

# Review of Australia's General Tariff Arrangements



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# **Review of Australia's General Tariff Arrangements**

## **Introduction**

The Minister for Industry, Science and Resources has directed the Productivity Commission to undertake a review of Australia's general tariff arrangements to be completed by July 2000. This is consistent with Australia's obligations with respect to trade liberalisation as a member of the World Trade Organisation (WTO) and Australia's APEC commitment to review its general tariff arrangements in 2000 or earlier.

The central issue of the review is the scope for a post 2000 reduction in the general tariff, covering rates of 5 per cent or less, excluding the Passenger Motor Vehicle (PMV) and Textiles, Clothing and Footwear (TCF) sectors. As part of the review the Commission will consider a range of issues, principally the costs and benefits of tariff reductions to Australian consumers, industries and their employees and the general community, and the implications of further tariff reductions for trade negotiations.

## **Position**

It is in Australia's best interests, as a trading nation, that international trade arrangements are as open and transparent as possible.

Trade liberalisation has delivered a range of economic benefits to the Australian community. This is primarily as a result of lower cost imports necessitating Australian industry to become more competitive, which has in turn led to the emergence of a range of internationally competitive and export orientated industries across Australia.

In addition, consumers have benefited from better personal choice through access to a greater variety of goods, and industries which rely on imports as part of their operations, such as farmers, have enjoyed reduced input costs as a result of tariff reductions.

From a macroeconomic perspective, therefore, the general thrust of the Commonwealth's efforts in trade liberalisation should be supported.

However, it would be irresponsible not to express concern regarding the fact that there have been economic and social costs associated with trade liberalisation. These range from the adjustment costs for businesses facing increased competition from imports with the inevitable consequences for employment to, in extreme cases, the elimination of certain activities altogether. At the core of

these impacts is the fact that employment is affected, which means that jobs can be lost.

It cannot be ignored that the impact on employment from tariff reductions is uneven across the community. It is often assumed that new jobs in competitive industries create replacement work for those retrenched in industries unable to compete with cheaper imports. This ignores the employment reality that the skills match between industries is imperfect, rendering retrenched labour in need of retraining before being productively employed in competitive industries, and the fact that in rural and regional areas alternative employment opportunities are often limited if in fact they exist at all.

With this in mind, ongoing trade liberalisation should only be supported provided the Productivity Commission can clearly demonstrate that the benefits and the social impact from the proposed 5% reduction in tariffs outweigh the costs of further reductions. If it cannot be substantially demonstrated that the benefits outweigh the costs and that Australians would be better off then, it is presumed that the Productivity Commission would not endorse further tariff reductions.

Also, the Commonwealth should provide transitional support, such as restructuring and retraining assistance to businesses and employees who bear the costs of further tariff reductions, in order to give these people the best opportunity of successfully adjusting to a changed working environment.

### **The NSW Economy**

The NSW economy is the largest, most sophisticated and most diverse economy in Australia accounting for approximately 36 per cent of the Australia's Gross Domestic Product.

The NSW economy grew by 4.1% in 1998-99 and reached \$210 billion in Gross State Product. Sydney is not only the financial and business capital of Australia but is increasingly being recognised as a regional centre in a number of modern and technology based industries.

In 1998-99 the manufacturing sector in NSW had a gross product of \$25.3 billion or 36 per cent of the Australian total. At November 1999, there were 349,800 people employed in 18,972 manufacturing businesses or 32 per cent of Australia's manufacturing workforce.

In 1998-99 gross product in the primary sector totaled nearly \$8 billion, which was 20 per cent of the Australian total for that sector and employed 143,900 people at November 1999.

The manufacturing and primary sectors accounted for 27 per cent and 35 per cent of NSW's total exports respectively, with services exports making up the balance.

Over the last ten years, exports of services and elaborately transformed manufactures have more than doubled as a proportion of total exports in Australia and NSW.

In a regional context, the NSW economy is larger than the national economies of Singapore, Malaysia, Thailand, the Philippines and Indonesia. The State's economic and investment base is diverse, ranging from traditional manufacturing, agricultural and mining industries to the new industries of information technology and telecommunications, film production, finance, aquaculture and biotechnology.

Therefore, as the largest and most diverse state economy, the NSW Government is keenly aware that the conclusions reached by the Productivity Commission have the potential to have the greatest impact on NSW.

### **NSW Issues with Trade Liberalisation**

Australia's manufacturing industries are now more diverse and generally more productive than in the past and that this is partly attributable to the program of tariff reductions implemented since the 1970's. It is also acknowledged that many new employment opportunities have been created which have been able to absorb many of the jobs lost through tariff reductions.

While this is the case there are, however, a number of concerns that the Productivity Commission, in the interests of balance, should address in its examination of the tariff issue. Again, while recognising the benefits and opportunities that trade liberalisation can offer, these must be considered in the light of the fact that the benefits do not accrue evenly or to everyone.

The principal issues that the Productivity Commission is asked to consider are:

- **Reciprocity and Non Tariff Barriers**

It is generally accepted that Australia is already one of the most open and deregulated economies in the world. Over the last 30 years the level of protection afforded to Australia's manufacturing industries, mainly via tariffs, has been progressively reduced from 35% to the present 5%.

Moreover, Australia's significant trade liberalisation has largely been unilateral in character that is, without seeking reciprocal obligations from other countries with which Australia trades.

