): Not all of the ECAs would be subject to OECD standards.

DR MUNDY: Let me ask you a two-part question. Of those who are signatories to those standards are you satisfied that they are?

MR ARMOUR (EFIC): I don't know if I can comment on that, frankly. Given the breadth of their activity I can't comment. I would presume. I think it's reasonable to presume that they are. However, there is - I'll leave it at that.

DR MUNDY: When you are engaged with other ECAs in partnership - your colleague described with respect to Ichthys - do you satisfy yourselves that in those circumstances where you're a partner that they are compliant?

MR ARMOUR (EFIC): Yes, it's a function of what we do and - - -

MR FIELD (EFIC): I think we haven't - compliant in what respect?

DR MUNDY: Well, that they comply with the relevant OECD standards and any other World Trade Organisation obligations?

MR FIELD (EFIC): I think there's two parts to this. There is what you would call is a buyer credit component where they are obliged to meet certain minimum price. The price hasn't been set, so I can't comment.

DR MUNDY: Perhaps a more general proposition - - -

MR FIELD (EFIC): And the framework around which they provide the money is also, to some degree, described under the OECD arrangement. We have no reason to doubt that they will not be compliant in that regard. But as I say, price has yet to be set, so I can't offer you a comment.

DR MUNDY: No, it was a general question.

MR FIELD (EFIC): The second part is to do with the untied support, which is a fairly dominant part of the activities of the Japanese and the Koreans at the moment. So this is support that brings capital, it comes to Australia, and the string that's attached to it, to use this term that seems to have gathered some momentum, is the purchase of the off-take, it's not to do with bringing Korean jobs or Japanese jobs to Australia.

DR MUNDY: They're presumably doing that for - - -

MR FIELD (EFIC): Long-term resource security - - -

DR MUNDY: So they have a public policy purpose for doing that.

MR FIELD (EFIC): Correct.

DR MUNDY: Of those ECAs which are not signatories to the OECD agreement, are you aware of circumstances where they have not been compliant with what those OECD standards would have been if they had have been signatories to them?

MR FIELD (EFIC): I don't think we have sufficient detail to give you an informed response.

DR MUNDY: What would you do if you formed that view, and you can take it as a: those who are signatories; and those who aren't. Would it be a matter that you would bring to the attention of government or would you keep it in the club?

MR ARMOUR (EFIC): At their most general level - in DFAT, Treasury, and Finance - we have, over a decade probably, outlined for them the continued increasing activity of export credit agencies in Australia. I can say, over that period there has not been a great deal of interest in what we have had to say. It is possible now, in the context of the significant source of capital they represent, that interest will be greater. If there was anything untoward, obviously we would bring it to people's attention. But I'm not sure. If they were offering something that is below what the OECD - and they're not obliged to follow the OECD, I think there is a limit to how far that conversation can go.

DR MUNDY: I guess my question is, if you became aware of that, would that be a matter that you thought would be appropriate to draw to the attention of the minister for trade, for example? Because it has a wider trade policy and bilateral negotiation context, I would have thought.

MR ARMOUR (EFIC): We would certainly discuss it. We would certainly discuss it with departments and, in that case, maybe rely on them. But we don't tend to pepper the Minister for Trade with observations.

DR MUNDY: Okay.

MS SCOTT: One of the findings that your submission objects to relates to the provision of information to the board regarding the market gap. The way I would characterise it is that you object to the commission's draft assessment that we query the quality of the information provided, drawing on the board papers we have seen. I just wanted to then ask, given that you reject this, I can find an instance where a major project had a market gap analysis in the board papers that goes for four lines and three words. Would you think that constitutes good practice?

MR ARMOUR (EFIC): It would really depend on the circumstance, commissioner. There are some where the gap is so evident that it requires less elaboration in the paper, although that is not to say that the conversation that the board has won't go into it in any greater detail. We do tend to keep our board papers concise and we allude to the principles and concerns. The board, as a board should, would interrogate me if they are at all unclear or uncertain as to why we are undertaking a transaction. I can assure you that they do interrogate management on this front. I think it is important, commissioner, to emphasise that the board takes its responsibilities as directors very seriously, and they understand their obligations and they do pursue them in their roles.

MS SCOTT: In relation to concerns about bribery, in light of the Solomon Islands experience and, more recent investigations, have you reviewed your current arrangements and do your current arrangements satisfy you that they are sufficiently robust?

MR ARMOUR (EFIC): I'm not aware of any issue with the Solomon Islands, commissioners.

MS SCOTT: Well, then taking into account the recent investigations, have you recently reviewed your processes to satisfy you about bribery, and do you consider that your current arrangements are sufficient?

MR ARMOUR (EFIC): So the general question is about our anti-corruption and money-laundering approach; I might ask our General Counsel to assist in giving you a fulsome answer. But this policy is reviewed frequently, it has been reviewed recently, and it meets the standards that you would expect of any commercial institution. Policy of this nature is there to mitigate a risk. A risk can never be avoided in this area, in the same way that any government program might be subject to people doing the wrong thing, but I will come back to make that general point in a second and ask John to introduce himself and then talk a bit about the development of our program.

MR HOPKINS (EFIC): Commissioners, my name is John Hopkins. I am EFIC's General Counsel. We have a number of policies and procedures internally to deal with bribery and anti-corruption. I can name several of them for you; but, effectively, we have an anti-corruption policy and various procedures that fall off that, and also we have an anti-bribery policy and procedures that fall off that too. Obviously these are living documents and, while they are compliant with our international and domestic obligations, we look to ensure they are kept are up to date on a regular basis. This involves internal investigation and also we involve external parties in updating those as well. In reference to outside investigations that are happening at present, it does bring those matters more to our attention and we focus on individual issues and how they may or may not improve our internal policies and procedures, and that happens on an ongoing basis.

DR MUNDY: Sorry, before I interrupt, the matter that Commissioner Scott refers to is in fact recorded in the Hansard, the Senate Hansard of 30 November 2009. It relates to the Gold Ridge mine in the Solomon Islands.

MR ARMOUR (EFIC): I'm sorry, I'm aware of the project, but if you could elaborate that would be helpful.

DR MUNDY: There were concerns about the probative landholder agreements, according to Minister Crean's answer, and he said that EFIC had evidence that raised concerns of the probative landholder agreements.

MR ARMOUR (EFIC): Well, as part of our due diligence - and Mr Parsons has alluded to this earlier - we would certainly look at not just the structure of landowner agreements but the process that they use to arrive at those agreements. However, in relation to the Solomon Islands, the first thing I have to say is we didn't actually proceed with that transaction, so there comes a point where our knowledge of it ceases. We were involved - well, if I take a really big step back, we were approached in the 1990s to support the project and we declined it because we felt it was too risky. It was insured by the private market and they payed out a massive amount of money. After the troubles, there was a national interest priority to help the Solomon Islands to re-establish its economy and we were asked to reflect on whether the redevelopment of this mine might support that objective. On our account, we provided an investment insurance policy for the feasibility study, and that expired and there were no issues with that. When it came to the project proper - I can't remember the dates exactly. It may - - -

DR MUNDY: It would have been around that time of the Hansard comment, but possibly subsequent to that.

MR ARMOUR (EFIC): We did not in fact proceed. The comment at that point was probably accurate, but I just have no recollection of what particular issue was concerned.

DR MUNDY: Were there any subsequent discussions with law enforcement agencies about this matter?

MR ARMOUR (EFIC): I cannot comment on that. I can perhaps elaborate in private, but I cannot comment.

MS SCOTT: Having taken on board the fact that it is a living document, your current arrangements to satisfy yourself, at this point in time, having the matter under frequent review, would you say that they are sufficient and satisfactory?

MR HOPKINS (EFIC): Yes, more than sufficient and satisfactory.

MS SCOTT: Okay. In relation to Tenix's transaction in the Philippines, could you indicate what you are expecting to be the gross and net position for EFIC from that transaction?

MR ARMOUR (EFIC): The gross position, I think, was published, but none of us remember it off the top of our heads. There have been a series of inaccurate reports in the media that we have not been repaid under that; that's wrong. I mean, you have our accounts, you understand that yourselves, that this exposure has been paid down and the most recent payment was last week. It will expire in two years time and we expect to be repaid in full - or, sorry, ANZ, under our guarantee, is expected to be repaid in full.

MR FIELD (EFIC): I think it's also worth adding that the claim that the guarantee had been called by ANZ is incorrect.

MS SCOTT: Okay.

DR MUNDY: One of the challenges that, indeed, everyone who operates in a public policy space is faced with, as soon as they use the words "small business", is what is one of these things. We have made a suggestion that it might be a turnover of $25 million and you are suggesting that is not adequate. Can we perhaps just understand a bit better as to how you have formed a view that the $150-million limit of small business is appropriate, accepting that, as you rightly drew our attention to, the EMDG is 50, and ASIC seems to have about three of them and the ABS seems to have a few more. It may well be the case that the definition suits the purpose for which the definition is being drawn, but I'm just interested in your thinking on this. Because I have to say that we aren't hard and fast wedded to that; we were just trying to tease out ideas.

MR ARMOUR (EFIC): Commissioner, I think the point you make at the end of your statement is very relevant to how EFIC formulated its view on this, and that is simply that we created a structure that would allow us to provide a level of service to smaller clients through the banking system. So the banks have a certain approach to small and medium-sized companies - small companies up to medium-sized corporates. In their business banking segment they have a particular approach. Our objective, as I think we have discussed previously, both from the perspective of the least-cost delivery channel and using the bank to test whether there was a failure or not, was to align our process with the bank. We develop experience with the institution, we develop insight into how their credit policies work, we develop a channel in order to reach those people at the least-cost way. Again, apropos the conversation we had earlier around limits, for us it's not really a limit; it's a characterisation for the purposes of delivering a service, rather than a limit. Again, from our perspective, as long as there is evidence of failure then there is a reason for us to consider it, whether it's a big company or a small company.

DR MUNDY: There was an article in the Australian on 15 March which the article asserts that EFIC is involved in six onshore resources projects. Now, I understand that there may be a question of misreporting here, so I would just like to give you the opportunity, Mr Armour, to set the record straight.

MR ARMOUR (EFIC): Again, this is a question of misreporting versus what the facts are and, I think, as Peter has alluded to previously, people may be talking to us in about half a dozen - and that is a very round figure - of projects, but at this point the only project that is under contemplation is the one we discussed earlier today, and that is Ichthys.

DR MUNDY: When this being talked to by about half a dozen, are we talking about things of the order of magnitude of Ichthys or Brookfield, or are we talking about, perhaps, small SME assistance, or does that space contain both sort of types?

MR ARMOUR (EFIC): The reporter's question I think was directed more to the former; that is, big project stuff.

DR MUNDY: The big things, yes.

MR ARMOUR (EFIC): But I haven't done a number in my head on what the two might add up to.

DR MUNDY: The nature of the support that would be being provided would be insurance, would there be loans involved in these projects?

MR ARMOUR (EFIC): There might be. Again, these are very preliminary discussions. It could be some form of credit, is what - - -

DR MUNDY: Some sort of credit, okay. The suggestion again in the media was that entering into one or more of these transactions may require EFIC to issue more debt to provide capital to enter into these transactions. That looks like another piece of misreporting, by your physical response.

