
4 Recent developments in assistance to selected industries

As well as providing quantitative estimates of the levels of assistance across the economy, each year the Commission documents and reports on key policy changes and developments affecting assistance to industry.

In this chapter, the Commission reports on recent developments in selected industries. These include the four more highly assisted industries identified in chapter 3, namely textiles clothing & footwear, the automotive manufacturing industry, dairy farming and sugar growing. It also reports on recent developments in relation to citrus growing, ethanol production, tourism, and airlines.

4.1 Dairy

Background

The dairy industry has been subject to adjustment pressures for some years. This process has been driven by a long-term trend of the cost of inputs rising faster than prices. In response, farms have generally become larger and herd sizes have increased, as have cow yields. Australian dairy companies have also increased their processing capacity. With domestic milk output growing more quickly than the consumption of dairy products, the share of production that is exported has increased. In recent years, over 50 per cent of total milk production, and 60 per cent of manufactured dairy products, have been exported (ADC 2001).

For many years the dairy industry was the most highly assisted industry in Australia. Until June 2000, Commonwealth and State arrangements inflated drinking milk prices in order to generate monetary transfers from Australian consumers to dairy farmers. Under these arrangements, State dairy authorities paid eligible farmers a fixed price for drinking milk, which was more than twice the farmgate price for freely traded 'manufacturing' milk destined for processing into products such as butter, cheese, milk powder and ice cream. These arrangements helped to deflect adjustment pressures in some parts of the industry.

During the National Competition Policy review process, strong support for dairy deregulation emerged in Victoria. Victoria is the largest milk-producing state, but produces the lowest proportion of drinking milk. Accordingly, Victorian farmers had been receiving far lower prices on average for their output than dairy farmers in other States. For example, in 1999-2000, Victorian farmers received an average of 26 cents per litre at the farmgate, whereas Queensland farmers received 39 cents per litre. In a ballot conducted by the Victorian Government in December 1999, a vast majority of Victorian dairy farmers voted in favour of deregulation.

Changes in assistance

The dairy industry was largely deregulated in July 2000, eliminating the artificial distinctions on milk supply in Australia and facilitating interstate milk trade.

As part of the deregulation process, the Commonwealth Government introduced an assistance package — the Dairy Industry Adjustment Package — to provide payments to dairy farmers. These payments will amount to around \$1.8 billion over the period to 2008.

The largest component of the adjustment package is the Dairy Structural Adjustment Program (DSAP), which is to provide \$1.63 billion in equal quarterly instalments to eligible farmers (and ex-farmers) over the 8 year life of the package. Farmers can use private financing arrangements to convert this assistance into a lump sum payment. To qualify for the program, dairy farmers must demonstrate that, on 29 September 1999, they had an interest in a dairy farm enterprise that delivered milk during 1998-99. Almost 30 000 farmers will receive DSAP payments averaging a little over \$54 000 over the life of the package.

Other programs in the adjustment package include the Dairy Exit Program, the Dairy Regional Assistance Program and the Supplementary Dairy Assistance Program.

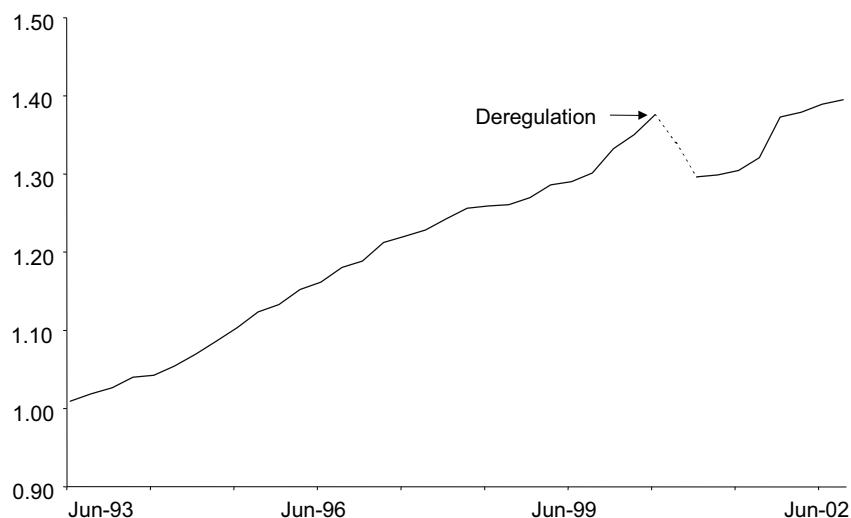
The cost of the package is funded by an 11 cents per litre levy on retail sales of drinking milk, to remain until at least 2008. Further details of the adjustment package and milk levy were provided in last year's *Review* (PC 2001).

