

Trade Policy Review Body

TRADE POLICY REVIEW

Report by the Secretariat

AUSTRALIA

Revision

This report, prepared for the fifth Trade Policy Review of Australia, has been drawn up by the WTO Secretariat on its own responsibility. The Secretariat has, as required by the Agreement establishing the Trade Policy Review Mechanism (Annex 3 of the Marrakesh Agreement Establishing the World Trade Organization), sought clarification from Australia on its trade policies and practices.

Any technical questions arising from this report may be addressed to Ms. Zheng Wang (tel: 022 739 5288).

Document WT/TPR/G/178 contains the policy statement submitted by Australia.

Note: This report is subject to restricted circulation and press embargo until the end of the first session of the meeting of the Trade Policy Review Body on Australia.

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SUMMARY OBSERVATIONS**(I) ECONOMIC ENVIRONMENT**

1. The high degree of transparency in the formulation and evaluation of Australia's economic policies in relation to their rationale, nature, and economic effects, enhances government accountability and public debate over the merits of these policies. Hence, transparency has contributed greatly to the continued process of reform, which began in the 1980s, and in which trade liberalization, much of it unilateral, has played an integral part. The extent of structural reform in Australia is exemplified by the drop in the effective rate of assistance (ERA) for manufacturing during the past two decades, from 25% to 4.5% in 2003/04, the last year for which the indicator is available. Structural reforms were accompanied by macroeconomic reforms: for example, the floating of the exchange rate in the early 1980s facilitated subsequent adjustment to tariff reductions. Structural reforms have been aimed at reducing, if not removing, distortions to competition in order to improve the functioning and therefore flexibility of markets for goods, services, labour, and capital, thereby accomplishing a more efficient use of domestic resources. The resulting rise in productivity and improved competitiveness of Australia's goods and services in world markets has enabled real GDP to grow at an average annual rate of about 3.5% during the past 15 years, which has raised per capita income to eighth place among OECD countries. Reform has also made the economy more flexible and resilient to external shocks, like the Asian financial crisis in the late 1990s and, more recently, the drought in 2006.

2. Against the backdrop of continued wide-ranging structural reforms as well as sound macroeconomic policies, Australia's economic performance has been impressive during the review period (2002-06), with annual average GDP growth of 3.2%. Growth has been led by a global boom in demand for mineral products, of which Australia is a

major exporter. Australia's prudent macroeconomic policies have helped to strengthen the economy's resilience to shocks, and thereby to sustain economic growth. As a result of increased inflationary pressure, the Reserve Bank of Australia has been tightening monetary policy. Consequently, inflation has, by and large, remained within the Central Bank's targeted range. Both the Commonwealth and state governments have achieved fiscal surpluses, and net government debt has been eliminated. In addition, unemployment declined to its lowest level since the 1970s, in great part due to reforms that have rendered the labour market more flexible.

3. Rapid growth in the resource sector and the accompanying rise in private investment, including inward foreign direct investment, have contributed to a widened current account deficit. The strength of the Australian dollar has put pressure on other sectors, particularly manufacturing. The increased demand for resource-based products has also revealed infrastructure constraints. Unfinished business in this regard includes reform of maritime and land transportation, and electricity and water services.

4. Corresponding to the global boom in demand for mineral products, the share of mining in total merchandise exports increased from 40% in 2002, to 48.4% in 2005. On the other hand, manufacturing accounted for around 80% of total merchandise imports. Australia's trade with Asia continues to grow. The proportion of trade with Singapore and Thailand has increased, possibly due to the regional trade agreements. By contrast, the proportion of trade with the United States fell.

5. Australia's stock of FDI peaked in 2004. It seems that Australia's recent RTAs (with Singapore, Thailand, and the United States), which include investment-specific provisions, have not increased investment from its partner countries. The authorities consider it is too early to assess the impact of these RTAs on foreign investment flows.

(2) TRADE POLICY REGIME

6. Australia has a highly transparent trade policy formulation and evaluation framework. Transparency has greatly facilitated the advancement of the economic reform agenda, much of it involving unilateral trade liberalization.

