COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

FOREIGN AFFAIRS, DEFENCE AND TRADE REFERENCES COMMITTEE

Reference: General Agreement on Trade in Services and Australia-United States Free Trade Agreement

FRIDAY, 9 MAY 2003

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SENATE

FOREIGN AFFAIRS, DEFENCE AND TRADE REFERENCES COMMITTEE

Friday, 9 May 2003

Members: Senator Cook *(Chair)*, Senator Sandy Macdonald *(Deputy Chair)*, Senators Hogg, Johnston, Marshall and Ridgeway

Participating members: Senators Abetz, Boswell, Brandis, Carr, Chapman, Collins, Coonan, Denman, Eggleston, Chris Evans, Faulkner, Ferguson, Ferris, Forshaw, Harradine, Harris, Knowles, Lees, Lightfoot, Mackay, Mason, McGauran, Murphy, Nettle, Payne, Santoro, Stott Despoja, Tchen, Tierney and Watson

Senators in attendance: Senators Cook, Harris, Johnston, Marshall and Ridgeway

Terms of reference for the inquiry:

To inquire into and report on:

1. The relevant issues involved in the negotiation of the General Agreement on Trade in Services (GATS) in the Doha Development Round of the World Trade Organisation, including but not limited to:
   a) the economic, regional, social, cultural, environmental and policy impact of services trade liberalisation
   b) Australia's goals and strategy for the negotiations, including the formulation of and response to requests, the transparency of the process and government accountability
   c) The GATS negotiations in the context of the 'development' objectives of the Doha Round
   d) The impact of the GATS on the provision of, and access to, public services provided by government, such as health, education and water
   e) The impact of the GATS on the ability of all levels of government to regulate services and own public assets
2. The issues for Australia in the negotiation of a Free Trade Agreement with the United States of America including but not limited to:
   a) the economic, regional, social, cultural, environmental and policy impact of such an agreement
   b) Australia's goals and strategy for negotiations including the formulation of our mandate, the transparency of the process and government accountability
   c) The impact on the Doha Development Round

WITNESSES

Committee met at 9.07 a.m.

CHAIR—I declare open this public meeting of the Foreign Affairs, Defence and Trade References Committee. Today the committee continues its public hearings into the General Agreement on Trade in Services and the proposed Australia-US free trade agreement. The terms of reference set by the Senate are available from secretariat staff and copies have been placed near the entrance to the hearing room. Today's hearing is open to the public. This could change if the committee decides to take any evidence in private.

Witnesses are reminded that the evidence given to the committee is protected by parliamentary privilege. It is important for witnesses to be aware that the giving of false or misleading evidence to the committee may constitute a contempt of the Senate. If at any stage a witness wishes to give part of their evidence in camera, they should make that request to me as the chairman and the committee will consider that request.

Should a witness expect to present evidence to the committee that reflects adversely on a person, the witness should give consideration to that evidence being given in camera. The committee is obliged to draw to the attention of a person any evidence which, in the committee's view, reflects adversely on that person and to offer that person an opportunity to respond. Witnesses will be invited to make a brief opening statement to the committee before the committee embarks on its questions.

[9.09 a.m.]

BAULK, Mr Brian, Senior Industrial Research Officer, Communications, Electrical and Plumbing Union

EASON, Ms Rosalind, Senior Industrial Research Officer, Communications, Electrical and Plumbing Union

McGRATH-KERR, Ms Marie, Chairman, Post Office Agents Association Ltd

TALBOT, Mr Michael, Consultant, Post Office Agents Association Ltd

CHAIR—It is my privilege this morning to welcome representatives of the Post Office Agents Association and the Communications, Electrical and Plumbing Union and to invite you to address your joint written submission.

Mr Baulk—Ms Eason and I represent the CEPU and Ms McGrath-Kerr and Mr Talbot represent the Post Office Agents Association. I would like to make a brief opening statement. Thank you for this opportunity to address the Senate Foreign Affairs, Defence and Trade References Committee. The issues which the CEPU wish to raise with the committee are of both a general and an industry specific nature. As you will see from our submission, they go to the questions of the nature of WTO and GATS processes as well as to questions which more immediately affect the key industry sectors in which the CEPU's communications division operates—that is, the postal and telecommunications sectors.

In relation to the first level of issues, GATS processes, we wish to reiterate our concerns about the lack of transparency which has characterised the negotiation of these agreements to date. We join with other sections of the community in calling for the development of mechanisms which will allow much wider public debate over, and input into, the negotiation of such agreements, which have potentially far-reaching consequences in so many areas of our community's life. We also must ensure that the decision making powers of our democratic institutions are not undermined by commitments which bind future governments indefinitely and which foreclose policy options in response to new technological developments.

At the international level, we are keen to see the GATS processes informed and disciplined by that broader debate on the impacts of globalisation which is now being conducted by communities and agencies worldwide. In our submission we have drawn the Senate's attention to a statement by the global union federation to which we are affiliated, Union Network International. This calls for a closer working relationship to be established between the WTO, United Nations agencies, other intergovernmental agencies concerned with services, and organisations representing those who work in the service sectors concerned—that is, trade unions. In particular, the statement calls for the involvement of the ILO and, at national level, trade union bodies in negotiations over the 'movement of natural persons', which by definition is a labour issue. It also emphasises the need for closer interaction between the WTO and such agencies as the International Telecommunications Union and the Universal Postal Union,

particularly in the ongoing assessment of the impacts of GATS on member nations. The CEPU endorse this stance and recommend it to the Senate committee.

The CEPU's closer interests in these current GATS negotiations relate, of course, to the postal and telecommunications sectors. We know Australia has received requests in both these areas which run counter to current policy and, in our view, to the public interest. In the postal area, Australia is being asked to undertake commitments in the postal and courier services categories which we have not done to date. This raises the possibility of a further liberalisation of postal services, a move which we believe would erode Australia Post's capacity to provide the first-rate service to all Australians that this community currently enjoys. We would emphasise to the committee that the Australian postal market is already significantly liberalised. The only area which is not open to competitors is the reserved service, which covers articles weighing up to 250 grams—a relatively low threshold by international standards. There are no foreign ownership restrictions on companies operating in the competitive sectors of the market. This all leads us to conclude that the area that these requests are targeting is indeed the reserved service. We would be happy to elaborate on the implications of opening up this section of the market in our later discussion.

The Australian telecommunications market is already fully liberalised: there are no legislative barriers to entry and the only foreign ownership restrictions are those on Telstra. These are the subject of the requests from the EU, and probably from the US. The union oppose any dilution of these restrictions, believing that majority Australian ownership—and indeed public ownership—of our one fully national carrier makes sense both economically and strategically. At first glance, it may appear that this is the only outstanding matter for Australia in this current round of negotiations—we have, as it were, little left to trade in the telecommunications sector. However, a closer look reveals a number of issues concerning international traffic exchange which we believe warrant the committee's attention and which we would be happy to discuss further. They are not easily resolved; in fact, they raise rather worrying questions about the capacity of the WTO or any other international body to constrain market power operating at a global level.

When we look at the debate over the treatment of international trade in both telephony and Internet traffic we could be forgiven for wondering whether the GATS is anything more than a mechanism for prising open the markets of weaker nations for the benefit of the strong. In our view, the Australian government has a responsibility to see that this is not the case, whether we are in the position of the stronger or weaker party in any negotiations.

This brings me to the US-Australia free trade agreement currently under negotiation. We have not commented in any detail on this proposed agreement in our submission, not least because the exact parameters of the negotiations remain, as usual, unknown. You will note, however, our letter to the Minister of Trade expressing our concerns about the treatment of postal services in such an agreement. They are in line with the matters we have already touched on in relation to GATS.

Two other matters that we think should be noted by the committee have come to our attention in recent weeks. One is the treatment of mobile services in the telecommunications chapters of both the US-Singapore and US-Chile free trade agreements. In both, mobile service providers are exempted from certain key provisions of the agreement, such as the right of regulators to

require interoperability of networks. This goes against the thrust of Australian policy and should not, in our view, be agreed to in the US-Australia negotiations.

The other matter is the commitments the US is likely to seek in the e-commerce area, judging from the content of these other bilateral agreements. These commitments are made in relation to digital products—a category that is alarmingly wide. Digital products are defined so as to include both goods and services and to encompass virtually any information or transaction that is digitally encoded. Obviously, nondiscrimination requirements in relation to such products have the potential to undermine cultural policy. However, the union is concerned that commitments made in relation to so sweeping a category could also feed back into the telecommunications and postal sectors.

The union notes that no commitments have been made in Australia's initial GATS offer in relation to e-commerce. We trust that this position will also be adopted in the US-Australia negotiations. We also note that Australia's initial GATS offer contains no commitments that go beyond the domestic status quo in the telecommunications sector and none at all in postal. However, it is still early days. The Australian community must continue to have opportunities to monitor and debate these agreements as they are developed. We congratulate the Senate for taking this particular initiative to help democratise the GATS and FTA processes.

Ms McGrath-Kerr—I am Chairman of the Post Office Agents Association. I am here with my colleague Michael Talbot today. It is not our intention to give a preamble as we are sharing the first hour—only an hour—with colleagues from the CEPU. The Post Office Agents Association represents 3,000 licensees—that is, owner-operators of licensed post offices franchised or licensed to Australia Post—and 6,000 mail contractors. All these people are private operators who have invested their own money in the business. We estimate their investment in the Australia Post business to be around the $800 million mark, so it is a substantial investment, and that is why we are particularly interested in the WTO GATS issue.

I am not an expert on this. We have cooperated and consulted with our colleagues at the CEPU. We are very happy to share a spot with them today. As Mr Talbot has done most of the work for POAAL on this issue, I will ask him to respond on our behalf to any questions directed to us.

CHAIR—Can you give us a picture of what your members' businesses look like. Are they exclusively agents or do they run mixed businesses in which an agency is typically part?

Ms McGrath-Kerr—Both. The majority of them have what we call stand-alone post offices, if we are just talking about licensed post offices. When the business levels are such that it is a fully-fledged business in its own right, it is quite onerous to take on another business as well as that, so most of them are stand alone. However, in country areas, as some of you would know, there is certainly not enough income from a licensed post office for it be viable, so most of them in country areas—particularly small country areas—are operated in conjunction with another business. This is usually a general store and sometimes a roadhouse or a small newsagency but it is usually a one-business town in effect—the general store and post office in one, and quite often it has the petrol pump outside.

Most of the 6,000 mail contractors operate just as mail contractors. Some of them, though, have to have a supplementary job, perhaps in the afternoons when they have finished their mail route. It depends on what type of mail contractor they are. If they are a parcel contractor working in the city, that is a full-time job. I hope that answers your question.

CHAIR—Mr Baulk, how many employees are there in Australia Post? What sorts of numbers are we looking at?

Mr Baulk—I understand there are approximately 35,000 employees of Australia Post, made up of full-time and part-time employees.

CHAIR—In a moment I will ask for questions from the committee. You have given us quite an extensive submission. On page 39, which is attachment 3, there is a table titled 'International comparisons on basic postage rates'. Can you explain those headings for me so I can understand what I am looking at.

Mr Baulk—I will do my best, Chair! When I have done that, I would like to raise one issue. I think we have a couple of changes to our submission.

CHAIR—Certainly. You could take those first, if you like.

Mr Baulk—I might ask Ms Eason to outline those changes.

Ms Eason—We have a minor correction; we perhaps should have done this at the beginning. There is a typographical error on page 8 in the section in bold: the word 'ensue' should be 'ensure'—it is a minor thing. I also want to table a list of commitments. I realise we have not attached this to our submission, and it may be useful for committee members who do not have it yet. It is the schedule of the commitments Australia has already made over the GATS rounds in these areas and, I think, other areas as well. It shows what commitments we have, particularly in the telecoms area.

CHAIR—Thank you.

Mr Baulk—I will do my do best to decipher this in order to answer your question about the international comparisons table, Chair. The source was the Universal Postal Union's annual report. It attempts to show the postage rates within the countries listed on the left-hand side. It then translates that into Australian currency terms, so you can then get some comparisons between the rate as it was then—it was 45c at that time; obviously it is now 50c—and rates within the particular countries; that is, the rate within a local currency. In our submission, we said that, with the exception of two or three countries—Spain was one; Mexico may have been another; I think the US was another—Australia Post's postage rate is far lower than that in various other countries. We also tried to make the point in our submission that, when you look at the size of this country and the complexities of the network, this is quite an achievement on the part of Australia Post to maintain that lower rate of postage for all Australians vis-a-vis some of those other countries, which are geographically much smaller. I have done my best to explain it in simple terms.

CHAIR—That is clear: we are cheaper than everyone, except Hungary, Mexico, New Zealand, Spain and the United States.

Mr Baulk—Yes. Sorry, I omitted New Zealand.

Ms Eason—If you look at those numbers, we will still stay pretty much in the same position, even with the rise to 50c.

CHAIR—No doubt this is to illustrate how efficient Australia Post is. I hope the Treasurer does not see this table ahead of Tuesday!

Mr Baulk—We would hope so as well, Chair.

Senator RIDGEWAY—On page 5 of your submission, two things caught my attention: the question of transparency in the process that the federal government, through DFAT, have held to date and what you call the minimum measures that need to be observed. Could you define what you mean by minimum measures to ensure 'a more democratic, open and transparent WTO negotiations process', the free trade agreement talks with the United States and so on?

Ms Eason—In that particular paragraph we have given suggestions as to what we would like to see as part of the process. I think everybody shares the view that we would like to actually see the offers and requests—at a minimum. It is very hard to have a discussion without knowing precisely what you are discussing. We seem to be shadow-boxing a lot of the time. The mechanisms we have suggested for public discussion, apart from full parliamentary scrutiny of all GATS discussions—that is, the content of those negotiations being fully available to the parliament—are cross-country information sessions and hearings on the GATS, which would allow community organisations and agencies that have an interest in particular sectors or a broad interest to participate in debate on these matters, and the creation of a public information bureau with responsibility for research and education relating to trade issues. Our thinking in this area is still in the early stages, but I think it is in line with a very broad feeling in the community that there need to be both formal and informal forums where these matters can be debated. While we do not have those, people have very few ways of engaging in this process, other than showing their alienation from it in the ways that we have seen around the world to date.

Senator RIDGEWAY—When you talk about a public information bureau—a centre of sorts—what do you mean by that? What were the thought processes behind putting some sort of structure in place? Where would it be located and what would it do exactly?

Ms Eason—Coming from the trade union sector, we have a kind of nostalgic fondness for tripartite structures. An agency that involved the union movement, representing workers in the government and business sectors—we also have to think about community sector involvement, whether it is through NGOs or other agencies—and that was funded by government and staffed in a way that allowed those functions of calling meetings and disseminating information would be a model that we would find attractive.

Mr Baulk—Could I add to that. It would be very remiss of me to ignore our New Zealand colleagues. Yesterday I was talking to a union from New Zealand at a conference, and they indicated that they had had assurances from the New Zealand government that, if there were to

be any changes, there certainly would be consultation with that union. We have found it a very difficult process so far in obtaining information. This has been our first real opportunity to have input into the process, but after this we are not really sure what opportunities we have to continue the debate on this particular issue.

Senator RIDGEWAY—There is another issue, on the same page again of your submission, that flows out of the ideas that you put forward. Because of the range of existing international standards, you suggest conducting community audits. Have Union Network International, for example, had an opportunity to put those ideas to bodies like the WTO? If so, what sort of response did they get?

I think it is in many respects a two-tiered process, dealing with domestic application of those types of standards and also what ought to happen at an international level through organisations such as the WTO. But I would be interested to hear your comments on this. It is an interesting idea to look at community audits, but how far has that gone in reality?

Mr Baulk—UNI have actually taken the issue up with the WTO. Whilst they have received some favourable responses, it still does not go far enough to assure them about due process and about the process of having that sort of transparency. So, even at that level, we are still having some difficulties in the process.

Ms Eason—I think it is very much, as Brian says, a matter of knocking at the door, as far as the global union federations go, in their discussions with the WTO. Indeed, it is still a matter of knocking at the door with those unions in an attempt to get a dialogue with the United Nations agencies that have responsibilities in some of these particular areas. So I think it is very early days as far as that movement goes. Indeed, the whole creation of the global union federations on the scale that they now operate is very much a response to the way the world economy has changed in last decade or so. There is a very clear focus on engaging with those agencies and trying to partner with them in some ways in trying to bring some pressure to bear on the WTO processes. But I think it is really just at the stage of proposing it, to be frank.

Senator RIDGEWAY—I have a final question for Ms McGrath-Kerr. On page 2 of your submission, you talk about the NAFTA agreement and some of the implications there, particularly in relation to organisations or individuals in similar circumstances to members of your association. You mentioned two cases there and you say that the actions have had material adverse consequences. Are you able to tell us any more about what those adverse consequences have been?

Ms McGrath-Kerr—I will refer that to Mr Talbot, if I may.

Mr Talbot—The two examples we used were in the context of the North America Free Trade Agreement, in particular between Canada and the US. The example offered was in the timber industry. Despite the free trade agreement between those two countries, the Americans felt that the Canadian government were subsidising their timber industry and providing unfair competition to the US timber industry. Despite the Canadian government refuting that, the Americans applied a 29 per cent tariff to the timber industry exporting timber into the United States. I happened to be in Canada at the time this was going on and my knowledge comes mostly from the newspaper reports at that stage. I guess our point is that, despite the existence of

these agreements, it does not necessarily mean that there is equality in the relationship. In this case, the Americans, looking to protect their own industry, have moved to penalise a member of their free trade agreement, notwithstanding denials by the Canadian government about subsidising their industry. The consequences described in the newspaper at the time were that two or three of the timber mills and many thousands of jobs were lost to Canadian commerce.

The other example was that a number of the agreements created a lot of legalistic elements between the two countries. In one example—again, our knowledge is from newspaper reports at the time—the giant American parcel company UPS sued Canada Post because they felt they were in breach of the free trade agreement, notwithstanding that the Canadian postal administration was operating within the context of Canadian legislation and within the constitution of Canada. So with that example we are raising a concern that, notwithstanding the essence of a free trade agreement, if one bargaining partner has more power than another, it can create quite a lot of difficulties and perhaps undermine the concepts that were originally contained in the free trade agreement.

Senator HARRIS—Firstly, to the CEPU: on page 7 of your submission under the heading 'EU requests of Australia Expose WTO GATS Threat' you say:

We consider that this has the potential to lead to the radical reduction or abolition of the reserved service component of Australia Post's market.

Could you expand on that for the committee and give us a better understanding of the reserved service component and how you feel GATS would possibly impact on that.

Mr Baulk—It is best to outline first that approximately 50 per cent of Australia Post business is in the reserved area. We are talking about the letter, which is very much a mature product. There has been, both in Australia and overseas, a flattening of growth within that product. In some overseas countries it has even gone into negative growth. Australia Post's views in relation to its flattening of growth relate to some of the heavy growth areas that it has experienced in financial areas, particularly credit cards, which are competing with other products at this point in time. At the same time they are expecting some drop in growth and even a decline because of product substitution. That is yet to hit Australia.

The reserved service is a mature product. That product is provided to all Australians under what is known as universal service, which provides that any person can post a letter from within this country to anywhere in this country for the same price. That is obviously applicable to nearly every country in the world. If the market was opened up, any competitors would not be interested in servicing the whole of Australia. There are the usual arguments about cream skimming, of course. They would only be interested in the major trunk routes—which is obviously the eastern seaboard—which under the existing regime of Australia Post is a product that provides a profit that cross-subsidises those areas where there are enormous costs in delivery. I am working off the top of my head, but figures have been quoted before in various submissions to inquiries that a letter going from Melbourne to Darwin can cost as much as $2.40 for its processing, transportation and ultimate delivery. Clearly, a fairly significant cross-subsidy applies in that particular instance. There are obviously various other areas—rural areas particularly—where there is a significantly high cost and they have the benefit of a letter being received or sent by them at the price of 50c.

We have raised this issue on numerous occasions, whether it be in relation to this or other inquiries, that clearly competitors are only going to go, as I said before, for the major trunk routes and cream skim. That really attacks the issue of universal service. Australia Post, I would imagine, in order to make sure it can compete with that, would have to make a commercial decision about its rates. Therefore the universal service that has been the hallmark of postal services in this country and the world would be severely under attack. That has major implications for jobs and for the revenue of Australia Post. We see that as being a fundamental threat to a very important communication system for Australia.

Senator HARRIS—Would it be possible for you to provide to the committee some of the figures as to the actual real cost of postage? You gave the Darwin example. If there are other similar figures available, providing them would assist the committee. Under 'Telecommunications issues' in the second last paragraph of the same page, you say:

> The CEPU recognises that these processes may open up commercial opportunities for members of the Australian telecommunications industry. We are concerned, however, that they also involve threats to key elements of domestic public policy.

Would you expand on what the union sees as those threats? To what specific public policies are you referring?

Mr Baulk—Before Ms Eason replies, as to the second part can I say that we will endeavour to find that information for you and the committee. May I make one other point. I raised '$2.40' but it may not be precisely that. I do not want it to be construed that I have misled this committee at all.

Senator HARRIS—Not at all.

CHAIR—I would like to raise a couple of questions which are part of the public debate on these matters. I raise them to get your response to them for the record of this inquiry. Australia Post, formerly the Postmaster-General's office, is one of the oldest departments of the Commonwealth. I think it is one of the portfolios that the founding elders of the Australian Constitution regarded that the Commonwealth should provide as a service to the community, so it kicked off from day one as a Commonwealth function. Over the years successive governments in different ways have not moved to privatise Australia Post, as has been the case with Telstra. But what has happened is that they have opened up areas of activity of Australia Post for private sector competition and, under competition law, have applied the principle of competitive neutrality, meaning that you can compete with private sector providers but you are to compete on the same terms as they compete and not use the resources of your organisation to cross-subsidise activities where you are competing and therefore drive them out of the market. The theory behind those moves has been that the Australian community gets a more competitive, varied and cost-effective postal service. With the efficiency of communications being a vital element of infrastructure in a modern, efficient society, the cheaper, more efficient and readily available it is the easier it is for the wheels of society and industry to turn.

What is your view, as organisations in the industry, as to the effectiveness of those changes? Have they gone too far? Have they not gone far enough? Are they about right? Did you welcome them but now have a different view about them? I would not mind having a view from you about

that issue, because what is implied here is further competition by foreign providers in the Australian market. If the Australian government were to accede to the GATS protocols on post and agree to the EU proposal, for example, that would potentially open the market for more foreign providers to compete. So, for the record, what is your view on those changes? Have they worked positively or negatively or are they about right?

Mr Baulk—Chair, can I just make sure I have got this clear: you mean changes to other products that Australia Post has? Is that what you referring to?

CHAIR—Yes.

Mr Baulk—There was a second part to the question Senator Harris asked. Do you want me to answer that first?

CHAIR—I did not mean to cut across Senator Harris's question; if there are outstanding elements to answering that, please complete them.

Mr Baulk—Perhaps I can get Ms Eason to answer Senator Harris and then I will come back to your question.

CHAIR—Right.

Ms Eason—Senator Harris, the most obvious threat that we are aware of is the threat to the foreign ownership restrictions on Telstra. We note that the government has not addressed that in the initial offer, but it sits there and there is no doubt that, both from the EU and the US points of view, those restrictions would be seen as problematic. From reading some of the material that comes out of the US Trade Representative's office, I would say that residual public ownership of Telstra is also something that is not viewed favourably—any involvement in the sector is not viewed favourably by the US. So I think ultimately these things will come under pressure in these further rounds of negotiations. Indeed, the US in particular favours the least level of regulation and public sector involvement in these new areas of telecommunications policy, particularly the Internet—which is an area that we have discussed in relation to payments—and also e-commerce.

