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TRANSCRIPT OF PROCEEDINGS

PRODUCTIVITY COMMISSION

REVIEW OF AUSTRALIA'S GENERAL TARIFF ARRANGEMENTS

MR J.H. COSGROVE, Commissioner
MR M.C. WOODS, Associate Commissioner

TRANSCRIPT OF PROCEEDINGS

AT SYDNEY ON FRIDAY, 28 JANUARY 2000, AT 9 AM

Continued from 27/1/00

MR COSGROVE: Good morning, everybody. This is the second day of the commission's hearings on the general tariff arrangements inquiry in Sydney, and our first participant this morning is the Australian Aluminium Council. David, would you mind coming to the microphone, at least initially, and identify yourself for our transcript and the capacity in which you're appearing today.

MR COUTTS: Okay. Thanks very much, John. David Coutts, I'm the executive director of the Australian Aluminium Council, and I'm appearing representing the aluminium industry and very happy to have the chance to say a few words in relation to this inquiry. Would you like me to go straight into the - - -

MR COSGROVE: Yes. Are you planning to use the screen?

MR COUTTS: I can. Perhaps I'll talk a little bit, and there are a couple of slides in the things there. There are a couple of slides which might be helpful in terms of explaining a few things about the industry, so I'll do that. John, I assume that it would be appropriate for me to make a statement.

MR COSGROVE: Yes. We've read your submission of course.

MR COUTTS: What I'd like to do is to just explain perhaps in a little more detail some of the issues there and emphasise a couple of particular points. In terms of time, have you got some guidelines on that?

MR COSGROVE: We are planning to bring on the non-aluminium participant after you and your colleagues around about 10 am.

MR COUTTS: Okay, fine. I'll lead off and then at an appropriate point we'll go to the more specific focus that Wayne Osborn is here for. Just a couple of words about the aluminium industry, because I think it's necessary to understand that, to perhaps understand what our particular interest and concerns are in relation to the tariff review. As you say, we've put in a submission, and that has summarised that, but I think it might be useful just to underline a couple of things. The aluminium industry in Australia may be not unique, but I think it is a very particular industry, in that it's an industry that takes raw material - that's bauxite ore - and value-adds considerably in Australia, much more so than most other primary mineral industries.

The council and the industry involves not only the bauxite ore but most of that bauxite is processed into alumina which is an intermediate product, aluminium oxide, most of which then goes into making aluminium metal in aluminium smelters. Quite a significant amount of that is processed in Australia into metal, but also a lot of it is exported. Australia is by far the world's largest producer and exporter of alumina; over 30 per cent of world alumina is sourced from Australia. So we are a world leader in that area.

Australia is also a major producer and exporter of aluminium metal. We're the fifth largest producer and third largest exporter in the world of aluminium metal, and quite a bit of that metal is further processed within Australia to, what's called, semi-fabricated products - extrusions, rolled product and various types of cast product. So by the time you take the bauxite and develop that into semi-fabricated products, you've increased the value very significantly. A tonne of bauxite is worth maybe $20 a tonne, something like that, whereas a tonne of semi-fabricated product is worth over $4000, so it is a very significant industry. If you don't mind, seeing that the projector is there, if I can just give you that picture.

I had a much prettier one which I put in the report, but my computer was misbehaving last night. That basically just summarises, and really there's a copy in the report, at the back, which is a little nicer. It has coloured boxes and things on it. But what that's telling you is that you've got the bauxite, the alumina, the aluminium and the semi-fabrications, and it gives some values. That value isn't actually right but the one in the report is. That should be changed to $4000 a tonne. The correct value is the one in the report. That summarises the sort of job numbers.

What happens is that the semi-fabrications then go to final products, much of which is also produced in Australia, and they're the sectors which are dependent or are involved in those - building and construction, transport, vehicles and others, packaging, and then some electrical consumer durables. But the big ones are building and construction, packaging and transport. I won't talk very much in detail about those sectors, particularly packaging, because Wayne Osborn will talk about those later.

The industry is also by the way - if I could just show you very briefly - very important in a regional sense in Australia. That map, which I haven't put in the report but I can supply it if it was of any interest, just shows where the operations are and, in particular, the semi-fabrication operations because they're the ones that are most relevant, I think, to the inquiry here. There are four locations for extrusion - Brisbane, Sydney, Melbourne and Perth - and two for rolled products which are Sydney and Melbourne. There are a number of locations for cast production, but mainly that is in Sydney and Melbourne. I'll leave that there, in case it's useful.

As I said, the aluminium industry is a major industry in Australia. Collectively in 1998-99 it was Australia's second largest export industry when you add the bauxite, alumina, metal and semi-fabricated products together. The industry has considerable potential to grow further. To a large extent that will be in the upstream sectors, particularly alumina, but hopefully in metal as well, but there's also some potential in the semi-fabrication sector, particularly in the case component sector but also in rolled products and other things.

The industry has invested over $5 billion in recent years and has the potential to invest considerably more in Australia, and this is important I think: the industry is a technological leader in Australia, particularly in the upstream sectors, because being the world leader in alumina, obviously Australia is a place where a lot of the research and development - at least we're involved in that, if not at the leading edge of it. As I said, a lot of the industry is concentrated in the upstream sector. There's a lot of strength there. In terms of tariffs, they're not significant in the bauxite, alumina and aluminium sector. They're not an issue. There are no tariffs in those areas, as far as I'm aware, but in any case there's no imports because we're a major exporter so there's virtually no imports, except for some very specialised metal alloys.

When you get into the semi-fabrication sector, however, it starts to become a critical point. Just running through the three components of the semi sector quickly. Extrusions: we produced about 100,000 tonnes of extrusions in 1998. About 5000 tonnes of that was exported. There were about 30,000 tonnes of imports. Some of those imports were from New Zealand, and there's a synergy there and CER operates in that case. There is quite a strong extrusion sector in New Zealand, and Australia is seen as their major market, and I guess the Australian industry has adapted to work with that.

However, in recent years there's been very strong competition as well with imports from Asia, particularly China in recent times, but from a number of other Asian countries as well. That is becoming, if not a problem at least quite an issue for the industry, and most of those, if not all of that production is in countries where there are quite significant protective walls of some kind; sometimes tariffs alone and sometimes tariffs and other non-tariff barriers. But the overall level of protection in countries like Malaysia and Thailand and Taiwan and those countries is quite high. I think it ranges from about 7, 8 per cent to over 20 per cent in some cases.

In the case of rolled products, we produced a little under 200,000 tonnes of that last. Over 100,000 tonnes of that was exported, and I won't go into more detail on that because that's all in Wayne Osborn's area, or almost all of it. A large part of that was exports of cansheet to Asia. There were some other exports of various sheet and plate products as well, but the cansheet to Asia is the dominant amount in that. There's also imports of rolled products, however; over 30,000 tonnes of that in 1998. They came from a variety of sources; some from Asia, but also from the Middle East and, increasingly, there's potential at least for imports of that I think from South Africa.

I think once again those industries are, to a large extent, expanding and being able to export to our market from behind fairly high protective levels in those countries, at least in the Asian ones, and certainly in South Africa as well. So in relation to tariffs, it's really the semi-fabrication sector that the industry is concerned to underline to the commission. All the semi-fabricated products in Australia, with one exception, I think still have a 5 per cent tariff rate, and the exception is cansheet. The tariff was removed last year over the dead body virtually of the industry. But it was removed, and I'm sure Mr Osborn will have a few words to say about that when he talks to you.

MR COSGROVE: On that point, David, could I just clarify. Is cansheet synonymous with can stock, which is mentioned in your submission, I think on page 4?

MR COUTTS: I use the term - maybe Wayne can amplify this - "cansheet" in a general sense to cover all the - but there are different types of products that are used in cans. There's the body stock and then there's end stock and tab stock, so there's three components in the can. But Wayne when he's talking can give you some more details on that.

MR COSGROVE: We can clarify that.

MR COUTTS: The general view of the aluminium industry, very strong view of the aluminium industry on the general tariffs that remain on the other semi-fabricated products is that Australia should be moving, along with other countries, towards the lowest level of protection possible, and therefore towards zero tariff on these products. However, our tariff rates are, in the main, lower and often significantly lower than the countries which we're competing with, particularly where the imports are coming from at the moment, so the industry very strongly has the view that these tariffs should be removed in the context of an international process, whereby the competing countries are also lowering and removing their tariffs.

The industry strongly believes we shouldn't act unilaterally to remove the remaining general tariffs on aluminium semi-fabricated products. You might say why is a relatively low 5 per cent tariff so significant for the industry. It is significant. It's significant because, for the industry to succeed in Australia, there's a whole range of things which it has to be able to do. It has to meet the demands of the Australian market, because it is mainly, with the exception of mainly the cansheet, targeting the domestic market. The domestic market is requiring certain types of semi-fabricated products and becoming quite demanding in terms of what these products are.

Take for example the window sector. Because of the great concern that's emerging on energy efficiency - this is just one example - but on energy efficiency, the aluminium extrusion sector, where a large part of that market is going into windows and doors and things like that, has had to respond by developing new types of extrusions which are energy efficient. A lot of the traditional extrusions are very simple types of extrusions and don't deliver the sort of energy efficiency ratings that the Australian market - not only the market requires but Australian government requires, because there are energy rating schemes which are being put in place nationally where every building, if it doesn't already, is going to have to conform to these energy rating standards.

So the aluminium industry in Australia has had to respond. The research and development and commitment to investment to produce those new extrusions is quite costly. It's not going to come from most of the countries that are exporting these extrusions to Australia, where they're more exporting the more traditional type of extrusion. So the sort of investment that the industry needs to make in things like that - that's just one example - it's much more likely to happen if there is at least some protection or some tariff still there to give at least a little bit of counterbalance to the very high levels of protection that these industries have got overseas.

There are other examples of that, and Wayne may talk about that. I know in the rolled product area, looking at investment in certain types of rolled product to meet demands of the marine sector does require a certain quality that does need quite a bit of research and development and investment, and expecting the Australian industry to make that investment while trying to compete with imports from behind very high levels of protection overseas is very difficult.

There is also that the industry has to try and respond to - and of course this is right and proper to do - the requirements of the Australian economy, where environmental standards, health and safety standards and all those things are very high. This is right and proper, as it should be, but the countries with which we're mainly competing are not meeting those same standards and certainly incurring those same costs. That's something that maybe has to develop in the longer term, but at least in the near future while those things work their way through in Australia and until they start to come into some harmony internationally, then it is a further disadvantage to Australia to the costs that are incurred there which, as I say, the industry completely supports but they're not part of what the competitors have to meet.

So in summary on that point, as I said, the aluminium industry supports moving to lower levels of protection for all sectors in all countries, but we think this must occur in a measured and harmonised trade negotiation framework, I presume through WTO and possibly some of the processes that might occur in APEC and the ASEAN context. I'm not sure myself what we look to in WTO after the Seattle meeting, but that sort of thing in our view is the right framework within which these things should be pursued.

If the remaining 5 per cent tariff on semi-fabricated products was removed unilaterally in Australia, it would make further major investment in these sectors very, very difficult, if not impossible, in my view. Wayne will have his own views on that when he talks to you in a minute. But that's very strongly the advice that I'm given; that there is potential for further investment if it's on a globally level playing field basis, but without that it's very difficult to achieve.

Just a couple of other points: the discussion paper does talk about the existing concession arrangements, the tariff concessions scheme and the project by-law scheme. I just wanted to mention that they are important to the industry as well. In this case not quite so much in the semi-fabrication sector, or there may be some implications there, but particularly for the investment in the refining and smelting sectors. These production facilities - as you can see from the map, there are in fact six refineries and six smelters in Australia. When you think of the proportion of world production that we produce, that means every one of those operations is very, very large. The capital investment in each of them is well over a billion dollars and probably two to three billion dollars in most cases - very large investments.

They have very specialised equipment for some purposes. The alumina refineries are very big and very complicated chemistry sets and much of the equipment that you need for those has to be imported; it's not available here. In the case of the smelters also, particularly in the electrical area, it needs very, very expensive and very complicated equipment. In addition, there are certain inputs to the industry like petroleum, coke, pitch, that have to be imported. They're not available - or only have very limited availability in Australia.

The industry therefore feels that the tariff concession scheme process ought to be looked at; that there is a tariff still of 3 per cent that's imposed on some of these imports which are not available in Australia and there are a number of administrative hurdles to get over even to achieve that situation. So the industry feels very strongly that we should be moving towards zero tariff for imports like that where they're not available in Australia. It's an unnecessary burden on an export industry to have to meet both the tariff and the administrative costs of doing that.

