OVERVIEW

Key points

- Government assistance to industry is provided by tariffs, budgetary outlays, taxation concessions, regulatory restrictions and other measures.
  - Assistance generally benefits the industry receiving it, but it can come at a cost to other industries, taxpayers and consumers.
  - Some assistance, such as R&D funding and measures with environmental objectives, can deliver net community benefits if well designed and targeted.
- In 2007-08, Australian Government assistance to industry amounted to $9.4 billion in *net* terms (that is, after allowing for the cost impost of import tariffs).
- The mix of industry assistance has changed over the five years to 2007-08.
  - Net tariff assistance has declined in real and nominal terms, and is scheduled to decline further with the phasing down of automotive and TCF tariffs.
  - In contrast, budgetary assistance increased by more than one third in real terms.
- Budgetary assistance to industry will increase further.
  - The Australian Government has announced outlays of around $20 billion associated with 'traditional' industry support, including assistance to the rural sector, automotive and TCF activities and R&D.
  - Concurrently, it announced more than $15 billion associated with infrastructure provision and regional development commitments, potentially providing some assistance to selected service providers or benefits to service users.
  - An additional $40 billion is directed to measures announced in response to the global financial crisis, much of which will benefit selected industries.
- Other recently announced responses to the global financial crisis, including the guarantee of bank deposits and wholesale funding and assistance to commercial property projects, will also confer assistance to industry.
- Policies that aim to reduce greenhouse gas emissions, apart from their environmental effects, also have a substantial impact on the assistance landscape.
  - The Commission has identified over 240 measures, involving an estimated $23 billion in government outlays.
  - By 2011-12, proposed Australian Government spending would amount to some $8 billion. In that year, the estimated cost to industry of proposed emission permits will be around $12 billion.
- The global financial crisis has increased pressures on governments to protect local industries. Although they have collectively committed to resist such pressures, trade restricting measures have been introduced in many countries.
  - To help maintain progress, international commitments and surveillance need strengthening. Over time, institutional arrangements that expose the domestic costs of each countries' own protection also have an important role to play.
- Governments are pursuing preferential trade agreements as a means of achieving trade liberalisation. More research on the effects of such agreements is needed.

Overview

The industry assistance landscape in Australia has been significantly reshaped over the last 30 years. Since the 1970s, large general reductions in tariff rates, removal of import quotas and reform of agricultural marketing arrangements have led to significant declines in *measured* levels of assistance. On the other hand, there has been an increasing trend, particularly over the last decade, towards greater budgetary assistance to industry.

Such trends are likely to continue with the announcement of numerous budgetary assistance measures in the past year, some involving an expansion of existing programs, such as for the automotive industry. Proposed responses to climate change concerns will also provide substantial new budgetary assistance to affected industries. The global financial crisis and subsequent recession have added a further dimension, increasing pressures to protect domestic industry. Although governments have collectively committed to resist such pressures, additional trade restricting measures in many countries have been introduced — posing a further threat to the world economy.

Trade & Assistance Review reports the Commission's estimates of Australian Government assistance to industry and recent policy developments with ramifications for Australia's assistance structure. However, assessing whether the benefits of any particular support program exceed the costs requires detailed case-by-case consideration — a task beyond the scope of the *Review.*

Estimates of assistance to industry

In 2007-08, total measured assistance to industry by the Australian Government was \$17.5 billion in gross terms or \$9.4 billion in net terms (that is, after allowing for the cost impost of import tariffs). The value of tariff assistance alone was \$9.2 billion, predominantly to manufacturing industries. At the same time, tariffs imposed a cost penalty on inputs throughout the whole economy estimated at \$8.1 billion. Budgetary outlays provided around \$4.7 billion in industry assistance while tax concessions conferred further assistance of \$3.6 billion.

In real terms, measured net assistance to Australian industries increased by 20 per cent over the five year period to 2007-08, with the mix of industry assistance changing considerably. Net tariff assistance declined in real terms. Agricultural pricing and regulatory assistance also declined and is likely to fall to negligible levels with the completion of the Dairy Structural Adjustment Program in April 2008. In contrast, budgetary assistance increased by 36 per cent in real terms to 2007-08.

Reviews of industry policy

In 2008, the Australian Government initiated four major industry policy reviews covering:

- export policies and programs (the 'Mortimer' review);
- national innovation system (the 'Cutler' review);
- automotive industry (the 'Bracks' review); and
- textile, clothing and footwear industries (the 'Green' review).

The reviews collectively made over 200 recommendations. These not only addressed industry assistance matters such as tariffs, subsidies and trade agreements, but also touched on broader issues pertaining to industry performance, including environmental regulation, industrial relations, government procurement and education and training.

Each review found a potential role for government in overcoming market failures and made recommendations for the continuation, or increased resourcing, of existing R&D, innovation and export development programs. The creation of several new programs was recommended.

The reviews also favoured a role for government in 'strategic priority setting' — for example, in identifying prospective export markets or goods and services on which to concentrate government efforts, setting national innovation priorities, ensuring long-term manufacturing of certain products and the establishment of industry councils to identify priorities.