MR ARMOUR (EFIC): It was a Wall Street Journal article, I think, in that respect, commissioner, and I had a very aggravated conversation with my Treasury at about 7 am, saying, "What am I talking about," kind of thing. So we have had a few issues with what has been represented in the media versus what our thinking might be.

DR MUNDY: So the suggestion that there will be bond issues emerging any moment now to support these projects is simply not correct.

MR ARMOUR (EFIC): No, that's correct.

DR MUNDY: We had some quite interesting evidence given to us in Perth by

Wellard Rural Exports, and part of the evidence they gave us was that not only were they having issues with operating in a space which is of concern to yourselves, but more generally the revelation was that they have actually moved their whole banking business offshore to Singapore. One of the things that is coming through to us in the submissions that we are receiving is a general difficulty that businesses are having with the banking sector generally. It is the nature of the commission and its statute requires us to consider economy-wide issues. Whilst, I guess, one of the questions that is going through our mind is, are there serious structural issues in the Australian banking sector which EFIC, to varying extents, is seeking to address on an as-it-finds-it or as-the-problem-finds-EFIC basis. Do you have any thoughts on more systematic, system-wide things that are problematic? We are told the banks in Singapore are more amenable to certain sorts of banking transactions. Particularly Wellard, which you would thought would meet the typical characteristics: there is an awful lot of land to take security over, all those sorts of things. So we're interested in whether there are systematic issues here that also need consideration.

MR ARMOUR (EFIC): I think probably our clients are better placed to provide comment on that than us, commissioner. We don't review in the same way you would or government treasury the structure of the banking system. I am aware of some of the difficulties of Wellard or firms in agribusiness have experienced form time to time, and that may vary. So, for example, it could be simply because they're exporting to an emerging or frontier market and the Australian banking system is reluctant or has no experience or insight into that market. I mean hopefully, frankly they've worked with us in order to look at a solution, but no, I'm sorry, I wasn't present for their testimony.

DR MUNDY: No, it was just a more general - it seemed to be - and indeed, just the sense you get that there is friction in the domestic banking system.

MS SCOTT: Clearly it's the case - I'm sorry, I haven't found the piece of paper I wanted to. I'll be frustrated - as soon as we finish I'm sure it will appear. But anyway, moving on, clearly you don't find it very amenable that our draft report suggests that EFIC be given a mandate to focus on SMEs. Just putting aside my question whether the turnover threshold or ceiling should be 25 million or another number, just still concentrating on SMEs, you say in your submission to us that you consider that will inevitably lead to a loss-making exercise. I just contrast that with your earlier submission where you drew attention to your particular expertise in dealing with the SME sector and your capacity over the longer term to discern projects or firms and their export activities that meet your acceptable risk profile. So what I'm saying is that your submission in relation to our issues paper suggested that you were SME experts and in relation to this one, now that we've taken that at face value, you say, well, the difficulty is that it will be a loss-making exercise because you won't be able to make the right judgments. I'm trying to work out why that would be the case.

MR ARMOUR (EFIC): It's not so much about judgments initially, thank you for asking the question. The issue we have with the recommendation is the characteristics of the SMEs that you describe, so newly-exporting, probably with limited credit history and a very low turnover. In our experience, that is a particularly risky part of the market. I think it would be fair to say that we have conversations today with firms who might qualify under the situation you're describing, and our immediate reaction in most cases, coming back to Commissioner Mundy's point is you have an equity problem, not a debt problem. You need to develop a certain amount of experience before you are actually capable of taking up debt in order to pursue growth.

That is a generalisation, and I've criticised generalisations in the past, but I think it's a relevant generalisation. The issue is at what point in the life cycle of that SME in their growth is it suitable for them to contemplate debt. Our concern with the proposal around newly-exporting SMEs with limited credit history, is experience would tell us that's a very, very risky part of the market. That's our concern. It's not SMEs per se, it's the credit quality. Actually, you have our credit manual - if you refer to it you say, how many years of export experience do they have? That's a fundamental test in terms of taking up debt.

MS SCOTT: So keeping on that SME space, besides the low turnover, which you've already had discussion with my colleague on, you're suggesting that we go to the existing credit manual and find characteristics of SMEs that you currently use to determine - acceptable proposition, and that could be the basis of our suggestion of an SME orientation for your firm?

MR ARMOUR (EFIC): Well, it is the existing orientation, so there's no need to make recommendation in terms of the sort of firms that we're dealing with. They have to have some credit history, some export experience. There has to be a fairly objective assessment of their capability of performing the contracts that we're being asked to support. That's a fundamental concern for us in order to avoid being a subsidy frankly, – whatever premium you might get from a relatively small pool of small firms will not rescue you from even a small number of underwriting failures with large losses. That is simply not going to happen. So it's important that you get your judgments right 99 per cent, 99.5 per cent of the time.

MS SCOTT: So it doesn't necessarily need to be loss-making. So if we configured it the right way you could easily envisage a situation where an SME-only focused EFIC could be profitable?

MR ARMOUR (EFIC): Under our definition of SME, yes.

MS SCOTT: Okay, thank you.

MR ARMOUR (EFIC): But the argument we would mount around the focus is if there is a market failure we're not sure why you discriminate against a firm on the basis of size. The examples we would use would be if you have a large firm working in succession in sort of Bangladesh, Pakistan, Indonesia, Kenya - I'm casting it widely obviously, but just for illustration - they will face challenges, perhaps, in constructing the finance they need in order to execute those projects. The failure doesn't arise around the firm. The failure arises around the development of the financial system in that country, for example, or the contractual issues that result from an emerging and frontier market. Those are the sort of things that we wrestle with, with large firms, usually good projects, bad neighbourhoods. That's typically what it boils down to, typically.

MS SCOTT: All right. Well, thank you very much, because we've got four more presentations this afternoon and we'd like to move to those, I think we'll finish your session now, thank you. But as we foreshadowed we may well need to come back and have another hearing to systematically go through your submission. So thank you for attending today.

MR ARMOUR (EFIC): Thank you, commissioner.

MS SCOTT: For your team's attendance as well. We might just take a three-minute break, stretch our legs, and then we will be resuming with the Australian Institute of Export.

MS SCOTT: Ladies and gentlemen, good afternoon, and we welcome to the table the Australian Institute of Export. We would ask that you identify yourself for the record, Ian and Peter, and state your full name and then state if you'd like to make an opening statement.

MR MACE (AIE): Peter Mace, the Australian Institute of Export.

MR MURRAY (AIE): Ian Murray, the Australian Institute of Export.

MS SCOTT: Please proceed with your statement.

MR MURRAY (AIE): Thank you. I'd just like to say a couple of words about what the Australian Institute of Export does. We're a not-for-profit business. We primarily support the small to medium size exporter. Our major role is education and training, but we do on top of that a whole host of things which is, I guess, associated with developing the export of international trade skills of Australian business. Just as a - before I hand over to Peter, my background is I'm a marketing person and I'm the chief executive of the institute. Peter's background is in international trade finance, and he is the general manager. I'll pass over to you, Peter, and take us through your comments on the draft report.

MR MACE (AIE): Yes, the draft report you would have a copy of, and we'd just like to add to that based on the findings of the commission, if we could, I guess first to reinforce the fact that we find, talking to a lot of exporters, that it is a very difficult situation out there for our exporters, with a high Australian dollar, a slow recovery in key established markets of North America and Europe. That slow demand is also leading to reduced demand in Asia for our inputs go into exports for those particular markets, so that's one sector.

The other issue, I think, is the tightening of credit for international transactions by banks. Two of the submissions lodged by Deutsche Bank and Credit Agricole sort of speak to that, the fact there is difficulty in finding the funds for certainly large transactions internationally. It also talks about the impact that Basel III might possibly have on the Australian banking sector, increasing costs and reduction, perhaps, in the money available for trade financing. Coupled with that again there's also the actions by our key competitors in the US and Europe. Having diminished return at home they've really stepped up their efforts by producing, I guess, an export-focused push from top government level where they're really looking at a whole of government approach to try and get their exporters internationally focused and focusing on new markets, particularly Asia, which I guess is the bailiwick of the Australian exporter during the GFC that has kept them abreast. So those three concerns are really setting the scene for how difficult it is in terms of the export market.

The other thing we would like to mention closer to home is the fact that Austrade have recently undertaken review of its operation and based on that they've stepped back from support for exporters into North America and Europe, apart from a couple of key sectors like education and clean energy, and their focus is now on helping Australian companies into the markets of Asia, Africa and South America. Now, to us it would seem logical that if this is the government's approach to take on those new and emerging markets, and sometimes risky markets, for our Australian exporters, the trade financing arm of government should be behind that effort and having the ability, capability, the products and services to support them. Unfortunately, we don't find any evidence that the Australian banks have changed their lending criteria to take on that new challenge.

The other part of that strategy is the fact that Austrade is stepping away from helping the start-up exporters, which is what we call the bottom end of the SME market, and they really want to help people who know what they're doing internationally, the export-ready exporters. We would tend to find those more at the middle and high end of that SME segment. They're the people that Austrade wants to help and they're the people they feel would have the best chance of long-term success of export sustainability. The whole issue of export finance has been an ongoing one going back to the Mortimer review in 2008, the Trade 2020 outcomes report in 2009, and also a Global Readiness Index that EFIC undertook in 2010 which found that access to finance was the key determinant or key negative determinant for Australian business.

So I guess in terms of all those situations we really think that now is not the time to be pulling back on any of EFIC's services. We certainly disagree with the limit of 25 million. We think that the current mix up to 150 million or thereabouts would be about right. That will encompass a range of companies of different sizes but companies who are export ready and who can be sustainable. We also note the depth of sentiment for those people putting submissions in, the 69 that have been lodged so far since the draft report indicates that they strongly support EFIC, strongly support the support they get from EFIC and also of the view that they wouldn't get that support from their local banks. I guess that's combined with the fact that as one local bank put a submission in initially, which the ANZ, talking about how much they valued having EFIC support for their transactions. Since the draft report there has been no submissions by banks, whether they haven't got time to do it or whether that's indicating that lack of interest - - -

DR MUNDY: There were actually two arrived on Friday night.

MR MACE (AIE): Is there? Okay, well, we haven't seen those as yet.

DR MUNDY: No, neither have we.

MR MACE (AIE): In our view, looking at the - talking to the banks we got involved in trying to put together the Navigator site and doing some seminars for EFIC, which didn't get off the ground at the time but talking to the banks at that stage there wasn't a focus on changing the credit criteria for SMEs going into export. They were really looking the same way as they did on a domestic transaction, which is bricks and mortar: if you've got a building to pledge your support, well, we'll try and help you, but if it's a big international transaction we'd rather not be involved, and if we do get involved we'd like the support of EFIC.

So I guess in a nutshell that's our view. We really think that EFIC has a wonderful role to play. We'd like to see it continue, and if anything, I guess we'd like to see that mandate expanded a bit because there are companies going overseas now looking at markets overseas. A lot of them find it difficult to get financial support from their bank and we think if EFIC were in that market, there was a expansion of their powers, that would certainly assist our exporters to grown internationally.

MS SCOTT: Thanks, Peter. What proportion of your membership, which I think is about a thousand, would be customers of EFIC?

MR MACE (AIE): Probably 5 to 10 per cent, I would say.

MS SCOTT: Okay. That's probably a higher percentage than - must be a much higher percentage than the proportion of Australian exporters, which we estimate on the basis of ABS figures, somewhere around 45,000 firms. One of the points we make in - - -

MR MURRAY (AIE): Sorry, that's firms that export?