The same comment in a way applies to project by-law arrangements whereby - certainly those arrangements have been available to the industry to make the equipment imports that it has needed to do but again, there are administrative hurdles and processes to go through. It's on a project-by-project basis so there are uncertainties as to whether the duty-free concessions are going to be available there. Where the equipment again is not available in Australia then the industry feels that there isn't any justification to have those tariffs.

I think that's about all I'd say like that, John and Mike, and I'd be happy to answer any questions that I can.

MR COSGROVE: Thanks, David. I think we do have some that you might be able to help us with. If you look at the semi-fabricated segment of the industry which, as you say, is the part most likely to be affected by any policy changes coming out of this inquiry, what has been happening in that part of the industry? We're conscious that the upstream sectors are growing pretty well. I'm not sure that I found in the submission any material that would give us a feel for rates of growth of output, employment and so on in the semi-fabricated sectors.

MR COUTTS: There is a table. It's a bit of a complicated one but I did put this in the report.

MR COSGROVE: I've got it at the end of the report.

MR COUTTS: You've got that in the report anyway.

MR COSGROVE: Yes, most of the figures only ran though for a couple of years.

MR COUTTS: We do have figures for a much longer period. I haven't got them here, but I can supply those if you're interested. Basically what you find is that the industry overall, I think, has been growing slowly in the semi-fabrication sector, but not very rapidly. If you look for example at the extrusions - that line down the bottom there - you find that the production in 93 was 92,600 tonnes. That figure is domestic production of extrusions from Australian metal. That's what that is, and that's only - that's gone up and down over the intervening period, but it was only slightly higher in 1998.

There is a fairly large story behind that. There have been all sorts of changes in some processes and production, forms of extrusion have been discontinued and others changing, but basically in total the extrusion sector has been - you know, not growing terribly rapidly. It is linked very closely, by the way, to the building cycle. A large proportion of extrusions goes into building construction and so if the building sector is growing rapidly then aluminium extrusions, domestic production will grow. You'll probably find too - I haven't got the figures going back far enough - there may have even been somewhat higher exports when you get back into the early 90s and things like that, and that has reduced.

MR COSGROVE: Although exports of rolled products seem to be growing quite rapidly.

MR COUTTS: Yes, and Wayne can talk more about that. As I say, I haven't got the longer-term figures with me. I have them back in the office and I can send them. If you go back for imports of extrusions - if you went back into the 80s you would find much lower levels of imports than we have now. That's taken off quite rapidly - I think it was starting in fact, that figure that we've got up there of 21,000 tonnes - you can see that's grown to 27 and 29. That would be reflecting the Chinese imports of extrusions. The New Zealand trade would be fairly constant - I think, if anything, even a little lower.

When you get to rolled products, John, then again the overall level of production has risen fairly significantly, but that's mainly - it's not due to the domestic market which, as you can see, has probably declined, or has declined a little bit, but to the impact of exports to Asia; if you compare the 80s to now - as I haven't got those figures back there. Wayne may know them but you would find, I think, that the export of rolled products - as you can see, it's been growing fairly rapidly anyway in those last three years we've got there, and it would be lower again if you went back into the earlier times.

Basically what that reflects, I think, is that Australian market for semi-fabricated products is a fairly mature market. If you look at the total Australian consumption figure per capita consumption figure there, you can see that's been growing but in a somewhat up and down fashion. 20 kilograms per head per year is quite high by global standards but below the sort of figure you'd have in the USA which would be more like the high 20s, I think, up around about 30. That's about the highest. But Australia is sort of in the more developed country area. We'd like that figure to grow up to the US levels but it's something that hasn't happened yet.

I think that just basically reflects the particularly Australian economy and the reason mainly why that per capita consumption figure isn't higher - if you look at the detail behind it, which I haven't got here, our level of consumption in the transport sector is at the moment a lot lower than it is in Europe and North America. There's a lot of potential, by the way, for that to grow, particularly in diecast engine components. One of the things that we're doing in the council is to try and encourage, with some parts of the government, investment in that sector. That's where the 5 per cent tariff isn't unuseful in terms of kicking off that sort of investment, giving people that little bit of extra confidence.

MR COSGROVE: You mentioned the domestic market as mature, so you're unlikely to get a lot of growth out of that sector, and that's the sector where the tariff has its application. If you're looking more - as these figures seem to suggest - for export growth, why is the tariff so significant in that context?

MR COUTTS: I wouldn't say that the industry wouldn't be looking to some growth in the domestic market.

MR COSGROVE: No, I'm sure there is some, but as you say it seems a relatively mature market now.

MR COUTTS: It's relatively mature but there are opportunities which the industry will be looking at, including the one I just mentioned. That's in the transport sector - not only in engine components, but in terms of other aspects of lightweighting transport vehicles. I mean, that is becoming very important as you try to respond to energy efficiency and greenhouse. Our industry has done some work internationally on that and it clearly shows that if you lightweight a car by 30 per cent using lighter materials - and aluminium would probably be the main one - then you make very significant savings over the life of the vehicle on greenhouse gas emissions, when you take all the emissions in making the fuel, etcetera, into account. So there is potential for growth in those sectors. What role Australia will play in that vis-a-vis overseas is a bit unclear, but there is quite a lot of potential there.

There is potential in the building construction sector as well, so the industry is not saying there will not be growth in those sectors. I think there is opportunity and that plus the fact that you have to run pretty hard to remain competitive in this industry, and to be able to provide what the Australian market is requiring in terms of the type of extrusions and the quality of rolled product from marine applications and very lighter weight cans to compete with steel and plastic, there's quite a bit of research and development that's needed to be able to meet those demands. So even to stand still you're going to have to make considerable investment, I think, in the industry. So the tariff is very significant in terms of just that little bit of counterweight to the protection that's being given in the competing countries.

MR COSGROVE: Are the foreign producers competitive in those more specialised applications of aluminium products?

MR COUTTS: I don't think you can give a general answer to that. My expectation would be that in a number of areas they probably wouldn't be competitive with Australia if they didn't have the level of protection they've got and in terms of the sort of products - some of the sorts of products, anyway - the Australian market is demanding.

MR COSGROVE: How does their domestic production enable them to be competitive in foreign markets? One tends to think of, as Australia's own experience has shown, highly assisted sectors as being essentially not good at exporting because they're not as efficient as sectors which operate without that assistance.

MR COUTTS: Well, all I can say to that, John, is that there has been considerable investment in aluminium semi-fabrication operations in Asia, in particular, and it's happening in South Africa now - right now - behind very high levels of protection and a lot of that is going towards exports. I don't believe a lot of that is efficient in an unprotected sense because it's not mainly a high labour-intensive industry. I mean, there are some benefits you can get from cheaper labour in places like Taiwan and China but it is a capital-intensive industry and so I don't believe a lot of those operations are competitive - if they had to face exactly the same terms and conditions that we do, but they don't.

To add to that I think a lot of that investment is probably not going to be competitive when you go down the track in the future but just at the moment it's there and it's been encouraged to be there by the sort of incentives and things which exist in those countries and it's competing therefore very aggressively for export markets.

MR COSGROVE: So is the implication here that they're selling in their foreign markets - that is, their export markets - at prices below those prevailing domestically in those countries? Is there any evidence about it?

MR COUTTS: My understanding is that's correct but it hasn't been - at least so far anyway - the evidence hasn't been clear enough to be able to actually pursue dumping provisions but it's been thought about. Quite frankly, the aluminium industry would rather compete without going into the dumping sort of issues and it feels that this is going to gradually sort itself out in these other countries because I don't believe long-term they are efficient and they are going to be competitive as things like the Asian crisis, the economic crisis, come along. They get put under a lot of pressure. The costs to their countries start to become a bit more obvious so that becomes a problem.

As I said, it does exacerbate the problem a bit if the very small amount of help that we get from the tariff was removed. If you look in the longer term, maybe 10 years down the track, particularly if you do it through a court or a proper sort of international negotiating framework, then hopefully their levels of protection will come down and the problem will right itself. If we are not careful we won't have an industry here to be part of that.

MR WOODS: Are you describing a situation where industry in other countries is not competitive in terms of their own efficiency of production but is competitive in terms of price of product in Australia that they're able to import? Is that essentially what you're - - -

MR COUTTS: They're selling in Australia at prices that are very competitive with our own industry.

MR WOODS: And there's a diversity of suppliers from a diversity of countries who are able to bring in competitive pricing into Australia?

MR COUTTS: There's imports of extrusions and rolled product from a number of countries to Australia and that's being sold at prices which are putting downward pressure on the Australian industry.

MR WOODS: In that circumstance, then - in your submission you refer to short-term gains to users of aluminium semi-fabricated products should the tariffs be removed. In fact, in two different parts of your submission you make that point, that the benefits from reduction would be only short-term, but if we're talking about a situation where there are a diversity of producers in a diversity of countries, that seems to suggest that there is some depth to the competition to the Australian producers, in which case one could reasonably expect that the competition and that price pressuring would continue in the long term. I don't understand fully why you suggest there would only be a short-term gain. Perhaps there would be a long-term benefit to users of the semi-fabricated product in Australia.

MR COUTTS: Well, in making that comment, I was suggesting that if the Australian aluminium semi-fabricated industry wasn't here or was dramatically reduced because it couldn't compete, then there might be a short-term lowering of price - marginal lowering of price - to buyers of these products. Once the discipline of an Australian industry wasn't there then I don't think, anyway, that those benefits would continue. I know what you're saying, that there are seven or eight potential suppliers and they're all going to cut each other's throats to import into the Australian market. Well, possibly. I don't know.

MR WOODS: So it is a possible scenario.

MR COUTTS: I don't know what would happen in that circumstance, quite frankly, but I do think that if you didn't have an Australian industry here to keep a discipline in terms of that direction of competition, particularly in terms of the sort of products that the Australian users of aluminium semi-fabrication need - and need because to some extent of the requirements being put on them by governments and by the market there - they're going to have difficulty getting some of those sorts of products at competitive prices from overseas, I think. They'll get cheap ordinary extrusions from China but they're not the sorts of things that are wanted in the Australian market now.

Maybe China will respond and start producing those things but we're a pretty small part of what they're targeting and I'm just suggesting that there will be some problems in the Australian market.

MR COSGROVE: Why, though, would they be providing as at present, in your submission, strong competition to Australian production, yet when that source of local production, in your view, might disappear, they would no longer be interested in competing for the market?

MR COUTTS: They would be interested in continuing to supply the market but I don't believe that they would do it at prices that would be lower in terms of what the consumers here would pay. That's all I was suggesting on that point; that the prices for imports would move back to levels at least as high as what they currently are very quickly. All I'm referring to on that point is that some consumers of these products in Australia, the semi-fabricated products, would possibly see a benefit in removing the tariff because it would lower their prices. I don't think that would be a long-term benefit.

MR COSGROVE: You're not here assuming any sort of collusion on the part of foreign suppliers.

MR COUTTS: No, I'm not.

MR COSGROVE: You're just postulating a lack of interest on their part in the Australian market; a lack of long-term interest in the Australian market.

MR COUTTS: Far be it for me to suggest collusion of any kind in the terms of this sort of thing, John, but I think the reality is that any gains to consumers of semi-fabricated products would be short-lived and there would possibly be the costs because to get the sort of product that they are going to need in the Australian situation in some sectors, particularly in the building and construction sector, is going to be more difficult without the Australian industry here, and therefore more costly. It might be cheaper if you had Woolworths-type - I don't mean to reflect on Woolworths - but cheap, ordinary sort of extrusions, but that's not what we look for.

MR COSGROVE: Present competitors like Europe and the United States couldn't service that part of the market or wouldn't be interested?

MR COUTTS: There might be some response there but they wouldn't be supplying at the sort of prices that you would be getting for protected producers in Asia.

MR WOODS: All this is predicated on a reduction of the current general tariff, that five percentage points being enough to eliminate the Australian producers anyway, which presumably you're not suggesting is the one fundamental point that affects the viability of the Australian industry.

MR COUTTS: No, I'm not. I am suggesting, though, that it would put very considerable additional pressure on the Australian industry and would certainly make it very difficult for major future investment in the industry, I think. It wouldn't close down overnight but it would certainly not be a - you know, it would affect those things.

