

AUSTRALIAN MANUFACTURING WORKERS' UNION



**SUBMISSION TO THE
SENATE SELECT COMMITTEE ON THE FREE TRADE AGREEMENT
BETWEEN AUSTRALIA AND THE UNITED STATES OF AMERICA**

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1. Introduction

The Australian Manufacturing Workers' Union (AMWU) welcomes the opportunity to make submissions to the inquiry of the Senate Select Committee on the Free Trade Agreement between Australia and the United States of America (the Committee).

The full name of the AMWU is the Automotive, Food, Metals, Engineering, Printing and Kindred Industries Union. The AMWU represents approximately 145,000 workers in a broad range of sectors and occupations within Australia's manufacturing industry. The union has members in each of Australia's states and territories.

For many years the AMWU has been an important voice for working people in debates concerning trade policy. The AMWU has consistently argued for fair trade rather than free trade. In the AMWU's submission, the proposed Australia - United States Free Trade Agreement (AUSFTA) is neither fair nor free.

This submission identifies a number of problems with the proposed AUSFTA. The problems discussed include:

- Australian manufacturing's trade imbalance with the United States and the effect of tariff reductions
- The broader economic effect of the agreement
- The inadequacy of the labour chapter
- The loss of tariff revenue
- The social and cultural impact of the agreement
- The commitments concerning foreign investment
- The capitulation over sugar
- Non-tariff barriers
- Issues concerning the rules of origin
- Issues concerning government procurement in the agreement

In addition, the AMWU analyses the alleged benefits of the proposed AUSFTA contained in the latest Centre for International Economics Report entitled "Economic Analysis of AUSFTA: Impact of the Bilateral Free Trade Agreement with the United States" (the CIE report).

The AMWU's submission concludes that the problems identified with the proposed AUSFTA are of such magnitude that the Australian government should not enter the agreement.

The AMWU strongly urges the Committee to recommend that Australia should not enter the proposed AUSFTA.

2. Australian Manufacturing's Trade Imbalance With The United States and The Effect of Tariff Reductions

2.1 The Status Quo: The Current Trade Imbalance

Australia currently has a significant trade imbalance with the United States. The Australian Bureau of Statistics reported that for 2002/03 Australia's merchandise trade deficit with the United States was \$12,129 million. This was easily the highest merchandise trade deficit that Australia recorded with any trading partner.¹

Australia's trade imbalance with the United States was most acute in manufactured goods. For example, in the 12 months ended March 2003 the Australian Bureau of Statistics reported that Australia had:

- a \$2,554 million trade deficit in chemical and related products;
- a \$696 million trade deficit in manufactured goods classified chiefly by material;
- a \$10,459 million deficit in machinery and transport equipment; and
- a \$2,267 million trade deficit in miscellaneous manufactured articles.²

Given the importance of the automotive industry to Australian manufacturing and the treatment of automotive products in the proposed AUSFTA, it is appropriate to give additional consideration to the trading relationship between the Australian automotive industry and the United States automotive industry. Interestingly, the latest U.S. Government trade data shows that in 2003 the United States had a massive trade deficit of \$US 109,982 million with the rest of the world in the automotive sector (as approximated by the HS Code 87). The enormous trade deficit in the automotive sector included a \$US 41,240 million deficit with Japan, a \$US 17,807,318 deficit with Germany and a \$US 15,815 million deficit with Mexico. However, the country with which the United States had the *largest trade surplus* in the automotive sector - an amount of \$US 885 million - was Australia. It is notable that in the auto components sector (which is within the broader automotive sector), the United States recorded a \$US 272 million trade surplus with Australia for 2003.³

2.2 The Status Quo: The Current Tariff Regimes

Although both nations presently have a low tariff structure, U.S. manufacturing tariffs are generally lower than Australian manufacturing tariffs. According to the World Trade Organisation, the average applied tariff for non-agricultural products for the United States in 2002 is 4.2%. In contrast, the World Trade Organisation has reported that Australia's average applied most favoured nation (MFN) tariff for industrial products is 4.7%.⁴

¹Australian Bureau of Statistics - International Trade in Goods and Services - 5368.0 - February 2004.

² Australian Bureau of Statistics - International Merchandise Trade - 5422.0 - March Quarter 2003.

³See US Office of Trade and Economic Analysis's "TradeStats Express" website at <http://ese.export.gov>.

⁴ World Trade Organisation, Trade Policy Review, United States of America, 1993; World Trade Organisation, Trade Policy Review: Australia, 2002.

Again, given the importance of the automotive industry to Australian manufacturing and the treatment of the automotive industry in the proposed AUSFTA, it is relevant to note that in the automotive sector, tariffs on Australian goods going into the United States are generally lower than the tariffs on U.S. goods coming into Australia.

For example, most auto components and passenger motor vehicles imported from the United States into Australia face a 15% tariff (10% from 1 January 2005) whereas (with the much publicised exception of utes) most auto components and passenger motor vehicles exported from Australia to the U.S. face considerably lower tariff rates of around 2.5%.

Therefore, while the vast majority of tariffs on manufactured goods in *both* nations will fall to zero upon entry into the proposed AUSFTA, Australian tariffs will too often have further to fall.

2.3 The Impact of the Proposed Tariff Reductions - A Minister Asleep at the Wheel?

Australia's large trade deficit on manufactured goods with the United States can, at least in large part, be attributed to the larger economies of scale enjoyed by U.S. manufacturers as well as U.S. manufacturing's higher rates of investment in research and development and technology. By way of example, Table A shows the relative size of a number of U.S. manufacturing sectors compared to the equivalent Australian sectors in terms of each sectors' importance to world production. The figures, which are for 2001, show an Australian manufacturing industry dwarfed by its U.S. counterpart.⁵

⁵The table is modified from table in ABS page 539 2004 Year Book Australia. The figures relate to 2001.

Table A

	United States		Australia	
	<i>Percentage of World Production</i>	<i>World Rank</i>	<i>Percentage of World Production</i>	<i>World Rank</i>
Food Products and Beverage	22.2%	1	1.8%	12
Wood and Cork Products	24.7%	1	1.8%	14
Printing and Publishing	32.4%	1	1.3%	11
Metal Products	23.4%	1	not available	not in top 15
Basic Metals	19.6%	2	1.7%	14
Transport Equipment	25.9%	1	0.9%	15

In addition to these advantages, the U.S. trading position has recently been dramatically enhanced by downward movements in the value of the U.S. dollar.

The United State's advantages in manufacturing will not disappear overnight. What then will happen when Australia surrenders its tariff advantage over the United States virtually overnight? The AMWU submits that it is clear that to the extent employers are unable to pass losses directly on to their workers through insecure forms of employment and downward pressure on wages and conditions, increasing numbers of Australian manufacturers will either cease production or move offshore.

It is in this context that the AMWU notes Canada's experience in relation to free trade agreements with the United States points to the risk of large scale job losses, particularly in manufacturing. Between 1989 and 1997 it has been estimated that Canada lost 276,000 jobs as the 870,700 export jobs created were not enough to match the 1,147,100 jobs destroyed by imports.⁶

The government has been quick to promote the potential for Holden to increase exports of utes to the U.S. market. However, General Motors is most unlikely to allow this to happen in any volume. The head of General Motors North American operations, Mr. Bob Lutz, has commented to the Detroit Press, that if the Australian manufactured Monaro (exported to the U.S. and co-badged as the Pontiac

⁶Industry Canada, Duncan P. and S. Murphy, 1999 "The Changing Industry and Skill Mix of Canada's International Trade", Paper No. 4

GTO) achieved sufficient volumes and market acceptability, production would be shifted from Australia back to the U.S.⁷

Even if Holden had the capacity (which it does not), a favourable exchange rate (which it does not) and support from American company and union officials (which it does not), why would the fate awaiting the Monaro not apply to the GTO as well?

Moreover, focusing only on the potential for increased exports while steadfastly ignoring the likelihood of increased imports presents a completely distorted picture of the likely effects of the proposed AUSFTA.

As Doug Harland, Manager of Toowoomba Metal Technologies (a company which makes wheels for the automotive sector) pointed out on ABC radio on 6 March 2004:

“We had about a 2.5 per cent tariff we paid on our product going into the States, they had a five per cent tariff on product coming into Australia, so the net result will be a 2.5 per cent benefit to American exporters”

The windscreen manufacturer Pilkington, has already announced the reduction of its workforce because of the loss of a 70 year old contract with Holden. The contract was lost due to increased import competition arising out of the Australia - Thailand free trade agreement.⁸ Previously Pilkington had lost a contract with Ford Australia who chose to source from China. This occurred because increasingly American companies are being required to source as much auto components as they can from China to sustain their own position inside that country's booming auto industry.

How many thousands of employees working for the Doug Harlands or the Pilkingtons out there are about to lose their jobs because every time the Trade Minister is required to consider the possible impact of increased imports under a bilateral free trade agreement he appears to drop into one of Dr Karl Kruszelnicki's “micro-sleeps”? Will the findings of this Committee or the Joint Standing Committee on Treaties force the Trade Minister to “stop, revive, survive” in time to save manufacturing jobs in Australia? Australian communities reliant on manufacturing and the AMWU can only hope so.