Very broadly, that free market thrust that we see coming very strongly out of the US in this area is a fundamental kind of challenge to the ability of national governments to regulate in the public interest. It could even go to the question—in the telecoms area, it is an arcane question—of interconnection prices, for instance: the amount that a competitor might pay to have access to the national network. At present, interconnection prices are not part of GATS except in a very broad way. There is a kind of provision in the regulatory reference paper attached to the basic telecommunications agreement that those will be cost oriented or cost based, but frankly that is very broad.

Senator HARRIS—You have raised the issue that Australia is a net payer: we pay far more for interconnecting fees, particularly into the undeveloped countries, than we receive in fees.

Ms Eason—Yes, I believe we are a net payer. That is in settlement rates. They are related but not exactly the same. In the settlement rate area, it is the underdeveloped countries, or the

developing countries, that have the most to lose. Our position in Australia is an intermediate one in these negotiations: we stand to lose in negotiations with more powerful countries and we stand to deal severe blows to less developed countries if we follow our self-interest in a narrow away.

Senator HARRIS—Thank you.

Mr Baulk—I will pick up on your question now, Chair. At Australia Post, particularly since it was made a corporation, there has been a great emphasis—it is not up to me to speak for Australia Post, but this is my understanding—on being particularly vigilant about making sure that their products are transparent with regard to costs. Therefore when any questions are raised, whether at Senate estimates or other inquiries—where a number of competitors have raised this issue about cross-subsidising from the reserved service to those products in the competitive area—I think Australia Post has made sure that that does not occur. Australia Post is expanding quite significantly in that area and I am sure if that transparency was not there the relevant minister or the government of the day would be raising some questions with Australia Post.

To pick up the other part of that question, we had been particularly keen to make sure Australia Post is allowed to be out in those competitive areas on a neutral basis. I say that because, I suppose, we took the view back in 1989 when we supported Australia Post becoming a corporation that it provided opportunities and freedoms to Australia Post which it did not have before to engage in other services. We saw that the market was going to expand.

If I may just give an example in respect of that, last year I was invited to address the 63rd Biennial Convention of the National Association of Letter Carriers in America, and in America they have an enormous dilemma in that they have a network that they have to service each day, and that network is actually growing by something like 15,000 new delivery points each day. The analogy they use is that each year America's delivery points grow by the size of the city of Chicago. At the same time, the main product they have, which is the letter, is in decline; therefore, revenues are in decline. Because of restrictions placed on them by congress, they have not been able to go into new areas at all. So there is a fundamental dilemma that they are experiencing now: they have to service that network, which is expanding at a huge rate, with a product that is declining.

With Australia Post's incorporation, which we have fully supported, we recognise—and, as I said before, the reserved service is a mature product—that it is important that Australia Post can get into other areas and compete with the private sector on equal terms. From our point of view, that will preserve jobs in the industry overall. We are quite open and frank about that.

Mr Talbot—I would like to add a couple of points, because I think that is an important question. There are the other benchmarks that Australia Post is assessed against. We have talked previously about the standard rate of postage and how it compares favourably with the rate in most other countries. There are two or three other elements, which are international benchmarks. One is the quality of the service offered in the reserved area. That comes in two parts: (1) the standard of the promise and (2) the actual achievement of the promise. By 'promise' I mean the promise to the letter poster that it is going to be delivered within a certain period of time. Australia has very high standards in that regard. Most mail is delivered the following business day, whereas in other parts of the world the promise is less onerous.

The second element is how successfully they meet that promise, and Australia Post meets that promise, in the latest recording, around 96 to 97 per cent on time with up to 99 per cent of it on the very next day. That is an international benchmark which goes to the efficiency of Australia Post, which is a reflection of the changes that have occurred in the infrastructure of that industry.

The third element is the percentage return on its assets or percentage return on its turnover. Again on a commercial benchmark, that ranks very well internationally and even against other commercial organisations within Australia. I think Australia Post's profit was in the order of $360 million last year compared with, say, the British postal service, which is reportedly losing £1 million a day—and they have a very open and competitive process.

The post office agents, along with the union and Australia Post, have embraced the reality of change—both the economic and environmental changes that are going to confront us—and have moved to bring down the barriers and improve the proficiency and productivity of the organisation over the last 10 years. The fact that it has been able to keep its price pegged for the basic service for 10 or 11 years is another testament to that.

Our concern, given that good work, is that if the government takes the choice of allowing foreign competition in so that all but the last vestiges of the reserve services are open to competition—that is, so that Australia Post is open to competition—and that competition impacts upon the reserve services, it will do so only on the profitable elements of those reserve services. That will seriously undermine the basic economics that Australia Post operates on. It is largely a large-scale operation with very marginal pricing, and if you interfere with the scale of operations then you can move an organisation from being a profitable one to a non-profitable one with only minor changes. That in turn is going to have consequences for the service to the community, the investment that the contracting part of the business has made and, of course, the employees' opportunities for work.

CHAIR—Is your concern, in a nutshell, that if Australia Post is pushed out of areas where it earns a quid—thus keeping the organisation profitable, efficient and cost sensitive—the ability of the organisation to deliver to regional Australia and across the board will be degraded?

Mr Talbot—Yes. We are fairly certain that is exactly what is going to happen.

Senator RIDGEWAY—I do not know whether you can speak for Australia Post, but doesn't that mean that Australia Post is at a standstill, particularly given that, whilst you have had 10 or 11 years of postage prices being static, from your own submission there is an apparent decline in the volume of business? What does that mean for the future of Australia Post? Surely there are going to be other additional pressures?

Mr Talbot—Yes. I cannot speak for Australia Post, but I can make observations about their performance. Certainly, for their main, core business—in mail and parcels—and for factors outside the elements of other industry competition—electronic and digital forms of communication and so on—there has been a flattening of growth. For many of those years, there has been between three and five per cent growth. Now we are starting to see either neutral growth or, in some cases, negative growth. They are the pressures that will apply to Australia Post. Currently, they are trying to move into other revenue-producing streams which come out of the competitive sector, such as billpay and the agency business that they do on behalf of other

organisations, and exploit the network that they have. They are using the core business as their fundamental rationale but looking to provide value added, or add-on, services that are going to continue to attract customers and provide a profit for their operations. Those sorts of pressures alone, outside of the foreign competition, are going to keep them very much on their toes if they are to survive into the future.

Senator RIDGEWAY—I imagine, if there are limited opportunities domestically, that Australia Post must be seriously contemplating offshore investments? If so, in what form? If they do not do that, then there are possible ramifications as well for you. So it is almost a case of 'damned if you do and damned if you don't'.

Mr Talbot—That is true. Again, I cannot speak for them and they must make their own commercial judgments about taking themselves offshore and about whether this process could facilitate that. But so far that has not been a commercial opportunity that they have seen. Although that sounds like an attractive proposition, let me give you an example from the American scene. Despite the USPS being a gargantuan operation, they say that they have something like 27 foreign postal operations in the United States. My knowledge of this is not very recent, but the last time I looked at that none of them were making a profit in the United States. So the opportunity to go offshore sounds attractive, but there are great barriers to getting a foothold in those places that have nothing to do with the trade arrangements but just with the commercial aspects associated with that. Our observation is that Australia Post has mainly gone offshore at the invitation of foreign countries in order to assist or to provide some services at a profit.

CHAIR—I have one other question, which is really directed to the union. Sometimes the analogy is made that the WTO is a bit like the conciliation part of the old Conciliation and Arbitration Commission, in that it provides a forum for countries to come and negotiate agreements between themselves. When they do agree, it registers that agreement as the agreement and, if there is a dispute between countries as to whether the agreement is being adhered to, it provides a mechanism for that dispute to be settled and for the outcome of that settlement to be binding on the parties. Therefore, attacks upon the WTO are attacks upon, if you like, the forum in which the agreements are made, not upon the people responsible for making the agreements. That is the analogy.

What is also argued is that, in the modern day, many unions are multinationals. Your organisation is part of an international group of postal unions. From the leaked EU bid, we know that the EU is making claims on—or requests of—postal services in Australia. Have you taken this up with your EU union counterparts to lobby their governments to back off? At the end of the day, it is the Australian government dealing with the EU in that type of negotiation that will decide what the outcome of this might be.

Mr Baulk—I will pick up the latter point if I may; I do not know if you want to deal with the former.

CHAIR—The former was just to put the question in context.

Mr Baulk—Perhaps I need to preface this by saying that our international body is a new body. It is a merger of four other internationals that have only recently come together under a new

structure, which is probably different to what those structures were before. Having said that, there is a lot more emphasis on particular sectors—whether it be postal or telecommunications or other areas that are international. In some respects there is some infancy in relation to relationships between the unions—like our relationship with many of the unions that make up the European Union—but nevertheless there is a strong emphasis by the international body, UNI, on encouraging unions to take up these matters in their own respective countries.

There are other sorts of developments that are going on which do not go exactly to GATS, but which do have a bit of a relationship. The international body is actually encouraging and trying to reach agreements with multinationals with respect to those multinationals recognising minimum labour standards in the countries they may operate in. The best example of that is what is known as the Telefonica agreement. Telefonica is a Spanish telecommunications company and, whilst the negotiations initially started off in relation to Spain, they did expand out at the end of the day. An agreement was finally struck in which Telefonica did recognise that if it were going to operate outside, in other countries, it would recognise minimum labour standards as well as other ILO conventions. That has been put forward—both Telefonica and the UNI were signatories to that and there was a fair amount of media comment about that.

Other agreements are being sought in relation to that so that there is an expectation that these multinationals will act responsibly in any country. In a very longwinded way, I suppose UNI is trying to facilitate and to get greater cohesion of the unions at the international level so that these issues can be not just aired within countries that may have a bit of enthusiasm for putting these forward to their respective governments, but so that at the same time some other countries will facilitate that as well. Whilst your observations are correct, it is very much early days—in the infancy, I suppose—in respect to this. Nevertheless, a lot of interest has been generated by GATS. We know our Canadian sister union has been very forthright in this. UNI has put out a document to explain the GATS process as best it possibly can, as well as encourage the unions to take up these matters with their respective governments.

Ms Eason—Having thought about your comments, I think that in this whole process there is a danger of focusing on the WTO as an institution and not looking at the broader processes that are flowing through it. When you look at those processes—that is, the struggle over trade globally—you perhaps get a clearer perspective of what GATS and apparently the subsidiary bilateral agreements are about. Increasingly, those processes need to be looked at as a whole. It is instructive to look at the US-Chile agreement and the US-Singapore agreement, and then to think about what that means for our agreement. Clearly, the United States has a policy of using these bilateral agreements as a way of pushing certain agendas. The weaker the partner in the negotiation, the more they will get which will flow through.

We should not be viewing those bilateral negotiations as somehow separate from the GATS process. They are part of a broader series of agendas and processes which are being put in motion globally. You can stand back from one section of the process and look at a series of processes whereby nations who have the capacity to do so will use the GATS framework and the WTO process up to a point. They will use a bilateral process where they can get a better result, and they will be unilateralist where they can get that result in relation to Internet regulation. The United States clearly say that they do not want a bar of it. They refuse to have it encompassed in GATS and they do not want it encompassed in the bilateral agreements either. As we raised the question in our introduction, what can force them to do so?

Senator HARRIS—For expediency, I have a brief question for Ms McGrath-Kerr. What is being aired is the possibility of downward pressure on your members' abilities to be viable if changes do come through. I am aware that there are minimum transactions that a post office must contract to on an annual basis to get a terminal in their post office. Am I correct that that is 10,000 transactions per annum?

Ms McGrath-Kerr—Yes.

Senator HARRIS—Then there is a disparity between your post office members and what I understand the government is requiring as a level for—forgive me if I have the terminology wrong—the new transaction centres that they are putting throughout Australia. I believe that that is either 7,000 or even lower.

Ms McGrath-Kerr—Yes.

Senator HARRIS—How would you see any changes coming through the GATS process adversely affecting your members because of the disparity between some of them requiring 10,000 transactions and having to pay a fee if they do not reach it?

Ms McGrath-Kerr—Under the rural transaction centre program, we have had extensive talks with the department and the relevant minister and we have included Australia Post in those discussions. As you say, rural transaction centres have now been extended to manual, rural licensed post offices where Australia Post technology, which is known as EPOS—electronic point of sale—does not currently exist. The number of transactions to access EPOS under RTS, following the provision of a business plan by the licensee, has now dropped to 5,000 per annum. As you rightly say, there is a shortfall fee payable by those people to access it until such time as they reach 10,000 transactions, if indeed they ever reach 10,000 transactions. We have recently done a survey on this. We have found that the transaction levels increase substantially once the electronic system is in place. That is very heartening; it reduces the number of people who are likely to pay the shortfall fee. However, that particular instance is in relation to banking, third party agency billpay and so on. It is not to do with mail. Unless my colleague corrects me, I do not believe that the GATS issue would impact on third party agency transactions across the counter.

Mr Talbot—That is not our understanding.

Ms McGrath-Kerr—Mr Baulk, would you agree that there would not be any impact?

Mr Baulk—That is our understanding as well.

Senator HARRIS—Thank you. That clarification is good for the committee, because it gives us one of the issues that any downward pressure could possibly have on our postal licensees.

Ms McGrath-Kerr—We must not forget, though, that mail is the core business. Once mail is damaged, foot traffic is damaged and the rest of the business could be affected.

Mr Baulk—If you would like it, I have a copy of a document from UNI, which I referred to.

CHAIR—Thank you all for coming along this morning and for providing us with a very detailed and fulsome submission.

[10.12 a.m.]

OXLEY, Mr Alan, Director, AUSTA

CHAIR—Welcome. Thank you for providing the comprehensive submission and attachments. You are a veteran of these sorts of proceedings, so I do not need to cue you in the way that a newcomer would be cued.

Mr Oxley—Thank you. It is a pleasure to be here. We have put in a detailed submission. I want to make four broad points, then leave it to questions from committee members. AUSTA has been a little frustrated in this process. We represent most businesses which have an interest in the Australia-US economic relationship. Frankly, we deeply believe that the primary advantage of a free trade agreement is the capacity to make the Australian economy more competitive and to create a better environment for Australian business to be able to compete in a global economy in this century.

When I say we are a little frustrated, we know that it is a very far-sighted thing. Not long after the group first met, we had a roundtable about what people wanted out of the free trade agreement. Evidently some of our members have some express and specific interests. BHP Steel is here and it will tell you what its specific interests are. The group was started by Southcorp. It had a specific interest. It was very concerned about threats of retaliation against wine exports during the Howe Leather dispute. It saw a free trade agreement as an opportunity to secure its access to what it considers to be a major growing market.

Wine exports to the US in the last five years have risen from $70 million to $500 million. But the group also, after identifying a specific interest, collectively said, 'We think it's vital to have an agreement like this with the US because our perception is that the way the world economy has developed, the way it's being moved into the information age and the way it's the US economy which is leading this is that the reference points for competitiveness in the future are the reference points used in American business.'

That is the reality of the world economy. The US economy is so large that, no matter what area of business you pick, there will be an American corporation or multinational with US legs which is actually the trendsetter and doing the market links. We have to be pretty realistic about the Australian economy and the capacity of Australian business to participate. We have some companies that are world-class players—many that are not—but the opportunities for doing business depend upon the capacity to plug into global systems. That often means working alongside or becoming part of some sort of global system and, by and large, they are going to be increasingly rooted in US values.

We still think that is the greatest advantage of this agreement. It is a long-sighted view. This is a 50-year view. We think the United States today should be seen in the way we looked at Britain at the end of the 18th century when it first industrialised and we saw the wave of industrialisation that followed. What we are seeing in the US economy now is the beginning of the information age. We therefore think that harnessing Australian business to that equips Australian business to be competitive not just in the US market in the future but in all parts of

world economy. So it is big picture. Regrettably, the media do not think it is very important. They prefer to talk about pharmaceutical benefits and agriculture—local content; and I will talk about some of that. But we want to stress this point because we think it is the ultimate and most important goal.

Secondly, I get asked lots of questions when talking to people in the media about what is the downside. We know there is a traditional view about trade agreements. Free traders always say that you do not get your gain unless there is some pain to competitiveness. That is the consequence of cutting your tariffs and seeing some business made more competitive and redistribution of resources. That model does not work in this case, because the reality is that the Australian economy is actually more open than the US economy. The only real difference between the two is higher protection of agriculture in the US. So if there is any pain in this agreement, the pain is on the US end.

I repeat the point simply: our average tariffs are about three per cent. We have an almost completely open economy. It is more open than it has ever been. The things that the Americans will ask for from us—and we will talk about some of those—are things that are not in fact going to be particularly painful in the broad order of events; in fact, I will argue that they are not going to be painful at all. It is very important to not presume this is like an ordinary free trade agreement, where you are talking about massive cuts in tariffs; we are not. Frankly, if there is an intellectual argument about having a free trade agreement it is 'why have one if the tariffs are so low?' We think it is important because the world economy is different now. The problem with calling this agreement a 'free trade agreement' is that it makes us think about tariffs. But in this open economy that we have now, tariffs world wide are pretty low—about 80 per cent of world trade now is bound by tariffs of between zero and five per cent. Our own economy is part of that system now.

Investment in some instances is more important than trade. In the last 10 years, two-way investment between Australia and the US in dollar terms has probably been as valuable as exports. There has been a big rise in Australian investment into the US market in the last 10 years. If you wonder why that is, just think about the super funds. They have got to invest somewhere. They have got to get world-class returns so they can pay Australians at the best superannuation levels. We now think Australian investment in the US market is regarded as being more than France's, more than Mexico's—about seventh or eighth. That is quite a big change.

The US has become the biggest foreign investor in Australia. For many companies, whether they trade or invest is a complete toss-up. It is a business choice. That is where we are in the global economy. For some of our bigger companies to succeed, they have got to have the facility to invest or trade—one or the other. That is what modern free trade agreements are about. One of our members said that we should perhaps call it a 'free trade and investment agreement'. It is understood that investment is a key part of this, and it is a key part of our future success.

The third point I want to make is that in the last year the environment has changed dramatically. We have got three agricultural groups as members of our group. One is the Australian Meat Council, which represents meat exporters. You would be aware that we export about $1½ billion to $2 billion worth of beef, mainly from the Queensland industry. The biggest exporter is Australian Meat Holdings, which is one of the biggest processors in the Southern

Hemisphere. That exports about $400 million worth of meat a year from a plant outside Brisbane. The dairy industry is a member of our group. They too consider there to be significant benefits in this agreement.

When we began this process I was always confident that we would get some extra access to the US market. That was not the popular view. Most of the old hands, who have been around the trade for a long time, were saying, 'What's the point?' In looking at the media, one of the most effective arguments, which seems to have resonated, is: 'We'll never get anything from the Americans in agriculture; what's the point?' I hope you do not mind me saying this—I live in Melbourne—but that is a very Sydney point of view. I seem to hear it more up there than anywhere else—'Why would you bother?'

We all know what has happened in the 18 months since September 11. Do not misunderstand me—I am not saying that going into the war was justified in any way in respect of the free trade agreement. But there is a stock of credit now for Australia in Washington that we had never seen before and our agricultural industries know it. I do not know if the meat, dairy or sugar industries are coming to see you. If they are not, I might suggest that you ask them to come in, because their attitude has done a flip in the last six months. It is not being talked about too loudly, but our farm industries now consider that, for the first time probably ever, we have a serious chance of getting very significant access to the US markets. These are serious dollar numbers.

I did a survey for the meat industry recently—I was in Washington six weeks ago—and the body language and the mood is different. The President and the Prime Minister have now accelerated the timetable for this—which could be a problem for the government, I think, in terms of times for consultation—and they said they want to try and finish this by the end of the year. The President said he wants to get it into congress next year. Your chairman knows more about trade than most people in this country. If you said, 'What is the point of putting a trade agreement into the congress in a presidential election year?', everybody would have said that there was no point. But I think that one thing you cannot say of George Bush is that he does not know his politics. The judgment must be there. They have sufficient confidence in the level of credit that exists for Australia that he will be able to carry something like that through the congress early next year. So it is a changed circumstance.

It is one of those things that significantly alter the landscape; it alters the dynamics of the politics of the negotiation. It is no secret that Australia asked for this agreement. If you negotiate something with anybody and you say, 'I want something,' they will say, 'Right, we will go along with that, but if you want something from me I have to get it back from you—otherwise, why should I bother?' The psychology of the negotiation was that Australia was always going to be a bit behind the eight ball. What has happened now is that the political credit that exists makes it actually easier, in a sense, for the United States administration to negotiate this. When its farmers say, 'Why should we bother to do this?' the answer is now going to be: 'Because Australia is one of our most loyal allies.' So the politics of this equation are actually quite different now. I am not saying that this is going to be that much easier—everything in the United States is difficult and the political process between the administration and congress is very random. But there is every sign that this administration has actually decided to load up some political credit. I think how well we handle those negotiations will be in direct relation to how good a result we get.

Finally, I am happy to go through each of the downside issues, such as pharmaceutical benefits, with local content. Just let me say that, generally, I believe the downside has been significantly overstated. I do not see much sign that what the Americans will be asking for in these areas is going to be an issue or will make that much difference to Australian interests. I would just leave that broad conclusion, but I am happy to talk about that, if you are interested. I might leave it at that.

CHAIR—Thank you, Mr Oxley. You have had an extensive experience in trade. You were Australia's ambassador to the GATT—I think it was in the early 1980s—and you have been in private consultancy on these matters for some time. In particular, you have been interested in this issue for some time. You now head up AUSTA. Are you in a position to make any predictions about what the outcome of the final package will look like?

Mr Oxley—These would be guesses based on how I would read the various positions; they are not based on anything that anybody in government has said. I remember that, years ago, when I was in Geneva representing Australia at the GATT, I asked my American colleague one day how a particular issue was going to run through the congress. It was a very nasty trade problem for the administration and there were threats that congress was going to tack it onto something and it would actually have had quite serious consequences. I said to him, 'How do you expect this will go?' He said, 'I haven't got any idea.' I said: 'How could you have no idea? You must know. In our parliament, you have a rough idea about what the position would be with the line-up of the parties and the attitudes of players, and you know what the parameters are.' He kept saying, 'It's not possible to tell.' I am a slow learner at times; finally, I did come to understand that the US political process does have this wild-card, random element in it. At the end of the day, the final deal that is done possibly depends on what goes on in the previous two days before things are finalised. I do not believe that, in the US, there is any plan in anybody's head about where they think this will be. They always tend to leave things until they have to think about them.

Having said that, I think we are going to get a surprising result on agriculture. I would not be surprised if we might get something like a commitment close to full access over a long period. That is certainly the case with beef. There is scope for us to get bigger access on dairy. I do not think we will get full access on dairy because we are too far behind the eight ball. We only export about $80 million a year into that market, but I see the New Zealanders export about $700 million—they have just been working the market longer. The reality here is that the cost of letting our producers into that market is actually quite small. Our beef producers currently only take about three per cent of the market. If that were doubled, and it would take our industry a long time to get up to that level, that is only six per cent of the US market. If you have got an administration that want to back back the US industry, saying 'Behave yourself'—and we have had intimations that that is actually what they have said to them—and argue for something like that, it could be done relatively painlessly. The access could be progressive and slow. And our beef industry is not in the position to do any rapid increases anyway.

I saw that the National Farmers Federation were critical of the fact that, in the Chile agreement, the Chileans got a commitment to removal of barriers on access, which, I must be honest, is much less significant than in our case. Most of the Chilean problems about access to the US market are quarantine issues, I think, not actually trade barriers. The Chileans for the commitment to remove the trade barriers—which is a lot cheaper for the Americans than

opening up for us in that sort of way—over 12 years when the normal span with the agreement was 10. The NFF said, 'That would be unacceptable to us.' I think if the NFF got a promise of full access over a 15- to 17-year period they would be over the moon, because the benefit for us would be quite significant.