MR COSGROVE: David, I guess the industry has been adapting over some years now to a progressive lowering of tariffs. How has the industry been able to cope with that process. Again, it raises the question of what is difficult about the additional 5 per cent.

MR COUTTS: Well, it has been coping with considerable difficulty, John. I think part of the reason there hasn't been more investment in the industry here is because our level of protection, if you like, has been reducing, as it should. But at the same time the level of protection in other countries has certainly not been reducing like that and, if anything, in some cases going up when you take all the protection and all the incentives that are involved in those countries. The impact of that has been the industry has adapted but it's been very difficult and part of that has been that it has become much more concentrated in terms of the products that it produces. I think you'll find the range of extrusions that are produced in Australia in any quantity now is much smaller than it would have been 10, 15 years ago and the same is probably true of rolled products.

MR COSGROVE: Does that suggest, though, that we may not be as naturally competitive in that part of the industry as in others; upstream segments?

MR COUTTS: I think it certainly raises some different issues. I think certainly we have a clear competitive advantage in Australia in the upstream sectors, particularly in the mining and refining sectors. The metal sector - that may or may not continue once the government has finished what it's going to do on greenhouse, but if we leave greenhouse aside, we're also very competitive in the metal sector as well. In fabrication it's not as clear and certainly with Europe and North America - and Japan perhaps - we do have difficulty competing in the full range of products there.

There's a rolling mill, for example, in Germany which is - I don't know what it produces but 700,000 tons or something of rolled product a year. I've been to visit it. If you look at our figures, that's four or five times what we produce in total in Australia. Now, if you have that sort of volume then you obviously can compete in a way that we can't. What happens in Australia is there are areas that we can compete in because there is the volume, or we just have been clever enough to produce the sort of product that we can compete with, but the range of things that we can produce like that has been narrowing and the amount of investment in the semi-fabrication sector, I think - I haven't got those figures here but I think you'd find that hasn't been growing very rapidly.

MR COSGROVE: We should keep an eye on the clock.

MR COUTTS: Yes. I am conscious that Wayne wants to talk to you and you have to get that in before 10 o'clock.

MR COSGROVE: I just might have one or two questions of a more detailed kind. You referred in your remarks, and this point is also mentioned on page 6 of the submission, there are some administrative and compliance costs associated with use of the tariff concession scheme and the project or policy by-laws. Could you elaborate on that at all or would you be able to provide us with evidence of those costs in a later piece of paper?

MR COUTTS: I could certainly attempt to do that. I mean, that is what I am advised by the member companies; that the project by-law arrangement is certainly appreciated because it is important but it is something that you have to put a fair bit of effort into achieving the clearances there and the same with the other one but, no, I haven't got the figures with me but that is what they tell me, John.

MR COSGROVE: If you could take it on notice if you are able to provide us with anything or your colleagues subsequently, that would be good.

MR COUTTS: I will attend to that.

MR COSGROVE: We hear a fair bit of anecdotal evidence to this effect but of course it is nice to have actual indications of the costs people have been bearing in using those systems.

MR COUTTS: I will take that up and see if we can get some figures to you.

MR COSGROVE: Thank you. My only other question I think relates to one of the main points in your submission that any further tariff reductions that are made by Australia should be made on the basis of reciprocal action by other countries. I was wondering how in practical terms you would see that happening. No doubt there is a range of tariff levels in the countries with which your members are competing. Does one wait until the highest of those tariffs gets down to three or zero or whatever and we move only then or do we - - -

MR COUTTS: In a perfect world you would but there would be arguments, I guess, for not necessarily doing that. There may be benefits to Australia from perhaps not being quite as rigid as that but certainly our concept is there should be significant movement by the high tariff high protection countries that we are competing with in this area, and they're countries like Malaysia, Thailand, Taiwan and those countries - China - before we removed our remaining, rather low level of protection but we are not absolutely rigid that everyone has to get to 5 before we ought to move.

MR COSGROVE: You mentioned China then but you have also referred to it several other times as being a sort of an emerging major exporter of semi-fabricated product. Presumably you have been following the various concessions they've been making in terms of entry to WTO. Is that in itself a sufficient signal to you that would warrant some re-examination of our current tariff arrangements or are you looking for a more broadly-based movement across a number of countries?

MR COUTTS: My understanding with China is that even with the WTO - the things they have been promising in terms of access to WTO is still a fair way from the sort of levels we have got. I haven't got those figures in front of me so I don't quite know where they have got to there with semi-fabricated aluminium products but I don't believe it would be enough in itself but certainly it's an encouraging move. Are you saying is that enough that we would be happy to see our tariff go to zero in return for what they're offering? I don't think so.

MR COSGROVE: I'm just wondering at what point you would concede that enough has been done and enough - - -

MR COUTTS: When passenger motor vehicles and textiles go we will follow.

MR COSGROVE: That is a different argument and I am happy to have your views on that as well in terms of relative assistance.

MR COUTTS: Yes.

MR COSGROVE: But that is, as I say, a separate argument to - - -

MR COUTTS: I know that is outside the brief here.

MR COSGROVE: That is a point you can make for the record but in terms of other countries I have difficulty in understanding at what point you would say enough countries have moved far enough for you then to concede that that final 5 per cent should be abolished.

MR COUTTS: As I said, the in-principle position is that when they get the 5 per cent then we all move down to zero but I think we would acknowledge that if say a country with 20 per cent tariff at the moment were to offer to move to 10 then it might be to Australia's advantage to consider, if you like, locking that in by some movement ourselves but one would have to look at the individual cases to comment on that, but the general rule would be what benefits are we going to get from lowering these semi-fabricated tariffs - - -

MR COSGROVE: I guess that gets back to the point we were discussing earlier.

MR COUTTS: - - - out of line with what others are doing.

MR COSGROVE: Yes.

MR COSGROVE: Presumably the users of the semi-fabricated products would argue that they are incurring a cost while we're waiting for this move to occur.

MR COUTTS: That's right.

MR COSGROVE: And so it's a judgment between how long the cost is versus - - -

MR COUTTS: We did acknowledge that some people may feel that way and we tried to address that point. Obviously we didn't quite succeed in convincing you on it, but it's a tricky point, that one, because there is a balance.

MR COSGROVE: Yes. It is one of the big issues in this inquiry certainly. Anything else, David?

MR COUTTS: No. I am fine, John. I am conscious Wayne needs to talk to you.

MR COSGROVE: Yes. Why don't we then now bring KAAL Australia to the microphones?

MR COUTTS: Thank you.

MR COSGROVE: Thank you.

MR COSGROVE: Would you mind identifying yourself for our tape-recording, please, and the capacity in which you are with us today?

MR OSBORN: Thank you. My name is Wayne Osborn. I am the managing director of KAAL Australia and I appear obviously for KAAL Australia in this regard. Thank you very much for the opportunity to appear. This is something that KAAL Australia and its board and its owners, Alcoa Inc and Kobe Steel, feel very strongly about. It is something that is very important to our business which, I guess, was formed in 1996, and I will take you through a little of that as we go but perhaps an opportunity maybe to answer some of the questions firstly that came up in the previous session.

You asked the question about what is really the importance of the tariffs in the home market or in the domestic market and if we have an export focus in our business why would that be so critical to us and perhaps, to give you an example, certainly KAAL Australia since its formation has been growing its export business, particularly in aluminium cansheet and that has been critical for us overall but we still have about 60 per cent of our volume supplies the Australian market.

Certainly with the small scale and mature nature of the Australian market our growth is certainly going to be overseas but we do have some import substitution opportunities as well as we look at our future but in particular what we've found in recent years is the tariff regimes of other countries where new producers are being established - and I will go through some examples of that - are in fact reducing our market, so we've had a reduction in export market of some 30,000 tons occurring during this year and will occur during the next year in an overall production base of around 160,000 tons, which we have to find new markets for, so we find that the protective action of other countries is in fact changing the market dynamics for us overall.

One of the other differences perhaps in nature we find is that most aluminium rollers have a home market which represent some 85 to 90 per cent of their total volume and so they're making decisions around export opportunities, particularly into the Australian and Asian region based on incremental costing, so you do see differences in pricing based on the fact that they say, "Well, okay, we've got a little production capacity here we can export into this market" and they tend to move in and out of those markets based on their current exchange rate, where they sit in relation particularly to the US dollar, what those markets are doing at the time and perhaps the prices available to them, so the pricing policies around that are certainly different than what they would see in their home market and it addresses one of the issues I think you put to David earlier that says if you had this industry in Australia disappear would that be better for our customers in a sense of having perhaps a lower cost supply and may do well for a while but they will also have a less continuous and less reliable supply because of the way those businesses treat the market, so there are a lot of dynamics at play associated with that and I thought it might be useful just to address those overall, so I guess obvious from my comments around the first point there that we do support, and strongly support, the retention of the 5 per cent tariff.

We see it as a critical aspect to our business. It is critical in terms of our current business strategy. It's critical in terms of our current expansion plans and some capital authorisations we have before the board at the moment and hence our submission here today. We have talked about reciprocity and I will cover some of the tariffs that do exist for some of our competitors later on but an extremely important part of our submission is that issue of reciprocity for us to operate in a playing field that is level overall. I guess lastly we see the tariffs that promote these principles are not nuisance tariffs but rather important to allow some balance in the marketplace overall.

Perhaps just to give you a little bit of background as to who we are. We came into formation I guess in early 1996, when Alcoa and Kobe Steel acquired the facilities in Sydney which were previously owned by Comalco - it was a rolling mill in the suburb of Yennora - and also the joint venture then acquired the rolling assets owned by Alcoa of Australia in Geelong. The asset base is 250 million. We have a capacity of around 180,000 tons a year. We certainly have the potential to grow that to the 200,000 ton plus range. Our plan this year is we will sell something around 160,000 tons, so we are operating below our normal capacity at the moment.

The product range we produce is aluminium cansheet and it goes by various names. Can stock usually refers to the sheet that makes the body, if you like, of the can. End stock or lid stock, the top of the can. Rigid container sheet is its actual more technical description but unfortunately it gets known by a variety of names, which tends to confuse people outside the specifics of the business. We also produce foil and general sheet overall, which is obviously the subject of what we're talking about today, and we see that as a potential to be a growth part of our business but threatened by the potential legislative changes which we may see around tariffs overall.

We employ 800 people, approximately 400 at the facility in Sydney and another 400 in the region of Geelong. Our revenues in 1998 were 650 million - they have been growing steadily since inception - and, most importantly, $350 million in export revenue associated with the business overall. To just give you an idea of the markets we supply - and this is our plan for the year 2000 - two facilities in terms of plant production output for this year. We might just start with - the South African market we expect to be about 7000 tons. That has previously been 20,000 tons a year for us. This will be the last year we export to South Africa. A company in South Africa has spent $US450 million in upgrading their production facilities and will become a major producer of aluminium cansheet and general sheet and foil and they're just bringing that facility on-line at this point in time.

The tariff into South Africa is currently 14 per cent. Will reduce to 10 over a period of years but there are certainly no plans to take it below 10 per cent, so from a market access we have as a producer - develops their own facilities there - we now need to find a home for 20,000 tons of product we supplied previously. If we look into our Asian exports - and this is where you've seen the growth in real products in rigid container sheet in recent years of 75,000 tons. Korea we expect to ship about

5000 tons into this year and we believe that will be zero or close to zero in the coming years. A recent change in Korea is that Alcan has acquired a company called Taihan Electric and they are reinvesting in that rolling mill business to become a major exporter for the region and Korea is currently protected by an 8 per cent tariff, so it will make it very difficult for us to come into their home market as well with an 8 per cent tariff barrier ahead of us.

We also export some quantities to the Middle East and you can see our Australia-New Zealand cansheet volume of 44,000 tonnes. A mature market - not a lot of room for additional growth unless people want to drink double the number of cans of Coke or Victoria Bitter or whatever overall, but it is quite a mature market.

In the common alloy or general sheet market we're currently supplying about 10,000 tonnes and about seven in foil. We really have opportunities for growth here. This market is about 50,000 tonnes in Australia, supplied significantly by imports. The foil market is about 20,000 tonnes in Australia, again significant imports coming in. We would like to be about to invest capital, and we've identified about $20 million which would allow us to basically nearly double this capacity here, but we have significant concerns about doing that in a zero tariff environment where the importers coming in are not subject to that same impact. I'm actually missing an overhead here, John, unless I've given it to you. It's the one with the tariffs.

MR COSGROVE: We have hard copy of it.