MS SCOTT: Yes. So one of the points we make in the report, one of the findings we make, is that most exporters can get by successfully without EFIC. That's why we saw it potentially playing a particular role in the market. I guess I'm hearing two things in your presentation, Peter, I just want to see if I've got it right. On the one hand, you're saying it's larger firms that can have a problem obtaining finance and, on the other hand, you're also saying that the very small end of town and nearly emerging market, banks insist on bricks and mortar and it hampers their development. So do you want both groups to be catered for or exclusively the large end, because that's where the big bucks are, or do you think it should be - - -

MR MACE (AIE): One or the other. Yes.

MS SCOTT: Yes.

MR MACE (AIE): I think the need is on both. Large corporations have the support of their corporate advisory team in the bank, who are quite happy to lend for general expansion and general terms of trade, which are generally up to 180 days, sale of goods. Where those companies do need support is large financing deals that EFIC gets involved in, which is infrastructure deals, long-term deals over more than, say, a year to two years, involving many, many millions of dollars. So in those large-structured long-term deals, often into difficult countries is where the banks themselves find them a high risk. For the smaller guys, it's more the straight-forward transactions out to 180 days, where they do rely on an overseas buyer to pay them. They can't always get payment up-front. For those facilities to finance that, that's where they come unstuck with the local banks. There is a distinct difference, I think.

MS SCOTT: What about the increasing focus that EFIC is placing on the resource sector, including domestic activity that is integral to resource activity? We were hearing today about Greyhound, the bus company, being in discussions with EFIC because of bus services to mining sites and we had a discussion about what resource projects should receive EFIC's support and so on. Are you supportive of EFIC moving increasingly in the direction of undertaking support for resource projects in Australia that may not be the exporter per se? There might be a firm supporting an exporter. What's your view on that?

MR MACE (AIE): That would be a policy decision for EFIC. I guess that's not an area that we would have a particular interest in.

MS SCOTT: You don't have a problem with that?

MR MACE (AIE): Yes. Most of the people we do look after are in that small to medium sector, so third-hand we hear about some of the concerns that larger guys have, but I don't think we're in a position to say whether that's the appropriate approach or not.

MS SCOTT: Did you hear the testimony from Angus Armour just before we had a little break? That was that he considered very newly exporting firms were not the ones that EFIC should support, because what they really needed to do is get sufficient equity to become an established exporter and it was more at the medium - I think it's all right to characterise it as that - more experienced exporter that EFIC was most interested in, in that segment of the market. Are you comfortable with that characterisation?

MR MACE (AIE): Yes, in the main. I think EFIC needs to be in there with the Australian banks, as they have been in the past, and that's a sector the Australian banks have great difficulty in, I guess, extending credit to. So to allow EFIC to come in and top up would be difficult. There might be a few in that sector, but it's not enough in a book to find enough transactions that are sustainable, that are from quality companies of that size to make it worthwhile. Having said that though, there are opportunities there where EFIC has stepped in and confirmed letters of credit which come out of various countries, so that's more taking on an overseas bank risk, where the Australian banks have reached their limit, and that could be for small companies in that sector, certainly, but that's a different credit scenario than actively supporting the small guys here.

MR MURRAY (AIE): We certainly do support Angus's view on that. At the beginning, when a lot of exporters first start, with a lot of them it's not sustained. They can float with export for one or two or three years and then they will move out of it for one reason or another. So the risk is much higher. But there's certainly a move now in Austrade to support the exporters that are more likely to be successful, and they're the people who have had a period of time on the ground and got some experience.

MS SCOTT: Have you ever seen any research that compares the long-term performance of the 45,000 or so firms that export without EFIC support versus the relatively small number of claims that EFIC supports in terms of long-term sustained export performance?

MR MACE (AIE): I don't think that research has been done unfortunately, so - - -

MR MURRAY (AIE): Only anecdotally.

MS SCOTT: What is your position on the anecdotal side? That a firm that has never approached EFIC is more likely to be successful than a firm that does approach EFIC or vice versa?

MR MACE (AIE): I think if a firm can be successful on their own, that's what they'll do and if they've got the wherewithal in terms of financial backing, that's what happens out there in the world. But unfortunately not all Australian companies do have that financial backing to do the whole nine yard by themselves. Some end up being sold out to foreign investors and a number of others are assisted by EFIC. I guess, given the fact that EFIC has got to play in a very narrow range, they've got to be a lender of last resort, to come in where the banks can't cover it, that does restrict their ability in that market. So, given that, that possibly accounts for the small number they have been able to support.

MS SCOTT: Or the fact that it's not necessary to support a very large number, if you understand what I'm saying. If 45,000 get by without them, then they get by without them.

MR MACE (AIE): I guess what we don't know is how many of that successful group, the 45,000, haven't been as successful as they could have been had they had extra financial support to move on faster.

MS SCOTT: While you're generally supportive of EFIC's current role and you actually favour an expanded role. In your submission on page 4, you indicate that EFIC's product range is skewed towards large exporters. Are you in favour of any re-waiting and how would you want that re-waiting to be achieved and what product lines are you suggesting should be available?

MR MACE (AIE): Good question. I think this also goes back to EFIC's mandate, that they can only come in as a secondary lender now to the banks. They can't be a first-class or first-stop lender to those banks. So that restricts the products they can get involved in. They've tried to expand into some of the new sectors, like providing support for foreign exchange services, providing support to the film industry, again without that mandate. So I think they're two examples where they could do a lot more, where there does seem to be a bit of a gap where the companies can't get the support. So I think that's an area where EFIC could look at opportunities. It's going to be industry-specific, it won't be across the board, because certain industries have a particular need more so than others.

DR MUNDY: The sense I got was that you were almost a little bit concerned about Austrade's decision to go down the path, or have I got the wrong end of the stick there?

MR MACE (AIE): I think that decision is probably partly brought about by a reduced budget, so they haven't got the money to do all the things that they would like to do. So, based on the available funds, they've decided that helping more established exporters get into the emerging markets is where they should be putting their focus. I guess our concern is those emerging markets can be risky. I don't see any evidence that the Australian banks are more willing than they were last year to support companies into those markets, so I really think there's a role there for EFIC, if that's the government strategy, to sit behind that with some products that would help that reach fruition, but in a safe way, that companies don't enter transactions that would end up in losses.

DR MUNDY: Is it your general view that the source of the problem in this policy discussion is the conduct, justified or otherwise, of the banking system? That's where the source of the problems is arising from.

MR MACE (AIE): I think to some extent it is. I think in this country - and it's noted in our report - we have a preponderance of large public companies, who are listed and who can get access to finance. We've got a lot of SMEs. There's not too many companies in the middle. The result of that is that the banks don't have a big portfolio of properly-equipped lending officers to look at difficult transactions. That's why it goes back to bricks and mortar. A bit like the housing loans, it's easier to tick the box. "If you've got some property or something to put behind it, we'll give you some money. Don't tell us it's export. That's a risk we don't want to know about perhaps." But I think that dearth of good-sized and mid-sized companies is one of the areas where banks don't have the capability to support - and I also think that is where the credit team have done a fantastic job. They do understand, I think, the risks of some of those developing countries particularly well and they do have a focus on certain industries, because they have built some expertise, as in ship building, and I don't think the banks, apart from the corporate sector, have that capability to look at that from a SME sector.

DR MUNDY: So what do you think an appropriate approach to encouraging the banks to develop this expertise would be?

MR MACE (AIE):   I would like to think it might be a bit of government pressure. But through Navigator and other avenues, EFIC and Austrade have tried to encourage the banks in. There has been a little bit of movement but not a lot. There is more information out there, but it requires a change, I guess, from probably the top of the banking sector. Our banks are very strong, as you point out in the report, they're very liquid, but they do very nicely, thank you, on the domestic lending they're doing now. To encourage them to move into maybe a more risky area is not something they particularly see a need to move into. Albeit, apart from the big corporate financing, where they like to get involved in that. But, again, as Deutsche Bank and Credit Agricole point out they want an ECA in there as well, for security.

DR MUNDY: Yes.

MR MURRAY (AIE):   It's not as if they don't know. It was raised in the Mortimer review, it was raised in the Trade 2020 review, it has been raised probably more often than any other issue. With the exception of a couple of small things, probably more than any other issue that has been on the top of the agenda for exporters for a long period of time. Trade finance has always been an issue.

DR MUNDY: Do you think there is - though EFIC places great store in the fact that what a lot of its products are about is working with banks, and I think that is something we probably would agree is the appropriate approach.

MR MURRAY (AIE):   And it seems to work.

DR MUNDY: Well, it seems to work to the extent that the SMEs are getting their finance. It doesn't seem to work that the banks are changing their conduct.

MR MURRAY (AIE): That's true.

DR MUNDY: From what you have told us.

MR MURRAY (AIE): Yes, that's true.

DR MUNDY: I guess what we're trying to find is a way of getting the public sector out of this activity, or finding a better way forward to deal with the problem that is having to be address by this intervention. Our preference is to deal with the problem rather than continue the treatment. I guess what you're saying is that your view would be that whilst this partnering activity is getting the business done, it is not getting the change in conduct in the banking sector.

MR MACE (AIE): But there has got to be a willingness to change conduct and I think a lot of the - well, a lot of companies we talk to and the submissions as well have said that they go to their banks first, they give them first option, and the banks just aren't willing to provide that finance.

DR MUNDY: And you have no sense that it's a regulatory impediment or anything like that?

MR MACE (AIE): No.

DR MUNDY: It's just an attitude.

MR MURRAY (AIE): It's an attitude. I mean, if EFIC walked away, the banks aren't just going to walk in and take it over; that's not going to happen.

MS SCOTT: Could you comment on what your membership tells you about EFIC's pricing practices?

MR MACE (AIE): They haven't told us a lot, to be honest. We do know that they do charge a good rate for their services. Some find it a bit more steep than what the bank would charge, but to get the deal done they are willing to pay that premium. Because it hasn't been a part of a survey we've done on how does EFIC compare to the banks, but anecdotally we would say that it probably is more expensive than doing it through your bank, but that is what they will pay to get the deal done.

MR MURRAY (AIE): And the responses, I think, to EFIC have always been positive; there is not much negative view at all towards EFIC from our membership base. I say our membership base, it's about 800 actually, but we also interface with about another 12 to 13,000 exporters.

MS SCOTT: What is that interface?

MR MURRAY (AIE): A whole range of things: we do training for them, we do a whole raft of things. A lot of people come to us, the Institute of Export, because, I guess, we have positioned ourselves as being the body that looks at the risk management issues for exporters. They don't go to Austrade, they don't go to EFIC, they tend to come to us. When it's issues around the process, the export process, or it's issues relating to minimising or at least understanding risk.

MS SCOTT: So you would have 13,000 approaches of businesses a year?

MR MURRAY (AIE): No, we communicate with - - -

MS SCOTT: I see. This is like newsletters?

MR MURRAY (AIE): Yes, and we get a lot of these people asking us questions as to how best they could finance their export business, how best they could cover the risk, things like insurance, all the different issues relating the export process.

MS SCOTT: How do you fund your activities?