7. While the Doha multilateral trade negotiations remain Australia's top priority, increased importance is being attached to the negotiation of RTAs. In addition to the Australia-New Zealand Closer Economic Relations Trade Agreement, Australia has signed RTAs with Singapore, Thailand, and the United States. The authorities state that Australia's commitments in its RTAs go beyond the current WTO Agreements in a number of areas, including services and investment. The Government is thus making efforts to multilateralize, through WTO negotiations, some of the progress achieved in regional trade liberalization.

8. Australia's foreign investment regime is generally transparent and liberal, although foreign equity restrictions in certain "sensitive" sectors remain, and a screening process continues to be applied to ensure that foreign investment is not contrary to the "national interest". Since Australia's previous Review, changes in the foreign investment policy have been primarily the result of the Australia-United States Free Trade Agreement (AUSFTA), which provides preferential treatment to U.S. investors vis-à-vis other trading partners.

(3) TRADE POLICIES AND PRACTICES

9. Trade liberalization has been an integral part of the structural reforms that have contributed to Australia's impressive economic performance. Liberalization has continued during the review period.

10. The tariff remains one of the main instruments of Australia's trade policy. As a result of unilateral reductions (in 2005) in tariffs applied to textiles, clothing, and footwear (TCF) as well as to passenger motor

vehicles (PMVs), the overall simple average applied MFN tariff rate fell from 4.5% in 2002 to 3.8% in 2006. While 96.7% of Australia's tariffs are bound, more than 40% of its bound rates currently exceed applied MFN rates by at least five percentage points. Although this potentially imparts a degree of unpredictability to the tariff, there has not been any increase in applied tariff rates during the period under review.

11. Nonetheless, some tariff and non-tariff barriers to trade remain. Despite the cuts in tariffs applied to TCF and PMV products, their rates are still considerably higher than the average applied MFN rate. In addition, non-ad valorem rates, applying to a few tariff lines, tend to conceal relatively high tariffs. In particular, judging from its high average ad valorem equivalent (AVE), the compound duty on second-hand vehicles is potentially prohibitive.

12. Although strict sanitary and phytosanitary (SPS) measures remain, steps have been taken to improve import risk analyses in order to make the process more transparent, efficient, and timely. According to the authorities, as international standards do not exist in some areas, the share of national standards that are equivalent to international standards remains at around 40%.

13. Australia has observer status in the WTO Committee on Government Procurement, but has no intention of becoming a party to the GPA. The authorities consider that accession to the agreement would impose unnecessary costs and delays on procurement operations. Government procurement of motor vehicles still incorporates local-content requirements.

14. Discretionary export licensing restrictions are maintained for reasons related to SPS, the environment, and alignment with international agreements. Export quotas remain on some cheese products and merino sheep. Despite the corporatization or privatization of some state-trading enterprises, and the termination of some state-trading arrangements, exports of certain agricultural

products are still managed by such enterprises.

15. Export assistance includes mainly the Export Market Development Grants (EMDG) scheme, duty concession programmes, and export finance, guarantee, and insurance operated by the Export Finance and Insurance Corporation (EFIC). Although local-content requirements were removed under the EMDG in June 2006, the values of the EFIC's contracts with recipients of such assistance continue to depend on the degree of local content.

16. Assistance is also provided to encourage the development of domestic industry. It may take the form of tariff concessions, tax incentives, grants, or concessional loans. Assistance delivered through the tax system accounts for more than two fifths of total annual budgetary assistance. The Tax Expenditure Statement publishes details of these tax measures annually, enhancing their transparency. The import duty credit under the Automotive Competitiveness and Investment Scheme (ACIS) is the most significant industry-specific assistance programme. However, the apparent lack of cost-benefit analysis of some schemes, including tax measures, makes it difficult to determine whether the assistance has yielded net social benefits.

17. Reform regarding competition policy continues. As part of the National Competition Policy, governments undertake to review and reform legislation that restricts competition. Following the review of the National Competition Policy, the Council of Australian Governments (COAG) endorsed a new National Reform Agenda, including competition and regulatory reforms. In addition, with a view to reducing the regulatory burden, the Banks Taskforce made a large number of recommendations (including regular review and cost-benefit analysis of regulations), most of which have been accepted, fully or partially, by the Government.

18. Australia's recently signed regional trade agreements changed various aspects of its trade policies, including protection of intellectual property rights. Amendments to the Copyright Act 1968, and minor changes to the Patents Act 1990 were made to incorporate requirements under the AUSFTA. The authorities state that these changes are applied on an MFN basis to all WTO Members.