MR OSBORN: Okay. I've got it, sorry. Here we are. If we look at the importers in the general sheet and foil area coming in, we've got significant volumes coming in from Bahrain, where they have 12 per cent in their home market, significant volumes from Germany at 7½ per cent, some volume now coming in from Spain this year at 7½ per cent, some volume from France, again at 7½ per cent, so if we look at people who are competitors in our business, they are sitting behind some form of protection in their home markets overall.

In fact if we were to adapt - we're certainly the only country in the world that's a producer of cansheet that has a zero tariff, and if we move on the general sheet and foil tariffs we'll be the only country in the world that's a producer that has a zero tariff, so this is the issue that we really are concerned with in the sense that it just puts us at such a disadvantage compared to our competitors that says, "Is that an environment which you ultimately" - can your business survive if we're in that kind of environment?

Why is 5 per cent important? It's about our margin, and the way we operate as a business - we buy our aluminium at market so we are a purchaser of either molten aluminium or scrap aluminium in pig form as import to our product. We value-add to that and then we sell at a total price, including the aluminium. So our margins sit very tightly, let me assure you, in that range, as we've said there, so you can move between an adequate return and a loss situation very quickly. Our bodystock business now sits at around - at break-even for the coming year overall, so it's a small percentage but it's a very important percentage as far as the business is concerned.

MR COSGROVE: Wayne, how should we interpret the word "margin"? Is it equivalent to a concept of rate of return on assets employed or - - -

MR OSBORN: No, in terms - - -

MR COSGROVE: Margin over costs?

MR OSBORN: - - - of profit. In terms of profit over total cost in terms of the - if you were selling a product for instance that happened to be say $4000 a tonne, including the aluminium and the value adding, it's in that margin.

MR COSGROVE: What would you say the rate of return on your assets is?

MR OSBORN: The rate of return is about 8 per cent at the present time.

MR WOODS: Can I just clarify on those margins. Elsewhere in your submission you talk about margins for many of the industry's high volume products by which presumably you mean canstock or whatever.

MR OSBORN: Yes.

MR WOODS: They're typically in the order of 1 to 2 per cent. That's on page 7 of your submission.

MR OSBORN: Yes.

MR WOODS: I'm just not quite sure why the differential, and if your high volume products are only 1 to 2 per cent how you're then averaging 2 to 5 overall.

MR OSBORN: That's not necessarily an average. It is certainly tighter in the rigid container or in the cansheet side. It differs by product, and the 2 to 5 per cent is an average across a broad range of products that we produce.

MR WOODS: But if your highest volume is at the tighter end, then you're making significant margins then on some of your smaller volume to get the same average across product.

MR OSBORN: No - okay, the 5 per cent is not an average per - is not a volume-related average. It would be an absolute average per product category - I'm sure if I've explained myself - there would be no product line in which the margin would be greater than the 5 per cent level. Is that perhaps a clarification?

MR WOODS: Yes. Thank you. Presumably that margin changes according to cycles. If you've got a building boom here or if you've got opportunities elsewhere - - -

MR OSBORN: Yes, it does.

MR WOODS: - - - there would be times in your cycle when your margin would exceed that.

MR OSBORN: Would be better than that, that's correct.

MR WOODS: Yes, okay.

MR OSBORN: And I guess in concluding, similar to David's submission, we're really saying we're looking for an appropriate - or the rate being comparable with competitors overall, so we have great concern in moving ahead of the market as we've done in terms of the aluminium cansheet business previously.

MR COSGROVE: Thanks very much, Wayne. Could I just try to clarify the question I put to David about canstock and cansheet. In the council's submission - I don't know whether you have it with you, but - - -

MR OSBORN: Not at the table at the present time. Yes, I do. Sorry, I do.

MR COSGROVE: On page 4 we see a statement - it's up under the marginal heading there. In the paragraph about two-thirds of the way down it says, "Such areas of strength" - that is, in an internationally competitive sense - "would include cansheet."

MR OSBORN: Yes.

MR COSGROVE: Then in the third-last paragraph on the preceding page we're told that the canstock no longer has a 5 per cent tariff that still applies to the semi-fabrication sector in general. So if those two concepts, cansheet and canstock, are identical, it raises the question of how the product can be one of competitive strength and yet still somehow be affected by a relatively small tariff change. Are they the same or not?

MR OSBORN: I think for the purposes of the submission I think they are the same. Let me maybe clarify and make some comments that I didn't make overall. Kaal Australia is a very competitive producer in cost terms. We have very flexible labour standards, we apply total quality management principles to our business, so we are not an inefficient producer by any means, and for our benchmark mill size we compete very very well, but we are competing in a business which is seeing returns which are at historically their lowest levels in real terms. We compete in the Asian market in this region which has the lowest cansheet prices in the world at the present time, so we are an efficient producer but we are competing. We are very good at what we do in a technical sense, in a cost sense, but we are competing in a very tough marketplace. So rolling mills are not a wonderful asset to make a huge return on investment, and if you look at the overall global market it is still characterised by a significant overcapacity.

MR WOODS: Is that a feature of a five-year period? In fact is some of the overcapacity reflecting the reduction of demand in the Asian area at the moment but should there be growth as appears in some of the countries in particular re-emerging - you know, is this going to be cyclical and in three to five years' time we might find ourselves in a different situation?

MR OSBORN: We haven't in the last three to five and in fact the industry has been able to support Asia growing very very well, and if I talk about Asia external to Japan, the cansheet market in Asia is growing from perhaps in 1991 something like a hundred - no, maybe less, about 80,000 tonnes, and these are very rough numbers, to about 340,000 in recent years, but during 1998-99 and the year 2000 that market has levelled off, so it has not increased in volume, due to the economic issues in Asia. We expect that will take off again but most analysis would suggest there will still be an overhang of excess capacity, even into the next five-year period.

MR WOODS: These presumably are some of the volatile elements of the climate for investment decisions that you're referring to in your submission.

MR OSBORN: Yes.

MR WOODS: That paragraph could have been interpreted as suggesting that Australia's future tariff rates were creating that uncertainty, whereas in fact I think your evidence just now was suggesting that there are many more macro factors that are affecting your investment climate and that the Australian tariff rate would be just one of those.

MR OSBORN: No, no. Let me go back on that, and please do not misunderstand me on the point. We are talking about some investment decisions associated with general sheet and foil products for the Australian market, and that has been part of our strategy to grow volume to improve our competitive base here. Those investment decisions are significantly impacted by the tariff regime that may or may not be in place, so that is why we regard this hearing as being very very important for the business, so please do not misunderstand me on that point. This is a key issue.

MR COSGROVE: I think we can understand that it is a factor in your investment decision-making but, as Mike was suggesting, there seemed to be a number of other factors that would be taken into account in a long-term investment decision - - -

MR OSBORN: Yes.

MR COSGROVE: Obviously the cost of capital is very important.

MR OSBORN: Yes.

MR COSGROVE: You would need to have made projections as best you can, and we realise they're difficult, of trends in your input prices - - -

MR OSBORN: Yes.

MR COSGROVE: Which to some extent of course would be driven by global market developments in the price of alumina, for example, or even at an earlier stage, bauxite. Then you have your sort of management-driven costs of operation, which you referred to a moment ago, like work arrangements. So we tend to think that you are going to be influenced by all of those, and why should one be more critical than others.

MR OSBORN: Perhaps let me explain. We have been for the last 18 months studying what our strategic options were in relation to our general sheet and foil business. We have done the business analysis, have done an analysis of what capital would be required at the facility; have made all those decisions; have come to the point of putting capital requests together with all the economic analysis at the stage where these hearings loomed on the horizon where we have a whole range of inputs where we have made some decisions on, and now we have another input which has the impact to take that from getting an acceptable return down to saying, "Where do you sit?" in an environment which says, "Australia wants to move ahead" - let me phrase this fairly carefully - "for our segment of the business seems to want to move ahead of every other country"

That signal is one which really gives concern to my board because they have their own options in terms of their own global operation, so I can sit here and represent Australian interests and Australian employment and so forth, they will make decisions based on - you know, they've got mobility of capital in terms of where they invest overall. So that tends to say if you happen to be a rolling mill operator, Australia has some strategic advantages in terms of its access to molten metal, in terms of proximity to Asia and some other things, but it also has some disadvantages - and David talked about we have a very high commitment to environmental performance, we have a very high commitment to health and safety, and properly so. You kind of balance all those out with your investment decisions. It just seems the scales are kind of getting weighted against you if you look at that dispassionately from a global viewpoint.

MR WOODS: You refer to looking at opportunities for import replacement of general sheet, eg the transport industry, and I don't know if you're referring to ferries and other things that consume - - -

MR OSBORN: Certainly in the marine applications which have been growing.

MR WOODS: Presumably if their purchases were becoming cheaper they may even be able to increase volumes of production which may create even further opportunities for your business in terms of amounts produced and spreading your costs across greater volume.

MR OSBORN: That would be an interesting analysis to go through and say whether that amount of growth is - you've probably got to treble or quadruple, I suspect, to get into that level.

MR WOODS: Yes. It's just part of the balance that you were referring to earlier, that there are many sides to weigh up and one needs to look carefully at obviously - - -

MR OSBORN: At all of them, yes.

MR WOODS: - - - both sides of the scale and what's in it.

MR COSGROVE: I take it you're not suggesting in the submission, Wayne, that these recent decisions to expand productive capacity in countries like South Africa and Korea are related to Australian tariff developments or - - -

MR OSBORN: No, I don't believe they are, John Cosgrove, I think what it does is for the company in South Africa, it says, "If they look around, what is an easy target for a market where there is no tariff", you know, "Australia is sitting there." So I don't think that was fundamental to their decision-making, but it gives them opportunities and that's kind of how the market operates obviously.

MR COSGROVE: Yes. Some might argue that a decision on the part of a business firm to invest in a country where tariffs are high is more hazardous than a decision to invest in a country where tariffs are low because of the risks associated with governmental decision-making. There is, notwithstanding what has happened in Seattle, I think still a general direction of industry assistance which is downwards rather than upwards around the globe, so if you look at some of these countries with tariffs in the range of 10 per cent plus you might think, "Well, if I go in there I might be okay for a while but how will I be in the medium to long run?" Isn't it better for a business firm to be in control of its own affairs, not reliant, in any significant way at least, on government assistance?

MR OSBORN: Far be it for me to make too much comment on that, but I think obviously other companies have found that investment environment conducive, that they have committed significant capital. If you look at the investment in South Africa, they're trying to build a new nation from a pretty sorry history, I guess, so you have perhaps some things that override economic theory in that situation in terms of their decision-making. So I'm not sure the investment process can be totally rational, I guess, in that sense,

MR COSGROVE: Could you tell us a little about how you price your own export sales? In particular, are they priced on the same basis as your domestic sales or is there some element of what you referred to earlier, on the part of other countries, as incremental pricing, involved?

MR OSBORN: No, it would be very difficult for us to price incrementally if you look at it in a sense of 40 per cent of the business being exported overall. They are generally annual contract negotiations. The nature of the business now is there has been significant consolidation of purchases, so people are buying on not quite global purchasing arrangements but very similar to that basis. The folks we sell to in Australia are very aware of the prevailing prices in the Asian region. They are a factor in the negotiations, so generally the industry information is available in the pricing environment, so it is relatively open in that sense.

MR COSGROVE: On the work arrangement side, do you have practices in place which enable you to operate your capital equipment on a full-time basis?

MR OSBORN: Yes, most of our facilities. Some of the areas don't operate totally on a full-time basis but most of it is seven days a week, 24-hour basis.

MR WOODS: You quote an article in a newspaper talking about a decade of rapid tariff cuts made Australia the most open market for imports in the western world, and presumably you're quoting that with some sense of agreement or approval. If we are an open market then to what extent does the removal of our final 5 per cent of general tariffs constitute a bargaining element to encourage others to reduce their tariffs further? Has its value diminished significantly, as this article would suggest by the fact that we are now perceived to be an open market, and therefore retaining that last 5 per cent as some way to gain leverage may have very little value?

MR OSBORN: No, I would disagree with that because it depends on the sector. If you happen to be in the cansheet sector, people are well aware of the changing tariffs - that is now a zero tariff sector - that people who are importing in the general sheet and foil sector have a very high awareness of the tariff levels.

MR WOODS: They may have a higher awareness of it, but is a 5 per cent general tariff still effectively seen by most people as making Australia "the most open market for imports in the western world", and therefore offering up that final 5 per cent to some form of international negotiations is not offering up very much?

