TRANSCRIPT
OF PROCEEDINGS

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PRODUCTIVITY COMMISSION

REVIEW OF AUSTRALIA'S GENERAL TARIFF ARRANGEMENTS

MR M.C. WOODS, Commissioner

TRANSCRIPT OF PROCEEDINGS

AT SYDNEY ON THURSDAY, 27 JANUARY 2000, AT 9.02 AM

Continued from 21/1/00 in Canberra

MR WOODS: Good morning, and welcome to the resumption of the public hearings for the Productivity Commission's Review of Australia's General Tariff Arrangements. My name is Michael Woods and I'm a commissioner for the inquiry.

The purpose of the hearings is to give interested parties the opportunity to discuss their views and their submissions on the public record. This will help us in assessing the costs and benefits to Australian consumers, industries and their employees and the general community of a reduction of all general tariff rates under review.

We will be releasing a draft report for public consideration in May and a further round of public hearings will be held after people have had time to examine that report. Reactions to the report will be taken into account in the preparation of a final report which we are due to deliver to government in late July. Copies of the draft and final reports will be circulated to all those who have made submissions, appeared at the inquiry, and otherwise expressed an interest.

A transcript of hearings is made to provide a record of discussions. Transcripts and non-confidential submissions to the inquiry are public documents and can be viewed at the commission's offices; also at public libraries in capital cities or purchased, and order forms are available today. Alternatively, submissions and transcripts can be viewed on and downloaded from our Web site.

Our first witness today is from Mayne Logistics E.A. Rocke. Could you please state your name and the capacity in which you are presenting evidence today.

MR DAVEY: My name is Colin Hugh Davey. I'm a tariff consultant with Mayne Logistics E.A Rocke. I have presented a submission of my own dealing with certain aspects of the inquiry and would like to address that as well as speak on behalf of one of our major clients, Volvo Truck Australia, on the potential impact of a review on their situation.

MR WOODS: Thank you, Mr Davey. Would you like to speak briefly to your submission?

MR DAVEY: Yes, thank you. Firstly, I would like to thank the commission for the opportunity to provide information on these specific aspects of the inquiry. In my role as a customs consultant the terms of the inquiry raise two major issues for me and for our clients which will almost certainly impact upon certain categories of the importing community. The two issues I speak of are (a) the possible abolition of the policy by-law system, and I interpret the policy by-law system as covering items 45, 46 and 56. That's equipment for resource processing, etcetera.

The second issue is the effect of the total general tariff reduction on those industries that currently survive because of special duty-free concessions in respect of their imports, and it's in respect of category B that I address the one issue in relation to Volvo Truck Australia.

Under item A, the policy by-law, the major groups which will be affected by any abolition of the policy by-laws are naturally the major project proponents. I understand the overall intention and the impact that a general tariff reduction would have. There are a lot of duty-free tariff items and a reduction from the current 5 per cent to 3 per cent would no doubt bring in an average duty rate on imports of considerably below three, and probably in the vicinity of one or one and a half.

However, in dealing with the projects that I have been involved in in the last five to six years, even a duty impost of one and a half would be significant, and from experience I believe that the majority of the equipment imported by these projects would be more likely to attract the reduced duty rate rather than come out with the average, or be eligible for duty-free tariff items. I have only been able to find one or two major duty-free tariff items for significant pieces of equipment in projects, which means that in all past projects the normal duty that would apply would have been the general rate, currently the 5 per cent.

It must also be taken into account that when the major project people assess duty on their imports they don't look at the general rate of five. They are well aware of the current tariff concession system, and if the goods are not available from the local manufacturer there is the opportunity to reduce that 5 per cent to 3 per cent. So when calculating duty impost on a major project situation they invariably look at something either at round about 3 per cent or maybe 3.5 to take into account some of the items that may attract five. They could get some equipment which is not eligible for tariff concession on which they have to pay the higher rate. But they certainly in the past - in my experience they haven't allowed a 4 or 5 per cent duty impost as being the amount they would attract if they went ahead with the project in Australia.

I also know that on two occasions - I've been involved with seven projects and I know on two the duty element was a big consideration. I won't say the only consideration because that would be totally wrong, but it was certainly a big consideration as to whether or not those projects did proceed in Australia.

Under item B the commission would be aware that I've been authorised by the Volvo Truck Australia factory at Wacol in Brisbane to make comment and to seek clarification on the extent of the commission inquiry in respect of their particular situation. Volvo currently have the ability to import truck components under what is termed the original equipment by-law, being item 41B in schedule 4 of the customs tariff. This allows them to bring the majority of their imports in duty-free, provided they use them to assemble original equipment trucks in Australia.

There are some exclusions to the 41B by-law which attract 5 per cent, but on a value of componentry worth approximately 100,000 Volvo would normally pay some hundreds of dollars in import duty. We do the drawbacks for Volvo and drawbacks average between 3 and 4 hundred dollars per truck. So the amount of duty that is collected is very small, and hence if the general rate reduced from 5 to say 3 per cent, once again the amount of saving that Volvo would get as a result of that general tariff reduction would be almost negligible.

Their concern is, as opposed to that, there are competitors who are the completely built-up unit importers who have been required to pay duty at the general rate for many years which is progressively reduced, and Volvo have had to adjust to take into account that reduction. A reduction of say 2 per cent from five in the general rate to possibly three would see these people save several thousand dollars on an imported unit.

As I have been instructed by Volvo, the margin of that several thousand dollars could be significant enough to mean a closure of the Wacol factory. They have undergone a very stringent cost-cutting program over the last few years to survive. They don't believe that they could survive much more.

I understand that my two issues are only a very small part of the inquiry. I have been fortunate enough to have attended overseas and international conferences on tariffs where the people from the World Trade Organisation have put forward their views. I understand the way that many countries around the world are looking at tariff reductions. I do believe that Australia is a step ahead of most countries in their tariff reductions, and my personal opinion, as I stated in my submission, I think a further tariff reduction in this point in time - I don't believe that is the way to go, but that's my personal opinion and there are a lot of things to be discussed at the commission that no doubt you people will consider.

MR WOODS: Thank you very much. In terms of the specifics such as the 41B issue we take Volvo's concerns on board and we will look closely at the submission and its dealing on that matter.

If I could turn particularly to your experience in this industry though and to draw on that to assist the commission in its broader considerations. You just then reiterated a point made in your submission about retaining the current status quo in respect of duty rates at this point in time. How would you align a further reduction in our general tariff rate with reductions in rates by those of our trading partners? Would you attempt to do it on some form of country-by-country basis, in which case are you possibly breaching the most favoured nation status principle? Would you try and do it on a industry basis? Would you look to forming some view about average tariffs across our trading partners and when they've got to a next lowest point that we can reduce further? I mean, I don't understand the implementation of the process. I understand the principle of reciprocity that you're discussing, but I can't easily envisage how that would work in practice.

MR DAVEY: Yes, it's very difficult, and I don't claim to be an expert in these matters. There's a lot of other people who would have greater experience in trade negotiations and where we're heading on a worldwide basis. From a consultant's perspective and from an industry perspective, speaking with the people in this particular industry, you get the general impression that Australia seems to be a couple of paces ahead of the other countries in its program to reduce tariffs and achieve a free trade situation.

You hear the comments about the recent lamb situation in America, and the question was asked of me if the USA is a member of the World Trade Organisation isn't it one of the rules of the World Trade Organisation that you can't increase tariffs, and if so, how can a country increase tariffs? It seems that other countries do protect specific industries. They do either bend the rules or step outside the rules. There doesn't seem to be anything which can stop them from doing that apart from diplomatic negotiations, and on that level I have never been party to it. But I do believe that one of the points you raised, the possibility that before we move into the next phase of reduction we look at how far down our trading partners have come, and maybe take that into consideration before implementing the next stage - that may be one way of looking at it.

Also industry-specific - you know, as I've just pointed out with Volvo, there are industries that general tariff reductions can impact upon in their opinion quite dramatically, but at the same time I've been around long enough to know if you start getting industry-specific you start creating a monster which is very difficult to administer. So yes, it's a difficult question. I don't know what would be the best way, but we do seem to be a little bit out of step and in front of most other countries.

MR WOODS: I guess the next consideration in that issue then is are there any benefits to Australia in terms of businesses using imported inputs - and Australian consumers - from the program of tariff reduction that we've had to date, and do you have any views on that?

MR DAVEY: Certainly the tariff reductions which have applied to many sectors of the business inputs - I believe over the years without them there would have been many more industries unable to survive. You go from one extreme situation to the other - the huge tariffs that were and still are on textile, clothing and footwear. To my mind certainly the tariff reductions in that area have brought about reform. There have been some casualties, but there have also been a lot of companies that have risen to the occasion and have imported state-of-the-art equipment, have changed their procedures and have survived and become more competitive. Whether they can continue to be competitive in a world market with our high labour costs here in Australia by further reductions in tariff remains to be seen. Once again, I think the further reductions in tariff will see a combination of some companies surviving - they will adapt and they will become more competitive - and others will go to the wall.

MR WOODS: Does that increased competitiveness have spillover benefits to other industries in the Australian economy and to consumers?

MR DAVEY: It certainly would have benefits to certain sectors, yes.

MR WOODS: So I guess the question before us is: is that next and last 5 per cent the most crucial point in the process of reform or is it a continuation of the reform?

MR DAVEY: I think, as you say, it's the last major step. From thereon in there will certainly be other factors that manufacturers in Australia will have to address. You know, there's more and more emphasis these days on the community protection aspects of making sure that the safety requirements are met and they don't contravene the commerce infringements and trade practices and all this sort of thing. But yes, I do think that the final 5 per cent - in reading the issues paper I got the impression that what is probably the preferred option - or the fact that a preferred option will be put through, and in reading between the lines I came to the assumption that a possible reduction of maybe 2 per cent might be the preferred option, but from your comments about the final reduction of five I take it that you're looking at the possibility of total abolition of tariff.

MR WOODS: At this stage we're collecting information and don't have a preferred view, but I'm just exploring options which include a phased reduction or a one-off reduction to zero or maintenance of the status quo. I mean, they're all within your - - -

MR DAVEY: I think a one-off reduction to zero would only increase the concerns that I've expressed with a lot of industries here. There are those industries and certainly they're getting less and less, but there are other industries that would rely heavily on the tariff concession. Even the 3 per cent would be a crucial factor in their production here in Australia, and the abolition of that three to a total duty-free does bring into play those two things that I have said: (1) it makes it much more difficult, and (2) the competitors who are not paying duty on other products have that added advantage.

MR WOODS: Thank you. In terms of some data that might assist us in understanding the implication of some of the schemes, you mention under the item 50 heading on page 2 of the Mayne Logistics E.A. Rocke submission the high monetary cost of preparing, pursuing and administering individual item 50 applications, and then you refer to that more specifically a little further on in your submission. Is there information that you can put before this inquiry either today or in subsequent follow-up correspondence that would help us understand the magnitude of the administrative costs involved?

MR DAVEY: Well, taking an actual tariff concession and an application as to how you approach it - and okay, I speak now as if I was an importer. I want to import a piece of equipment and from my knowledge of the local Australian industry I don't believe I can purchase that piece of equipment from locally produced - here in Australia. I would then have to take into consideration - and bearing in mind that there is only a 2 per cent duty saving on most instances from the general tariff. That's assuming that the goods would attract five - there's only a 2 per cent duty saving under the general tariff. Naturally anything short of $100,000 in value, which would give you a couple of thousand dollars rebate, is not even worth looking at.

As a matter of fact, the 100,000 is probably the very very bottom line. Most companies would look at maybe 500,000 as what they would have to import and pay -

the value of the actual piece of equipment - before they would consider tariff concession.

MR WOODS: That's a figure drawn from your experience as being a useful criteria?

MR DAVEY: Yes, I recommend to our clients to actually lodge and process a tariff concession - the amount of time - and by the time you research and you do what is required under the system, unless you're getting back in excess of $2000 you're not going to get much for your return and you run the risk that you could spend several thousand dollars and achieve nothing because the tariff concession is refused. So it's got to be worth the effort.

MR WOODS: That's been helpful. Thank you.

MR DAVEY: You are then required to research the extent of the local manufacturer capability which is difficult at times. There are some publications, but it is difficult, and Bob would understand the processes in this. Having researched that you then have to prepare your application. The wording of the application is very important because customs require a wording which is not product-specific, it's to be generic, but if you go to generic you run into a situation where you describe it in a way that people do not appreciate the magnitude of the range that the equipment is needed to encompass, and therefore you get a lot of objectors who would throw up their hands saying they can supply, only to realise afterwards and acknowledge that had they been told and had a certain range of specifications they couldn't have met those specifications. So it's a bit of a task to be generic in your description and at the same time not be product-specific.

Having lodged that then the application does get gazetted. I'm not sure if you're aware of the process, but the local manufacturers have 50 days in which to raise objections, and then if the application is accepted it is approved and you can utilise it in importation. In the majority of instances - or I suppose not the majority, but in a number of instances during that period you will get objections from local manufacturers which requires you going back to address them specifically to determine the extent of their capabilities and manufacture to try and negotiate a change of wording which still gives you the tariff concession but doesn't cut across their range of goods.

Added to that the actual system itself is very interpretative, and on numerous occasions cases are taken to the AAT. So if customs refuse it and the client is not prepared to accept that substitutable goods are able to be produced in the normal course of business by the local manufacturer then they will take the case, if there's enough involved, to the AAT. So it causes a lot of work both for customs and for the importers. In my opinion we have addressed a lot of other risk assessment areas in different ways. I believe if people sat round the table and looked at it and there was an industry meeting with various government departments I'm sure we could come up with a simpler way of administering the tariff concession system.

MR WOODS: If one of your clients was so prepared to put before us a case history of an example of preparing a tariff concession request indicating the sorts of costs that were involved from their side, including, no doubt, consultancies and other things, that would be most helpful to us too.

MR DAVEY: Certainly there are several clients that I can approach. They will probably request me to do all the preparatory work.

MR WOODS: I'll leave that between you and them.

MR DAVEY: But yes, I'm pretty sure I could put that before the commission.

MR WOODS: That would be most helpful. One option that you referred to would be to switch the onus of proof from the importer to local manufacturers which strikes me as similar to a scheme that applied back in the early 90s.

MR DAVEY: Yes.

MR WOODS: I think the outcome of a review at that point was to the effect that local manufacturers were undergoing considerable cost to demonstrate their capacity, but only one of them would have the opportunity to recoup if in fact they were successful in winning the order, or none of them would recoup if the order still continued to be placed overseas. Do you have any comment on why you would prefer to see that system in effect reinstated versus the importer bearing the cost?

MR DAVEY: Yes. Quite frankly, in my opinion, Mike, I would prefer to see the tariff concession go completely. I think it is too interpretative, and a reduction in duty from five to three would see the abolition of it and it would obviate all these problems. If, however, a tariff concession did remain, yes, in the case of the cost of the local manufacturer versus the importer - over the years the changes that have been brought in - and you are correct when you say that years ago the local manufacturers - there were many issues they had to address in raising objections, etcetera, and there is only one person who can win the contract, and to be perfectly honest, I think in probably greater than 50 per cent of instances when tariff concessions are applied for the goods are basically not so much ordered, but it's in the importer's mind that he doesn't believe he can get them in Australia anyway, and he's going to go overseas. He's got to reach that conclusion before he lodges it anyway, because, you know, he's not going to lodge it just as a flier to see if he can get a couple of per cent duty savings.

So yes, there's very little chance of the local manufacturer getting in on the act. It's a matter of proving that he can't make it, and at this point in time the way the system is set up, as I said in my submission, you actually do the research, and these days there is only one organisation which is accepted by the government and customs as the organisation who is prescribed under the act, and that is the Industrial Supplies Office.

To utilise the services of the Industrial Supplies Office - if you are utilising their services in a project and you approach them long before any goods are ordered overseas you can obtain the services either free of cost or at a negotiated price which is reasonable. If you utilise the services of the ISO in which to research a particular submission and after the goods have been ordered or committed overseas, then you are going to have to pay a fee, and the fee is normally quite considerable - several thousands of dollars - more than the actual cost of lodging an application in many instances to actually obtain confirmation as to the capability of local manufacturers.

Having done all that and having paid that money up-front I have to tell the importers that even though they've sent all this money and the ISO may have come back and said they do not believe there is a local manufacturer, it gets gazetted, and any one of a dozen other local manufacturers can then throw up their hands and you have the added process of having to go through the steps of refining the application or withdrawing it or whatever because of these local manufacturer capabilities.

Now, I just feel that the two steps that have to be faced - local manufacturers I believe have come a long way from the times when the old system was in. Most local manufacturers in those days didn't subscribe to the Commonwealth Gazette, they didn't read them, they didn't pay a great deal of attention to imported goods unless they were contacted by somebody who was going to bring them in.

I have a number of companies these days that are importers - sorry, local manufacturers in Australia - who request me to scan the gazettes for them and keep them apprised of any equipment that they think they may be able to produce in their own factory. There are two reasons: one may be to raise objections on tariff concessions and a second reason, and just as valid, is to monitor the trend and see where people are going and what equipment is required and, if necessary, adapt to that equipment. Maybe they can't make it for this time and they won't object, but they certainly will look at if they have the capability to make it the next time.

So I think local manufacturers are more aware these days of what is required, and I don't know whether or not reverting to the old system would be as dramatic as what it was in the old days or whether they would be able to cope with it a little bit more. My idea of that, as I say, is it was only because of the fact that if the tariff concession system is retained then maybe that should be looked at as a possibility and spread the costs a little bit more.

MR WOODS: Yes, I understand. You do make several comments about the Industrial Supplies Office system and the fact that they are involved at both stages of the process, at both the search stage, and if so requested, also at the second stage.

MR DAVEY: Yes.

MR WOODS: We have drawn your submission to the attention of ISONET and have asked them for their reaction, and should they do so, of course, that would be available as public evidence, and you may wish to comment further. But apart from the issue of local manufacturers taking some of that onus of proof on, do you have a suggestion as to the alternative of ISONET or the ISO network being involved in the second stage of the process?

MR DAVEY: I think when you get to the second stage - and I take it we're referring to once we get past item 50, which is substitutable goods, and getting into item 45 which is more specific goods.