Payments under the new arrangements represent a significant reduction in support for the dairy industry compared with the previous arrangements. The DSAP delivered around \$180 million in funding in 2000-01, while the previous Commonwealth and State arrangements are estimated to have provided around \$450 million in assistance in 1999-2000. As a result of the changed arrangements, the effective rate of combined assistance for dairy has decreased from 31 per cent in 1999-2000 to 13 per cent in 2000-01 (although they are estimated to have increased again, temporarily, to around 16 per cent in 2001-02 — see chapter 3).

Effects on consumers

Notwithstanding the 11 cent per litre levy on drinking milk imposed in July 2000, retail milk prices fell by around 5 per cent in 2000-01 (figure 4.1). In the year before deregulation (1999-2000) and the next year after deregulation (2001-02), milk prices rose by about 6.5 per cent. The ACCC reported that prices for plain milk sold in supermarkets fell 22 cents per litre in the first six months of deregulation. Savings to consumers in the 12 months following deregulation were estimated to exceed \$118 million from supermarket sales alone (ACCC 2001).

Figure 4.1 Nominal retail prices for drinking milk, 1993 to 2002
\$ per litre of standard white milk



Source: ABS (2002c).

That said, retail milk prices actually increased in the ACT and the Northern Territory after deregulation. This is because farmgate prices were not previously regulated in the territories, while the price of raw milk used for UHT milk products had been previously set at a lower level than for other drinking milk products. Consequently, the 11 cents per litre retail milk levy exceeded the reduction in purchase costs for milk at the farmgate (ACCC 2001).

For the sector as a whole, retail prices for dairy products (including products such as cheese and ice cream as well as drinking milk) fell by around 1 per cent in 2000-01. In the year immediately before deregulation, prices increased by 4.6 per cent, and in the next year after deregulation, they increased by 6.7 per cent.

Accordingly, deregulation appears to have caused an initial, one-off reduction in retail prices. Prices now appear to be growing largely in line with their earlier trends (figure 4.1). Price changes are still subject to short-term fluctuations in supply conditions, such as the current drought which is reducing supply. In terms of demand, per capita consumption of drinking milk has remained fairly stable for a number of years, averaging around 100 litres per year. Another one-off fall in prices is likely some time around 2008 when the retail levy is removed.

Effects on producers

Under the previous assistance arrangements, the farmgate price of milk used for drinking was far higher than the farmgate price of the same milk if used in manufacturing. In 1999-2000, the drinking milk price averaged 47 cents per litre, compared to an average per litre price of 21 cents for manufacturing milk (ACCC 2001). As noted earlier, these arrangements created significant disparities in the average farmgate price for milk received by farmers around Australia.

Deregulation has caused a re-balancing of farmgate prices (table 4.1). In 2000-01, the average price for milk received by farmers in New South Wales, Queensland and Western Australia fell by around 20 per cent. There was also a marginal reduction in the average farmgate price in South Australia and Tasmania. However, in Victoria, where most milk is produced, farmgate prices rose by around 13 per cent. Across all states, the average farmgate price for milk remained unchanged at 29 cents per litre in 2000-01. Farmgate prices in all States increased in 2001-02.

Table 4.1 Farmgate milk prices, 1999-2000 to 2001-02

<i>State</i>	<i>Farmgate prices (per litre)</i>			<i>Post deregulation change^a</i>
	1999-00	2000-01	2001-02	%
New South Wales	36.0	29.1	32.5	-19.2
Victoria	26.0	29.3	33.3	12.7
Queensland	39.3	30.6	34.5	-22.1
South Australia	28.0	27.7	31.5	-1.1
Western Australia	36.0	26.6	28.7	-20.3
Tasmania	25.9	25.0	32.7	-3.5
Australia	28.8	29.0	33.0	0.7

^a Post deregulation change reports the percentage change in prices in the year following deregulation, that is, between 1999-00 and 2000-01.

Sources: ACCC (2001) and ADC (2002).

Accordingly, while there has been a long-term decline in farm numbers, in the year following deregulation dairy farmers exited the industry at a higher rate, particularly

in NSW and Queensland. Between 1985 and 1999, the number of dairy farms in Australia declined, on average, by 2.3 per cent per year. In contrast, the number of dairy farms declined by almost 8 per cent in 2000-01 (table 4.2). The main driver of the spike in exits has been the removal of price and production controls and the availability of the DSAP, which has probably brought forward many farmers' decision to exit the industry (ABARE 2002b).¹

Table 4.2 Changes in retail milk prices, farm numbers, herd sizes and production, 1985-2002

Annual percentage change

<i>Years</i>	<i>Retail drinking milk prices</i>	<i>Number of farms</i>	<i>Average herd size</i>	<i>Milk output per cow</i>
1985-1999	5.8	-2.3	1.4	3.2
1999-2000	6.6	-2.0	0.7	3.4
2000-2001	-5.2	-7.9	5.1	-8.0 ^a
2001-2002	6.5	na	na	na

^a Poorer seasonal conditions contributed to the decline in milk production in 2000-01. **na** not available.