MR MURRAY (AIE): Through membership fees. We run the export awards in New South Wales and that brings in sponsorship. Through a couple of projects that we run with Austrade; we're providers of Tradestart. So it's a whole variation of things. Probably no one part of it would be more than 20 per cent; it splits in about five lots of 20 per cent. We are also very close to the Export Market Development Grant scheme. There are 100 consultants that are part of us and we work with them in managing their code of practice with Austrade, and there is a fee for that, obviously, with them.

MS SCOTT: Gentlemen, I think we've finished our questions. Thank you very much for coming along today and thank you for your earlier submission.

MR MURRAY (AIE): Thank you.

MR MACE (AIE): Thank you.

MS SCOTT: Now we have the NSW Department of Trade and Investment, Regional Infrastructure and Services, please. Welcome to our hearings. Thank you very much for coming along today. Would you like to state your names and your positions within the department, and give the full name of your department, please, for the purposes of our transcript.

MS ORIEL (NSW DTIRIS): My name is Gabrielle Oriel. I work with Trade and Investment, Regional Infrastructure and Services.

MS SCOTT: Gabrielle, you are going to have to speak a lot louder than that, I think. This microphones aren't for amplification, they're just for recording. So you might need to - - -

MS ORIEL (NSW DTIRIS): I may struggle a little with that, but I'll try.

MS SCOTT: Just pretend you're shouting at someone.

DR MUNDY: If this person is standing up the back, flapping her ears, that means she can't hear you.

MS ORIEL (NSW DTIRIS): Okay.

MS SCOTT: Thanks, Gabrielle.

MR SMITH (NSW DTIRIS): I'm Vince Smith, I'm the director of Australian operations in the investment and export services area of the department. I manage a portfolio of 12 to 13 export advisers around the state, some of whom are partly engaged with Austrade on the Tradestart program.

MS SCOTT: Thank you very much. Would you like to make an opening statement.

MS ORIEL (NSW DTIRIS): Yes, if it's okay, I would like to read this for you. I am an export adviser with Trade and Investment New South Wales. I work in a dedicated division called Investment and Export Services. I have worked for about five to six years in that role and I work within the team, as Vince just pointed out, of about 12 to 13 export advisers. We service all of New South Wales for export advice. The area that I particularly service is from the Queensland border, so Tweed Heads, down through the Northern Rivers, down through the mid-north coast, down to the top of the Hunter area, so it is quite a large area. I also deliver the Tradestart contract for Austrade for that same area.

New South Wales government has got six of the nine contracts. The six contracts for those Austrade services - for Tradestart services, sorry - are in regional New South Wales, so we have got full coverage of regional New South Wales. As such, I'm coal-facing, so I work with companies. So that the range of industry sectors and clients in my patch extend through agribusiness, manufacturing, creative industries and services. Turnovers range from around the 800 million-ish right down to the lower end.

MR SMITH (NSW DTIRIS): This is - excuse me a moment. Gabrielle has taken the lead on this because of her day to day contact with clients and working through finance and other support means that they have.

MS SCOTT: Thank, Vince.

MS ORIEL (NSW DTIRIS): Trade and Investment New South Wales. One of our roles is basically to assist regional and metropolitan New South Wales businesses, particularly with international market entry and growth. That is where we come across this finance section and this sitting down the clients and actually working through their finance needs to support their market entry.

New South Wales government has got a 2021 plan. That plan has got an economic development component and Trade and Investment New South Wales has got a lead in three areas. (1) is to improve the performance of the economy, (2) is to drive economic growth in regional New South Wales, and third one is to increase competitiveness of doing business with New South Wales. In New South Wales goods and services export are roughly 52 billion a year. If you look at that in comparison to Australia's total exports it's roughly 16 per cent of goods and about 39 per cent services exports. That's the demographic of New South Wales.

Relationship between EFIC and Trade and Investment. We have an existing alliance agreement with EFIC, and that has just been reviewed just recently and it has been extended further. It was signed by Trade and Investment director general, Mark Paterson, and Angus Armour, CEO of EFIC, on 8 November 2011. Some of the issues that sit within that alliance and that agreement are shared promotions using web sites, the Export Navigator, and newsletters; participation in major seminar series and workshops; we do joint selling through our statewide network of export advisers with the banks, we, particularly in the regions, have relationships with the banks in the regions, as does the metro people; and we also provide access to other New South Wales government agencies.

How we prepared the submission. Basically we drew on our knowledge and experience from working with several thousand exporters face to face across the year through our team, and in addition we also conducted a series of informed discussions and interviewers with active exporters, so it's anecdotal evidence. So when we asked what do New South Wales exporters know about EFIC, our consultations basically proved to us that there's an increase in awareness of EFIC's services and products. In recent years they've put in considerable effort into trying to increase a range of services and reaching to the SME sector, which has included the Export Navigator tool, which is an excellent tool, might I add, and that was a response from the Mortimer Report; greater engagement with allies such as ourselves - - -

MS SCOTT: Sorry, Gabrielle, you don't mind if I interrupt as we go?

MS ORIEL (NSW DTIRIS): Yes, please do.

MS SCOTT: So what was the level of name recognition or role recognition, did you say? What was it before and what is it now?

MS ORIEL (NSW DTIRIS): It has increased.

MS SCOTT: Yes. No, you said it's increased but what was it before and what is it now? How do you know it has increased?

MS ORIEL (NSW DTIRIS): It has increased simply because of the work that we have done and the work that EFIC have done getting out there and reaching out to those people, so through web sites and seminars and - - -

DR MUNDY: I think where my colleague is trying to go is has it gone from 5 per cent to 10 per cent or has it gone from 10 per cent to 70 per cent?

MS ORIEL (NSW DTIRIS): I could not give you an actual number on that.

MS SCOTT: It's a judgment you guys have made, is that right, that because of, you know, your renewed effort, got this alliance, you've got a relationship with the banks, you're out there and you're talking about EFIC quite frequently and you think - - -

MS ORIEL (NSW DTIRIS): Yes, we are.

MS SCOTT: Previously people would sort of say, "EFIC, who are they?" Now, they're saying, "EFIC? Know what they do." Is that how you - - -

MR SMITH (NSW DTIRIS): Can I give you a recent example? There was a export finance seminar held in Dubbo which you wouldn't normally expect a huge crowd at. That was publicised as a joint venture with ourselves, ANZ Bank and EFIC, and 51 people turned up. Some other locations we're lucky to get a quarter of that, and I think that's a good example. There has been a rolling program of EFIC with a variety of the major banks having those sort of sessions and the client base that we are able to draw on, because we're the main holders of the invitation list in the regional areas.

MS SCOTT: Okay, got you, thank you.

MS ORIEL (NSW DTIRIS): So I would say it's fairly high, to be honest, simply because it's one of the tools that I use with all of my clients.

MS SCOTT: Yes.

MS ORIEL (NSW DTIRIS): Basically say, Export Navigator, go through it, come back to me, tell me what you think. So to come to the draft report now. So basically what issues are they facing? There are many issues that exporters are facing, of course, but to raise five points that I would like to identify now that relate primarily to the recommendations and EFIC's operations on the commercial account of things. Number one is access to finance. We agree Australia has a mature capital market and sophisticated credit insurance capabilities. However, New South Wales exporters feel they are facing considerable tightening of the credit-lending conditions. Smaller transactions by SMEs risk not being viewed as favourable in that marketplace.

Under its current operations EFIC has assisted quite a few exporters to gain access to products that are of real benefit to the exporters. I'll give you an example of one. There's a lighting company, a lighting specialist company, based in New South Wales, exports about 60 per cent of its output. It had a contract, a multimillion dollar US contract, to supply lighting in the Middle East. The contract was with an Asian construction company that they had worked with previously, they were smaller deals, but when it came to this large contract there was a 40 per cent advance bond. The company was unable to raise funds through Australian banks due to capital constrictions and their comment was if EFIC had not stepped successfully into that contract then they wouldn't have been able to complete that profitable and lucrative contract.

My second point is about non-traditional export models.

MS SCOTT: Sorry, just back on that.

MS ORIEL (NSW DTIRIS): Yes, sure.

MS SCOTT: Thank you for the example about the lighting company, that was good. You talked about the tightening of the financial market. Given that within New South Wales there's $52 billion worth of exports, EFIC is only ever going to be a drop in the ocean in terms of the total volume of export sales, so in terms of government policy - this tightening in the financial market, can EFIC really be the answer to any tightening? I mean it only ever touches a small number of the total number of firms that even you - you deal with a thousand.

MS ORIEL (NSW DTIRIS): That's true.

MS SCOTT: That's right? A thousand a year.

MS ORIEL (NSW DTIRIS): I said we deal with several thousand, our team collectively.

MS SCOTT: Yes. So you're dealing with several thousand. There are 45,000 exporters in Australia. EFIC, its transaction base is in - well, it doesn't get much above a couple of hundred, so are you sure that you're concentrating your efforts at the right bit of that?

MR SMITH (NSW DTIRIS): Can I comment on that?

MS SCOTT: Yes.

MR SMITH (NSW DTIRIS): We refer to a light touch with around 5000 clients a year, which is discussions with export advisers, attending seminars and workshops, a range of focused training, that sort of thing. That's the start of the pipeline. On our side of the business when you come to our premium product, the Global Growth program where we'll give a significant grant to companies to develop a program across a number of activities which will enhance their capacity to build and sustain their export - so from the 5000 we come down to about 150 involved in the premium product. I think EFIC is similar, same orders of magnitude. If you promote through the written word, through advertising, through the web site and all those sort of things and there's a touch with clients, but it also means they become more aware of the opportunity. So when they've advanced to a particular stage in their export sustainability and growth they're ready to talk to one of the EFIC people in this room or other advisers about that support, and as we've said all along, quite commonly in conjunction with the established banks.

MS SCOTT: Okay, thank you. Thanks, Vince. Okay, Gabrielle, yes, please keep going. I think you were up to point 2.

MS ORIEL (NSW DTIRIS): Yes, my point 2. It's a long recommendation about - to cease assisting companies supplying goods and services onshore providing inputs into export supply chains. Our comment is basically that the globalisation of the world economy has meant that Australian exporters conduct exporting activities very different than they did 10 years ago. The reality of international engagement for many of our SMEs is as inputs into supply chain. They are tier three and tier two suppliers into the primes, and that's the reality. When big companies win big projects, especially in many markets SMEs couldn't enter on their own, then Australian suppliers tend to get pulled through that supply chain, if you know what I mean?

MS SCOTT: Yes.

MS ORIEL (NSW DTIRIS): So we need more of those sorts of products, not less, for that purpose, as they provide a soft international landing, and through that, those SMEs who didn't have the risk appetite before, they didn't have the capital before or the capabilities or financial means, actually gain that confidence to enter into those markets in their own right.

MS SCOTT: Yes.

MS ORIEL (NSW DTIRIS): So if the review considers it's critical to keep that recommendation then we would suggest that it might be accompanied by an assessment of the consequences on exporters withdrawing from those services, particularly around our competitive markets.

I'll give you an example of one. There's a composite material manufacturer. They were selected on an internationally competitive basis, it was worldwide, to provide to Lockheed Martin, which is a aerospace company, as the sole supplier of particular composite wing flap for the jet fighter force. That contract - using that contract they managed to secure financial guarantee using EFIC to develop a new facility and expand a facility, a $10 million financial guarantee, which is not particularly large, within Bankstown in New South Wales in Sydney. Basically that facility will be developed to supply that, and that will pull the other subcontractors through that supply chain with them to supply the whole world, because they've got that sole global supply source. That's a very large contract that EFIC was able to help them establish that in here, but that will pull those New South Wales exporters along with them.