MR WOODS: Yes, item 45.

MR DAVEY: It is my understanding currently, and I believe that there were meetings last week with ISO and some other organisations to determine or maybe not to determine - I didn't get the full context of what the meetings were on but I got the impression that they were going to look at where they go once they get beyond item 50. I believe ISO certainly have a role to play in the item 50. They have a database which gives information on local manufacturer capability. They have experience in companies, knowledge of companies that have been involved in these industries, and they can certainly provide a lot of information on substitutable goods.

The definition of substitutable goods is a little bit interpretive but I believe that the way it is interpreted by ISO and customs - we don't have a great deal of problem with that. When we come down to more specific goods in relation to projects, I've been told by two of the state organisations of ISO that they will not involve themselves in item 45 assessments on specific goods. They prefer to have that done by an independent assessment. I think that this is probably one of the aspects which is currently being discussed as to whether or not ISO will remain in the area of giving assessments on item 45 applications or whether that will be sort of subcontracted out and addressed in another way.

My experience with the item 45 projects is that it requires somebody to actually take a look at the total overall project and, if I could use an example here, we had some filter presses for the Sun Metals zinc refinery. The filter presses that were required had to do a specific task in line with new technology in the electro-winning of zinc. There are certainly companies that claim to be a manufacturer of filter presses here in Australia but they use a different process. The process they use is not conducive to the latest technology in electro-winning. However, under the terms of the customs sections of the act and things like, they could very easily lose their case and it could be maintained that substitutable goods are produced in Australia, even though those goods cannot do the exact job that they require.

I understand that in the terms of item 50 on substitutable. It doesn't sit well in the terms of item 45, where it was always my understanding that the more specific goods, you had a case to argue that these were not available from local manufacture, and that's where I believe the grey areas come in with ISO. But I do think that that will probably be resolved internally in the near future.

MR WOODS: Is some of the difficulty in being able to accurately specify the nature of the process that the goods must be able to undertake or is it more related to customs taking a slightly more generic perspective on what the process is?

MR DAVEY: I think customs are obliged to take a more generic view of the process because of the way in which the act is worded and because of the wordings of the policy by-law or the item 45 by-law. I certainly believe, sitting on the other side of the fence, that yes, the actual processes and what is required to achieve that process - bearing in mind that all of these major projects - I haven't struck a major project yet that has been set up in Australia that has been anything less than state-of-the-art. If they're going to be world competitive, they've got to be right up there at the top of the tree. They've got to have the latest in technology.

You put yourself in the project proponent's position. They are developing a process here in Australia and building a plant. They require the latest in technology. They've sourced the world to find out from either their own experience or from outside sources what type of equipment will do the job best. They've probably - maybe not as in-depth as customs and local manufacturers would like, but they've also assessed the local manufacture market to a degree. They've found companies that have produced either exactly what they want or something so close to it that they are comfortable with it.

To then expect them to turn around and to place an order on a company in Australia who has maybe made something which is nowhere near as close to what the overseas company can do or that they know that they produce a product, but, as in the case of the filter presses, it doesn't work on the principle that is required, which doesn't extract enough water from the product so therefore that's going to impact upon their processes further down the line, I think this is where the greater communication between ISR, the importer, the broker, is required to be taken into account and that the delegate should then have a degree of discretion that, having familiarised himself with all of the processes which are required and the fact that this is something which is state-of-the-art and if he's satisfied that the local product won't fit the bill, then make the decision from there.

In our current situation I don't think we go that far. The delegate certainly spends time, and you put your case to him but I think that there are situations where it could be further developed and it could be taken a bit further.

MR WOODS: Your description - and very complete, and I thank you - suggests an added expense in the process. Would that be reasonable to conclude, that the more detailed and the greater the time of the delegate in understanding the requirements, etcetera, does involve further time and expense?

MR DAVEY: Certainly. In the one that I'm currently dealing with now, if we proceed with an AAT hearing, the client has recognised the fact that not only will he have to spend a great deal of his own time and his own engineer's time to put together all of the technical information to prove that the system or the process is beyond the scope of the local capabilities, he also under the system will probably have to obtain an independent assessment and in some of these areas getting an independent expert is very difficult because we're dealing here with projects which are probably utilising a process that is used very minimally around the world, so therefore they have to obtain an independent assessment if they want to enhance their case, and to get something like that you're looking at tens of thousands of dollars in some instances.

MR WOODS: For a potential saving of 2 per cent or up to five if it's a major project?

MR DAVEY: Well, in our case - no, five if it's a major project.

MR WOODS: Five if it's a major project.

MR DAVEY: Yes. Three if it's already been granted item 50 but five if it's - - -

MR WOODS: Five for a major project - - -

MR DAVEY: Yes.

MR WOODS: - - - which could be a saving in that particular case in the order of how much?

MR DAVEY: Well, the one I'm dealing with now, $120,000 was paid in customs duty. They estimate that it will cost - if they win the case, it will cost something around about 50 or 60 or maybe more to get it back.

MR WOODS: So they would be recovering again 60,000 or so.

MR DAVEY: $60,000, maybe 50 per cent. Those figures naturally would vary from case to case, depending - - -

MR WOODS: Absolutely, but it's still useful, and if you feel that that's an illustrative case - - -

MR DAVEY: Well, it's the most current one that I'm involved in and I know the figures and I know they're reasonably accurate. No doubt if there was a quarter of a million or a half a million dollars involved, then obviously the return, if the case is successful, is going to be much greater because the legal costs and the independent assessment costs will probably be much the same as they are in something like this, maybe a bit more, but yes, certainly a considerable cost to pursue these things.

MR WOODS: That's very helpful to us to understand those magnitudes. Are there any further matters that you wish to put to us, either on behalf of the Mayne Logistics E.A. Rocke submission or the Volvo Truck Australia Pty Ltd submission?

MR DAVEY: No, only in relation to Volvo, Mike, I would like to very much be able to see something which tells us just how far the inquiry is likely to go, particularly in Volvo's case in relation to those schedule 4 by-laws. I shouldn't use the word "by-laws" - schedule 4 concessions, the ones that are not policy by-laws, but do - - -

MR WOODS: Yes, such as the 41B in particular.

MR DAVEY: Yes, 41B and things like that. If they - - -

MR WOODS: I guess somebody will respond on that.

MR DAVEY: Yes. If they're not to be affected, well, then, one of Volvo's concerns is obviated. If they are to be affected, well, then, we have to look at maybe putting in a little bit more information.

MR WOODS: Thank you very much.

MR DAVEY: Thank you for your time.

MR WOODS: I appreciate that.

MR WOODS: Our next witness is from Atom Industries, if you could attend the table, please. Could you please state your name and the capacity in which you are presenting evidence today.

MR NOTARAS: John Arthur Notaras. I'm general manager of Atom Industries.

MR WOODS: Thank you very much. We have received your submission and thank you for providing it to us in such a timely manner. Would you like to present to the commission an overview of the key points that you wish to raise?

MR NOTARAS: Yes, I would. We've been manufacturing for quite some time in Australia and we currently manufacture lawn edgers, powered lawn edgers, and I'd like to say the world's best lawn edgers. They've been patented by us, they're fully manufactured by us. Everything is manufactured in Australia except the engine. The engine is not made in Australia, it's not available from Australia, and has to be imported. By coincidence, or irony, I suppose, we were the only manufacturer back in the 70s to manufacture a lightweight engine in Australia, but with the tariff changes, etcetera, that was phased out.

We currently import this engine or several engines of the small range of 31 and 34 cc. When we started manufacturing the lawn edger a few years back, the engines came in duty-free. We had a TCO number for two types of engines that we imported. Then the government slapped on the tariff, which we don't mind paying, providing everyone else does. It just so happens that the lawn edger that we're manufacturing is under the same tariff classification of many other devices that compete against us that come into Australia totally duty-free, using the same engines.

Now, not only do we have to pay the import duty but we have to pay also the sales tax component on top of that, we have to bear the extra interest charges and all the other add-on costs, so it accelerates or brings up the penalty that we're paying from 3 per cent to 5 per cent. Now, this gives the overseas manufacturer an unfair advantage against we Australian manufacturers. They in effect are being subsidised because they are not paying these extra taxes and because they have a monetary advantage they are being subsidised.

Now, why our government discriminates against we Australian manufacturers I'll never know. Anybody and everybody that we speak to outside of the bureaucracy says it is absurd, and it is absurd. Business sense dictates that we should manufacture for example in the USA and import the goods duty-free, but what good is this for Australia? We are loyal Australians and we'd like to see the industry maintained here. We're world-class manufacturers, second to none. We already export to the USA, we export to Europe and our other products we also export to many many countries worldwide, but we are just not given a fair go by our own government, and this is absolutely ridiculous, to say the least.

We want to achieve economies of scale by increasing our sales locally, increasing our production, putting on more staff, training more people so we can take part in this globalisation process. Our product is unique. We have a tremendous potential, particularly in the USA - overseas, but particularly in the USA - and everything can be made in Australia, except at the present time the engines which have to be imported. We cannot achieve economies of scale because of the discrimination against us, and I repeat that it is an absurd situation where the overseas manufacturer is subsidised against we Australian manufacturers.

It's almost like Bill Clinton saying, "Well, you Aussies, your lamb can come into USA duty-free, and I'm going to slap on an extra tax against the US lamb producers." Who would ever hear of an absurdity like that? All we want is a level playing field. We just want to be treated like anybody else. We're not asking for any handouts, we're not asking for tariff protection, we just want a fair go so we can participate, not only for the good of Australian manufacturing, but to also increase employment and increase skills that are required.

As said before, we use world's best practices in our manufacturing. We use CADCAM systems, our tooling and everything else is absolutely world-class, but we're being penalised by this discrimination. That's about all I have to say at this point of time, although I would like to add that we have written numerous letters to people in Canberra, the government in Canberra, the various departments - everything gets looped from one minister or another back to Office of Manufacturing, and we receive the same letters saying that we should contribute to the economy; all businesses have to participate. We don't disagree with that if all businesses do, but the imported product does not participate, and again I say it's an absurd situation and it's utter discrimination. Thank you.

MR WOODS: Thank you very much. Could I seek clarification on a couple of points.

MR NOTARAS: Sure.

MR WOODS: One is if you could indicate the value of the duty that you're paying.

MR NOTARAS: 3 per cent.

MR WOODS: Yes, in quantum terms compared to your total manufacturing costs, just to give - - -

MR NOTARAS: I wouldn't have that with me, sir. It's 3 per cent plus the add-on costs which bring it to about 5 per cent.

MR WOODS: It would be helpful just to understand whether we're talking in terms of total manufacturing costs. What proportion constitutes the duty?

MR NOTARAS: Obviously it's not very high because if it was too high we wouldn't be manufacturing and we'd shut down or transfer the manufacturing overseas. But it's the principle. It's the principle, it stinks, to use some words - - -

MR WOODS: You mentioned that you were manufacturing for both the domestic and the export markets. What sort of proportion of your production is devoted to exports?

MR NOTARAS: With the lawn edger at the present time it's probably about - well, last year it would have been about 15 to 20 per cent - probably 15 per cent - but this year it's going up substantially and it should increase if we're given a fair go to get economies of scale.

MR WOODS: Very good, and you were saying that was primarily to the US?

MR NOTARAS: That's the biggest and best market, yes. But nevertheless we have sold into Europe as well.

MR WOODS: And there are no comparable lightweight engine manufacturers left in Australia, are you saying?

MR NOTARAS: No, there's absolutely none. We are the only ones who have ever in the history of Australia manufactured a lightweight small engine. It was a 60 cc - and also a 75 cc - back in the 70s. The only engine currently being manufactured is by Victa. It's about 166 cc. It's extremely heavy, and it's totally unsuitable for the job. It's a good engine, but not for our job.

MR WOODS: Because here you're talking 31 or 34 cc, so it's a totally different scale.

MR NOTARAS: Correct, and the weight difference is completely different, yes.

MR WOODS: Thank you, that's very helpful. I don't have any further specific questions. I think your submission has been quite clear in identifying the issue that you're facing, and we're certainly wishing to take that on board in preparing our report. Are there any concluding comments that you would like to make?

MR NOTARAS: All we ask for is a fair go for Australia. That's all we're asking - for the manufacturers of Australia.

MR WOODS: Thank you very much.

MR NOTARAS: Thank you.

MR WOODS: We will take a short break and resume at 10.30.

MR WOODS: If I can resume the Sydney hearings, and the next witnesses are from the Broken Hill Proprietary Company Ltd. Could you please state your names and the capacity in which you are presenting evidence today.

MR MARJORIBANKS: Yes, I'm Andrew Marjoribanks and I'm the head of external affairs for the steel business of BHP.

MR LANDY: I'm Bernie Landy, vice-president marketing, BHP Steel.

MR McDONALD: I'm Ross McDonald. I'm manager government and investor relations, BHP Steel.

MR WOODS: Thank you, gentlemen. Do you wish to make comments on your submission which we have received and read?

MR LANDY: Yes, please, Mr Woods. Firstly, we would like to thank you for the opportunity to come and have another talk with you. This review is important to us because there are 255 steel items involved, and also indirect steel imports are covered - that is, steel containing manufactured products.

Just to summarise our position, which I guess is covered in the submission already made - but our position is that we believe that tariffs should reduce in line with the agreed timetable and in accordance with the APEC commitment to move to a zero tariff by 2010. We agree with that. We believe that if tariffs are reduced that should not occur without some offsetting trade benefit with other countries. We can go into that a little bit more in our commentary. We believe that the tariff concession scheme of 3 per cent on many business inputs where there is no local manufacturer or no substitute should be removed, and Manufacturing-in-Bond arrangements should be available to manufacturers who wish to participate while the tariff system continues. They're the four points of our position in summary.

Just to go on to perhaps elaborate on our position, BHP is a substantial exporter of steel to many countries. In many of those countries that we're exporting to there are tariffs in place in accordance with the summary that was attached to the back of the submission. In many cases those tariffs are quite a degree higher than the sorts of tariffs that we have here in Australia. So I guess we're saying that we believe that we don't have any problem with reducing tariffs, providing the same thing happens in our competitive markets, and that we have the so-called level playing field in those types of situations. I guess that's the case particularly in the Asia Pacific region which we see as the market which we most frequently compete in.

We also have the issue that the Australian steel industry is a major employer of people - 17,000 people - and many of those in regional locations such as Whyalla, Newcastle and Wollongong. We are, I guess, concerned that a further impost on our competitive position might have an impact on jobs - maybe indirectly, but it may have an impact. We believe that a further reduction of tariffs without some commensurate reduction in other countries in which we're competing will put added pressure on the

Australian steel industry but won't have a big impact on consumers due to the fact that steel is basically a raw material, and in typical manufactured goods steel doesn't represent a major component of the cost. So we doubt that if there is a reduction in tariffs the consumer will see any of that passed on.

The other aspect I think we would like to stress is that in recent years we've seen natural market forces occurring which have opened up the Australian market significantly. We've seen steel imports increase dramatically, which is also covered in the submission, Mr Woods. The average duty - if you look at the weighted average duty on steel products, the weighted average between developing countries which have a zero tariff entry to those which do have some sort of tariff, there's roughly a little over 3 per cent - 3.1 by our calculations. So we think that the steel industry basically is competing now globally with a fairly low tariff anyhow.

I suppose in conclusion before we enter into some discussion, our major point is that tariffs in our major Asian steel markets are well above the current rates in Australia, and I think before the Australian government moves to reduce tariffs in this country that we would like to see some commensurate reduction in the other markets to the match the tariff reductions that we make here. Our preference is that we would not like to see Australia lead the way unilaterally in major changes to tariffs.

MR WOODS: Thank you very much. Just to pick up your end comment of Australia leading the way, I take it from the table 1 appendix that the duties applying in Japan, the US and the European Union are all significantly lower than our tariffs. Am I reading that table correctly? They're in the order of 2 and up to 3 per cent compared to our price?

MR McDONALD: Yes, that's correct. One of the major points there is that we don't have a culture in Australia of relying on non-tariff barriers, whereas those countries do. Secondly, our tariff, our effective tariff, rate is not 5 per cent but 3.1 per cent. So that's pretty lineball with those developed countries.

MR WOODS: Okay, but it doesn't put us at leading the way in the sense of something that may be well produced - - -

MR LANDY: I guess the comment about leading the way is to go to zero.

MR WOODS: Yes.

MR LANDY: That's what I mean by "leading the way".

MR WOODS: That would lead the way on this table?

MR LANDY: Yes.

MR MARJORIBANKS: Yes, if there's another round of agreements on reduction of tariff then Australia would be part of that and would float down. But leading the way means doing it on our own unilaterally.

MR WOODS: And I would like to explore that in a moment, the sequences of that. But you do refer in our submission to the multilateral steel agreement, which I guess is what you're referring to in part in terms of collective floating down. Can you elaborate on what is the likelihood of such an agreement? You refer to it still being pursued under the OECD Steel Committee. Is there any sense of progress and timing?

MR MARJORIBANKS: First of all, the reason the multilateral steel agreement wasn't reached as part of the Uruguay Round, was because of difficulties raised largely by the United States in relation to the treatment of subsidies in the early history of state-controlled steel industry which was privatised. I mean, that was the big issue. It was said at the time, for instance, that when British Steel went public the government, in effect, wrote off 800 million pounds of debt when they nationalised. So the American contention was that that's a subsidy which has to be recognised.

The British Steel one wasn't the only one by any means, but that might just serve to illustrate the point. So people were in general agreement that there should be free trade in steel products around the world. I mean, that was not the issue. The issue was the mechanism for ensuring fair play, if you like, for fair trade, and the issues then related to subsidies and countervailing duties and dumping action and quotas and how that might all be treated and, in effect, those issues became too hard to be solved in the context of the Uruguay Round.

My understanding is that the multilateral steel agreement is essentially run in Geneva and the Australian government has certainly been a player in that. It's still extant, I think was the word I used; it's still alive. But the main debate is continuing, as I understand it, in the forums of the OECD Steel Committee, and if we are going to get an internationally cohesive agreement on steel tariffs it's probably going to come out of that arena. But it's still an issue which is being debated.