The sugar industry, having now been to Washington, believe they can get some extra access as well. That is quite a change because those guys had a pretty hard time. Sugar has been punished more than any other sector in the US and they actually lost access. What would be the return for that? I believe we would be advised to have fewer restrictions on foreign investment. Our group supports that. Just how much and what is a moot point, but, currently, every foreign investment over $10 million in this country has to be vetted by the Treasury. It is a pretty paltry sum, frankly, if you consider what is involved. We, as a group, are looking at what we would like, but if you talk to people in business you hear that it is a pain in the neck for business to have to go through the hoops of sitting down with Treasury and going through every step with every investment. The reality, at the end of the day, is that we have quite an open investment market anyway. Probably you would need to have reserved some sort of national interest right on big grounds, perhaps even something like a Woodside reservation. In terms of where the criticism would normally come from, basically I think the objection to more automatic rights of foreign investment for Australians would be more political than economic. But if we could see some decent access on agriculture so that people could say, 'Well, maybe you do not like it, but if we're going to get some extra agricultural access in return, don't you think it's a fair deal?' I would think at the end of the day people would probably say, 'Well, yes.'

On the investment side, it is very important to stress the benefits for us. What you would be looking for in investment is something in the agreement which promises foreign investors the same legal rights as the domestic investor. It is called national treatment. This would be a valuable right, we think, for Australian business in the US. The main problem with foreign investment is usually not the federal government; it is usually county officials, city officials and state governments that come along and say: 'How about this? How about that?' This would give our investors in the US market a legal right to say, 'No, you can't ask us to do something that you can't ask of the American investor.' We are not used to thinking about the investment issue in these terms. Normally we think about foreign investment and the foreign money coming in here, but in this case there is something available for Australia in terms of investment out there.

In terms of other measures, I would like to hope we get agreement to much freer movement of business personnel. That is something that business wants. Oddly enough, as I am sure BHP Steel and other companies can tell you, things that we do not think rate very highly do actually matter to business. The whole process of trying to get visas for senior business executives moving back and forth is quite a time-wasting impediment to business. I think it is quite likely that we could get something better there.

In terms of services, our market is probably more open than the American market. There are probably fewer restrictions on telecommunications in our market than in their market. There are probably fewer restrictions in banking as well. I do not see that it is a big ask of us; usually countries do not ask for things that they have not got themselves. They might ask to have something looked at in terms of the Wheat Board. The Wheat Board single desk has been on the table. It is not strictly an issue that sits in there. I feel that that would not be a make or break issue. I note that there is a long-term trend to corporatise the Wheat Board and ultimately cut it

loose. At some point, if the government turns the Wheat Board into a fully independent company, it will probably slip the noose of the single desk. I cannot see how the Wheat Board can be a proper thriving business while it still depends on a government fiat like that. There may be some room for a long-term commitment there but I really do not know. I have not thought much about that.

Obviously, we would both agree to reduce tariffs to zero. They average about 3½ per cent each so that is not much. Automobiles is an interesting area. Are Holden going to address this committee?

CHAIR—They are not on our list at the moment.

Mr Oxley—They have a new interest in the US market. The MD from GM came over here and looked at the Monaro and said that there was a spot for it in the US market. They are gearing to sell that. Holden is now quite interested in selling their Maloo, their hot ute; they think there is a market for that. The tariff on the Maloo in the States is about 25 per cent. That is the higher tariff in the US market on pick-up trucks. Holden seem to believe that there is scope for them there.

Our people would push quite strongly in the interests of BHP, Southcorp and the lamb industry to see whether something can be negotiated in the agreement that reduces the capacity of American industry to get their system to harass our importers. What they are looking at is a safeguard mechanism. You might remember that the Americans triggered the safeguard mechanisms on steel recently. Several countries took them to the WTO and they were told to change the system because it does not comply. However, it exists and it is a regular device. This really is not usually in the hands of the administration in the US. Over the years the lobbyists have been quite smart in getting laws passed in congress which reduced the capacity of freedom of manoeuvre by the administration. There are automatic triggers and they are pressed and they are told that the measure has to be put in place. The safeguard mechanisms are set up for that. There are similar measures with countervailing and antidumping which are in a different class. I think people feel that that is just too hot an issue to make headway in. However, I believe our negotiators are confident and our companies are very insistent and keen that we get something there.

CHAIR—What about quarantine?

Mr Oxley—The quarantine issue has evolved somewhat. One of the mysteries about quarantine is that the Australian market is not particularly significant. The sorts of American industries that would have been interested would have been the chicken meat and pork industries. I and some of my associates not directly related to AUSTA's work have actually been told by the US industry that they do not regard the Australian market as particularly significant. Quarantine was originally run up the flag because in the view in the American meat industry was an expectation that there would be pressure to open up for some Australian meat. Their view was, 'Hell, if you're going to let more Australian meat into the US then we don't want to see any restrictions on the capacity of the US providers to get into the Australian market, even if they don't.' So quarantine has been up there. We have asked for it a bit. The quarantine administration are imperfect—that is the best way I can put it. I have thought for a long time that they have been a sitting duck for a challenge on natural justice grounds.

Senator RIDGEWAY—Is there an issue there on genetically modified crops and labelling systems?

Mr Oxley—I have not seen that. It was run up early and a lot of the civil society groups are saying that it is an issue. When the Zoellick letter, the first letter of notification to congress, went in, right at the top it had biotech related to the food issue. A couple of groups thought that meant GMOs. I was over there and I asked the American negotiators what the issue was and they were surprised to be told that it was GMOs. They do not have a GMO agenda. Somebody has jumped the gun on that one.

On the rest of quarantine, I understand our officials have been having a dialogue with the Americans—and I am sure they have told you this—to get a better understanding of processes. They also have their own list of quarantine demands of the Americans which is about as difficult for them as theirs is for us. It looks to me as though it is set up for a nil-all draw. Off the subject, I think the EU challenge on quarantine is much more serious.

CHAIR—Thank you for that overview. I really only have two questions, but there are some details in the first one that I would like to discuss. From the agricultural point of view, one of the big areas of agriculture we have traditionally looked at is the dairy industry. Other areas, which are not as big but are nonetheless quite important, are cotton and peanuts. Do you have any comment on accessing those commodity areas?

Mr Oxley—I actually do not. I have not looked at them.

CHAIR—Of course I accept your up-front qualifier and that I am inviting you to speculate, but you were saying about beef that there may be a 15- to 17-year phase-in period.

Mr Oxley—In every trade agreement in the world, the more difficult trade areas are always put on the longer time tracks. Traditionally, the two difficult areas are agriculture, and clothing and textiles. It does not matter where you look, in every bilateral agreement, in the WTO and in every regional agreement—it is the same with the ASEM free trade agreement—they say, 'We are going to remove everything over 10 years.' When you get to agriculture, you find the different time line. You find exceptions. I think that, among the various counters, Australia's negotiators have got to play with the Americans. The Americans giving us some concessions on this will be difficult, so you would obviously be expecting to find some way to make the bitter pill easier to swallow. Of course, the great instrument in trade equalisation is very slow market opening. It is quite sensible, anyway. Very few enterprises are capable of gearing up in a very short time to rapidly increase their supply. Because of the drought, even the beef industry is now going to face quite a cyclical downturn. It is going to take a while to restock the herd.

I have an associate who knows the industry quite well. This is nothing formal, but we were idly speculating about the sort of pace of pick up he thought there would be for the beef industry. It is a bit silly even speculating on these things. You are actually speculating on the weather—you can get it so badly wrong. He thought that, even if we got, say, a big opening of the market at a 10-year period, he did not think our industry would be capable of supplying that in that sort of time, given the amount of time it takes to stock up and grow. The industry's point of view is that it would need small steady steps. For us, the big negotiating deal is: can you get a long-term commitment to fully open it.

CHAIR—Accepting your observations, in agriculture that would mean we would have access to a corrupted market in the sense that US agricultural producers are heavily subsidised; our exporters are not. We would be able to get in and compete with them in the market, but they would be subsidised and we would not. That would be the case, wouldn't it?

Mr Oxley—True; but I think they are competing with them in that way now.

CHAIR—They are.

Mr Oxley—Every market is corrupted, really. They always need to have a lower cost level and so on.

CHAIR—My point, though—to make the obvious one—is that we are not talking in these negotiations of being able to remove the agricultural subsidies US farmers have that so distort their production.

Mr Oxley—I doubt it. I think the reason for that is the geopolitics. It is not correct to say that you cannot negotiate agreements not to have subsidies in a bilateral agreement. We did that with New Zealand—we agreed with New Zealand that we would not pay any subsidies to trade between the two. I think the problem for the Americans is that we are small beer when it comes to subsidies. Their big issue, as you know of course, is the community. I think they would find it all too difficult to agree. They could not do it inside their own market. How could they avoid subsidising a beef producer if Australia is competing inside the market with them? The only issue is: would that arise if the Americans opened the market to everybody? While the market is a bit closed as it is, there is probably a slightly higher price. In a fully open market the prices will come down. That is probably when the subsidies would matter a bit more. If we are talking about giving an increase in the market for Australia, with the rest of the regime pretty well staying in place, I think the competitive base would be quite strong.

CHAIR—Okay. What has, in the common debate, been cited as the value of an Australia-US free trade agreement is this figure of $4 billion, which is derived from the Centre of International Economics study and is calculated on the assumption that the markets were open on both sides and that after 10 years the value to Australia would be $4 billion. This package that you are forecasting would be valued at much less than that, wouldn't it?

Mr Oxley—I cannot answer the question, actually. I often wonder why it is that so much of our political life in Canberra devolves around econometric models. If you sit and work with an econometrician and they tell you how they put their numbers together, it is befuddling stuff. The one thing those models do not capture is dynamic factors. They are static. So most economists would agree that if they think that is the modelling number they have got, the real return is probably much larger.

CHAIR—I can perhaps share part of your cynicism about the weight that is given to econometric modelling. You have to actually look at the assumptions upon which that model is based, and some of those assumptions—I am talking conceptually now—are fairly wild on occasion. It is pretty much: rubbish in, rubbish in; or quality in, quality out. This is an area of some considerable speculation, so I share that cynical view. Nonetheless, in political debate, weight is put on these figures because they are tossed up, almost in a sloganeering way, as: 'This

is the value of it.' In the case of this particular study, which has been quoted by the Prime Minister and other ministers, it is that the market on both sides opens completely and after 10 years—and after you have spun all these wheels, based on all the assumptions—the value is $4 billion to Australia. But on what you are forecasting here—and I appreciate this is a forecast—it would be not even half that.

Mr Oxley—I think that model bravely presumed a full opening of agriculture. I must say at the time I thought, 'That is actually not particularly realistic.' I do not think it is a good idea to base public policy positions on the results of an econometric study. The debate we have had between the ACIL study, the two on that—the CIE and the Mckibbin studies—and Ross Garnaut's critique reminds me, I might say, of that old adage of having an argument about how many angels can sit on the head of a pin. I have provided you an analysis of the Garnaut critique of the numbers; and Ross seems to have stopped using it now. His strongest point is a political point—it is about relations with Asia. But the numbers, in terms of impact and so on, are actually, by his own admission, relatively small. In econometric models you never take small results as serious. The use of econometrics gives you broad trends. The day you get down to taking really small results and saying they are significant and then treating them as real is a second mistake. I must say it is unusual for a professor of economics to do that.

CHAIR—Then there is the other thing: that after 10 years how would you know whether those particular changes created that particular result, if they did? Would you care to offer us a suggestion on what you think the value of a package of the nature you have forecast would be to the Australia economy?

Mr Oxley—Honestly, no. Australian agriculture exports to the US—total exports—are about $2 billion. Beef is about one and a bit billion. Dairy is not in the game and sugar has come right back. If we got some serious additional access in those areas I do not think it is infeasible to consider a doubling of those numbers over a longer-term period, which is pretty serious stuff. But I think it is a mistake simply to focus on that. There are other trends going on with the relationship which are actually pretty important. This is why it is so difficult to make these guesses. In the last 10 years the fastest sector of our exports to the US has been manufactures. I mentioned wine: we do not usually regard wine as an agricultural product.

The prospect of getting quite significant increases in automobile returns into the US has to be there if General Motors get it right. Already we export about $400 million worth of cars. They are basically Mitsubishi Magnas that are sold into the States as Diamantes. The component part industry is now quite competitive. I do not see why, unless our manufacturers are unable to withstand a recovery of the dollar—and I do not think they are that fickle—we will not see a significant, steady increase in manufactures over time. The reason is that it is a reflection of the basic change that has occurred in our economy. We are now competitive in every sector of the world economy. This is brand new for us. It is natural therefore that we will start to see an expansion of our businesses in services and manufacturing into the markets that are open in the world's biggest market—that is, the US. The interesting contrast is Japan, where we have seen no significant increase in manufactures. There is something basically wrong with that relationship. But we have seen quite a steady rise in the US and Europe. It may even outgrow the increase in agriculture.

CHAIR—I accept your answer, but you are not prepared to forecast what you think the amount will be.

Mr Oxley—If you want a number, we will say it is double. We think it is about $8 billion in terms of the dynamic effect. If you talk to anybody in business, they say, 'It is always going to be bigger than that.'

CHAIR—That is your best guess on these changes, on this outlook, which you acknowledge is much—

Mr Oxley—No. I would not dare to suggest that I would give you a guess like that. The $4 billion was a pretty modest result and we think that it significantly underestimates the growth lift that making the private sector more competitive, through the agreement, will achieve in the Australian economy.

CHAIR—I know that view, but it is also a view which is unable to be quantified, so it is an animal-spirits view.

Mr Oxley—Yes. It is better than the other one.

CHAIR—I am not sure what the value is of either of them, to be honest, but we do get into this debate about these things. The virtues of these proposals are sold to some extent on promising the Australian community that there will be a particular value. I want to conclude this relatively quickly if I can. My next question is about the process. I do not need to go through that because you are an expert in it. There is a great deal of transparency in the United States Congress in the negotiations and final approval by the congress. In Australia we do not have any comparable degree of transparency. From the point of view of the parliament, vis-a-vis the executive, the only role the parliament has is to deal with consequential legislation, if there is any, once an agreement is completed. Do you have any views to offer us on whether, compared to the level of transparency the Americans enjoy, the Australian transparency is acceptable? Would you care to share with us any changes that you would like to see that would enable the Australian community to be better informed by being able to have greater access to what is going on?

Mr Oxley—Sorry to be tedious, but I know generally what is going on in the US but not the details. I am not even completely clear about our own processes. But I will say this: if this agreement is to be put together in the time that is given, we think it is very important that the public, the community and everybody with an interest in it is fully engaged and understands the issues. I think the fast timetable presents some real challenges. We would not advocate drifting away from the timetable. My suspicion is that the reason that the two leaders put such an ambitious timetable up is that they are probably fully aware of how ephemeral political credit is in Washington. I think they probably know that things change so quickly in the political scene there that they have only a limited amount of time before they can actually use it. Not only will that put real pressure on the negotiators to do what they have to do, because the time is exceedingly short, but if they have to get people used to changes and ideas they have actually got to put the time in. To me, the parliament is an obvious vehicle for that. I do not have any specific suggestions on how and where to do it, but we would say as a group that we think it is very

important that all those people who are involved in this and have interests be brought along and carried with it as best they can be.

CHAIR—Do you agree that it would be disastrous for the bilateral relationship if, for want of transparency, briefing, better understanding and access to information, a disagreement between the legislature and the executive led, for example—this is hypothetical—to the Senate rejecting consequential legislation arising from a free trade agreement negotiation with the US?

Mr Oxley—Yes.

CHAIR—Does it not follow, therefore, that the onus is on the executive to keep the legislature informed of the developments so that the legislature knows the implications of the changes they are being called upon to vote for?

Mr Oxley—Yes, I would agree with that—but there is a difficulty here. I know that in the US, because the congress is that much more powerful and the administration can often have its legs cut out completely from under it by not going along with the congress, there are a lot more established processes for having the congress engaged in the evolution of executive decisions. That is relatively unusual here. There is a problem in negotiations of course about the actual negotiating position. In a typical negotiation, nobody agrees to anything until everything is fixed. I would think that in this negotiation, because the agricultural issue will be so difficult, it will probably be the last thing fixed, and if you were on the other side of the fence you would not allow any concession to be taken as a given until you saw the whole package. That makes it difficult for the executive to have a discussion with the legislature about what the terms of the package are likely to be, because in a sense what has to be done is about protection. You are familiar with all this—it is the same sort of thing at the WTO. So I think that there would have to be a very good cooperative relationship between the executive and the parliament for that process to succeed.

CHAIR—And the way that is expressed in the US model, given the current trade promotion act, is through the appointment of a congressional oversight committee that has access to the developments on the American side in the negotiations. We do not have a similar structure in Australia.

Mr Oxley—As I said, I am not familiar with the details of what goes on in the congress, but I have heard such things.

Senator MARSHALL—You have raised several times some of the benefits that may come through the vehicle industry. What do you think could be the possible downsides for the vehicle industry and vehicle component industry—particularly in Victoria and South Australia, given the nature and size of the industries in those states?

Mr Oxley—I understand some of our component producers are concerned about American product coming in and competing with them, whether they are concerned about price or relationships—because in the motor industry relationships between component suppliers and the actual assemblers are very important. One thing I would say is that people sometimes presume that the 15 per cent tariff on automobiles is the same for components—it is not. The component people lost it a bit in the last negotiation on the vehicle plan and forgot to ask for a guarantee that

the government would give them a mechanism which gave them 15 per cent. They forgot that the protection they were enjoying was through the manufacturers' scheme. When they turned around after the scheme was in place, they found that the average tariff on components varied greatly. It is certainly not an average of 15 per cent; it is well down from that. So, if that is the case, I do not think there is too much to be concerned about. As I understand it, for the industry, cost is not everything in terms of relationships with component suppliers. I know some of them are nervous—I do not know if they all are. Some of the bigger companies are not. Given the relative levels of competition, I would be surprised if it were problematic.

Senator MARSHALL—Do you know if any modelling has been done on the potential impacts, particularly for those industries? There are substantial flow-on effects if that industry is damaged in any significant way.

Mr Oxley—No, I have not seen any modelling, but don't forget you would be looking at very significant increases in exports.

Senator MARSHALL—I understand that the argument would be that if you lose your job in the vehicle industry you can go and work in the milk industry, but I am not sure that that is easily—

Mr Oxley—No, the argument is that with increased exports the industry gets bigger. I understand that, over in Adelaide, General Motors have now put a third shift in for the manufacturing of Commodores, because they are exporting them so well to the Middle East.

Senator MARSHALL—That is if the gains outweigh the negative side.

Mr Oxley—Traditionally they do. Remember we are not looking at high tariff barriers here. This is the model that works with large numbers. In fact, I do not know why people keep talking about the issue of employment in the motor industry. The hollowing out in terms of the work force happened ages ago. It is a relatively lean industry now in terms of work force.

Senator MARSHALL—Yes, but it is still a substantial industry. That is why I was asking whether modelling is done on these sorts of issues, because some very serious implications proceed from it.

Mr Oxley—If you are looking at Adelaide, do not forget the reason why, in a sense, Mitsubishi have survived. Mitsubishi originally elected to send their cars to the US market from here, at a time when the Americans were making life difficult for Japanese exports directly from Japan. I would have thought that if there was to be some improved access—although the actual tariff on the vehicle is not that high, if it comes down a bit—it would be to Mitsubishi's advantage. The bigger problem for them is the basic health of the company, rather than their export position.

Senator JOHNSTON—It has been a fascinating debate between you and Professor Garnaut in various articles flowing backwards and forwards. About those issues, which I think are unresolved, on the one hand we have one person saying that the gains are not measurable and that if you do measure them they are probably not going to be very great. You, on the other hand, are very positive and quite expansive as to the benefits. I have a number of questions but, firstly,

with the dichotomy of us going down the American path in a bilateral agreement such as this, what security implications do you think that has in our region with respect to Indonesia, Malaysia and further afield into East Asia? That is a consideration I think advocates are not giving enough attention to. What is your response to that?

Mr Oxley—Usually they talk about the economic issue rather than security, but do you want me to address the security issue?

Senator JOHNSTON—I think security is an important issue that no-one is injecting into the overall consideration.

Mr Oxley—I do not think it would really make any difference. It is very easy to overstate how people see us. In Asia we have always been seen as allied to the United States, and I do not think that anything we do that strengthened that would much change that perception. There is no doubt that a free trade agreement would be an indication of a close relationship with the US. That is obvious. I do not think it would affect the security equation for us in any particular way. I have not seen anybody else argue that. Professor Garnaut's arguments have been principally about whether we would be jeopardising our capacity to trade and do business in Asia.

Senator JOHNSTON—I hear you saying that trade is an adjunct to and a basis upon which you then move to talk about security and other issues.

Mr Oxley—The Asian region is steadily going through some changes and, I think, as time passes, is looking bleaker and bleaker. I think we should now be quite concerned about the security situation in South-East Asia as a result of Bali. I think we are going to see far worse things occurring in the Philippines. In Indonesia they have now stopped talking about all the killing and instability; it is just taken as a given. The security situation is not improving there. From an Australian standpoint I think it becomes a bit more important that we possibly have some sort of stronger military relationship with the United States, but I think Iraq achieved that, not the FTA. In terms of whether we could have more collective security in the Asian region, if that is what you are getting at, I cannot see that.

Senator JOHNSTON—I just think that we should send a clear message that we are at the crossroads of two separate paths. One is multilateral South-East Asian and East Asian trade on a broadscale WTO footing. A bilateral agreement such as this sends a signal that we are moving down a different path.

Mr Oxley—All I will say is that in Asia they do not see the world that way. If they did, they would not be doing all the bilateral and regional agreements that they are doing. That perception is stronger in the minds of some of our multilateralists than reflects the reality in the region. What they are doing among themselves shows almost no regard for the value of a multilateral trading system. The Chinese have flippantly said, 'Let's do a free trade agreement with AFTA.' That agreement is destined to produce very little. Then they said, 'Let's add Korea and Japan.' Japan is talking about doing bilateral agreements with people and trying to find agreements that will not cause any economic pain. It is talking about negotiating one with Mexico. The Koreans are now talking about it. The Singaporeans have done one with Japan and they want to do another one with the United States. The Thais are out there looking for bilaterals. They did their own ASEAN free trade agreement, which is actually not a good agreement. It will be okay in the

long run but it is a bit unfriendly to people outside ASEAN. If that is a concern, I do not think that there is anything that shows that that is the way they see it.

Senator JOHNSTON—You talked about the pain and the gain. You are obviously prone to talking predominantly about the gain. Most of us sitting here want to know about the pain. We have briefly discussed the car industry. I am a little fuzzy on your response to that. My understanding is that the Americans can produce cars at a greatly reduced rate for export into our situation here, such that it would create enormous pressure on our car industry. When you throw in the government's support for that onshore industry, there is a problem, is there not?

Mr Oxley—The Americans supplying into Australia?

Senator JOHNSTON—Yes, exporting vehicles into Australia.

Mr Oxley—One problem the Americans have is that they do not build very many right-hand drive cars.

Senator JOHNSTON—But there are a fair few of them here, though, aren't there?

Mr Oxley—There are not that many. You have the Jeep. Ford had the Taurus for a while.

Senator JOHNSTON—There are Chryslers and Chevrolets. There is the Chevrolet people mover—the large vehicle. I cannot think of the name of the Chrysler vehicle but there are a fair few of them around.

Mr Oxley—Our industry is quite peculiar; there are basically three models. The industry regards itself as relatively vulnerable. The Americans in a sense will be competing against other people supplying those segments. Our industry now depends upon two things for long-term success. It still has to get off the tit. If you add the subsidies to the bottom line, no matter what success Holden has had recently you might find that Holden's profit is still largely accounted for by a fair whack of domestic subsidies. It has to be competitive and it has to get itself to the point where that no longer has to be the case. It has time for that.

The second thing is that they are seeking to integrate themselves into the bigger company operations around the place, so they are all bidding to get the research and design elements here. Holden have an Asia-Pacific research and design centre. Toyota is bidding for one. They seem to be having some success with their big companies. The third thing is exports. In the last few years we have seen considerable success. I would not have thought that the agreement with the US would do anything but support those.

