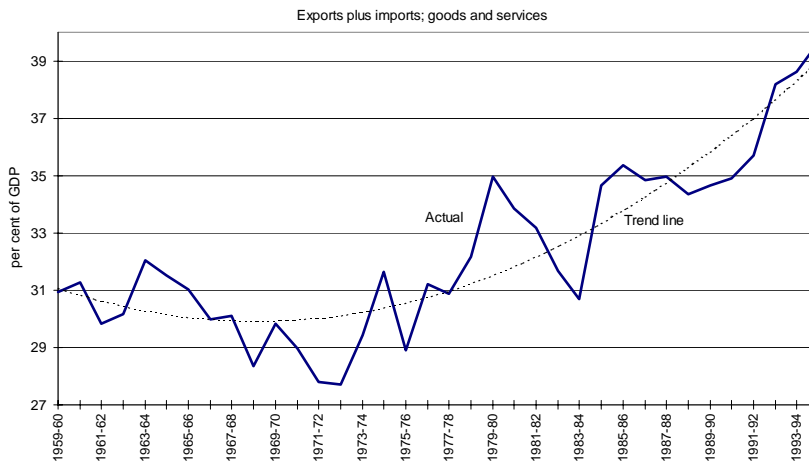


Trade, Globalisation And Australian Incomes

Chart 1
TRADE AS A PERCENTAGE OF AUSTRALIA'S GDP



Australia Is Increasingly Linked To The Global Economy

As a result of declining protection, financial deregulation, and improvements in trade and communications, Australia is becoming more closely linked to the global economy. For example, trade has risen from around 30 per cent of GDP in the 1960s to almost 40 per cent in the mid 1990s (see Chart 1), and international income transactions doubled to around 6 per cent of GDP. While these ratios are still not particularly high by OECD standards, the Australian rate of increase has been one of the strongest.

Can Australia Compete Against Low-Income Countries?

A common argument is that relatively high incomes and costs make Australian products uncompetitive on local and international markets; and the emergence of new low-income pro-

ducers and reduced Australian protection have contributed to Australia's large current account deficits.

However, the evidence does not fit the theory:

- ◆ Japan, Luxembourg and Switzerland do not have persistent trade deficits, while India and Vietnam do not have persistent surpluses.
- ◆ As shown in Charts 2 and 3ⁱ, on average, Australia tends to export to poorer countries and import from richer countries.

◆ As is also shown in Chart 2, on average, Australian income levels have been rising more slowly than either Australia's import-supplying or export-purchasing countries.

◆ The argument has some well-known ancestors - "how can we compete against Japan (1950s) / Hong Kong and Singapore (1960s) / Taiwan (1970s) / South Korea (1980s)?"

Is Globalisation Increasing Inequality In Australia?

According to Robert Reichⁱⁱ, as economies become more open, income relativities are pushed closer to those in the rest of the world. Unskilled employees are cheap and plentiful in the world market; businesses and their products are internationally mobile; and so unskilled workers are increasingly competing directly with those in other countries. (The argument is consistent with the economic concept of "factor price equalisation".) Consequently, unskilled workers are