As the extracts provided below illustrate, unlike Australia's Trade Minister, interest groups in the United States are not oblivious to the proposed AUSFTA's likely effects on manufacturing. Neither have the likely effects on Australian manufacturing workers escaped the notice of economists or a number of important stakeholders.

⁷Lutz was quoted in an article in *The Detroit News Autos Insider* on Wednesday November 5 2003:

“The 2004 Pontiac GTO is now based on a coupe built by GM's Australian unit Holden Motors. Due in dealerships next month GM is limited to building 18,000 GTO's a year, in part because of the sensitivity to the United Auto Workers Union. GM also hopes to create demand for the GTO by curtailing volume. But once the new rear wheel platform is put into place in “several years” Lutz said the car could be built in North America by union workers in somewhat larger volumes.”

⁸Bachelard M, “Holden Dumps Its Aussie Glass Firm”, *The Australian*, 12 February 2004 page 4.

2.3.1 *Commentary Concerning the Effect on the Manufacturing in the United States*

The President of the National Association of Manufacturers has predicted that the AUSFTA will bring a \$US 2 billion gain per annum to U.S. manufacturing:

"This superb agreement can result in close to 2 billion dollars in new U.S. manufactured goods exports"

"With all the up-front benefits for manufacturers and the American economy in general, there is no reason to delay in getting this FTA implemented"⁹

The U.S. Trade Representative had the following to say to the *Wall Street Journal* in relation to the proposed AUSFTA on 3 March 2004:

"This agreement will eliminate tariffs on more than 99% of U.S. manufactured goods exports to Australia on day one. Those exports account for 93% of total U.S. sales to Australia's large market, and support 150,000 good-paying American jobs. In creating new export opportunities for America's manufacturers, this deal will help a vitally important segment of our economy while also expanding markets for America's services firms, creative artists, and farmers."

...

"Australia is America's ninth-largest export market, and a significant consumer of American-made products such as aircraft, construction equipment, trucks and SUVs, machinery, chemicals, and paper. Every year, Australia buys more than \$13 billion in products from the United States. Every single U.S. state sells to Australia, and it is a particularly important market for companies in the heart of our Midwestern manufacturing belt. With virtually all of those exports going duty-free under this agreement, America's manufacturers estimate they could sell \$2 billion more per year to Australia, and they predict that U.S. national income would grow by nearly that much as well."

In his "Trade Barriers Report, Australia, 2004", the US Trade Representative observed that:

"If enacted, the FTA would eliminate tariff barriers over 0 to 4 years in the automotive sector and over 0 to 10 years in the textiles sector. **U.S. industry estimates the removal of barriers affecting trade in textiles would lead to increases in U.S. exports to Australia of \$100 to \$500 million in textiles and by \$100 to \$500 million in autos and components.**"¹⁰ (emphasis added)

⁹Media release of National Association of Manufacturers 8 February 2004. The media release can be found at www.nam.org.

¹⁰The report can be downloaded from the USTR's website at www.ustr.gov.

Meanwhile the U.S. Business Roundtable said in a press release on 9 February 2004:

"The U.S.-Australian free trade agreement will significantly further economic growth in America. This agreement will also strengthen our more than 50-year relationship with one of America's most reliable allies. Tariffs will be eliminated for more than 99% of U.S. products and will boost U.S. exports to Australia by close to \$2 billion. This will mean increased output and new jobs in our nation."

A U.S. Chamber of Commerce Letter to the U.S. House of Representatives on 19 February 2004 stated:

"Bilateral trade between the United States and Australia reached over \$28 billion last year, and the United States enjoys a substantial trade surplus with Australia of over \$6 billion. The FTA would further eliminate trade barriers, lower tariffs and provide increased market access for U.S. companies. By knocking down trade barriers in Australia and in the rest of the world, we can help support even more American jobs."

And the Chairman of the American - Australian Free Trade Agreement Coalition claimed in a press release on 9 February 2004:

"This is the most significant reduction of industrial tariffs ever achieved in a U.S. free trade agreement. The United States is the largest and Australia the 15th largest economy in the world and this agreement will strengthen these economies even further. American workers will benefit the most from this deal, especially manufacturing jobs"

2.3.2 Commentary Concerning the Effect on Manufacturing in Australia

Meanwhile, the original Centre for International Economics (CIE) report commissioned by the government predicted a worsening of the bilateral trade balance in the automotive sector under a AUSFTA and a contraction in output in the industry:

"the majority of additional exports from the US to Australia as a result of AUSFTA are manufactured goods ... For example US exports of motor vehicles and parts to Australia increase by US\$525 million following Australia's elimination of bilateral motor vehicle and parts tariffs."¹¹

...

``However we observe a slight fall in the output of the Australian MVP sector, meaning that the sector's loss of market share to US MVP imports outweighs any expansion

¹¹ Centre For International Economics, ``Economic impacts of an Australia - United States Free Trade Area'', June 2001, at page 43.

effect brought on by cheaper production inputs and increased export opportunities to the US."¹²

The study commissioned by the Victorian Department of Premier and Cabinet from the Centre of Policy Studies came to similar conclusions about the impact of AUSFTA on Australia's auto and component industry. As the authors of the study concluded in summarising the impact on Victoria "over 1,100 full and part-time jobs will be lost from the Motor Vehicles and Parts Industry in the long run. Of this around 800 will come from Melbourne and almost 200 from the Barwon region."¹³

The modeling commissioned by the South Australian Government from Allen Consulting Group also found that there would be likely job loss and contraction in South Australia's automotive and auto component industry.¹⁴ Allen Consulting Group noted the uncertainty and disagreement amongst auto and component companies about the agreement:

"Some segments of the industry in South Australia see opportunities from the AUSFTA. Others are concerned that the AUSFTA could disrupt plans made under previous assistance arrangements implemented by the Commonwealth Government."¹⁵

A University of Michigan analysis of a "free trade deal" between the United States and Australia (completed prior to the text of the agreement becoming available) predicted a small overall gain as a result of the agreement but also a reduction of output and employment in many Australian industries including: agriculture, mining, leather products and footwear, wood and wood products, chemicals, non-metallic mining products, metal products, transportation and equipment, machinery and equipment, other manufactures, electricity, gas and water, construction and government services.¹⁶

The AMWU notes that the CIE has subsequently released a later report with alternative findings in relation to most industries. The AMWU believes the new study provides a flawed estimate of the likely effects of the proposed AUSFTA. The AMWU details a number of its concerns in relation to that agreement in section 11 of this submission. However, even the latest CIE report predicts employment losses in a large number of manufacturing industries including: textiles; wearing apparel; wood products; paper products, publishing; petroleum, coal products; chemical, rubber, plastic; mineral products (other); ferrous metals; metal products; transport equipment; and machinery.¹⁷

At the same time as the above warnings there have been concerning messages coming out of Mitsubishi and Toyota. Prior to the finalisation of the AUSFTA Ken Asano, the Chief Executive of Toyota Australia, was quoted in *The Age* on 1 December 2003 as saying:

¹²Ibid at page 40.

¹³ The results are reported in the Victorian Government submission to the Joint Standing Committee on Treaties's inquiry into the AUSFTA. The submission can be downloaded at www.aph.gov.au/house/committee/jsct/usafta/subs/SUB91.pdf.

¹⁴ Allen Consulting Group, "The Australia – United States Free Trade Agreement: Potential Impacts on South Australia", October 2003 at page vi.

¹⁵ Allen Consulting Group, "The Australia – United States Free Trade Agreement: Potential Impacts on South Australia", October 2003 at page viii.

¹⁶Brown D, Kiyota K, Stern R, "Computational Analysis of the US Bilateral Free Trade Agreements with Central America, Australia and Morocco", University of Michigan, February 2004.

¹⁷ CIE report at page 85.

"A free-trade deal between Australia and the US that cut automotive tariffs quickly would be "suicide" for the local industry".

Similarly, there continues to be intense speculation about where Australia will fit into a forthcoming review of Mitsubishi's world-wide operations.¹⁸ The proposed AUSFTA will do nothing to encourage Toyota or Mitsubishi to remain committed to Australian manufacturing.

As the Committee would be aware, the closure of an automotive plant in Australia would be a disaster for those communities reliant on the automotive plant. Submissions to the 2002 Productivity Commission Inquiry suggested job losses from Mitsubishi's closure in South Australia would be somewhere between 11,000 and 22,000. If the AUSFTA in any way inhibits Mitsubishi's competitiveness relative to other producers and its capacity to export product to North America, it could well be the final nail in the coffin for Mitsubishi Australia.

Not only would this be a disaster for South Australia, the flow on effects from such a closure would have very serious consequences for the Australian manufacturing industry as a whole.

2.3.3 Some Further Context: The Rising Aussie Dollar and the AUSFTA

The AMWU asks that the Committee be particularly mindful of the challenges faced by Australian manufacturers and Australian manufacturing workers as a result of the recent appreciation of the Australian dollar. While in April 2001 the Australian dollar fell to a low of \$US 0.48, the dollar is now consistently above \$US 0.70. Last year alone the dollar rose by around 33%. In a small to medium sized open economy, a currency appreciation of such a magnitude inevitably puts significant pressure on many manufacturing businesses.