MR WOODS: But you don't see any short or even medium-term resolution of the issue?

MR MARJORIBANKS: No. I think colleagues in Canberra would also agree with that.

MR WOODS: Therefore, the only hard timetable at the moment is the APEC commitment?

MR MARJORIBANKS: Yes, that's right.

MR WOODS: If there was to be an agreement to an earlier date through this process, you would clearly sign it.

MR MARJORIBANKS: Clearly we've supported the multilateral steel agreement.

We've had a clear position on that. If the MSA was resurrected and if there was an agreed timetable which was quicker, but provided it was agreed with all the other steel manufacturers and steel-producing nations, clearly we would be party to that.

MR WOODS: Thank you very much. Reciprocity is one that you refer to, both in your overview and in the italicised conclusion on page 4 of your submission. Could you explain how you would implement that in practice? You talk about "looking for offsetting trade benefits" in one place. "Proportionate responses from other countries" is another phrase you use. In practice, are we talking about matching other countries' tariffs, in which case you're breaching the most favoured nation status arrangements? Are you talking about industry by industry? Are you looking to some form of average reduction across major trading partners that would trigger a further reduction by us? I'm not sure how I'd implement such a concept. I understand the principle behind it, but I don't know how it would look in practice.

MR MARJORIBANKS: My colleagues can comment in a minute. But when we wrote that, we had in mind something that looks a bit like a bilateral agreement. I mean where one country to whom we are exporting has got a tariff on our exports into that country and if Australia as a whole was going to see itself reducing its tariff for whatever goods are coming in here - be they steel or whatever - there's an opportunity for us to be a bit more competitive with our steel exports into that country. Now, a hypothetical country might have a tariff of 10 per cent on all steel products, and we've got a tariff of 5 per cent - well, notionally 3 per cent coming in here - it gets back to the basic argument, why should we unilaterally reduce our tariff from 5 per cent to zero without a benefit? The benefit might be a bilateral agreement for a reduction in tariff in some trading partner.

MR WOODS: That's assuming that there's no benefit to business inputs and to consumers from that process. We can explore that in a minute. There may be other benefits than just reciprocal reduction in tariffs coming from our own actions.

MR MARJORIBANKS: The benefit to business is that we then become able to export better and there are consequences for use of our capital and use of our labour.

MR WOODS: Yes, I understand the benefit to yourself. I was thinking of benefit to other users of your products as business inputs, who might benefit from a unilateral reduction. But we can explore that point in a - - -

MR MARJORIBANKS: That's a very important point that we want to come back to, because that relates to how we ourselves as a company support exporters using our product. So that's a point we want to make in due course.

MR WOODS: That would be helpful to pursue that.

MR LANDY: Mike, if I could just make another point.

MR WOODS: Yes.

MR LANDY: I think probably if there is an instrument there under the auspices of APEC that's designed to run its course, that is the preference. What we are proposing there on page 4 of our submission is really an alternative as input. It's not proposed as the preferred alternative, clearly. As stated in my opening comments, our preferred position is that it should reduce in the agreed timetable as designated under the APEC agreement.

MR WOODS: There arises the question of how important is a decision by Australia to offer a reduction of its general tariffs from 5 per cent to 3 per cent or zero or some other combination in terms of getting leverage from other nations, particularly when you also have players such as Japan, the US, the European Union in the total process of trade negotiations. If I can draw your attention to the submission from another company - and that submission is available through this process. It's from Monsanto who stated that:

> On the general issue of tariff reductions and their usefulness in multilateral trade negotiations, we believe any perceived leveraging opportunities from the 5 per cent level would be negligible. It's believed that around 80 per cent of Australia's imports already attract duties of 5 per cent or less, and at these levels the Australian market is generally perceived as highly accessible.

That's a counterview put to us, that Australia is generally seen as open anyway; that us offering up 5 per cent given our small proportion of total world trade really isn't a leverage that has much value in the international marketplace. Is that contrary to your perception?

MR LANDY: We've had a recent example - and I don't think we're here to say tariffs are the chief impact on our competitive position globally, but they are a factor.

MR WOODS: It would be helpful to examine that in a second.

MR LANDY: Okay. Recently we sought the tariff on tinplate reduced to zero and since then - and I repeat, it's not the major factor - we've seen imports of tinplate go up quite significantly, so that there is some evidence that there may be a link. It's not the total hard-wired link, but some - - -

MR WOODS: I understand that in terms of affecting your operations, but I don't see the connection particularly with us getting leverage in the international marketplace of offering up our residual 5 per cent.

MR MARJORIBANKS: I go back to my hypothetical case. If there is an ASEAN country that we're dealing with that can be persuaded to lower its tariff by whatever percentage as a result of us lowering ours from five to zero, then that makes our steel product going into that country, in competition with other exporters from other parts of the world into that country or into that region, just marginally more competitive.

MR WOODS: I understand that, but I'm just not quite sure as to whether us offering up our final 5 per cent is of sufficient weight to cause that nation to lower its tariffs which it's lowering to the world through an MFN process.

MR MARJORIBANKS: Frankly, it would seem to be better to try than to just simply accept or postulate that's not going to happen and carry on and reduce the tariffs anyway.

MR WOODS: I understand that, particularly should there be no cost of continuing with our tariffs. But if there is a cost to the economy generally through us continuing with our tariffs, then we're trading off the continuity of that cost versus a possible benefit from reciprocity, and that's one of the challenges that have been put to us in our terms of reference that we need to pursue very carefully.

MR MARJORIBANKS: The marginal argument cuts both ways. I mean if it's not significant going that way, it's not significant coming down the other side.

MR WOODS: Which is a point that Bernie raised particularly - and this might be the right time to come to it - that you said, in intent as I understand it, that you doubted whether a reduction in tariffs would likely be passed on as a price reduction to consumers. If that's the case, two questions come to mind. One is who would gain the benefit from the reduction in tariff? The second is that if there isn't any consequent price reduction, then why is a tariff necessary as a protection instrument if it doesn't give you price advantage?

MR LANDY: To answer your first question, Mike, I think it would probably be banked by the manufacturer. Ross, where was that table that showed the relative - there it is, in figure 3. If you have a look at washing machines, for example, there's $40 worth of steel in a $1000 washing machine. We just don't think that would get passed on to the consumer. It would be basically banked by the manufacturers, particularly given that there really is now in that particular segment basically one Australian manufacturer. So it may assist them in being more competitive, but I can't see that level of discount would be passed on.

MR WOODS: That's quite a helpful conclusion to reach. You discuss in your submission that you produce 6.3 million tonnes a year, of which over a third is exported. You don't identify the main countries to whom you export, although you talk about Asia or ASEAN generally. Can you elaborate on the target markets in particular?

MR LANDY: Yes. We're exporting to Japan, Korea, Taiwan, Thailand.

MR WOODS: Is that in any sense of order of priority or just collective?

MR LANDY: No. We're just coming off the Asian economic crisis, so there's been a bit of disruption to the way we've exported.

MR WOODS: Sure. I understand its impact.

MR LANDY: We've actually changed our mix more away from Asia, but prior to that our biggest export market was Korea. Indonesia was also significant at one time. The Philippines we participate in.

MR WOODS: And you mentioned Japan which has fairly low tariffs.

MR LANDY: Yes.

MR McDONALD: Prior to the Asian crisis BHP Steel's major export market was Asia, and that was totalling 70 per cent of exports. But that's been reduced and some diversification of markets subsequent to that.

MR WOODS: Sure. I understand that - which suggests to me that you're already world competitive if you're able to overcome their tariff barriers and still export significant amounts of your production into that area. I notice your reference to being one of the three lowest cost hot-roll strip producers in the world. It again raises the question then, how important is this tariff protection if you're already at that world competitive level?

MR MARJORIBANKS: We're at the world competitive level at that particular point of the product stream. There's no question that we've got a long way to go in improving competitivity downstream from the hot-roll point.

MR WOODS: So you're picking that point for that part of the production's process. What you're saying is then there's room for improvement.

MR MARJORIBANKS: The point we're making is that we are not sort of sitting naked behind a tariff wall, terrified that the thing's going to fall down. In the last 10 years we've spent an enormous amount of capital. More importantly, we've devoted an enormous amount of attention to our workforce, to the way our workforces behave and to changing culture, so that we are becoming very much more competitive. I put in there the example of how we've improved safety performance - - -

MR WOODS: Yes.

MR MARJORIBANKS: - - - which is absolutely at the core of a workforce's culture and its behavioural pattern as an illustration of how we're changing. So we're not in any sense wanting to stand on an argument that we need protection. The argument is very very much more along the lines of there is under APEC an agreed timetable. We can't see why that should be departed from. We can't see any instant great benefit for consumers, and our secondary fall-back position is, if you are going to do any reduction then we should get some value for it, we shouldn't just unilaterally do our thing without at least raising it in the forums and offering to trade against an advantage.

MR WOODS: Yes, I understand the weight you've put on the reciprocity argument, and then it's a matter of judgment as to whether the costs of the protection more generally outweigh or don't outweigh the possible benefit that one could get from that trade leverage.

MR MARJORIBANKS: I think there will be an effect on us. I mean, that was illustrated in the tinplate situation that my colleague Mr Landy referred to where it was fairly instantaneous, the reduction in price of tinplate, but that's one of the things we have to live with, and we would have to live with an accelerated cost reduction due to tariff or a price reduction due to tariff and our response would be a much greater acceleration in cost reduction and all that that entails for investment and labour and all that sort of thing.

MR WOODS: All right, so we no longer need to pursue those principles. If I could spend a little time just clarifying some of the points of detail, that would help to fully understand your submission.

MR MARJORIBANKS: Yes.

MR WOODS: You talk about the divestment of businesses. What impact, if any, will that have on the amount that you export? Are any of those businesses part of that current export figure that you provide? And would their divestment reduce either the proportion or the volume of exports?

MR LANDY: A lot of those businesses actually have been rationalised in recent years and have significantly reduced their exposure to export.

MR WOODS: So they're focused more on the domestic market?

MR LANDY: More on the domestic market.

MR WOODS: So you don't expect them to have a big impact, then, on these macro figures of exports as a proportion of your production?

MR LANDY: No.

MR McDONALD: The closure of Newcastle, which had substantial exports, has been taken into account in those figures that we have given you, too. So to that extent they're largely reflective of the current position after the closure of Newcastle.

MR WOODS: That's post Newcastle. And presumably your description of them as being good businesses with strong market positions again reinforces that you're not seeing them needing to hide behind tariff protection.

MR LANDY: Which is this case for our - the businesses will remain also, as Mr Marjoribanks just stated.

MR WOODS: Yes. You make a brief reference to continuing with things such as Manufacturing-in-Bond. My understanding is that that's not yet been a roaring success in terms of take-up. Does your mention of it here suggest that you see something in the pipeline of it picking up interest in the Australian economy?

MR MARJORIBANKS: Well, we're coming from a very particular point of the compass on that one because we joined in with the Newcastle Chamber of Commerce and the Hunter Development Authority and so on in proposing that the so-called Steel River site which we'd made available in Newcastle, with the intention that in the longer term it would be something of a replacement of employment, not necessarily for the actual steelworkers but as a source of employment in Newcastle, and the concept of giving it a competitive advantage through creating it - originally the concept was an American-style foreign trade zone but that subsequently got changed into being Manufacturing-in-Bond, and the company went to some lengths to support the idea that Manufacturing-in-Bond would be available.

We still feel quite strongly about that, and to the extent that it's an issue in this debate at all, we just wanted to vote that we're still very interested in that as something which would be available for Steel River.

MR WOODS: That's helpful to understand the reference there.

MR MARJORIBANKS: But of course if tariffs disappear then the rationale disappears.

MR WOODS: Yes. You talk about imports of steel products doubling from 1991-92 to 98-99. Is any of that due to the closure of your stainless steel production facility and, if so, would that account for a significant component of that?

MR LANDY: The answer to the first part is, yes, it does. There are some imports but it is a relatively tiny quantity.

MR WOODS: Some but not significant.

MR LANDY: It is not significant at all.

MR MARJORIBANKS: Can I add to that?

MR WOODS: Sure, yes.

MR MARJORIBANKS: For quite a number of years, since the middle 80s, in fact, the stainless steel operation itself ran on imported hot-rolled stainless coil, so - - -

MR WOODS: Do you mean cold-rolled?

MR MARJORIBANKS: And we cold-rolled it. That was what we did. So in terms of volume the exports wouldn't have changed because the market demand for that product would be fed totally from, I guess, imported finished product as opposed to imported semi-finished product that we finished.

MR WOODS: We have a submission from the Australian Stainless Steel Development Association which is also generally and publicly available and it says in part:

> In 1996 the Australian government imposed a tariff on imports for business inputs, effectively imposing a 3 per cent tax on imports for BHP's feed material and all other stainless steel goods. Shortly following this decision BHP announced it would close its stainless steel plant at Port Kembla, effective May 1997.

Was there any actual relationship between the two decisions, or were they just coincident in timing?

MR MARJORIBANKS: I think we said at the time - and I can check back on this, but I think we said at the time that we had already had that decision in train, but certainly the impost of 3 per cent wasn't going to help the thing at all. But I think at that point in time the decision was in train.

MR WOODS: Thank you.

MR MARJORIBANKS: But if that's a significant point we can confirm that.

MR WOODS: No, it's just a clarification of it. I like to cross-reference submissions to understand. That's fine. You make reference on page 4 of your submission to China increasing its exports to Australia by 36 per cent per annum, Malaysia 29 per cent, Taiwan 15 per cent and Korea 8 per cent. They're very large increases but could I understand what sorts of bases these increases are building from. Do you have a table on that? Even if you provide it later, it would just help us to understand.

MR MARJORIBANKS: We'd prefer to provide it later, I think.

MR WOODS: I mean, 36 per cent might be a very big figure, but it may not be a very big figure if the actual volumes being referred to are not high in the total scheme of things.

MR MARJORIBANKS: Yes. I'd say that perhaps whilst in overall volume terms China on its own may not be significant, it is quite significant in certain areas or segments of the market where the volume may not look as great - - -

MR WOODS: But they're strategic in that particular market segment.

MR MARJORIBANKS: - - - but the impact is quite significant.

MR WOODS: Presumably you've been following China's various concessions as part of its WTO entry procedures. The reductions that it has been offering in that process, does that constitute some of the reciprocity that you're looking for?

MR MARJORIBANKS: I'm not across the detail in that myself. I mean, in a general sense, yes, it would do in the longer term.

MR WOODS: Yes. I just don't understand at what point others giving up some of their tariff protection in your minds would be sufficient for us to then make a next move and so on. I'm just throwing in these examples to try and understand that a little further.

MR LANDY: Mike, if I could just continue to expand on that point, whilst we don't have the data - we can provide that later - - -

MR WOODS: Yes, at your convenience.

MR LANDY: - - - the reference to China, since you've raised it - most of that increase has been in a product we call steel plate which goes into manufacturing of sort of heavy structures, tankage, it goes into fabrication of machinery. It's quite a heavy, thick material. China has been exporting to Australia quite significant quantities of that. That, coupled with the general downturn in demand in Australia, has really caused some significant issues for the particular facility that manufactures plate in terms of keeping the volume up to economic levels. So, as I said before, in certain segments there is potentially - whilst the volume is not great there is a fairly significant exposure to the activity of certain countries in their exports to Australia which can be quite damaging.

MR WOODS: Yes. Thank you. I don't have any further detail that I want to explore at this point, but I do thank you for both your submission and the lengths you've gone to in providing answers in our discussion this morning. Would it be reasonable to say that at the core of your submission is a judgment as to the importance of Australia relinquishing its last 5 per cent on general tariffs as a trading negotiating tactic versus whatever costs may be incurred by retaining the tariff to those who are using your product as business inputs and to consumers, and that that's where the essence lies, in making that judgment?

MR MARJORIBANKS: There's one point that we said earlier on we would come back to, and that is in relation to the issue of Australian manufacturers who use our products in products which they themselves export.

MR WOODS: Yes, please.

MR MARJORIBANKS: I will ask Mr Landy to comment on maybe some of the detail on that, but in general we give substantial rebates against steel purchases for the specific purpose of exporting, and those rebates by and large would be greater than the reduction that a 5 per cent tariff would achieve. So as far as export manufacture in Australia from using BHP Steel product, the reduction of tariff would not be a factor. Now, I don't know whether you want to - - -

MR WOODS: Yes, so that's a company initiative - - -

MR MARJORIBANKS: That's a company initiative.

MR WOODS: - - - to support those who are using your product in their own export.

MR MARJORIBANKS: Yes.

MR WOODS: Does that also apply to those who use a high proportion of steel as part of the process in manufacturing a product that gets exported?

MR LANDY: That's what we're talking about.

MR WOODS: Well, sorry, I interpreted it as meaning particular machinery or other product where the steel itself is exported, as distinct from products that have utilised steel products in their manufacture.

MR LANDY: We're really saying that for customers who buy steel and use the steel in Australia, in Australian manufacturing applications - that's what we give the incentive to.

MR WOODS: Thank you.

MR MARJORIBANKS: The classic examples are the automotive industry exporting motor cars, so that proportion of the sheet steel which we supply for a car which is destined for export is rebated on the amount of steel they purchase to manufacture the export motor car.

MR WOODS: Yes. Thank you.

MR LANDY: And that goes across a number of segments.

MR WOODS: Yes.

MR LANDY: In fact, virtually anywhere that our customers are exporting, we do partner with them in those initiatives because it seemed a way we can jointly grow together.

MR WOODS: Do you have some further material on that that you could put to us to assist us in understanding this arrangement?

MR LANDY: I guess if you have a specific request we can provide something. We don't have anything to furnish today, but if you want us to, we can put something together.

MR WOODS: Yes, we will contact you should we see that that would be helpful to us.

MR LANDY: Okay.

MR WOODS: Okay.

MR McDONALD: Mike, we would also like to add that when the Productivity Commission is looking at the cost to industry and to communities that you take into account the high regional location employment that the steel industry infers on its location. That's detailed in our submission.

MR WOODS: Yes, we understand your locations and the implications of that for regional Australia.