Sources: ABS (2002c), ADC (2001).

The increase in exits in the year following deregulation coincided with an increase of 5 per cent in the average herd size (table 4.2), indicating that some of those exiting the industry have sold their stock to other dairy farmers. This should allow the remaining farmers to benefit from 'economies of scale'.

Data on the total number of farmers exiting the industry in 2001-02 are not available, but it is possible that there has been further rationalisation within the industry, driven by the effects of the price changes and declining incomes due to the drought, as well as the ongoing availability of assistance under the various adjustment programs.

¹ In contrast to the popularity of the DSAP, there has been a limited take-up of the Dairy Exit Program (DEP). To be eligible for the DEP, farmers must have less than \$157 500 in assets after the sale of their farm. DEP payments are also reduced to take into account any adjustment assistance already provided under the DSAP. The Commission understands that, in 2001-2002, of the 228 farmers that applied for the DEP, 123 farmers were granted payment. Further, the total level of assistance provided under the DEP is \$5.28 million, with a small number of claims still to be assessed.

4.2 Sugar

Background

Centred mainly in north-east Queensland, the Australian sugar industry has been subject to a number of reforms since the mid 1990s.

Following a National Competition Policy review of the industry, tariffs on imported sugar were removed in July 1997 and domestic price supports were partly dismantled by the Queensland Government. These arrangements had provided significant assistance to domestic canegrowers and sugar millers, at the cost of domestic consumers and food processors. As then measured by the Commission, assistance to the industry fell from \$66 million in 1996-97 to \$13 million the following year.

To help offset the reduction in assistance, the Commonwealth Government introduced a \$14 million Sugar Industry (Research) Assistance Package in July 1998. Two years later, in response to adverse climatic and farming conditions in the industry, the Commonwealth introduced an \$83 million Sugar Industry (Cane Growers) Assistance Package. A condition of the Government's provision of this package was that the industry develop proposals for comprehensive structural reform (Truss 2002a). The Queensland Government also allocated \$10 million for concessional loans for the replanting of sugar cane crops. These developments are described in more detail in *Trade & Assistance Review 1999-2000* (PC 2000).

Recent developments

In February 2002, the Commonwealth Government commissioned an independent assessment of the Australian sugar industry — the Hildebrand report (Hildebrand 2002). The report examined the overall state of the Australian sugar industry, with particular emphasis on its economic, social and environmental drivers. The report, which was delivered to the Government in June 2002, made a number of findings and recommendations, including:

- the sugar industry is largely unprofitable, and farmers' business management skills are variable and often not well-developed;
- government and industry need to continue efforts to gain access to protected European, US and Japanese markets;
- product diversification of both cane and raw sugar must be further encouraged;
- the sugar industry must adopt an 'engage not defend' approach to environmental matters; and

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- options should be explored to support some cane growers to exit the industry — in the context of achieving more consolidated and viable industry arrangements.

In its response to the report in September 2002, and against a background of continuing climatic and financial difficulties in the industry, the Commonwealth announced a new Sugar Industry Assistance Package. The package is worth up to \$150 million, and is expected to last for five years. The main elements of the package include:

- a Regional Projects Program — \$60 million for regional adjustment, diversification and industry rationalisation;
- a 50 per cent interest subsidy scheme over two years for loans of up to \$50 000 that are taken out for replanting purposes;
- a \$45 000 one-off tax free payment, available from February 2003, for farmers who leave the industry; and
- short term income support for a period of up to 12 months to help stabilise the industry and to assist those in immediate need.

The package will be funded mainly by a levy on domestic sugar sales (including sales of imported sugar and sugar for retail sale, food services and food processing). The levy of 3 cents per kilogram will last for approximately five years, commencing in January 2003. Exports of refined sugar will be exempt from the levy and a rebate will be available for sugar used in manufactured products for export (Truss 2002b).

In addition, the Queensland Government also announced that it will contribute \$30 million to the assistance package (Beattie 2002a). Its contribution entails:

- *Sugar Innovation Fund* — \$10 million to support new management systems and new technologies, increase export-oriented production of value-added sugar products and develop more efficient supply chains;
- *Regional Change Management Program* — \$10 million to assist farm viability and address environmental, water and training issues; and
- *Concessional Loans for Sugar Farm Consolidation* — \$10 million to assist cane growers to expand their operations by purchasing other sugar farms. The loans will be available at concessional interest rates over a period of 20 years, and can be combined with private finance.