MR SMITH (NSW DTIRIS): This is where we link this end of the business with the larger companies like Lockheed Martin. They're a defence supply chain accredited supplier along with a number of others. So we're working with Lockheed at this level and the client at this level to stitch the deal up and to make sure that the smaller client is aware of where the larger supplier is coming from and that it works.

MS SCOTT: So you're actually interfacing between the two, are you, and you brought them together?

MS ORIEL (NSW DTIRIS): Well, not necessarily.

MS SCOTT: No.

MR SMITH (NSW DTIRIS): No, it's more that we're working with the company involved as a SME, growing SME exporter, but we're also working with Lockheed Martin, not necessarily bringing them together but by understanding of the situation at both ends of the chain we're able to help that develop.

MS SCOTT: So you're involved in that process. Do you get paid for that service?

MS ORIEL (NSW DTIRIS): No, we don't.

MS SCOTT: You don't? You're invited to do that service or you found your way into that service?

MS ORIEL (NSW DTIRIS): Our facilitation is something - one of the roles that we do as part of our international - - -

MS SCOTT: But people ask you to perform that activity of your facilitation role?

MS ORIEL (NSW DTIRIS): Absolutely.

MS SCOTT: That little firm came to you or the larger firm came to you and said, "Guess what? We've just won the - - -"

MS ORIEL (NSW DTIRIS): "We've just won a $100 million contract".

MS SCOTT: "We would like you to facilitate - New South Wales Department of Trade and Investment, Regional Infrastructure and Services, we would like you to facilitate this for us"?

MS ORIEL (NSW DTIRIS): To assist.

MR SMITH (NSW DTIRIS): We'd link our involvement with - in actual facilitation with our involvement in investment attraction.

MS SCOTT: Yes, got you. All right, good, thank you, it's point number two.

MS ORIEL (NSW DTIRIS): Third point, definition of SMEs, the recommendation to limit to newly-exporting companies with a turnover of less than 25 million and support three transactions. In our submission we did note the continuing need of SMEs and that limitation there to have access to EFIC services, but we'd be very concerned if that was interpreted - and the review appears to be implying that - that support for medium size businesses, if we take that new definition of above, 25 million, as opposed to the former 150 million, were not included in that.

MS SCOTT: In New South Wales you'd have some small business programs yourself, wouldn't you?

MS ORIEL (NSW DTIRIS): Yes, we do.

MS SCOTT: What definition do you use?

MS ORIEL (NSW DTIRIS): Small business programs tend to focus far more on the lower turnover for businesses.

MS SCOTT: So what definition does the New South Wales government use?

MS ORIEL (NSW DTIRIS): For small business programs?

MS SCOTT: Yes.

DR MUNDY: Because you've got a small business commissioner, because I've met her.

MS SCOTT: Yes.

MS ORIEL (NSW DTIRIS): We have recently.

DR MUNDY: So presumably her act - the act in which she is established would determine a small business because otherwise she wouldn't know how long a piece of string was.

MS SCOTT: So what figure do you guys use in New South Wales for small business - and then we can talk about medium, but is it two million, 10 million, five?

MR SMITH (NSW DTIRIS): Not sure.

MS SCOTT: Not sure? Okay, look, we'd love to hear from you guys about what that is. Then Gabrielle, you suggested that our number is not right. Would you - - -

MS ORIEL (NSW DTIRIS): No, I'm not saying it's not right. I was just - - -

MS SCOTT: You'd like us to consider a different number?

MS ORIEL (NSW DTIRIS): No, I'm just saying please don't ignore medium size businesses.

MS SCOTT: No.

MS ORIEL (NSW DTIRIS): I'll give you an example.

MS SCOTT: No, I'd like to know what the figures that you want us to consider are just before you go on. So are you happy with the status quo that EFIC uses of 150 million or do you think that's too high, too low? What sort of size firm are you thinking about?

MS ORIEL (NSW DTIRIS): The feedback that I've had from companies is that that 150 million it's a cumbersome approval - application process, that there should be a easier or a simplified methodology for the smaller end - your 25 million, for example, end - as distinct from the 50 million plus end.

MS SCOTT: Okay, simplified process - - -

MS ORIEL (NSW DTIRIS): Most of Austrade and most of our work revolves around 30 million.

MS SCOTT: Is that right? Good.

MS ORIEL (NSW DTIRIS): That's our definition.

MS SCOTT: Okay, thank you, that's very helpful.

MS ORIEL (NSW DTIRIS): Between that, those two.

MS SCOTT: Yes, got you.

MS ORIEL (NSW DTIRIS): That's all I'm saying.

MS SCOTT: Okay.

MS ORIEL (NSW DTIRIS): I'll give you an example for that. If it did come in at 50 million - there is a blueberry grower, producer in New South Wales. They're about 50 million turnover, so they're over that 25 million, but they don't really use that service. They employ about 1000 people, seasonal grape pickers, but the season is about 10 months, so it's not exactly two-week picking periods. They export about

40 per cent to Japan. Japan has just closed its gate to Australian blueberries because of a technical issue relating to the terminology going into Japan. So they have a major market issue there where Japan is closed to them. They would be a perfect opportunity there where they now are scrambling to get into China and to Russia. They would need to put cold storage facilities in China to house their product. Basically the Australian dollar is so high they've got direct competitiveness from Colombia and all those typical market forces issues that are quite relevant - Australian dollar is high, they've got a lack of capital to be able to do that - that would be a perfect opportunity where they may be excluded from that 25 million turnover criteria, and they hadn't used EFIC's services before but they may be needing to use that. That's an example of what I would call a medium exporter.

MS SCOTT: Okay, got you. That's great, yes, thank you, Gabrielle. Okay, fourth point.

MS ORIEL (NSW DTIRIS): Fourth point, developing markets. One recommendation is that EFIC should revise its risk management policies to include a limited exposure to particular industries. Our comment is basically to consider that where there is market failure is where they should go regardless of the market and regardless of the industry sector. Exporters are moving away from a focus on traditional markets and they're moving their business opportunities into breach, like China, India, Brazil and all of those. Austrade has been reshaping its organisation. I'm sure you're aware of that - - -

MS SCOTT: Yes.

MS ORIEL (NSW DTIRIS): - - - and moving into these market failure countries - which are those ones as we have just mentioned, so sub-Saharan Africa, Colombia, Mongolia, Kazakhstan type of area - and encouraging exporters and Australian exporters to pull through with them into those markets. Moving into those markets banks are not as easily satisfied as they are in the more traditional markets. So EFIC has a role there. Similarly DFAT are doing the same thing with the free trade agreements. So we've got free trade agreements with Chile, for example, that type of thing, which is again encouraging for exporters into those markets. So EFIC has a role there to support those exporters into those riskier emerging markets.

MS SCOTT: So you would like the criteria that EFIC would apply to be, "Is this a commercial project?" "How large is your firm?" and then you would like to have a priority to newly emerging markets. Is that right?

MS ORIEL (NSW DTIRIS): No. Not a priority towards newly emerging markets. But if they were, for example - I think one of the things you highlighted was shipbuilding.

MS SCOTT: Yes.

MS ORIEL (NSW DTIRIS): If it was shipbuilding, so be it.

MS SCOTT: You don't mind the fact it's mainly in Western Australia, Tasmania. You're comfortable with that?

MS ORIEL (NSW DTIRIS): To my way of thinking, if that's where the markets are, then that's where the markets are. Follow the exporters. If that's what their needs are, then I have no particular - - -

MS SCOTT: If that sector had been receiving support from governments for the last 50 or 60 years, you would be perfectly relaxed about that as well.

MS ORIEL (NSW DTIRIS): I don't really understand the point there.

MS SCOTT: You said basically if 50 or 60 per cent of their exposure is in shipbuilding, just go where the need is. I think that's what you're saying. Have I got that right?

MS ORIEL (NSW DTIRIS): Yes.

MS SCOTT: It's true that you could end up with large exposure to shipbuilding. Would it concern you at all that shipbuilding has been a very prominent recipient of government support over the course of the last 50 or 60 years? Does that worry you?

MS ORIEL (NSW DTIRIS): If it's an emerging market, no.

MR SMITH (NSW DTIRIS): I don't think Incat has been going that long and probably Austal as well, which are the two main current ones. My recollection is it's around 15 to 20 per cent. It's a fair slice of the available funds and the available staff resources. Maybe there should be a more even spread.

MS SCOTT: There are internal audit reports suggesting that they have an overexposure to some sectors, but I understand you. I think you're basically saying if it's shipbuilding, you're comfortable with that.

MS ORIEL (NSW DTIRIS): My last point really is about the reliable risk assessment. That's the last point that I think EFIC plays a great role. In most New South Wales exporters, it can be unrealistic. Sophisticated economic and political corporate analysis is costly and can involve multiple players, multiple companies, multiple suppliers into that supply chain, and it's simply beyond the resources of most exporters. So the purchase of assessment capabilities is either built into the trade finance or the exporter may look at a potentially lucrative project with little understanding of the capital risks involved. EFIC provides exporters with free access to timely, reliable and comprehensive risk information, and I think that's a very important role that they can play with exporters, especially with time limits.

MS SCOTT: Okay. Good. Thank you.

MS ORIEL (NSW DTIRIS): Thank you very much.

MS SCOTT: So, aside from that small bit of anecdotal evidence about onerous paperwork, your clients are very happy with EFICs performance as is.

MS ORIEL (NSW DTIRIS): Yes.

MS SCOTT: Okay. I think that's clear.

MS ORIEL (NSW DTIRIS): That's just the definition of what an SME is in relation to paperwork.

MS SCOTT: Yes. So you would like paperwork to be streamlined for the very small end of town.

MS ORIEL (NSW DTIRIS): Yes.

DR MUNDY: I just want to come back to this issue that Patricia was getting at with respect to exposure to particular sectors. That of course means that just because EFIC becomes concentrated - this is a point they make - that the business becomes inherently more risky. That means that the Commonwealth bears this risk. Is this a risk that the New South Wales government has ever considered sharing with the Commonwealth? Are you happy for the Commonwealth taxpayer just to bear all of this, bearing in mind that a third of them are people from New South Wales.

MR SMITH (NSW DTIRIS): I'm not sure that a third of EFIC's market is New South Wales, although it is Sydney based and outreach is from Sydney. We invest quite a deal of funds - and you're going to ask me how much; I can't tell you - in support for businesses. We generally, with one recent exception, don't charge fees for that work. There's often debates within the organisation about priorities and about the issue of if you help one company, then the others don't get help and, quite often, they're paying for it and it's a competitive situation that - - -

DR MUNDY: Is that a competitive neutrality issue that has ever been referred to treasury or the relative competitive neutrality complaints people?

MR SMITH (NSW DTIRIS): Our major funding in support for exporters until the year just concluding requires treasury endorsement support across a number of areas: across the return on investment, the value to the taxpayer. I gather that competitive neutrality is an issue that has been considered as part of that, but it's part of the package.

DR MUNDY: So competitive neutrality is an issue that the New South Wales government would consider in its processes, as it should, because it's obliged under the competition principles agreement. You said that treasury considers a rate of return. How does treasury get at that? How does it assess what is reasonable? Is it just the cost of funds from TCorp or is it more than that?