MR MARJORIBANKS: Yes, and I think the only other point that we did make in our submission that we draw your attention to is the 1995 ACCC - the old Prices Surveillance Authority investigation of steel.

MR WOODS: Yes, I read that with interest.

MR MARJORIBANKS: Where they said, as we said in the report, "Domestic steel prices have increased at a much lower annual increase than prices of other materials," and so on, so the argument we're coming with there is that consumers of steel have been well treated by the steel business in the last several years.

MR WOODS: I noticed that and you referred in particular to international prices rising sharply in 94-95 when Australian steel prices did not. Does your reference to relative stability also mean that the troughs in pricing that occur internationally are not matched by yourselves as well, that you do some form of equalisation?

MR MARJORIBANKS: Yes, we have a substantial number of markets where we are pricing on that sort of basis. I don't know whether you want to elaborate on that.

MR LANDY: Well, that's right, but on the other hand we do have other segments where we do follow a fairly strict line with what's happening overseas. It really depends on the market segment. Some customers like to go with the flow, others like to have the volatility ironed out and we tailor our pricing accordingly.

MR WOODS: Yes, I wasn't entirely sure by the reference to your specific point there whether you meant that you only part-matched the rises but fully followed the troughs or whether you sort of part-matched the troughs as well as the rises. But as you say - - -

MR LANDY: It depends on the segment.

MR WOODS: - - - you pick your pricing for your customer relations.

MR LANDY: Yes.

MR MARJORIBANKS: Well, in an arena where most of our customers are becoming global, you can't - - -

MR WOODS: Yes, you're following more troughs than peaks.

MR MARJORIBANKS: Yes, we follow more troughs than peaks because, when all is said and done, the Australian steel market is regarded as an open market. We don't have quotas. We don't have D'Avignon plans. We don't have any number of other mechanisms. We don't have the lower house of parliament voting to go back to 1996 levels of importation from all countries. That bill actually went through the congress in the United States. We don't have any of that sort of thing so we are an open market.

MR WOODS: Yes, and that's a point that has been made by others, although they use that point to argue against reciprocity whereas that is not your situation. Thank you. Any concluding points that you wish to raise?

MR LANDY: Just an overall comment I think that basically, given the state of the global steel market, we think there are enough natural market forces on supplies in Australia of steel to make sure they're competitive without, you know - well, basically that's the statement I would like to make. I think we are in a globally competitive and volatile market and we're responding to it. We're taking that initiative ourselves and with our customers.

MR WOODS: Thank you, and thank you again for both the submission and the detail that you've been able to provide to the commission.

MR WOODS: My next witness is Ronald Fisher Trade Consultants Pty Ltd. Thank you very much. For the record could you please state your name and the capacity in which you are presenting evidence today.

MR FISHER: Yes, my name is Ronald Claude Fisher and I'm appearing on behalf of the Printing Industries Association of Australia, York Street, Sydney.

MR ANDERSEN: My name is Philip Duncan Andersen. I'm national director of Printing Industries Association of Australia and it is in that capacity that I'm appearing.

MR WOODS: Thank you very much. We have received your submission which is quite detailed and very helpful. Do you have an opening comment you wish to make?

MR FISHER: Not really, other than to say, as we have requested there, that the industry has at many of these inquiries been in favour of the movement towards free trade. We're quite relaxed about that provided that we move in concert and that the tariff is on the material inputs that are quite a substantial part of the cost structure of the industry - move at the same pace and the same time.

MR WOODS: Very good. Can I take you through your submission.

MR FISHER: Surely.

MR WOODS: Some of my questions are matters of detail and some go to the heart of the principle of your submission but if I can just take them in the order in which they appear.

MR FISHER: Yes, please.

MR WOODS: I notice, as you say, the traditional parts of your industry are such things as stationery and business forms and the like. With changing technology and a lot of in-house printing as part of the process of producing a letter or an invoice or the like, is that having a marked effect on your industry?

MR FISHER: No, I think that the trend to in-house and I guess Quick Print and those sorts of things - who are part of the industry anyway as being with us - the real change in the industry is the growth in IT of course and this industry embraces that. As we say in these action agendas that we're talking about - even Bill Gates says, "I will go and print it up on my screen," and that is part of printing. We have broadened out from ink on paper to other areas, so the industry is changing but it's also growing because it embraces that new technology.

MR WOODS: Okay, so you see that as inclusive in that process.

MR FISHER: Yes.

MR WOODS: You mentioned just then the action agenda and I was quite interested as to what you see it as encompassing and what the time frame is for its development.

MR ANDERSEN: The time frame I guess began early last year with the launch by the industry minister, Nick Minchin. We then held a series of workshops in Canberra to do some industry swot analyses. We have then since then done a whole range of further swots, if you like, with major users of print in this country. The time frame we are working towards now is to have an initial report completed by the middle of this year at which time the government will probably step back. However, the industry participants will be continuing because we anticipate there being a whole series of issues that will arise in this investigative phase that will require further work. It will be up to the industry then to work on - come to some answers.

The range of issues that we are looking at in this action agenda program is very very broad because we really have looked at all aspects of our competitiveness, where we see our weaknesses, where we see we have some distinctive competencies that perhaps we can build upon, what are some of the roadblocks which are impeding our ability to have some sort of sustainable future. If we identify those roadblocks, then what action, either as an industry or as individual companies or as governments, can we do or take to overcome those roadblocks? That's the sort of process we are following.

MR WOODS: Thank you. That's helpful. Now, you make reference in the next paragraph to not yet being export-oriented, although moving in that direction. Again, could you elaborate a little on that for me.

MR FISHER: Yes. I guess the printing industry has been over the years a little bit insular. For many years it was closeness to customer and those sorts of things that dictated performance. Technology and globalisation have moved people away from that cosy little environment where you sit down and do that. There have been some good exports in the industry, mainly in niche markets. We have developed good markets in Hong Kong, Singapore, and others, for particular products. New Zealand of course is the major market for Australian print and packaging. America is probably the second market, but the industry itself until very recent times has never really had as an industry that outward-looking perception that, "Yes, we need to go out and look at export markets," that 1 per cent of the American market, if you can get it, is a significant increase in what you've got in your domestic market and adjusting globally.

Now they've got to do that, they are doing that, the association encourages them to do that, and they're starting to achieve some significant gains. Even in the book production area, if you like, which was very sensitive and where the major import competition came - probably something over 50 per cent of books on sale in Australia are still printed overseas and it tended to be, "Because of that why should we look for markets overseas for our books? We can't compete." That's changed significantly and book printers are now making significant export gains.

MR ANDERSEN: If I could perhaps just give two examples of that export area where we have done that - one in very much a niche area. We have a member who prints the little tags that go on the end of tea bags and they do that for Ceylon Tea. They ship containerloads of those around the world for Ceylon Tea. Very much a niche product but very good business for that company. Another one is where the development of technology has made an impact and allowed a small Wollongong company to actually do the design work for Brax Confectionery in the United States for the wrappers that go round the individual chocolates, and that was an opportunity which truly wasn't there 10 years ago but is now because of the technology. They can send that design electronically. They haven't actually physically to be there.

MR FISHER: The industry tends, in some instances, to piggyback on other industries. The tremendous growth in wine exports from Australia has led to a significant growth in wine label exports where Californian growers and that are seeing the expertise that we've developed with wine labels and, you know, there's quite a good market for Australian label printers.

MR WOODS: You made reference in your comments to "insular" and "cosy" and in your submission referred to the dark ages of the high tariffs. I think all of that reinforces your general point that you're not a supporter of tariffs as such but looking for ensuring that there are no anomalies in the process of progressive reduction of tariffs. Is that a fair summary?

MR FISHER: That's certainly a fair statement. I think the greatest concern of the industry is now not with tariffs, except on raw materials when they go, but what we would see as the all too easy avenue of dumping applications, particularly on paper, and that tends to negate some of the gains that you can make out of tariff reductions by substituting a dumping duty for a tariff. It creates significant problems for the industry because only around 50 per cent of paper requirements can be produced in Australia. Unfortunately, if you've got a dumping duty of significant proportions on that other 50 per cent, it must come in. It's not something you can pass on to your own customer and you tend to absorb that, and that, of course, just lowers your profitability and might retard investment a little bit.

MR WOODS: Presumably you make those fears known during inquiries into - - -

MR FISHER: Certainly do.

MR WOODS: You choose a date of 1 January 2005 as being a target date for removal of tariffs. Any particular reason for that date, other than it's somewhere between now and 2010?

MR FISHER: Not really, no. I guess it's a halfway house. There's no real reason, other than if you look at your reporting time and then you look at an adjustment time. This industry wouldn't be fussed if that was 2003, for argument's sake; that there are a couple of years of adjustment and getting people used to it. But no, there's nothing significant in 2005. It shouldn't go out to 2010, though.

MR WOODS: So you'd see that as an end date, rather than a target date.

MR FISHER: Yes.

MR WOODS: I guess certainty is so important in business planning.

MR FISHER: Predictability and certainty, so that there are a couple of years that you know it's going to happen; you adjust to it and you live or die by it.

MR WOODS: And your members generally would be comfortable with that perspective.

MR FISHER: Yes, they are.

MR WOODS: That's very helpful. You made reference that there had been a lot of change and the adoption of world best practice, exposure to international competition, taking up rapid technology, although you then went on to point out that that's led to chronic overcapacity and underutilisation. Is that working its way through the industry?

MR FISHER: I think it'll take quite a while because technology is still changing rapidly. It's not as though it changed and now we've got a hiatus where you adjust. It is still - we're very much in a technological age. It's not just germane to the industry in Australia; it's an international phenomenon, the overcapacity and everything else. The increased perception of export possibility is starting to help but it's something that's going to be with us for the foreseeable future anyway, that overcapacity. You can't just buy half a printing press. You can't run it at half speed because it's totally uneconomic. You've got to use best practice, you've got to run the machine at its maximum capacity and then, if you haven't got the work for it, it doesn't run.

MR ANDERSEN: As part of the action agenda process we actually conduct a limited survey to try and get a better handle on the capacity utilisation levels in the industry, and if that would be helpful we can certainly forward that to the inquiry.

MR WOODS: Thank you, that would be helpful. You made reference to some long-term econometric modelling of the industry - short and long term. Is that bearing fruit at this point and, if so, is this part of your action agenda work or is this unrelated to that?

MR FISHER: Preceded the action agenda but is inevitably part of it. I guess the need for it arose because of a lack of government understanding, if you like, of the industry; a perception that this is an old craft industry with ink under the fingernails and everything else, and we needed to change that perception with government. The GST made it even more imperative that we had models so that we could go to government and talk about the effect of GST on various sectors of the industry.

They're dynamic models and they'll continue to be updated annually, and we will continue to use them and firms will continue to use them to test various things, but certainly we will be testing this when Chris Murphy is back at work from his holidays. Through both of those models we will be testing both in a time frame in the 5 per cent to give you some better data as to the effect on the industry and the community at large.

MR WOODS: Do you have a view as to the timing when some of that data would be available?

MR FISHER: The first couple of weeks of February.

MR WOODS: You make a reference to the question of reciprocity which a previous witness was also proposing but you frame it in a sense, as I understand it, of reciprocity being a desirable but not essential component of the process of tariff reduction. Is that a fair assessment of your view?

MR FISHER: Yes, I think that's right. We'd certainly like to see reciprocity but we wouldn't like to see the process halted because there wasn't reciprocity. I think we've got to continue to fight for that. We've been engaged in that for a little while with APEC and working with Foreign Affairs and Trade on those reductions and the speed-up of tariff in the forest products area, which includes paper and printing, of course. I haven't seen it yet but I know that the USA and New Zealand combined certainly in a non-tariff barrier sense to set down all of the non-tariff barriers of those APEC countries that would impede free trade between the members. I think that's just been completed.

Now, we would like to see that used and brought to fruition to remove those barriers but we don't want to sit back and say, "We don't move till they move." We move because there are gains anyway and eventually we hope those gains are reciprocal.

MR WOODS: Very good, and that's a point we were debating with the witness prior to yourselves.

MR FISHER: Yes, I heard you talking, and I think you were making the point, maybe not as blunt, that it of itself doesn't carry an enormous amount of weight in international trade - our 5 per cent - and I'd agree with that.

MR WOODS: So that would be your judgment?

MR FISHER: Yes, it would be, certainly, and again that's why we shouldn't sit back and wait. We need to get the gains now, here and now for our country, and then fight for that to be carried through internationally.

MR WOODS: So you would argue on the basis that the unilateral gains outweigh the potential cost of waiting for - - -

MR FISHER: Indeed they would.

MR WOODS: - - - movement by others.

MR FISHER: Yes.

MR WOODS: That is the judgment to be made.

MR ANDERSEN: I think the other thing that we need to make sure we understand there is that we're not just referring to tariffs in these other countries but also some of the non-tariff barriers. We'd be fighting for those as well - for their elimination.

MR WOODS: You argue against phased reductions from 5 per cent. Can you elaborate on that for me? Clearly it's an option but it's not one that you favour. Is there something that you'd - - -

MR FISHER: I think that, at least in the history, the history of phasing - and there has been phasing over time in tariffs from the 55 per cent days to the 5 per cent days - it just tends to delay the initiative in the industry to adopt best practice, to move with the times, to get technology. You put off the hard decisions until crunch time arrives and I think it's easier, and better for all concerned, to have crunch time up-front and adjust to it.

MR WOODS: You make reference to Manufacturing-in-Bond and that your members take advantage of it and TRADEX schemes. Is there any specific Manufacturing-in-Bond arrangement by your members that you're aware of, or you firm more to the TRADEX?

MR FISHER: Probably more to TRADEX. There is a bit of Manufacturing-in-Bond. I think Carlton with exports of - and we're talking here of cans and again labels on bottles. There is a bit of in-bond manufacture for export but TRADEX would be used more so than an actual Manufacturing-in-Bond.

MR WOODS: Thank you. I don't have any further particular questions on your submission, which I found to be very helpful. Are there any concluding comments that you would wish to make?

MR FISHER: No, not really, other than we're grateful for the opportunity. We would like to reinforce the point we made about the tariff concession system; that I think it is inequitable at the present time that you have 3 per cent on producer materials and duty-free on consumer materials under the scheme, and we would like to see that - and we've made representations to the treasurer - to mention many times. We would like to see that imbalance, if you like, corrected as soon as possible. It was a revenue measure. It was there supposedly to help fill in that black hole that they inherited that no longer exists. We're into surplus budget and we don't see the 3 per cent as a revenue measure as anything that should continue as of tomorrow - as soon as you can make the appropriate recommendation.

MR WOODS: Thank you very much and thank you for the time that you've devoted to assisting this inquiry.

MR FISHER: Thank you very much.

MR ANDERSEN: Thank you.

MR FISHER: And we will forward Murphy's analysis as soon as we've got it.

MR WOODS: Much appreciated.

MR FISHER: Thank you.

MR WOODS: Our next witnesses are the Australian Industry Group. As they're not present at this point, we'll take a short adjournment until they arrive.

MR WOODS: The next witnesses are the Australian Industry Group. Could you please for the record give your names and the capacity in which you're presenting evidence today.

MR HERBERT: Yes, I'd be pleased to do that, Mr Woods. My name is Bob Herbert. I'm the chief executive of the Australian Industry Group. Perhaps I could introduce my team that will be here and available to talk with you about the issues today. On my immediate right is Prof John Quiggin from the Australian National University and the Queensland University of Technology. Prof Quiggin has been commissioned by us to prepare a paper on some of the issues relevant to the review, and he would like the opportunity today - as we would - for him just to speak briefly to that during the course of this presentation.

Mrs Heather Ridout is the executive director of public policy and communications with the Australian Industry Group and has been particularly involved in quite an important survey of our members about this issue, and she would like to speak to that matter this morning. Mr Leigh Purnell is the executive director of the international division of the Australian Industry Group and Mr Purnell particularly will concentrate on WTO, APEC matters, and the TCS. You may be aware that he accompanied Minister Vaile to Seattle earlier this year or late last year for what might be described as fairly difficult WTO considerations, and there's a paper that relates to that amongst the submission we've given you.

MR WOODS: Thank you.

MR HERBERT: I'd like to, if it's convenient, make some general comments in opening before my colleagues speak.

MR WOODS: You'll be addressing a submission which, for the record, you're submitting as part of presenting evidence this morning?

MR HERBERT: That's right. We had a submission that we have provided you with now, and additional copies are available as required. You'll find that it's a very comprehensive submission and it's structured in a manner to deal with the terms of reference of the review. It is regrettable that you have not had this document in advance of our presentation today, and it may help you, therefore, if we were to just take a minute to explain how it is structured, and with the embellishments that we will give to the submission in our personal presentations you will quickly get a good grasp of the theme behind our submission.

MR WOODS: Thank you very much.

MR HERBERT: If you were to just turn to the contents page I think you will quickly have an appreciation of the structure of it. It deals with an introduction, the implications of findings for a further unilateral reduction in the general tariff, then it summarises five key papers that have been prepared and are part of this submission. Without running through each of the titles of those papers - their content - they will be obvious to you by looking at that page. So they're summarised in section 3, there are conclusions and recommendations in section 4, and then each of the papers that I've referred to follow, in effect as inclusions in the document, and of course the terms of reference are included there. I'd like, if it's appropriate, to make some opening comments.

MR WOODS: Please.

MR HERBERT: I think it's fair to say that we - the Australian Industry Group - didn't welcome this review, and we're on public record as saying that. When it was first mooted we argued that it was inappropriate and unnecessary and ill-timed. But be that as it may, the review has proceeded and we have approached the preparation of our submission in what we believe is a very thorough and diligent manner to ensure that industry's views are properly understood and taken into account - the recommendations of our members, which are embodied in the submission.

We represent in the Australian Industry Group some 11 and a half thousand companies, and the majority of these operate in the general manufacturing sector. These companies are going to be directly affected by the outcome of this inquiry, more particularly the decision the government may make following receipt of your recommendations. Now, I have mentioned that we have prepared the submission to encompass five important studies which are relevant and relate to the terms of reference, and they are summarised in the document and the full papers are there.