MR OSBORN: I think that's well beyond my expertise to actually comment on that point.

MR WOODS: It's just that your submission suggested some form of reciprocity was an appropriate policy of saying that we shouldn't be reducing ours until we could get others to reduce theirs further, suggesting it was a bargaining, a negotiating tool.

MR OSBORN: I don't think we were suggesting it was so much as a negotiating tool in terms of the machinery of how that might be achieved, but in terms of how this industry sees a level playing field, that is our belief, that there should be reciprocity in tariff reduction overall. I just cite the examples where we've had to search for new markets for 30,000 tonnes of business because of the reverse situation which makes life very difficult for an Australian manufacturer.

MR COSGROVE: That's happening in lots of markets, not just aluminium markets, I mean every day of the year of people competing for business.

MR OSBORN: I'm sure it is.

MR COSGROVE: In that same context though, Wayne, there is the Australian government and other government's commitments in the APEC region to free trade by the year 2010, so would you expect that you're going to have to be competitive essentially with no tariff assistance by that time?

MR OSBORN: We would be very happy with a zero tariff situation. We have no argument specifically for retention of tariffs, it's the equality and even-handed market access that is really what we're about in that situation.

MR COSGROVE: But the APEC arrangements allow some of your competitors, the less developed members, to continue to apply tariff protection until the year 2020 under the APEC agreement.

MR OSBORN: Okay, right.

MR COSGROVE: Is that of concern to you in terms of maintaining the profitability of your enterprise?

MR OSBORN: It may be. It's not a question I feel qualified to give you an appropriate answer on at this stage.

MR COSGROVE: I think that's all the questions we have, Wayne. Thanks very much for the presentation today.

MR OSBORN: Thank you.

MR COSGROVE: Now, we had planned to take a morning tea break at this time. Our next participant is the New South Wales Farmers Federation, who are already here. We're in your hands to some extent. If you would like to appear now, we're quite happy to do that. I think we might continue, and if others would like to avail themselves of the tea and coffee outside then feel free to do so. Would you please introduce yourselves and indicate the capacity in which you appear today.

MR KEOGH: My name is Mick Keogh. I'm policy director of the Farmers Association.

MR GIDLEY-BAIRD: I'm Angus Gidley-Baird, research assistant at New South Wales Farmers.

MR COSGROVE: Thank you. We have received a copy of your submission but at this time I'm afraid I haven't had time to do it full justice. You might like to draw the main points to our attention.

MR WOODS: At the opening you indicated, in the version that we have, that this was a draft submission. Is that the submission you will be speaking to or are there any amendments? Is this the submission that will be going on the record?

MR GIDLEY-BAIRD: There are some slight amendments but no major - - -

MR WOODS: So in terms of discussion we can use this but you will be lodging a formal final submission today or soon?

MR GIDLEY-BAIRD: Unfortunately not today but hopefully early next week.

MR WOODS: Okay, thank you.

MR GIDLEY-BAIRD: First of all, thank you for giving us the opportunity to talk to you here today. The New South Wales Farmers Association represents over 15,000 members from a broad range of agricultural enterprises across New South Wales. The agricultural sector relies heavily on international trade, both as a source of income and as a source of farm inputs, and therefore issues concerning trade restrictions are of great importance to the agricultural sector, not only because of the direct effects but also through indirect effects such as the reciprocating or the retaliatory actions.

The association is of the broad belief that the tariffs and other protection measures restrict the efficient allocation of resources and impair the nation's ability to grow through international trade. The association therefore broadly supports a move to remove the general tariff arrangement. At the same time, however, we recognise that there may be some specific cases where the tariff is necessary and the overall benefit to the community substantiates its retention. In this case we believe the onus of proof must remain with the individual business or industry to prove the need for the tariff to be retained.

Just broadly on the benefits and costs to Australian producers, we can't actually comment on the costs and benefits of removing the individual tariff lines and talking with specific numbers. However, we can make some general conclusions. Many of the agricultural food products listed with the eight-digit level, I think it is, we would assume have an equivalent Australian processor. However, the extent to which producers receive higher prices because of the tariff are unclear and many of the producers would in fact argue that the benefits of this tariff are not actually passed on to the producers themselves through the form of higher prices.

The association recommends that in the situation where the tariff is removed the ACCC, or a similar body, be appointed to ensure that the cost of removing the tariff is not actually passed on to the producer through a form of reduced prices. At the same time it probably should be noted that if the case was to be shown that the tariff does allow a higher price than what might be received, and the removal of this tariff would probably result in a reduction of the price to the producer, it would be our understanding that such a situation should be allowed. However, we suggest that the ACCC, or a similar body, be appointed to monitor such situations.

In terms of other items at the eight-digit level, the association believes that the benefits of removing the tariff would outweigh the costs. Many of the items listed include numerous mechanical parts, chemicals and other farm inputs which, when combined, represent a significant cost to the running of a farm business. Just in terms of trade aspects, the Australian agricultural sector is expected to receive significant gains through the trade liberalisation process and, given that Australia's general tariff is one of the highest amongst developing nations, the removal of the general tariff may provide some opportunity to call for the removal of similar tariffs in other countries. However, it should be recognised that the benefits of trade liberalisation are geared mostly to those who remove the protection first.

In light of this, together with Australia's commitment to the Bogor agreement in APEC, the association recommends the removal of the general tariff, consider reciprocating arrangements and calling for reductions in tariffs in other countries, but not to postpone any decision because of them. In the case that the general tariff is not removed and would possibly be reduced, or no action is taken, the association would recommend that the tariff concession scheme and similar arrangements be retained, as they relate to import goods not manufactured in Australia.

Finally, in conclusion, I would just like to reinforce that the association recommends that the general tariff be removed because it would provide significant benefits in the terms of reduced costs for agricultural producers, and that further details would probably be contained in our submission.

MR COSGROVE: Thank you, Angus. Are you able to give us any specific examples today of benefits which you feel would be gained by your members as a result of a reduction in the general tariff?

MR GIDLEY-BAIRD: Not actually today, we haven't got specific figures. It would probably be something we could look into though. But generally, in terms of the cost of their production and just roughly looking over a list of the tariff items, there are a significant number of their - even down to the small gaskets or things used in mechanical production - that when added together represent a fairly significant cost to the whole running of a farm business.

MR COSGROVE: Yes. If your final submission could give us a few little examples of that kind, I think it would be worth knowing about.

MR GIDLEY-BAIRD: Yes.

MR COSGROVE: I have some questions for you: the executive summary, this is page 4 and you mentioned this in your opening remarks, you say that review and removal of tariffs should be conducted on a case-by-case basis to ensure that industries that might be termed infant and requiring assistance are identified, allowing concessions to be made. How would you see that actually operating in a practical sense? Do you literally mean tariff line by tariff line?

MR GIDLEY-BAIRD: No, not as such, in that the list of tariffs is fairly specific and detailed and to go through each one individually would be probably another cost in itself, but to identify specific industries or perhaps businesses within those industries that do require such a tariff to operate. It was more to encourage the development of infant industries rather than to provide protection as a type of long-term ongoing thing to those businesses which should be able to compete internationally.

MR COSGROVE: What would you think of as an infant industry in Australia?

MR GIDLEY-BAIRD: I'm no expert in terms of how long it takes to set up a business, but something that would allow it time to establish domestically and then reach a stage where it could compete internationally.

MR WOODS: That compares with a comment you make in your submission, where you're suggesting that following the line that any assistance should be decoupled, the general tariff on all items should be removed and, if necessary, some other form of assistance be provided to developing industries or businesses. What did you have in mind by "other form of assistance"? I'm trying to reconcile that comment with your recommendation which ties case-by-case to infant industry approach. Would you, on reflection, try and reconcile those two points and suggest removal of general tariffs and, as you say here, look at some other form of assistance to developing industries?

MR GIDLEY-BAIRD: I think in terms of what I was trying to say there was just, if assistance was required, to provide some form that doesn't impede international trade flows or trade flows themselves, and is removed from tariffs or subsidies or the like, but to provide a more indirect form. I couldn't suggest a specific type because it would probably be industry or business.

MR WOODS: Specific, yes.

MR GIDLEY-BAIRD: Specific. Something that - - -

MR WOODS: But if you could look at that proposal at the same time as looking at your recommendations, because there seems to be a tension there between the two. On the one hand you're suggesting a case-by-case examination of tariff removal to protect infant industry, but here you're suggesting that maybe decouple the lot and look at other forms of assistance. So any opportunity to try and reconcile those would be helpful to us.

MR COSGROVE: In that same vein, Angus, as you look at the recommendations on page 5, a couple of questions emerge. The first is whether what - well, the fifth recommendation, even though they're not numbered, the recommendation that all tariffs on imported agricultural machinery, spare parts, be removed. Should we take that as a free-standing recommendation which applies regardless of other recommendations in your submission, or is it somehow a subsidiary of the more general recommendation, the first one that we've been discussing?

MR GIDLEY-BAIRD: No, I think it should probably be interpreted as a general-type - it was probably one more to comment on here but it was a specific piece of policy that we've got, and I interpret it to mean applying to all inputs used in the agricultural process - - -

MR COSGROVE: Yes, I understand that, I think. But the question is whether that particular recommendation stands on its own or is, in some way, contingent upon the more general recommendations earlier in that list.

MR KEOGH: I would tend to think that would stand pretty much by itself.

MR COSGROVE: Yes.

MR KEOGH: That in terms of those particular inputs to agricultural industries, we don't see any justification for maintaining those sort of arrangements.

MR COSGROVE: Fine.

MR WOODS: Does the time frame of your second recommendation of removal in the year 2005 apply to that recommendation?

MR KEOGH: I think most of our members would argue that that recommendation should occur as soon as possible.

MR WOODS: In which case if you could again clarify, because it was uncertain as to whether or not that 2005 time frame applied to all of your recommendations or whether some of them were separate and free-standing.

MR GIDLEY-BAIRD: I think just on that, it was more a date that I thought would be appropriate rather than basing it on any expert knowledge as such, in the fact that there will be considerable domestic microeconomic reform and tax reform in the next couple of years and given Australia's commitment to remove or reduce tariffs by 2010 I thought it was sort of an appropriate medium that would allow us to receive some benefits, but at the same time allow for domestic businesses to overcome some of the reforms that are occurring at the moment.

MR WOODS: Yes, in fact on page 7 you go into some argument as to why 2005 is an appropriate time, which we've taken notice of. Interestingly, in that particular point, you talk about providing some political leverage going into trade negotiations. Do I take it from that that your view is that by moving to zero in fact gives greater political leverage than offering up the final five?

MR GIDLEY-BAIRD: Again, it's very difficult to comment but it seems that people, or countries, in removing or reducing tariffs are not always successful in creating reciprocal arrangements with other countries, and I don't think removal of our tariffs should be based solely on the fact that we're trying to achieve some other removal from or reduction in other countries, in that negotiations seem to be continuing forever and indefinitely and not a lot of results are being obtained.

MR WOODS: Presumably you see that there are sufficient benefits to the Australian economy from the removal that warrants that action, irrespective of reciprocity occurring in the negotiation forum.

MR GIDLEY-BAIRD: Yes.

MR WOODS: Is that the line of your argument?

MR KEOGH: Certainly the line of argument has been that in terms of resource allocation efficiency those are the benefits that an economy derives by moving ahead of the pack, and when the inevitability of some of those trade measures eventually unfolds you're much better positioned to make advantages out of that than you are in being at the same state of progression in terms of trade removal.

MR COSGROVE: You mentioned near the bottom of the recommendations page that the government continued the planned reduction of the tariffs in the car and TCF industries, so you're accepting the existing schedule which the government announced a couple of years ago for those two industries - no action now until 2005 and then a movement towards the free trade commitment in 2010. Is that right?

MR KEOGH: I think we're accepting the political realities rather than the technical benefits.

MR COSGROVE: Yes.

MR KEOGH: I suspect we would always argue that in terms of both those industries a more urgent removal of those tariffs is of significant benefit to the agricultural sector. I mean, motor vehicles are a fairly major input into a lot of farm businesses, and we're still talking about two and a half thousand dollars odd extra costs associated with that as a result of the existing tariff arrangements. I think we would always argue that a quicker removal of those might be desirable, but I suspect the political realities are not going to achieve that ahead of the schedule.

MR COSGROVE: Is the TCF sector as important for farmers as the motor vehicle sector?