In a recent survey the Australian Industry Group found:

- 57% of exporters reported a reduction in export orders due to the higher Australian dollar in 2003. This is estimated to have resulted in the loss of \$3.2 billion export orders.
- 53% of Australian manufacturers reported increased import competition. This is estimated to have resulted in the loss of \$4.1 billion orders.
- The combined loss of \$7.3 billion income from fewer exports and imports resulted in nearly 10% of manufacturers employing fewer workers because of the dollar's appreciation.
- With the higher dollar, around 20% of manufacturers are considering moving some of their production offshore.¹⁹

At the same time, in the recent round of AMWU delegate consultations in the lead up to the AMWU's National Conference later this year, delegates reported rising job insecurity and increased levels of casualisation as Australian businesses have sought to assign a greater proportion of the risk of doing business in a global economy directly to their workforce.

¹⁸See for example the article entitled "Long Term Doubt Over Mitsubishi" by Michael McGuire and Robert Wilson in *The Australian* on 1 April 2004.

¹⁹See Aussie Dollar Challenges Manufacturing Competitiveness, Australian Industry Group, January 2004.

In this context, the AMWU further notes that in its recent survey of delegates in the auto component sector 74% of respondents were of the view that a free trade agreement with the United States would have a negative impact on the company at which they worked. While 77% of respondents were of the view that a free trade agreement with the United States would have a negative impact on the auto component sector in Australia as a whole.

In such circumstances a preferential trade agreement with the United States, which requires Australian manufacturers to face down the most powerful manufacturing nation in the history of the world, is clearly not the answer for Australian manufacturing or Australian manufacturing workers.

Moreover, it is the AMWU's concern that the proposed AUSFTA will not only cost Australia manufacturing jobs in the short to medium term but may well have the effect of tying one hand behind the back of future state and federal governments when it comes to the type of flexible and coordinated policy development that will be essential to growing manufacturing in Australia in the long term. This additional effect of the proposed AUSFTA is further developed in the context of the AMWU's discussions of foreign investment and government procurement later in this submission.

The AMWU urges the Committee to recommend that the Australian Government not enter the proposed AUSFTA on the basis that the AUSFTA will negatively impact upon Australia's manufacturing industry and Australian manufacturing workers.

3. The Broader Economic Effect Of The Agreement

The AMWU submits that the government's credibility on the issue of the overall economic costs and benefits of the agreement has been severely compromised. The government's misuse of earlier modelling, the highly questionable handling of the ACIL Consulting report and the refusal to involve the Productivity Commission or any truly independent economic analysis of the proposed AUSFTA is enough to raise legitimate concerns about the government's willingness to play politics with the economics of the proposed AUSFTA.

The AMWU strongly submits that it is highly unsatisfactory that the government did not have the economic modelling that it is using to justify entering the proposed AUSFTA available for public scrutiny at the time of the close of submissions to the Joint Standing Committee on Treaties. The AMWU similarly submits that it is similarly highly unsatisfactory that the government did not have the economic modelling available for public scrutiny until the day of the formal close of the submission to this inquiry. In any event, it is the AMWU's view that the modelling in the CIE's latest report is so flawed that it makes almost no contribution to the debate over whether Australia should enter the proposed AUSFTA. The AMWU has made a number of criticisms of the latest CIE report in section 11 of this submission.

The AMWU notes that notwithstanding the latest findings of the CIE, the weight of opinion of mainstream economists appears to be that the broader economic effect of the agreement on Australia will be negative:

- ACIL Consulting in its report "A Bridge Too Far - An Australian Agricultural Perspective on the Australia/United States Free Trade Area Idea: A Report for the Rural Industries Research and Development Corporation February 2003 " predicted that a AUSFTA agreement would create losses rather than gains for Australia.
- An International Monetary Fund Working Paper "The United States and the New Regionalism/Bilateralism "²⁰ also found that a bilateral trade agreement between Australian and the United States was likely to create losses for Australia - particularly if agricultural goods were not included.
- The Productivity Commission has twice questioned the economic utility of bilateral agreements. Once in its Staff Working Paper "The Trade and Investment Effects of Preferential Trading Arrangements - Old and New Evidence"²¹ and most recently in its Annual Report²².
- Greg Cutbush, of ACIL Consulting when pushed by Michael Brissenden on the ABC's 7:30 report indicated: "I would be expecting small single digit billion negative answers on this deal."²³

²⁰The working paper by Alvin Hilaire and Yongzheng Yang is coded WP/03/206.

²¹Adams R, Dee P, Gali J and McGuire G, "The Trade and Investment Effects of Preferential Trading Arrangements - Old and New Evidence", Productivity Commission Staff Working Paper, Canberra, May.

²²Productivity Commission Annual Report 2002-3003, page 14

²³The interview was broadcast on 11 February 2004 on the ABC. A transcript can be found at www.abc.net.au/7.30/content/2004/s1043094.htm.

- Professor Ross Garnaut has many times questioned the economic gains to be made by pursuing a bilateral free trade agreement with the United States.²⁴

The AMWU submits that the proposed AUSFTA will not deliver the gains to Australia that the government has claimed. The AMWU submits that the proposed AUSFTA will in fact deliver more costs than benefits for the Australian economy.

The AMWU urges the Committee to recommend that the Australian Government not enter the proposed AUSFTA on the basis that the agreement will not be economically or socially beneficial to Australia.

The AMWU further urges the Committee to recommend that for future trade agreements no Joint Standing Committee on Treaties review should take place until the government's final economic modelling of the agreement is made public and there has been a reasonable opportunity for that modelling to be analysed.

²⁴See for example Professor Garnaut's submission to the Senate Foreign Affairs, Defence and Trade Committee's Inquiry into the proposed Australia - United States free trade agreement and the general agreement on trade in services. The submission can be downloaded at www.aph.gov.au/Senate/committee/FADT_CTTE/gats/submissions/sublist.htm

4. The Inadequacy Of The Labour Chapter

The AMWU submits that Australia should not enter trade agreements that do not guarantee that all parties subject to the agreement must observe the core labour standards contained in the International Labour Organisation's Declaration on Fundamental Principles and Rights at Work. These standards include:

- the right of workers and employers to freedom of association and the effective right to collective bargaining (conventions 87 and 98);
- the elimination of all forms of forced or compulsory labour (conventions 29 and 105);
- the effective abolition of child labour (conventions 138 and 182); and
- the elimination of discrimination in respect of employment and occupation (conventions 100 and 111).

The Labour Chapter in the proposed AUSFTA contains various commitments to "strive" to ensure that certain internationally recognised labour principles are upheld. Indeed in the first Article of the Labour Chapter the parties purport to "reaffirm their obligations as members of the International Labour Organisation (ILO) and their commitments under the ILO Declaration on Fundamental Principles and Rights at Work and its Follow-up". However, it is important to recognise that these commitments are *not* enforceable under the AUSFTA.

The *only* part of the Labour Chapter that is enforceable under the AUSFTA's disputes settling procedure is the obligation contained in Article 18.2.1(a). Article 18.2.1(a) provides:

"A Party shall not fail to effectively enforce its labour laws, through a sustained or recurring course of action or inaction, in a manner affecting trade between the Parties, after the date of entry into force of this Agreement."

This obligation is watered down by Article 18.2.1(b) which provides:

"The Parties recognize that each Party retains the right to exercise discretion with respect to investigatory, prosecutorial, regulatory, and compliance matters and to make decisions regarding the allocation of resources to enforcement with respect to other labour matters determined to have higher priority. Accordingly, the Parties understand that a Party is in compliance with subparagraph (a) where a course of action or inaction reflects a reasonable exercise of such discretion, or results from a bona fide decision regarding the allocation of resources."

The AMWU submits that the protections for workers contained in Article 18.2.1, which are the only enforceable protections in the agreement, are so slight as to be almost meaningless in the context of the AUSFTA.

The proposed AUSFTA patently fails to provide any enforceable mechanism to address domestic laws in the United States or in Australia that do not meet the relevant ILO core labour standards.

Experience has shown that failure to implement enforceable mechanisms which guarantee core labour standards into trade agreements can lead to greater exploitation of working people. In this

context the AMWU particularly notes a paper by Harley Shaiken which observes that the Mexican experience of the North American Free Trade Agreement has been that:

"While manufacturing sophistication soared, wages have declined or remained stagnant over much of the last two decades, depressed by government policies to attract investment and a lack of labor rights, among other factors".²⁵

The AMWU urges the Committee to recommend that the Australian government not enter the proposed AUSFTA on the basis that the AUSFTA does not contain clauses which guarantee the observance of core labour standards.

²⁵Shaiken H., "The New Global Economy: Trade and Production under NAFTA", *Journal für Entwicklungspolitik*, 2001, pp241-254.

5. The Loss of Tariff Revenue: A \$1.5 Billion Black Hole

The U.S. Trade Representative has claimed in its fact sheet on the AUSFTA:

“Because Australian tariffs are much higher than U.S. average tariffs, American firms today pay 10 times as much in total annual import tariffs to Australia as the U.S. collects from Australian imports. The U.S.-Australia FTA will eliminate this disparity.”²⁶

The AMWU submits that it is not in the national interest to enter an agreement which would eliminate such an obvious benefit to Australia.