Therefore, it is timely and important that the Commission recognise that Australia's considerable achievements in the area of tariff reduction, must, in the spirit of free trade, be reciprocated by Australia's trading partners. Efforts should be made to ensure as far as possible that the issue of reciprocity is an essential element of any commitment to further tariff reductions.

Australia's tariffs are already low by world standards, and given that Australia has virtually no non-tariff barriers, Australia is now one of the most open market for imports in the world.

While recognising the presence and role of non-tariff barriers, the main focus of the WTO has been on tariffs. Historically, Australia has not made use of less transparent, non-tariff barriers as a means of assisting the development of industries. Therefore, in meeting its obligations under the WTO Australia has been reducing its only form of protection while other nations, while perhaps reducing their tariffs, have not been obligated to dismantle their non-tariff systems of protection. A number of Australian businesses seeking export opportunities have identified non-tariff barriers as a major impediment to overseas markets.

On the basis that our only form of protection is already small then our ability to influence or negotiate for further tariff or non-tariff reductions is diminished. In other words we should consider further tariff reductions in the context that our markets are already largely open to free trade, and that the remaining low level of protection in place provides Australia with a bargaining position which should not be relinquished without achieving access to other markets.

The Commission may also wish to comment upon the negative reaction to ongoing moves to free up trade by some groups and its possible impact upon the commitment to free trade principles in some countries. This was particularly evident in Seattle and Davos recently and it may be shortsighted to dismiss these events.

- **Timing**

There are two timing issues that the Commission should note in its deliberations.

Firstly, there is the issue of when should tariffs be reduced. Australia is currently experiencing strong economic conditions characterised by low inflation and strong, sustained economic growth. Recent increases in interest rates by the Reserve Bank of Australia may lead to a new cycle where the rate of growth will be constrained.

The Commission is asked to consider whether it is an appropriate time for the removal of Australia's general tariffs if the economy is moving into a downward, albeit managed, cycle where alternative employment options are contracting. Essentially, is it appropriate for the Commonwealth to impose structural adjustment costs on industries during a period where increased economic uncertainty appears to be emerging?

The second timing issue is more broad and relates to the need for the Commission to consider, in a more strategic context, whether we have achieved our goals with respect to our economic objectives and to what degree further tariff reductions could influence the achievement of those objectives. Before we reduce tariffs further knowing that there will be at least some impact on business, we need to consider if we can afford to lose some industries which might otherwise survive were tariff reductions to occur at a later date. It needs to be carefully considered whether the global agenda should be subordinate to Australia's own agenda in these instances.

Furthermore, the gains from trade liberalisation decrease proportionally as the level of protection decreases. Given that Australia's average tariff rate is, at 5%, one of the lowest in the world already, the efficiency gains from further liberalisation will likely be minimal at best. Therefore the timing of further tariff reductions should not be driven by the expectation of significant economic benefits.

- **Strategic Importance of Manufacturing**

The Commission should clearly establish a position about whether it sees manufacturing as a strategically important activity in Australia. This could address issues such as whether manufacturing in Australia is in a strong position or in decline, and the role tariff reductions have had in this process.

The Commission should establish, in the context of declining employment in manufacturing, why further tariff reductions will be beneficial and where those benefits will be realised, in particular whether these benefits will occur in rural and regional Australia.

The comparative advantage thesis, which is an important element in the argument for trade liberalisation, does not always complement State and Commonwealth Government industry policy. For example, the wish to retain certain industrial capabilities may be based on other considerations such as Australia's defense needs. Also, there may be cases where, for a number of reasons, it is desirable to encourage the development of new industries that, say, build on Australia's skills in industries such as information technology, telecommunications and biotechnology. In such cases, while we may not have a comparative advantage in these

industries we may elect to encourage such activities based on other imperatives such as the long term industry and employment policy goals of various governments.

The Commission's views on these instances would be welcomed in terms of providing a balanced assessment of the tariff issue.

- **Small Business and Regional Communities**

There are serious concerns regarding the impact on small business and regional communities from further tariff reduction. In terms of numbers, small businesses account for 98 per cent of Australia's manufacturing firms and many of these are located in regional areas. For example, there are approximately 2,700 manufacturing enterprises in country NSW that employ about 43,000 people directly and have an estimated turnover of more than \$7 billion. While a portion stand to benefit from reduced tariffs some will not benefit and by virtue of their size will be less resilient to change, particularly their ability to compete against cheaper imports. The Commission is asked to be sensitive to this situation.

## **Conclusion**

Australia's rate of tariff protection is already low by world standards. Therefore the Commission's review is essentially examining the removal of the final layer of tariff protection for Australian industry (with the exception of the PMV and TCF sectors).

As stated above, moves towards a more liberalised global trading environment should generally be supported and the overall benefits from lower cost imports and new trade opportunities will provide economic benefits for the Australian economy as a whole.

There is, however, a need to consider these issues in a broader and more balanced context which takes account of the negative consequences of tariff reductions, where those effects will be felt, where the timing of such reductions may conflict with the industry objectives of State Governments or where and why proportionate action is not taken by Australia's trading partners.

The Commission must identify and quantify the benefits that will be achieved through the elimination of Australia's final layer of tariff protection and ensure that appropriate and effective assistance in the form of structural adjustment, retraining, modernisation etc, is made available to those businesses that suffer difficulties as a result of further tariff reductions.