In addition, the Commonwealth and Queensland Governments signed a Memorandum of Understanding to help facilitate reform in the sugar industry. The Memorandum addresses a number of issues, including ‘the repeal of elements of the *Queensland Sugar Act 1999* which adversely impact on the industry’s efficiency and limit its flexibility to foster new industries and alternative products to maximise

returns to growers' (Truss 2002b). In commenting on this aspect, the Commonwealth Government stated:

Although the Queensland Sugar Act is Queensland legislation and can only be amended by the Queensland Government, the Federal Government supports the removal of all impediments to reform, including any embedded in the Act (Truss 2002c).

In September 2002, the Commonwealth Government also announced that it would provide a subsidy for the production of ethanol which, although mainly derived from wheat at present, can be derived from sugar. Associated with this, it agreed to provide assistance to the Mossman sugar mill for the construction of an ethanol production facility (see section 4.8).

4.3 Citrus growing and processing

Over the last decade, the citrus industry has been undergoing significant structural change. The industry has been required to adapt to shifts in consumer tastes, along with increased opportunities to export fresh fruit and substantial growth in imported Frozen Concentrate Orange Juice (FCOJ) from Brazil. This growth in FCOJ imports has been driven by reductions in tariffs from 35 per cent in 1989 to 5 per cent currently.

In September 2001, the Commonwealth Government asked the Productivity Commission to inquire and report on the competitive situation and outlook for the citrus growing and processing industry. The Government also sought advice on whether any measures were necessary to enhance the industry's competitiveness, and whether a formal 'safeguards'² investigation was warranted.

In its April 2002 report, the Commission considered that additional industry-specific assistance was not justified and that a safeguards investigation was not warranted. The Commission argued that much of the citrus industry was already adapting successfully to change, and that such assistance would not efficiently or equitably target low-income citrus growers. The Commission also found that the existing export controls may be impeding the development of overseas markets for Australian citrus products.

In responding to the report in November 2002, the Commonwealth Government noted that some sectors in the industry are facing difficult times and offered to

² Article XIX of the General Agreement on Tariffs and Trade (1994) allows for safeguard action against imports of particular products which are deemed to be causing, or threatening to cause, serious injury to an industry. Safeguard action is intended to provide temporary assistance for industries to adjust to increased competition from imports.

extend the joint Commonwealth/NSW Murrumbidgee Irrigation Area (MIA) PowerPACT program.³ It also announced the continuation of export control regulations for the industry, stating:

The growing industry has demonstrated a need for export control powers to continue in its high value markets and that the Government is moving to continue those powers beyond February 2003 (Truss 2002e).

4.4 The automotive industry

Background

Although assistance to the motor vehicles and parts (MVP) industry has declined significantly since the mid-1980s, MVP remains one of the most highly assisted industries in the manufacturing sector.⁴ Its assistance derives largely from tariffs and tariff concession schemes, such as ACIS and TRADEX:

- Tariffs on imported new passenger motor vehicles (other than 4WDs) have been fixed at 15 per cent since 2000, but are scheduled to fall to 10 per cent in 2005.
- Under ACIS, which commenced in January 2001, MVP producers receive transferable credits based on their domestic production which can be used to reduce the customs duty payable on eligible imports. Total import duty forgone under the scheme was capped at \$2 billion over the five year period for which the scheme was initially to run.

In addition to tariffs and tariff concession schemes, the MVP industry also receives assistance from other sources including government procurement programs, the luxury car tax that applies mainly to imported vehicles and prohibitive tariffs on imports of second hand vehicles.

While the local vehicle market has been growing steadily over the last decade, domestic producer's market share (in volume terms) has fallen from 80 per cent in the late 1980s to 40 per cent today, largely in parallel with reductions in import

³ The PowerPACT program forms part of the Rural Partnership Program. To receive assistance from the latter program, citrus growers are required to develop a business plan. The MIA PowerPACT program provides subsidies of up to 90 per cent of the associated costs of a business plan, up to a maximum of \$2700.

⁴ As discussed in chapter 3, the effective rate of combined assistance to the MVP sector in 2001-02 was 11.2 per cent, or more than double the manufacturing average. As part of its recent inquiry in the automotive industry, the Commission estimated that the effective rates of assistance for a typical motor vehicle assembler and component producer in 2000 exceeded 30 per cent. The differences between these estimates principally reflected the broader coverage of the MVP industry which is used for the estimates published in *Trade & Assistance Review*.

protection. At the same time, exports have grown significantly, now accounting for more than 30 per cent of production, and production levels have been relatively stable during the 1990s. The MVP industry, centred in Melbourne and Adelaide, now accounts for around 0.6 per cent of value added and employment in the economy.