The first is a survey of some 550 of our member companies about the review and the impact of a reduction in the general import tariff upon them. That's paper 1 and Mrs Ridout can speak to that as you may require this morning. The second, as I mentioned, is the paper we commissioned Prof Quiggin to undertake to examine the welfare benefits to the economy of a reduction in the general tariff, and as well the interaction between the tariffs and the exchange rate, and that's embraced by paper 2, and Prof Quiggin will be able to speak to that.

The third paper is on progress in world trade liberalisation, including the progress - or, as I mentioned, the lack of it - in the WTO negotiations, and Australia's obligations and performance under the APEC arrangements, and an analysis of Australia's barriers to trade vis-a-vis competitor nations. That's dealt with in the third paper and Leigh Purnell will speak to that. The fourth paper is an analysis of the tariff concession system and, finally, there's a paper which deals with the strategic importance of Australia's manufacturing sector.

Mr Woods, the five studies that are encompassed in our submission taken individually and collectively indicate that, given the adjustment costs to the economy and the community, there is no scope for further unilateral reductions in Australia's general tariff. They suggest that to do so would involve considerable risk with little potential benefit. You will see from Prof Quiggin's analysis it indicates that the welfare benefits from a reduction in tariffs to zero would be small, while the adjustment costs - and I quote - are "likely to outweigh any static efficiency costs".

When Prof Quiggin speaks to his paper shortly, he will also deal with what is the definition of free trade in a floating exchange rate environment, a fairly important issue I think for this review to consider. The survey that I have referred to of 550 of our member companies would suggest that the adjustment costs, particularly in terms of employment and production, would be substantial. It further suggests that investment in the industry would contract sharply, putting at risk the long-term viability of the industry in Australia.

Mrs Ridout will deal with the key statistics but just to give you a flavour of the survey 56 per cent of companies said if you were to so move to reduce the tariff to zero you could expect quite significant employment implications, averaging - for those 56 per cent of companies - about a 15.2 per cent drop in employment. In terms of investment, equally dramatically 46 per cent of companies said such action would reduce investment on an average of 25.7 per cent.

The paper we present on the strategic importance of manufacturing particularly relates to the defence sector, and it reinforces the point not to allow the long-term viability of industry to be put at risk. Our analysis of trade liberalisation in Australia and abroad would indicate that a decade or more of rapid and unilateral tariff cuts has made Australia perhaps the most open market for imports in the Western world while other countries have lagged behind. We contend that Australia's tariffs are now among the lowest in the developed world and, unlike other countries, Australia has hardly any non-tariff barriers, and in this regard our survey comes into play again because a little more than one in four companies are saying that as they seek to sell overseas the non-tariff barriers constitute a major restraint for them in selling their products in overseas markets.

We also contend that Australia is also already well ahead of many of our APEC partners in trade liberalisation programs, and this means Australia, in our view, has virtually no negotiating coin left to play in world trade negotiations. We have everything to lose and little to gain from a world stalling on its trade liberalisation programs. In the meantime, we contend the prospects for further world trade liberalisation in the immediate future looks pretty bleak. The WTO and APEC action appears unlikely until well into the first decade of the new century. Indeed, it appears that the opposite is more likely to be the case as there might in fact be a resurgence of some protectionism as evidenced perhaps in the USA and Asia.

The studies support a holistic approach to this issue in Australia, one which acknowledges wider community goals and which places tariff policy within the broader context of mechanisms which can influence our economic performance. The studies that are a part of our submission provide no support for placing a tariff on inputs to production which are products not manufactured in Australia. It's clear that the current TCS - tariff concession system - is damaging the competitiveness and viability of Australian industry. It's a tax on industry and we believe the case for its removal is irrefutable. Consistent with this, every effort to remove genuine nuisance tariffs should be supported.

The outcome of this review is extremely important to Australian manufacturing industry. You would be aware it constitutes 12 and a half per cent of GDP, about 12 and a half per cent of employment. Over a million Australians are employed in manufacturing, and they're the biggest provider of full-time jobs. 90 per cent of employment in manufacturing is full-time employment. We contribute 33.9 per cent to the total export effort of Australia, 21.1 per cent of new capital expenditure, and we account for 57 per cent of private sector R and D. So it's our contention that a unilateral reduction in tariffs would render further damage to this sector, which is clearly so significant to the Australian economy, for very little gain.

It would come as no surprise that the trade deficit in manufacturing has increased rapidly and substantially during the 90s, contributing to our current economic woes. The manufacturing trade deficit accelerated largely in response to strong growth in imports, as you would be aware. Overall, the manufacturing trade deficit widened to $55.8 billion in the year 1998-99. That's a rise of 13 per cent over the previous year, and a 78 per cent rise since the start of this decade. I don't think we need to remind anyone that the current account deficit remains a big and dark shadow hanging over our economic future.

The submission we make to this review leads us to make these four main recommendations. First, given the adjustment costs to the economy and the community, there is no scope for a further reduction in the general tariff from five to zero and that to do so would involve considerable risk with very little potential welfare benefit. Second, any reductions in Australia's barrier protection should be contingent upon reciprocal and proportionate action by our trading partners. Third, the present duty applied to inputs to production under the tariff concessions system should be abolished. Fourth, efforts to abolish nuisance tariffs should continue where such tariffs serve only to increase business input costs and do not provide support for any local manufacturing capability.

Mr Woods, that's an outline of our position. I think it would help you, in view of the fact that you haven't had the benefit of seeing our submission in advance, to have my colleagues speak to some of the key papers.

MR WOODS: Happy to do so.

PROF QUIGGIN: I have been asked to look at the review primarily from a welfare economics viewpoint. The policy proposal under discussion is a general move from 5 per cent tariffs to zero. Looking at first the case in favour of this, it basically comes obviously from the theory of comparative advantage, and the associated what's typically called in this debate static welfare theory. And under assumptions which are well-known of full employment and so forth, we do indeed get from that theory a view that the optimum rate of protection is zero, that free trade is the welfare optimum.

However, the gains from the move from 5 per cent to zero are in this context estimated to be very small. I have produced some estimates of, for example, about two days' worth of GDP growth. That's based on lowish elasticities of supply and demand. Looking at the evidence from the survey response I'd now probably want to go somewhat higher, but we're still talking very small percentages of GDP. I would suggest estimates in the range of 0.01 per cent of GDP to 0.05 per cent of GDP are implied by the fact that we have got a 5 per cent tariff applying to approximately 10 per cent of traded good that are approximately 10 per cent of GDP.

MR WOODS: Your calculations didn't have the opportunity of taking into account the survey?

PROF QUIGGIN: No. I did the calculations - because the survey has only just - so the survey in fact suggests somewhat larger elasticities of supply than those I used illustratively.

MR WOODS: I take that point.

PROF QUIGGIN: Of course, the supply, the adjustment costs and the welfare benefits move proportionately in this respect. The crucial theoretical point is that the adjustment costs of a 5 per cent change in prices are the same whether that's produced by a change from a 30 per cent tariff to a 25 per cent tariff or from 5 per cent to zero. On the other hand, the welfare benefits are proportional to the square of the deviation from first best prices, so the welfare benefits decline dramatically for further reductions as we move down towards zero tariffs, whereas the adjustment costs remain linear in the cost of adjustment. So assuming adjustment costs are positive on average, there must indeed reach a point where the adjustment costs are going to outweigh the welfare benefits of further moves towards zero, if we focus on the static case.

Of course there has been a good deal of discussion, usually fairly loose, of dynamic arguments to do with reductions in tariffs. We make a number of points on this. First there are of course dynamic-type arguments that are in favour of high tariffs rather than against; various sorts of arguments derived from new growth theory and so forth. Second, and I think very importantly, most of the arguments that have been put forward in favour - for example, that the pressure of import competition will make industry leaner and meaner; that an outward orientation is preferable to an inward orientation - those arguments, if they're taken seriously, generally imply that the ultimate tariff is negative; that we should be taxing our import-competing industries rather than supporting them.

And from the fact that I very rarely see arguments of that kind put forward in this kind of debate, I conclude that the dynamic arguments are typically used as rhetoric supporting the conclusion derived from the static case, rather than being taken seriously and evaluated in a way which would produce certainly an environment of considerable intervention, although possibly including negative protection of some industries rather than positive. So I think they're never going to take them seriously. We certainly wouldn't get to non-intervention as the optimum. We'd get to some complicated form of intervention that depended on which particular pandemic arguments you base credence in.

So we can certainly get benefits. I've got some rough estimates using the Harberger welfare triangle approach. As I say, I probably want to raise those somewhat in the light of the estimates of high supply elasticities that we've seen, but still very small and, while obviously a general equilibrium approach would be preferable, I think if the general equilibrium approach gave estimates that were already out of line with that, that would suggest that it was the general equilibrium model that was at fault rather than the basic estimates because they're fairly robust to modest changes in the kinds of assumptions you use.

The adjustment cost is a much more difficult issue. I've again had a look at some of those, using the kinds of estimates of supply response that we've seen. I have used them from the survey in this case - I've got somewhat larger estimates - and it seems reasonable to suggest that, even assuming that there are considerable benefits in other areas of the economy that partially offset a withdrawal from the labour force associated with adjustment costs, we still are going to look at adjustment costs which are comparable in magnitude to any welfare benefits arising from the tariff and even when we consider only impacts on labour, when we consider costs such as increase in bankruptcies and other forms of adjustment which are typically socially costly, typically dissipate resources, it's my view that the adjustment costs are likely to be comparable to or larger than the welfare benefits of a move to free trade.

I now want to talk a bit about the issue of exchange rate uncertainty. It's obviously true that when we're talking about a 5 per cent move in the tariff, variations in the exchange rate over moderate periods considerably outweigh the effect of the tariff one way or the other, and this raises a question as to whether the case for zero is the optimum which is developed in typically a barter economy without any exchange rate type instruments; what the effect of that is when we take into account the existence of exchange rates and when we take into account the fact that exchange rates fluctuate and spend long periods away from the purchasing power parity level where theory would suggest they ought to be.

There has been a modest literature on this, and I've quoted some of the papers. The first point is that if we have a complete set of state contingent financial markets, there's no change of course to the classical result; that is, in the context of perfectly operating international financial markets in which firms can completely hedge any exchange rate risk they face in a costless and efficient fashion, then we just get back to the conclusion that zero tariffs are optimum. But of course there's very considerable evidence, starting with the large and persistent deviations from purchasing power parity that I've talked about, that those assumptions aren't valid and that therefore we need to look at the situation of a risk-averse firm facing uncertainty which cannot be perfectly hedged.

In this context it's certainly possible to obtain a range of results, but if we assume that the firms in the protected sector are risk averse, then certainly there are going to be situations under which the optimum tariff can be positive to offset it because of the insurance or buffer effect provided by the tariff against the exchange rate fluctuations. It's also necessary, I think, to take account of the fact that the exchange rate isn't merely a random shock. It is in fact significantly influenced by government policy, particularly monetary policy, and it's arguable that in significant periods over the past decade or two we've had exchange rates held above the purchasing power parity level for macro-economic reasons, in which case again the effective rate of the assistance to industry is going to be negative.

That's an issue, I think, which still requires a great deal more exploration, but which at a minimum casts a good deal of doubt on the assumption that we can rely on the predictions of a model which is based on either a barter economy or an implicit assumption that the exchange rate is always at or close to purchasing power parity. I think that probably covers the main points that I want to raise. I could talk a bit more about the dynamic issues if you want to discuss that.

MR WOODS: We'll see how the discussion goes, but clearly you've covered a significant amount of ground in your paper and I look forward to reading it and reflecting on it. I'm not quite sure that we can do justice to your points based on a fairly quick overview of it. But we'll see how we progress.

MR HERBERT: Could I suggest that Ms Ridout might take you to this very important survey because that gives you a very good insight of the thinking of our members, particularly manufacturing in this context.

MS RIDOUT: When the commission called the inquiry we conducted a survey of our members in December; a tough time of the year to do a survey.

MR WOODS: We reflect also on the timing.

MS RIDOUT: Yes. We received responses from 550 companies in 11 sectors, and it was done on a national basis and included a number of regional areas. The questions asked of them covered both their attitude towards tariffs and the adjustment costs which would be imposed on their companies if there was a reduction in the general tariff from 5 per cent to zero. Set out on page 16 of our submission is a paper on the survey results, but I'll just summarise them to you briefly. Members were evenly divided on the need for the review. 54 per cent favoured it, 42 per cent opposed it, and 4 per cent were undecided.

Having had a good look at the 54 per cent I would quip that a lot of people saw it as an opportunity to have tariffs increased, which I found fascinating. But also in terms of their responses half of those that did support the inquiry were strongly supportive of maintaining the tariff at 5 per cent. Put together with the other responses you've got, almost three-quarters of companies supported the tariff remaining at that 5 per cent, which is a realistic position given the nature of the industry in a globalised sense and its dependence on imports.

MR WOODS: Was this a surprising result or an unsurprising result?

MS RIDOUT: No, it's not a surprising result. When we were MTIA we used to quip that we should become the Metal Trades Importers Association because there was becoming such a global interaction in terms of production. So I think members are very conscious of looking at their books and seeing where they're better off in terms of their whole production, so there would be an element of the industry that would be undecided or, as I said, support. But by far the majority of the industry supported the 5 per cent. I would add that 81 per cent, an overwhelming majority, preferred a reciprocal action by Australia - by our trading partners in exchange for any reduction.

That view was very very strong in the industry. They would seek reciprocal and proportionate action by our trading partners before there's any further unilateral lowering of tariffs, and that came through very strongly in the survey. It also came through very strongly in another study we did last year, which was on regional Australia, and in that study there was a very strong response from regional companies, and often at the political level, against tariff reductions.

In terms of the adjustment costs, they were very strong, as Mr Herbert has indicated. About 58 per cent of respondents, just over half, while they said that selling prices would fall, you had 56 per cent of respondent companies reducing production by an average of 14.3 per cent and sales by a similar percentage in the same number of companies roughly, an average again of 14.2 per cent reduction in sales in those companies. In terms of employment and investment, 56 per cent of companies anticipated a reduction in employment of 15.2 per cent in their operations, and a 25 per cent - average 25.7 per cent reduction in investment was forecast by 46 per cent of respondent companies. So they were substantial costs, and in fact really were quite reinforcing of Prof Quiggin's comment in relation to the adjustment costs that would be involved in any further lowering of tariff, and gave great credence to his view that the last 5 per cent and the first 5 per cent are almost just as important in terms of this whole debate.

We also asked whether industry would accept a trade-off, which was in your discussion paper, between creating an industry development fund and removing the last 5 per cent, and I'd say there was uncertainty about this but about half were against it, 22 per cent were unsure and 24 per cent were in favour. So almost a quarter of members said, "Well, we'd trade it off, put it in an industry development fund of the same value, and do that," but over half the industry, as I said, were against and preferred the bird in the hand, I think.

The other issue which came through very strongly in the survey was that one in four companies identified non-tariff barriers as a major restraint - it was 27 per cent - in selling their products in overseas destinations, and this was a very significant finding to us, obviously indicating the extent that these non-tariff barriers really were penalising companies in their operations.

In terms of the sectors, to give you an idea of where the major impacts or the strongest impacts were, I think you'd have to say they were fairly evenly spread. If you go to the paper - it's all set out there on table 2.4 - you've got food, beverages and tobacco, a third of companies roughly expect a fall in employment, 41 per cent expect a fall in investment, and both in the proportion of 19.4 per cent fall in employment and 32.9 per cent in investment. Food of course is the biggest sector in manufacturing. Textiles was obviously very high, as was transport equipment, as was basic metal products; 73 per cent expected a reduction in employment of 9.8 per cent on average, 63 per cent expected a reduction in investment of 25 per cent almost on average. So these are very substantial estimates.

I would have to say that I think the companies, given we didn't have over - we had a very honest response from companies, and we encouraged that, to this survey. As I said, not everyone signed off; not the whole of the industry signed off on the 5 per cent. There was a small minority in our view that supported its reduction. So I think what we have here is a very honest expression of what the adjustment costs would be and what the real situation is.

MR WOODS: Thank you, and thank you for going to the time and cost of doing that, also your members.

MS RIDOUT: By the way, I would say, Mr Woods, that this analysis of the survey was done by Melbourne University, so we again took the step of being very objective in the way we had it written up and analysed, as we have with Prof Quiggin's work.

MR WOODS: Sure.

MS RIDOUT: Not that we didn't think our evidence wasn't objective.

MR WOODS: No, no, but, yes, I look forward to incorporating that data in our analysis and I will pursue a couple of general questions but I'll wait till there's further debate, until we've had time to absorb this.

MS RIDOUT: We'd be very happy to give you more detailed break-ups if the commission would find them useful.

MR WOODS: Thank you.

MR HERBERT: Could I suggest Mr Purnell might just deal with those WTO-APEC matters and the TCS.

MR WOODS: Thank you very much.

MR PURNELL: Commissioner, thank you for that. Section 3 of the paper deals with our APEC-WTO commitment which is very much central to the reference that we have to pursue this because of our APEC commitments. I'd like to break this section up into two parts: some tables, to talk about where Australia fits in terms of its tariff protection and non-tariff protection and our import penetration rates compared to the rest of the world, and, if you like, just some of the attitudes of APEC and WTO countries and ministers towards progress and where Australia fits into that.

If we look firstly at some of the tables that I've put in our paper 3, table 1 looks at the production-weighted average tariff rates, Australia compared to other industrialised economies, and we see there that for manufacturing, for the latest figures, and these are based on an OECD economic outlook published last year, June 99, we have the US, the latest figures in 96, at 5.4 per cent, the EU at 7.7, Japan at 3.3, Canada at 14.4, Norway at 33.4 - and I can only say that they've obviously had tarification of other things to bring it to that level - Switzerland 3.2, Australia 4.8, New Zealand 6.4 and Mexico 19.9. So on any basis there clearly Australia is very much at the lower end, and if you look at our paper when we look at developing countries, the average tariff on any basis for developing countries is 17 per cent, being very generous to the developing countries as to their tariff rates.

Table 2 is another important table that we provide to the commission which shows Australia as one of the highest countries subject to import penetration rates, and again the latest figures there - and these are all based on OECD figures - the US has an import penetration rate of 18.2 per cent, Japan 9.1, the EU at 12.9, Canada at 49.4, Australia at 31.4, Korea 26.3 and Mexico at 40.2 and Norway 45.8. The table does point out that, depending on the rates there, you could look at the size of the economy, productivity and other matters that might affect that import penetration rate. But, given all of those, Australia is still very very highly subject to import penetration.

