

Background - How did we get here?

- 2.1 This Chapter will consider some of the current debates in the international trading environment, examining some of the circumstances surrounding the AUSFTA. The Committee acknowledges the recent report of the Senate Committee on Foreign Affairs Defence and Trade and the issues it covered regarding the history of the GATT, GATS and the WTO.
- 2.2 While it may be the case that ‘debate about multilateral versus bilateral trade liberalisation is now academic in regard to the AUSFTA’¹, it is worth noting the level of debate in the context of evidence received by the Committee.
- 2.3 The Committee notes that commentary on the world trading environment occupies a large amount of print and television news. It also informs public opinion, as can be seen by the column inches devoted to it in the print media, the hours of discussion on television and radio, and the letters and petitions sent by members of activist groups who wish their concerns to be noted. The Committee acknowledges that the impact of trade policies is seen throughout Australian society and the issues are broader and more complex than can be given in any review of this size and nature.
- 2.4 Given the extent of evidence received during the course of this inquiry which made specific or general mention of trade policies in the context of this Agreement, the Committee considers that it is of benefit to recognise the range of positions held.

1 Allen Consulting Group, *The Australia – United States Free Trade Agreement: Potential Impacts on South Australia*, October 2003.

- 2.5 The Committee is not qualified to present a wide-ranging and comprehensive analysis of debates about the history and influence of international trading arrangements on national economies and societies, nor is it tasked to. It will however offer some comments in acknowledgement of the range of opinions which have been expressed concerning the Agreement.

The ‘multilateral vs bilateral’ debate

- 2.6 The Senate Report tabled in November 2003 gave a useful background to the Committee’s understanding of the issues facing the Parliament as it debates legislation which, when passed, serves to enable Australia to comply with the obligations contained in trade agreements.
- 2.7 The Committee also notes the ongoing work by the Parliamentary Library which prepares analytical papers discussing the impacts and influences of an increasing number of trade agreements as well as shifting norms in trade organisations and institutions.
- 2.8 It is largely recognised that there is an increasing focus on bilateral and regional agreements as multilateral agreements stall. The increasing numbers of members of the WTO mean that consensus is more difficult to achieve so nations look to increase market access in bilateral or regional agreements.

Regionalism

- 2.9 The Committee notes that the last decade has also seen an increase in Regional Trade Agreements (RTAs); the Committee was interested to learn that more than half of world trade occurs within existing or prospective RTAs. Scholarly opinion remains divided over whether such preferential trade agreements are ‘building blocks’ or ‘stumbling blocks’ towards freer global trade. What does seem clear is that a ‘domino effect’ towards RTAs has developed, with many countries concerned about being left out of new arrangements.²

2 John Kunkel, ‘Australian trade policy in an age of globalisation,’ *Australian Journal of International Affairs*, Vol. 56, No. 2, 2002, p. 245.

Criticisms of bilateralism

- 2.10 The Committee notes the critiques of bilateralism including the increasing number of differences between agreements and their consequent impacts. The Committee considers that the findings of a recent US Congressional Committee can be equally applied in an Australian context.

A minority believes that, though not a fault of the Agreement, there is a concern that the current melange of global, regional and bilateral international trade agreements have different, congruent and conflicting substantive, procedural and enforcement provisions. This creates confusion and uncertainty and encourages global forum shopping and multiple proceedings. Congress should look at this patchwork quilt in its entirety, not only one piece at a time and consider the long term impact these agreements will have on American interests over the long term.³

- 2.11 The Committee also notes commentary which refers to a ‘spaghetti bowl’ approach; the more FTAs that are signed, the more incompatible standards and rules of origin emerge. This can have a negative impact on the efficiency gains made by any move towards free trade, creating administrative difficulties with the implementation of agreements with different standards for various trading partners.

- 2.12 The Committee further notes that a WTO Trade Policy Review of the US, released in January this year, raised questions about the increased use of bilateral trade agreements by the US, noting that

care should be taken that negotiating and administrative resources are not distracted away from the multilateral system and that vested interests are not created that complicate multilateral negotiations.⁴

3 US-Singapore Free Trade Agreement Report of the Trade and Environment Policy Advisory Committee (TEPAC), February 27, 2004.

