

New Zealand Defence Industry Association Forum

Speech by John McKinnon, Secretary of Defence

13 October 2009

It is a pleasure to be able to attend the Defence Industry Association's annual forum – my third as Secretary of Defence.

Earlier today you heard from the Associate Minister of Defence, the Hon Heather Roy, in which she discussed the three companion studies being led by her as part of the Defence Review 2009, in particular the study into the New Zealand defence industry.

That your sector's contribution to equipping, maintaining and sustaining the New Zealand Defence Force is the subject of a separate study that will inform the wider review is evidence of its importance. Based on the guidance provided by a comprehensive review of Defence, there will be many more opportunities for the defence industry in New Zealand, particularly in through-life support. I encourage you all to participate.

I intend to focus my comments today on the Defence Review, while also touching on the "business of defence".

The key issues facing Defence generally relate to one of two interdependent questions. These are:

- how we use the Defence Force; and
- how we manage the Government's significant investment in Defence Force capability?

The success of the Review will ultimately rest on whether we can provide a durable framework for guiding decisions on these questions.

This framework will be developed and refined over two documents. The first, a Defence Assessment, is being conducted by the Ministry and will report on defence policy priorities and strategies. It will also develop a range of options for aligning policy, capabilities and force structure. And it will examine options for

improving the administrative and organisational capabilities of the Defence agencies, including around procurement.

The Defence Assessment is due with Ministers in December.

The second document, a Defence White Paper, will be the culmination of a process of consultative review, both across government and with the public. Drawing on the options in the Defence Assessment, it will chart a policy direction for Defence, provide guidance to policy planners, and signal the Government's security intentions.

The intention is to complete the White Paper in the first quarter of next year.

Whereas past reviews have resisted forecasting likely levels of expenditure, it is our intention to present the Government with fully costed options, providing the basis for a transparent and sustainable funding track for Defence. While not a budget itself, the Review will inform budget decisions.

Why is a review timely?

As mentioned by the Associate Minister, this is the first major review of Defence in over a decade. In that time, not only has the global security environment become more challenging, but the factors shaping the New Zealand Defence Force's ability to respond are of a different order.

At the end of the 1990s, the Defence Force was under considerable pressure because of an increasing operational tempo, declining expenditure on defence, and failing capabilities, especially in the Army and the Air Force.

The Government of the day was cognisant of these problems – they had been aired in the 1997 White Paper, *The Shape of New Zealand's Defence*, and the Foreign Affairs, Defence and Trade Select Committee Inquiry into *Defence Beyond 2000*.

The period of intense acquisition activity that followed was focused on the recovery and ongoing operation of the New Zealand Defence Force. In the ten years to 2009, over \$4 billion was committed to:

- enhancing the Army's mobility and firepower;
- upgrading or replacing all the Air Force's major platforms; and
- re-balancing the Navy.

Under the Defence Sustainability Initiative, operating funding was also increased, providing for a recovery in personnel numbers and reserve stocks.

As a consequence, the New Zealand Defence Force is now benefiting from improvements in capability, performance, and reliability.

The current Defence Review is an opportunity to build on this platform by putting in place a long-term, realistic, and financially sustainable plan for the future development and operation of the New Zealand Defence Force.

It will focus in detail on the five years to 2016. However, reflecting the long-life of capital equipment, it will extend out to 2035.

The Government has indicated that it wants a deep review. Reflecting this, the Minister has appointed an independent panel of eminent persons to test and critique the core assumptions underpinning the Review.

The work of the Review is being undertaken in eight parallel workstreams that have been designed so that they can be drawn together to provide the substance of the Defence Assessment.

The workstreams correspond to the main issues identified in the Terms of Reference, which are publicly available. They are:

1. Policy, Objectives and Strategy;
2. Military Capability Options;
3. Human Resource Issues;
4. Real Estate and Infrastructure;
5. Defence Organisational Structure;
6. Procurement;
7. Funding and Financial Management; and
8. Cost and Personnel Modelling.

It is not my intention to discuss each of these separately. Instead, I want to focus my comments on those workstreams which are of relevance to defence industry.

The Review's recommendations must be grounded in sound policy. Defence is after all an expensive business - it is also an uncertain one. Too often the link between policy and capability has been weak, leading to some unsatisfactory outcomes. Having a clear policy framework based on an assessment of our current and future security environment is critical to determining a capability mix and force structure that provides the Government with an appropriate set of options for meeting its security obligations, as well as delivering value for money.

Having a clear policy framework is also good for defence industry. It provides a greater level of certainty, while also increasing the information available to support planning and investment within the sector.

Policy development does not take place in a vacuum. It involves a stock-take of what we are doing now, and a judgement as to whether this will likely continue and, if so, in what form. At a risk of oversimplification, there are two main ways in which New Zealand governments have deployed the Defence Force since 1999:

- in our immediate region, for deterrence, surveillance, and assistance with stability, as well as undertaking civil tasks; and
- beyond our immediate region as a contribution to collective security operations.