The American parents probably are not going to take action to undermine their local plants here. Ford always have a big headache because they built such a big car that they do not know what to do with it. They might be vulnerable because what they do is not any world car component. General Motors at the moment is one of the most profitable arms of the GM empire in terms of return on business.

Senator JOHNSTON—Let us turn to something that is a bit more demographic and geographically based—airlines. What if the Americans, pursuant to this agreement, wanted to

run a domestic air service inside Australia and hook it up to an international service so that United arrived and they just continued running jumbos around the profitable routes of Sydney, Melbourne, Perth and Brisbane?

Mr Oxley—I have not seen any suggestion that air rights would be on the table in this.

Senator JOHNSTON—So air rights are carved out?

Mr Oxley—They are just not in play.

Senator JOHNSTON—There are going to be a lot of things that are not in play, aren't there?

Mr Oxley—But we are further advanced than that. You can look at the American list to see what they notify and what their ambitions are. You have seen the Vaile list of what the Australian ambitions are. That pretty well defines the issues on the table; that is almost set now. To bring airlines in now would be odd, and I think Qantas would quite easily stop it. And, at the moment, the American airlines are not in a position to do much.

Senator JOHNSTON—That is right. I am looking at the changing nature of events in America, and our domestic routes seem to be among the only profitable ones left.

Mr Oxley—It is still fairly small.

Senator JOHNSTON—Yes. Let us look at oil and gas. For instance, if the Treasurer were to have to deal with Chevron in a takeover bid for Woodside, how would we stand?

Mr Oxley—I cannot answer that. It should depend on the deal. I am not a fan of government intervention in any of these deals, I have to tell you.

Senator JOHNSTON—I am a Western Australian; I have to be a fan. Just tell me: how are we going to fare in those circumstances? Is Chevron going to have a right of action against us on that basis, or are the mechanisms going to be adequate to protect Australian ownership of that resource?

Mr Oxley—It is very difficult to answer your question, because it is so hypothetical and within a frame.

Senator JOHNSTON—We can do it now.

Mr Oxley—Yes.

Senator JOHNSTON—Are we going to jeopardise that capacity?

Mr Oxley—I would be surprised if any government gave up the right to reserve a national interest intervention for a major investment.

Senator JOHNSTON—Are you saying we would still have national interest interventions against foreign investment?

Mr Oxley—It is up to whatever people negotiate. I do not know exactly the position of our group; we have not formed a position yet on this. We want less fiddling about with the investment proposals but just how much less is something we will work out. Personally, given how important foreign investment has been to this country, I do not understand why anybody should think Australians should be frightened of foreign investment. We could not have grown without it.

Senator JOHNSTON—Let us move on from that. We have seen, particularly in Singapore, the effect of the downturn in IT and dotcom speculation which generated the negatives that came out of the US and into South-East Asia through Singapore and Malaysia. If we are even more connected to the US economy than we are now, are we going to be even more greatly exposed down the track to, for instance, deflation?

Mr Oxley—It depends entirely on how competitive our own economy is. What happened in Singapore is that that manufacturing base was hung onto for far too long. The manufacturing base in IT in Singapore was uncompetitive about five years ago, and Singaporeans knew it. The moment the US industry crashed, they got wiped because their costs were simply too high. The answer to your question, I think, depends on that. But do not forget something else about our economy which, in terms of the trade sector, is its greatest strength: we have a remarkable diversity of spread in our dependence on foreign markets and products. It is quite interesting to compare now with 1950, when—I might have the numbers a bit wrong—something like 70 per cent of our exports were wool and something like 70 per cent of them went to the UK. That was the boom period, with one product and one market—very vulnerable. Today, our biggest single export market is Japan, where we export 20 per cent of our exports as basically three or four products—coal, wool, iron ore. Our biggest single export commodity is probably coal, followed by tourism or maybe even foreign students. Coal is about 13 per cent. And it spreads right across. In fact, our diversity by product and by market is very unusual—very few countries have that—and so our capacity to weather changes in particular markets is actually quite robust. That is one of the reasons I am quite bullish about our future; we have ourselves well positioned. The US will never turn out to be our biggest market. No one country is going to be our biggest market, because of the way we have ourselves spread across all four sectors of the economy with exports.

Senator JOHNSTON—You touched on the single desk scenario. I have some understanding of the need for some changes there, but are we going to see a traditional, Australian, evolutionary change which brings along all of the stakeholders, or, through this agreement, are we going to see a short, sharp, forced change? Is it going to be painful?

Mr Oxley—It will be as good as the negotiators and what they want. I do not think it is very high on the American list, frankly. Nothing is high on the American list; it is one of the things about this agreement. Remember, we asked for it. When people say, 'What do the Americans want?' they are actually scratching about saying, 'We are going to have to do this. What are we going to put up?' There is not really anything much on the US list which is a deal-breaker.

Senator RIDGEWAY—In relation to your comments and/or predictions about the things that you have already gone through, do you have anything to say about the local content rules in relation to film and television? No doubt you would be aware of the meeting held here on Wednesday evening with the Australian film industry and Stephen Deady. I am not sure whether you have any comments on that or whether you are familiar with the consequences of NAFTA in relation to the Spanish language or Mexican film production industry and its implications when that was put into place. They were not put out of business but certainly Hollywood dominates a lot more than it has in the past. Do you have any comments?

Mr Oxley—I do. As I understand it, the Australian independent film producers are the ones most exercised about the impact. It has been interesting that the industry, except for a bit of publicity lately, has been relatively quiet, certainly quieter than when the New Zealanders succeeded in getting New Zealand products treated as eligible for local content. At that time, I was quite upfront about it. I was giving some advice to the New Zealanders; I did some economic analysis for them. The debate was far more virulent than it is now. I have often wondered why. One of the differences is that our film industry is now quite different. It has grown quite significantly. Last year the industry sold about half a billion dollars worth of business. This is the studios—Fox and so on. It is stuff going back into the US market. That means important work for the industry, not only for the actors but also for postproduction and all the support. Independent film producers would be relatively blind because they would be concerned about whether there is still going to be money around for the movies that they make. If you do the numbers, and I would like someone to do this properly, I do not know what the props of our film industry would be worth of that $500 million worth of business. I suspect that it is less than $100 million.

Let us look at the four props that exist for our industry. One is the local content provision, which guarantees that a certain amount of production has to be made for showing on television. The second one is tax concessions, which is the most valuable of all. The third is subsidies from the Australian Film Commission and the state film commissions. There is not so much money there but I suspect that they are probably relatively important for the Australian film producers. While people like Paul Cox would not get anything shown on Australian commercial television, they would be interested in the subsidies and movies that he and his ilk would make. The fourth prop was the requirement that a certain number of ads be made here. You are probably aware that that has been reduced. We now allow some American commercials on television.

They are the four legs that provide the support for the Australian film industry. Local content is only one of them. It is not a big deal for the Americans. They are raising the issue of local content—I have raised this in the past—as shadow-boxing because they really have their eyes on the Europeans in the WTO. That was a big issue in the Uruguay Round. I am sure you remember that the French were as angry about that as they were about agriculture. In fact, the threat to culture even became a bigger issue for them. That was the key American target. The Americans sell quite a lot of product here; it is not such a big market. Even if—and it is a big 'if' here; I am going to qualify it in a moment—we decide to change the quota, not eliminating it but supposing we shaved 10 per cent off it, the economic effect in terms of what provides support for the Australian film industry would be probably insignificant. It would be worth talking to the TV producers, the TV broadcasters. They almost say that the quota is not necessary in order for them to fund Australian production because they now need Australian production in order to get the ratings. Australia has a strong preference for seeing Australian product. The old argument that

the American stuff is so cheap is countermanded. I am only hearing that by gossip but it would be worth talking to some of the TV broadcasters about it.

Finally, I was told the other day by an executive with one of the companies which is a big film production house that the primary interest of the American film industry was to see a toughening of our compliance laws on piracy of movie DVDs. That has become a really big issue—it is now far bigger than the recorded music issue. They are losing a bag of money and it is very serious, given the numbers.

Senator RIDGEWAY—Which we have just deal with.

Mr Oxley—I was told that you have just agreed to some legislation. Is it in the Senate?

Senator RIDGEWAY—It has gone through already.

Mr Oxley—I am told that that has basically satisfied the primary interest that the American film industry had—in other words, they are not so interested in local content. Time will tell. They probably will not take it off the table, for whatever reason, but it was an executive who told me that. In a sense it fits. Campaigning out on local content, even if they did have an interest, I would not have regarded as a deal-breaker. In fact I am told that frankly our officials see it in this light as well.

Senator RIDGEWAY—I would like to go back to an issue that Senator Johnston has raised in relation to the debate going on with Professor Ross Garnaut and so on, and more particularly on the question of deep integration or this harmonisation between the Australian and the US economies. Could you talk about that in the context of what that means about the regulation of Australian and US companies, particularly given the need to look at examples such as Enron and WorldCom and corporate practices or standards. Does that mean that we ought to be operating to American standards, or how might that be dealt with?

Mr Oxley—It does not automatically come up in an agreement like this. It really depends on whether the regulators see an interest in doing it. All foreign companies—not just Australian companies—who need to work in the US have to comply with US standards. So if you figured that it made more sense to adapt some of our standards to US standards or international standards simply in order to have only one system of accounting, then there may be some benefit in that. I cannot imagine that our people would go along with something that they considered produced a worse standard than the one that we currently had. I cannot comment on whether what went on with Enron—

Senator RIDGEWAY—Is that going to present difficulties for the US?

Mr Oxley—I would not have thought so. You might ask some of the larger companies who are in the market about that. I have not seen it listed as an issue. It is not on their list of things that they are interested in.

Senator RIDGEWAY—Thank you.

Senator HARRIS—Mr Oxley, you made a comment earlier on that you would envisage there would be some investment rights and you mentioned national status. In the past, with the failed MAI program, one of the big concerns was that a segment of it was purported to ensure investment capital to the extent that it may have had to have been guaranteed by the taxpayer. We have actually had people who have raised the chapter 11 section of NAFTA. Do you see a similar chapter 11 facility in this agreement? If it did eventuate, what would be some of its benefits, but what could be some of its possible downsides when we look at how the American companies have been able to use section 11 against the Canadian government specifically?

Mr Oxley—And the Mexicans. And in fact the Canadians are trying to use it right now against the Americans. I don't know, is the short answer as to whether there will be something like it. There is something comparable in the US-Singapore agreement, and our group is looking at that now. We are talking to our members about whether they would be attracted to the legal right—which that chapter 11 mechanism provides—for a company to contest its right to national treatment.

There are some interesting illustrations. The whole debate in the United States has become somewhat skewed, because green groups there have really turned it into an environment issue rather than an investment issue. Usually, you will find that the issues that they make the biggest fuss about have an environmental overlay in there somewhere. To show you how it works there, there was a case in Mexico where a company—I forget whether it an American or a Canadian one—had approval from the Mexican government to proceed with an investment and it was ruled off. Then, when it got to the local city authorities, they jacked up and refuse to approve it. There was an environmental spin in there which was one of the factors. The company then said, 'Under NAFTA, we have a legal right to be treated on the same terms as a Mexican company.' That was really the point. It is a little unusual for companies—usually, with agreements, it is governments that have the obligation and the right to pursue them.

In this particular case, a legal right has been created. I do not think there is any loss of sovereignty here. There is a conscious effort to go in and people secure the same benefits in each place. I think of it in terms of our companies operating in the US. Often with foreign investments it is not the federal or the national government that is the problem; it might be a city government, a state government or a local council which will come to the foreign company and say, 'How about you do this or that,' and seek more favourable terms from the company, because it is foreign, than they would from a national company. I look at it from the standpoint of whether it would benefit Australia's companies operating in the US market to have some sort of right of recourse like that, to defend its right to get equal treatment to an American company. So that is how I would see it panning out. As I said, from our group standpoint, we are having a look at it. We will canvass our members to see whether they think something like that would be useful or not.

Senator HARRIS—Is there any possible downside?

Mr Oxley—I honestly cannot see one. You can get into the business of whether the local or county authorities are entitled to take a different position to the federal government, but I would have thought that it helps to secure your right not to be treated as a foreigner. Foreign companies are a bit vulnerable. In my experience, most big companies actually go a long way out of their way to be better corporate citizens than domestic companies do. I have worked for a long time

with foreign companies here and you tend to find that the very big companies—you will not be surprised that they are the ones with the big names—will often be quite loath to go and press an issue with the government because they are concerned about not being seen to be a good local citizen, whereas an Australian company would do it. In a sense, that is the other side of their concern—it also means that they are liable to have people coming to them to try and extract concessions.

CHAIR—We have had you at the table for a lot longer than the original appointment—and we have skipped morning tea for ourselves!—but the Australian Wheat Board has been unavailable so we have been able to exploit your presence.

Mr Oxley—You should ask them about the single desk, not me!

CHAIR—If you are not pressed for time, there are a couple more questions we would like to ask. Our next witness is due at a quarter to 12.

Mr Oxley—That is fine.

CHAIR—We had a day of hearings yesterday in which we heard from a basket of critics. Except for one witness—a former colleague of yours, who was on GATT—you are the first pro-Australia-US free trade agreement advocate that we have had and obviously, given your position, you are one of the most authoritative, so this is a good opportunity for us to pursue some questions with you. Just going back to your answer to my obvious, bald question: 'Can you crystal-ball what the outcome of this package might be?' you kindly did that for us—

Mr Oxley—Which I would rather not be held to account for!

CHAIR—If we were to hold you to account for it, it would be a bit like the debate we were referring to on the value of all of this. You made up-front waivers about how this should be regarded, but in an effort to cooperate with us you then proceeded to offer an opinion, and that is fine. One of the obvious areas that you did not comment on was the Pharmaceutical Benefits Scheme. I think it would be remiss of us if we did not ask you about that.

Mr Oxley—Medicines Australia is a member of our group, so I can speak to a degree for them but not too far down the track because, as I understand it, they are still sorting out the detail of their position. But the first thing to say is that it is not the position of the Australian pharmaceutical industry or the American pharmaceutical industry to see the public benefits scheme dismantled. It is not their position and it never has been. You always wonder where things come from when they start running around and getting picked up. I am still not quite clear where this came from, because it was never on the US trade watch list—I am talking about abolition of the program, which was said to be what the Americans wanted. What do they want? Their primary issue is the way in which some of the prices are set.

While we are inclined to think of Pfizer and Bristol-Myers Squibb as big American companies, they are actually no more foreign than Ford or General Motors. They employ 12,000 people in this country and they are significant investors and exporters. There is a longstanding issue about our pharmaceutical prices, which are a consequence of the PBS for the industry, which the government has always in fact conceded in the past. As you know, in the past the

government accepted the argument that the Pharmaceutical Benefits Scheme required them to get lower prices for their pharmaceutical goods—and they claim that they are lower than in any other industrialised country market—and, for a number of years, the government was willing to pay them subsidies to bridge the gap so that they would invest here and would export. All I would urge is that we do not forget that setting in respect of this particular question. The issue is a question of process—the way that prices are set. Now they have to sort themselves out and explain their position. The line that has been run around here that that is a key thing that the Americans want is not really close to the facts. It is an issue on the table, but the suggestion that pulling the scheme apart is the quid pro quo for the deal is not supportable.

CHAIR—Recognising all the qualifiers you have expressed about venturing into this area of crystal balling, are you saying that you do not think the American side will press us on access to more open pricing on pharmaceuticals?

Mr Oxley—I cannot say that—they have not yet sorted out what they want—but, as I understand it, they are looking at the question of transparency and how pricing is done.

CHAIR—You asked how these stories get up. Obviously, health is one of the more incendiary public issues.

Mr Oxley—Of course.

CHAIR—The big elements of the health debate include the high cost of pharmaceuticals, particularly new drugs on the market, how long the IP restrictions that prevent generic production last and so forth. Clearly this is a matter of some public anxiety and we pick it up as we move around, with our ears to the ground. A number of American companies have also made no secret of the fact that, while they participate in the PBS, it is not their ideal operating format—they would prefer a more open market. That adds credibility, if you like, to the anxiety that has already been expressed.

If the American side have not yet made up their minds, as you have described, about what their real target in the pharmaceutical area is and if we are looking at a closer deadline for the conclusion of these negotiations than we might otherwise have been looking at, with the remarks of the President over the weekend, when might we expect to know, do you think, what the American objectives will be? This goes to the question of public scrutiny and debate so that we can form a view about them. Another way of putting it is that it would be terrible if there were a sense, justified or not, that we were ambushed on pharmaceuticals in these negotiations.

Mr Oxley—I cannot answer that question directly but I am happy to share with you the advice that I have given to members of our group: that everybody should be getting their positions together as soon as possible because the pace of this negotiation is actually going to be quite rapid. Anybody who does not do that and get their ducks lined up is going to miss out.

Senator HARRIS—I want to follow up your train of thought on the PBS. A concern that I would have would be if, within the negotiations, the actual focus of America was placed on dismantling the Australian process of the government being the sole purchaser of all of the pharmaceutical products and then distributing them through the PBS. This is a 'what if' question: do you see that as maybe being the bottom line of what America is setting out to do, so

the bottom line would not be the price structure but the actual function of how Australia administers the Pharmaceutical Benefits Scheme?

Mr Oxley—Honestly, I could not answer the question, but allow me one piece of pedantry. These are Australian companies. They might be American owned but these are companies with large numbers of employees here and they are a significant export industry. I do not disagree with the points that you are making—I think you understand it completely; it is politically extremely sensitive—but I think it is important that we do not let slip the idea that this is simply what the Americans want. This is what the companies based here want. They are constantly preoccupied by the question of whether they can stay in the market here; that is their primary concern. It is not a matter of their ripping off the government or anything else. Their primary consideration is: are they able to continue to do business here? They are all quite small in terms of the size of their bigger networks. If you talk privately to the heads of the operations here, they would probably express to you anxiety that they are within a hair's breadth of having their operation pulled out because the market is too small and the returns are too low. I understand what you are saying about the pricing. Pardon me being a bit tedious on this but I think it is an important point.

Senator HARRIS—The focus was not on the pricing. My concern is if America moves towards negotiations to dismantle the process by which we access the market—in other words, the government being the sole purchaser into Australia of the pharmaceutical product and then distributing it. It is the equivalent of a single desk. If the Americans' focus is on removing that and then allowing the companies access to whatever the markets are individually within Australia, there would be far less control for the government over the costs of pharmaceuticals.

Mr Oxley—I will make a couple of general comments. Firstly, it is not normal in trade agreements to go after a major social welfare scheme. I cannot think of one where that has happened. Even if that is the broad trend, I would express general surprise if this negotiation went that way. Secondly, it may well be that whatever is done here is more a function of some government reform agenda than what the Americans want, given that it is an issue in play. But it would not be the natural order of events for this to be allowed to become a major issue in this agreement, given the relative importance of it compared to all the other things—but you can see I am not into the detail here.

CHAIR—I will go to the car industry for a couple of quick questions. We do a preferential trade deal—which in economic terms is about what? I do not know what the term 'free trade agreement' really means in technical jargon for the type of arrangement we are talking about, but it is the accepted term. Economists might argue that it is a discriminatory trade agreement or a preferential trade agreement—different sides of the same coin. But if we do an agreement with the United States which means that for the car industry, as you have suggested, we remove our level of tariff protection for them and not for the Japanese, do you see any implications for our relations with Japan, South Korea and Europe, which are the other providers of motor vehicles in Australia? This is more particularly so with Japan, because there are four manufacturers here and two are American and two are Japanese.

Mr Oxley—It is an issue which I expect the Japanese and European companies would be looking at very closely. There are many ways in which these things can be addressed. Since it is our belief that this should be done to make the Australian economy more competitive, we

actually did say as a group, when we put our submission to the government, that we thought that whatever tariff cuts the government agreed to should, in fact, be applied MFN—such that if we make a cut for the Americans we do it for the rest. That is our formal position and that, in part, obviates some of the criticism about preferential agreements, discrimination and so on. Yes, this free trade agreement is a preferential agreement. The idea of a free trade agreement is to remove all barriers between the two countries and not the ones outside. The extent to which discrimination matters depends upon the height of the barrier. If the barrier is small, it does not matter. In the auto area, we are talking about 15 per cent, so it would be regarded as significant. I am not sure when that is due to come down to 10 per cent. What is the date for that?

CHAIR—I am not sure either. I think it is in a year or so.

Mr Oxley—So it will actually be a 10 per cent barrier, which is a bit easier to manage. We hope that whatever decision is taken is in the best interests of the Australian industry, and we would be a bit surprised if anybody took a decision that did not get that result.

CHAIR—Are Ford or General Motors members of your group?

Mr Oxley—Holden is.

CHAIR—That is General Motors.

Mr Oxley—Yes.

CHAIR—They argue publicly and—having been the minister at the receiving end of this—with considerable force that we should not reduce those barriers.

Mr Oxley—They did, didn't they.

CHAIR—And they do. They are still doing so. The current industry minister has had this argument put to him strongly as well. It sits oddly that they, as an industry group speaking in their own voice, are arguing that they cannot sustain their production in Australia if the tariff falls to the level of the program.

Mr Oxley—Are they still arguing that?

CHAIR—Yes. They argue it at every point. It seems to me from what you are saying that, through your group, they are saying out of the other side of their mouth, 'Let's get it on.'

Mr Oxley—The commitment is to take the auto tariff down to five per cent by 2010. If the agreement were for 10 years, which is normal, and if we were to get it in a year's time, in 2004, it would go through to 2015. If we are making tariff cuts, they are usually progressive and slower. We are not looking at large numbers here. The auto industry are interesting. I have worked for them on and off, and the interests of the four companies are all a little bit different. One of them, notwithstanding willingness to remain solid with the rest of the industry—because they do, as you know, usually try to work towards a common industry position—claimed a few years ago to have already reconciled itself to a zero tariff environment for Australia. You could pretty well work it out, in terms of their business positions and who is exporting and who is not.

Mitsubishi is in the most difficult environment, because of the company's broader fortunes. There are some shades of difference between them, but they are not arguing against the rate of cuts which has been agreed, are they? Are you hearing that?

CHAIR—I am hearing that they are concerned about their ability to sustain their production at that rate of cut.

Mr Oxley—Yes. When is the car plan next up for renewal?

CHAIR—Then we get into this murky area. The government's current position, as I understand it, is to promise a review of the car plan before it proceeds any further. That suggests that, depending on the outcome of the review, the next steps may or may not be viable. It would be silly to have a review and then do what you wanted to do anyway—what would be the purpose of the review? You might as well just do it. The other concern is that, because the car plan has been a longstanding feature of the Australian industry—and cars as well as TCF, as you know, were exempted from the general level of tariff phase down because of the sensitivity of those sectors—by consensus, various groups, not just the manufacturers, signed onto those plans, and governments have given their word and undertakings about how they will manage those places.

It is perfectly legitimate for an advocacy group like yours to put forward a particular view—there is no argument about that. But looking at it from the government point of view, there are myriad commitments and nice balances that have been struck here, and from what I hear I am not sure whether or not all of those have been adequately digested by the industry. The argument on the Japanese front is that the undertakings that we gave in the Nara treaty with Japan—to extend to the Japanese the same concessions that we might extend to a third party—would be invoked by the Japanese in this case to say, 'If you give these concessions to the Americans, then you are bound by virtue of that treaty to extend them to us.'

Mr Oxley—They might, but I would not have thought that they would be on very strong ground, given what they have just done with the beef clawback.

CHAIR—They might regard themselves as being on strong ground when they look at the terms of the treaty.

Mr Oxley—There are no enforcement or dispute processes in the Nara treaty.

CHAIR—No, there are not, but it is a treaty about having a good relationship with Japan which has at its core an undertaking that we will not treat our partner Japan any less favourably than we treat other parties.

Mr Oxley—I understand that, but—

CHAIR—It is a moral argument.

Mr Oxley—As I said, I think our general position is that it would be sensible to make cuts equally to all, but just how this one would pan out I do not know. Bear in mind one other thing—the American industry itself has protection of its auto sector.

CHAIR—Of course.