4 WTO, *Trade Policy Review of the United States*, 16 January 2004, WT/TPR/S/126.

Bilateralism won't affect the multilateral process

- 2.13 The Committee notes contrary views which suggest that fears that FTAs will undermine the multilateral approach are unfounded. The Committee is aware that several countries, Australia included, have concluded bilateral agreements while continuing to conduct multilateral negotiations. It notes an observation made that the US government signed pacts with Israel, Canada and Mexico during the Uruguay Round negotiations from 1986 to 1994 without reducing its commitment to a final multilateral agreement.⁵
- 2.14 The Committee also notes the view that FTAs can provide useful templates for broader negotiations.

As membership of the WTO grows, reaching consensus becomes more difficult. Negotiators can be forced to consider only the lowest common denominator. Negotiating with one nation or a small group of like-minded countries can allow more meaningful liberalisation in areas such as sanitary and regulations, technical barriers to trade, service trade and investment, electronic commerce, customs facilitation, labour and environmental standards and market access for politically sensitive sectors. Those talks can blaze a trail for wider regional and multilateral negotiations ... Despite their peculiarities and incremental nature, the agreements can serve the cause of freedom and development by breaking down barriers to trade between nations.⁶

Australia's place in the world trade environment

- 2.15 It has been long-recognised that Australia has one of the most open economies in the world. The Committee notes the progress that Australia made to reduce tariffs during the 1980s, making it one of the world's most open economies.
- 2.16 Australia has been a world leader in trade liberalisation in bilateral FTAs such as ANZCERTA, regional fora such as APEC and pushing for liberalisation within multilateral institutions such as the WTO.

5 Daniel Griswold, *Financial Times*, 27 July 2003. Dr Griswold is Associate Director of the Center for Trade Policy Studies at the Cato Institute.

6 Daniel Griswold, *Financial Times*, 27 July 2003.

Australia also established the Cairns Group of agricultural nations, and has been active in regional trade fora in the Asia Pacific region.

ANZCERTA

- 2.17 Few Australians realise that one of the most advanced regional trade agreements already exists between Australia and New Zealand.

Like most new model FTAs, ANZCERTA extends well beyond goods trade to services, investment, harmonisation of standards and even the (relatively) free movement of labour, thus now bordering on being a fully fledged common market. This cross-Tasman integration process, beginning modestly in the 1960s, was motivated primarily by a mutual benefit in the need for structural adjustment and a common fear of being 'left out' in a regionalising world.⁷

- 2.18 Recognising the breadth of the AUSFTA and the number of bilateral and regional treaties currently either in force or being negotiated, the Committee considered it timely to examine in brief a widely acknowledged example of one of the world's most comprehensive and integrated free trade agreements, the Closer Economic Relations Treaty with New Zealand (also referred to as CER or ANZCERTA). The Committee received some advice from DFAT on the changing nature of this agreement since it came into force in 1983.

- 2.19 Mr Alastair Maclean from the Department of Foreign Affairs and Trade (DFAT) stated that the ANZCERTA was originally built on a series of preferential trade agreements between Australia and New Zealand, including the 1966 free trade agreement between the two countries. He explained that by the late 1970s, those agreements led to the removal of tariffs and quantitative restrictions on about 80 percent of trans-Tasman trade. In March 1980 the concept of closer economic relations—CER—between the two countries was introduced, culminating in the negotiation of the CER, which entered into force on 1 January 1983.⁸

- 2.20 The Committee notes that the CER has developed quite considerably in the years since. A significant protocol called 'the acceleration of free trade and goods', sped up the phase down of tariffs and quantitative

7 Graham Dunkley, 'There goes the neighbourhood! The regional free trade adventure', Chapter 5 in *The Free Trade Adventure*, Melbourne 1997.

8 Mr Alastair Maclean, *Transcript of Evidence*, 14 May 2004, p. 32.

restrictions five years ahead of the original schedule. Services were brought into the CER from January 1989.