A general problem confronting the reviews was a lack of information on activities or industries receiving assistance and consequent outcomes. Moreover, some of the claimed benefits of government support in inducing additional activity and the extent of alleged public benefit presented in the reviews appeared optimistic.

To enhance program assessment, there would be merit in improving information about industry assistance program participation and how economic outcomes have been changed by that participation.

Recent industry-related announcements

Since November 2007, the Australian Government has announced substantial new spending with potential implications for assistance to Australian industry. Most proposed outlays are to occur within the next five years, though some will extend beyond this.

Around $20 billion is associated with traditional forms of assistance to industry as normally reported in the *Trade & Assistance Review*. Most of this amount relates to support for business R&D, exports, agricultural and related activities and the motor vehicle and parts industry. Around $5 billion (of the $20 billion) is associated with ongoing programs.

A further $15 billion was committed by the Australian Government for infrastructure and support of regional development. In addition, the Government has made a commitment to support the development of a national broadband network. These various commitments will have a range of impacts on industry, some of which would confer assistance either to recipients or user industries. The level of assistance and its incidence, however, is often difficult to determine and would depend on factors such as: the level of government contributions and the risks transferred to the private sector; user charges relative to the costs of service provision; and the public good nature of the infrastructure.

Measures announced in response to the global financial crisis — the Economic Security Strategy, ‘Nation Building’ package, and ‘Nation Building and Jobs Plan’ include some $40 billion that is ‘industry related’. As in the case of infrastructure provision and regional development commitments, the parts of these programs that affect investment returns or service costs and prices have potential implications for industry assistance. However, the packages also include components that are not industry-related, totalling $20 billion, such as one-off cash payments to pensioners, carers, students and eligible families.

In addition to budgetary outlays, the Australian Government has announced other measures that may directly or indirectly benefit industry, including the guarantee of bank deposits and wholesale term funding, the purchase of residential mortgage backed securities and assistance to car dealer financiers.

Carbon emission reduction programs

Governments are increasingly introducing measures that aim to reduce carbon emissions or assist industry in transitioning to a lower carbon economy. In this *Trade & Assistance Review*, the Commission has compiled a list of existing or prospective Australian Government and State and Territory measures of this kind.

This initial stocktake has identified over 240 assistance measures involving around $23 billion of actual or proposed outlays over the five years to 2011-12. Australian Government measures account for 94 per cent of the total *value* of outlays identified, although only 34 per cent of the *number* of budgetary measures. Assistance to industry is also provided through quotas on the use of renewable or low-emission energy and higher prices for electricity sourced from small-scale, low-emission generators.

Australian Government annual spending is scheduled to increase from around $300 million in 2007-08 to some $8 billion in 2011-12, mainly as a result of the proposed Carbon Pollution Reduction Scheme (CPRS) — the largest component of the measures identified.

- The CPRS would account for $6 billion of projected total assistance in 2011-12 alone (largely made up of permit allocations to affected industries).
- At the same time, the proposed requirement to buy emission permits will impose additional costs on industry of around $12 billion in that year.

Apart from their environmental effects, these policies will significantly alter the industry assistance landscape and impact on the economy. Some assistance to affected industries is likely to impose costs on the broader economy, including through higher carbon permit prices. Further, the effects of the carbon emission reduction measures are inter-related, including with other national policy measures, such as energy efficiency, road congestion and transport pricing.

For these reasons, carbon emission reduction measures require regular review and evaluation. Governments have committed to undertaking reviews of the national Renewable Energy Target and most other forms of assistance, including assessments of the potential to streamline some measures in light of the CPRS. Given the level of interaction between different measures (many being administered by different governments) there would be merit in giving greater weight to the design of national mechanisms to guide the coordination and review of these measures.

International trade policy developments

Before the global financial crisis, the primary focus of international trade policy was on achieving trade and investment liberalisation through multilateral, regional and bilateral forums. However, the financial crisis and resulting contraction in world trade, has brought a new set of pressures on governments to support domestic businesses and activities, typically at the expense of trading partners.

Although many governments have collectively committed themselves to resisting calls for greater protection, most notably at recent G-20 meetings, the WTO has identified at least 80 new protectionist measures. Moreover, the Doha Round of multilateral trade negotiations, which could strengthen liberalisation and help resist new protection, remains unresolved after eight years of negotiations. Initiatives to clarify the coverage of commitments at international forums and improve transparency through the WTO are needed.

In addition, to underpin enduring reform, there is a need for initiatives to examine and make transparent the *domestic* costs of each country's own protection measures.

A lack of progress in multilateral forums may also result in governments further pursuing preferential trade agreements (also referred to as 'free' trade agreements). Although these agreements may lead to some increase in trade and investment among those involved, unlike multilateral or unilateral reforms they can also divert trade away from least cost sources of production, thereby impairing national and global productivity and economic growth. In addition, the proliferation of product-specific rules of origin that apply in preferential agreements can further inhibit trade and innovation. In light of the complex and two-sided effects of preferential arrangements, more research on how they are operating in practice is needed.