Recent developments

Over the last two years, several measures have been introduced to assist individual MVP projects or the automotive industry in general:

- In December 2000, the Victorian Government provided an assistance package to Holden to build a new engine plant in Melbourne. The plant has also received \$12 million in funding under the Commonwealth's Strategic Investment Incentive Program.
- In March 2001, the South Australian Government provided an interest-free loan to the value of \$20 million to Mitsubishi Motors. The company also received a grant of \$500 000 from the Commonwealth to assist the company to develop feasibility plans for future production in Australia.
- In May 2001, the Commonwealth Government announced a measure in the budget to enable registered businesses to claim full GST input tax credits on fleet vehicles, thereby reducing the cost of motor vehicles to businesses by around 9 per cent.
- In July 2001, the Commonwealth tightened the eligibility requirements for used vehicle imports under the Low Volume Scheme.
- In November 2001, the Victorian Government provided an assistance package, largely in the form of payroll tax relief, to the Ford Motor Company in relation to planned production of a new four-wheel-drive vehicle.

These developments were discussed in more detail in last year's *Review* (PC 2001).

More recently, in April 2002 the Commonwealth Government announced a \$35 million assistance package for Mitsubishi Motors Corporation. The assistance will be available from 2004-05 and is contingent on Mitsubishi meeting specific commitments on the timing and scale of its investments. In particular, the assistance is conditional on the creation of an additional 900 direct jobs in Mitsubishi's Adelaide manufacturing operations and the establishment of a global R&D centre in South Australia with on-going employment of around 300 people. The South Australian Government is to provide an additional \$50 million in cash and 'in kind' assistance to Mitsubishi to help facilitate the necessary investment (Howard 2002a).

Post-2005 assistance arrangements

In March 2001, the Commonwealth Government requested the Productivity Commission to undertake an inquiry into post-2005 assistance options for the automotive industry.

In its report, the Commission (PC 2002a) indicated that a tariff of 5 per cent should be a target for the industry. It favoured a one-off reduction to this rate in 2010, facilitated by continuation of the ACIS after 2005. However, the Commission's preferred option was that the capped component of assistance available under the ACIS end in 2010.

The Commonwealth Government announced a new assistance package for the automotive industry in mid-December 2002 (as this report was being finalised). Under the package, after their scheduled reduction in 2005, automotive tariffs are to remain at 10 per cent until January 2010, when they will be reduced to 5 per cent and remain at that level until (at least) 2015. The package includes an extension of the ACIS from January 2006 to December 2015, with assistance under the new scheme to comprise:

- uncapped duty credits estimated at \$1.2 billion over the ten years;
- capped assistance of \$2 billion, to be spread evenly over the period 2006 to 2010; and
- an additional \$1 billion in capped assistance to be provided during the period 2011-15, subject to phasing arrangements to progressively reduce the assistance over the period.

The Government also announced that it would establish, from the vehicle producers' portion of the ACIS budget, a \$150 million R&D fund to operate over the period 2006-08 to 'support key technologies put forward by vehicle producers that warrant specific encouragement' (Costello 2002b).

In announcing the new arrangements, the Government stated:

The new look package goes far beyond what was recommended by the Productivity Commission Review, adding an extra 50% or \$1.4 billion over the 10 year continuation of the scheme. The package is also aimed squarely at innovation, it has a greater emphasis on R&D, rather than production subsidies...

Similar to its predecessor, the post-2005 Automotive Competitiveness and Investment Scheme will be a transitional scheme that will encourage competitive investments by firms in the automotive industry in order to achieve sustainable growth (Macfarlane 2002c).

The Government also indicated that it will ask the Commission to undertake a further inquiry in 2008 to determine whether changes are warranted to the legislated tariff reductions in view of conditions in the international trade environment.

4.5 Textiles, clothing and footwear

The textiles, clothing and footwear (TCF) industry has the highest level of tariff protection among all manufacturing industries, even though its assistance from tariffs (and quotas) has declined significantly since the mid-1980s. All TCF tariffs (apart from those already at rates of 5 per cent or less) were reduced to rates of 25 per cent, 15 per cent or 10 per cent in July 2000. TCF tariffs are to remain at these levels until January 2005, when tariffs on apparel and certain finished textiles, footwear and fabrics have been legislated to decline to 17.5, 10 and 7.5 per cent, respectively.