MR SMITH (NSW DTIRIS): The funds are not capital based. They're part of the CRF, the consolidated revenue fund.

DR MUNDY: So they're just part of an appropriation, which is administered by your department, but treasury funds an eye over it.

MR SMITH (NSW DTIRIS): And it's subject to a four-yearly review, or has been for the last 12 years that I've been involved, and quite a rigorous review in that process, which is not only treasury, but it's the premier's department and the Budget Review Committee, the Expenditure Review Committee.

DR MUNDY: Is this of the programs that you administer as a whole, or is this individual grants, coming out of - - -

MR SMITH (NSW DTIRIS): Programs.

DR MUNDY: It's the programs.

MR SMITH (NSW DTIRIS): The current four-year program, which started three and a half years ago, there's a new market expansion program, which has an annual allocation and the funding is then provided as grants to individual companies.

DR MUNDY: Treasury is not involved in that individual decision-making.

MR SMITH (NSW DTIRIS): No.

DR MUNDY: That's presumably done by your director-general or it's delegated down.

MR SMITH (NSW DTIRIS): With our Tradestart obligations to Austrade, we do come across the Audit Office and the Department of Finance reviews.

MS SCOTT: I think we're fast approaching our time. Gabrielle and Vince, thank you for coming along today and thank you for your presentation and for your earlier submission.

MS ORIEL (NSW DTIRIS): Thank you for hearing us.

MR SMITH (NSW DTIRIS): Thank you.

MS SCOTT: Okay. Anna might give you her card so that you can send an email on that definition of the SME.

MS SCOTT: I'll just check that we've got Stolway Holdings available. Good afternoon and welcome to the table. Michael, for the record, would you state your name and your company, please, and if you would like to make an opening statement, we would appreciate that, as long as you keep it, say, to 10 minutes or less and then we've got a few questions for you.

MR BRIGGS (SH): Fine. My name is Michael Briggs. I'm the managing director of Stolway Holdings Pty Ltd. We are a wholly-owned Australian SME operating in the oil and gas industry internationally. We have two subsidiaries: one which provides flameproof airconditioning equipment and the other which provides natural gas processing equipment for treating natural gas streams, tank storage, and similar duties in the oil and gas industry. We operate both at the upstream level, on the production platform and production vessels, all the way down to the petrochemical side. In excess of 85 per cent of our business is in export markets and we have equipment operating in 30 countries. We were formed in 1993 and we employ a highly skilled workforce of engineers and tradespeople. We are located in Wollongong. It is quite unusual for an oil and gas operating firm to be based in Wollongong. There are numerous submissions which cover many of the points that I would probably like to make, which I have seen over the last few days. Today I would simply like to present directly to the commission our experiences in SME.

MS SCOTT: Sorry, just before you do, Michael, what did you say your turnover was, approximately?

MR BRIGGS (SH): I didn't say my turnover and I'm not prepared to disclose it.

MS SCOTT: Okay. Would you be - just giving how they sometimes ask you your age and they say Under 50 and Over 50, in our draft we have suggested a turnover of firms of 25 million might be the focus of EFIC's work. If we had a benchmark of 25 million, would you be in scope or out of scope?

MR BRIGGS (SH): Under 25 million, you say? It depends which year you're talking about.

MS SCOTT: All right.

DR MUNDY: So you're around the boundary?

MR BRIGGS (SH): Around the boundary, yes.

DR MUNDY: Yes, you're not 5 and you're not 150.

MR BRIGGS (SH): Well, it can fluctuate quite significantly.

DR MUNDY: Are you able to tell us how many people you employ?

MR BRIGGS (SH): 35.

DR MUNDY: Thank you.

MS SCOTT: Yes, thank you. Sorry, please proceed.

MR BRIGGS (SH): I suppose I was quite shocked, to be quite frank, when I first read the draft report. I had, I suppose, somewhat naively thought that perhaps it would be looking at a way for EFIC to increase its productivity. But certainly it appears that the converse is in reality what is coming out in the report and I think that is rather alarming for companies like us and others that I speak to in the export environment. Particularly in the oil and gas industry I know some other companies have had EFIC support in the past. I was quite taken aback by the negative tone in regard to exporting in general, I suppose, and in - - -

MS SCOTT: Where did you detect that, do you think?

MR BRIGGS (SH): I don't know. Some of the statements made:

> But promoting exports per se will generally only shift domestic resources (labour and capital) away from more profitable activities and potentially drive down prices of the exports (benefiting foreign buyers). This would reduce, rather than increase, Australia's aggregate income.

So there are some statements like that throughout the report, which I found, to be again quite frank, to be rather negative towards the exporting environment in general.

MS SCOTT: You understand the significance of the "per se" in that sentence. I mean, if you increase exports of, I don't know, iron ore at the expense of exports of uranium, you may not actually be any better of.

MR BRIGGS (SH): You may not, but it didn't state that it was one export to the other in the statement.

MS SCOTT: All right, but it could also apply in a situation where it is one export versus another activity which generates productivity and employment, or economic activity.

MR BRIGGS (SH): That may well be the case, but if you were suggesting that - if I ask my employees to comment on that statement, they would be saying, "If we don't export, we have no job," and in Wollongong it is a very pertinent statement. If you pay any attention to the local economy down there, there have been jobs lost at a rate of about 50 a week over the last few months. So that sort of statement, when I talk to my people about it and they read that, is taken very negatively, so I am at issue with - and I don't know whether anyone else has said it to the commission, but a lot of people in the background that I have spoken to have said the commission's report is very negative towards exporting. I had hoped to see that there would have been some criticism of EFIC along the lines that, "You aren't promoting well enough Australian exports. You should be doing more." That is what I hoped to see, naively, from the commission's report. So I'm particularly at odds.

I just want to go and explain to you some of the things that happened as to why we need EFIC support and why other companies do, from an SME. I think as we grow - and we have been doing business for quite a long time in this market, as I mentioned earlier. In most years we're one of the 45,000 exporters that don't need EFIC support and we are exporting currently into China, into Singapore, into Holland for a project in Brazil, into the UAE, and into various other countries. A lot of that is done without EFIC support, as the base of our business. Now, as we grow and as working capital requirements go up and down in the business - the GFC has been particularly rough on a lot of business, including us. As we come out of that, as we start to get orders on, which employ people, the working capital requirements increase. In fact, as a business grows, you would be aware that if you move from 10 to 20 million dollars' worth of - you typically don't generate cash, you absorb cash.

You have mentioned in the report some of the difficulties in raising cash for small business. The difficulty in the stock exchange, there's no access. The difficulty in family and friends. It has been mentioned on numerous occasions, difficulty in the banks. We have a contract for the Netherlands which used a lot of working capital. Our bank is providing the bonds, our first source. We have another job where we are doing the bonds from cash reserves. In the background there are maybe 10 other jobs going or 20 at the time, which are all being funded internally. When some of the larger ones come on that allow us to grow, we need support to provide bonds. We are doing some work in Korea which is a particularly difficult market. In the oil and gas industry the Koreans have dominated the market over the last five or six years at the main EPC level. Every payment we get - the advanced payment, the progress payments, and the final payment - for warranty, requires a bond. Without that, we can't do that sort of - without the support of EFIC, after we have already been to our bank and exhausted our own funds, we can't grow and do that sort of work. Now, we may have another couple of jobs that might need EFIC support this year; next year we may not need any.

There are a couple of things that the draft recommendations tied up there, and in 3.1, "Most products offered by EFIC are also offered by the private sector." Yes, our banks deal in bonds. But certainly we have reached the limit where the bank will no longer do those bonds, and that includes personal guarantees from the directors. In terms of overlap with our bank, there is none. You alluded to - I forget how it was worded, but it was around the incomplete information provided to the banks from SMEs. We provide information to our bank every quarter; monthly if needed. They have a very good understanding of what we do. As an SME we do produce audited accounts, so there is really no information gap as to what might be provided to the bank. Indeed, they know more about our business than EFIC ever will. There is no information gap between what our bank is getting from us and what EFIC might get from us. It is simply a gap in that working capital requirement, which does fluctuate for businesses large and small and it can fluctuate quite wildly over a number of years.

In our experience the vast majority of banks we have talked to, the banks simply won't provide the bonds without cash. They have the ability to increase their exports, and I think increasing exports - and they're still not going to be taken up by the banks, those funding gaps; they reached the limit of their funding. This goes to where you are saying EFIC should extend guarantees only and not bonds. Bonds are an integral part of the funding required by exporting companies. Where, as I mentioned with our example of the Koreans and indeed the others, bonds are required. So I think rather than bonds not being available from EFIC, they are quite low risk. We have no bond called; I'm not aware of the calling of bonds through EFIC. Low risk, they provide a good form of working capital, and I think EFIC should be supplying more bonds with reduced security from directors and at reduced fees.

I would also think the draft recommendation 10.5, in regard to the limit of three transactions, for the reasons I have alluded to earlier, is probably unrealistic as companies grow. As I mentioned, we are a perfect example, where some years we don't use EFIC support and other years we do. I have also, and I will table for you, a commercial-in-confidence. I can give you a couple of tables that demonstrate the difference in the cost of funding between EFIC and Westpac.

MS SCOTT: That would be very interesting.

DR MUNDY: That would be helpful.

MS SCOTT: Very helpful.

DR MUNDY: Can I just ask you, you would expect that over time, as a bank became more familiar with your business, you had developed a history of performance under your bonding arrangements, that the bonds would either become cheaper, the terms would become less onerous, that in a sense they would be easier to get less expensively, because there was a track record. It's a bit like a no-claim bonus on your car insurance, I guess. What you're saying is the banks do not exhibit that sort of behaviour?

MR BRIGGS (SH): No, they don't. We have moved the bank a little bit towards that sort of behaviour, where they are giving us a bond on basically what they call cash flow lending, but that took a long time and a lot of history to be able to get there. I don't think your issues of support or trying to have EFIC tell the banks what to do is going to change that. In fact, I'm sure of it.

DR MUNDY: What was motivating our concern was circumstances - and I'm not saying this about your company. But a concern that we have that businesses may become dependent upon EFIC support or at least, alternatively, not look around for alternative banking arrangements. In fact, the banks might become dependent on EFIC support.

MR BRIGGS (SH): I don't think that's the case, commissioner. In fact, EFIC often says, "Well, what's the position of your bank in providing this?" It is something we talk to them about before we even approach it, so I think - and we have been with the same bank since we started. We have looked at various banks along the way, including overseas banks HSBC and Arab Bank, who operate in our market, obviously, in the Middle East. Certainly we would have advanced nothing by going to them. In fact, it would have been detrimental, because they didn't know us to the extent that our bank does. So I don't think it's a valid concern. One of the other things with the report is also I notice there were a lot of meetings with government enterprises in Canberra, but it didn't state that there were any meetings with SMEs prior to the draft report being issued. I think the report could have benefited from a little bit more knowledge from people in the SME environment, like myself, who have these needs.

DR MUNDY: That's the reason why we issue an issue paper and seek comment on the issues. That is why we have these hearings.

MR BRIGGS (SH): I understand.

DR MUNDY: That's why we issue a draft report.

MR BRIGGS (SH): I think the issues paper probably didn't get to become an issue for people like ourselves until we saw the contents of the draft report. It is a moot point, the fact - - -

MS SCOTT: How did you become aware of the draft report?

