

Productivity Commission's Review of Bilateral and Regional Trade Agreements

Western Australian Submission

Scope of study

The Commission is requested to:

Examine the evidence that bilateral and regional trade agreements have contributed to a reduction in trade and investment barriers. Consider also to what extent such agreements are suited to tackling such barriers, including in the context of the proliferation of such agreements between other countries;

The WA Government has cooperated with and supported the Australian Government in negotiating various FTAs. WA Departments involved continue to consult with industry to identify WA's key interests. However, the timeframes for negotiating FTAs can be significant and often specific comment from WA businesses is only received when there is a recognised problem or issue in trading into that particular market.

The process by which FTAs are negotiated is geared towards reducing the extent of trade and investment barriers. For example, before even proceeding to the negotiation stage, the current prospective Australia-India and the Australia-Indonesia FTAs first involved a joint feasibility study, including independent economic modelling, to determine the potential benefits of entering into a FTA. Industry and other interested parties are also consulted to identify any major issues and impediments that currently impact on trade that could be raised in the negotiations.

The FTAs that Australia has signed provide for a range of reductions in quotas and tariffs and other areas of trade liberalisation. It has been noted that where Australia has entered a FTA, changes in total annual trade figures (both exports and imports) tend to be volatile, which indicate that factors other than FTAs may be the driver of change. Although the impacts of FTAs may be difficult to measure, they are of immense value to Australia.

The Department of Foreign Affairs and Trade (DFAT) has recently released a publication "Benefits of Trade and Trade Liberalisation" which leads to the broad conclusion that "...trade liberalisation added 2.5-3.5 per cent to the Australian economy over the past two decades, and benefitted the average Australian working family by up to \$3,900 per annum." This result is based on independent modelling from the Centre for International Economics. This would indicate that the benefits of trade liberalisation and the opening up of the Australian economy, both at a bi-lateral, regional and multi lateral level have overall provided benefits to Australia.

In FTA negotiations, a balance has to be struck between each parties' goals and aspirations, what they ideally would like and whether it is sufficiently beneficial to Australia's interests. Even within Australian industry one sector may find that an FTA deal seems sufficiently beneficial to warrant its signing while to another aggrieved sector who didn't achieve all they sought (or in the timeframe they expected) it might seem like an unfair deal. It is common, with such complex and comprehensive negotiations across multiple sectors of the economy including areas of trade in goods, services, investment and various legal and other issues, that there will be a disparity of views on whether an FTA is sufficiently beneficial to Australian interests.

The benefits that FTAs are capable of providing are to an extent determined by the cooperation of industry and governments. The benefits of FTAs are not automatically generated and have to be achieved through trade development strategies developed by companies seeking new opportunities from changed trading environments.

While it is often acknowledged that the multi lateral Doha round of trade negotiations will result in the largest shifts forward in achieving trade liberalisation globally, one advantage that bilateral and regional FTA negotiations have is the level of detail that can be included in the negotiations that may not always be included at higher level multi lateral talks. These can include areas such as competition policy, e-commerce, environment and labour issues and economic cooperation. The negotiations can also be useful in terms of setting up dispute settlement mechanisms to adjudicate differences between parties at an early stage before they escalate.

Apart from the benefits of potentially opening up other markets and so increasing the scale that Australian businesses can potentially operate at, FTAs can also have the effect of opening up Australia's economy to greater investment and increased participation from foreign firms. Although FTAs do result in benefits to Australian industry and to other countries that are signatories to them (as can broadly be expected from the increasing numbers being entered into), there may be competing views towards each individual FTA as to whether it provided sufficient benefits, and over a reasonable period of time if tariff reductions will be phased in.

The final agreement settled will also be influenced by the strength of the parties involved and their respective bargaining power (for example, the dynamics of the negotiations between say Singapore and Australia will be different to the Australia-US or Australia-China FTA). The timeframe over which the negotiations took place and the pressure to meet a deadline, as well as the importance of the existing economic and political relationships and the impetus to get some deal agreed, may also influence the negotiations.

Examine the evidence that bilateral and regional trade agreements have safeguarded against the introduction of new barriers. Consider also the potential for trade discrimination against Australian businesses without full engagement in the evolving network of bilateral and regional agreements;

There are a number of mechanisms to lock in benefits gained through the FTA negotiating process including those detailed below.

Most FTA negotiations agreements are often put in place to ensure the hard earned benefits gained are safeguarded for the future. For example, under the World Trade Organisation (WTO), countries will have certain bound limits for tariffs they can apply to goods they are to import. While Australia may be granted a lower tariff on our export to that country presently, there is no guarantee that the tariff can't be increased over night up to that country's limit. FTAs can and should aim to lock in, or bind tariff levels, to current existing rates for Australian exporters therefore providing a much greater level of certainty.