A new package of budgetary assistance measures for the TCF industry — the main component of which is the TCF Strategic Investment Program (SIP) — commenced in July 2000 and is scheduled to run until 2005. The SIP is projected to cost \$700 million over the five years. The main activities eligible for SIP funding are investment in new TCF plant and equipment, R&D and product development. Total benefits under the scheme are subject to a limit of 5 per cent of sales of eligible products in the previous year. The SIP also provides regional adjustment assistance in the form of payments to assist the purchase of ‘state of the art’ second hand plant and equipment where existing firms have consolidated or merged.

The Government made several changes to the operation of the SIP during 2001. Among other things, the changes expanded the coverage of the SIP to ‘...provide earlier and more flexible access to grant funding’ for eligible firms. Details of the changes were reported in last year’s *Review* (PC 2001).

In 2001-02, TCF attracted combined tariff and budgetary assistance of around \$800 million. Its effective rate of combined assistance was around 25 per cent — several times the average of the manufacturing sector (chapter 3).

In November 2002, the Commonwealth Government asked the Productivity Commission to conduct a public inquiry on a range of related matters that will affect the sector’s long term viability, and policy options for post-2005 assistance arrangements for the TCF sector. The Commission is required to finalise its report to Government by 3 July 2003.

4.6 Tourism

Background

The tourism 'industry', as defined by the ABS, comprises parts of several other industries, such as *Accommodation, cafes & restaurants* and *Transport services*. It reflects expenditure by both domestic travellers and visitors from abroad. So defined, tourism is an important part of the Australian economy, accounting for 4.7 per cent of GDP in 2000-01.

Tourism in Australia has grown significantly over recent years, and the Tourism Forecasting Council expects the current annual number of international visitors to increase by two-thirds by 2012 (TFC 2002).

However, tourism faces significant challenges at present, due largely to recent terrorist attacks, the global downturn in air travel, the collapse of Ansett in late 2001, and rising public liability insurance premiums.

Early in 2002, the Commonwealth Government announced that it would develop a strategy for the tourism industry with input from a wide range of government and industry stakeholders. This medium to long-term strategy is due for release in 2003.

In the immediate aftermath of September 11 and Ansett's demise the next day, a Tourism Industry Working Group was established in late September 2001 to report on the effects of these events on the tourism industry. The group identified three areas that it considered required attention to ensure that the industry remained viable over the short to medium term:

- the maintenance of consumer confidence and demand;
- employment and cashflow concerns; and
- the restoration of domestic air capacity and discounted airfares (Burnes 2001).

The working group recommended several initiatives to address these matters, including additional funding for the Australian Tourist Commission to promote Australia as a 'safe haven' and direct consumer initiatives to promote domestic tourism, particularly to regional Australia. It also recommended initiatives to address the immediate cashflow problems facing the industry, such as deferral of the December 2001 company tax payment and the provision of concessional business loans to tourist operators.

Assistance measures⁵

In response to the working group's report, the Commonwealth Government announced the expansion of a number of existing tourism programs, including:

- *Australian Tourist Commission* — an additional \$24 million will be provided over the four years to 2005-06 to refocus the promotion of Australia as a 'safe haven';
- the *Regional Tourism Program (RTP)* — an additional \$8 million has been allocated to 2005-06; and
- the *See Australia* campaign — an additional \$8 million will be provided to 2005-06 to foster tactical marketing and domestic tourism in regional areas.

A number of new assistance programs, including two specifically related to the collapse of Ansett, were introduced to maintain the short-term viability of the industry:

- *Travel Compensation Fund* — \$5 million was allocated to the Fund in 2001-02. The Fund compensates consumers who had purchased a holiday package, but who had not taken the holiday and lost the value of that package because of the Ansett collapse. The Commonwealth Government offered the assistance to cover the expected increase in claims on the Fund. This assistance was matched by State governments.
- *Ansett Holiday Package Relief Scheme* — \$15 million was allocated in 2001-02 to assist small businesses affected by the Ansett collapse. Small to medium sized

⁵ The Commission has not previously published estimates of assistance to tourism in *Trade & Assistance Review* or, until recently, elsewhere. However, in its current study of the *Industries in the Great Barrier Reef Catchment and Measures to Address Declining Water Quality* (PC 2002c), the Commission developed preliminary estimates for the industry. The estimates incorporate funding for the Australian Tourist Commission, the Regional Tourist Program, the Domestic Tourist Campaign and the Regional On-line Tourism Program. The estimates also include a proportion of the net tariff and budgetary assistance received by other tourism-related industries, as defined by the ABS. While the estimates suggest that net assistance to tourism may be negligible, the Commission emphasised, among other things, that it has yet to investigate all measures that may benefit or penalise tourism. Among other things, the Commission's estimates did not include State and Territory assistance to tourism — the estimates in appendices C to J suggest that the sector receives more dedicated assistance from State and Territory Governments (around \$300 million in 2001-02) than from the Commonwealth (around \$120 million that year). The Commission intends to undertake a more detailed study of assistance to tourism in the year ahead.