The AMWU notes that even the National Impact Assessment (which considerably underestimates the cost of the agreement to the Australian taxpayer by not including the additional administration costs of the agreement or the effect of trade diversion flowing from the agreement) indicates that the Australian taxpayer loses \$190 million in 2004/05, \$400 million in 2005/06, \$420 million in 2006/07 and \$450 million in 2007/08.

This money would be better spent on health, education or local industry policy initiatives - rather than as a \$1.5 billion leg up to U.S. multinationals.

With around one third of Australia's imports of US manufactured goods involving a US parent selling to its subsidiary, it is perhaps no wonder that the AUSFTA has received some strong support from certain U.S. business interests in Australia and the United States.²⁷

The AMWU urges the Committee to recommend that the Australian government not enter the proposed AUSFTA on the basis of the huge cost to the Australian taxpayer.

²⁶The fact sheet can be downloaded at www.ustr.gov/new/fta/australia.htm.

²⁷Productivity Commission 2003, Trends in Australian Manufacturing, Commission Research Paper, AusInfo, Canberra, page 135.

6. The Social and Cultural Impact of the Agreement

The AMWU is an active member of the Australian Fair Trade and Investment Network (AFTINET). In submissions to the Committee, AFTINET has identified serious concerns in relation to the social and cultural impact of the proposed AUSFTA. The AMWU adopts the submissions of AFTINET and commends them to the Committee for its consideration.

In addition, the AMWU wishes to expressly state its opposition to the inclusion of a number of matters in the proposed AUSFTA.

6.1 The Pharmaceutical Benefits Scheme and Generic Drug Manufacturers

The proposed AUSFTA contains provisions which require changes to Australia's Pharmaceutical Benefits Scheme. The changes appear likely to provide benefits for U.S. multinational pharmaceutical companies at the expense of the Australian taxpayer. In this context, the AMWU particularly notes the comments of Republican Senator Jon Kyl to a US Senate Finance Committee, quoted in the *Sydney Morning Herald* 11 February 2004:

"One of the ways of addressing the causes [of high US pharmaceutical prices] is to get the other countries of the world to help bear part of the burden of the R&D. So, my hat's off to your [Mr Zoellick's] team and the work that you did in at least beginning to address this with Australia."

The AMWU also notes the submission to this Committee of Drahos, Faunce, Goddard and Henry. That submission predicts that Australia's Pharmaceutical Benefits Scheme will have to pay "at least one third more for its drugs with the FTA than without it". In 2003 figures this would translate to an additional \$1.5 billion cost to the Australian taxpayer.

The submission of Drahos *et al* also notes that a recent study by the Australia Institute found that the proposed AUSFTA's effect on generic drug manufacturers could lead to an extra \$1.1 billion being spent over the period 2006 to 2009 on the *five* drugs the subject of that study.

This shift of costs from US multinational pharmaceutical companies onto the Australian taxpayer is totally unacceptable.

The Pharmaceutical Benefits Scheme provides affordable medicines for all Australian workers and their families. It is a scheme that works and works well. The scheme must not be undermined by a bilateral trade agreement with the United States.

6.2 Media Local Content Requirements

The proposed AUSFTA contains provisions which will prevent Australian governments from increasing media local content requirements beyond the present levels. The proposed AUSFTA also seeks to restrict the future regulation of Australian content requirements in new media. A democratically elected Australian government should have an unfettered right to support Australian voices and Australian stories in the Australian media.

There is clear precedent for the United States entering free trade agreements without a commitment in relation to cultural services. The AMWU particularly notes that the Canadian government did not make any concessions in relation to cultural services in the NAFTA agreement. Furthermore, most nations, including Australia, have given no commitment in relation to audiovisual services during GATS negotiations.²⁸ Restrictions on our cultural services is too high a price to pay for the limited concessions the government has managed to achieve in relation to agriculture.

The AMWU strongly submits that restrictions on media local content requirements have no place in a bilateral trade agreement with the United States.

6.3 Other Concerns

The AMWU also shares AFTINET's concerns with respect to the effect the AUSFTA will have on blood plasma product supplies; the new restrictions on the regulation of services and investment; and the likelihood of increased U.S. influence on quarantine, genetic engineering laws and environmental policy making.

Although the AMWU is pleased that the proposed AUSFTA does not contain an investor-state complaint mechanism, the AMWU does not support the inclusion of the clause providing that a future investor-state complaints process may be developed if it is requested by an investor.

The AMWU urges the Committee to recommend that the Australian government not enter the proposed AUSFTA on the basis that it is likely to have negative social and cultural impacts on Australia.

²⁸Yeung M. and Kerr W., "Canada and the Australia-US Free Trade Agreement: Enhanced Opportunities or Loss of Special Status", Estey Centre of Law and Economics in International Trade, November 2003 at page 64. A copy of this paper can be provided on request.

7. The Commitments Concerning Foreign Investment

The AMWU strongly opposes the commitments in relation to foreign investment in the proposed AUSFTA.

The AMWU notes that, with a number of narrow exceptions, the proposed AUSFTA would dramatically reduce the ability of the Australian Government to screen foreign investment to ensure that it is in the national interest. Under the AUSFTA the Foreign Investment Review Board's threshold for reviewing foreign acquisitions would be lifted from \$50 million to \$800 million.

While the AMWU acknowledges that the national interest test has rarely been invoked to prevent foreign investment in Australia, the AMWU notes that the changes would mean that almost 99% of Australian manufacturing companies could be acquired under the proposed AUSFTA with no regard for whether such an acquisition is in the best interests of Australia or Australian workers.

In addition, by entering the proposed AUSFTA Australia would be agreeing, with a number of specific qualifications, not to place requirements on foreign investors to undertake a whole range of performance requirements including:

- (a) to export a given level or percentage of goods or services;
- (b) to achieve a given level or percentage of domestic content;
- (c) to purchase, use, or accord a preference to goods produced in its territory, or to purchase goods from persons in its territory;
- (d) to relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with such investment;
- (e) to restrict sales of goods or services in its territory that such investment produces or supplies by relating such sales in any way to the volume or value of its exports or foreign exchange earnings;
- (f) to transfer a particular technology, a production process, or other proprietary knowledge to a person in its territory; or
- (g) to supply exclusively from the territory of the Party the goods that such investment produces or the services that such investment supplies to a specific regional market or to the world market.²⁹

The AMWU submits that such unwarranted restrictions on Australian industry policy are not in the national interest.

The AMWU urges the Committee to recommend that the Australian government not enter the proposed AUSFTA on the basis that the provisions in relation to investment will prevent Australian governments from legitimately seeking to exercise control over foreign investment to ensure that such investment is in the national interest.

In addition, the AMWU urges the Committee to recommend that the Australian government not enter the proposed AUSFTA on the basis the provisions in relation to investment will prevent Australian governments from using useful policy levers to enhance the benefits of foreign investment to Australia and Australian industries.

²⁹ See Article 11.9.1.

8. The Capitulation Over Sugar

The AMWU condemns the Howard government for capitulating to the United States over the exclusion of sugar from the proposed AUSFTA. The AMWU submits that sugar's exclusion, combined with the treatment of manufacturing tariffs in the proposed AUSFTA, clearly confirms what the AMWU and others were saying prior to the release of the text of the AUSFTA - that the Howard Government would not be able to negotiate a bilateral trade agreement with the United States that would provide benefits to Australian workers and their communities.

Like manufacturing workers all over the country, the 39,000 Queenslanders who are employed in the sugar industry have been badly let down by the Howard Government.

The AMWU urges the Committee to recommend that the Australian government not enter the proposed AUSFTA on the basis that the agreement has failed to consider the interests of the sugar industry, workers in the sugar industry and communities reliant on the sugar industry.

9. Issues Concerning the Rules of Origin

The AMWU rejects the government's claims in its fact sheet on the proposed AUSFTA that the rules of origin in the agreement are "simple and objective". On the contrary, the AMWU submits that the hundreds of pages of product specific rules of origin are extraordinarily long and complex.

The AMWU's view is that in many cases the rules of origin clauses in the agreement appear insufficient to ensure that only products which are substantially produced in Australia or the United States obtain concessional entry under the agreement.

The AMWU is particularly concerned that not only will the rules of origin in the proposed AUSFTA grant concessional access to products for which a significant proportion of their manufacture took place in a country that has not granted reciprocal access to Australian producers but that it will also grant concessional access to products for which a significant proportion of their manufacture has taken place in a country or countries with a very low commitment to environmental or labour standards.

For example, the partial reliance on the change in tariff classification approach used in the AUSFTA incorporates a significant element of arbitrariness into the tariff treatment of many products. The arbitrariness arises in part because the Harmonised System was not designed for the identification of origin but for the presentation of trade statistics. As the Productivity Commission has noted when recommending against a proposal to change the rules of origin under the Australia - New Zealand CER Trade Agreement to a tariff classification approach, "the extent of transformation involved in a change in tariff classification would vary between classification levels and between categories at each level".³⁰ Merely because a good may have changed (or may have not changed) tariff classification in a country does not mean that a product was (or was not) substantially produced in that country.