MR KEOGH: Perhaps not as important in the sense that in both the cotton and the wool industry - I think cotton, 80 per cent is exported and wool 95 per cent is exported, so that component of domestic demand that those two industries derive is only quite small. That notwithstanding, I think it's been estimated that the costs of those arrangements for, for example, wool textiles in Australia, add about 50 per cent to the cost of fabric used in clothing manufacturing.

MR COSGROVE: Yes.

MR KEOGH: I think a lot of farmers would argue that clothing isn't a big component of their overall costs - a pair of overalls and a few things like that - but nevertheless in terms of the overall demand in the economy there is probably a marginal gain there if that extra cost that's added by the tariffs - you know, we might see a small expansion in domestic demand, notwithstanding that it's such a minor market for those industries that it really doesn't have much impact.

MR WOODS: You argue in your submission of the benefits of the removal of the general tariff but then on page 8 you have a sentence that says:

> It is difficult to ascertain whether the removal of the general tariff will lead to the development of sustainable and prosperous industries within Australia.

That's the top of the second substantive paragraph. I'm not quite sure of the point that you're making there, given your argument of the economic benefit of removal of the general tariff. Perhaps it's something you might want to reflect on when you're finalising your report.

MR GIDLEY-BAIRD: Yes. I think in terms of that it was difficult just coming up with figures of costs and benefits whereas in a more theoretical-type approach the benefits can be proven.

MR WOODS: Yes. All right, I'll leave that to you.

MR COSGROVE: Angus, one point to which you referred in your opening remarks and which is mentioned initially at the bottom of the recommendations page with a little more material on it at the bottom of page 12 and the top of page 13 was this question about the ACCC being asked to ensure that the cost of removing the tariff is not passed on to producers through lower prices. I'm not quite sure - - -

MR WOODS: Lower prices for producer product is how I understand it. But could you clarify that?

MR COSGROVE: Yes, could you clarify that for me?

MR WOODS: Is that the correct interpretation?

MR GIDLEY-BAIRD: In terms of the tariff providing some form of assistance to the processor and them passing on that assistance to the producer in the form of higher prices - but the extent to which that occurs is very unclear, and many would argue it - - -

MR COSGROVE: What sort of tariffs do you have in mind here? Are these tariffs on inputs?

MR GIDLEY-BAIRD: The general tariffs, such as processed food and dried fruit and what have you; the fact that the tariff exists allowing domestic processors to receive higher prices for their product - - -

MR COSGROVE: Higher prices - yes.

MR GIDLEY-BAIRD: - - - and whether they pass that on to the producers.

MR COSGROVE: I see what you mean.

MR GIDLEY-BAIRD: In terms of the product that they buy from domestic producers for their production process.

MR COSGROVE: Yes.

MR GIDLEY-BAIRD: Whether that's passed through.

MR COSGROVE: Yes.

MR WOODS: Do you have particular examples of industries in mind, or segments of your industry in mind, when you make that point? If so, are you prepared to include those in your submission?

MR GIDLEY-BAIRD: Right. Yes.

MR COSGROVE: I think I can understand the conceptual point now, but how significant is it in practice?

MR KEOGH: It varies across industries, and I think what we're talking about is seeing a concentration in the markets for a whole range of agricultural products, and

I suspect the recent inquiry into the retail sector was a reflection of that phenomenon where, for example, a lot in the horticultural sector would argue that in terms of their fresh produce, they're reduced to two markets, and not a great deal of transparency between those markets about pricing and volumes and all those sorts of things. So when you get to that level of concentration the transparency disappears in the market and it's very hard to determine whether in fact a benefit such as reduction in that tariff would in fact be passed through to the producers, and that's I guess a common problem right across.

MR COSGROVE: Yes.

MR KEOGH: Certainly in some of those processed food, fruit and vegetable industries. I think that's one that, as the concentration in those industries downstream occurs, the producers would be increasingly concerned that we're not seeing a transparent market that behaves as it should.

MR COSGROVE: Although I think some of the recent inquiries that looked at that also found, in some cases at least, that the terms of contract offered to efficient suppliers of fresh foods and so on were to the suppliers' advantage; they were put in a more secure position in terms of the period of contract and were able to be assisted in some way to increase their efficiencies. I'm not sure of all the details, but it wasn't completely a one-sided story.

MR KEOGH: No, and I think the reality is - as we've indicated - somewhere in between 70 and 80 per cent of agricultural products end up exported.

MR COSGROVE: Yes.

MR KEOGH: If you have a close look at, for example US beef prices and US beef supply and demand conditions, that's basically the driver of the price here, so a lot of agricultural producers are always caught in that situation where the key driver of their price is in fact export conditions, and the domestic side of it is a bit of a wash-back from that, if you like, in terms of what's left over.

MR COSGROVE: Yes. Thank you. This may be a related point to the one we've just discussed. Down the bottom of page 6 you say:

> On the domestic front allowances should be made for the implementation of the new tax system and any national competition policy arrangements that may specifically affect certain industries.

Could you again try to tell us what arrangements and industries you have in mind there?

MR GIDLEY-BAIRD: As in competition policy arrangements?

MR COSGROVE: Yes. Which aspects of national competition policy and which industries need allowances to be made for them? I think you develop the tax point a little later in your submission - or it may be another submission. I've been reading too many. I'm sorry. Anyway, could you try to enlighten me on that, please.

MR GIDLEY-BAIRD: Yes. The competition policy arrangements - we probably aren't able to comment really on how they are affecting specific businesses and processes that receive the direct benefits from the general tariff, however situations in rural Australia such as the deregulation of the electricity scheme and what have you, and the actual effects on rural businesses - the benefits that are being perceived to come from the national competition policy arrangement, I think it's been pointed out, are not always going to accrue to rural businesses, or not to the same extent that they accrue to other businesses.

MR COSGROVE: Yes.

MR GIDLEY-BAIRD: So in terms of those effects I think it just needs to be considered from a perspective of those businesses in rural Australia; they're not at the same level or possibly not receiving the same benefits that some of the businesses in metropolitan areas are.

MR COSGROVE: So you see that as reinforcing the case for the tariff to be lowered?

MR GIDLEY-BAIRD: Yes, but in terms of processors that are located in rural Australia, if they're not receiving the same benefits as processors located in metropolitan areas, I think rather than just grouping together, consideration just needs to be made in terms of the effects there.

MR COSGROVE: How could that be done by use of tariff policy, though? We can't have a two-part tariff, so to say - one for the city producers and one for the producers in country areas.

MR GIDLEY-BAIRD: No, I'm not calling for that at all, but just in looking at the removal or reduction of the tariff consideration needs to be made that not all businesses are the same as metropolitan businesses, in that there are some in rural areas that might in fact face the same cost structure because of these competition policy arrangements.

MR COSGROVE: So I'm not quite sure, again, what the practical policy significance of that is. Does one need to consider other elements of policy - ie non-tariff policy - to accommodate the different position of some processors or producers?

MR GIDLEY-BAIRD: I think that probably comes more under the actual competition policy arrangements themselves and the removal of the general tariff is probably a separate issue altogether.

MR COSGROVE: Yes. Under Concession Arrangements, the bottom of page 11, you say:

> If the general tariff is not put at zero but reduced somewhat the tariff concession scheme duty rate should remain at the same rate, so if the tariff was reduced to 2 per cent or less the concession would mean that no tariff was paid on those imports.

Why in that situation wouldn't you prefer to have the actual concessional rate set at zero rather than 2 per cent? There seems to be no concession if both the general rate and the concession rate are the same?

MR GIDLEY-BAIRD: I think the basic principle of the concession rate is to allow those imports that don't have a domestically produced competitor - are not taxed in the same way.

MR COSGROVE: Yes.

MR GIDLEY-BAIRD: So that the users of those imports aren't at a disadvantage just because there's a general tariff and they can't afford - or it's not supporting a domestic industry.

MR COSGROVE: Yes.

MR GIDLEY-BAIRD: I think I also made the point that if the tariff is reduced to a level of 2 or 3 per cent then it probably needs to be considered as to whether the benefits of retaining such a concession arrangement - probably need to be considered, but we would prefer it that imports coming into Australia where there's no domestic competitor should not be taxed at the same level as those imports coming in that are competing with domestic - - -

MR WOODS: So we should read that second-to-last sentence as being that there be a concession of 2 percentage points on the prevailing general tariff rate - - -

MR COSGROVE: Yes. Yes, I see.

MR WOODS: - - - rather than that the concession rate be 2 percentage points?

MR GIDLEY-BAIRD: Yes.

MR WOODS: Okay. Fine.

MR COSGROVE: And again on concessions, at the top of the next page you say you believe that:

> A cost-benefit analysis needs to be conducted for each concession arrangement to ensure that it is economically viable.

What do you mean by the word "each" there; each scheme and not, I take it, each individual order?

MR GIDLEY-BAIRD: Yes. Again, this is going back to the question you asked before in terms of identifying each individual item.

MR COSGROVE: Yes.

MR GIDLEY-BAIRD: I don't think - - -

MR COSGROVE: Yes. Okay.

MR GIDLEY-BAIRD: - - - such an activity would be really warranted in terms of the cost point of view, but broadly speaking, business is all groups of imports.

MR COSGROVE: Yes. We touched on this a few moments ago, Angus. I think it's more a question of the heading throwing people off track, at the bottom of page 12, Goods with No Significant Australian Production. The remainder of the discussion there seemed a little disconnected from that point. I may be missing something, but you might like - when you're reviewing the final version - to have a look at how you introduce that. That's all I have.

MR WOODS: Yes, thank you.

MR COSGROVE: Okay, thank you very much for your draft submission and for coming along and explaining parts of it today. We look forward to the finished product.

MR GIDLEY-BAIRD: Thank you very much.

MR COSGROVE: Our next participant is Rodda Castle and Co, I think. Would you please introduce yourself and indicate the capacity in which you're appearing today.

MR RODDA: Certainly, Mr Commissioner. Ian Rodda, I'm a director of Rodda Castle and Co. My interest in this inquiry is that the bulk of my clients, who are from the mining, recording and computer industries - what they have in common is that none of these industries has any assistance on their output and they do have tariffs on their inputs. That sort of dictates the direction I'm going to take. I sent my submission down last night. I doubt though that you've had the opportunity to have a - - -

MR WOODS: No.

MR COSGROVE: I'm afraid I've only skimmed it, so you might like to take us through the essential points, please.

MR RODDA: Okay. The first matter that we've addressed ourselves to in the submission is the question of whether we need a general tariff in the longer term. Certainly my clients' perspective is that we certainly don't. The sooner we go to zero tariffs across the board, the better. The mining industry in particular is one - I say the mining and agriculture industries for that matter are two industries whose capacity to be competitive on world markets is hampered by the fact that there are taxes on the production side of their operations. I think it's pretty clear that if those taxes are removed the cost competitiveness of the industries would be improved quite significantly.

In fact a couple of years ago - just to illustrate this point - one of my clients, South Blackwater Coal, developed a greenfield mining project at Kenmare in Queensland and the total duty that was payable on the various items of capital equipment that were purchased for the project came to around a million dollars. We applied for policy by-law under item 45 - and I've referred in this submission to the fact that it's only just been resolved in the last few weeks, this application - but at one stage the managing director of the company wrote to the minister - no, I'm sorry, it wasn't to the minister, it was to the Mortimer inquiry - and pointed out that with some of the producers being only marginally viable because of competition from Canadian and Chinese coal producers, some mines in Australia were producing coal at a profit of only around five cents a tonne.

This million dollars duty that was required to be paid in relation to the equipment that had to be purchased to develop a new mining project represented something like the profit on 20 million tonnes of production, and 20 million tonnes roughly equals the reserve of a small mine. When you see the tax effect of tariffs in that sort of context, you can really appreciate just how it does go to the heart of competitiveness of industries that are competing in world markets.

So our clients' preferred position, of course, as I've suggested, is that we remove tariffs across the board. We accept the political realities of the fact that that isn't going to happen overnight. The present government has to face an election within the next couple of years where the voters will still have fresh in their minds the impact of the GST and with only a five seat majority in parliament I would expect that no-one is going to throw petrol on the fire by removing tariffs as a platform for the next election.

We anticipate that tariffs will be removed consistently with our APEC commitments and one of our requests is that the general rate of 5 per cent just be retained at the present level until 31 December 2005, and then phased down to zero to give effect to our APEC commitment. I haven't said this with tongue in cheek - admittedly we could have suggested also that the general rate be phased out at the rate of 2 per cent per annum commencing now and still wind up at zero in 2010. We've suggested keeping the present general tariff until 2005 only to pay lip service to the political reality that it's just not going to be practicable for a government to do that before 2005, I would think.