businesses which had provided a service that was part of an Ansett Holidays Package and had not received payment were eligible for funding.⁶

- *Holiday Incentive Program* — \$5 million was allocated in 2001-02 to encourage Australians to take a domestic holiday. The program offered a rebate of \$150 for eligible domestic travellers and was administered by AusIndustry through licensed travel agents.

Government measures to assist the airline industry itself, in the aftermath of the Ansett collapse, will also have affected tourism. On the one hand, it will have benefited from the government assistance provided to keep Ansett and its regional affiliates flying after its initial collapse. On the other hand, the ‘Ansett ticket levy’ imposed on domestic flights increased ticket prices and may have reduced air travel by tourists within Australia (see section 4.7 below).

The Government also announced several new initiatives in 2001-02 to enhance tourism infrastructure in regional areas:

- *Cairns Foreshore Promenade Development* — \$9 million is to be allocated over 4 years to provide a foreshore precinct, including an environmental centre, a heritage centre and a ‘Pacific Rim forum’;
- *Stockman’s Hall of Fame* — \$4 million provided to 2002-03;
- *Fishing Hall of Fame* — \$3 million allocated to 2004-05;
- *Tasmanian Regional Tourism Infrastructure Package* — \$1.4 million allocated to 2004-05 to add to regional Tasmania’s range of tourist attractions; and
- *Back of Bourke Exhibition* — \$1 million allocated to 2002-03.

4.7 Airlines

Background

Prior to 1990, Australia maintained a highly regulated airline industry. There were two domestic carriers — the government-owned Australian Airlines and the privately-owned Ansett. Qantas, the one designated international carrier, was also owned by the Government, as were the major airports. Qantas served a limited number of domestic trunk routes as part of its international services.

⁶ The Commission understand that, in the event, only \$3.2 million in assistance was required by this target group, and the Government subsequently allocated \$1 million of the under-subscribed funding for tourism initiatives in regions affected by the NSW bushfires

In October 1990, the Government deregulated the domestic aviation market allowing the incumbents to determine capacity, fare levels and route structures. New airlines were permitted to enter the domestic market, although foreign ownership restrictions were retained and Qantas was restricted from expanding further into the domestic market.

Later in the same year, Compass Airlines entered the domestic market but the venture failed within 12 months. A second venture — Compass II — failed 18 months later. The Trade Practices Commission concluded that, aside from the competitive responses of the two incumbents, the most significant factor contributing to the failure of the Compass ventures was shortcomings in the companies' entry strategy and management (Lazar 2001).⁷

By the end of the 1990s, the aviation landscape had changed considerably:

- Qantas was privatised in 1993 and acquired Australian Airlines in 1994.
- The Australian Government removed Qantas's rights to be the sole international operator from Australia in 1992 and, subsequently, Ansett was designated Australia's second carrier for service on international routes.
- In June 1999, after Government changes to Foreign Investment Review Board (FIRB) rules that allowed foreign-owned airlines to operate domestic-only air services, Air New Zealand acquired 100 per cent of Ansett.
- The change in the FIRB rules also allowed Virgin Blue to enter the domestic market and, in 2000, both Virgin Blue and Impulse Airlines (a regional operator) announced plans to begin operations with modern aircraft and lower cost bases.
- The privatisation of the national airports made it easier for these new entrants to gain access to terminal facilities and gates. In addition, the internet became a viable distribution channel and an attractive, lower cost alternative to travel agencies.
- Average annual growth in scheduled passenger movements for domestic travel in Australia between 1990-91 and 2000-01 was 8.2 per cent. The availability of discounted fares and sophisticated booking systems contributed to this growth in passenger movements (DOTRS 2002).

Although Impulse Airlines has been subsumed by Qantas, Virgin Blue has been able to make significant inroads in the market, due in part to cost advantages over its more established rivals.

⁷ Other reasons noted by the Trade Practices Commission were the impact of recession in Australia, excess capacity in the Australian airline market, and difficulties in gaining terminal space and gates (Lazar 2001).

Against a background of intense competition, in April 2001 Ansett's fleet of Boeing 767 aircraft was grounded by the Civil Aviation Safety Authority because of non-compliance with certain safety directives. This placed further pressure on Ansett's patronage and financial viability and, on 12 September, the airline was placed under voluntary administration, with its flights scaled back and subsequently terminated.