On its present analysis the AMWU is not satisfied that the additional requirements attached to some products will be sufficient to remedy this problem.

Taking another example, a proportion of products are subject to a modified change in tariff classification approach which involves either an additional or optional (lesser) test in relation to the value of inputs not coming from either Australia or the United States. Under this approach domestically sourced materials and processes must reach an agreed proportion of the final value of the product (the regional value content requirement). The agreement provides for three methods to work out the regional value content. These methods are a "Build Down method"; a "Build Up method" and a "Net Cost method".

The Build Down method generally requires 45% regional value content. The Build Up method generally requires 35% regional value content. The Net Cost Method, which applies only in relation to some products in the automotive sector, generally requires 50% Australian / United States content.

The AMWU is yet to be convinced that such additional requirements will be effective in preventing the problems that the AMWU identified above. After all, if up to 65% of the value of a product was

³⁰Productivity Commission, Rules of Origin under the Australia- New Zealand CER Trade Agreement, Interim Research Report, Canberra at page 133.

added in Mexico, why should such a product be considered to be from the United States for the purpose of the AUSFTA?

The AMWU is particularly concerned about this aspect of the proposed AUSFTA. Lack of respect for core labour standards and low wages are a key feature of manufacturing in Mexico. It would appear that under the proposed AUSFTA, some goods presently assembled in Mexican maquilas would be allowed duty free access to the Australian market. While ever core labour standards are not observed for Mexican workers (or while environmental standards are not met) the AMWU strongly believes that it is not appropriate that goods which undergo substantial manufacture in Mexico are in effect granted preferential access to Australian markets.

The AMWU also questions why the rules of origin in relation to the automotive sector are more lax in the proposed AUSFTA agreement than in the North American Free Trade Agreement. In the North American Free Trade Agreement, rules of origin originally required a regional content value of 50% however, this has since risen to 62.5% for automobiles, light trucks, engines and transmissions (and 60% for other automotive products).

The Productivity Commission reports that average local content in Australian produced vehicles is around 75%. Why then did the Trade Minister agree to such a low rule of origin for passenger motor vehicles?³¹

The AMWU also notes that the rules of origin appear to largely operate on a self-assessment basis. Although there is some capacity for requiring the production of records after the event, the AMWU is concerned that the agreement will in practice be difficult to monitor and enforce.

The AMWU urges the Committee to recommend that the Australian government not enter the proposed AUSFTA on the basis that the rules of origin in the agreement do not protect the integrity of the agreement and are not in the national interest.

³¹Productivity Commission 2002, Reivew of Automotive Assitance, Report No. 25, Canberra.

10. Non-Tariff Barriers

The AMWU submits that notwithstanding the bilateral reduction in tariff protection proposed in the AUSFTA there remain a large number of non-tariff barriers which will have the effect of limiting any increase in Australian exports to the United States. The AMWU briefly notes a number of such non-tariff barriers below.

10.1 Product liability insurance in the United States

The AMWU notes the comments of Paul Shepherd, a Victorian manufacturer of metal filters, that for Australian small businesses the costs and logistics of obtaining product liability insurance in the United States are prohibitive:

"I think if you're over there, if you're in America, it's fine, you can get local insurance, but from a perspective here in Australia, local insurers or even multinational or international insurers here, the underwriters won't cover small business.

I mean, we don't even think about sending goods to the States because, you know, I mean we're not all sitting around agonising over it, we're just getting on with exporting in other places in the world ..."32

The AMWU submits that product liability insurance constitutes a considerable trade barrier for small businesses in Australia.

10.2 Technical Standards

The AMWU submits that different technical standards in the United States are a significant barrier for many potential Australian exporters. For instance, as is noted in the AMWU discussion paper appended to this submission:

"Even after the U.S. - Australia FTA comes into effect American exports to Australia of some products such as pressure vessels will enter duty free while most Australian exports of pressure vessels to the U.S. will not be allowed because they do not meet U.S. standards. There is likely to be a number of manufactured products where this is a problem. While mutual recognition of standards is to be addressed by the parties at a later date, there is little evidence to suggest it will not continue as a significant impediment to Australian exports to the United States (both in the procurement market and economy wide)."33

³²The comments were made on ABC Radio on 17 February 2004. A transcripts can be downloaded at www.abc.net.au/am/content/2004/s1046590.htm.

³³AMWU Discussion Paper, "The Implications of the AUSFTA For Government Procurement: What Will Australia Win and Lose" at page 9.

The AMWU submits that technical standards will continue to be a significant trade barrier for Australian exporters to the United States.

10.3 Barriers in the Automotive Sector

A number of the non-tariff barriers which exist for Australian automotive exporters were noted in the Productivity Commission's recent review of automotive assistance. For example the Productivity Commission found:

"Head office constraints and other non-government barriers can also impede exports. While global linkages provide a range of benefits to Australian automotive producers, global sourcing policies can be a significant constraint on exports. Indeed, they may sometimes preclude exports to markets where there are no significant trade barriers in place. Thus, as noted in chapter 4, the decision by Ford (US) to export the Crown Victoria to the Middle East has locked Ford Australia out of that market. More broadly, in discussing the implications of global sourcing policies for its operations, the Australian-owned component producer Air International said: "there remain powerful impediments to the export of technology and design services even though there are effectively no tariff or transport barriers. These might best be summarised as the head office mentality".³⁴

...

"In contrast, there can be no dispute that the understanding which certain US vehicle producers have with the UAW to limit importation of vehicles from their overseas subsidiaries, is designed to help support activity and employment in the US industry. This understanding has previously cost Australian firms export business (see box 8.1). Moreover, at the public hearings, Holden said that in the absence of the USA's 25 per cent tariff on certain light commercial vehicles, demand for its utility in that market would exceed the 20 000 unit ceiling that applies under the understanding between its parent and the UAW."³⁵

...

"In developed countries, firm-specific incentives are often available. Some recent examples include: the provision by the State of Alabama of an assistance package to secure Hyundai's investment in a new assembly plant, which has been variously reported as worth between \$US 123 million and \$US 253 million"³⁶

...

"However, industry-wide investment incentives can also be part of the assistance package in developed countries. For example: " Since 1993, under the Partnership for a New Generation of Vehicles program, the US Government has provided annual

³⁴Productivity Commission 2002, Review of Automotive Assistance, Report No. 25, Canberra at page 105.

³⁵Ibid at page 106.

³⁶Ibid at page 104.

funding of around \$US 240 million for automotive R&D directed at improving environmental, competitiveness and innovation outcomes."³⁷

The above examples of non-tariff barriers represent a significant advantage to U.S. manufacturers in the automotive sector. The AMWU submits that non-tariff barriers in the automotive sector will continue to pose a significant trade barrier for the Australian automotive industry.

10.4 Australian Ship Building and The Jones Act

The proposed AUSFTA does not address the restrictions to foreign suppliers in relation to ship building in the United States (incorporated in the *Jones Act*). In this context, the AMWU notes the submission of the Department of Premier and Cabinet Western Australia to the Joint Standing Committee on Treaties on this issue:

"11.1 The outcome for the shipbuilding industry is seen as a lost opportunity. There do not appear to be significant gains in respect to access to the shipbuilding industry, with only ship repairs and maintenance having its 50 per cent tariff reduced.

"11.2 Shipbuilding is a significant and growing industry in Western Australia and its fast ferry industry is regarded as a world leader. Removal of the Jones Act related restrictions would have allowed the industry to sell Western Australian manufactured boats directly into the United States market. The continuation of the US prohibition on the import of any boats for US domestic use under the Jones Act is disappointing and limits further growth potential."³⁸

In the same way that hundreds of AMWU members in the sugar mills of Queensland have been let down by the Howard Government, it is clear that AMWU members in the ship building industry have similarly been let down. For the AMWU, the exclusion of the Jones Act is just another example of why the proposed AUSFTA is neither fair nor free.

The AMWU submits that non-tariff barriers in relation to ship building will continue to pose a significant trade barrier for the Australian ship building industry.

10.5 Other Barriers

In addition to the barriers identified above the AMWU notes the United States maintains a myriad of other non-tariff barriers on goods and services. Many of these barriers have been identified by the European Commission in its "Report on United States Barriers to Trade and Investment 2003".³⁹ The barriers are extensive and include:

- National security restrictions

³⁷Ibid.

³⁸The Department's submission can be downloaded at www.aph.gov.au/house/committee/jsct/usafta/subs/SUB128.pdf.

³⁹European Commission, "Report on United States Barriers to Trade and Investment 2003", Brussels, December 2003. A copy of the report can be downloaded at http://trade-info.cec.eu.int/doclib/docs/2003/december/tradoc_115383.pdf.

- Trade defense instruments
- Technical barriers to trade
- Subsidies and government support, including support for U.S. airlines.
- Tax measures
- Lack of prompt compliance with WTO rulings and recommendations

Given that many of the issues identified in the European Commission's Report are not dealt with in the proposed AUSFTA, the AMWU submits that it would appear that a whole range of U.S. non-tariff barriers will continue to pose significant trade barriers for Australian industry.