That brings me to my next request, though, in relation to the 3 per cent revenue levy that is currently imposed on business inputs. I know that was put there at the behest of treasury to fill the 9 billion - or whatever the sum was - black hole in 1996. In fact, John Moore - who was then the minister - asked me to do him a paper on the approach that might be taken to filling some of that deficit, because obviously some kind of a short-term levy was one of the matters under consideration. My suggestion was that we abolish tariff concessions on consumer goods, so it was interesting to see that treasury's recommendation was that we do the opposite. My clients in particular were terribly unhappy about this for reasons that will become apparent later in the submission. A tax on business inputs particularly for those industries that have got zero assistance on their output just didn't seem to make very good economic sense although it may have made good sense from the government's perspective in getting its hands on some money in the short term.

In deference to the political realities we've also requested that the tariff concession system should be retained to provide for zero tariffs on any goods for which local industry doesn't manufacture a substitute. We've also requested that the criteria for the tariff concession system be changed. As you're probably aware, there's been a lot of litigation over the years on the intended effect of the tariff concession legislation. I've expanded on that point later in the submission so I won't touch on it now.

We also request that the policy by-law system be retained in the event that the general tariff rate of 5 per cent be maintained because there are national interest considerations that we think really demand that encouragement be given to those industries which are export oriented, particularly mining and agriculture. What I'm saying there in effect is that the government should have a policy of picking winners and assist mining and agriculture in particular at the expense of the engineering industries. I say that only because the mining and agriculture industries do contribute the bulk of our export revenues and it seems to me to not make very good economic sense for those industries to have their international cost competitiveness affected adversely through the desire to provide assistance for another industry that doesn't provide anywhere near the same sort of contribution to national revenues and to GDP.

In making that request - it's actually on page 2 of the request - I've just spelt out some criteria which we think the government ought to be taking into consideration as a basis for maintaining a policy by-law system to operate quite separately and independently of the tariff concession system. What underlies the distinction that I'm making between the two situations, or the two concessional systems, is that with the tariff concession system we're seeking only the removal of protection for those industries - or in those circumstances where there is no local industry to protect. But a policy by-law system really has a different kind of effect altogether. It is really intended to favour one group of industries over another, and that is a different kind of national interest consideration altogether. I've explained and expanded on that point a little later in the submission.

I'll take you now to section 3 on page 4. The arguments for retention or abolition of tariffs are pretty well known and what I've done here is plagiarised the Industry Commission's 1994-95 report on this issue. I thought that the observation that was made on, I think, page 19 of that annual report summed the whole issue up very succinctly. For the benefit of the commissioners I've just reproduced that section here. I think it says it all. We did note that the commission did say in that report that once the tariff reduction program finished in 1996 - bearing in mind this is the 94-95 report - that when the tariff reduction program finished in 1996 that the cost of tariff protection of the manufacturing sector would be costing consumers around $4 billion per annum.

We're mindful of the fact, though, that that figure includes protection for the passenger motor vehicle and TCF industries. For the rest of the manufacturing sector generally I would think that the figure was considerably less - perhaps only in the order of a billion to perhaps one and a half billion. So looked at in that context I suppose the equation now becomes, "Is the cost to the community of one and a half billion dollars per annum a justifiable expense having regard to what would be the cost of removing it? What would be the cost to the community generally of not having that tax in place?" That's the issue we've really posed in making this submission.

As I've said on page 7, that particular issue raised by the commission in that annual report brings us to the heart of the matter for this inquiry. I've referred there to some of the measures that have been used in the past, the gross subsidy equivalent definition, the net subsidy equivalent definitions that were defined so carefully in the 1973 IAC annual report. Some of the measures that have been used to quantify the cost of protection to the community generally - and in particular to look at issues such as the cost of having employment in particular industries - I know these were always wonderful arithmetic exercises and I can remember in years gone by, when I gave evidence at industry-specific inquiries, it was always fun to sit down and work out an effective rate of protection and the gross and net subsidy equivalent costs for protection, but by the year 2000 I have to confess I've got some doubts as to the validity of what we were really doing when we did those exercises, because I don't think they ever told us the whole story.

This was really brought home to me recently in matters that have got nothing to do with reductions in tariff, for example, but the small town of Aberdeen in the northern part of the Hunter Valley recently had its abattoir closed and several hundred people lost their jobs. That abattoir was the principal employer in that community. With people losing their jobs the effect on the community across the board was really quite devastating.

It wasn't simply the loss of household incomes that had to be taken into effect. There was the fact that with people suddenly being unemployed and having to leave no-one could sell their home, so the value of property declined. Small businesses that relied on the community's population being at a certain level suddenly found themselves no longer being viable because the level of population and the level of community income suddenly had declined to a point where small businesses in the area couldn't be maintained either. So there was a ripple effect right through the whole community.

That didn't come about because of any adjustment in tariff policy. It came about for other reasons altogether, but there have been more recent examples where the impact of tariff reduction policy has been noticeable. In the town of Taree - or Kempsey - the King Gee factory closed. Not so long ago the Berlei factory closed in Lithgow and the people there lost their jobs. Lithgow, in particular - there was quite a significant effect from the closure there because there had already been mine closures in the area which had an effect on employment in the mining sector. Then there's the industry that has been in the news for the last couple of days where the Prime Minister unfortunately mentioned to the people affected that they were victims of economic reality. I wonder if he'll be a victim of political reality in the election. Perhaps it wasn't a terribly sensitive thing to say.

Even so, we can see - and it's unfortunate that I need to refer to the TCF industry as an example of the effect on a community because we know that TCF industries are very significantly overprotected anyway - but the same kind of impact can be felt in other sectors. I could well imagine, for example, the impact on, say, the Wangaratta region of northern Victoria if the Bluegum Technology plant - which is the old IBM factory - were to close. The effect on that community would be utterly devastating. These are the sorts of things that really do need to be addressed, I think, in an inquiry of this kind. I just wish I had the resources myself to undertake that kind of analysis but, unfortunately, I don't. I'm sure that this is an issue that's going to be of major concern in this inquiry. It's certainly the sort of thing that the government will want to be advised on.

I think there's probably not more that I can say on that. As I said, the arguments are so well known there's probably no point in going over them again. The only other thing I would mention, though, is that if we do retain the general tariff at the rate of 5 per cent, the nominal rate for most industries taking account of freight and the various other factors that go into calculation of the nominal rate, it's probably only going to be between 4 and 4 and a half per cent anyway. So I just pose the question as to whether the community at large might think that a tax on imports, which has the effect of raising prices between 4 and 4 and a half per cent, is a price worth paying to maintain employment in industries that are currently protected by that 5 per cent tariff. No doubt that's a matter you will be turning your minds to.

I did refer also to some of the effects that will obviously follow from the removal of tariff assistance. These will no doubt be matters that the commission will be turning its mind to. They start on page 10 but these issues, I think, are probably so well known anyway that I needn't elaborate on them.

I'd like to turn now to our observations on tariff concessions. This commences on page 4. Of course, if the government does decide to abolish tariffs across the board then everything that follows in our submission is superfluous. However, on the assumption that the government isn't going to suddenly abolish tariffs, then there is perhaps some point in making these observations. We do think that a tariff concession system should be retained for the very simple reason that if we're going to maintain a 5 per cent tariff then it's not going to be for simply the purpose of raising revenue which, of course, is another valid reason that a government might decide to have a tax on imports anyway. The revenue considerations are obvious.

In the event that a tariff is maintained for the purpose of providing some measure of protection against import competition for the manufacturing sector, we think that there should be a relief mechanism in those circumstances where there is no local industry to protect, and a tariff concession system is probably the most convenient vehicle for that purpose. We do have a concern, though, about how this might be given effect because attempts over the past 15 years or so to properly define the circumstances in which relief from a general tariff can be given have been the subject of a few problems. There's been a lot of litigation. I thought the recommendations that the IAC made in 1984 about identical goods and similar goods were very good definitions from the economic perspective because they gave effect to the twin principles of trading in an environment of perfect competition, which is the identical goods concept, and trading in an environment of imperfect competition, which is the similar goods concept.

Unfortunately, it seemed, though, that those responsible for administering the legislation didn't really grasp the economic principles that underlay the legislation and the result was we finished up in court. I think the case that first brought this matter to the attention of the lawyers was the Davies Craig case which was a decision of the Administrative Appeals Tribunal which then went on appeal to the Federal Court. Unfortunately, the judge's efforts to give a commonsense meaning to what the legislation said resulted in further confusion. So in the end it was decided that the legislation should be amended, and I don't think the amendments necessarily improved the situation.

I think it would be nice if we could go back to that kind of concept where if you've got anything which is a substitute for something else in conditions of either perfect competition or imperfect competition, then you don't get a concession. You have to show that there's no substitute in those circumstances to get your concession. I think it might be helpful this time, though, if instead of leaving the drafting of the legislation to the poor old bureaucrats, we got a few lawyers in there who do actually understand the principles here and got them to assist. I guess that will be a matter for the commission as to what tack it wants to take.

With the policy by-law system, as I mentioned before I see this as really giving effect to a different set of national economic interests. This really should be the vehicle through which the government favours some industries over others. Obviously, the critically important ones are those that contribute the bulk of our export incomes because they are always confronted with realities of competition on the world stage. I might just mention that, in my view at least, the policy by-law system has been administered so poorly since November 1994 onwards, or maybe December 94 onwards, that today it simply does not give effect to the underlying beneficial purpose.

I think that comes about because there's no longer a recognition of the purpose for which it was introduced. I've said something in there of the history of the policy by-law legislation. It first got under way I suppose in a theoretical sense in 1988 but probably more practically in 1989 when the then government made its decisions on the IAC's report on the mining, construction and agricultural equipment industries. Item 45 and 46 were introduced to provide relief from duties for goods for use in mining and goods for use in the agriculture industries. It's important to recognise that at the time that the policy by-law system was introduced the tariff concession system allowed the entry, free of duty, of goods in two different categories or two different circumstances.

The first was where it was established that there was no local manufacture of substitutable goods or, alternatively, free entry was also allowed in circumstances where there was local manufacture of substitutable goods but the making of a tariff concession order would not have a significant adverse effect on the market in Australia for those substitutable goods. What that really meant was that the only goods that would be the subject of a policy by-law determination or decision would be those goods in respect of which there was local manufacture of substitutable goods, and the making of a TCO would have a significant adverse effect on the market for the Australian-produced goods.

This was a concept that, I think, was very well understood by those who had the responsibility for administering the legislation in the first five years or so after its introduction. With changes in personnel in the customs department from about that time onwards, that basic philosophy seems to have been well and truly lost. I think that if the policy by-law system is going to function in accordance with what was always its intent there needs to be a return to that philosophy. I've made some observations in relation to a small number of the existing policy by-law provisions, and commencing on page 16 I've made some comments about item 43. Now, although the legal provision for item 43 still exists in schedule 4 to the Customs Tariff Act, the fact of the matter is that there have been no determinations issued under item 43 since November 1994 - coming back to that.

I've made some observations here, and it might be worthwhile just having a brief glance through these because there are some points I want to make in relation to the utility of this particular by-law in relation to certain aspects of government assistance policy, in particular following the abolition of tariffs on mining and agricultural machinery in 1989. I might just pause for a moment and give you the opportunity to have a look through pages 16 and 17 and then I'll speak a little further on that.

That saga of the longwall mining machinery industry and its demise as a result of the decision not to issue item 43 determinations from late 1994 onwards I think is quite instructive on how the policy by-law system has been very, very poorly administered. It was interesting from my point of view - indeed, a lot of these companies were clients of mine, too, so I'm quite close to this. Quite apart from the work I do for the mining companies themselves, a lot of the mining machinery manufacturers were also clients.

So it was particularly distressing to see that following the abolition of tariffs in 1989, and the acceptance of the local mining machinery industry of that situation, that they all suddenly found that they were thriving by being able to import their componentry free of duty under item 43, because it then meant that if a local manufacturer wanted to tender for the supply of a major item of machinery to a mining company for a big project, that they would always be able to quote as world prices, which meant then that they would not be disadvantaged if a foreign longwall machinery manufacturer was also quoting or bidding for the same contract.