The final table that I would just like to draw attention to is table 6 of our submission , which looks at the non-tariff barriers, and again Heather Ridout spoke about one in four of our companies saying that that's very much a problem when they are exporting our products to other markets, but table 6 again says that if you look at the import coverage of non-tariff barriers, in the US the latest figures - it's 7.7, in the EU it's 6.7, in Japan it's 7.4, Canada it's 4, Norway 3 per cent, Switzerland 9.8, Australia is 0.6 per cent, New Zealand 0.2, and Mexico 6.9.

We have, commissioner, a massive wad of non-tariff barriers which we've done in consultation with the Department of Foreign Affairs and Trade, in conjunction with the APTA-CER proposal that we're developing with the government on a whole host of non-tariff barriers within the ASEAN economies that we're very happy to provide you with, and that's material that we're working with the Australian government on, in conjunction with ASEAN economies under the APTA-CER policy arrangements.

So I think that clearly when you look at those non-tariff barriers, leaving aside any voluntary restraint agreements or any other political negotiations that happen between some of the biggest economies, again Australia is very open in terms of our tariff or non-tariff rates.

The other point that I would make in our paper 3 is how do we stand in terms of just the negotiations, what are the dynamics of our WTO and APEC positioning? I do quote in it the trade ministers' communique that was in New Zealand last year, where they met, and those ministers said that reflecting on business concerns they agreed to further improve the credibility of the individual action plans, and that communique clearly demonstrated that APEC trade ministers realised that the progress they were making was very much below the progress that was considered essential way back at the Bogor Declaration.

Also, as Bob Herbert said, I was a part of the official Australian government delegation to the WTO in Seattle, a total disaster, and if you look at the outcome that you could try to project under any progress there, 2000 is a wipe-off because of the US elections, if nothing else, so at best we start to get down to some sort of meaningful negotiations maybe in 12 months' time. If you took the very best time frame to trying to wrap it up, Uruguay took seven years. If we said, "Well, we halved that because the whole world has gone crazy and thought it could do something wonderful," you're not talking - the earliest 2004, 2005 before we see any outcome.

Now, while we have agreements standing over from Uruguay in relation to agriculture and other products, the manufacturing sector - as Bob Herbert said in his opening statement, we have everything to lose and nothing to gain from the world stalling on this, and our position ultimately is, on the evidence that we provide the commission, on the tables that are there, international figures, on all the facts about tariff and non-tariff barriers, we believe that the Australian government has effectively committed itself very strongly to the APEC outlook, that other economies are lagging on any benchmark that we can put forward, and therefore we believe we can hold our APEC credentials high and, from our point of view, to take this last unilateral step of reducing tariffs from five to zero, when other economies not only in a direct sense but in a proportionate sense are way behind Australia - we believe that it's not warranted and, as we said, the adjustment costs far outweigh any benefit.

The other matter that I would like to very briefly refer to - and our paper is quite brief - is the tariff concession system. It was a crude grab for cash. It was initially instigated by the previous Labor government. They were going to have the TCS tax or tariff at 5 per cent. With the change of government the Liberal government said that they would bring it to 3 per cent. It gives the government on the latest figures, 1999-2000, something like $413 million. In past years this organisation used to appear before this commission and talk about the tariff revenue benefits to government and it was never considered an argument that we could ever mount, so on your own consistency basis we would say that you shouldn't use the tariff revenue benefits on this to be any basis for retaining it. It is an input cost, it is bad policy. It has no protective benefits to Australian industry and we strongly oppose it, have always opposed it, and we would like to think that the commission would strongly recommend that the government abolish this immediately.

As far as business input costs again, we have worked very cooperatively with the industry minister and his department. We've gone through all of the items and we've had a commitment from the minister that where we can show there was

Australian manufacture that they weren't going to be caught up in the nuisance tariffs reduction, and we've annexed the various items that we've given to the government where inadvertently tariff item lines have been caught up in that and the government has been happy to say, "Well, we'll put those aside," and we've annexed all of those we've given to the government, and we would strongly support all nuisance tariffs being removed where they in fact don't support local manufacturing capability. They're our critical points to make in those submissions, commissioner.

MR HERBERT: Commissioner, the final paper deals with the strategic importance of manufacturing to the Australian economy - particularly instances the defence sector. The paper stands on its face. I don't intend today to take you through that but there are some obvious conclusions one can draw about - - -

MR WOODS: I think I understand.

MR HERBERT: So that is the nature of our submission in brief. Again I'm sure it would have been better and helped you to have it in advance but as you haven't I'd be very pleased to ensure my colleagues and I are available at some later occasion, if you so desire, but we're quite happy to attempt to answer any questions you might wish to pose.

MR WOODS: Thank you, and we may well take up your offer of pursuing some matters after we've had the opportunity to read these papers, and thank you for the trouble you've gone to with them. Perhaps for today's purpose it may best be served by going to your recommendations and dwelling on those a little. Could you take me to the page where I will find those four recommendations you referred to.

MR HERBERT: Yes, I'm pleased to do that.

MS RIDOUT: Page 15.

MR HERBERT: Conclusions and recommendations.

MR WOODS: Perhaps I can turn to 15 where in bold you've got those four dot points and let's examine those in the light of your opening comments. Taking the last first, the nuisance tariffs, the government went through a nuisance tariffs review just recently and announced its outcome. I take it from your inclusion of this as a recommendation that you don't feel that went far enough.

MR PURNELL: Can I make two points on that?

MR WOODS: Yes, please.

MR PURNELL: The first point is that to the extent that any analysis shows that there are further nuisance tariffs, we support that being more extensive.

MR WOODS: And that being a dynamic process, there will always be change in the industry. We understood that.

MR PURNELL: And we're very happy to work cooperatively with the government, but one of the annexed tables does show that inadvertently under that 200 tariff items listed there were some tariff item lines where there is local manufacture, and under the basis that the government didn't want this to be a backdoor way of reducing tariff for local manufacture, we have listed some tariff items under that 200 listing where there is local manufacture and we believe and our industry supports the companies - because we extensively surveyed our membership - that the tariffs not be removed under the nuisance tariffs exercise where we can show that there is local manufacture and where the companies have inadvertently been caught up in it. So there's not an extensive list but there is a listing, as you'll see in the annexure of our paper, where there are some tariff items caught up in that. So that could be our caveat - - -

MR WOODS: So your general principle is that where they genuinely exist as nuisance tariffs that they be abolished because it serves purely as a tax on activity.

MR PURNELL: Absolutely, and I'd like to state - - -

MR WOODS: And you remain ever vigilant that there may be a local manufacturer who may get caught up in that process.

MR PURNELL: Yes, and we do whatever we can in working with the government to identify those and the government has said to us that that wasn't the intention of the nuisance tariff exercise and they're very happy to work with us and agree under that particular basis that the tariff not be removed.

MR WOODS: Is there a definitional issue in terms of what constitutes substitutable products versus compatible products and the like?

MR PURNELL: Commissioner, just recently under the international technology, the IT agreement, we in fact had that, so you do get definitional problems. We had a company that's in the power transmission industry - - -

MR WOODS: Yes, I'm aware of that particular one.

MR PURNELL: - - - and its capacitor was caught up supposedly, like the thing about the size of a match head that goes into computers, and they found when we extensively surveyed our membership and said, "What do companies feel about the IT agreement?" they didn't even look at all the schedules we sent out and then inadvertently they find that their 5 per cent was removed. That's been a problem. So yes, there are some instances of those, and companies don't have the resources now for people to be looking through them. We try to notify industry about issues that arise but there will always be some definitional problems.

MR HERBERT: We've gone to quite extraordinary lengths to try and help our companies understand the list and what might be there, but there will be some that will slip through the crack in this, and some ongoing mechanism to ensure that any that have as a consequence of definitional problems ought to be there, and we put that to the government as a way of dealing with this.

MR WOODS: Okay. Well, I think that one is clear enough then. The second-last - again I think your point is crystal clear.

MR HERBERT: You don't need another impassioned sort of advocacy on that.

MR WOODS: We understand that one totally, so - - -

MR HERBERT: We would welcome you getting on side on that one.

MR WOODS: I think you could agree that we can put that one to one side for the moment, but we fully understand that particular issue, which gets us to your first two recommendations. At the heart of some of your presentation is the survey. You quoted, and I look forward to reading through, a number of results of possible effects of a reduction in tariffs from 5 per cent to zero for the general tariffs. Is the base line of that survey what currently is, or is the base line a trend line of the sort of restructuring due to changes in technology, productivity, labour reform, the general micro-economic program that's been progressing to date? What is the base line that that survey uses when they talk about reducing employment by 15 per cent for 56 per cent of companies and the like? Are we talking about based on what is, or are we talking about based on the trend of adjustment that's been happening to date?

MS RIDOUT: In the question we asked them we didn't say, "Answer this question contingent upon this arrangement of being the case or that arrangement being improved or maybe more competitive." We said to them, "Look at your cost structures, examine your operations and give us a view in terms of the operation of your plant over the next years ahead." Now, I don't know whether they took into account the fact that we might get the flexibility in wages, whether the waterfront will eventually deliver productive benefits of the reform package greater than they are experiencing at the present time, and also of course the tax reform are issues that we have mentioned, of course, because we have been strong advocates of tax reform, and in dealing with that whole issue we have always let our members know there are potential benefits there. But I don't think you could really say they're directly linking prospective benefits. But they really are looking at trends in their operation and what's going to make them competitive and what's going to make them less competitive.

MR WOODS: Prof Quiggin, you've been a keen watcher of this process and a commentator from time to time.

PROF QUIGGIN: Yes.

MR WOODS: Do you have a view on whether there may be a bias in the results because people are seeing that there will be a reduction in employment due to technology or something anyway, and putting the two together?

PROF QUIGGIN: I think the inside focus on there is the investment results which are in general - I mean, if we took it that the people were treating this as a comparatively static exercise you would expect a large impact on investment because that's a marginal - you know, a marginal effect on capital stock and a relatively smaller effect on employment. That in broad terms is what we see.

If we're expecting an extrapolation of current trends - you know, people saying, "What are you going to be doing over the next few years?" - I would have thought we would be saying, "Well, we will be substituting capital for labour." So I would be expecting to see very few people responding with a reduction in investment, and we would see the investment figures going the opposite way from labour.

What we see in the survey might be consistent with people saying, "If your output bias was reduced by 5 per cent or whatever, the equilibrium of that would be what would be the impact of that, all other things equal." That would be consistent with the fairly large impacts on investment that are in the surveys, and in that sense the employment results, I think, can be interpreted as impacts of that change specifically, not impacts of the general process.

MS RIDOUT: I would add to what's been happening in manufacturing in terms of prices. In the last 12 months manufacturing prices went backwards by 0.7 per cent, I think, in Australia. Really throughout the 90s pricing power has been lost to the manufacturing sector and that hasn't necessarily been an Australian-own experience. We have experienced huge margin pressure, and that's irrevocable. I mean, this is the world of competitive manufacturing. So every change in your cost structure has an impact on your company.

Now, I know the question was asked very directly about the impact of the tariff on their investment and on their employment. Whether they saw it as another straw on the camel's back - I mean, in a sense it's like what John was saying, that might be the case, but I think that really the question was very direct about the five to zero.

MR HERBERT: Yes, I think you could probably get some comparison too with our most recent survey where we looked at the industry sectors in some depth, but they were just asking more about the outcome for the December quarter and a look at the March quarter for this year where the figures on employment and investment were quite markedly different to the question we posed here about the impact on the tariff.

MS RIDOUT: Yes. I mean, you would have to say that investment has been reasonably flat in the sector, as has profitability, I might add. It hasn't been anything too flash.

MR WOODS: Yes, but also tied up in part with the particular part of the economic cycle that the economy is in. Again, in any one of these surveys, of course, the manufacturer out in delivery land there has many competing things to try and grasp, and it's a matter to try and sort out what impact is a consequence of a particular action, as you would well be aware. Where is it possible through your survey techniques to show that you've teased out the singular impact of tariffs?

MS RIDOUT: I think in a sense it's very hard to single out the impact of tariffs. I mean, in reverse, I suppose, the reduction in tariffs is often given credit for promoting a massive increase in productivity and global orientation in the industry.

MR WOODS: Challenged by some - - -

MS RIDOUT: Yes, that's right. But you could also say that there are a number of other factors operating coincident to it, like the exchange rate, the growth in Asia, and we've been fair in giving both a proper view. But if you look at the analysis of the performance of the manufacturing sector during the 90s when the technical point was reached at about 15 per cent, I think in 1992 in terms of tariffs, you really have seen the industry - and we quote the figures here - grow during the 90s at 2.1 per cent per annum compared to a 4.1 per cent economy-wide growth, and that's even when the downturn of the early 1990s is excluded from the figures.

So the manufacturing sector has hung in there and it's increased its exports by 117 per cent during that period, well above the growth in world trade in manufactured exports. So we've actually bettered the world trend, but the industry has faced extraordinary competition. The market is more contested. Our import penetration has doubled during the decade, but it's really been a very sharp end felt by the sector.

Also this issue of pricing power and the pressure on margins caught up in global trends with overcapacity existing right around the world. Big corporate operations in Asia and not shutting them down elsewhere, the drive for productivity, the Uruguay Round has all put pressure on Australian manufacturing as it has on world manufacturing. Our industry has responded positively, but at the same time it is going through a tough period and rationalisation is resulting from that.

MR WOODS: Is an assumption made in the survey that a 5 per cent reduction, or a reduction of the 5 per cent to zero, would fully flow through to end consumer prices, because we've had various representations which suggest that there would be some absorption of that on the way through from time to time?

MS RIDOUT: The survey shows, commissioner, that for 58 per cent of respondents input costs and selling prices would be expected to fall by a precise amount. So I mean in a sense I think there is a fairly strong flow-through in the effect on companies. But certainly we can take that question on notice and give you some more information.

MR WOODS: Is that a result you would expect, Prof Quiggin?

PROF QUIGGIN: Well, I guess you would expect some general equilibrium effects, but I suppose looking at the aggregate impact it seems to me - although this is a bit larger than what I used in my calculations, we're still looking there - that's between one and two which seems a plausible response. It's very difficult to work out what judgment the manufacturers have made as regards where that 5 per cent is going to fall, but, of course, they have had considerable previous experience in reductions in tariffs, so presumably they're not - obviously their mental model is presumably not way out of whack, and certainly the aggregate numbers seem to me to be plausible-looking sorts of numbers for the kinds of impacts you might expect.

MR WOODS: I look forward to exploring that and having a good look through the results and the assumptions. There was a reference made, Mr Herbert, in your opening comments and Mr Purnell reinforced it to the effect that Australia is one of the most open markets, if not the most open market, in the Western world.

That then draws my attention to your second recommendation that if we are the most open market what is the effective negotiating coinage? What value does one give to it of proposing a reduction of our general tariff from five, whether it be to three or zero or whatever, to try and encourage other countries to bring their tariffs down? I mean, if we are already open then what are we offering as part of this argument of reciprocity?

MR HERBERT: Do you mean almost it doesn't matter any more?

MR WOODS: Well, that's the question. I mean, I was drawing on your comments that we're the most open market, and if so, I then ask myself are we offering anything, and particularly when you look at Australia in terms of world trade, and you look at the tariffs already in many areas like Japan, the European Union, the US which are as low or in some cases lower than ours if you take the FOB and CIF debate, etcetera. What are we offering?

MR PURNELL: Can I intervene?

MR WOODS: Please.

MR PURNELL: Firstly, of course, we're not talking about idealism here, we're talking about hard-nosed trade negotiations, and we still have five percentage point tariffs, and even though on all the figures and tables we're able to produce we're showing that tariffs are very low at the bottom end, when you add in non-tariff barriers Australia is really absolutely very exposed, and when you get developing economies which are part of APEC, and this is the basis of supposedly our APEC commitment that we've got this thing under way, Australia is very open, but we still have 5 percentage points. So you can talk the moral persuasion argument which can be one argument that you would like to pursue, and I know that is an arguing point, but in hard-nosed terms we have five percentage points left.

We have the APEC economies and the WTO, but on all the evidence that we can provide, and I think the commission would agree, we're lagging in multilateral forums in terms of trade reductions. If we unilaterally put our last five percentage points on the table, firstly there is no indication at this point on where the world trading negotiations are going, that WTO or APEC economies will follow - point number 1. The second point is that even if that is a reduction then all the non-tariff barriers and other issues are still there that are going to affect our exports and won't be caught up even in that more transparent trade negotiations/tariff reduction program.

So on either counts we would say this is not the time to do it. Then if you said not only reciprocal but proportionate, we're going down to zero, it's virtually the only protection we have left, and margins are tight, and this five percentage points does count for companies. As we have seen in that power transmission issue with companies with the information technology instance just recently, every percentage point does count if it's there to help Australian industry against imports.

So it's not the time. Other economies are not going to follow suit, we believe. Certainly in the international forum it's not happening, and if it's the tariff we've got no non-tariff barriers, we are totally exposed, and if there was a proportionate response by other economies then there would have to be massive reductions by many economies to get down to zero.

MR WOODS: Absolutely.

MR PURNELL: Which is where we'd be at. So we believe the arguments are very strong and the evidence is there to support us. Now is not the time for a unilateral move. It gives us nothing. We should be in world forums. We strongly support the fact that, as we said in our statement, we have everything to lose and nothing to gain from the world being protectionist or reverting to protectionism, but we believe that as part of world negotiations to throw away unilaterally at this point when all that evidence is there - as I've said, not the time. We don't get the maximum benefit. We don't achieve the best outcomes for the Australian economy.

MR HERBERT: I might just add as an aside that using this argument, before this review was announced, we were unsuccessful. We tried. So now is not the time, because of the very point you've just made, to proceed with the review. I make the aside we weren't successful.