(4) SECTORAL POLICY DEVELOPMENTS

19. The agriculture sector (including forestry and fisheries) accounts for a relatively small portion of the economy, but plays a much bigger role in exports. With around two thirds of the sector's output exported directly, it is the most export-oriented sector after mining. Domestic support for agriculture remains well below the OECD average. Tariffs on agricultural products remain low (averaging 1.4% in 2006), but ad valorem equivalents for a few non-ad valorem duties are much higher. Despite the privatization/corporatization of some state-trading enterprises, state-trading arrangements have been maintained for exports of some agricultural products. In addition, Australia's quarantine framework remains strict.

20. The mining sector has been one of the major driving forces behind Australia's recent economic growth. Owing to the global boom in mining commodities, Australia's terms of trade have increased by around 30% over the past three years. The mining sector operates in a competitive market. There are no sector-specific restrictions on foreign investment, and the sector receives very little government assistance. The effective rate of assistance for mining was virtually zero in 2003/04.

21. Reforms aimed at simplifying the regulatory framework have continued in the electricity sector in order to create a fully competitive national market. As Australia has limited water resources, reform is being undertaken to establish a market framework for the management of water resources in both urban and rural areas.

22. *The share of manufacturing in GDP and employment fell during the review period. Nevertheless, manufacturing continues to receive the largest portion of budgetary assistance. In 2003/04, ERAs for textiles, clothing and footwear and motor vehicles and parts, in particular, were 24.2% and 10.6%, respectively, much higher than the average of 4.5% for manufacturing as a whole. The ERAs may have fallen subsequently, as a result of Australia's unilateral reduction in the tariffs for these sectors in 2005.*

23. *Services dominate Australia's economy, accounting for nearly two thirds of GDP and roughly three quarters of employment in 2004/05. During the review period, government assistance to services has been increasing, mainly through measures to encourage investment, R&D, and exports.*

24. *The legislative and institutional frameworks for financial services have changed little, although stricter prudential regulations were announced in 2006 to bring them into line with international practices.*

25. *The regulators of telecommunications and broadcasting, the Australian Communications Authority (ACA) and the Australian Broadcasting Authority (ABA), were merged to form the Australian Communications and Media Authority (ACMA) from 1 July 2005. It was also announced that foreign ownership restrictions on media would be removed from 2007.*

26. *Australia's merchant fleet has shrunk, reflecting its growing reliance on foreign-flagged vessels. However, it seems that despite the recent global boom in mining commodities and the associated increase in demand, exports have been constrained by the lack of transport facilities, particularly coal ports in some parts of Australia. In response, an Export and Infrastructure Taskforce was established to identify infrastructure bottlenecks. The taskforce found evidence of capacity constraints at most of Australia's bulk ports for coal and iron ore. The regulatory framework was identified as the greatest*

impediment to the development of Australia's infrastructure. Accordingly, the COAG has agreed to a range of initiatives to improve planning for ports and associated shipping channels and, through its new National Reform Agenda, measures to reform the regulatory system for infrastructure.

27. *During the review period, a few policy changes on civil aviation have been implemented. In particular, since the signing of a bilateral agreement in 2003, international airlines from New Zealand have been accorded cabotage rights. Also, price regulation of airport services has been relaxed since 2002, and the Government has discontinued price notification and price-cap arrangements for all airports, and introduced price monitoring for the seven most important.*

(5) PROSPECTS

28. *Australia's economic growth is expected to remain strong. The authorities are of the view that as a result of the ongoing and deepening structural reforms, the economy is now very resilient to external shocks. The major challenge in the short term is to maintain macroeconomic stability in the face of the high commodity prices. However, the authorities believe that the economy's vulnerability to an eventual end to the commodity price boom has been reduced owing to earlier reforms, such as the introduction of a floating exchange rate in the early 1980s and more flexible domestic markets for goods, services, capital, and particularly labour. Nonetheless, in the face of the slowdown in total factor productivity in recent years, there is a need to press ahead with structural reforms as outlined in the National Reform Agenda, especially those concerning key infrastructure-related services, such as electricity, water, and transport, in order to raise productivity. Increased productivity would also enable Australia to address the longer term challenge of an ageing population, particularly the associated rise in health and social welfare costs and implications for the labour market.*