Chart 2

INCOME LEVELS OF AUSTRALIA'S TRADING PARTNERS

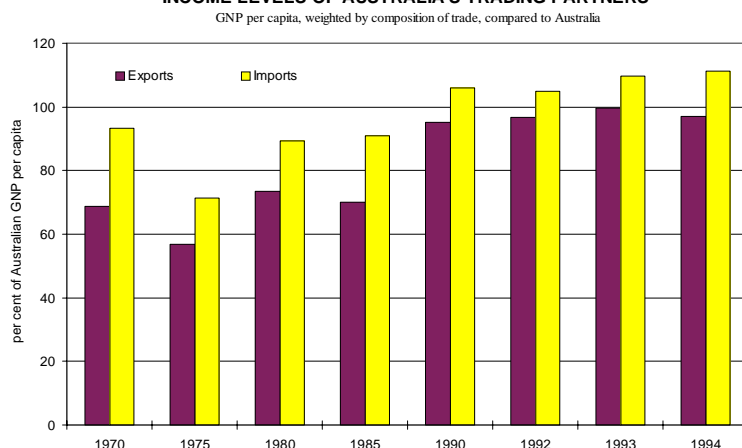
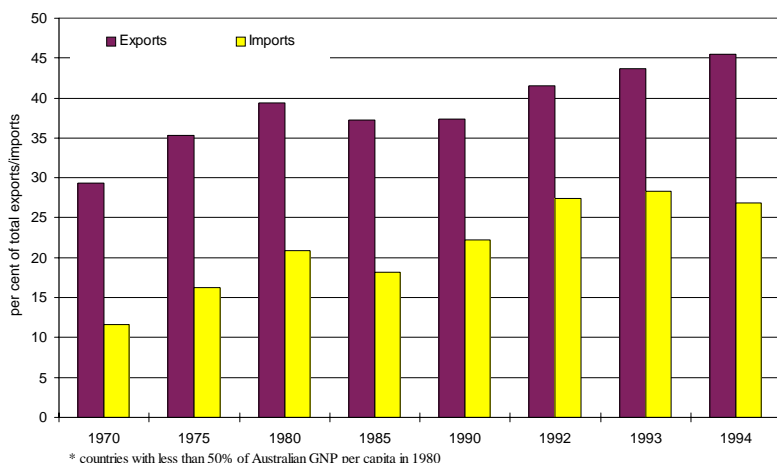


Chart 3

AUSTRALIA'S TRADE WITH LOW-INCOME COUNTRIES*



getting poorer relative to skilled workers. Because the Australian economy was relatively closed in the past and the wage determination system often favoured compression of relativities, the wage structure may have been more strongly affected by globalisation than some other countries. In Australia, over the last fifteen years, the proportions of employees at the lowest and highest wage levels increased, while the proportion in the middle decreasedⁱⁱⁱ. Trends to greater wage dispersion were also identified in twelve of seventeen OECD countries for which data were available, including Canada, the United Kingdom and United States^{iv}. Increased income dispersion is an alternative to the “we can’t compete” argument, as it helps increase competitiveness with low-income countries.

Some alternative explanations considered by the OECD were

the effect of technology, decline in unionisation and demographic changes. They concluded that increasing demand for educated labour and declining demand for unskilled workers were key factors, driven by technological change. They considered that trade may have had an effect on demand but were uncertain. Paul Krugman^v rejects the influence of trade on growth in wage dispersion for the US because the bulk of its trade is with high income countries and the increase in inequality occurred after the growth in trade had levelled off. Interestingly, while Krugman accepts that inequality is increasing in many countries, he also rejects other explanations, such as government policy and technological change, concluding that the cause is not yet known.

In Australia’s case, the increase in the trade ratio was later, and coincides better with the increase

in inequality than the USA. However, Australia’s imports from low-income countries (defined as having GNP per capita of less than half Australia’s in 1980) still amounted to only about three per cent of Australia’s GDP in 1994. Furthermore, while Australian imports from low-income countries have grown rapidly, exports to these countries are larger and have also grown rapidly (see Chart 3). Even where imports from low-income countries are minor, it is possible that the influence is also felt in import-competing and exporting industries, and ultimately the whole economy.

While it is not proven that globalisation is affecting income dispersion in high-income countries, it seems to be a plausible factor.

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ⁱ **Sources- Direction of Trade:** Trade by country from IMF, *Direction of Trade Statistics*. 1994 data from *International Merchandise Trade* (ABS 5422.0).

Gross National Product Per Capita: World Bank, *World Tables* and *Atlas*. Data are on an exchange rate basis. Taiwan data were obtained from *Industry of Free China*. A few small trading partners were omitted due to lack of data (eg French Polynesia, Brunei and Nauru). 1994 data are not yet available, so 1993 data were used as a proxy. While wages would arguably be a better indicator, GNP per capita is closely related and is more available and consistently defined than wages.

ⁱⁱ now Labor Secretary in the Clinton Administration. See *The Work of Nations*, Knopf, New York 1991, especially chapters 16 and 17.

ⁱⁱⁱ Table 1, Paul McGuire, “Changes in Earnings Dispersion in Australia, 1975-92” in *Labour Economics and Productivity*, Vol. 6, No. 1, March 1994.

^{iv} OECD, *Employment Outlook*, July 1993, Chapter 5.

^v *Peddling Prosperity*, Norton, New York 1994, pp. 146-150.