Mr Oxley—It is 25 per cent on pick-up trucks, I understand, and about three per cent on cars, so I am not sure they would be in a real hurry to demand something faster from us that they might not be prepared to do themselves.

CHAIR—I think we have kept you longer than we intended, and we are grateful for your time, Mr Oxley. We may want to hear from you again after we have finished collecting evidence from hearings.

Mr Oxley—Any time—I would be delighted.

CHAIR—Thank you for your submission and thank you for your attendance here today.

Mr Oxley—Thanks.

[11.45 a.m.]

KERR, Mr Paul, President, Australian Dairy Products Federation

LAVERY, Mr Peter, Chief Executive, Lavery International; and Chair, Trade Commitee, Australian Dairy Industry Council

PHILLIPS, Mr Christopher, General Manager, International Trade, Australian Dairy Corporation

ROWLEY, Mr Patrick, President, Australian Dairy Industry Council

CHAIR—Good morning, gentlemen, and welcome to our inquiry. Thank you for lodging your submission, which we have before us. The normal method of proceeding is to invite you to address it briefly and then be available for questions. It is for one of you or all of you to take up the option to address your written submission.

Mr Rowley—Thank you. This group represents all of the dairy industry: Peter Lavery chairs the Australian Dairy Industry Council's trade group; Paul Kerr is Operations Manager for Murray Goulburn, the largest exporter of dairy products in Australia; Chris Phillips is manager of international trade development for the Dairy Corporation; and I represent the dairy farmers.

The Australian dairy industry strongly supports a free trade agreement that includes the complete elimination of all barriers to trade in agriculture and food products. We believe that agricultural trade reform should be at the heart of such an agreement and is central to its final value. The phased elimination of trade barriers will provide opportunities for Australian firms to increase trade. It will also open the way for trade from the US, particularly in products that producers use as inputs.

We are fairly conversant with free trade agreements, in respect of our CER with New Zealand. Back in the mid-eighties we produced about 5.2 billion litres of milk. Since the CER agreement and the Kerin plan, over the 20 years, Australia has doubled its production to 11.2 billion litres. The present value of exports has risen to $3.2 billion. So we have had some experience and we believe that freeing up trade, particularly in the areas that the free trade agreement would free up, would initiate investment in production.

As an industry, we are basically excluded from the major markets of the world—the US, EC and Japan—with their very high tariffs. We are basically exporting into South-East Asia and the Middle East, with a little bit of product into South America. We believe that this free trade agreement would act as a blueprint for our major thrust, which is to try and get the multilateral negotiations into a position where the terms of trade out there are more receptive to dairy.

Both Australia and New Zealand—and Australia in particular—have the wherewithal to produce more milk and more products. A lot of investment in regional Australia and a lot of jobs are at stake if we can improve those terms of trade. So we see the free trade agreement with America as giving us an opportunity to work on the elimination of those restrictions, carry that

through into the multilateral negotiations and improve Australia's dairy position. We would be prepared to answer any questions that you might care to ask us.

CHAIR—Thank you, Mr Rowley. Do I take it that you are speaking on behalf of everyone or are there supplementary statements that others of your party wish to make?

Mr Rowley—That is our opening statement.

CHAIR—Then we can go straight to questions. We have just had, as you would have heard, Mr Alan Oxley of AUSTA before us. I do not know whether you were in the room at the time—and I certainly do not wish to in any way misrepresent what Mr Oxley said—but the first question I put to him was: given his experience in trade and as a former ambassador to the GATT for Australia, and his proximity to the US negotiations, could he crystal ball for us what he thought the likely outcome would be? He is a prudent man and he made, of course, a number of up-front disclaimers, and it would be wrong to put too much weight on what he said. He himself would not put too much weight on what he said, because it is a crystal balling operation.

Having said that, what did he say? He did not initially include dairy as an area in which he foresaw, in his presentation, the likelihood of a greater degree of liberalisation. So I asked him directly about dairy. My recollection of his reply was that he was not close enough to the issue or he had not heard from you guys well enough to make an informed comment, which is perfectly acceptable and reasonable. It does not mean to say that the prospects for dairy liberalisation are not strong; it just means that he is not in a position to comment on it. Now that the first contact in the negotiations has been made, and you have been able to take the temperature of the negotiations on the American side, what do you think the likely outcome for dairy will be in this agreement?

Mr Rowley—I will pass that question over to Mr Lavery.

Mr Lavery—I will make some comments not necessarily related to your line of questioning. The first is that there are no real precedents for this negotiation as far as dairy is concerned. The nearest that you might come would be with regard to Chile, where the free trade agreement provides for free trade in dairy after a period of time. It really raises the question of what we mean by free trade. I noticed that you queried that earlier. We do not envisage some arrangement where free trade will arrive on 1 January in such and such a year and the doors will be thrown open.

There is a question of how you get to free trade. We have taken, as you say, the temperature readings at the other end. They are fairly hot, but that is not unexpected. It is the nature of dairy; it is the nature of their industry and the way it operates politically. We still believe there is a good chance of negotiating an arrangement which would provide for free trade. The skill will be in negotiating the phasing to get to that point to minimise the adjustment problems at both ends. There could be problems at both ends in this process, more particularly at the US end, but we believe it is possible to negotiate an arrangement which will provide for stability in the American industry while reaching a point of free trade.

Mr Phillips—One of the issues on the US side is that dairy is a sensitive product for a number of their industry groups, but we believe that is based on a misunderstanding of what the

commercial threat to them would be from a liberal trade arrangement in dairy, given the relative size of the two industries and the size of the US market relative to the international market. You have to put in perspective the fact that the US dairy market in its own right—that is, over 75 million tonnes of milk produced each year—represents about double the actual size of the international trade market in which we are allowed to trade at the present time and some seven times what our total industry production capacity is at this point in time. We believe there is scope for considerable liberalisation of the market access arrangements into the US without a significant impact on their domestic wholesale price and support structures in the short to medium term, which is where the concern from the US industry side is coming from.

CHAIR—If I can put it in these colloquial terms, having seen the whites of their eyes in the first round, you remain optimistic that there is the prospect of breakthroughs for you in this sector?

Mr Lavery—Indeed.

Mr Phillips—That is correct.

Mr Lavery—We are having some work done which will provide some independent economic modelling of the impacts, but it is not available yet, I am afraid.

CHAIR—Do you know when it might be available?

Mr Phillips—Our expectation would be June or July, because we want it to be available fairly soon after the ITC report becomes available in the US. That is an important part of the discussion which will take place on both sides before the third round of negotiations when some of those formal request/offers numbers might come into process.

CHAIR—When it is completed will it be available publicly or is it for your private information?

Mr Lavery—It is not going to be much use to us unless it is used publicly.

CHAIR—From the point of view of this inquiry, I imagine that in June or July—I have to say this with some regret—we will still be sitting on this reference. If we are extant when it does become available, may we have a copy of it?

Mr Lavery—Of course.

CHAIR—What we are talking about here is access to the US market. We are not talking about removing the preference and subsidies that US dairy farmers receive from their own government. What we are talking about is Australian exports competing with subsidised, home-grown products in the United States. I know your preference would be for Australian dairy farmers who, apart from the adjustment schemes, are unsubsidised, to compete on a level playing field with unsubsidised American dairy farmers. But it is not possible in an FTA to remove those subsidies, so that is not on the table. How do you assess our ability to compete against subsidised domestic producers as importers in the US market?

Mr Phillips—We would take one perspective on it. On the issues of subsidies, in the US the price support system is not about subsidising the final selling price of the product; it is about trying to maintain a minimum price level for US dairy farmers. Under their current support arrangements we believe our industry would be very competitive at competing with US dairy industry producers under their existing Farm Bill arrangements, which would operate until 2007-08. We do not know what the new Farm Bill operations will be in terms of their support structures beyond that. But under the current situation and arrangements we believe our industry would be quite competitive.

Our situation internationally is that Australian dairy is, if not the first, at least equal first in international competitiveness in terms of delivering quality processed food products out to world markets. We believe in all those areas we would be competitive against the US industry. But we recognise that in negotiating the agreement some of the core products which form their basic support mechanisms may be more sensitive in terms of how they would allow access for those products. Paul may be able to make a more definitive statement there.

Mr Kerr—From our perspective, Murray Goulburn, the largest dairy company in Australia, processed over four billion litres of milk last year and exported approximately 70 per cent of that. Our business is built around export markets. We export to over 100 countries. We have made significant investment in technology and developing new products particularly in the protein and the nutraceutical area, and we already export significant quantities of those products to the US. Those products are not made today in the US because their system does not encourage them to make those products. We are looking to expand our opportunities in the US in the value-added market, but it is difficult at the moment.

Senator JOHNSTON—Could you tell us what sorts of products they are?

Mr Kerr—Milk protein products, casein caseinates, nutraceutical colostrum type products, whey protein isolates. Our company has spent something like $500 million in capital investment equipment in Victoria over the last five or six years. Part of it is in that area. Those products are high value. They are not skim milk powder, they are not butter, they are not cheese; they are adding value, and they are products not made in the US today. So we see the free trade agreement as giving us further opportunity not to displace US product but to grow the market. The US is the largest economy in the world. It does offer us an opportunity and we are very pro the FTA for that reason: because we can grow our business and add value.

Currently, our products are under attack in the US. They are talking about introducing tariff quotas on some of these products. There is a feeling amongst some producers over there that these products are substituting for their product, but in reality they are not. They are new products and they are growing the market.

CHAIR—Are the range of other diary products like cheeses, creams and yoghurts part of this as well or are we talking about milk in its liquid form and milk based products?

Mr Lavery—It is inevitable that there will be some movement of products like butter and cheese under a free trade agreement. In answer to your earlier question about why we think we will survive there or why it is attractive: the simple answer is that the internal prices in the US

always have been, presently are and look like for a long time remaining well above international levels, which is where we have to survive commercially now, so it has to be attractive.

It is important to take the point that Mr Kerr is making, that we tend to think of the diary industry as being butter, cheese and milk, but it has become a very sophisticated industry. Milk is a very complex product and it can be taken apart, put back together and processed in various ways to do all sorts of sophisticated things in food processing. The American market is the biggest sophisticated food processing market in the world. We would see Murray Goulburn being able to address that area. We have a big advantage over the American industry which, because of its support, churns out butter, cheddar and skim milk powder because they are the products that the government supports. This is why Murray Goulburn are running into the sorts of problems they are running into. We see that sophisticated end of the market, which is not being addressed, running through in time into a greater integration of the two industries with investment flows. We would envisage probably joint ventures with some of our cooperatives to produce these more sophisticated products for the American market. We are thinking well beyond the milk, butter and cheese stage.

CHAIR—When I was a kid in short pants I was sent down to the shops by my mum with a shilling in my hand to buy a bottle of milk. It was in a bottle and all you got was a bottle of milk. Now when my wife sends me down to the supermarket with a credit card in my hip pocket and I front up for a bottle of milk there are virtually no bottles but there is a whole range of what is milk. Then the dairy products off that are just huge. I acknowledge the change.

Mr Lavery—You have the better of me, Senator. I remember when it was left in a billy at the doorstep.

CHAIR—I was trying to hide my age—I remember that too! I want to go to the question of whether or not doing an FTA with the United States will be a lever on the multilateral round. I take the point Mr Rowley made about how heavily agriculture is protected around the world. In passing, I make the point that agriculture has immense political influence around the world. In Japan it is the rice farmers that seem to run the country. In France it is the peasants—which is a horrible term to describe a farmer—across a whole range of commodities who hold the ring politically. And throughout the European Union and in the United States, as the Farm Bill testifies, there is immense political clout by the farming lobby. In Australia there is a party that is part of the federal government that was initially based as a farmers' party. I am not saying this is a bad thing; I am saying the truth is that the agricultural industry, more than most, has immense political clout. The dairy industry in the United States is well represented in Washington and is an effective lobby as well. So your remarks about talking with them and getting them to understand the real impact of competition from Australia, as opposed to what their darkest misgivings might be, is interesting.

But, having said all that, the main game is to open up the agricultural markets internationally. This is presented through the orthodoxy DFAT advocates, which the government advocates—the current newfound orthodoxy—that if you do a multilateral agreement with the United States somehow that can prise open the round. That is the strategic argument. I do not believe that is true; it is a fallacy, in my view. Why do you think that a multilateral agreement with the United States might somehow energise the round? What are your views?

Mr Lavery—Do you mean a multilateral or a bilateral agreement with the States?

CHAIR—I understood Mr Rowley to say—and correct me if I am wrong, but it is a common view that is the government's view—that if we do bilateral trade agreements we can use those to prise open and energise the round and win the multilateral game across the board. Unless I am mistaken, that is the view that you have put to me. I am just flagging that I do not agree with that necessarily. But I am really asking you to justify that view to me.

Mr Rowley—We put a lot of effort into the Uruguay Round. We are putting a lot of effort into the Doha Round and we are spending a lot of time and energy because we have got to try and change the whole world scene that operates for dairy products, as you said. A bilateral agreement with the US could well create some blueprints for the way it could operate. Taking Chris Phillip's point on board, about the view in the United States that all this is very damaging, when you look at the size of the market and what Paul Kerr said about the products that are going in, I think we could use that argument in the multilateral negotiations to demonstrate to some of the other major players, in particular the EC, that allowing access into these markets is not as damaging as they believe it is. I would like to defer to one of my colleagues to go into some of the detail.

Mr Lavery—In dairy we have a particular perspective. Dairy has always seemed to be more difficult. If you look at the last two major rounds—the Uruguay and Tokyo rounds—the settlements, such as they were, on agriculture essentially arose as a result of a transatlantic accommodation pretty much in grain, with the other major economic group, the Japanese, tending to fall into line. That is probably a rather crude summary but it is probably not an unreasonable assessment.

CHAIR—I agree with that. In previous rounds, if Europe, the United States and Japan agreed, the rest of the world fell into line and we had a round outcome.

Mr Lavery—Yes. There are two aspects to what we are facing. Firstly, the major attractive markets for diary products in the world are the US, the EU and Japan. There are other attractive markets and we certainly do not want to give them away, but those are three big remunerative markets, the US being one of them. If we can get something going in the US, then in a sense we have solved one of our three major access problems and we have probably solved it more effectively than will come about in a WTO round. But, more importantly, it creates within dairy some precedents which may provide guidance or a lead in how dairy might be handled in the WTO. It has been a transatlantic accommodation, we think, because both Europeans and Americans have political problems with diary and that is why dairy has tended to be left behind. In that context, we see it as very useful to pursue a free trade agreement with America. Frankly, as diary industry, we would be irresponsible to our farmers if we did not jump at the opportunity.

CHAIR—I understand that from an industry point of view. You may be aware that the *Economist* magazine last year devoted a complete edition to this very debate in which it argued in its editorial that the oxygen had been sucked out of the Doha Round by a proliferation of bilateral agreements and that the energy was going into bilateralism, meaning that the round itself was falling behind its own pace. Coming up to the Cancun conference this year, we can see that we are well off the pace as far as agriculture is concerned. Agriculture has been left behind. The real gain for your industry in trying to get that mythical level playing field is to remove

those subsidies. The only prospect of doing that is through the round, not through a bilateral negotiation. While it is absolutely right, and I agree with you, there may be gains at a bilateral level, the real game where the biggest gains are achievable is at the multilateral level. If that is stalled because of bilateralism, there is a strategic problem here that we have not quite got right.

Mr Lavery—We certainly do not resile from the fact that the main game is the WTO. There is no question about that. The problem in that process is probably that—and this is a personal view—some of the oxygen is going out as a result of people looking at bilateral arrangements or preferential deals. That could partly be because of frustration with the process, but I believe also that the process has pretty much slowed up because one of the major parties, the EU, cannot get themselves sorted out on agriculture. That has meant that everything else has drifted. We are waiting for the Europeans to pull themselves together and work out what they want internally before we can get on with the multilateral round.

CHAIR—That is a fair comment.

Mr Lavery—You talked about getting rid of subsidies. From a dairy point of view and from all the economic modelling work that we have done, our biggest problem is not the subsidies but more so the question of access.

CHAIR—I would be interested to see that.

Mr Lavery—The modelling work that we have had done indicates that there is some gain from the removal of subsidies but it does not hold on as long because of price adjustment effects and supplier responses. It is the access that gives us the real benefits because the market is bigger. It does two things: it gives us a bigger, more profitable market to work in and, because the market is bigger, it is more stable.

CHAIR—I am not implying a criticism by arguing the way that I have. It may be that at the end of the day all these strategies and theories about which is the best way forward are fine, but in pragmatic terms you take the gains where you can find them.

Mr Lavery—That is our problem.

Senator MARSHALL—Are there quarantine issues in relation to dairy trade between the US and Australia?

Mr Phillips—There are not major direct dairy quarantine issues. We have some issues that we would like to see the negotiations deal with in terms of standards and labelling requirements and mutual recognition of Australian standards being built into the US system as part of any final outcome. That is an important point for us because some FTA requirements on factory inspections and other issues can act as technical barriers to trade opportunities. Even though you offer free access for products, there are some ways—factory inspections, regulations and others—which can be used to block off commercial trade. We are very concerned that the negotiations deal with those mutual recognitions of standards that operate in Australia and they get built into any final agreement. There are no direct issues of dairy products subject to quarantine issues at the present time.

Senator MARSHALL—With regard to those other issues that you talked about, is that because a higher standard is applied, or just a different standard?

Mr Phillips—There are different standards. There is an element of standards which they apply to their own industry in theory but not in practice. They say, 'You must comply with those in Australia.' An example is cream. Every herd has to be tested each year for TB, whereas Australia has a TB-free status. We ask, 'Do we have to go through these processes in order to trade that product?' Some of our trading competitors have different memorandums of understanding which allow them more favourable commercial access for those products, so we want to ensure that we get as close to a level playing field as possible as part of this arrangement.

Senator MARSHALL—In terms of dairy trade coming into Australia from the US, are there any quarantine or same standard issues that you were talking about?

Mr Phillips—Not that I am aware of in the dairy sense. Since CER, we have been operating pretty much with free access for all dairy products into the US. There have been relatively minuscule amounts of US product traded into Australia from time to time; it is a matter of the price competitiveness of their industry. That is the primary issue driving the trade this way across the Pacific, but there are no real quarantine issues between the two industries.

Senator MARSHALL—I want to clarify something with you, Mr Rowley. You said that the dairy trade issue has to be addressed in this free trade agreement, which is essential to its final value. Did you mean that without dairy the whole agreement would not have value for Australia, or are you talking about value for your own industry?

Mr Rowley—I was talking about the broad agricultural trade rather than dairy particularly, but dairy is inside that category. What I am really saying is that it is obvious from the responses from the other side of the Pacific that there are some difficult areas in agricultural trade. But if somebody believes that you can leave these areas on the backburner until the end of the phase-in period before addressing them, Australia will lose some of the value. Dairy needs to be addressed inside agriculture, inside the total negotiations, because that will create the best possible outcome.

Senator MARSHALL—Are you saying that without agriculture you do not see any real benefit for Australia entering into a free trade agreement?

Mr Rowley—No, I am not saying that. I am simply saying that agriculture needs to be right up there on the frontline early and that the difficult issues need to be addressed. People from the other side are saying that sugar and dairy are difficult. We all know that, but they ought to be right up there on the frontline and talked about early. The last thing that we want to see, particularly from dairy's point of view, is that we end up right down at the end of a phase and then we start talking dairy. That is not acceptable.

Mr Phillips—We have not done a separate analysis of the benefits, so dairy does not have a position on the national impacts of the FTA on the Australian economy. We have looked at it from our industry perspective but we certainly do not want to see a negotiation end up like a NAFTA for dairy with Canada where it is excluded from the arrangements. It certainly

minimises the potential export earnings, the extra regional employment and other downstream benefits that would flow from an FTA arrangement with the US that incorporates dairy.

Senator JOHNSTON—I suppose it is fair to say, from a Western Australian perspective, that this industry has gone through a very torturous reformation at a producer level. It worries me that we have come this far. Does New Zealand have 700 million litres going into the United States? Is it something like that?

Mr Lavery—It would be something like that. It is certainly substantially greater than anything we have.

Senator JOHNSTON—I am also mindful that Mr Kerr has introduced the innovation and diversification that we wanted from the process in some ways. What are we doing to defend our backsides—if I can put it in those rustic terms—with New Zealand and some states having great excess capacity in this area? If we have an export drive that delivers considerable tonnage into the United States, possibly to the detriment of New Zealand, is there a possibility that we will get instability in our domestic markets and be in for a round of more pain? What are we doing to look at how we handle an increase in export demand, with New Zealand seeing domestic demand increasing onshore in Australia? Are we looking at what is happening with respect to our most optimistic outlook and the flow from this disagreement?

Mr Rowley—The moment we walked into full CER with New Zealand, we had two industries basically of similar size in 1992, give or take a bit, 3½ million people in New Zealand, 19½ million people in Australia, 95 per cent of exports coming out of New Zealand and, at the present time, about 54 per cent coming out of Australia. What I am alluding to is that the New Zealand export price virtually sets the Australian domestic price. I do not see anything that upsets that in a free trade agreement with America. What you are alluding to is that there will be some balances change.

But the real issue for me as an individual producer and for every Western Australian producer is that the manufacturing milk price in Victoria is the benchmark price for all milk produced in Australia. Off that benchmark price in Western Australia and Queensland come other considerations like continuity of supply, quality and no hassle with the process of picking up a phone and chasing milk out of Victoria or New Zealand. There is a benchmark; the benchmark is the New Zealand import parity price into Australia, which is governed off their performance in the world price. If you extend the free trade agreement for Australia but not New Zealand you do not, in my view, alter the equilibrium of the marketplace that I am talking about. You give advantages to Paul Kerr's Murray Goulburn in the specific market-driven specialised products, which relate back to those producers in that process of performing, but the underlying position is import parity in New Zealand, and it will always remain so.

Senator JOHNSTON—I think that is a very good perspective. If New Zealand's exports were damaged through our entry into the market with a bilateral agreement to which they were not a party, would that be a problem?

Mr Phillips—I think you have to understand that most New Zealand cheeses, butters and other than protein products are subject to quotas which will not be affected by an FTA arrangement with Australia because they are built-in commitments under the WTO—so that

trade effect would not be there. With other products—the protein products—there may be some issues in terms of the differential product, but ultimately, going forward, the commercial market price for those would be driven by the international market price rather than the bilateral US market price. We do not think it would have a major issue in terms of New Zealand's commercial position versus the Australian market.

We are aware that the US industry will be very sensitive to ensuring that a free trade agreement with Australia does not create a backdoor opportunity for New Zealand product into their US markets, so they are paying particular attention to the rules of origin of product that would be subject to an FTA agreement. As an industry, we are very aware of that issue and we have been talking with the government negotiators. The key point for us is that we do not want the rules of origin, the rules and standards that are imposed there, reducing the commercial attractiveness of any of the access gains or trade opportunities that may come out of an FTA. So we are working fairly closely with the government negotiators to make sure that those issues about rules of origin can be dealt with in a way that is administratively simple enough so that the companies can take advantage of the commercial opportunities that come rather than making them headline access gains, but where you end up finding the paperwork and administration associated with it reducing your ability to actually take advantage of the opportunity. It is a big issue in terms of the final agreement.

Senator JOHNSTON—Mr Kerr, does your company have an outline of the type of products that you export? I do not know about the other committee members but I would be very interested to see and understand the type of diversity and technological developments your company has arrived at in producing these types of goods, because I am not terribly familiar with them. I would be very much obliged if you could send us a copy of a brochure or something that explains the nature of your products.

Mr Kerr—We do have brochures and information. We can arrange for that to be sent to the committee.

Senator JOHNSTON—Thank you.

Senator RIDGEWAY—Could you clarify your opening comments in relation to your industry being unduly under attack by comparable industries in the US and what seems to be an emphasis on looking at dairy processing products. You mentioned things like caseins, proteins, colostrum and so on. Is that a strategic decision to look at investments in those types of products as compared to, say, what you might be doing in leading destinations like Japan?