MR BRIGGS (SH): EFIC, the Institute of Export, and other people. Anyone else that saw the report and had major alarm bells ringing. I think that could have been established before it got to that stage.

MS SCOTT: So in fact EFIC or the Institute of Export could have drawn your attention to the issues paper.

DR MUNDY: And they didn't.

MR BRIGGS (SH): Not that I saw.

MS SCOTT: No.

DR MUNDY: Fair enough.

MR BRIGGS (SH): You must probably appreciate that people like us get an enormous amount across our desk each day.

MS SCOTT: Sure.

MR BRIGGS (SH): And unless it affects us, we tend to ignore or bin those things.

MS SCOTT: Sure.

DR MUNDY: Just coming back to this bank behaviour, other than the ongoing support of EFIC, the sort of issues you describe are actually symptomatic for some Australian firms who operate primarily within Australia: they have issues with working capital.

MR BRIGGS (SH): Absolutely.

DR MUNDY: What do we do with the banking systems to try to make it get over these sorts of behaviours, or is it just too hard and we should give up and go home?

MR BRIGGS (SH): Well, I don't know. Wayne Swan can't seem to convince them, so I don't know what you can do. I think the only thing is history, and that is indeed why our bank has extended some bonds into the cash flow, because they have seen what we've done over a long period of time, they've seen what we've done with EFIC. But I think EFIC is complimentary with the banks and I think that if you read - I did a little bit of research, and I haven't got the benefit of the time the commission has to do an enormous amount of research on what is happening with other ECAs. In fact, I didn't know who a lot of them were. Certainly most of them state that they are working with the banks. In the industry, as I travel, I hear the ECAs are supporting competitors and jobs we're not involved in.

International markets are still quite unstable, credit is difficult, the ECAs in other countries are being increasingly active, and I think without EFIC to support the ones that are in the situation we are, you are going to find that it is going to do a lot of damage to the export industry. I note the statistics about the 45,000 exporters, and a lot of it does have without support. But I think the criticism at EFIC is that it should be doing more, like overseas ECAs are. I don't know what the bureaucratic or the economic ideology in terms of getting out and getting the banks to support that sort of funding. The reality is that they will support to a level and they won't go any further. When overseas customers require large amounts of bonds, it is either you provide the bonds through EFIC or you don't do the business.

MS SCOTT: Thank you very much for coming along today. We appreciate your contribution and your interest in this. I don't think we have any further questions for you.

DR MUNDY: That's very helpful.

MS SCOTT: Thank you very much.

MR BRIGGS (SH): I can give you a couple of pages, if I may.

DR MUNDY: If you could give them to our folk up the back and then they will make sure that they are properly protected.

MR BRIGGS (SH): I'll certainly do that. I'd be most happy to reduce the cost of EFIC, because it is quite a lot higher than the banks.

MS SCOTT: Is Grahame White available?

MR WHITE (BI): Yes.

MS SCOTT: At this stage, a quick invitation to anyone in the audience - well, there's very few in the audience. But is there anyone that does want to make a statement at the end? No, all right, I have asked. Wait, okay, so we'll have one comment from Jubilee. Now, over to Bronx International;. Thank you for coming along today and especially for sitting in on our hearings today. For the purposes of the record, could you please identify yourself and state your role and your firm, and then we'd be most keen to hear your words of wisdom in terms of an opening statement.

MR WHITE (BI): I'm Grahame White. I'm the chairman of Bronx International. I'm a non-executive chairman. I'm sitting here today because our managing director, a chap by the name of Rod Sawyers, would normally be put in this role, but he's having a nice holiday up north somewhere, so good for him.

MS SCOTT: Yes.

MR WHITE (BI): I'm accompanied by Leontia.

MS TRIMBOLI (BI): My name is Leontia Trimboli. I'm the finance director of Bronx International.

MR WHITE (BI): Thank you very much.

MS TRIMBOLI (BI): Good. What I propose to do in a very short submission is not to not tell you all about our company, but tell you a couple of things about our company which I think are particularly relevant to the way we operate and the way we operate with EFIC's help, because we do utilise EFIC's help and, I'll say at the start, we value it very highly, but we use it very deliberately in a limited way. We seek not to rely on it to address some of the comments that have been made earlier. So I'll talk about that. I'll talk about how we use EFIC and make a couple of other brief comments at the end.

The features of our business I think that are relevant is, firstly, that we are in the steel industry. Secondly, and particularly important for talking about exports, is that we export capital equipment. I'm sure we're not the only exporter in Australia of capital equipment, but I don't think there are too many. It's not a normal thing that happens in Australia. It's developed in a way that has been reasonably successful, particularly taking into account the rather mature industry in which we work.

Bronx has been going since 1989, and the relevance of that in terms of exports is that it's been an exporter right from the start. We export 100 per cent of our output in general terms. We have built, over that period, 76 steel coating lines, that's galvanising lines or colour coating lines, which, by the way, make galvanised-sheet steel or colorbond, as we know it in Australia. We do the coating stage of those. Each line would be in the region of, say, four to 25 million dollars, and we did a rough calculation of the ones we supplied over the last few years. They work out at about $17 million per project.

We're not a huge organisation. Let me pause just a moment. In terms of exporting, we don't export anything to the USA, we don't export anything to Western Europe, we don't export anything to New Zealand or Canada. In other words, all of our exports go to developing countries. All of those 76 lines, bar two, have gone to South-East Asia, Central and South America, South Asia, East and West Africa and, latterly, Eastern Europe. So we're entirely export. The other two lines, by the way, have gone to BHP or BlueScope, as it is now. They bought one small pilot line from us for Port Kembla and another line has been installed in Sydney and is operating quite successfully. We make a good product in competition with BHP, I might add, or BlueScope.

So I was just going to say that we're talking about capital equipment. We're talking about a lead time for each item of about 18 months. So we're talking here, as you'll appreciate, about dealing with less-developed countries. We're dealing with project finance in reasonable-sized lumps. Not huge, but reasonable size, particularly for the markets we're going into, and we're dealing over a long lead time.

MS SCOTT: Are you a family business? You're not listed, I take it.

MR WHITE (BI): We're not listed. There was a business owned until 2000 by a parent company in England, which ran into some strife, and at that time it was acquired by one shareholder in England and some local shareholders here.

MS SCOTT: Thank you.

MR WHITE (BI): So it's held by executives, I guess, or ex-executives.

MS SCOTT: I don't want to ask you a question that is commercially sensitive, but would you characterise yourself as an SME, and are you towards EFIC's definition of an SME, which is up to 150 million, or more towards what we went with in the draft report of 25 million? I'm just trying to get some sense of the size of your firm. You're clearly very active in the marketplace, but - - -

MR WHITE (BI): I've given that a bit of thought and I'm sure Leontia might have a comment on that too. We've certainly been below that limit from time to time. We've been above it from time to time, like your previous presenter. It varies greatly, particularly in our industry. We're dealing with capital projects. It's very, very lumpy.

DR MUNDY: Can you tell us how many staff you've got. That will help us scale things.

MS TRIMBOLI (BI): We've got 25 full-time staff.

DR MUNDY: 25.

MS SCOTT: But you must be scaling up and down as you're - - -

MR WHITE (BI): We employ contractors.

MS TRIMBOLI (BI): So, as our business changes, we go out and we contract staff to the engineering department or what process we're up to.

MR WHITE (BI): In terms of whether we're an SME or not, that occupied my mind a little bit because, even if we go up to 150 million, to take that figure, in a very real sense, we're still going to be an SME, because we don't have physical assets. Our input to the product is soft, as I term it, not hard. All the fabrication work and similar work we subcontract, so that we could go up by quite a large amount, up to 150 million, and not really increase our capital very much.

Indeed, because we're operating in the project business, it should all be project finance and shouldn't be financed by us. That's the view we take. It should be financed by the project, with the help of all the people needed to do that. That's the basis on which we work. So that's where export project financing becomes very relevant to us. So maybe, in that regard, I might just mention the type of customers we deal with, because again that's relevant to this particular issue.

We have three types, we say. We've got people like steel mills. We've got people in markets in Africa or Asia or elsewhere who are maybe making roll-form steel-building products and they're going to build a galvanising line or a paint line. So they're narrow-focused, going into the industry quite new. Also in those markets, very typically and very interestingly, from my point of view, you've got people who are just diversified entrepreneurs. They might be making bottles, concrete, Scotch whisky, whatever they make. They're into everything and they think they've got to have a steel coating.

So that last group, going backwards, very often has access to their own finance. The first group, the steel mills, to whom we are designing, by the way - they're a very small group for us - would have their own finance. The middle group are people who generally tend to find it rather more difficult.

DR MUNDY: They're, what, essentially building products type companies and developing companies?

MR WHITE (BI): Yes, who are building up their business, think they will backward integrate and they need capital to do it and, as I say, they might be in Bangladesh or they might be in Guatemala, we're currently doing a project. So they're looking to do it and they're doing it, in a way, pretty hard, because they're in markets which are pretty tough or project markets. So that brings us, I think, to EFIC. The first comment that I think I'd make is that we have pretty good relationships with our banks or a banker.

MS TRIMBOLI (BI): A banker.

MR WHITE (BI): A banker, primarily. Leontia might want to add something here now. That relationship has been improving. I've noticed in your draft work you're talking about the increasing sophistication and capability of the banking system. I'd agree with that, but, taking up points which you've raised with other presenters, it's not increasing enough. It can increase more and, in answer to the question which I'm sure you would ask if I don't answer it now, no, I don't know the way that you get banks to lend more to exporting businesses.

DR MUNDY: Someone must.

MR WHITE (BI): I'd offer a little comment. We have some experience with England, where we have a smaller associate company operating. If anything, the companies in the midlands have done it even tougher, as regards banks, than we have here. It has been really tough. It's got to the stage there where the government representatives have been calling in various areas, such as Midlands and such as Cambridge where I see you've spent some time - - -

DR MUNDY: Yes.

MR WHITE (BI): - - - calling together the local industry people and saying, "How are we going to get the banks to lend you more money?" This is government to industry. I'd only say that whatever they've done, things have improved, at least from our point of view, our perception.

DR MUNDY: That may be reflection of the fact that most of the UK banks are currently owned by the British government.

MR WHITE (BI): Indeed, yes. I think it probably reflects government pressure through that way or some other way, yes, so it might be worth looking at that. But anyway, that's the issue there. Getting to EFIC, we use EFIC in two ways. I'll deal with project financing first. Project financing where EFIC comes into the game for us is very highly valued, but I would emphasise very limited. We've been dealing with EFIC basically since 1990 when we started. Up till about five years ago frankly we didn't get a lot out of them. For whatever reason, and I don't know what reasons, they were never able to make an offer that worked for us in any way. In that latter period things have been much better, they have been much more productive, but as a matter of our company policy we don't go to our customers saying, "Hey, get some finance from EFIC." We'd rather they get their own finance, from our point of view. They're in their country, they've got their banks, we'd rather they go to their banks, get their finance, give us the necessary security we need for the deal - LCs, confirmed LCs - and then away we go ahead and do the project. We build the line.

DR MUNDY: Can I just stop you there. How do you find your banks' acceptance of the LCs that you get offered?