2.21 The Committee understands that

since July 1990, some seven years after it initially entered into force, all goods meeting the CER rules of origin have been free of tariffs and quantitative restrictions, and there are now very few restrictions on services. Whilst CER is the principal agreement that supports the trans-Tasman economic relationship, there are a number of other agreements and arrangements which have been developed since.⁹

2.22 The Committee understands that these arrangements include:

- the 1996 customs cooperation arrangement which assists in the harmonisation of and cooperation in customs policies and procedures, with significance for the administration of the rules of origin, which underlie the CER trade arrangements
- the 1998 Trans-Tasman Mutual Recognition Arrangement (TTRMA), which was an important development in deepening the economic relationship
- the open skies agreement signed in November 2000, which established seventh freedom rights¹⁰ and allowed Australian and New Zealand international airlines to operate across the Tasman and beyond to third countries without restriction.

2.23 The Committee was advised that CER issues such as business law reform and tax imputation are currently being advanced. DFAT advised of the existence of other areas of cooperation in science and technology, biosecurity, quarantine, industry and competition issues.

2.24 The Committee understands that the TTMRA is currently being reviewed by the Productivity Commission and the two governments have signalled their commitment to the further development of a single market between Australia and New Zealand.

2.25 The Committee heard from Mr MacLean that

We have consistently observed the fact that the CER remains one of the world's most open free trade agreements. I think the figures point to it having been extraordinarily fruitful in

9 Mr Alastair Maclean, *Transcript of Evidence*, 14 May 2004, pp. 32.

10 Seventh freedom rights allow a dedicated freight carrier to operate services directly from another country to third countries without operating out of their home countries.

improving and extending trans-Tasman trade and investment links. Since 1983, two-way trade with New Zealand has expanded about 500 per cent, with annual growth of around nine per cent over the past decade. So it outstrips total growth in trade. Obviously the difference in the size of the economies means there are some differences in the relative profiles of Australia for New Zealand, and alternatively of New Zealand for Australia. New Zealand, despite the difference in size, is still Australia's fifth largest market. It takes 5.9 per cent of our total exports—that includes goods and services—and total bilateral trade with New Zealand was more than \$16.2 billion in 2001-02, including \$3.8 billion in services.¹¹

Australia's involvement in other trade agreements

- 2.26 Apart from the ANZCERTA discussed above, the Committee notes that Australia signed a bilateral free trade agreement with Singapore in February 2003. It is a broad agreement, covering trade in goods, services, investment and a range of other sectors, although agriculture and cultural issues were specifically excluded. While the Committee does not intend to make a comparison between the SAFTA and the AUSFTA in this Report, it notes that the Committee has had a previous opportunity to review some of the issues which have arisen in this inquiry process. The presence of the SAFTA is also noted in the context of Australia's current and recent involvement in other bilateral trade negotiations.
- 2.27 The Committee also notes that a free trade agreement between Australia and Thailand has been concluded and is currently the subject of parliamentary review. A report is expected from this Committee later in the year. Australia is also conducting preliminary discussions with Japan and Korea about potential trade agreements and the Committee will monitor this situation with interest.

Impact of the AUSFTA on Australia's relations with the rest of the world

- 2.28 The Committee notes the comments of Professor Ross Garnaut in evidence received by this inquiry. The Committee further

11 Mr Alastair Maclean, *Transcript of Evidence*, 14 May 2004, p. 32.

acknowledges Professor Garnaut's contribution to debate in the wider community. Professor Garnaut believes that bilateral trade agreements exclude or disadvantage other trading nations and can be of limited value even to those who sign them.

The completion of an Australia-US free trade agreement at a time of high insecurity for our country is more likely to diminish than expand Australian economic opportunity. And it may weaken Australian security in important ways ... The agreement would be a significant new factor in the contemporary pressures for the unravelling of the open, multilateral trading system and the reversion globally to re-World War II patterns of bilateral and small-group preferential arrangements. It will be the first big scalp of the new US strategy of seeking to pursue its trade interests through many bilateral agreements. And it will be the first free trade agreement linking substantial economies from different regions ... Such an agreement would increase the risks of Australia being left outside preferential trading arrangements that include as members its major trading partners in East Asia.¹²

- 2.29 Professor Garnaut views are supported by Peter Lloyd, who is similarly dismissive of the real value of bilateral agreements. While Professor Garnaut claims that bilateral agreements should be resisted because of the damage they cause to the multilateral system, Mr Lloyd recognises that regional 'street gangs' are pushing countries into a series of bilateral deals. Australia must join in, or risk being beaten up.¹³ The Committee notes Professor Lloyd's statements as reported in *The Australian* newspaper in November 2003.