10.6 Conclusions on Non-Tariff Barriers

The AMWU submits that the non-tariff barriers not dealt with in the proposed AUSFTA constitute a significant limitation upon Australian exporters to the United States. The AMWU submits that the proposed AUSFTA will not be effective in removing such barriers and will not lead to free and fair trade between the United States and Australia.

The AMWU urges the Committee to recommend that the Australian Government not enter the proposed AUSFTA on the basis that the non-tariff barriers facing Australian exporters in their relationship with U.S. industry prevents the proposed AUSFTA from bringing about genuinely free or fair trade between the United States and Australia.

11. Government Procurement

The AMWU submits that the proposed AUSFTA will have serious implications for Commonwealth and State Government procurement policy, industrial development policy and employment opportunities in all states of Australia.

The AMWU notes that the recently released CIE report undertakes an analysis of the government procurement provisions in the proposed AUSFTA. However the CIE report contains only a partial analysis of government procurement:

- The report does not deal with state government procurement.
- The report significantly overestimates the potential gains for Australian firms in exporting to the US procurement market.
- The report incorrectly assumes that the changes to Australia's procurement regime will not lead to any increase in Australian procurement going to US suppliers and other importers.
- No attempt is made to assess the impact of abandoning "buy Australian" policies on industry development in Australia.

In contrast the AMWU has conducted an analysis of the government procurement provisions of the AUSFTA covers both state and federal procurement. That analysis is contained in a Discussion Paper appended to this submission. In summary, the data available on foreign access to US procurement market leads the AMWU to conclude:

- Better access to US Federal and State procurement markets is likely to lead to Australian firms winning less than \$100 million worth of procurement contracts (they already win \$50 million without the AUSFTA).
- By 2010, or shortly thereafter, Australia will lose in the vicinity of \$400 million to imports as a result of changes to local procurement policies.

The AMWU therefore believes the government procurement provisions will result in a substantial net loss to Australia. This will have a significant negative effect on local jobs and industries. However, it is of perhaps even greater long term significance that Australia will be giving up its current capacity to promote growth in industries of the future such as: biotechnology and life sciences; information and communications technology; electronics; and advance materials. If Australia is to thrive in a global economy it is critical that our governments maintain enough policy levers to build and encourage industries of the future. If ratified, the proposed AUSFTA will severely limit the capacity of Australian governments to fulfil this vital role.

Finally, the AMWU believes that it is particularly notable that no Canadian provincial government has agreed to be bound to a procurement agreement with the United States. This is despite the Federal Canadian government signing the World Trade Organisation Government Procurement Agreement.

The AMWU urges the Committee to recommend that the Australian government not enter the proposed AUSFTA on the basis that the provisions relating to government procurement are not in Australia's national interest.

In the alternative, the AMWU urges the Committee to recommend that no State Government should agree to be bound by the procurement provisions in the proposed AUSFTA.

12. Failing the Laugh Test: The Centre For International Economics Report

The AMWU submits that the latest CIE report paints a distorted picture of the likely effects of the proposed AUSFTA. The CIE report significantly overestimates the benefits of the agreement while either ignoring or seriously underestimating the costs.

The CIE report claims the proposed AUSFTA is likely lead to three types of benefits to the Australian economy: investment gains, dynamic gains and static gains. The AMWU does not accept the likelihood of these gains. The AMWU highlights problems with the calculations of each of the claimed benefits below. In addition the AMWU notes the importance of some of the costs that CIE has simply put in its "too hard basket".

12.1 The Predicted Investment Gains

There are at least two fundamental problems with the CIE estimate of the gains accruing to Australia as a result of the investment provisions of the proposed AUSFTA. Firstly, the CIE overestimates the increase in investment that is likely to take place as a result of relaxing Australia's investment rules. Secondly, the CIE over simplifies the effect of any increase in foreign investment brought about by a loosening of Australia's foreign investment screening procedures.

12.1.1 *The Increase in Investment*

The CIE report dramatically overestimates the likely increase in foreign investment to be brought about by the relaxation of Australia's foreign investment rules. This is surprising as the CIE is clearly aware that in practice Australia's investment controls have rarely been used to prevent foreign firms from investing in Australia. For instance, the CIE report notes that over the past five years, once residential real estate is excluded, only 4 of 2285 (0.18%) proposals for foreign investment were rejected.⁴⁰ In this context the AMWU further notes that in 2002-2003, once residential real estate is excluded, no foreign investment proposals were rejected.⁴¹

Such figures strongly suggest that the controls Australia currently has on foreign investment do not amount to a significant limitation on the level of foreign investment in Australia. When the CIE rhetorically asks "how many investments could have been deterred by the presence of the restrictions", the only reasonable conclusion must surely be "extraordinarily few".

Instead, the CIE appears to assign considerable weight to the findings of an OECD Report which claimed that Australia is "at the restrictive end" of the OECD scale on restrictions to foreign investment. However, such headline results can be misleading. For example as Richardson has noted in a paper on the proposed AUSFTA and foreign investment:

"The OECD also gives some quantitative research on the restrictiveness of the various regulatory regimes that deal with foreign investment in the 28 OECD countries. The OECD ranks countries in terms of their restrictiveness and, on that basis, suggests that

⁴⁰CIE report at page 32.

⁴¹Richardson D., Current Issues Brief No. 7 2003-04 Foreign investment and the Australia United States Free Trade Agreement, Australian Parliamentary Library, 8 March 2004. The article can be downloaded at www.aph.gov.au/library/pubs/CIB/2003-04/04cib07.htm

Australia is much more restrictive than the US. For example, the US with a rank of 0.17 is the 15th most restrictive of the 28 while Australia with a rank of 0.27 is the 5th. (Ranking goes from least restrictive at zero to most restrictive at one.) This research suggests that Australia, being the heavier regulator, may well have more obligations to make concessions. However, to a large extent the OECD exercise compares apples and pears. The US comes out with a higher score on absolute limits on foreign ownership but lower on screening and restrictions on foreign personnel and operational freedom. Australia's screening could be seen as hardly worth worrying about compared with absolute limits on foreign ownership in communications and other sectors of the US economy.”⁴²

It is the AMWU's submission that given the extremely infrequent rejection of foreign investment by Australia's Foreign Investment Review Board, the effect of relaxing Australia's foreign investment provisions will have little or no measurable effect on the “equity risk premium” discussed by the CIE and will therefore not lead to an increase in U.S. investment in Australia to anything like the extent predicted by the CIE.

12.1.2 Benefits Associated With the Investment

The AMWU further submits that not only has the CIE overestimated the potential for increased investment as a result of the proposed AUSFTA, the CIE has over simplified the effect of any increase in foreign investment that may take place in the proposed AUSFTA regime.

While the type of modelling used by the CIE relies on fairly typical neo-classical assumptions concerning perfect competition and the behaviour of firms, the actual effect of foreign investment on an economy is heavily dependent upon the type of investment undertaken and the circumstances in which that investment takes place. Again it is relevant to note the observations of Richardson:

“The term "foreign investment" includes a continuum of transactions from short-term speculative capital investments of the type that were implicated in the Asian crisis through to direct investment by foreign interests that contributes to the Australian capital stock. Examples of the latter would be a foreign-owned car manufacturer tooling up to produce a new model or a foreign-owned mining company developing a mineral deposit.

A more problematic example of direct foreign investment is the case of a foreign takeover of an Australian company. Such a takeover could be argued to involve benefits for the company concerned. Its operations may be improved by better access to management, technology or overseas markets. Indeed, it could be argued that there would be no incentive for any takeover unless the acquiring management thinks it could earn additional profit by utilising the assets of the target company better than the incumbent management.

In principle we can think of a market in corporate ownership and control and, subject to certain conditions there will be a competitive equilibrium in which ownership and control will go to those who are in the best position to most effectively manage the corporate assets. However, this is complicated in the real world because generally the businesses involved are large players with some influence in their market. The

⁴²Richardson, *ibid.*

company initiating the takeover may well be motivated by a desire to better manage the assets of the target company. However, there may also be an aim to dominate the market at the expense of customers, suppliers or some other group. If the parties to the takeover are in the same country then at least the winners and losers will offset each other. However, when the winners and losers are in different countries then one country can be said to gain at the other's expense. In order to really determine whether or not there are merits in a takeover some knowledge of the economic environment is required, including some idea of the incentives facing the actors involved.”⁴³

Clearly by relaxing the restrictions on the screening of foreign investment it is almost inevitable that at least some investment will enter Australia which to a greater or lesser extent may not be in Australia's national economic, social or environmental interest. The possibility of such costs are not accounted for in the CIE's modelling which assumes uniform *gains* to the Australian economy. Indeed on balance there is no reason to conclude that the predicted potential gains to the economy would not be more than offset by the equally likely potential losses.

Moreover the concessions made in relation to investment limit the ability of Australian governments to take a more proactive approach to foreign investment, that is, one that extends beyond the Foreign Investment Review Board national interest test. As noted elsewhere in this submission by entering the proposed AUSFTA, Australia would be giving up many very useful tools including the ability to insist upon local content requirements and technology transfers when approving foreign investment in Australia. Such opportunity costs are also excluded from the CIE modelling.