MR WOODS: Yes, I understand your initial reactions to the review. Is it a matter of ultimate judgment as to whether, given our openness, those five percentage points count, and if so how do you weigh that up? What do you weigh it against? Do you weigh it against on the one hand, if there are any benefits, unilateral, from a reduction in terms of consumer prices, in terms of benefits to business who use imported inputs, offset again on the other side by the work that I look forward to reading which suggests that there are significant adjustment costs that on some analyses may outweigh those other benefits to the economy more generally? Would you agree it's ultimately a matter of judgment, of weighing up the relative effects and importance of those factors to come to that conclusion?

MR HERBERT: I think it is a question of judgment in the sense of, we argue strongly that this must be considered in a holistic approach. You've got to look at the impact in all areas, not just the theory of it; that you have to look at the consequences. We argue very strongly and, indeed, our whole submission intends to give you that broader impact by what impact it would have on our members, what they're saying to us about the broader issues of investment, employment and production. So in making the judgment we say quite clearly you have to take a holistic approach to this, and that is a very fundamental and underlying theme of our submission.

MS RIDOUT: I'd also add, Mr Commissioner, that really if you just look at it in a purely technical sense, as John Quiggin has done, I think his point that the 5 per cent to zero is a linear thing in terms of adjustment costs but a diminishing effect in terms of welfare benefit to the economy, is a very powerful argument. Our survey tried to put some flesh on the bones to those adjustment costs, and I think they are fairly strong figures - they even surprised a lot of us - and it does warn you that the industry is fairly precariously poised in Australia. It's rationalising rapidly. It will respond to whatever signals it receives from the market in Australia, and has been doing it, and we don't want to do anything to accelerate the further reduction in the manufacturing capacity of the Australian economy.

Arguably, we should be trying to strengthen it and, if we make it less competitive, we'll get more importing, more branding of products, with all the consequent effects on the economy that that will bring. You've got the narrow economic cost and then you've got the broader economic and social costs that go with that. So it is a balancing act.

MR WOODS: Let's move then to the practical implementation of such a policy. If we're talking about reciprocal and proportionate, how in practice would such an arrangement work? Presumably we can't do it country by country because we're breaching the most favoured nation status arrangement. Presumably you wouldn't want to do it industry by industry because of the various anomalies that would throw up as to who's in, who's out, who has it and who doesn't, and the negative protections and all of that debate that we all understand so well. How, therefore, would you propose that the government would assess some level of progress on reduction of trade barriers - let's not talk tariffs, let's talk barriers more broadly - by other countries that would cause it to then say, "All right, sufficient has been done that we will then move to either 3 per cent or zero," or whatever is the next step?

MR PURNELL: I think that in either forum, but if we took the APEC forum we have world leaders there. I think the Australian government would, firstly, proceed to just put the evidence on the table; the material that we've put here before this inquiry and a lot of other information that they have. I think the factual position shows that Australia stands high in terms of its openness in terms of world trade and other economies with their tariff and non-tariff barriers. That's a very strong point that I think could be presented.

The second position that we would put forward is that other economies, based on that analysis, need to catch up. I don't think it's rocket science in a negotiating sense to talk about our APEC commitments being 2010 and 2020. If you look at the commercial reality of many companies 2010 is a long time away for many companies. Even on that time frame I think many companies in a commercial sense would feel that's a very long way to wait anyway for other economies to catch up with us. So I don't see it as a very technically difficult negotiating position. I think the facts speak for themselves. I think that through the APEC forum or through the WTO - and clearly that's going to take longer to even start to get down to this level of detail - we can put the facts there and hold our head high and say that we have achieved a lot and it is time for other economies to match us. When you have tarification of non-tariff barriers, then I think our credentials are very strong.

MR WOODS: Yes. Tarification certainly brings them to the - crystal clear. It is, as we were discussing before though, a matter of judgment, and I'm reminded of a submission by Monsanto that is available to you - it's on our Web site - which said that:

> On the general issue of tariff reductions and their usefulness in multilateral trade negotiations, we believe any perceived leveraging opportunities from the 5 per cent level would be negligible. It's believed that around 80 per cent of Australia's imports already attract duties of 5 per cent or less and at these levels the Australian market is generally perceived as highly accessible -

which is a view that you share as well. So we will need to weigh the various perspectives and views of organisations.

MR PURNELL: Can I just add that the one point there is, where there are tariffs still remaining they're often on sensitive issues, and that's why they're still remaining, and if you look at tariff peaks of course you find that's exactly the case; where that tariff exists at higher levels than the average, it's because the products are often highly contested globally, where there are particular domestic reasons why you'd want to have that protection. So there are competitive issues for other economies to be looking at that and saying, "While it might be minimal, you still do have some negotiating ability by keeping it or trading it in the most rigorous fashion possible."

MR WOODS: We've had an amount of evidence put to us by various witnesses that the previous tariff reductions they have considered to have been significant in the various restructuring they've gone through and that they've in fact described positive values to some of that restructuring process for their industry perspective, although there is a whole-of-economy perspective in terms of employment and adjustment costs and the like that one must also take account of. But then to turn back to a body that rather than industry-specific is slightly broader, the Australian Chamber of Commerce and Industry, in their submission they state in part that:

> The ACCI recognises that there are benefits to the Australian economy from unilateral reductions in tariffs and believes that Australia should continue to reduce tariff duties -

although they, as you do in your second recommendation, go on to argue that although there are such large benefits from unilateral reductions, such benefits would be, in their words, "vastly increased if there were simultaneous reductions in protection levels by our trading partners". So I look forward to reading your submission in the light of other submissions to us, where there is apparent weighting given to the benefits of tariff reduction over and above the welfare and other costs. But I don't know if you have any initial comments you may want to make.

MR HERBERT: Just in a general sense. We, too, would look forward to looking at the ACCI submission to see whether they've introduced the same evidentiary material that we have with our survey, and the view that they've formed and how that was derived. Was it from their member constituents, because the ACCI of course is made up of a range of individual organisations, not companies. So we'd look very carefully to see how they came to that view.

MR WOODS: Yes, I look forward to the debate.

PROF QUIGGIN: I'd like to comment a bit on the argument as I understand it, which is that the pressure of the tariff cut forced these companies to undertake restructions which were then positive. The first point implies that the pressure they're supposed to feel of maximising their returns to their shareholders didn't lead them to undertake this restructuring without this external shock, which is I think problematic. If there are profitable restructuring opportunities available, why are these firms not taking them until they're forced to in some sense by government? If you take the logic of this, should the government be cracking the whip over companies in general who are doing well in order to get them back on their toes? I think it's an argument which leads you in some very interesting directions which, in general, I've found people aren't willing to pursue once we start down that road.

Secondly, I think in terms of the response you get and, accepting that shocks do obviously lead to certain sorts of restructuring, I think that it's now on a selection bias in the responses; that is, undoubtedly a significant number of companies have exited these industries. I doubt that they're the ones who are being - or the former employees and former managers of those companies - asked whether the restructuring was beneficial to them and, indeed, there may well have been companies which might in fact have had reasonable long-term prospects of adjusting but didn't successfully handle the restructuring exercise, and therefore had a negative shock over and above the long-range general equilibrium impact. So I suppose on both of those counts this sort of argument must be viewed with a good deal of scepticism.

MS RIDOUT: Can I make one comment to you. When you look at the Reserve Bank literature about what got manufacturing into export, that comes down on exchange rate issues - very strongly - and I think we always have to leave that in mind. As I said in my comments, the 90s was a different world, and manufacturing with some prodding undoubtedly from tariffs and having to find a living, but actually the opportunity was there to be competitive in growth markets, and 50 per cent of the growth in manufacturing came from the margin in Asia which was one of the reasons why manufacturing exports fell in a hole in 1997. So it's very hard to attribute what happened solely to any one issue.

MR WOODS: Which was the debate we were having about your survey as well.

MS RIDOUT: That's exactly right.

MR WOODS: To make sure that we were trying to - - -

MS RIDOUT: Yes, and we're not trying to be unbalanced about that, commissioner. We're just saying, if you look at that work done then by them - - -

MR WOODS: Which we will, with great interest. Thank you for doing it. I'm not sure that we can take the debate significantly further until we've had the opportunity to read your submission, but I look forward to doing so and, as appropriate, we'll undertake a follow-up. Any concluding comments you wish to make?

MR HERBERT: Nothing in particular. I don't think we need to add more, except just one of a technical nature you would have observed on page 15. We have just discovered there are a couple of typographical errors. Is it appropriate to convey them to someone to make sure that the record is corrected?

MR WOODS: Yes.

MS RIDOUT: There are two tiny words which are just - - -

MR WOODS: Yes. Our staff will fix it.

MR HERBERT: But thank you for listening to us. As I've said, we would be pleased to come back if you so desire at a subsequent time.

MS RIDOUT: I'd just like to make one comment. I think the issue of the 5 per cent as a buffer in a floating exchange rate regime is a very very important issue that needs to be looked at as part of this argument. We do know that the Malaysians have a view that free trade in a floating exchange rate regime is closer to 10 per cent tariff, so I think it is a new argument, given the new world, and it would be very interesting to me if the commission was heard about that issue. We've tried to deal with it with Prof Quiggin but, as he said, the literature is fairly early on it but it's certainly an interesting one given the global world we're now dealing with.

MR WOODS: Perhaps we could conclude on your definition of what constitutes free and open trade and investment, I think is the correct phrase. Do you have a view on - - -

PROF QUIGGIN: I guess, rather than go in for a definition, I would make the point that the two issues are interlinked and to the extent that there are clearly deviations from the assumption of market perfection on the capital side, and I think the evidence of the last few years strongly supports that view, that creates a big range of second-best issues with regard to the appropriate trade policy. But if we can't assume that financial markets are going to get the exchange rate right, and I think it's pretty clear that we can't, then we can't reasonably say that a zero tariff means that the principles of comparative advantage are always and everywhere operational as far as the goods market goes. But there clearly can be significant and sustained deviations from the prices that a comparative advantage would involve.

MR WOODS: I think that's a useful point to end up on. Thank you very much.

PROF QUIGGIN: Thank you.

MR WOODS: Our next witnesses are due at 2 o'clock, so we'll have a short lunch break to that point.

(Luncheon adjournment)

MR WOODS: If you could give your name and the capacity in which you're presenting evidence today for the record, please.

MR JACKSON: Good afternoon. My name is Tim Jackson. I am the director of commercial affairs for the Scotch Whisky Association. I'm also wearing a second hat as chairman of the trade committee of the European Confederation of Spirits Producers, and accompanying me is Mr John Halmarick who is the chairman of the Scotch Whisky Association Advisory Group here in Australia.

MR WOODS: Thank you, gentlemen. We've received back not only the Scotch Whisky Association submission but the other that you referred to. Are there some opening comments that you wish to make?

MR JACKSON: Well, thank you very much indeed, and I'm most grateful for the opportunity to appear here today. I'm only sorry that I seem to have brought the Scottish weather with me for the last three or four days.

As I've explained, I'm wearing two hats. The Scotch Whisky Association is the representative body of the Scotch whisky industry. It is a very important industry to the economy of the UK. It's one of the top five exports from the United Kingdom. It's exported to more than 200 different countries to the value in excess of $A5 billion each year and Australia is the industry's 13th most important export market, with annual exports valued at $A91 million. My second hat is the European Confederation of Spirits Producers. CEPS is its name. This is the representative of the European spirits industry. It consists of 36 national associations, including the Scotch Whisky Association; producers of cognac, other producers of brandy, gin, vodka, ouzo. You name it, we represent it. All the 15 EU member states are members.

We also have observer members from those countries in Eastern Europe who are potential members of the European Union, such as Hungary, Czech and Slovak Republics. We also have partner associations. These are the major spirit associations from around the world that represent their respective industries. We have DSICA here in Australia, the Distilled Spirits Industry Council of Australia. We also have DSANZ in New Zealand as a partner. We have the Association of Canadian Distillers, the Distilled Spirits Council of the United States as well as representatives from Japan and Mexico.

That is very important to us because of course spirits are internationally traded products, so it is very very important that we have this continuing liaison and cooperation with our friends throughout the world. I would like to reiterate unequivocally that both the organisations that I represent here today are strongly in favour of tariff elimination for all imported spirits. Here I think it is important that we just mention that we're talking about the 22.08 category and we're talking about products such as brandy, gin, rum, vodka, whisky and liqueurs. The reasons have been set out in both the submissions but I would just like to highlight the key points if I may.

MR WOODS: Please.

MR JACKSON: The first point is that the revenue derived from import duty on spirits we would say is insignificant. It is only some $A11 million out of total revenue raised through excise on all spirits which, I am told, is in the region of some $A870 million. That of course excludes sales tax. It is also widely felt that the administration and compliance costs associated with the collection of the revenue from a 5 per cent tariff are significant both to the government and to the industry. We would also contend that the domestic industry has no need for protection from the tariff which I am always intrigued is entitled "the customs protective element" in the duty tax regime.

As you would have seen from our submission imported spirits account for nearly 80 per cent of the total spirits market here in Australia. A high proportion of those imports are imported in bulk by Australian companies for processing, bottling and distribution to the benefit of the Australian economy in terms of investment and employment and, if you take the case of Scotch whisky, some 60 per cent is imported in bulk for that purpose. It is also of specific note that there is no local production of whisky. All whisky on sale in Australia is now imported.

In the case of the domestic market there is some 20 per cent held by domestically produced rum and brandy. We contend that the 5 per cent tariff affords them very little protection and in effect has very little impact, as well. In the particular case of brandy it is interesting that this product benefits from a more favourable excise tax rate than all other spirits in the category and even despite that I understand that its market is declining here in Australia. In the particular case of rum I understand that a large quantity comes in duty-free from the developing countries and then if you take the case of white spirits there are many vodkas and gins that are coming in currently from New Zealand tariff-free, as well.

I think the other point is that in the case of brandy and rum if one was looking at the actual overall effect one is essentially talking about, so I am advised, 22 cents a bottle out of a retail price of some $22. That is a very small amount but, even if small, obviously if that tariff could be removed that would naturally be passed straight on to the benefit of the Australian consumer. We find it significant that so far as we're aware the Australian domestic spirits industry - in particular the brandy industry - has not filed any comments with the commission. We like to think this is because the industry here in Australia sees any question of protection to be something from bygone days and their emphasis now is much more on the development of a sustainable, prosperous and competitive industry producing high-quality and competitively priced goods to consumers and also perhaps with consideration being given to the significant export opportunities that exist for their products throughout the world.

I think the other point we would wish to make is that tariff elimination would bring Australia into line with commitments made by some of its leading trading partners. Canada, the European Union, Japan, New Zealand and the United States have all eliminated their tariffs as a result of a Quad agreement following the Uruguay Round of world trade negotiations. There have also been cases where countries such as Taiwan and Hong Kong have eliminated their tariffs. There have also been recently agreements to show that the international trend is towards tariff elimination in our sector through the negotiations between the European Union and South Africa to eliminate import tariffs on spirits. Very recently as well there has been an agreement between the European Union and Mexico to eliminate all spirits tariffs and it is a known fact that the European Union is about to start negotiations with MERCOSUR with a view to doing exactly the same.

We would also like to take the opportunity to point out that we understand our US colleagues from DSCUS, whose name I mentioned earlier on, have also made a submission in support of tariff elimination. This, they believe, would bring Australia into line with the APEC commitments on tariff elimination. We would also like to point out that in our view the tariff would not seem to be significant enough to have any impact in any future bilateral or multilateral tariff negotiations. Of course it is easy for industry to say that. The people actually dealing with it may feel differently, but we would suggest that a 5 per cent tariff is pretty minimal in terms of negotiation.

Finally, with respect, we do believe that elimination would meet the Australian government's policy objectives as outlined by the Productivity Commission in its paper. In conclusion I would like to thank you again for the opportunity to be here today and also to reiterate that both organisations which I represent are strongly in favour of the earliest possible tariff elimination for imported spirits. Now, with the assistance of my good friend John Halmarick, I will be happy to try and respond to any questions you might have.

MR WOODS: Thank you. I have before me both the Scotch Whisky Association's submission and the submission by the European Confederation of Spirit Producers and I notice some convergence of perspective by - - -

MR JACKSON: We are of course a member of the European Confederation.

MR WOODS: Yes. If I can pick up a couple of points - one in terms of the Scotch Whisky Association. You do us credit by saying we're the 13th most important export market but what does that mean in terms of actual percentage of production that comes here? I mean, presumably your largest markets have a very great level of consumption. Is a reasonable way of judging that to look at the 5 billion versus the 91 million figure to get an understanding of where we sit in terms of proportion of total consumption of Scotch whisky?

MR JACKSON: I can't here and now give you the exact sort of breakdown but we are talking, as I mentioned earlier on, about a figure of exports of 91 million to Australia and that against a total figure of exports of 5 billion in Australian dollars.

MR WOODS: All right, so that 5 billion is exports, not total production.

MR JACKSON: That is exports of Scotch whisky throughout the world. Then of course there is - - -

MR WOODS: So that's not for the domestic consumption.

MR JACKSON: That would not include the sales of Scotch whisky within the United Kingdom.

MR WOODS: Rough idea of what that might look like?

MR JACKSON: The figures, off the top of my head, essentially two-thirds, 70 per cent, of all Scotch whisky is exported around the world.

MR WOODS: That's enough to give me an understanding of where we sit in the scheme of things. You refer to there being no domestic production to protect with tariffs. Obviously there's no domestic production of Scotch whisky, but it raises the question of substitutability, I guess, first within the brown spirits category and then more broadly within the spirits category more generally. In that context I draw your attention to a submission by the Winemakers Federation of Australia, because one of their components is the Australian brandy industry. They have been picked up through that submission, so you may, at your leisure, like to go back into our Web site and pick up that submission. They don't actually address brandy, but they have been encompassed in a broader umbrella. But what are your views on the question of substitutability picking up, I guess, within the brown spirits first and then spirits generally?

MR JACKSON: Well, I think the first point to make is that all spirits, be they Scotch whisky, brandy, gin, vodka, all compete with each other. Indeed all alcoholic beverages, be they spirits, beer, wine, all, at the end of the day, compete with each other in a fiercely competitive market. In the particular case of spirits we believe, and this has been proved to be the case in WTO cases concerning internal taxation regarding Japan, Korea and Chile, that all spirits, at the end of the day, are not only like products but essentially directly substitutable and competitive with each other. So we feel very strongly that all spirits compete with each other in the marketplace and, for that reason, it makes sense for the import tariffs on all spirits to be eliminated.