Quoting another economist, Professor Lloyd said: 'Regional trading agreements are like street gangs: you may not like them, but if they are in your neighbourhood, it's safer to be in one'.

And

We may not like regional trading agreements, but if our export competitors like Chile or Canada, and possibly in the future South Africa ... if those countries get preferential

12 Ross Garnaut, *The Australian*, 4 March 2003.

13 Michael Bachelard, *Weekend Australian*, 15 November 2003, p. 25.

access to our major markets, we will be at a severe disadvantage. So we joined the street gang.¹⁴

- 2.30 This view was opposed by Professor Garnaut, who claimed that bilateral agreements would destroy the economic and political support for multilateral trade, damage the multilateral system and lock some disadvantaged countries out of the new system. The Committee similarly notes his view that

Medium-sized countries like us end up getting beaten up pretty badly if it becomes gangsterland.¹⁵

Australia's approach

- 2.31 Most observers agreed that multilateral trade liberalisation was preferable to bilateral trade liberalisation. The Committee notes the evidence from Ms Joanna Hewitt from DFAT that

It is very clear from the portfolio perspective that we see the WTO process, in a trade policy sense, as a first best option and indeed Australia's top priority. That has long been the case. We have been putting and continue to put a tremendous amount of effort into the Doha process. We have to take stock of the fact that last September in Cancun we had quite a serious setback in the WTO process. There was a standoff following that setback in Cancun that lasted for some months. Only last week I was in Geneva with colleagues for the first serious round of reengagement in the negotiations. We had an agriculture session in Geneva. There are some encouraging signs about the possibility of parties getting back together and being able to put together a framework text for the Doha negotiation. That would not be a full, detailed outline of what will be achieved in the end but rather a sort of skeleton agreement. We are hopeful that that will be possible, but I have to say to you that there are also still very big gaps and differences between the parties—between major developed economies and increasingly between developed and developing economies—in the WTO process. WTO now has 148 members. The very process of reaching agreement is cumbersome and difficult, which does not make it any less important. We feel strongly that, from an Australian point of

14 Michael Bachelard, *Weekend Australian*, 15 November 2003, p. 7.

15 Michael Bachelard, *Weekend Australian*, 15 November 2003, p. 7.

view and indeed from a global and development point of view, a process where you have liberalisation of markets on a coordinated basis, where everybody moves together, is obviously the way you are going to get the biggest and most lasting legally binding results. But it has become more and more difficult to move through those processes quickly. We recognise that it is going to take time, but it is still worth investing our major effort in trying to achieve that. There are some things that can be done in the WTO—I am thinking particularly in the agriculture sector, which is so central for Australia. It is just not possible—as we have seen in our negotiations with the Americans and what we see of others—to negotiate down export subsidies, for example, or the whole raft of agricultural support unless that is done in a parallel way between the major subsidisers. The WTO is the only place where that can happen.¹⁶

- 2.32 The Committee agrees that multilateral trade liberalisation should continue to be pursued within the Doha round.

Trade diversion

- 2.33 The Committee notes evidence which suggested trade would be diverted. Professor Garnaut stated that

... a preferential area is not all about movement in the direction of free trade. The other, contrary movement in a preferential area is in the direction of trade diversion, because one thing that happens in a preferential area which does not happen in a genuine movement to free trade is that some low-cost production from a third country is replaced by high-cost production from the trading partner. For example, Australia imports some brands or types of cars from Japan because they meet Australian consumer needs more cost-effectively than equivalent products from the United States. However, if you took away the 15 per cent tariff on American production but kept it on Japanese production then it might be cheaper to bring in a car from the American subsidiary of Nissan rather than from the company in Japan, even though the cost of production in the American subsidiary was higher than in Japan. In that case, the preferential area would lead to the

16 Ms Joanna Hewitt, *Committee Briefing*, 2 April 2004, pp. 5-6.

replacement of a low-cost source of supply—in this case, Japan—with a high-cost source of supply—in this case, the United States.¹⁷

- 2.34 Australia has just concluded FTAs with Singapore and Thailand, and embarked on a study of an FTA with China. The Committee notes a report which suggests that the negotiation of the AUSFTA may actually *encourage* future bilateral arrangements rather than threaten them. The Committee notes the view of Mr Andrew Stoler in this regard.