MS TRIMBOLI (BI): It depends what country we're talking about. Some countries our banks can do confirmation of LCs. Our bank is actually St George who is now Westpac as well. They actually have an association with the World Bank at the moment, so some of the LCs we're able to get St George to confirm because of their arrangement with the World Bank. We also use HSBC who are more open to trade with the banks that our customers deal with. So we're lucky we have an association with both banks to do it, but we also have a board policy that if we cannot get HSBC or our bank, St George, to confirm the letter of credit we tell the customer, "You have to find another bank."

DR MUNDY: You mentioned HSBC. Is that simply because the nature of their business they're more geographically spread, so - - -

MS TRIMBOLI (BI): Yes, they've got more branches on the ground and we find with St George that if they're trying to talk about deal in Bangladesh they don't know about the market. They are risk-adverse at the moment, whereas HSBC know the market a bit more and can confirm the letter of credit for us.

DR MUNDY: So would you see that over time - I mean the ANZ has recently given some indication to the review that's being run by Ken Henry of its intention to drive its business model essentially through Asia. I'm not talking about the ANZ in particular but would you expect over time as Australian banks develop that business that you'd be able to access and confirm LCs more readily because they look more like HSBC?

MS TRIMBOLI (BI): I just see the way St George - the way they've worked is they've gone to the World Bank because they know they can't take that risk themselves.

DR MUNDY: Okay.

MS TRIMBOLI (BI): Whereas HSBC, you know, are more open for that. So we've been with - we actually were with ANZ previously and we actually left them because they couldn't do any confirming LCs for us.

DR MUNDY: Okay.

MS TRIMBOLI (BI): They may be more - better in Asia but the markets that we're in they can't assist with. We're not in the easy markets.

MS SCOTT: Not in Turkey and so on.

MS TRIMBOLI (BI): No. The markets we deal with aren't the easy ones.

DR MUNDY: Okay, so it's a reflection of them being in the right place for your business?

MS TRIMBOLI (BI): Yes.

DR MUNDY: Okay. Sorry.

MR WHITE (BI): As a general comment, by the way, we find, don't we, that EFIC has a pretty good international network and support.

MS TRIMBOLI (BI): Yes.

MR WHITE (BI): As good as the banks, I think.

MS TRIMBOLI (BI): Yes.

MR WHITE (BI): Yes.

MS SCOTT: Would you like to say something about the charges or pricing policy of EFIC on the activities that you've undertaken with them?

MS TRIMBOLI (BI): Yes. The main cost for us is regarding the bonding line that we have with EFIC. We have also a bonding or a guarantee line with St George and we use both in order to help our business grow. So we use the St George one as much as possible because they are cheaper than dealing with EFIC.

MS SCOTT: Okay.

MS TRIMBOLI (BI): EFIC is more expensive but when you want to go for a contract and you need that bond you then have to include that extra cost into your estimates.

MS SCOTT: Are we talking about chalk and cheese there, because St George is, in terms of their bonding line, that they're dealing with particular markets and not interested in others, whereas what you're seeing from EFIC could be reflecting the higher - - -

MS TRIMBOLI (BI): Regarding the bonding line, the bank guarantee line we have with St George they don't care who I'm issuing the guarantee too. So they will issue a guarantee to Bangladesh. They're taking the security of Bronx International as the company. So it's not the fact that the costing structure is around to who the customer of the guarantee is going to, it's just we have a facility, that's the cost with that facility and with EFIC that cost is higher.

DR MUNDY: So basically you go to EFIC when you've used up the line?

MS TRIMBOLI (BI): Correct, yes.

DR MUNDY: So it's not credit differentiated in any way?

MS TRIMBOLI (BI): No, it's basically - - -

DR MUNDY: Because they're pulling on your risk, not - - -

MS TRIMBOLI (BI): Correct, yes.

DR MUNDY: So it's a capacity?

MS TRIMBOLI (BI): Yes.

DR MUNDY: Given that that's the circumstance have you looked at going to CBA, NAB, ANZ for similar products?

MS SCOTT: They were with ANZ.

MS TRIMBOLI (BI): We were, yes.

MR WHITE (BI): Yes.

MS TRIMBOLI (BI): Just to let you know, the facilities that we had with ANZ were about a quarter of the facilities that we have with St George. That was one of the main reasons we moved because they understood our business a lot better, whereas - we're not a huge company. We don't tick all the boxes with the bank, and ANZ we just couldn't grow with them, whereas - that's one of the main reasons we moved.

DR MUNDY: So really, what has happened is that St George, for some reason, has formed a view different to ANZ's?

MS TRIMBOLI (BI): Correct, yes.

DR MUNDY: Just on this point, have you explored options with the other banks?

MS TRIMBOLI (BI): Yes, we've actually had talks with HSBC to see what they could do and to increase our facilities. They couldn't match by any means what St George gives us.

DR MUNDY: What about EFIC?

MS TRIMBOLI (BI): Sorry?

DR MUNDY: What about the facility you have with EFIC? Was HSBC more expensive or more onerous then - - -

MS TRIMBOLI (BI): They wouldn't give us facility at all.

DR MUNDY: They wouldn't?

MS TRIMBOLI (BI): HSBC wouldn't give us anything.

DR MUNDY: Okay.

MR WHITE (BI): I think we found that pretty interesting. You know, we do have such an internationally diverse business and HSBC is similarly matching. In a previous age I used to work with HSBC and Standard Chartered and found them very good. But here they're subject to some sort of constraints which don't let them operate in that way, unfortunately. If I may - although I might say my previous employer was BHP - so that I might had some impact on that also - with small companies and BHP.

DR MUNDY: Yes.

MR WHITE (BI): But I might just make the point here in passing in relation - I did mention the project finance sector. We don't go to our customer and say, "Here's their offer. How about using EFIC?" We only introduce EFIC as a possibility when we know the customer is having trouble and the project is starting to look a little bit difficult. So we just did a little calculation, about 10 per cent of our volume over the last five years had some sort of EFIC support, and they're the marginal ones. So the point I wanted to make there is that that's pretty important to us, because that's the extra 10 per cent that we probably wouldn't have got otherwise. But in relationship between project finance and bonding support - - -

MS TRIMBOLI (BI): Bonding line.

MR WHITE (BI): - - - bonding line, the odds you mentioned. To us the bonding line is a much more significant operation because we can be in a situation where we don't need many guarantees at all, and just a few months ago we were in just that situation, and then hey, now we've got a few orders and they've come in a lump and Leontia has already calculated what we'll need to get beyond what the bank can do for us. So to cater with those sort of surges the extra support that we get from EFIC has been pretty important and we've found them much more helpful than in the past.

MS SCOTT: Grahame, have you had exposure to the export credit agency in the UK from your previous life?

MR WHITE (BI): Well, our associate company has, and they've had no joy with them at all.

MS SCOTT: Okay.

MR WHITE (BI): Yes.

MS SCOTT: All right, interesting.

MR WHITE (BI): You're talking about a company which is in a sort of similar business to us but at the heavier end of equipment, so they're dealing with steel mills. I've been interested to see that in an exporting country like the UK with a region that's not doing so well - we're talking about the Midlands here - that they just don't get any help at all.

MS SCOTT: Okay, all right, thank you.

DR MUNDY: Good.

MS SCOTT: We've gone through pricing and availability. Is there any other - I guess you've highlighted what you see as an effective arrangement for you. Is there any areas for improvement, in your view, or are you basically satisfied with the services that you are able to access through EFIC?

MS TRIMBOLI (BI): Like the previous gentleman said, one of the comments I would like to make is that the paperwork side of EFIC sometimes can be very cumbersome. For a medium to small business the amount of paperwork that is required or discussions that are required before a project can be financed can sometimes take a little bit of time. When you're - our type of business where you're trying to execute a project quite swiftly, sometimes the - I wouldn't say delay but the time taken to sort of go through the process that EFIC requires can sometimes delay the start of a project for us.

MS SCOTT: Okay. You've had quite a significant number of transactions over the years, so there must be a certain level of familiarity and confidence building in both sides of the relationship?

MS TRIMBOLI (BI): Yes.

MR WHITE (BI): Yes. I think that's substantially improved the performance, from our point of view, of EFIC that they know us well.

MS SCOTT: Yes.

MR WHITE (BI): I might say the same also goes for the banks.

MS SCOTT: Yes.

MR WHITE (BI): Leontia, in particular, has built up a relationship with the banks now where they know us pretty well too. Over time that works, so we're looking to try and grow and we'll need more of those guarantees.

MS SCOTT: What size of activity would you need to get to before you would - you might not want to answer this question - before you would consider finding other equity partners?

MR WHITE (BI): Other equity partners?

MS SCOTT: Yes.

MR WHITE (BI): I think that will only happen if we wanted to diversify into a different sort of business, into more of a manufacturing-type business, not a project-type business. We don't see any need really to get a lot of equity for the sort of business we're doing now, which is very much project focused and which we can service with extra contractors and by building up our resources.

MS SCOTT: I see.

MR WHITE (BI): But we have given some thought to diversification, and who knows?

DR MUNDY: That was very helpful, thank you.

MS SCOTT: Thank you very much for coming along. Where are you located?

MS TRIMBOLI (BI): Peakhurst.

MS SCOTT: Okay.

DR MUNDY: Peakhurst? I grew up in Narwee.

MS TRIMBOLI (BI): That's not far away.

DR MUNDY: Not at all.

MS SCOTT: Very good, well, thank you very much for coming along.

MS TRIMBOLI (BI): If you need any more information on our company please don't hesitate to call.

MS SCOTT: It's a kind offer, thank you.

DR MUNDY: Thank you.

MS SCOTT: I think that then means that we're back with Carmelan. You just want to make just a few comments. Is that right?

MS POLCE (JA): Yes.

MS SCOTT: Well, could you come to the table?

DR MUNDY: So we can get it on the record.

MS SCOTT: Again, for the transcript, could you identify yourself and then your time starts, and we'd like to think that five minutes is it.

MS POLCE (JA): It will be less than that. Carmelan Polce, deputy director of Jubilee Australia. I wanted to speak very quickly to a number of comments made during the day about the importance to Australia of exports, particularly exports to developing countries, it has come up again and again. Eurodad research indicates 80 per cent of debt owed by lesser developed countries is owed to export credit agencies, 80 per cent.

Jubilee Australia was formed during the Jubilee 2000 movement for debt relief for developing nations when the world finally turned its attention to the crippling level of debt owed by lesser developed countries. Much of that debt was illegitimate, that is, arranged via a loan contraction process that involved perhaps breaches of fiduciary duty, illegality and even criminality. Of course borrowing for productive investments like the Bronx International investments, investments that promote sustainable and equitable development can be an important strategy for less developed countries. For that reason the Australian government should ensure that official export credits and guarantees provided by EFIC are open to public scrutiny, with information on projects that have environmental, social and human rights risks made available prior to transaction approval. Thank you.

MS SCOTT: Thank you. Right, well, with that, happy to call today's hearings to a close. We resume our hearings in Canberra tomorrow. I don't expect any of you to be turning up again, but just in case it's worthwhile mentioning it to you. Once again, thank you very much for your participation today and your interest, and where people have made submissions, for their submissions.

DR MUNDY: Thank you.

MS SCOTT: Thank you to transcription and our staff.

AT 4.11 PM THE INQUIRY WAS ADJOURNED UNTIL
TUESDAY, 27 MARCH 2012