Final Episode In The Drawn-Out Holden Drama

Economics & Deregulation | Alan Moran
Australian Financial Review 12th December, 2013

The soap opera of General Motor's departure from Australia is ending. The company has been operating with sporadic profitability for a decade and more.

Last year it lost $153 million. This was in spite of it benefiting from the 5 per cent tariff protection on domestic sales and $73 million in government grants, although half of that was for the commercially fruitless pursuit of the green car political ideology.

In recent years, Holden's products and quality have shown vast improvements from the models sold 15 years ago.

Locally assembled cars have been losing Australian market share. But this is to be expected in a global business that operates an internal market where each area sources models from the most appropriate location. That spells specialisation of products, more imports and more exports.

Holden's export strength is in the "muscle cars" which have received considerable critical acclaim in the United States. But even then, they were forced to sell at very low profit margins to keep competitive. And US sales, having risen to 30,000 a year prior to the 2008 global financial crisis, have fallen 90 per cent.

Holden Australia has found itself in the wrong market segment with a product whose labour costs and government impositions make it more expensive to build than GM cars in other locations.

It's the same story with engines. Holden's V6 line is losing favour and its output is falling below the long-planned 100,000 level. Even within the GM family, the Australian V6 is losing out to similar engines made elsewhere.

Holden's cost problems are well-known. They do not stem from the company being undercut by cheap third world labour. Even those plants in Europe, Japan and North America, where living standards are similar to ours, operate more productively. Very little of this is due to greater economies of scale overseas.

Holden has become little more than an enterprise run by unions for the benefit of workers and union officials, with lavish employment conditions bringing a crippling cost disadvantage.

One indicator of this is the starting wage for a production line worker: $23.50 an hour in Australia, compared to $14 an hour agreed by unionised plants in the US (even less for non-unionised plants). On top of this, Australian workers get shift penalties and overtime rates, and more than twice the normal weekday rate for

Sunday shifts. These and other conditions are unknown in the US and make Australian labour market costs double those elsewhere.

PROFOUND MISUNDERSTANDING ON THE LEFT

Although labour costs in assembly only comprise 20 per cent of total costs, these are crucial and not irrelevant, as the secretary of the Australian Council of Trade Unions Dave Oliver has argued.

Oliver's view, shared by so many on the political left, represents a profound misunderstanding of the drivers of business decisions in an interlinked world.

If wages are 20 per cent of costs and double what they might be, this wipes out profitability. Such cost-padding requires a price rise of 12 per cent. Yet the industry faces tight competitive conditions and Australia is integrated into a world market which provides no scope for such a price increase. Hence, the cost must come from profit, which it virtually eliminates.

Similarly, the carbon tax and the renewables requirement add severely to Holden's woes.

Holden estimated the carbon tax was costing it $45 a vehicle but the total cost of carbon emission measures - including renewable requirements - on assembly and components is much greater.

Compared to its overseas competitors, these imposts might add as much as $600 to the cost of a car. This alone is 5 per cent of the ex-factory costs and halves the firm's net profit, providing international management a clear pointer about future global capital allocations.

Holden's Australian management acquiesced to union demands, buying short-term peace at the expense of the strategic loss of value for the company. In part, this was due to the centralised wage-fixing conditions loaded in favour of unions. Management at Holden saw the immediate loss of output from industrial unrest as too great a price to pay. Noting that costs were excessive, they hoped something would turn up, including further subsidies from governments besotted with the idea that a motor vehicle assembly industry was the key to economic well-being.

They had ample justification for thinking this. In addition to subsidies, Labor in Canberra and Adelaide financed numerous consultants' reports that told a tale of massive employment multipliers and technology gains from motor vehicle assembly. Of course, these were all mythical. Such gains can be counted for every new job, but when the job is financed by taxation, its multiplier additions are offset. If the new job comes out of profits, the future is jeopardised.

Now we have the endgame. Unions face lower revenues from scamming the motor vehicle companies. Workers face much lower wages in alternative jobs - even if these become available.