Mr Kerr—From our perspective, it is a strategic direction. As we trade in the world markets, we are subject to the volatility of the world market. Prices go up and down for skim milk powders and cheeses—even in Japan. We are a 100 per cent cooperative—our farmers own the company—so we have to look for opportunities to deliver better sustainable returns. In the current corrupt world market that is pretty hard to continue to do. So it is a deliberate strategic direction for us to enter into that market and to focus on the US, the UE and Japan, but at this point in time the US is a more progressive market in that area.

Senator RIDGEWAY—Over the longer term, do you see that as a key part of what business you will be in in the future or would you still be looking at, for example, the export of milk production?

Mr Kerr—Given our volume of production was over four billion litres last year, it is unlikely in the foreseeable future that we will not still be a major player in the value-added dairy ingredients. As our business grows, that market will grow, but you need to understand that it is only a small part of the quantity of product produced but it is a large proportion of the value. So we will still be involved heavily in those other markets.

Mr Phillips—We need to put it in perspective for you. The two single largest products Australia exports at the present time are cheese and whole milk powder. In the foreseeable future, they would stay as the major utilisers of our milk for export. In the case of the US, at the moment we have access for 7,000 tonnes of cheese into a 2½ million tonne market for cheese. We have 0.02 per cent access into their markets. There are no commercial opportunities or flexibilities under the current arrangements for us to develop cheese products for the US. Under free trade, if you had the flexibility, there would be commercial decisions. It is about commercial flexibility and returns from your milk imports—where the best returns are for the various input components of your milk. An FTA would give the companies that much more flexibility about what products they market and where the best returns are for the funds.

Senator RIDGEWAY—That probably partly answers the next part of my question, which is more to do with looking at the value adding products, particularly those products that might be listed, for example, on the current PBS listing, like baby formula and so on. Casein and so on are used in those products. Do you have concerns about some of the issues that have been raised in relation to the Pharmaceutical Benefits Scheme through the way that the media has reported it? Part of your strategy seems to be about presumably offshore investment in milk production and dairy processing. What does that mean to foreign ownership restrictions in relation to your company or members?

Mr Lavery—That is a process that finds its own way. If you take as a guide the closer economic relationship we have with New Zealand, over time they have increased their share of our market. They have now started to make investments in our industry in areas where they find it appropriate. We do not have a big problem with that as long as it is a two-way process. In the case of New Zealand it has not been very two-way, although you can get a bit of chance now. You referred to infant formulations. The American market is a huge market for infant formulations. There has already been one joint venture in this country with Murray Goulburn for infant formulations. There is no reason that a large American company might not come down and seek to do the same. That would mean some foreign ownership, probably in the processing sector, but that is not any threat to the farm sector. Given the strength of the cooperative sector in our industry, it is pretty likely that we will keep a fairly good foot on ownership and control. It will be more in the nature of cooperative arrangements than ownership arrangements. I am talking about the future; these things have a habit of changing, of course.

Senator RIDGEWAY—Thank you for that.

Senator HARRIS—Following on from Senator Ridgeway's line of questioning, in your submission you said that the ADI urges the government to agree on measures to facilitate further

investment in both directions for the benefit of both Australia and the US dairy industries. How would the ADI see this being achieved?

Mr Lavery—We see that coming through the natural commercial process by having the two industries more in touch with each other. Freedom of movement of goods, ideas and probably also people, and increasing trade naturally tends to bring people together. They start talking and the entrepreneurial spark starts working.

Senator HARRIS—My question was more about how you see the investment being facilitated.

Mr Lavery—There is not a specific role for the government in facilitating the investment that an FTA, by creating the opportunities and the commercial flexibility that comes from that, would create. In the initial instance, the discussions are all about what products and services are going to flow between the two parties, but an important long-term impact of an FTA is the integration between the two industries. As Peter has said, the contact makes people think about how they invest, where the most appropriate place to invest is and where they put their production plants. Instead of us sending products to a US firm for it to process, the decision will be made to do the processing in Australia, closer to the original source of the product, but what happens 10 years down the track depends on the commercial environment in which the companies have to operate. That is where they will make their commercial decisions.

Mr Kerr—I think it is fair to say that the FTA would create some certainty of market access. At the moment, we have access to the US but we are under threat from the milk producers over there. They are threatening to increase tariffs and change their subsidy program. We are looking for the FTA to give us certain access into the market. Then the commercial forces will take a role from there on in.

Senator HARRIS—You also made a comment about export competition. Your concern was that the export subsidies not be used in the free trade area or in third markets where Australian dairy producers and exporters have established commercial interests. Can you expand on that? What are the specific concerns?

Mr Phillips—The primary issue with export subsidies in the US is the use of subsidised skim milk power, through programs such as the Dairy Export Incentive Program, and the use of those surpluses in artificial food aid programs. This disrupts the commercial markets. We have significant concerns with direct export subsidies and export credit programs that interfere with commercial prices in the world market. Our companies have to live with the end results of those subsidies. We recognise that the WTO round will ultimately deal with the removal of export subsidies and rules about export credits to get rid of some of the issues there. We put it in our submission to government because an ideal FTA would also address the issue of the US using subsidies in markets that affect us. But, ultimately, our primary target for export subsidies is the WTO round. If you can get some additional commitment out of the US in terms of use of subsidies directly against us that would be a great benefit to us because they do cause commercial disruption in the international marketplace. But we do not see the FTA as the primary focus of that discussion. We want to see the government working on the Doha Round to deliver those outcomes.

Mr Lavery—A discussion on the FTA would give the opportunity to get better coordination of the manner of administration of US subsidies. At the moment, the US administration will tell us they are only selling where it is not commercially damaging to us. That is a view from an ivory tower. If you operate, as we do, on the ground, you know it is having an impact. Apart from the direct impact, there are second- and third-level impacts as these things roll out through the market. We are not pretending that an FTA is going to result in the Americans abandoning their Dairy Export Incentive Program, but we do think that, in passing, we could have discussions which would improve the coordination of what is being done.

Senator MARSHALL—Mr Kerr, assuming the agreement is successful from your point of view, what would it mean to Murray Goulburn? How do we translate the tangible benefits? Are we talking about investment in new plants? Are we talking about tens, hundreds or thousands of new jobs?

Mr Kerr—Certainly in the marketplace it would give investment in new plant and equipment. We are sitting here today with not enough plant and equipment to supply the market into the US in the protein area. We could supply significantly greater quantities than we do today, but we are reluctant to spend the tens of millions of dollars required at this point in time to further increase our production process to gain in that market given the uncertainty of the TRQs on the MPCs, the caseins and the milk proteins. To quantify what that means in jobs and dollars is difficult, as a previous speaker said. Certainly, the dairy industry is the largest employer in rural Australia. It is the largest value added food industry in Australia. I am not quite sure of the employment figures in Victoria but they are significant. Our company employs around 2,500 people, and 3,500 farming families supply us.

Senator MARSHALL—What does it mean for growth? It is one thing to say it increases your opportunities, but does that just mean your profit margin goes up? What benefits will people in rural Australia see?

Mr Kerr—From Murray Goulburn's perspective—we are a cooperative and our margins do not go up—the benefits are that our returns to our farmers go up. As Pat said, the export price is the benchmark for setting prices in the dairy industry. In reality, that is probably Murray Goulburn representing about 40 per cent of all milk produced in Australia—we are the benchmark. If we can increase returns to our farmers, there is a flow-on effect through the rest of the industry. Last year our company exported about 405,000 tonnes of dairy products valued at $1.3 billion. Ten years ago we exported about 100,000 tonnes of dairy products valued at a couple of hundred million dollars. It is difficult to quantify going in, but our business has doubled in the last four or five years and could potentially double again. We export to over 100 countries—the US is only one of those. We see that as a significant benefit to the Victorian and Australian economy.

Mr Lavery—As Mr Kerr says, it is very difficult for him to measure jobs and that sort of thing, but maybe we can look at the opportunity. We have an industry which is producing 10 billion to 11 billion litres of milk at the moment. We sell into an international market which is rated at somewhere around 30 billion to 35 billion litres. The US free trade agreement would put another 75 billion litres on the size of that market, and it is a remunerative market. It depends on what goes on in international pricing and what comes out of WTO, but I think from those numbers the opportunity is obvious.

CHAIR—The distinctive feature of your company is that you are a vertically integrated cooperative as well, so you are not just a producers' cooperative, you are a processor and marketer of brand names.

Mr Kerr—Yes.

Mr Phillips—And that would be the case for 70 per cent of the industry. So Murray Goulburn's example would be the most common for the industry.

CHAIR—And in this bilateral agreement at least the vexed issue of geographical indicators does not necessarily raise its head.

Mr Lavery—On that issue we are on side with the Americans—about 98 per cent, I would say.

CHAIR—Thank you all very much.

[12.38 p.m.]

BELL, Mr Stuart, Finance Manager, International Markets, BHP Steel Ltd

GOODWIN, Mr David John, Executive Vice President, Corporate Affairs, BHP Steel Ltd

CHAIR—Welcome. Thank you for being patient, Mr Goodwin and Mr Bell; I apologise for calling you later than your appointed time. You have been in the audience for a while, so you know what the committee's approach is. Please go ahead with your opening statement.

Mr Goodwin—As I am sure you are aware, BHP Steel is Australia's largest steel company and one of Australia's newest publicly listed corporations, having been spun off from BHP Billiton in July last year. So, though a new company, we have a long history as a manufacturing company and exporter from Australia, having been in the steel industry for about 88 years. We are now completely separate from our former parent, BHP Billiton, though sometimes we encounter audiences who have not noticed our public listing. My responsibilities cover government relations and public policy issues for my company as well as a host of other communications activities.

With me is Mr Stuart Bell, who, as BHP Steel's Finance Manager, International Markets, has responsibility for all financial and commercial matters for sales into international markets. Last year he project managed BHP Steel's response to the United States investigation under section 201 of the Trade Act into its steel industry issues and its subsequent introduction of tariffs upon steel imports. That is a topic we think may be of interest to this committee, as may our experience over the past year and a half in dealing with dumping and trade actions in a range of other countries. In past roles, Stuart has managed sales offices and operations around our overseas network of businesses and has spent considerable time living and working in Asia.

This year BHP Steel will export steel products with a total value of over $A325 million to United States markets. We export nearly half of the five million tonnes or so of steel that we manufacture each year in Australia. A sizeable proportion, over 600,000 tonnes, finds its way to US customers. Eighteen months ago, in the midst of the US section 201 process, we feared that those sales and customer relationships were at risk by virtue of the potential for US tariffs to be applied in significant numbers to our products. That situation raised major risks for our company's level of profitability, for our ability to find quality markets for our production and for employment in our communities around our major producing centres, particularly Port Kembla in New South Wales and Western Port here in Victoria. In order to understand the background to the US action, it is necessary to appreciate the parlous state of the US steel industry during the year 2001. Global overproduction of steel and soft demand had led to 20-year lows in steel prices. The US industry, as a result of some structural weaknesses, including relatively high labour costs and high unit costs for raw materials, was finding itself uncompetitive. The integrated US steel mills are at the top end of the US international cost curve of steel companies. More than 30 US steel companies at that time were in chapter 11 bankruptcy, and the industry was struggling to find the resolve to rationalise itself and close inefficient capacity. The fact that the inefficient facilities were concentrated in electorally sensitive states meant that a political

solution was desired, and President Bush initiated section 201 safeguards action to protect the US steel industry.

The US government's section 201 investigation aggregated imports of Australian steel tonnages into the US with those of other countries and found that, considered in aggregate, steel imports were causing injury to the US industry. That was the first stage of its analysis. A lengthy process then followed to consider what remedies were appropriate to protect the US industry. Foreign producers such as ourselves were able to engage in the consultation process on remedies. This exercise involved considerable effort by a large number of executives from our company and representatives of the Australian government, in particular our Washington embassy through Ambassador Thawley and his team. The outcome of the overall process, which was announced in early March 2002, was that for most countries and products across the board punitive tariffs, at an initial level of 15 to 30 per cent, were applied to US steel imports. The initial outcome for Australian and for BHP Steel was only partially satisfactory. Our largest single product group, which is steel slabs, was not subject to the tariffs but was covered by a tariff rate quota. However, under the initially announced arrangements a wide range of our other products were subject to the 30 per cent tariff. Some intense last minute negotiations and lobbying then delivered an outcome whereby an additional 250,000 tonnes of our hot rolled coil product were exempted from tariffs.

The final wash-up was that exclusions from the 30 per cent tariffs were secured for over 600,000 tonnes of slab and hot rolled coil exported to the US by our company, and there have also been other exclusions granted in smaller volumes to other Australian steel companies. We successfully argued at that time that Australian steel exports were essential inputs for manufacturers in the US and should continue to be tariff free. The exclusions granted to Australia have enabled BHP Steel to continue supplying our longstanding US West Coast customers with critical volumes of Australian steel feedstock over the past 12 months. The lobbying efforts succeeded for a range of reasons, including the fact that we were able to demonstrate that Australia's steel industry had already undergone significant restructuring in the 1990s and earlier to reduce capacity and enforce greater production discipline. This was particularly the case with the closure of BHP Steel's Newcastle steelworks, which was concluded in 1999.

The fact that Australia was able to argue for and negotiate these levels of tariff exemptions is evidence of the strength of Australia's trade and diplomatic relationship with the US. Furthermore, the experience in steel shows how Australians can succeed when negotiating with US counterparts on trade issues, which is why we do not agree with the sceptical view some people have been expressing that, in these FTA negotiations, somehow American negotiating muscle will prevail over Australian naivety or good will. However, the tense and fraught situation we were in at that time is not an experience we wish to undergo every three or four years. We cannot discount the potential for future trade actions against steel, given the ongoing difficulties and political sensitivity of the US industry. We are looking for a framework of the maximum possible certainty in our trade relationship with the US and believe an FTA can deliver that.

BHP Steel strongly supports the initiative to negotiate an FTA with the United States. An FTA can secure better access to the US market. Along with many other commodities, steel exports face an ongoing threat from the imposition of antidumping, countervailing duty and safeguard

measures. In our submission we have itemised some examples of clear gains we believe are potentially available from a steel-specific point of view in this area. For example, firstly, we hope an FTA can offer respite from the threat of sudden retaliatory trade restrictions, which are permitted under US trade law. Canada and Mexico enjoy those benefits under the NAFTA agreement, with special treatment in safeguard injury determinations that prevent their exports being cumulated with those of other countries. We can seek benefits similar to that. A second example is that other FTAs the US is party to, such as those with Israel and the Caribbean nations, provide for stand-alone injury findings in antidumping or countervailing duty investigations. Thirdly, an FTA with the United States could provide better mechanisms for dispute resolution and appeals in trade disputes than are currently available—for example, similar to those under NAFTA. Fourthly, since the mid-nineties, Australian painted and coated steel products exported to the US—the Colourbond product, for example—have been subject to antidumping duties. We are keen to see a provision that obligates the United States to revisit such existing injury determinations on a stand-alone basis. This might result in termination of some existing restraints on our exports and open up new opportunities.

I should add that BHP Steel has significant manufacturing and technology investments in the United States. We own 50 per cent of a large steel minimill in Ohio, which produces 1.4-plus million tonnes of steel each year. We also have an interest in a steel technology joint venture company with a US partner, developing new steel casting technology. We therefore have an interest in the potential for an FTA to lead to increased labour mobility between the two countries and to facilitate two-way investment flows.

In my comments today I have focused on the benefits of an FTA for steel, but the benefits are equally compelling for Australian manufacturing generally. Bilateral trade between the two economies today, as Mr Oxley pointed out earlier, reflects a broad, diverse relationship, including significant Australian exports of manufacture, such as chemicals, office and telecommunications equipment, and motor vehicles and parts. If we regard wine as a manufactured product, half of our exports to the US are now manufactures. The US has recently become Australia's largest market for elaborately transformed manufactures. The benefits to the country do not hinge solely on increasing market access for agricultural products like beef, dairy and sugar, notwithstanding their importance. Australian manufacturing has benefited from over a decade of sustained reform. In many sectors we are as good as any in the world. A well-negotiated FTA between Australia and the US will provide a further boost to manufacturing by providing access to a market of over 200 million people and by fostering innovation and best practice. We would be happy to take any questions.

CHAIR—Thank you, Mr Goodwin. The point that Mr Oxley made, which is appropriate, is that it is basically a reasonably open economy anyway, and what we are talking about is removing what are, by world standards—in the manufacturing sector anyway—not great impediments but, nonetheless, impediments. I congratulate BHP on being able to lobby successfully in the United States to prevent the section 201 impact adversely affecting its company. You are value adder of Australian mineral products, and that is a good thing.

My concerns at the national level about the use of 201 in the steel industry arise notwithstanding your success, because a number of my constituents from Western Australia work in the mining sector and provide input commodities to steel manufacturers elsewhere in the world that have been discriminated against by the 201 action. That has an adverse impact on jobs

and profits for those companies. So we are not out of the woods, but it is a good thing that you largely are. As a significant Australian employer, in your new personality as BHP Steel, do you support that part of the US claim against Australia that includes Australia signing up to ILO core labour standards?

Mr Goodwin—Your question is around the fact that a request for Australia to sign up to those standards has been placed on the table as part of the US negotiating position?

CHAIR—Yes.

Mr Goodwin—I must admit that when we encountered that we found it interesting that this is a different type of negotiation for the United States than it to date has had in most of its FTA negotiations, where I believe it might have seen itself as being in the position of coaching the rest of the world on an uplift in terms of labour issues. When the negotiators came to Australia four to six weeks ago, I think they encountered a reasonably sophisticated system here that is a complex system. I know that there is a process they need to go through under their trade promotion act to verify the labour standards that are being adhered to by countries with whom they are making FTAs. So my consideration of that issue has been premised on the assumption that they would find Australia to be in reasonable shape in the area of labour laws.

CHAIR—We would probably be in advance of them.

Mr Goodwin—Yes. So it is certainly a flip-over from the Caribbean, Jordan—

CHAIR—Morocco, Singapore.

Mr Goodwin—Chile et cetera. So it is not an issue that we have really focused on, and we have not articulated a position on it. Is there a particular concern that Australia should be engaging on that issue, from the feedback that you have been receiving?

CHAIR—I would make two points in response. One is that we have not in the past embraced trade agreements that have specifically included clauses on the environment or core labour standards, and both are involved here. Originally the United States had those provisions outside their agreement, in the case of NAFTA; but, since NAFTA, they have included them as a standard inside their agreements. My second point goes to the issues themselves. It is unclear what the government's view of this will be. It was reported in the *Australian* earlier this week, by an unnamed source, that they were not disposed to include it, although it is clear that the US Congress, which has the final up and down vote on this, expects to see labour standards in US agreements, and the letter Zoellick gave to the congress saying what his negotiating purpose was included that it was to achieve this. So my question, framed more directly, is: do you have any objection to it?

Mr Goodwin—The AUSTA submission, which we are a party to, stated that the group did not support the inclusion of provisions around labour and the environment in an agreement of this sort. I think that we would subscribe to that position.

CHAIR—Let me take it to the next stage. Clearly, the Americans are insisting; the Australian government's position might be ambiguous; and you are opposed to it. If it were the make-or-

break issue, is your opposition such that you would not want to proceed with the agreement? Or, if it were the make-or-break issue, is it something that could then be embraced?

Mr Goodwin—If it were the make-or-break issue, the question is reasonably hypothetical. We have the kinds of interests that I outlined in my opening comments around safeguards and, particularly, market access. We are keen to see those elements included in any eventual agreement. If part of the trade-off on the table were an American position around those issues we would form our view at the time, but we would be very enthusiastic about seeing an agreement concluded if it included the sorts of provisions that we are most focused on.

CHAIR—Would that answer apply equally to environment as it applies to labour standards?

Mr Goodwin—Yes, it would. Again, we are not closely focused on those environment provisions.

CHAIR—Mr Goodwin, you have put quite a sophisticated submission to the committee. Looking at BHP Steel's interests, they cover a range of motivations. From reading your submission, my impression is that the main motivation, but not the only one, is that you want shelter from punitive action against you, such as the possibility that arose under the recent section 201 issue, and that what you are looking for out of such an agreement is that sort of protection. Is that a fair comment?

Mr Goodwin—Yes, I think it is. To elaborate on that, Mr Bell might be able to comment on the environment in which we have to export into the US market. It is a system that is not dominated by tariffs to which we are subject—that is, pre the section 201 special tariffs. The general tariff position is not the issue. The issue tends to be more around the aggressive use of trade actions and the like as part of the fabric of the system.

Mr Bell—Our position is that anything that would support free trade or that would not disrupt our industry, particularly trade steel flows, is important. By continually using trade actions against steel products, the United States disrupts the world flow of steel. Whether it is from the European Union to the United States or the United States into Japan or Korea, every time they raise an action it creates severe disruption in their industry, not just for the importers of steel into the United States but also for the consumers of that product in the United States.

CHAIR—I understand, too, that Southcorp have a similar concern. There they were sitting around minding their own business, conducting a commercial relationship—a very successful one—with the United States, exporting Australian wine, and the US arguably and, I think, correctly held that Australia was in breach of its trade obligations when it came to banning Canadian pork, some of which originated in the United States. Then, as they are entitled to under the WTO, they said, 'We'll take punitive action and we'll knock off the wine sector which will hurt Australia and cause it to then bring itself into line on the pork issue.' That is a situation that happens all the time in world trade. I can understand it and sympathise with the sudden panic that occurs in a company which is not associated with the dispute in any way, shape or form—sitting there minding its own business, conducting a very effective commercial enterprise, and suddenly it hears that its major market might slap a punitive tariff on it for no fault of its own.

Mr Goodwin—Our interest and that of Southcorp are fairly closely aligned. We are both members of the AUSTA group and we are both in dialogue with the members of the negotiating team as they develop their position on these sorts of issues.

CHAIR—You are aware that you do not need a full-blown free trade agreement to achieve this, are you?

Mr Goodwin—There are a number of forums through which we are seeking to do something about these issues. There are multilateral forums as well as the bilateral forums. Under the auspices of the OECD, there has been a process under way for close to two years—it was prompted by the US 201 action—where OECD nations plus other countries such as India are engaged in discussions with a number of other non-OECD countries such as the Ukraine and Russia. Those discussions have sought to make progress on two fronts: firstly, to achieve a reduction in the overcapacity that has existed in the world steel industry, in particular the excess inefficient capacity, and to make sure that that capacity is closed, and closed finally, as soon as possible; and secondly, to explore the possibility of an agreement for eliminating subsidies around steel, which is an adventurous aspiration.

There has been good progress under the OECD umbrella, and some talk of that process shifting into the WTO process later this year. It remains to be seen whether that transition is effected. We have been heavily engaged in the discussion. The club of major steel companies in the world, the IISI, the International Iron and Steel Institute, of which our chief executive is deputy chairman, has also been seeking some processes to create a bit of momentum around those issues. On a further bilateral note, we have been quite engaged with other countries in our region in Asia, who have been introducing their own safeguards, actions or short-term tariff arrangements, effectively as a response to what has gone on in the US. Mr Bell has been actively involved in all of that, as have I. We are trying to pull all the levers that are available to us to maximise our market access and avoid these distortions.

CHAIR—You are probably aware that the OECD undertook a similar thing when it came to shipbuilding subsidies. Unfortunately, that collapsed because the US Congress twice rejected a reduction in protection for its own industry, thus justifying the return of protection in North Asia and in Europe and adversely affecting our ability to compete. But I hope that process is successful.

Senator HARRIS—In your submission you speak about the imposition of antidumping countervailing duties and safeguard measures. What would BHP look for in the FTA to reduce their exposure to that type of threat?