That ensured that the local industry was able to stay in business. I think at one point the turnover got as high as $800 million per annum, which is a pretty significant kind of an industry. I would say between 80 and 90 per cent of what was actually manufactured was Australian content. I mean BHP, for example, was a major supplier of steel for use in the construction of roof supports and armoured face conveyors. A lot of companies that manufactured hydraulics were producing rams for use in these things There were - no, there weren't, there were no chain manufacturers - a lot of flight bar manufacturers in this country. But all of these things, collectively, amounted to a very, very significant utilisation of Australian raw materials and Australian resources.

When the Australian Customs Service decided to stop issuing item 43 determinations for longwall components the local manufacturers realised that the only way that they would be able to compete with foreign suppliers would be to just import a complete unit because you can import a complete system free of duty, so what was the point of manufacturing locally? So they all stopped manufacturing. Because some of these companies are still clients I talk with them from time to time and say, "What are you going to do? Are you going to recommence manufacture?" and they've said, "No, not unless we get some certainty from the government that we're not going to be crucified."

So I think it's a tragedy that an industry that had a turnover, you know, at its peak of upwards of $800 million a year, should have fallen by the wayside because of maladministration of a system that was put in place for their benefit. Anyway, I make that observation. I've got a dozen stories I can tell you about the policy by-law system, but maybe we'll do that some other time. Quite interestingly, on the last occasion on which I lodged an application for an item 43 by-law for components for longwall equipment, I received a letter back from customs saying, "It's not government policy to give concessions on goods of this kind." So I went through the gazettes for the previous five years and made a note of every determination that had been issued for longwall mining machinery over that period of five years and said, "How do you explain this?" and I got no answer.

Now, on page 20 I've made some observations about item 45. When it was originally enacted item 45 - as I said before, tariffs on most items of capital equipment for use in the mining industry were abolished in 1989, so when item 45 was put in place it said, "Goods designed for use in mining." Of course what was actually covered by the expression "Goods" was parts. Although it was possible to say that major items of equipment, major items of capital equipment like production machinery, was comparatively easy to identify under substantive classifications and the rates reduced to zero. Of course, it's not the same situation with parts and if you wanted parts to come in free, and you wanted to make separate provision for all of them, of course the tariff would have been so fragmented the exercise would have just been unrealistic. So the item 45 by-law was put in place there to allow the free entry of parts for use in the goods that were, themselves, entitled to free entry.

That system worked quite well for some years. In the middle of 1996, however, the word "Goods" was removed and the words "Capital equipment" substituted. I really couldn't understand the logic of this, because most items of capital equipment became duty-free in 1989. So I've got absolutely no idea of what was intended to be achieved with the change of that wording. I've asked people who were associated with it and no-one has been able to give me a satisfactory answer.

The situation today of course is that we still have item 45 there, but it's so hamstrung with administrative requirements that it's just not capable of achieving its objective, there are some really quite absurd conditions attached to it. For example, the administrative guidelines say that if you lodge a goods request after the date of the importation of the goods, then the request will be deemed to be retrospective and you can't have a concession, and that's without any regard to the merits of the issue. But, quite interestingly, one of the forms that you're required to lodge in support of your application is a form which contains details of the entry numbers on which the goods were entered. If the goods have already been entered, that means you can't have your concession. So, I mean, this is just nonsense, but unfortunately it typifies the way the system is administered. I think it does need a major overhaul and I've made some suggestions in here as to how that might be achieved.

I've also given some illustrations of how the present approach really undermines the whole purpose of item 45. One of my clients in the Hunter Valley is about to upgrade one of its mechanical shovels and it's going to import a slew ring that's worth just under a million dollars. These things aren't made in Australia, the machines themselves are free, the shovels themselves are free, they've been free since 1989, but now, because of the way item 45 is administered, we can't have duty-free entry of that slew ring. We can get a tariff concession on it but that means we pay 3 per cent, not free. All of these things have nuisance value. I mean, I'm sure the company can actually accommodate the cost but I really see no point in this ongoing practice of imposing taxes on an export-orientated industry in a way that serves no sensible, economic purpose. I've made some other observations there, given some other examples of this and I really don't think there's much point in going over them here.

The only other observation I'd made is that there is a policy by-law as well for raw materials and intermediate goods. I think it's an excellent by-law and it's one that is of particular importance to the recording industry and any other industry, for that matter, which has zero assistance on its output and tariffs on its inputs. We did raise these issues in the packaging and labelling industry, I recall, a couple of years ago, and the commission has reproduced our submissions in there. Quite interestingly, the commission's preferred position in that seemed to be to do as we had requested; that was abolish tariffs of all of the industry's inputs. But unfortunately the suggestion was that it should be done in the context of a general review assistance, which is what this inquiry is of course, but I doubt that you're going to be in a position to make any kind of recommendations about industry's specific matters in the context of this inquiry.

So although it was very helpful that you made that suggestion in that inquiry, unfortunately it didn't get us anywhere because a general tariff inquiry wasn't covered by the terms of reference. However, we did make the observation in that particular inquiry and I appreciate that, from a practical perspective, it's just not feasible to go through and make specific provision in the tariff or elimination of tariffs on inputs for those industries that have zero assistance on their output. Maybe the item 57 by-law is a very convenient vehicle to get rid of anomalies of that kind, and what we would propose is that one of the recommendations, particularly if you want to say anything about item 57 - one of the criteria that is to be taken into account for the utilisation of item 57 is that you'll look at the question of whether that industry is assisted or not assisted. If it's not assisted, make it competitive in the Australian market by using item 57 to remove the taxes on the input side of its manufacturing operations. I think that would be a sensible economic policy.

MR COSGROVE: Thanks very much, Ian, for a very clear exposition of a comprehensive range of issues. We'll certainly be reading your submission carefully as we will with the others. I might just ask you a couple of questions in response to some of the points you've made: some people, including some who appeared before us earlier today, have expressed doubt that a lowering of the general tariff - let's leave aside your judgments about political considerations and all that - they're saying that any lowering would be unlikely to result in long-term price benefits to the users or consumers of those goods covered at present by the tariff. What's your view of that?

MR RODDA: I think competition would ultimately force that. I suppose that's true in relation to industries that have assistance on their output and no assistance on their inputs, I think they do get a free kick. There, the effective rate of protection for those industries would be fairly significant. But that's not a general thing across the economy, and certainly not across the manufacturing sector. I think the industries that are going to survive long-term on zero assistance are those that are already cost-efficient anyway and they're going to continue on. Those industries that do rely on tariff assistance to maintain viability may not be able to survive longer term, but I suppose that's really a value judgment now for the government. As I said before, since the nominal rate on a 5 per cent tariff is only going to be between 4 and 4 and a half per cent anyway, the question I pose is, is a tax of that magnitude a justification for maintaining protection for those industries that need it? So there's no easy answer to that one. I wish I could do an analysis to come up with a conclusive position on that, but I just don't have the resources to do it.

MR COSGROVE: You've recommended this 1 per cent per annum phasing of the tariff after 2005.

MR RODDA: Yes.

MR COSGROVE: Is there any particular reason for selecting that method of phasing, rather than a shorter number of steps?

MR RODDA: That's probably the shortest number of steps I could think of actually. Given, as I said before, that there are some political realities associated - first of all, I don't think any government is going to just wipe the general tariff overnight. I think the outrage in the community, particularly the manufacturing sector, would be so great that no government would want to do it. To enable industries to adapt anyway to the changed commercial environment, I think phasing it in is probably the most sensible thing to do. I mean we had the phasing-down of the tariff from 20 to 5 per cent under the Button plan over a period of about 10 years or so, I think, wasn't it?

MR COSGROVE: Yes.

MR RODDA: And although some industries had a bit of a grizzle about it, certainly it was a comparatively trouble-free transition to the environment that we have today. I think that if we're going to get rid of tariffs then we would need to do it on the same basis once again. So the question then becomes if we meet our APEC obligations in 2010 do we take it down at the rate of 1 per cent every two years starting now, or do we take it down at the rate of 1 per cent per annum from, say, 2005?

MR COSGROVE: Yes.

MR RODDA: Or maybe there's some other intermediate step, you know, half a per cent a year maybe - - -

MR WOODS: Isn't such a system keeping all of the administrative costs but particularly towards the end having very little beneficial impact?

MR RODDA: Yes.

MR COSGROVE: And aren't you in danger of getting to a point - once you get to 3 per cent you've sort of taken out quite a large proportion of the benefit over and above the concession scheme anyway. But if you're talking about 1 and 2 per cent, but retaining the full overheads of administration, wouldn't a cost benefit, examination of that, suggest that they're consuming more in administration than they are gaining in protection?

MR RODDA: Yes, I understand your point. I think that assumes, though, that any infrastructure that's put in place now for the purpose of administering, say, a concession scheme, for example, would continue on unchanged throughout the period of the transition. But as we found when the 3 per cent revenue levy was imposed on free goods in 1996, although the number of applications for tariff concessions dropped fairly significantly, customs was able to reduce the number of people that it actually put into that processing activity. I think at one stage there might have been 40 or 50 people in the tariff concession area. Today I don't think it is any more than about 10. So I don't see any reason why the administrators of any concession schemes couldn't simply adapt themselves to the changing environment as it changes. I don't really see that as an impediment.

MR WOODS: That's the administration on the side of government but the administration on the side of businesses - and many businesses have said to us that it imposes costs on them; they would still be incurring the full costs of having to comply with the scheme and 1 per cent or even possibly 2 per cent getting very little protection.

MR RODDA: Yes. I suppose once we get there and close to zero, businesses would make their own judgment as to whether or not it was worth their while to pursue a concession or not pursue it. I do know that where there is a fairly high level of expenditure on something or if you have got an item of capital equipment that is worth say $20 million, an application for a tariff concession order does represent a fairly significant kind of a cost saving. Or with a new mining project - I mean, this South Blackwater job or project, for example, I think the expenditures there were something like $800 million so duty relief in those circumstances was going to be very significant.

MR WOODS: But are they perhaps at the top end of the spectrum?

MR RODDA: Yes, and certainly at the bottom end I don't think people are going to worry terribly much. I mean, a tariff of 1 per cent in say the year 2009 is going to be a hiccup. I mean, I think movements in the exchange rate are going to have a greater impact on the cost of imports than the existence of a tariff. So by the time we get to that stage I would say, on the government's side, there probably aren't going to be many resources in place at all for administrative purposes or for the purpose of administering those provisions and industry may very well have found that they're pretty well redundant, you know, from the point of view of cost benefit.

MR COSGROVE: Do you think the announced schedule for reductions of tariffs in the motor vehicles and particularly the TCF sector after 2005 has any relevance in this context? I haven't got the figures in my head but I think in some areas of TCF there may be an annual reduction in the tariff after 2005 of as much as 5 or 7 and a half percentage points. 1 per cent seems pretty insignificant in that context but you would still favour the 11111?

MR RODDA: I think all I really favour is making the adjustment process as painless as possible and giving those industries that are going to be affected, capacity to adjust as each step of the transformation process occurs. I don't think I could put it any higher than that.

MR COSGROVE: The other question I was going to ask you about, Ian, was this idea you posed in the context of use of the policy by-law system of picking winners and it's not surprising, I guess - - -

MR RODDA: I shouldn't say that but the Japanese do it; so do the Americans.

MR COSGROVE: No, people on whose behalf you are appearing before us today, one does tend to think pretty quickly of the mining and agricultural sectors, and you are placing particular significance on the export revenue that they produce, but these days just about every sector of the economy is significant as an export earner. Why should one give preferred treatment to those two sectors on that basis over, say, manufacturing or services where exports are now very significant?

MR RODDA: When those other sectors of manufacturing industry start contributing to the economy in the way the mining and agriculture sectors do, they can demand favourable treatment as well. That's all I have got to say on that one, yes.

MR COSGROVE: Thanks again.

MR RODDA: Sorry, black coal I think at one stage was producing 24 per cent of our export revenues.

MR COSGROVE: Yes. I don't doubt that.

MR RODDA: That is an industry I think we ought to be encouraging, the environmental considerations aside.

MR COSGROVE: Yes. Okay, thank you very much for coming along, despite your injury which we hope repairs quickly.

MR RODDA: So do I. It's wrecking my boating activities.

MR COSGROVE: I don't think we have any other participants today so that concludes this initial round of public hearings. We will hold a further round of public hearings after the commission has released its draft report. Those hearings are likely to take place in June.

AT 11.50 AM THE INQUIRY WAS ADJOURNED ACCORDINGLY

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