Agreements can also have ratchet mechanisms that lock in any liberalisation so that if, for example, a measure within the FTA is at some point made less restrictive or discriminatory it cannot be made more restrictive at a later date. Therefore over time the agreement 'ratchets down' the level of discrimination. In addition, Most Favoured Nation treatment can be included to ensure that after the FTA is signed, Australia will not be treated more unfavourably than the conditions of any future agreements that country negotiates with others in the future.

What is important is that Australia is included in FTA agreements especially with our major trading partners, where competing nations are also looking to lock in such agreements and enhance trade access. If this does not occur there is the possibility that local exporters will face trade discrimination in favour of those nations or blocs that have finalised FTAs. For example, in terms of Western Australia the three major agrifood, fibre and fisheries export destinations in terms of value of exports in order are North East Asia, ASEAN and the Middle East. To safeguard access to those markets for Australian exporters on favourable terms it will be important to have FTAs in place at least comparable to those other competitor trading nations and blocs are negotiating.

The recent introduction of the ASEAN-Australia-New Zealand Free Trade Agreement (AANZFTA) is an important agreement in terms of maintaining access for Australian exporters and opening up our own economy to this bloc of countries in addition to the already signed Singapore-Australia and Thailand-Australia FTAs.

It will also be increasingly important to move forward with the current negotiations that are taking place in the Middle East (with the Gulf Cooperation Council of 6 countries) and negotiations with north Asian countries such as China, Japan and Korea.

These negotiations are always complex and often require years to potentially reach a positive outcome. One of the difficulties Australia may face in the negotiations is the fact that it has already removed or reduced many of its tariffs to a low level and is already quite an open economy. In most negotiations this can reduce the bargaining power that Australia has available to offer against the targeted reductions it seeks from the negotiating partner.

Several of Australia's negotiating partners have small but very vocal and powerful agriculture lobbies. Globally, agriculture is one of the most intractable sectors in terms of achieving trade liberalisation because of the historical and emotional support shown for domestic agricultural producers, who have the ability to wield political power. In this area Australia will often struggle to achieve its FTA goals of liberalising agricultural trade.

However the negotiations will continue to progress with the aim of locking in market access at least comparable to what other trade competitors are able to obtain who may have stronger bargaining positions or more to offer in terms of trade-offs.

It has also been noted that there is a level of public scepticism about the reform agenda of the FTAs, with the view that little meaningful material has reached the public on the net gains accruing to the Australian economy as a result of trade reform. This can negatively impact on the willingness of businesses and industry to engage with FTA reforms.

Consider the role of bilateral and regional trade agreements in lending support to the international trading system and the World Trade Organisation;

A successful conclusion to the Doha multi lateral WTO negotiations should be a primary aim of the Australian Government because it will provide the greatest results in terms of trade liberalisation. Although there is the view that Australia should improve its efforts to ensure progress in multilateral liberalisation within the WTO and APEC, these negotiations are often lengthy and complex.

In contrast, bi-lateral and regional FTA negotiations are usually more efficient in terms of negotiation and implementation than the global WTO negotiations. Bilateral and regional FTA negotiations can also have a much greater scope in terms of issues raised and areas of economies included within the negotiations because they are just between two nations (or several nations in the regional FTAs).

This allows the negotiations to be tailored to better suit the needs and aspirations of the parties coming together, and for much more specific issues to be resolved, as well as include areas that the WTO doesn't touch on in the multilateral negotiations. Where possible FTAs should aim to be WTO plus, or exceed the results of the multi lateral processes. The use of FTAs at a bilateral and regional level can complement the international trading system

as well as be a useful avenue for progressing trade liberalisation when multi lateral talks are often deadlocked.

Analyse the potential for trade agreements to facilitate adjustment to global economic developments and to promote regional integration;

There is the potential that FTAs can detract from global economic development due to the trade diversionary nature that can occur from signing. For example, a country may get preferential access for its goods not because it is the most efficient producer of that item but because it was able to negotiate the deal because of political issues or trade offs made in other areas.

From a global perspective that means that agreements on international trade may not be being conducted from an efficiency perspective but from a preferential one, leading potentially to the most efficient producers (having a competitive advantage to produce the most output from a given set of inputs) being denied access to the detriment of the consumers of the nations within that FTA. To overcome this the aim should be to make the benefits, in terms of trade creation, greater than any negative issues that may arise from the trade diversionary aspects of lessening competition globally from the preferential access deals offered by FTAs.

The purpose of FTAs overall is trade creating through the opening up of economies to greater competition, investment and integration. As such, the benefits of firms being able to compete more effectively internationally and the greater size of potential markets to be serviced allowing goods to be produced more efficiently, indicates that there should be a positive effect on global economic development.

FTAs can also allow trade to occur more efficiently by reducing many of the barriers to trade including taxes, charges and customs processes, regulations, standards, testing and certification. This leads to greater transparency and cooperation in rules governing trade resulting in less delays and reduced costs and charges on firms which can then flow through to consumers.

The increased competition for older, inefficient industries that can no longer compete will also ideally result in either restructuring or in a phased transitioned out of those markets and result in their resources being deployed more effectively elsewhere, again resulting in benefits for local consumers and potentially the global economy.