Mr Goodwin—We probably went into some specific details in a part of our submission that was drafted with the assistance of lawyers for the benefit of the government. These dumping and other determinations tend to proceed in two stages, the first stage being an assessment of injury: has there been injury caused in the US market to its industry? The rules around how injury is established are quite complex. It can be done by aggregating the imports coming in from a range of countries. If you conclude that, yes, all of that adds up to 20 per cent of the market, then it is determined to be causing injury. Alternatively, the assessment can be done on a country specific basis, as it is for Canada under the existing NAFTA arrangements. They might find that Canada is supplying three per cent of the market—perhaps it is more than that—and they might get a

negative injury finding at that stage but they will not proceed onto the remedies phase. The way in which we are assessed, whether it is in our own right or our volumes are added to together with others, such as the Ukrainians and the Koreans, and their volumes going into the US, makes a big difference to the threshold.

We have some specific suggestions about what might be done based on other precedents we have seen in other FTAs. Secondly, when you then proceed into the remedies phase, there are some other mechanisms that potentially can be applied there. The other area is dispute resolution and mechanisms for review of decisions that might be taken, say, by the United States, to put in place arrangements that could help Australia to have reviews done of adverse or erroneous findings.

Senator HARRIS—You also make the comment that if the FTA between Australia and the United States were negotiated you would therefore urge the Australian government to pattern the provision regarding safeguard measures on the NAFTA model. Putting aside the safeguard measures, what would your position be in relation to a section 11 or something similar? Would you support that, or do you think that could be used adversely against BHP? We are being told that it is construed that a corporation can actually sue a country. Could you see any way that a country could, in the reverse, sue a corporation?

Mr Bell—In the steel industry we have had a situation where, as a result of the United States imposing dumping duties on separate countries, the Unites States have been reimbursing the steel companies that have suffered as a result of alleged dumping. We certainly do not think that is appropriate. We do not see that there should be a mechanism for a country to prosecute an individual entity or company as a result of its behaviours.

CHAIR—I think they would just tend to impose tariffs on you, without leaving it up to a judge to find out whether you are right or wrong.

Mr Bell—The biggest impact, particularly around anti-dumping, is where the United States has the potential to impose tariffs retrospectively. So, up to the point in time where you have a decision, there could be 12 or 18 months of saying, 'We know something is going on, but we don't know what the impact of it would be.' Until they actually come up with a determination, you could be running anything from 'we do not believe there is any injury or impact' to maybe 20 per cent or 50 per cent or 150 per cent, depending on what the allegations are. That certainly has a severe impact on an industry like ours.

Mr Goodwin—It means that you have to hedge your trading position during that period of time against the risk that there might be a financial penalty applied retrospectively.

CHAIR—Where do you see your main offshore markets? Is it the United States, or are there other markets around the region—Europe, Latin America or Africa?

Mr Bell—We have a very wide geographical customer base. Our spread is pretty much in four geographical areas. It is very much between 20 and 30 per cent in each of them. North America is about 30 per cent, North Asia is around 30 per cent, South East Asia is around 20 per cent and Europe is about 20 per cent. So we have a very wide customer base.

CHAIR—Do you have a view about which of those markets has the greatest growth potential?

Mr Bell—I think there is no question that the North Asia-China-Vietnam region has the highest growth potential. If you look at a country like China, you will see that two or three years ago they were producing 100 million tonnes of steel. In 2001 they were doing 159 million tonnes. Last year they did 206 million. They are predicting that by the end of 2010 they will be producing 359 million tonnes of steel.

Mr Goodwin—That is production, but underlying demand is probably stronger than the production increase.

CHAIR—It is outstripping it.

Mr Bell—Yes.

CHAIR—One of the arguments that we have before us is, of course, the argument about preference and diversion and the argument that, by doing a US free trade agreement, the view may be taken in our high-growth Asian markets that we are cuddling up to the United States and neglecting them and that, by providing preferential access to our own market to the United States but not to them, we are discriminating against them. As a consequence, they may be disposed to return the discrimination against us. Since this is an area of high growth and strong export for your company, how do you react to that argument? Does it worry you?

Mr Goodwin—Stuart's comments about those different markets and the relativities are directed towards where our Australian manufactured tonnages go, but the primary growth region for our company is actually South-East Asia, extending up to Vietnam and China. That is the area in which we have been, over the last 10 years, progressively building in-country manufacturing operations which often take feedstock from Australia. You would be familiar with the strategy of international trade where you start off by exporting, then put relatively low-cost in-country manufacturing operations in place and then, when a sufficient scale is reached, place a larger investment in the country. That is really the model that we have deployed successfully in Malaysia, Indonesia and Thailand. We are an in-country operator in 10 or 12 countries in Asia, and in some of those countries we have hundreds of millions of dollars of capital invested. So our perspective is that of someone operating within the system in those countries as well as exporting to those countries. I think I agree with the comments I heard Mr Oxley express earlier, that within ASEAN and the extended ASEAN region there is certainly a lot of bilateral conversation going on. We are engaged with some of that. We are benefiting from some of the intra-ASEAN trade opportunities that exist. We do not think that Australia pursuing a bilateral relationship of this nature with the United States will adversely affect our aspirations in that part of the world. Would you agree with that, Stuart?

Mr Bell—Yes.

CHAIR—We have just seen China and ASEAN announce that they are going to do a bilateral free trade agreement between them. And we have seen the emergence of ASEAN Plus Three—the ASEAN bloc plus Japan, Korea and China—from which Australia is excluded. We have often used our diplomatic clout to try and break into that arrangement, but we have always been

excluded from it. One of the arguments here is that the world is breaking up into major trade blocs. The Europeans have just extended membership of the EU to pick up the old middle European countries. NAFTA has gone north and south, and now NAFTA is going to the whole of Latin America in the Free Trade Area of the Americas process—it has cherry-picked Chile out of that. In Asia we have China, which is the emerging superpower, Japan, which is an economic superpower but is wallowing at the moment, Korea and ASEAN forming a bloc. Australia is out of that.

This argument continues on that, for a country like Australia, the transactional costs of doing business in each of these blocs—because the regulations are different, rights of entry are different, internal subsidies and provisions favour the members in the bloc—make it harder for Australia to succeed at export. We most frequently see the rivalry between the blocs in the transatlantic debate between the EU and the United States more than anywhere else—and on trade matters that is a very prickly relationship. It may be different on other matters, but on trade it certainly is a fairly stern and prickly relationship. Do you have a view about this in terms of your own company's growth strategy, that in the end it means that Australia has to join one because otherwise it will be excluded by all?

Mr Goodwin—Our strategy as a company is to have well-established positions within each of those regions, founded on the operations that we have in some cases but also on the relationships we have with customers. Our strength is not the trade construct but the relationships we enjoy with those customers. We approach it that way. We are also developing our position, as I said, within ASEAN in particular and in the growing economies that form, in effect, the expanded ASEAN. To us, it is critical that we have high-quality relationships in all regions. We do not see the particular issue of the bilateral agreement with the United States dislocating that.

CHAIR—No. But I am looking at it from the point of view of the Australian national interest. As I understand your answer, your strategy for dealing with this is to locate the value-adding component of your business in the market—and not in Australia—and to supply that market with low value added or poor commodities.

Mr Bell—I disagree with that.

CHAIR—I understood you to say that, in the case of China and your other markets, your strategy is to develop your business—which is not a warehouse but is actually a value-adding business—there. Perhaps I am wrong about that. The question about net value to the nation is: where is the value adding done? We are stuck with this whole argument that says we are a quarry, a farm and a big, broad, sandy beach for tourists—and nothing much else. It was not your company, but another major company in the resource commodity area invested a huge amount of money in R&D, with Australian government subsidies, to develop a new process in steel making so that they could set that up in China and be assured of a market for their iron ore. From a national perspective, many might argue: why don't we make the steel and sell them the finished product and get the value-adding component added to our economy?

Mr Goodwin—It is important to remember we are also developing our business within Australia. Demand in the Australian domestic market is very strong and has been for some time. We are not executing a replacement strategy here; we are actually having to grow our service offerings and our capacity to keep pace with the demand for our products in all of our markets.

In those Asian markets, it is important to have some finishing facilities close to customers in the markets. What we are doing, in a lot of cases, is drawing feedstock for those from other steel suppliers internationally and not necessarily just from Australia.

CHAIR—Some of those governments insist on you having, or encourage you to have, some finishing facilities in their country.

Mr Bell—Essentially, it is a commercial reality. That is what you have to do to be able to service the market. There has been a lot of government support for in-country manufacturing and support not necessarily from Australian investors but from investors in those other countries. Where they do have a quality product that we can source, it makes economic sense to do that.

CHAIR—We do not have any further questions. Thank you for your submission and your participation here today.

Mr Bell—Thank you.

Proceedings suspended from 1.19 p.m. to 2.32 p.m.

LLOYD, Professor Peter John (Private capacity)

CHAIR—Welcome. We have received a written submission from you. I invite you to make an opening statement on that submission, and then take questions from the committee. The floor is yours.

Prof. Lloyd—Thank you very much. The negotiation of a US-Australia free trade area will mark a further step in the trade policy of Australia by quite significantly extending the number of regional trading agreements we have. All such regional agreements are by nature discriminatory. Some people are opposing the negotiation of this agreement on the grounds that it is discriminatory; some are opposing it on the grounds that some of our major Asian trading partners might be offended by this apparent shift in the direction of Australian trade. My own view is that both of those grounds for opposition are incorrect in principle.

There is a very strong movement in all areas of the world towards regional trading agreements. It is extremely strong: there are virtually no members now of the WTO, apart from China and Taiwan, who are not already members of one or more regional trading agreements. One argument for joining this movement is a defensive one: if we are excluded from markets in the sense that we do not get the same access as other members of preferential agreements, we ourselves will be disadvantaged. As for the argument that some Asian countries might take offence, I do not see that happening because all of them, again with the exception of China, are currently negotiating one or more such regional trading agreements. Everyone is doing it. However, as I indicated in my submission, I think that by strategic diplomacy we should make it apparent to those trading partners that we are not seeking to downgrade our relations with them and that we are willing to engage in similar negotiations with them when it is mutually suitable.

As to the choice of partner, the United States is our most important trading partner in trade for goods and in trade for services. In the movement of people, it is the only major country in the world with which we have a net outward movement—more Australians are moving permanently to the United States than Americans are coming here. As far as investment is concerned, the United States is by far the most important source of foreign investment coming into Australia and also the most important destination of Australian direct foreign investment.

Also, the United States is engaging, as you well know, in a massive negotiation with some 34 other countries in the Free Trade Area of the Americas process. If that comes about—and at this stage it looks as though it will—we could be at a significant disadvantage, vis-a-vis countries like Chile and Argentina, for a wide range of agricultural, mining and manufacturing products.

As to the terms of the agreement, I have indicated that it should be as comprehensive as possible. It should cover trade in goods. It should certainly cover trade in services. It should, in my view, cover foreign direct investment and the temporary movement of labour. It should have a minimal bureaucracy and be modern in its orientation. Recent regional trade agreements have incorporated features that previously were not common, like provisions relating to e-commerce and information technology, and we should aim for that. We should seek rules of origin which are as unrestrictive as possible. We should seek safeguards that are minimal and not product specific or industry specific. We should try to persuade the Americans to adopt a prohibition on

antidumping duties against us as partners of a regional agreement, similar to that in an agreement signed between Chile and Canada about two years ago.

Market access for goods is probably the single most important aspect of the agreement. In my view, we should aim for completely free trade here. I do not think completely free trade is achievable with the Americans at the moment, but a goal of zero tariffs on all goods, including agricultural goods, may be achievable. Other features will be subject to negotiation. We should pursue the elimination of tariff quotas but we are unlikely to achieve that on a bilateral basis.

There are many other features that I cannot say anything about at the moment, but I would like to make very brief comments on four or five of them. We should be prepared to make what are seen as concessions—which in my view are changes of policy—in relation to foreign direct investment rules, quarantine and single-desk marketing. However, there are some American requests which I do not think we should accede to. I personally would list two. One is that we should try to maintain the television content plans, and I would be happy to talk more about that. The other is that we should resist strongly any American attempt to persuade us to change our policy with respect to parallel imports of copyrighted goods. If we can achieve satisfactory negotiations along those lines, and I would be happy to say more, I believe that such an agreement is desirable.

CHAIR—Thank you. In this debate over multilateral and bilateral—with the question: which is the best way to proceed?—Australia has over the last decade or even longer been committed to the belief that the multilateral approach is by far the best. Most recently, official thinking has converted to favouring taking all steps—which is another way of saying: to open the door to aggressively pursue bilateral trade agreements.

As you are aware, and you refer to it yourself, there is a debate about what is the best way to go, and that debate is open. I think your paper could be taken as arguing that aggressive bilateralism is a positive way to go, which is not to say that multilateralism is wrong but it is to say where the balance of effort should be. I can see that you are nodding, so I guess we are still in agreement at this point. Accepting that view, if you look at the world from Australia's national interest point of view you could make this observation: most of our exports go to Asia, our fastest-growing markets are in Asia, and you could also argue that the best prospect for increasing our exports is in that region of the world, given the growth rates in China and so forth, even though there is a sluggish economy in Japan. So if you accept the view that the day has dawned for aggressive bilateralism, why do we not pursue it with Asia? Why do it with the United States?

Prof. Lloyd—In my view we should do it with both; I do not see them as exclusive. I think we should continue to press for negotiations with ASEAN in particular. As you know, ASEAN and CER have been engaged in a dialogue. There was an investigation and the task force recommended it some four years ago. I think we should seek carefully and diplomatically to revive those negotiations at a suitable time. But at the same time we can pursue bilateral negotiations with the United States and possibly some other parties. I do not see them as exclusive; moreover, if we do more simultaneously, the dangers of having our trade diverted or turning our back, you might say, on important markets are reduced.

This is a strategy that a large number of countries are now following; it is a fairly recent development. A country like Mexico, for example, has the record, with more than a dozen agreements already with almost all of its major trading partners, including the European Union but not including Japan. Chile, Canada, Singapore, New Zealand and a number of other countries are pursuing the strategy, so it is not a peculiar strategy these days—in fact, it is becoming quite an important strategy. I agree that it would be better if trade reductions, tariff reductions and other trade liberalisation measures were conducted multilaterally. But the multilateral negotiations are progressing very slowly and there is still a serious risk that they might not eventuate, although I think that is probably pessimistic. I think we would be unwise to rely on multilateral negotiations and to withhold from bilateral or regional negotiations.

CHAIR—I accept your point that we could do both together, that they are not exclusive. But when it comes to where we put the balance of our effort to achieve the best results—people might want to argue this point but I do not think it really is arguable—there has been a very strong effort by the Australian government to convince the United States that we should do a bilateral agreement with them. I think it is a strong point—and, again, people may contest this point, but I think it is a strong point—that nothing like the same effort has been put into convincing, for example, China or, after Prime Minister Koizumi's visit to Australia last year in which he opened the door to a regional trade arrangement, Japan. As a consequence, if you like, we have exercised a positive choice by voting with where we place our effort, which may not be logical in terms of the economic self-interest. Is that a view that you might wish to comment on?

Prof. Lloyd—I do not quite hold that view myself. Australia did make a very considerable effort with respect to ASEAN. That was our first preference and is probably still our first preference, but the door was shut by Mahathir, in particular, and also by some opposition from Indonesia and the Philippines. I personally think we managed those negotiations badly, but there is probably no point in pursuing that issue.

An agreement with China would be very advantageous, but China has signalled that at the moment it is only really interested in talking to ASEAN countries. I doubt whether China would be very receptive at the present time to a bilateral approach from Australia. Japan might be, and that is something we should certainly look at. I would like to see us pursue ASEAN, Japan and the United States which, I think, are all possible.

With regard to the United States, the timing now is more propitious than it has ever been or is ever likely to be, partly because of a combination of national security and other political circumstances—September 11, Bali and Iraq. We are more likely to get a favourable outcome now from negotiations with the United States than we were in the past or we probably ever will in the foreseeable future.

CHAIR—Would you say, therefore, that more effort than is obviously being made should be made with Japan?

Prof. Lloyd—Yes, I would. I think we should certainly pursue Japan.

CHAIR—I take your point about the quality of our effort, which has been a continuing one over many years, dating back to 1994. It is really about CER and AFTA being linked in some way.

Prof. Lloyd—Yes.

CHAIR—I take that point. There is an argument around that one of the initial drivers motivating the government with respect to the United States is security interests rather than economic interests. On the security front, we have a common view. We are in an alliance. People might wish to debate how independent we are within that alliance, but that is another matter. We are in an alliance; that is clear. The areas of conflict in our relationship, historically and currently, are on the economic or trade front. Since this concept was born out of the 30th anniversary of ANZUS, what else can we do to deepen and strengthen the relationship? There is this argument that one of the primary drivers is the security relationship. From the United States side, one of the key drivers of their decision to aggressively seek bilateral trade agreements—starting with Jordan and Morocco and then working their way around the world to Chile and Singapore—is that they are seeking to use their economic strength for security purposes rather than for selecting partners of economic advantage to the American economy. The underlying argument here is that we are being drafted on a security basis rather than on a fairly objective analysis of the genuine economic interest. Do you have a comment on that?

Prof. Lloyd—Yes. It is true that security matters are important, and I am in no doubt myself that our current close security and defence links with the United States are part of the reason why the United States is more receptive to negotiating a free trade agreement. However, I would note that the present government initiated, or sought to initiate, negotiation of a free trade agreement with the United States before September 11, Bali and Iraq.

CHAIR—That is true.

Prof. Lloyd—And, of course, ANZUS long predates those. I think from the Australian point of view the concern has been with trade itself, particularly with market access for agriculture and a few other products from some manufacturers—mining, ferries and things like that. As a trade economist, I get very nervous about links between trade and security or trade and defence or other things which are not closely related to trade, because they can distort the kind of agreement that comes out of it. But in this case I think it is working in our favour from a trade point of view, and security matters are not going to be part of the agreement in any significant sense. I think we should proceed with the negotiations for those reasons.

CHAIR—I think your point is sound. But this began before the question of terrorism, before 9/11, although the argument is that it coincides with the ascendancy of the Bush administration. If I could couch it in journalese, the argument is put that the Neocons in the White House always had a view to try to wrap their alliance together on a trade matter to strengthen America and the security alliances that way. Because of those other events we have seen a strengthening of the view, but that view was always there.

Taking note of your remarks about multilateralism, the *Economist* magazine—I forget which month or week it was last year—devoted an edition to multilateralism versus bilateralism and editorialised strongly that the flowering of bilateral trade negotiations around the world has, I think using their phrase, ‘sucked the oxygen out of the multilateral negotiations’, stalling those while nations divert their attention to bilateral trade agreements, which at the end of the day reward their economies less than if they were to pursue the multilateral argument. That was the main theme—and I am sure that you are familiar with this debate.

The *Financial Times* has written this story as well and my own view is that it is a very strong and compelling argument. Therefore, if we are to accept the doctrine of aggressive bilateralism by putting our balance of effort there, we reduce, or in fact veto, our chances of success at the multilateral level. That is the argument, as I understand it. Your paper suggests that you are not convinced by that argument. Would you like to elaborate?

Prof. Lloyd—Yes, I would. That is an old argument. The WTO itself and the OECD, for example, have both looked at this over the years and they have generally concluded that bilateralism up until that time had not interrupted the progress of multilateral negotiations. Let me point out one very important link between bilateral or regional agreements on the one hand and multilateral agreements and what happens at the WTO on the other. Many of the major innovations incorporated in the WTO in the last round, the Uruguay Round, had precedents in regional agreements. In fact, the most important one of all is GATS. Before the Uruguay Round there was very limited provision for trade and services—there was nothing multilaterally and very limited agreement in the regionals. The European Union was the only one that had really sought to do anything. But the Canada-US agreement, which was concluded before the Uruguay Round was completed in the relatively early days of those negotiations, in particular had many of the provisions and the distinction between alternative modes and so forth, which were pioneered in a bilateral agreement and later formed an important precedent that was adopted and expanded in GATS itself.

One can find many other examples. An obvious current example, for better or worse, is the investor-to-state dispute settlement procedures which the United States has incorporated in all of its recent agreements, and it may ultimately find its way, for better or worse, onto the multilateral scene. I say 'for better or worse' because opinions on that particular subject vary strongly. The European Union is adamantly opposed to any investor-to-state dispute settlement procedures in either the regional agreements or the multilateral scene. Nevertheless, it is true that regional agreements have pioneered a lot of new modalities and new areas—e-commerce being one. There was nothing in the Uruguay Round, nothing at all in GATT 1994, relating to e-commerce itself. There is an information technology agreement, which is somewhat different, relating mainly to telecommunications and so forth, whereas a number of regional trading agreements concluded in the last three or four years have e-commerce provisions.

The standard argument used to be—and for many people still is—that you can do both. The obvious risk is that the energies, if you like—not so much the possibilities, but the energies and priorities—of national governments might be diverted regionally. I do not think that is the cause of the troubles in the Doha Round. The Doha Round is running into a lot of trouble, but not, in my view, because of the regionals. It is because the agenda is so broad and the issues involving developing countries and agriculture are so difficult that they are just not getting on top of them.

CHAIR—In your head remarks, or in some of your other comments, you said that the multilateral round now is slow and may not happen, which seems to suggest that the argument that oxygen is being sucked out of it may be true. You make the comment now that the original agenda may have been overly ambitious and the timetable imposed—on itself—for the round may have been particularly ambitious. That would certainly appear to be the case coming up to the Cancun conference later this year—that we are behind schedule in just about every sector and cannot seem to generate the momentum to catch up. Against that, there is the cynics' point of view on trade negotiation—that things are always bound to get worse before they get better, that

the shape of the international economy is not all that flash and that at G-8 level or some level such as that where thought is given to the health of the global economy people will say, 'We have to do something to demonstrate confidence to reignite momentum in the global economy; let's get the round done.' That is the cynics' view. I followed the Uruguay Round quite closely and it seemed to me that every step forward came out of the fact that people panicked because there was a crisis and it was not moving, and that crisis stimulated the effort to go forward. What is different here compared with there is that that same attention need not be paid to the round if there are short-term smaller gains at a bilateral level. I am just running around in circles on this discussion, but I put that to you as a concern.

Prof. Lloyd—It is a concern. There is something in that argument. However, I do not want to be too pessimistic. Let us not forget that the Uruguay Round negotiations were very difficult. They took seven years. The American fast-track authority had to be extended. They looked as if they were going to collapse two or three times during that period but eventually they were not only concluded, what emerged was far more ambitious than what they set out to do in the first place. The original terms of agreement set out in the Punta del Este Declaration that set up those negotiations did not envisage a new body—the WTO—for example. That came out of the committee which was set up when the going was really tough. There is a precedent which shows that, if we persist, eventually rational and hard heads might persuade some of the countries that are being difficult to be more cooperative and then things can start to happen. I sincerely hope that we do go through something like that, and the sooner the better.

CHAIR—Would you agree that one of the difficulties about a multiplicity of bilateral agreements is that you saddle Australian industry with a new raft of regulation and you probably create a new class of adviser to industry—a trade adviser or a trade consultant—because the rules are different for you to sell your goods in different markets, and that that higher transactional cost is inefficient economically?

Prof. Lloyd—Yes, I would. That is a problem, especially in areas like rules of origin. There is a hideous problem in that particular area. However, I think we have to try to seek convergence in these areas. There is nothing much happening in rules of origin, and I regard that personally as the most difficult area. Incidentally, I have pretty grave concerns about the negotiations in this respect. You may want to come back to this, but if you do not I would at least like to say that we should avoid NAFTA type rules of origin at all expense. It is the worst feature of the NAFTA agreement which might be adopted as a precedent for the current negotiations.

Multilaterally, and to some extent bilaterally, we should try and get greater uniformity in agreements. That will not be easy, especially if we are negotiating with, say, Asian partners, who have a rather different style in some areas, and the United States, which has its own style of trade negotiations. There is nothing much we can do about that individually; we can just hope that in the Doha Round and elsewhere there is some greater convergence in areas like rules of origin, and standards.