The AMWU strongly submits the CIE report on this issue is so flawed as to not represent a useful contribution to the decision of whether or not to enter the proposed AUSFTA.

12.2 The Predictions of Dynamic Gains

The AMWU is extremely doubtful that the controversial issue of "dynamic gains" from trade agreements has reached the point where such gains can be reliably modelled.

The AMWU notes for instance that while the CIE posits that "[a]ny dynamic productivity gains for Australia from AUSFTA would be facilitated by the linkages between competition, innovation and productivity"⁴⁴ the AMWU is not convinced that the such linkages *must necessarily* lead to a growth in welfare for Australian workers, let alone the types of gains inferred by the report. Furthermore, because it is most unclear exactly how such gains come about (to the extent they can be shown at all) there is a need for great caution in interpreting such apparent windfalls.

As the CIE report notes the “dynamic gains” debate is not free from controversy and there remain those who "continue to doubt the link between trade liberalisation and dynamic productivity gains".⁴⁵ As Quiggin observed, in a paper noted by CIE and delivered at the Productivity Commission's workshop on Microeconomic Reform and Productivity Growth:

“4.4 Dynamic gains and X-efficiency

⁴³ Ibid.

⁴⁴ CIE report page 19.

⁴⁵ CIE report page 17.

Most estimates of the welfare costs of microeconomic distortions are small relative to national income. A common response has been to argue that these estimates are static and that the removal of distortions will yield large, but unspecified dynamic benefits. Although the growth model of equations (4.1) to (4.3) is dynamic, it is not immediately obvious where dynamic benefits of reform might arise.

It is often argued that increased competition will force firms and their employees to become more efficient, by working smarter. This is a variant of the X-efficiency hypothesis put forward by Liebenstein (1966). In the context of the current model, it may be argued that, in addition to the initial effect of removing allocative distortions and thereby generating once-off increases in A, microeconomic reform will increase competition and thereby lead, over time, to the elimination of technically inefficient firms. This will result in an upward trend in A, and therefore to higher rates of growth of Y. These arguments are critically assessed by Quiggin (1998), drawing on Stigler's (1976) critique of X-efficiency theory. It is argued that most apparent improvements in X-efficiency arise, in reality, from increased work intensity, and therefore do not involve increases in Y/L.”

The AMWU submits that should any "dynamic gains" arise from additional competition causing an increase in "work intensity", a breakdown in working conditions, more dangerous work, less family friendly work practices or a greater use of precarious employment - then the types of *gains* predicted by the CIE may actually represent significant *losses* for Australian workers and Australian communities.

Furthermore, the AMWU also takes issue with the manner in which the CIE attempts to calculate the claimed dynamic gains of the agreement. If the AMWU correctly understands the approach taken, the calculations appear to be based on the so called dynamic gains suggested by Chand (and a number of co-authors) in relation to various sectors within manufacturing that underwent a unilateral reduction in industry assistance from the late 1960's to the early to mid-nineties. The CIE's approach is to average the results from three of Chand's studies and, after making a calculation to try to take account of the bilateral nature of the current proposed tariff reductions, apply those figures to the whole economy.⁴⁶

While the AMWU has not yet had the opportunity to analyse the studies relied upon by the CIE, the AMWU submits that there are a number of obvious problems with this method for estimating the claimed dynamic gains in the proposed AUSFTA.

Firstly, there is no reason to suggest that merely by taking the average of three separate studies the CIE has arrived at anything approaching an appropriate figure. The AMWU notes that in taking the average the CIE appears to have taken the upper end of the one of the studies and therefore skewed the average upwards however, even if the CIE had taken a number from the lower end of the study, there is still no reason why the average of three studies is in any way a valid process to arrive at a relevant estimation.

Secondly, the reliance placed upon the results of at least one of the studies (the study which was presented to a Productivity Commission Workshop) appears to be inappropriate in a public policy

⁴⁶CIE report page 20.

context.⁴⁷ The AMWU notes the comments of the “discussants” published at the end of the paper which included the following observation on Chand *et al's* paper:

"Chand , McCalman and Gretton (CMG) analyse the effect of changes in the level of protection on output of eight manufacturing industries. **As an academic piece of research, this paper represents an interesting investigation of the problem** and concludes that the falling trend in protection over the last 27 years have been accompanied by increased growth in industry output adjusted for the level of the assistance. **If however, this research, like any other, is used to draw actual policy conclusions, additional econometric analysis is necessary.**" (emphasis added)⁴⁸

The AMWU submits that this is clearly not a strong enough foundation to base calculations which estimate alleged dynamic gains associated with the proposed AUSFTA.

Thirdly, the studies relied upon appear to have only dealt with a very limited part of the economy (for instance the paper presented to the Productivity Commission workshop dealt with only eight sectors of the manufacturing industry). There is nothing to suggest that such results can be validly used as a proxy for proposed economy wide gains. The AMWU again notes the comments of the Productivity Commission Workshop in relation to the paper by Chand *et al* presented to that workshop (and relied upon by the CIE to estimate the potential dynamic gains to the economy):

"It was also recognised that while there is evidence of scale economies in manufacturing industries, there are many service industries that tend not to exhibit significant economies of scale. **Overall, the differences between the sectors serve to complicate comparisons between microeconomic and macroeconomic studies of productivity growth.** The relative growth of service industry activities has further complicated the reconciliation of macro and micro trends in productivity growth."⁴⁹ (emphasis added)

Again, the AMWU submits that the data upon which CIE bases its calculation of the dynamic gains to be made by entering the proposed AUSFTA are clearly not appropriate for such a purpose.

Finally, the AMWU notes the studies all dealt with a period of time that ended at the latest nine years ago. There have been extensive changes to the manufacturing industry both in Australia and globally over the last ten years. Equally there have been substantial changes to the broader Australian and global economy over the same period. The AMWU therefore questions to what extent the data derived from the studies can be used to predict current reductions in assistance in the context of a bilateral preferential trade agreement with the United States.

For all of the above reasons the AMWU strongly submits that the estimates of the CIE in relation to the so called dynamic gains of the proposed AUSFTA are manifestly unreliable and cannot form part of any alleged benefits to the proposed AUSFTA.

⁴⁷See Productivity Commission and Australian National University (PC and ANU) 1998, Microeconomic reform and productivity growth, Workshop Proceedings, AusInfo, Canberra. The full report of the proceedings can be found on the Productivity Commission's website at www.pc.gov.au/research/confproc/mecrefpg/

⁴⁸ Productivity Commission and Australian National University at page 276.

⁴⁹Productivity Commission and Australian National University at page 280.

12.3 The Predicted Gains From Tariff Reductions - Merchandise Trade

The AMWU first makes the point that even assuming the CIE report contains a reasonable estimate of the "static gains" to be made as a result of the proposed AUSFTA - those gains are very low and do not outweigh the other economic and social costs of the agreement. The AMWU does not however accept that the CIE report does contain a reasonable estimate of the costs and benefits of trade liberalisation under the proposed AUSFTA.

12.3.1 *Neo-classical Assumptions - Best Left In the Classroom*

Firstly the AMWU notes that the models used by the CIE contain all of the standard neo-classical assumptions about perfect competition, standardised consumer preferences, full employment and "rational" behaviour. Nobody outside of the economics department of universities actually believes these assumptions are valid. As such the AMWU does not accept that the models are capable of providing an accurate assessment of real world changes to trade and industry policy.⁵⁰

12.3.2 *Specific Limitations of The Modelling*

Secondly, even if the dubious assumptions underpinning the neo-classical approach are put aside for the sake of argument, the modelling still appears to contain features which render the modelling better suited to academic debate than assessing important public policy issues:

- The modelling makes some spectacularly unrealistic assumptions in relation to labour. For example the modelling assumes that all wages across all industries are the same. The modelling then proceeds to predict wage and employment movements.
- The modelling reduces the complexity of the real world by operating at a sectoral level. For the GTAP model this involves reducing the world to 57 sectors, while the G-Cubed model reduces the world to only 12 sectors. This means, for example, that the GTAP model is unable to distinguish between car manufacturers and components manufacturers, while the G-Cubed model is even less sensitive and cannot distinguish between metal products, chemical products, machinery, electronics or petroleum products.
- The CIE in calculating the sectoral effects of the agreement, appears to use standard price elasticities for all sectors and all nations.⁵¹ The elasticities assigned to a product will determine what the import substitutability is on any particular item. The elasticities are critical to determining the trade flows of a trade agreement. The AMWU submits that by using standardised elasticities the modelling *cannot* provide an accurate assessment of how different sectors and subsectors will be affected in the real world where elasticities are not standardised.
- Because tariffs vary from product to product and the CIE models only apply at the sectoral level, in order to calculate the protection afforded in each sector, the modellers must apply some method of aggregating the relevant tariffs. In the latest study it appears the CIE have used a combination of import weights (which underestimate the protective effect of tariffs) and arithmetic averaging. Significantly CIE states that it *did not have time* to use production weights:

⁵⁰See for example page 146 of the CIE report.

⁵¹CIE report pages 81 and 91-92.