Assistance measures

Australian governments have provided a range of assistance to Australian airlines in recent years.

In 1999, the Queensland Government provided largely undisclosed incentives to entice Virgin Blue to locate its headquarters in Brisbane, including tax concessions worth several million dollars. More recently, the Government has assisted Virgin Airlines to build an aircraft maintenance and training facility in Brisbane (Beattie 2002b). Similarly, though on a smaller scale, the ACT Government provided \$8 million to attract Impulse Airlines to base its operations in Canberra (ACT Government 2000).

Following Ansett's collapse, the Commonwealth Government imposed an Air Passenger Ticket Levy (the 'Ansett ticket levy') on all tickets for scheduled passenger flights originating in Australia from 1 October 2001. The levy is to fund a government guarantee to pay Ansett employee entitlements, pending attempts to recover entitlements from Air New Zealand and/or the proceeds of liquidation of Ansett assets.⁸ The Commonwealth also provided a \$195 million loan advance to cover voluntary redundancies, to be recouped at a later date from funds owed to Ansett by Air New Zealand.

Commonwealth and State governments also subsidised Ansett's regional subsidiaries under the Rapid Route Recovery Scheme. The scheme was designed to provide short-term transitional support to restore air services to regional communities affected by the Ansett collapse. Funds were provided by way of grants or loans, and a total of 18 air service operators have been assisted under the scheme. In 2001-02, \$18 million was expended, with a further \$5 million committed for 2002-03.

Major recipients included:

- *Skywest* — a \$2.5 million loan;
- *Hazelton* — \$3 million; and
- *Kendall Airlines* — \$3.5 million.

⁸ To avoid further impeding small, regional airlines, the \$10 levy was exempted for planes with fewer than 16 seats.

Other assistance measures included a Commonwealth agreement to underwrite tickets sold on Ansett Mark II, up to the value of \$25 million, until 31 January 2001. The Commonwealth also agreed to underwrite the resumption of Ansett services to Adelaide and Hobart at an estimated cost of \$150 000 per week.

More generally, all airlines have benefited from recent changes in accelerated depreciation provisions. The Commonwealth has legislated statutory caps on the 'effective life' of aircraft which has increased the assistance effect of the provisions (see section 5.1). The general measures to enhance tourism (as discussed in section 4.6) are also expected to benefit the airline industry.

4.8 Ethanol

Ethanol is an alcohol based fuel produced primarily from the fermentation of sugar derived from grain starches or sugar crops. Domestic production of ethanol is currently around 50 million litres per year. Ethanol can be blended with petrol and used as fuel in motor vehicles. Ethanol used in petrol has traditionally not been subject to the petrol fuel excise (38.143 cents per litre).

In recent years, the Commonwealth has provided assistance from the Greenhouse Gas Abatement (GGA) program to a number of ethanol-based projects. For example, in April 2001, the BP oil company was granted funding of \$8.8 million to trial ethanol-blended fuel and to provide infrastructure for the receipt, storage, blending and distribution of ethanol, while the Mossman sugar mill was granted \$7.4 million for an ethanol production facility.

In May 2002, the Commonwealth commissioned a two-year study to address market barriers to the increased use of biofuels in transport. The study is to develop a broad strategy to increase biofuel production to 350 million litres per annum by 2010. It will also conduct vehicle testing and a technical assessment of a 20 per cent ethanol-blended fuel in motor vehicles. This testing is partly in response to concerns raised by some vehicle manufacturers and other stakeholders that higher blends of ethanol may increase the risk of operational and mechanical problems (Truss and Kemp 2002).⁹

In September 2002, the Commonwealth announced that it would provide a production subsidy for ethanol produced in Australia. The new arrangements involve extending the excise on petrol to both domestically-produced and imported

⁹ Preliminary findings, released in December 2002, indicate that vehicle operability may deteriorate with 20 per cent ethanol-blends, although the impact on engine and fuel system durability is at present unclear (EA 2002).

ethanol. The excise paid by domestic producers of ethanol is then fully rebated in the form of the production subsidy, which mean that only imports bear the cost of the excise. The subsidy, which took effect in September 2002, is expected to last for about 12 months and cost around \$20 million.

Longer term issues regarding the use of biofuels in Australia, such as mandating a minimum ethanol content in petrol, are currently being considered by the Government. The Government has noted that:

This short-term production subsidy will provide a targeted means of maintaining the use of biofuels in transport in Australia, while longer term arrangements are considered by the government regarding the future of the emerging renewable energy industry (Howard 2002e).