Just recently, an Indonesian minister, hearing of the FTA results, suggested that his country might be next in line for an agreement with Australia ... The idea that the AUSFTA has distracted Australia from the Doha round, and that this is why the round is in trouble, is almost too silly an argument to consider ... Far from being left out of the deal, most Australian agricultural sectors should do quite well under the AUSFTA. Far too many people are quick to forget that in this modern Australian economy, nearly three-quarters of people work in the services sector where the AUSFTA clearly promises more competition and cost savings in Australia, and enhanced access for services exporters to the US.¹⁸

- 2.35 The Committee also notes the views of Mr Peter Hartcher¹⁹, who suggested that three threshold questions should be asked in relation to the AUSFTA.

- Is trade liberalisation good for Australia in principle? Australia has become one of the world's most open economies and has survived the collapse of Asian growth, and continued to grow while the US fell into recession. The answer is yes.
- Can Australia pursue trade liberalisation? It would be better to do so through multilateral deals. When this approach isn't available, it is best to do so through bilateral approaches.²⁰ Bilateral and regional

17 Professor Ross Garnaut, *Transcript of Evidence*, 3 May 2004, p. 59.

18 Andrew Stoler, *Australian Financial Review*, 25 February 2004, p. 55.

19 'With no multilateral choice, the answers must all be yes', *Sydney Morning Herald*, 1 May 2004.

20 Hartcher notes that 'given that [the multilateral] approach is not available, the world's governments have responded with a frenzy of activity in the only avenues open to them – bilateral and regional deals. In 1990 there were 40 such deals. By 2002 there were 250 and more than 30 more are under discussion.'

deals are messier than a clean global agreement, but they represent the only realistic way forward. So, the answer is yes.

- Does this particular deal represents a net benefit for Australia? While the traditional way of calculation represents a tiny benefit, a bigger benefit is found by ‘using a newer method that tries to capture the overall “dynamic” effects, as investors reallocate resources to pursue the most profitable endeavours.’ Therefore, the answer is yes.

Additional arguments in favour

2.36 Some of the commentary made in recent months concerning the AUSFTA is the period in which it has been negotiated. It has been reported in some circles that it is a rare opportunity for Australia to negotiate an FTA with the world’s largest economy, largely due to the strength of the bilateral relationship.

2.37 The Committee also notes that former Australian Consul General to New York, Mr Michael Baume AO, believed that there was a narrowing window of opportunity to bring the AUSFTA into force.²¹ The Committee notes his comments given in evidence at a public hearing, and also in print media:

... negotiators cannot be given more time as the process would then blow out until 2005, by which time the special goodwill Australia enjoys in the US Congress, which must approve any deal, may have diminished somewhat.²²

Consultation with the public

2.38 Consultation will be discussed in the next chapter, and will arise as a separate issue at various points throughout the report in relation to specific chapters. What should be recognised in general is the extent of positive feedback from witnesses and in submissions about the level of consultation conducted by DFAT *before* and *during* negotiations.

2.39 DFAT noted the extent to which earlier consultations informed and gave direction to the negotiating teams. The Committee therefore

21 Michael Baume, *Transcript of Evidence*, 6 May 2004, p. 54.

22 Michael Baume, *Australian Financial Review*, 17 November 2003.

notes that while the Agreement did not deliver gains to all sectors as hoped, gains that were made were likely to have been assisted by the involvement of industry and community groups lobbying for the outcomes they wanted. The Committee notes departmental comment that from the beginning of the negotiations, the Government sought to ensure adequate opportunities for interested individuals and organisations to provide comment, including through public submissions, and that this process assisted in formulating objectives and negotiating positions.²³

Concluding observations

- 2.40 The Committee notes evidence it received relating to the relative merits of multilateral and bilateral trade agreements, and claims made by several parties with regard to the impact of one type of treaty or the other on the international trade environment. Most evidence agreed that multilateral liberalisation was preferable to bilateral liberalisation.
- 2.41 The Committee accepts that in the absence of progress in the WTO it was reasonable to pursue a bilateral trade agreement with the United States. The Committee believes it is important that Australia continue to work for progress on multilateral liberalisation within the Doha round.

23 DFAT, NIA and RIS, Consultations.