"Despite the (potential) advantages of using production weights, the time available for this study has meant that it has not been possible to obtain production weights and to use them to aggregate the tariffs contained in the tariff schedules".⁵²

The AMWU notes that in its earlier study on a proposed Australia - United States Free Trade Agreement the CIE used production weights.⁵³ The AMWU strongly submits that it is totally unsatisfactory that the examination of the possible effects of the proposed AUSFTA is so rushed that the modellers commissioned to estimate the economic effect on their own admission cannot get an accurate estimate of the trade barriers to be reduced.

- In relation to the automotive sector, instead of comparing the reductions in assistance to the level of assistance at the time of writing the report, the modellers have already factored in the Howard Government's proposed unilateral tariff reductions (including a fall of the tariff protection from 15% to 10% in 2005 and from 10% to 5% in 2010). The CIE has also factored in to the baseline calculation the tariff reductions contained in the yet to be ratified (and not publicly disclosed) Australia - Thailand Free Trade Agreement⁵⁴. The AMWU submits that by factoring such policies there appears to have been a significant underestimation of the results of reducing protection in this sector.
- Again in relation to the automotive sector, the AMWU notes the modelling cannot take into account what will happen if Mitsubishi or another automotive manufacturer ceased operations in Australia because of changes in trade policy. The consequences of such an occurrence would represent a serious "shock" which the CIE's models simply cannot predict or capture.

For all of the above reasons, the AMWU does not accept that the results produced in the latest CIE study in relation to tariff reductions provide a sufficiently accurate estimate of the likely effects of the proposed AUSFTA for the results to be relied upon in a public policy context. Indeed the CIE report's most significant contribution to the consideration of whether or not Australia should enter the proposed AUSFTA is perhaps that it exposes the serious inadequacy of the process by which potential trade agreements are considered in Australia.

The AMWU urges the Committee not to accept the CIE's modelling of tariff reductions.

⁵²CIE report, page 136.

⁵³Centre for International Economics, "Economic Impacts of an Australia - United States Free Trade Area", Canberra and Sydney, June 2001 at page 20.

⁵⁴CIE report page 64.

12.4 Some Costs Not Included in the CIE's Estimates

As has been discussed above, the CIE has relied on some highly questionable assumptions and methodologies to enable its latest report to squeeze out every possible or theoretical gain arising from the proposed AUSFTA. The CIE is however markedly less willing or able to assess the likely costs of the agreement. The following represent a few of the notable examples of costs that expressly fell into the CIE's "too hard basket".

12.4.1 Costs of Negotiating the Agreement

The CIE was unable even to "estimate a likely range" of the costs incurred by the Department in negotiating and drafting the proposed AUSFTA, as well as the money spent by various groups lobbying the department.⁵⁵

At least as far as DFAT is concerned, the AMWU would find it surprising if DFAT could not provide an estimate of the costs negotiating, drafting and promoting the agreement.

It would also be useful - although admittedly much harder - to speculate as to what the opportunity cost of diverting such resources to attempt to secure a free trade deal with the United States.

12.4.2 Administrative Costs

The CIE report states that it is "unclear whether there will be a net increase or decrease in ... administrative costs".⁵⁶

The AMWU submits that with the creation of a number of new working groups, appeal processes and disputes mechanisms, combined with an additional set of rules to sit along side the other pre-existing trade and investment rules which apply to other nations - there will clearly be a substantial increase in "administrative costs".

The AMWU also questions how the CIE's inability to determine the existence of additional administrative costs sits with the CIE reported results from GTAP modelling which suggests a 0.1% increase in employment in "public administration" (combined with a 0.2% wage increase for employees in that sector).⁵⁷ At the very least such a result, assuming the authors of the report are willing to stand by their own results, surely points to a not insignificant increase in costs to Australian governments in relation to employment and associated costs.

12.4.3 Costs from the Extended Copyright Term

The CIE notes that "in the absence of robust data on the average economic life of creative works, we are not able to estimate the extent of the additional cost consumers may incur in purchasing existing works".⁵⁸ The AMWU submits that an absence of robust data has not stopped the CIE from predicting a number of significant gains from the agreement.

⁵⁵CIE report page 84.

⁵⁶CIE report at page 84.

⁵⁷CIE report at page 85.

⁵⁸ CIE report at page 38.

In not estimating the effects of the changes in copyright laws that would become necessary because of the proposed AUSFTA, the CIE appears to be prepared to largely ignore the concerns that have been expressed by Vice-Chancellors and librarians - people with first hand knowledge of the likely effects of the proposed changes to Australia's copyright laws.

12.4.4 Government Procurement

This issue is dealt with elsewhere in the AMWU's submission however, it is important to note in the present context that while the CIE report is able to give an estimate of possible benefits to be gained as a result of limited Australian access to the US procurement market, it appears to be prepared to make the totally implausible assumption that there will be no costs associated with giving up the right to have offsets or local content requirements in federal government spending. The AMWU submits that forgoing such a right will in fact lead to much greater costs than will be covered by the access granted to Australian firms to the US government procurement market.

This likely deficit in government procurement has significant consequences for the accuracy of the CIE modelling which is erroneously based on an expected \$200 million gain.

12.5.5 Labour Transaction Costs

The AMWU submits that it is unsatisfactory that "labour transaction costs" are not taken into account in the CIE report.⁵⁹ In reality "labour transaction costs" represent the "collateral damage" of free trade policies. "Labour transaction costs" can include: the economic loss of skills when a worker is made redundant and not able to use their skills in their next job, the costs of retraining workers for new employment, the costs incurred by workers in looking for work, the costs of relocating, the costs of social services such as employment placement and counselling, the costs of unemployment benefits and other social security payments, and the costs associated with poorer health outcomes and family breakdown due to the psychological stress of being made redundant.

In this context it is pertinent to note that Australian Bureau of Statistics figures show that rather than having the characteristic of "perfect mobility" a great many unemployed workers incur significant costs prior "transacting" into another position. For example, the latest ABS statistics show that the average duration for unemployed workers in Australia is 49.7 weeks.⁶⁰ Such periods of unemployment translate into substantial "labour transaction costs".

The AMWU further specifically notes that in relation to those workers who are retrenched or made redundant, ABS statistics published in 2002 show that as at July 2001 of those workers who were employed:

- 50.5% of workers who had been retrenched or made redundant in the previous three years had left the industry.
- 40.6% of workers who had been retrenched or made redundant in the previous three years had changed occupation.

⁵⁹CIE report at page 84.

⁶⁰ Australian Bureau of Statistics, "2004 Labour Statistics In Brief Australia", ABS Catalogue No. 6104.0.

Meanwhile 16.6% of those who had been retrenched or made redundant in the previous three year period were unemployed.

The above figures give an indication of some of the lost skills and personal hardship which are inevitably involved in "labour transaction costs". While ever CIE modelling or similar modelling makes no attempt to account for the real life costs associated with unemployment, the AMWU submits the modelling is of little value in a public policy context.

12.6 Conclusions on the Modelling

The AMWU submits that the CIE Report is so flawed that it cannot be regarded as a useful estimation of the effects of the proposed AUSFTA. Although the CIE is careful to acknowledge many of the limitations of the modelling it is hard to escape the conclusions that ultimately the report was commissioned, and will be largely used, for the quotable (*though entirely flawed*) predictions of billions of dollars worth of economic gains to Australia.

In this respect the AMWU notes the views of two prominent commentators in the trade policy debate.

Firstly, Alan Wood, Economics Editor of *The Australian*, in an article entitled "If this FTA is so great, why won't a scared John Howard let the Productivity Commission review it":

"Because the Government has already determined the result it wants and it can't trust the [productivity] commission to deliver it"

"The modelling work commissioned by the Government is not going to convince anybody if it simply confirms Howard's view. It certainly won't dispel the suspicion the Government has something to hide, so the FTA may end up a political liability rather than an asset for the Government."⁶¹

And secondly, Professor Garnaut on the latest results of the CIE modelling:

Some of the results don't pass the laugh test. Uh, now in econometrics, where you're relying on complex models to draw conclusions, what comes out the other end depends on the quality of what goes in. And before economists are really satisfied with the results of any piece of econometric modelling, they put it through the laugh test.

And the laugh test is, can someone who knows the real world that's meant to be described by the modelling exercise look at the results and not laugh? And I don't think that this exercise passes the laugh test.⁶²

The AMWU urges the Committee to recommend that the proposed AUSFTA not be entered into on the basis that there is no reliable study to show that the agreement is in the economic, social or environmental interest of Australia.

⁶¹See the article "If this FTA is so great, why won't a scared John Howard let the Productivity Commission review it?" Allan Wood, *The Australian*, 9 March 2004.

⁶²Ross Garnaut on the proposed AUSFTA, ABC Radio, PM, 3 May 2004.

12. Conclusion

The AMWU submits that each of the problems the union has identified in this submission justifies the Australian government not taking action to enter the proposed AUSFTA.

Whether considered on an economic, social or environmental basis the likely benefits of the proposed AUSFTA are not sufficient to outweigh the likely costs.

The AMWU strongly urges the Committee to recommend that Australia should not enter the proposed AUSFTA.

Appendix: AMWU Discussion Paper on Government Procurement