New Zealanders expect the Government to play a significant and sometimes leading security role in the South Pacific. This expectation is matched in the region itself, and is shared by our principal defence partner, Australia.

The force of our response to the devastation and tragic loss of life caused by the tsunami that struck Samoa is an example of this. Moreover, on three occasions in recent years meeting this expectation has resulted in the commitment of a large number of Defence Force personnel and assets – in Timor-Leste, Solomon Islands and Tonga. The consensus amongst diplomats and

defence planners is that we should expect a recurrence of such tasks over the next 30 years.

Beyond our region, the expectation that New Zealand continues to play a role in upholding collective security arrangements is unlikely to change given our own self-interest in a strong, rules-based international order. Currently the New Zealand Defence Force is heavily committed in Afghanistan. However, in an unstable world, there will be other requests.

In both circumstances, we need to take into account the changing nature of conflict and the prevalence of conflict with rather than between states and with protagonists who regardless of their armament can inflict casualties on their opponents.

As mentioned, a key outcome for the Review is providing government with a framework that converts high-level policy considerations into decisions about military capabilities and force structure. Fortunately, we are not starting from a blank canvas. Since 1999, new capability worth around \$2 billion has been introduced into service, or is being introduced, while a further \$2 billion is in the acquisition phase.

But within the timeframe of the review, we have a number of very significant decisions to make regarding replacements for the C-130 Hercules and P-3 Orion fleets, and the Naval Combat Force. While it is premature to think in terms of platforms, the requirement to transport troops; the importance of maritime domain awareness; and the ability to make a credible contribution to maritime security operations in the Pacific and Asia is unlikely to change in the short to medium term.

Because of the significant sums involved in acquiring these capabilities, the Government has indicated that a priority for the Review is to ensure that the procurement and budget procedures within the Ministry of Defence and the New Zealand Defence Force are cost effective and meet best international and commercial practice.

Turning capability choices into real capabilities is a linear process that includes capability development, asset acquisition, introduction into service, operational service, and disposal. For our more complex capabilities it will also include a mid-life upgrade.

Seen as silos, the component parts of this process appear to be working reasonably well. For example, fluctuations in the cost of equipment in the acquisition phase are normally less than 0.1 percent. When taken as a whole, however, the procurement process does not lend itself to silos. The cost of ownership is incurred throughout the whole life of an asset, and not at the point of acquisition. We need to be certain that the incentives within each component part are all working to minimise the true cost of owning a capability over its life.

The Procurement and Defence Organisational Structure workstreams are being led by senior external consultants with proven expertise. This is appropriate - the use of external experts in these areas adds credibility to the process and should mitigate any risk of a perceived conflict of interest.

The Government has been careful not to constrain the policy process prematurely by imposing fiscal parameters. We are, however, realists. Defence planners internationally are preparing for a prolonged period of austerity. While New Zealand is better placed than many comparable nations as we come out of recession, we are not approaching the Review on the basis of a significant increase in defence funding.

The Minister has indicated that expenditure of around 1 percent of GDP on Defence is about right, and that the replacement of the Defence Force's major capabilities is affordable within the current budgetary framework.

This means we must get maximum value out of every dollar. This will be done, in part, by establishing a clear logic linking New Zealand's strategic interests to specific military capabilities. It will also be done by focusing on savings in the supporting 'middle and back' of the New Zealand Defence Force, and by rationalising the Defence estate. All options are on the table, including partnerships with the private sector.

While the Review is a priority, the business of Defence continues. The Deputy Secretary for Acquisition, Des Ashton and his New Zealand Defence Force colleagues will provide you with a detailed update on our acquisition projects tomorrow. In the meantime, let me outline some of the key platforms Defence is awaiting to introduce into service:

- two new Offshore Patrol Vessels as part of Project Protector;
- the new NH-90 medium utility helicopter fleet;
- the new A109 training and light utility helicopter fleet;
- the upgraded C-130 Hercules fleet; and
- the upgraded P3 Orion fleet.

The arrival of these new or upgraded platforms will provide additional opportunities for industry to provide through-life support, maintenance and supply to the New Zealand Defence Force. I encourage you to think of innovative ways in which your companies may be able support the range of New Zealand defence capabilities.

Active and ongoing engagement with industry is central to developing capabilities which meet our requirements. To this end, the Ministry of Defence is a committed supporter of the annual Defence Industry Forum and we value our engagement with the Defence Industry Association. I would like to thank the Chairman of the Defence Industry Association, Mike Wardlaw and his team for hosting such an important event.

In closing, I would reiterate that with the guidance provided by the Defence Assessment and Defence White Paper, there will be many more opportunities for defence industry in New Zealand, Australia and beyond. The current economic slowdown aside, the future looks positive, especially in through-life support, maintenance, and supply. Opportunities will continue to arise for partnership activities between local industry, international companies and Defence and we will encourage them.

Finally, I wish you well with this forum, and for the awards dinner tomorrow night. Thank you.