FTAs can also be used to enhance the integration of the economic, political and societal aspects between nations and within regions that the multi lateral trade negotiations alone cannot achieve. Examples include agreements between regions such as the European Union, APEC and ASEAN that have not only resulted in enhanced trade between member countries, but also often closer political integration and social/cultural interaction.

The attendant mechanisms established for managing the regional agreements and resolving trade and political disputes can also lessen the potential for friction or unrelated issues escalating between participants because of the stake they now share in the future success of the agreement.

From this perspective, regional FTAs can play an important role in bringing together countries and regions and allowing them to focus on their potential futures together and the benefits and prosperity that will result, rather than on their historical and current differences. The negotiation of trade agreements will often develop and expand into many other areas of interaction.

Assess the impact of bilateral and regional agreements on Australia's trade and economic performance, in particular any impact on trade flows, unilateral reform, behind-the-border barriers, investment returns and productivity growth;

The Western Australian economy is heavily reliant on international trade. Our export markets are by far our largest markets and we need imported goods and materials to meet our requirements.

Evaluating the impacts of FTAs on WA's economy is complex and the following examples illustrate some of the limitations on the analysis of data to assess the real costs and benefits of FTAs:

- Measurement of FTA's tends to focus on merchandise trade flows, but there are also positive impacts on investment and services, though these are even harder to measure;
- From a Western Australian perspective, the economic impacts of FTA's to date are relatively small but positive, particularly in cases where FTA's are most beneficial to emerging and high growth industries such as ICT and biotechnology;
- While the benefits of individual FTA's may not always be significant, FTA's in general are part of the world trade development process – and neither Australia nor Western Australia can afford not to participate in the process of developing them;
- There are often significant time lags between the introduction of an FTA and realizing benefits from it;
- FTA's are about freer trade rather than free trade – reforms are generally relative and small, not of the 'big bang' variety.

By way of example, the WA Government was closely engaged with all aspects of the AUSFTA negotiations. The benefits of the AUSFTA, along with other FTAs, were assessed in the 2008 Review of Export Policies and Programs report. A 2004 preliminary analysis of the AUSFTA's impact on Western Australia suggested that the benefits were likely to be relatively modest. Under the AUSFTA, all metal and mineral exports are duty free, however, the rates of protection applicable to Australian exports of petroleum, mining and basic metal exports were marginal, thus it was expected that there would be little change to the significant export areas of minerals and energy. Potential opportunities for WA were expected to be in the export of

horticulture products (e.g. strawberries and olives), dairy products, lamb, beef, and wine. It was also expected that imports of US manufactured goods would be cheaper. Further findings about the impact of the AUSFTA in 2008 were that it generally represented an improvement in trade and investment conditions by reducing barriers to goods, services and investments. However, there was little evidence of a substantial export response.

Assess the scope for Australia's trade agreements to reduce trade and investment barriers of trading partners or to promote structural reform and productivity growth in partner countries. Consider alternative options for promoting productivity improving reform in partner countries;

As mentioned above, one of the main outcomes of FTA should be that they reduce many of the barriers to trade including taxes and charges and customs processes, regulations, standards, testing and certification and result in greater transparency and cooperation in rules governing trade resulting in less delays and reduced costs and charges on firms that then flow through to consumers.

Similarly in the areas of services and investment, the rules should open up the partner's economies to greater investment by Australian companies and vice versa, and also provide a greater level of certainty for investors and rules and processes by which these investments can be managed and safe guarded. Uncertainty can be one of the greatest impediments to investment in any country and FTAs should increase transparency about what investors can expect.

In many FTAs there can also be sections on competition policy to assist in progressing domestic competition policy reform, maximising benefits of trade and investment liberalisation and strengthening bilateral cooperation on competition policy, leading to greater structural and economic reform in partner countries that Australia is negotiating with.

These reforms can be important because many of the guarantees on market access and other guarantees provided by an FTA can be negated by anti-competitive activities of a co-signatory once the FTA is signed and comes into force. It also depends on how open and transparent an economy was in the first place as to the amount of issues that may need to be covered in such competition policy chapters.

Lastly, while it is always possible to promote productivity enhancing measures that other countries should adopt, where these may impact on powerful domestic lobby groups or sensitive areas of the economy, there is a greater chance of achieving reform if foreign governments see a direct benefit to themselves.

FTAs, and the trade and other benefits that can accrue by signing up, can provide a powerful stimulus for governments to look at their economies as to where reform can and should take place.

Assess the scope for agreements to evolve over time to deliver further benefits, including through review provisions and built-in agenda.

One of the benefits that FTAs should result in is the establishment of institutional arrangements to manage the FTA, resolve disputes and develop forward work programs to enhance cooperation and progress the FTA into the future. As much as possible, these institutional arrangements should be worked into any FTA so that the agreement can develop and evolve over time to meet new challenges and deliver enhanced benefits to all parties involved.