I think if you were to consider the particular case of Scotch whisky here in Australia there is, of course, no local production of any whisky. So, in a sense, Scotch whisky is only directly competing with American bourbon which is the other prime whisky imported into this country. So essentially, Scotch is competing with everyone in the alcoholic beverage category, in particular with all other spirits but most particularly with other whiskies and other products in the brown spirits category. I don't know if John would like to add anything to that.

MR HALMARICK: No, that's pretty right in terms of the market demographics. Brown spirits are the dominant spirit, and there's certainly a competition between Scotch, bourbon and rum in the different age groups. Scotch is more in preference towards people who are a wee bit older, than bourbon, and rum has a peculiar consumption pattern depending on whether you live in Queensland or other parts of Australia.

MR WOODS: But I guess I should understand your comment "thus there is no domestic production to protect with tariffs" - I should read that in the context though that there is competition within the brown spirits, and therefore in that sense there is potential competition with Australian-produced brandy.

MR JACKSON: Indeed. I mean, we compete with all other products containing alcohol.

MR WOODS: That's helpful. That just puts that sentence into a broader context. You also make the point that the costs associated with the collection of revenue from such large tariffs, the 5 per cents, are significant both to government and the spirits industry. Is there any chance of quantifying the cost of administration of the tariffs?

MR HALMARICK: I suppose there could be. It would take a little bit of a while to get it together but there are costs in compliance time with customers. There are certainly costs in compliance times with people who have got to - people who import the product in have got to record all the information separately from the excise and other duties. But I couldn't actually tell you off the top of my head what it would cost.

MR WOODS: If on reflection, as you leave here, you thought it was possible to pull together some figures, that would assist.

MR HALMARICK: Yes.

MR WOODS: We understand your general point.

MR HALMARICK: Yes.

MR WOODS: But until it has some sort of values wrapped around it it's hard to give it a weighting that - - -

MR HALMARICK: Yes, we'll try and get some relativity to that 11 million that was actually collected.

MR WOODS: That would be most helpful. It will be important to differentiate between just complying with customs generally, which will need to occur anyway, versus the element that relates to the tariffs specifically. I don't want to try and confuse those two.

MR HALMARICK: No.

MR WOODS: But, you know, to the extent that it's possible within reasonable resources - - -

MR HALMARICK: There are different forms of returns required.

MR WOODS: Yes.

MR HALMARICK: Different types of paperwork, extra computer time. There are quite a lot of costs.

MR WOODS: Yes. You make several points about tariff-free access for distilled spirits around the world, and you talk about the Quad country agreements and the like. You then take a jump to saying that there is a strong nucleus of international support for the principle of free trade. Now, that's quite a jump from tariff-free, when one reflects on excises, sales tax, prohibitions, restrictions, regulations and all the other things that surround your particular industry. Is that a very big jump?

MR JACKSON: I would not say so necessarily. I mean we, as an industry, devote a tremendous amount of time, energy and resource to tackling a plethora of tariff and non-tariff barriers that we face around the world. These can either be tariff rates, they can be discriminatory tariff rates, there can be taxation levels, there can be discriminatory taxation, as I explained, as the industry has managed to secure three successful rulings in separate WTO cases in Japan, Korea and Chile, problems of importing licensing quotas and so on. So we devote a lot of time to trying to improve the general climate in which our members are trying to sell their products. At the end of the day we are not seeking any special treatment for our products.

What we are trying to do is to ensure that the terms of trade are fair as between the various competing products, in particular in the case of domestic versus imported. Naturally if it is possible for us on any occasion, with the help of our government, with the help of the World Trade Organisation to secure, through a specific initiative, tariff reductions in our major markets which essentially has been the case up until now, this helps us to ensure that - I won't say that it is free trade, but it essentially means that we are able to trade without discrimination, without any restriction. We are not saying that, sadly, there will ever be a day when we will not have excise tax on our products.

I think though that there is, increasingly, recognition in our sector that as we already are subject to excise tax in every country in which we sell our product it really is unfair and unreasonable for us also to be penalised by the imposition of import tariffs. So, sadly, we will never have a day when we don't have any excise I fear. What we will have I hope, is a time when, in accordance with the general international trend, governments will decide to eliminate import tariffs, and that has certainly been the case in our sector of late.

MR WOODS: Thank you. You have an attachment to your submission where I notice, I might say with a tinge of sadness perhaps, that the free-on-board price of $6.89 ends up at $40.65 for the price to the consumer. A couple of questions: one is are we talking there about a bulk import that must then go through a local bottling process, or are we talking there about pre-bottled? Presumably there is more cost transference and activity in this one, or is it just a generic model?

MR HALMARICK: Actually this example is based on a litre bottle, which is not the standard size here, 700 mils is about the standard off-premise.

MR WOODS: It will do.

MR HALMARICK: But anyway, based on a litre bottle.

MR WOODS: Yes.

MR HALMARICK: It would be based on bringing bulk spirit out here and bottling. However, the costs of bottled in Scotland, if you like, or bottled in the United States, whiskies, landed here, are virtually the same as if one bottles it in Australia. That is because most of them bottled in Scotland or bottled in the United States are big brands and they have the savings and the costs of providing or bottling for lots of parts of the world. In fact bringing out bulk whisky, or bulk anything you like, in a container, it's about the equivalent of three times the quantity in case goods.

MR WOODS: Yes.

MR HALMARICK: But the saving there is offset by the savings in bottles and production costs.

MR WOODS: Yes.

MR HALMARICK: So that it's basically the same.

MR WOODS: Okay.

MR HALMARICK: I mean the significant costs are in excise and sales tax.

MR WOODS: I can see it well.

MR HALMARICK: Unfortunately.

MR WOODS: Why I draw attention to this is that you made a comment that if there was a reduction in the tariff, that - I think your words were - would be passed directly to the Australian consumer. In this particular example are you suggesting that the market pricing is such that the $40.65 would immediately and fully drop down to the $40.31, or are you suggesting that also there are mark-ups that pick up that figure and that the reduction to the consumer would even be greater? Or is it in fact a feature of the industry that they pick price points, depending on where they think that the market will bear a price and depending on their advertising and their marketing strategies?

MR HALMARICK: Realistically the marketplace off-premise prices goods - spirits usually ending in 95 or 99 cents, so it's $20.95 and the next price point is $21.95 or thereabouts. But what would happen for instance, in this case, as with any other savings that comes along, one would, as a manufacturer and wholesaler, reduce the wholesale price by whatever the savings are. The wholesaler who distributes to the retailer would have a fixed margin, so those prices would come down. It would then be up to the retailer to adjust his margins. Obviously people who are wholesalers can't tell retailers what to sell their goods for under the Trade Practices Act but one would hope that that same reflection - a cost saving - would be passed on to the consumer. It would mean the customer getting it from 21 to 20 dollars or something of that nature.

However, under GST the whole ballpark is going to change and the proposal of the government is to increase excise by some 45 per cent over the current figures to compensate for the loss of the 37 per cent sales tax. It's possible that the prices at retail won't just ordinarily roll up to 95 or 99 cents, particularly given there's a bit of a problem with rounding up anyhow, and one would imagine in the future that price points would be much more variable through the whole spectrum, and it would make it so much easier then to pass on 20, 30 or 40 cents a bottle.

MR WOODS: All right. Thank you, that helps. You make the point that tariffs under consideration are very low at 5 per cent or less, and then you go on to say their value as bargaining counters is therefore relatively small. There is a lot of debate generated on that particular issue, and I have other submissions which take the same view as yourself, and others who argue that having this as a last negotiating lever is worth a considerable amount and that we can exercise a lot of influence in the international market. Would you like to expand on your point that you make there?

MR JACKSON: I would simply say that if one compares the position here in Australia with other countries around the world, one has to say the tariff is on the low side. I would simply suggest that if against a background of - in our sector the government already unilaterally, as I understand, having reduced the import tariff on spirits in recent years, already having made that move, and having reduced it down to the current 5 per cent, that in the overall scheme of things is not a major bargaining chip for a government negotiator to go into any negotiations with. I can understand that perhaps when you have in the palm of your hand a sort of high import tariff and there's someone pushing very hard to reduce that, with that tariff you have a greater card to play. But it would seem to an outsider that if you had a very low amount, that actually is not going to be a big card to play.

MR WOODS: Thank you. I have completed the particular matters that I wish to raise with you in relation to these two submissions but are there any concluding comments that you would wish to make?

MR JACKSON: I would simply like to thank you again for giving me the opportunity to represent the Scotch whisky and European industry's views on this issue. We feel for all the reasons explained in our submission, and expanded on today, that there are significant grounds for eliminating the tariff. We very much hope that this will be the case and that the tariff will be eliminated on all imported spirits as soon as possible. Finally, it goes without saying that if there is any further assistance or help that the commission would require in addition to the information you have requested, we would be very delighted to produce it for you.

MR WOODS: Thank you very much, and I trust you enjoy Australia's summer.

MR JACKSON: I look forward to it.

MR WOODS: The next witness is the Australian Stainless Steel Development Association. Could you please state your names and the capacity in which you are presenting evidence today.

MR MATHESON: My name is Richard Matheson. I'm the executive director of the Australian Stainless Steel Development Association. I have with me a member of my association, Mr George Finlay. Mr Finlay represents a company called Stainless Steel Tube Mills, a substantial consumer of stainless steel flat products, and he has some experience in matters in relation to importation as well.

MR WOODS: Thank you very much. We have your submission and have read it with great interest. I have some matters that I wish to raise with you but do you have an opening comment that you may wish to make.

MR MATHESON: Thank you, Mr Woods. It's not my proposal to go over the submission in any detail but I would like to raise just a few points. Our submission deals with removal of the policy of the federal government to impose a 3 per cent tariff on imports for business inputs under the TCS arrangements. It is aimed at flat products of the stainless steel market. These are intermediate goods. In all its objectives ASSDA deals with these materials more than any other.

The stainless steel industry is important in its own right but it is also a vital supporting industry for many other important Australian industries. These include the food and beverage production preparation industries, mineral and energy production, transport, pulp and paper and a number of others. Stainless steel flat products are no longer produced in Australia. When they were, production enjoyed a very modest tariff protection at around the 5 per cent level. Many of the advantages provided by the producer to the local industry have been lost and we're not sure yet - stainless steel cycles are quite long, and we haven't seen the full impact of the loss of the local production yet in my opinion.

In regard to substitutes, in the majority of applications stainless steels are used for their particular qualities, these being durability, corrosion resistance, hygiene, safety and environmental issues. These qualities are typical of stainless steel or more exotic materials that are largely not made in Australia and I guess those more exotic materials are more expensive than stainless steel. Substitute products lower the efficiency of consuming industries, either on an initial cost basis or on a life cycle cost basis which is why stainless steels are used.

We believe that the removal of the 3 per cent tariff imposition would improve the overall efficiency of the Australian economy. In 1996 we were told the 3 per cent TCS arrangements on imports for business inputs was industry's share of the pain for overcoming a budget deficit problem. The budget appears now to be in surplus, so this original imperative for the tax appears to have gone. The 3 per cent adds inefficiency to our industry by providing an advantage to foreign competitors and adding cost. While this has been going on we've lost our local producer and that has added complexity, it has added time and it has also added costs to our consuming sectors which have compounded the situation.

We believe that the removal of the 3 per cent will encourage the development of sustainable, prosperous and internationally competitive industries in Australia. Stainless steel is consumed, obviously, by many viable industries here. If we look globally, growth and consumption of stainless steel stands at between 5 and 6 per cent per annum year on year since 1950. I don't know of any other material to have such a sustained prosperous growth over such a long period of time. This growth has accelerated in the last decade and there is no foreseeable reason why this trend will halt internationally. Stainless steel is certainly prosperous.

Australia has some good-quality industries, such as a very significant food industry and a number of others, on which a world-class fabrication industry could be based. Australia already has a substantial stake in the stainless steel industry globally through our very substantial nickel production facilities, virtually all of which is consumed in the stainless steel sector, and Australia has grown from being the third largest producer of nickel in the world, well on its way to being the majority producer of nickel in the world. We also obviously have very substantial iron resources which we export, some of which ends up in the stainless steel industry. We also have a substantial stainless steel scrap industry all of which is exported into stainless steel mills.

We believe that removal of the 3 per cent tariff will promote the provision of high-quality, competitively priced goods and services to Australian business and consumers. The tariff is simply factored into the price and passed on to the consumer in the case of the stainless steel industry, or at least in the case of the majority of it that I can identify. Because the stainless steel input is usually a high cost component of the ultimate product, removal of the tariff will have an influence, and often a significant influence, on the price of products.

Our recommendation to the commission is one of fairness for our industry in that you recommend to the government strongly the removal of the TCS arrangements around the 3 per cent.

MR WOODS: Thank you, and thank you for the submission, which goes into those matters in some further detail. We had BHP as a witness earlier in the day and I quoted them an extract from your submission in relation to the closure of their stainless steel production. They referred to that decision having been in train at the time of the announcement of that 3 per cent, that it sort of reinforced in their mind that that was an appropriate decision on their part.

Could I say, in that section, in background, you present what I consider one of the better and most clear descriptions of the benefits of having a local producer where you discuss things such as short order lead times, the ability to supply small orders, quality service, also having a supply of product that can then be drawn on, etcetera. I found that very helpful as a description of some of the positives of having local producers.

You talk in your submission about the departure of BHP has meant that some of these advantages have been lost with cost implications to the industry, and then in your overview today you talk about cost, time and complexity. Can you provide any more detailed evidence to the commission on the sorts of costs, times and complexities that are involved, having gone through the transition from being able to draw on a local producer in the sense they converted one product into a more usable product for you, to now relying on imports only? If not today, then if there is any supplementary information you can provide to us?

MR MATHESON: There is certainly some supplementary information. You are quite right, I can't provide it to you now, but in terms of lead times, there is very clear information available on that. In terms of the costs of not having a large central local stockpile that can be drawn upon, we have been in a phase globally in stainless steel of what you might call overcapacity which means that it becomes a buyer's market. We're not sure at this point which way the particular worm will turn in relation to capacity utilisation but the forecasts are that in the near term we will see a shortage of capacity in the stainless steel industry globally, and this is the first time this has happened since BHP's departure from the market. So this is where we will begin to see whether or not shortages have a substantial influence in the sustainability of local industries.

I can endeavour to put together some figures for you on our expectations under these circumstances, but where, I guess, a large proportion of the country's stockpile was in the hands of one person in the past, it now resides in the hands of - it could be 20, it could be 40 people who don't talk to each other necessarily.

MR WOODS: Yes. It's just a useful point to focus on, that if you lose local manufacturing capacity, you then lose some of the benefits that you describe so clearly here. So to the extent we can have that teased out in further information that would be particularly useful.

You make a point about the level of stainless steel consumption per capita and refer to Germany of 15 kilograms per head, Italy 30 kilograms per head, Japan 20 kilo per head and Australia sitting around five kilos. What sort of product consumption are they engaging in that we don't or is it in their industry structure where they're different from us, that they have got such high consumption patterns?

MR MATHESON: My suspicion is that they have firstly a culture that's oriented towards life cycle costing. Secondly, their industries are highly export driven, so our consumption figures there are based on intermediate products such as stainless steel flat products, not on end use products such as sinks or dishwashers or these sorts of things. Our consumption may well be higher but it's very difficult to identify it, based on the fact that we may import products from those countries.

MR WOODS: That clarifies it, if you're talking about product which they may then convert into consumer goods which then get exported back out to elsewhere.

MR MATHESON: As you can see though from our appraisal of the market here, much of our consumption is in capital goods. In some industries we're very strong, such as the wine industry; we have very strong penetration of stainless steels into capital goods. In others we are less strong and perhaps in some of those industries we lag behind the world in terms of consumption of stainless steel in capital goods, which has efficiency implications and longevity implications for our industries.

MR WOODS: Yes. I notice your reference there to the wine industry, and you use that as an example. I'd advise that we had the Winemakers Federation of Australia here at an earlier time and, although it wasn't spelt out in their written submission, in their evidence that they presented to us the material they presented was of a similar nature in the sense of the importance of the cost structure of stainless steel to their industry. You made some comment on the CER with New Zealand. What's the relative flow between the two countries and how important is that for your industry?

MR MATHESON: The relative flow is increasing. I can't quantify it for you in tonnage terms. It may be possible in one or two industries to quantify it for you in dollar terms. We are certainly having more difficulty competing with New Zealand, and of the cost factors that we can identify that will assist us to compete, the TCS would be one of the largest.

MR WOODS: It would actually be quite useful, in terms of ranking the various initiatives that the industry identifies to become more competitive, to know where that 3 per cent fits in amongst a range of other initiatives that you have before you so that we can get some relative perspective as well as just the absolute value that that 3 per cent constitutes.

MR MATHESON: We can endeavour to do that.

MR WOODS: That would be quite helpful. Well, that concludes the particular questions I have in relation to your submission, which I may say I found very helpful. Are there any concluding comments or matters that you'd like to reinforce to the commission at this point?

MR MATHESON: Just a couple of things, Mr Woods. It wasn't my intention in my submission to draw a parallel between the introduction of the TCS arrangements and the departure of BHP. They certainly followed each other, and I gather that the cost to BHP would have been in the vicinity of some several million dollars to comply with the TCS arrangements when they were certainly a borderline industry or a borderline company at that time. So that wasn't my intention in the submission.

If I could make the observation, however, that there are a number of submissions you've received on your Web site in relation to stainless steel. The TCS issue has certainly generated some feeling within my industry and I would certainly reiterate my request that a recommendation to remove the tariff be adopted.

MR WOODS: We have noticed that that is your firm recommendation to us and we understand the issues surrounding it. Thank you very much for your evidence and your time today.

MR MATHESON: Thank you.

MR WOODS: That completes the hearings for today. We will resume tomorrow morning at 9 o'clock.

AT 2.59 PM THE INQUIRY WAS ADJOURNED UNTIL
FRIDAY, 28 JANUARY 2000

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