CHAIR—Let me conclude my questions so that my colleagues can have the floor. Previously in all trade negotiations Australia has entered into it has been avoided or resisted, including, in trade agreements, questions of labour standards. Although the WTO has an environmental dimension to it—it is bound to take into consideration the environmental impact—it is not a prescriptive provision.

Prof. Lloyd—No.

CHAIR—As a nation we have avoided including such provisions in any trade agreements. In the case of the Australia-US FTA, the United States is suggesting that Australia should include labour standards. Obviously, the precedence of what it has done with Singapore, Chile and elsewhere gives force to the argument that the US Congress regards those as a template for Australia and would look to Australia agreeing to their inclusion on labour standards, and on the environment as well. Do you have any comments about, firstly, whether they should be included and, secondly, the nature of such provisions?

Prof. Lloyd—I would prefer to see them not included. I regard them as areas that have some relationship to trade, but trade is not the central determinant of industrial relations and other labour standards issues, or the environment. However, the United States Congress saw fit to insist on these as a part of NAFTA—not only congress but also the current acts, which authorise negotiations, require them to have side agreements on labour and the environment. Having said that, I would prefer they were not there. From an Australian point of view, I do not think there is a great danger in those two areas. Originally they were put in NAFTA largely to persuade Mexico. Mexico is a country with very cheap labour. It is a country where child labour, for example, was used extensively—and to some extent, I think, it is still used. American manufacturers and other service industries had a concern about that kind of competition. That is not an issue in Australia. Australia has a relatively good record in the ILO. It has adopted some of the conventions and not others. Although I have not looked at this in detail, I cannot see that the Americans would have any great concerns over our industrial relations procedures or other labour standards like equal opportunity and so forth.

The environment provision was mainly in NAFTA as a device to persuade Mexico to get modern and start measures to adopt domestic environmental policies and ways of enforcing them. In relation to the environment, I think the greater danger is not the environmental side agreement but the possibility that the dispute settlement procedures—investor to state procedures, in particular, if we have them—might be misused for this kind of purpose. You may know that in NAFTA there have been a number of disputes between American corporations in Mexico and Mexican state-level governments. The corporations have used the DSP as a mechanism to try and lever changes in Mexican policy. That route, rather than the side agreement itself, which is likely to be confined to matters of general principle, might be of more concern to us.

CHAIR—There is the strong view around that, since the WTO is the only international body that has a dispute settling mechanism that binds its parties to the outcome, one of the reasons why the WTO is the target of various other sectors wanting to have their matters considered in a trade context is to avail themselves of that enforcement mechanism and to be able to spread standards by enforcement. The counter view to that is that this mechanism was designed to settle trade disputes. If you load it with other issues associated with trade—and everything in one way or another is related to trade—the mechanism itself will cease to function. Do you have a comment on that?

Prof. Lloyd—That is very true. I have no doubt that the environmental lobby, the pro-investment rules people and the competition policy people—virtually all those pursuing the so-called Singapore items—want to have them added to the rules of the WTO precisely because the

WTO rules are not only binding but also enforceable through these procedures. However, I note that the WTO rules are strictly state to state—to use that terminology. They only involve government measures. For example, in the Fuji versus Kodak dispute, Kodak believed, I think with a great deal of evidence, that in various ways it was being excluded from even marketing its products, let alone from competing fairly, in the Japanese market but it could not adopt the standard state trade practices issues. The dispute the United States took to the WTO could only involve legislative measures, large store acts and one or two other measures, which the American government then alleged had been part of the way Kodak had been excluded from the market. The WTO has to have such provisions but they are limited to state-to-state measures. I personally would prefer to see issues like competition policy not advanced in the WTO because I believe the WTO is quite an inappropriate body for such issues. They involve totally different matters of private trading which are well outside the scope of historic WTO rules.

CHAIR—Do you have a view about whether the WTO should go to an international code of corporate conduct, for example by projecting our Corporations Law at an international level?

Prof. Lloyd—For the same reason I would prefer that the WTO stayed primarily a trade agreement or a set of trade rules, which could include services. Services are part of the problem. I did not come to talk about that, but the GATS has been one of the mechanisms by which the scope of the WTO has been greatly expanded, not only in terms of the services or industries covered, but in terms of the modalities covered. As you know, parts of GATS, especially the basic telecommunications agreement, already involve quite specific rules relating to what we can call corporate behaviour. They ban certain kinds of cross-subsidies and other trade practices matters. Historically, the WTO had no such rules. They had rules relating to state trading but they were not concerned with the competitive aspects of state trading, they merely wanted to make sure that they were not hidden or discriminatory tariffs. One of the major parts of the Uruguay Round agreements has introduced new issues relating to competition policy. The fact is that the WTO is not well equipped to investigate these at all. Those parts of the agreements are not working very well because they just do not fit comfortably with the standard way GATS handles government measures and government-to-government disputes about government measures, as opposed to private-to-private disputes about trade practices, breaches of contract or corporate behaviour in terms of the kinds of things we talk about in corporate governance.

CHAIR—With the WTO that is clear—there is state to state settlement of disputes. We had evidence put to us yesterday that in NAFTA that is not the case—there are company to government disputes able to be dealt with—and that Australia adopted this principle in the Australia-Singapore free trade agreement. What is therefore obviously an issue coming up under the Australia-US free trade agreement is whether we adopt that format too. If we were to, do your remarks about dispute settlement still apply?

Prof. Lloyd—Insofar as the scope of these private to state disputes relates to matters of trade covered by the terms of the trade agreement, that is quite legitimate. But the danger is that there is a thin end of the wedge aspect here. Again, if you look at NAFTA—and the environment is one of the major issues—there can be some provision somewhere in the agreement which relates to, say, the environment. That can be seized upon by private corporations and they can try and use the dispute settlement procedures. One can see why Australian corporations, as well as US corporations, would want to have some recourse if they thought the other government was not

living up to terms of the agreement. But if the wording of the agreement and the scope of the agreement are not confined, that can virtually open up governments to all kinds of disputes.

The other thing I would say in the case of Australia and the United States is that, while our law differs quite substantially in many areas of corporate law and so on, both countries have a well-entrenched rule of law, which is not the case in Mexico. Part of the problem in some of the Mexican cases I have read or looked at is that Mexican governments did things which are, I think, unthinkable in the United States and Australia. So I do not think we would get into quite the level of disputation that they have got into in Mexico.

CHAIR—Nonetheless, what has been put to us—and this goes to my concluding question—is there is disquiet that, where you have panels created in those bilateral frameworks, members of those panels do not have tenure, you do not develop a consistent pattern of jurisprudence and there may be arguments about people being conflicted, which raises question marks over conclusions arrived at. Unless we embody a judicial approach—an all singing, all dancing and all laughing legal structure—then those panels are inferior to a proper legal process that involves company rights. I am someone, I have to say—with due respect to my colleagues on this committee—who does not automatically assume that the best way to resolve conflict is to bring in the lawyers. Nonetheless, this argument says that if you are going to have a dispute resolution you have got to do it within what we understand as a conventional legal framework on trade matters. Do you have a comment on that?

Prof. Lloyd—I might answer that by drawing attention to the difference between the kind of provisions which the US has incorporated on the one hand and those of the European Union on the other hand. The European Union has a quite different approach of course because such matters can go to the European Court, but that is an established court procedure and I think it has not had the problems of jurisdiction, lack of consistency and so forth which have emerged in the settlement of some trade disputes. Yes, I agree that there is a danger there—not being a lawyer, I do not know quite how to try and contain that, but I agree that there is some possibility that these provisions could be abused or could lead to pretty unsatisfactory resolution. But again, I think there is far less danger in a US-Australia agreement in this regard than in, say, an Australia-Japan or Australia-China agreement, where I would probably just want to exclude such provisions altogether.

CHAIR—I would have thought, given America's conduct at the WTO and the legal talent they marshal behind their USTR, that if there is the classic litigious society it is the United States and if there is a classic country where issues are resolved through legal means it is the US. While I decry somewhat the extent of litigiousness in Australia, the home of it seems to be that we are importing that culture from the United States. I would have thought that this would just be another example of it. But I accept your comment.

Prof. Lloyd—They are very litigious. I can only repeat that it might get out of hand, but I think it could be designed in such a way that the risks of such excessive litigation could be controlled.

Senator MARSHALL—Professor, you argue that we should not make concessions in respect of TV content and parallel importation, but wouldn't the same public interest issues go to other areas, such as quarantine and the Pharmaceutical Benefits Scheme?

Prof. Lloyd—They are all issues that need to be looked at. Perhaps I can say something about quarantine. It is possibly the most important of all of them. I think Australia is in trouble with quarantine laws in general at the multilateral level and the regional level. The EU has indicated quite plainly that it does not accept that our supposedly science-based system is not unduly trade restrictive, and it plans to take action in the WTO against that.

We have been in bilateral disputes with a large number of countries in recent years—New Zealand, Canada, the Philippines, Thailand, the European Union and others. The reason is that Australia, probably along with New Zealand, has the most tight, and therefore the most trade restrictive, quarantine laws of any of the WTO members. We are at the extreme in terms of excluding quite a range of products regularly, and usually a total prohibition, whereas other countries use their quarantine laws more selectively.

Of course, the explanation is that, being a remote island continent, we are relatively disease free. We do not have all sorts of things, like foot-and-mouth disease. On the other hand, there is a general perception that our rules are unnecessarily trade restrictive and that we could protect our vital interests while allowing in more goods than we do at present.

Take Thailand, for example. I have just spent in time in Thailand, and I do know that Thai exporters of mangoes, pawpaws, bananas and some other products have complained for a long time—as have Philippines exporters, about much the same products—that our laws are unduly restrictive. I do not think we should change fundamentally our quarantine laws, and I am not recommending anything remotely like open slather, but I think we have got to be able to justify prohibitions by demonstrating a real risk and no other method of inspection or treatment as an alternative.

One cannot be specific—I cannot say that for this product we should do exactly this—but we do know that AQIS, for example, has been changing its methods of imports risk assessment in recent years and moving in that direction. So what I am proposing is not totally radical. We are moving, but pretty slowly, towards less trade restrictive quarantine measures. If we are not perceived as being reasonable on this score not only are we are going to be the subject of more disputes at the WTO and bilaterally but the revision of the SPS agreements and whatever might happen in this regard in the current Doha Round are more likely to go against our interests.

CHAIR—It might be politically impossible for the government to move on this front, though.

Prof. Lloyd—It may be, but we are going to have to move. It is possible—I do not know—that the current Doha Round will, if and when it is concluded, incorporate measures that force us to liberalise our quarantine. Apart from New Zealand, we have got virtually no other allies. We are fighting the whole of the WTO. We are fighting developing countries, the European Union, the United States and Canada. We are isolated.

Senator MARSHALL—But it is argued that the public interest in terms of quarantine is much greater than that for TV content, for instance. You have specifically picked out TV content as something we should not move on.

Prof. Lloyd—Yes.

Senator MARSHALL—You have picked out two items. Are you really saying that there are only two that we should not make any concessions on and we should make concessions on the rest? Again, I would go to the issue of pharmaceutical benefits.

Prof. Lloyd—Yes. We can come to that in a moment. I am not quite sure in which order I should take them.

Senator MARSHALL—In any order you like.

Prof. Lloyd—As far as pharmaceutical benefits are concerned, again, I think we should make it plain to the United States government that we are not prepared to amend the fundamental principles of our Pharmaceutical Benefits Scheme. What we are currently doing is not in breach of the intellectual property agreement, TRIPS. It is primarily a matter of subsidies and prices. We should make it plain—we will have to make it plain, even if we do not want to—that we intend to abide by the rules of TRIPS. We should make it plain that we intend to protect American copyright. I would not want to see any change in that, except in parallel imports, which are a different matter again, and there we are not breaching copyright either. I believe in the principle of the protection of copyright and I believe the Australian government has a responsibility to make sure that the copyright of American companies, as well as Australian or any other companies, is protected. But we can do that without amending the fundamental way that the Pharmaceutical Benefits Scheme operates. My reading of the statements which emerged from the first round of negotiations was that—and this is really what the chief American negotiator said—they were not going to require a change in the principles, but they were concerned about some of the operating details. I do not know what that means. I will reiterate that we should not sacrifice the PBS, but I believe we can do so in these negotiations.

I personally think that that is not going to be the major issue. The Americans are likely to give us much more trouble over the TV content than they are over the PBS. I might be proven wrong, but TV content is so plainly a trade restrictive measure. I accept that, but I take the same view as the Canadians: this is the one area in all of the goods and services trade where I personally think there is a sound argument for the protectionist view. The reason is that it is the old Canadian argument about cultural industries. If we abandon the TV content rules, I fear that Australian television would be indistinguishable or barely distinguishable from American television. The quality of programming on the ABC and SBS free-to-air channels would deteriorate. I think that TV and newspapers are areas where different arguments apply. I am opposing the American Motion Picture Association line of argument there. I hope that the government stands its ground and points to the precedent in NAFTA itself where the Canadians held out and managed to get a special exception in the area of service trade relating to so-called cultural industries.

Senator MARSHALL—Another area where it might be argued that the public interest would be better served by not making any concessions might be the Foreign Investment Review Board. Do you have a position on that?

Prof. Lloyd—It might be, but I do not come out on that side of the argument. I think the present Foreign Investment Review Board based type of screening, which we have, is not working well. The Americans are opposed to any kind of screening. We do not have to concede that. FIRB is a very secretive organisation; it does not publish any principles. I personally think it has not been nearly as open and transparent in foreign investment decisions as the government

and the old Tariff Board, Industries Assistance Commission and Productivity Commission process has been in relation to the trade in goods and services.

FIRB appears to be a servant of the Treasury. It has followed a fairly consistent line in being very secretive. It does not hold public hearings. It does not publish principles. I do not think FIRB is a model method of screening. Foreign investment rules around the world are being liberalised. I think we can liberalise them further while at the same time retaining the ultimate right to veto mergers and acquisitions and greenfield investments in special cases. I am in favour of a greater degree of liberalisation of direct foreign investment, I am unhappy with FIRB and I think we ought to be able to reach agreement with the United States in this area without going all the way to an American style, virtually open slather foreign investment regime. The government should retain the powers, but I would like to see it do so in a much more open and transparent way.

CHAIR—Do you mean something like the Woodside case?

Prof. Lloyd—Yes.

Senator JOHNSTON—I would like to take us back a step to Senator Marshall's point. You raised the two areas where you thought there should be exceptions. It strikes me that, if you are going to nominate a cultural ingredient as being the indicator of where it is important to carve out a topic, we get into a very large area of enterprise in Australia that has the potential to be viewed from a cultural perspective. It strikes me that it is the tip of a very big iceberg and it has the potential to undermine the fundamental principles that drive our desire to get into a relationship like this.

Prof. Lloyd—Yes, I agree. I advance this argument with some caution because, as a trade economist who has argued for years against protectionism in favour of tariff liberalisation, it makes me nervous to put forward this argument. However, I would not want to extend it to all cultural industries. Perhaps that was not plain. I think the main area is public television and newspapers. As far as music and the theatre are concerned, for example, to take two areas, with music in particular there are, to my knowledge, no such restrictions. That is a big industry. I think that in terms of volume of sales it is probably at least as important as television, and that is an area where the Americans already have a very large share of the market. I hope I did not mislead you. I am not seeking a cultural industry exception which would be open ended and cover any cultural industry. Specifically, I see no argument at all for that in the area of music and audiovisual, other than for television. I would not want to apply it to the theatre. I would not want to apply it to ballet or orchestral music. Those are the areas of communications which are so important in determining our society. Newspapers and television are the main sources of news and information for the great bulk of Australian households.

Senator JOHNSTON—The point strikes me as being a little incongruous, because I see Anthony La Paglia go over to New York and put on a New York accent to gain roles in various films, hiding the fact that he is a foreigner. It is only a matter of time before we have American actors coming over here and putting on an Australian accent and hiding the fact that they are foreigners. What is the difference? We even have black Americans pretending to be Aborigines and goodness knows what.

Prof. Lloyd—Let me give you an example that highlights the point. Actors' Equity in the United States has very restrictive rules that our government might well take up. These things cut both ways. The Actors' Equity requirement is that American actors or American registered actors—I am not exactly sure, but they have to be American actors—get most parts. It is exactly the same kind of restriction that we have, so the Americans do it also. I do not support an Actors' Equity type of agreement. I would not want Australian actors to argue that Australian productions have to have 80 per cent Australian actors. The direction and the subject are critical. Those, rather than the actors, are what determine an Australian film or an Australian television program.

Senator JOHNSTON—But it is a pretty big ask to have someone be the ultimate arbiter of what is Australian in an area of art performance that then qualifies for protectionist policy.

Prof. Lloyd—Yes, but we currently do that under the content—

Senator JOHNSTON—Is it right that we do it?

Prof. Lloyd—In that area, I am prepared to go along with it because I fear that, if the content plan were abolished totally, we would get more American based programs—everything from children's programs to news programs. Personally, I do not want to see that.

Senator JOHNSTON—I worry that the principle we apply to that—and I think there is a lot of argument in support of it—has a problem in that it can be transported right through a whole host of industries.

Prof. Lloyd—Yes, I agree it is a slippery slope, and all I can do is repeat that, personally, I would limit it exclusively to television and newspapers and rule it out for other cultural industries.

Senator JOHNSTON—What about the Internet?

Prof. Lloyd—It is too late, and the very nature of the Internet means that you cannot regulate there. If, in future, people get their news from the Internet then I suppose that will undermine my principle, but I cannot see how we can have a sensible area of content on the Internet. It is impossible without going to a Chinese style regime, which would be quite abhorrent.

Senator JOHNSTON—This would mean, in practice, that you would restrict access to satellite communications for non-Australian content television?

Prof. Lloyd—I think I mentioned free to air—I have to say I am chiefly concerned with the ABC and SBS. So far as satellite and cable television are concerned—television which goes beyond the free to air—I think people can buy what they want. If I have available, and I am assured that other Australians have available, a free-to-air service on basic news and other programs, I would be content with that.

CHAIR—I do not think anyone is saying, in this cultural exception argument, what Gerard Depardieu the French actor said in defence of the French position on cultural protection—that only pigs watch American television.

Senator JOHNSTON—That is in *Hansard*!

Senator RIDGEWAY—Did he say that in English or French?

CHAIR—He said it in French, naturally—or at least he is reported to have said it in French. I never heard him; I have to be very careful. Whether he said it or not, it sounds like a French type comment to me. But I think the cultural industry in Australia essentially argues that what Australians require—or what any nation requires—is for their art to be able to be vibrant enough to hold up examples of Australian life in Australian culture by Australian people and that even universal or classic dilemmas be represented in an Australian context to an Australian audience. They argue that that ought to be there as a right, which requires some government intervention in this sector to protect it. They are not saying that it ought to be to the exclusion of anything else but that it should be there as part of a strand of cultural artefacts coming at you by whichever medium you choose. I think that is what they are saying.

Prof. Lloyd—I have tried to draw a distinction between culture in general and those kinds of cultural aspects which relate to communication—news, information and things like that. We are using 'culture' here in two slightly different senses.

CHAIR—Yes.

Prof. Lloyd—I mean the news sense. I do not see any case at all for protecting Australian artists, theatre, opera or music in the same way. They have been, and are presently, competitive and they are not protected. They get subsidies as a form of assistance but, apart from subsidies to the arts—we might want to talk about that and the Americans may raise that—which basically go to young artists, with the exception of the Australian Opera and some orchestras, these subsidies are mainly intended to develop new forms of art and new artists. Aside from those subsidies, I do not see any argument for the cultural industries, outside television and newspapers.

Senator RIDGEWAY—What about the book industry? As you would know, even under the existing parallel importation laws, books and the printing industry, including sheet music and other publications, have been excluded or exempted from the lowering of the restrictions that were in place up until February-March this year. Do you think that the authors, the creators and the publishing industries in this country deserve protection?

Prof. Lloyd—No, I do not. I think the copyright system is their fundamental protection. As far as parallel imports of print material go, for example, I think we should follow the intellectual property system known as the international exhaustion of rights. That would allow parallel imports. They do not breach copyright; the copyright has been paid. It is not a matter of copyright. I see the American style limitation on parallel imports as a restriction on trade. I think they are against consumer interests and they are not doing much to protect producer interests.

Senator RIDGEWAY—How do you respond, then, to the recent American decision to extend copyright beyond 50 years after the death of a creator in the case of Disney products such as Mickey Mouse? They have increased the length of the copyright period by an additional 45 years for the very reason of commercial exploitation by foreigners.

Prof. Lloyd—But that is a copyright matter itself, as distinct from a parallel import matter. I do not know enough about that case. It is really a question of how long a copyright should hold for. I think the present law is 15 years, isn't it? I am subject to correction on that.

Senator RIDGEWAY—It is during the life plus 50 years.

Prof. Lloyd—I do not know. I have not endeavoured to work out what the optimum length of copyright is, and I would be surprised if it were a subject of negotiation. What is likely to come up is the matter of parallel imports.

Senator RIDGEWAY—Are you familiar with the experience in Mexico following NAFTA, particularly in terms of their film industry?

Prof. Lloyd—No.

Senator RIDGEWAY—As I understand it, because they were predominantly a Spanish-speaking country, they did not take the same initiatives that Canada did to look at cultural protection in the agreement, thinking that their industries would continue to thrive. The outcome of that agreement is that the film industry in Mexico now is a very small percentage of what it was, mostly because the United States has been able to use its own buying power in relation to distribution. That has resulted in the distribution of all of the American films through all of the legitimate outlets in Mexico, which has therefore killed off, indirectly or as a by-product, the Mexican film industry.

Prof. Lloyd—I was not familiar with that. It would reaffirm my desire to do something to protect the Australian content of free-to-air television. So far as films are concerned, I suspect the Mexican situation may be different from the Australian situation. The Australian film industry, although it has its ups and downs, is fairly competitive. It has done quite well in recent years, and it has done so without protection, except through subsidies, for example, with the new Docklands studio in Victoria and so forth. The state and Commonwealth governments have over the years given quite a few subsidies to film producers and a wide range of other art producers. But the Americans can hardly argue against those kinds of subsidies. If they do we can point out that the US Farm Bill has subsidies which are so many hundred times greater than that and that this is merely a partial offset. Subsidies are going to be very difficult to include in the current negotiations. They are difficult in the WTO. The WTO does not prohibit subsidies and it has not done much to limit subsidies in any field except export subsidies. I will be surprised if they are an important part of the current negotiations, because most governments, including the US government, want to retain widespread freedom to subsidise various industries.

Senator RIDGEWAY—Going back to the issue of quarantine and customs and the food labelling laws, you would no doubt be familiar with the fact that the US trade representative has signalled that as an area where the Americans regard our requirements as being trade restrictive. Do you have a view on that? Particularly with the recent scandal concerning Pan Pharmaceuticals and the increase in allergies amongst children these days, how do you deal with that question? Is it possible to build up a social argument or a health argument as to why it is that some things need to remain, or do the Americans need to come up to better practice standards?

Prof. Lloyd—I do not agree with the American view on that. It is paradoxical, though. Whilst the United States was one of the first countries to start labelling foods, dietary supplements and so forth decades ago, they do not go as far as we do in some respects. The argument that labelling is trade restrictive is quite ridiculous. It is information. The information put on a label has to be accurate, of course. You should not be able to mislabel in any deceptive way. Provided the information is accurate and provided there is a health or safety argument in favour of it, as there is in a wide range of areas—it is not just genetically modified foods or even foods; it is children's clothing, which might be flammable; it is all sorts of things—it is a part of our standards. We should politely tell them not to be ridiculous. It is not trade restrictive. It does not inhibit the sale of those products. The consumer does not have to read the label. The label is merely there if any consumer wants information about the contents or properties of the product.

CHAIR—That concludes our questioning. We invited you to come earlier and kept you later than we intended, and you were kind enough to stay. Thank you, Professor Lloyd.

Prof. Lloyd—Thank you very much for the opportunity to appear.

CHAIR—That concludes our hearing. We adjourn until a date to be fixed and a location to be named.

Committee adjourned at 3.43 p.m.