In the national interest: how to approach trade negotiations

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Submission to the Joint Standing Committee on Trade and Investment Growth's inquiry into the Australian Government's approach to negotiating trade and investment agreements.

In 2010 the Productivity Commission tabled an excellent report on bilateral and regional trade agreements.[1] The then government responded at length, accepting most of the recommendations. Perhaps the most important comment in that response was:

"the best trade policy is domestic economic reform". [2]

International trade is an important mechanism for increasing competition for the benefit of both consumers (through lower prices, more choice and higher quality) and producers (through better inputs allowing more efficient production and through the competitive impetus to improve innovation and customer focus).

It is therefore extremely disappointing to see no mention of either competition or consumers in the lengthy terms of reference for this enquiry. Nor is there any mention of either consumers or competition in the evidence given to the committee by Department of Foreign Affairs (DFAT) officials on 13 September 2023.

In this submission I address:

- why a robust free trade is an important policy issue;
- stakeholders, vested interests and the national interest;
- transparency in policy goals and in treaty implementation;
- trade promotion, trade diversion and non-trade chapters;
- trade, health and the environment – managing competing priorities; and
- legislating trade processes – the global experience with the US Trade Representative.

Why is free trade a good thing?

The benefits of free trade derive from the role of competition in ensuring markets perform well, benefiting both final consumers and consumers of intermediate goods and services (firms). This is the mechanism through which free trade increases prosperity for everyone. It therefore must be closely allied with a broader agenda to ensure the most competitive domestic environment possible.

The first three terms of reference focus on government (rather than national) priorities, stakeholders (ie interested parties, but not citizens or consumers), and representatives of industry and workers (but not of consumers or competition watchdogs). Underlying these poor terms of reference is the profound mis-understanding that trade policy should be about exports rather than increased domestic competition.

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[1] Productivity Commission, November 2010, **Bilateral and Regional trade Agreements**, https://www.pc.gov.au/inquiries/completed/trade-agreements/report

[2] Gillard Government Trade Policy Statement, April 2011, **Trading Our Way to More Jobs and Prosperity**, https://webarchive.nla.gov.au/awa/20110422102506/http://www.dfat.gov.au/publications/trade/trading-our-way-to-more-jobs-and-prosperity.html, p.9.

It should not be necessary to point out – in addition to every economic textbook on trade and the excellent understanding evidenced in the 2011 Government Trade Policy Statement – that the principal benefit of free trade is increased domestic competition. Our trade agenda needs to be based on a clear understanding of priorities to reform uncompetitive sectors and industries. It is simply a matter of arithmetic that the benefits of improved domestic competition substantially outweigh the benefits to selected operators of increased exports. Further, domestic reform benefits everyone, provided adjustment assistance is made available where increased competition incurs transitional losses for what had previously been protected areas of the economy.

A well-founded approach to trade policy should thus arise out of an active domestic economic reform agenda – something that has been sadly missing since the Hawke-Keating years.

Unfortunately this is not what we get.

A review of our approaches to trade agreements show that our trade negotiators profoundly misunderstand the economics of trade agreements, focusing on exports rather than imports. This is clear in the evidence presented by DFAT officials on 13 September 2023. In their 2015 review of the Australia-United States Free Trade Agreement (AUSFTA) ten years on, Capling and Ravenhill demonstrate the perils of allowing political/strategic goals to drive trade policy. They demonstrate – using Australian bi-lateral trade treaties – the consequential poor outcomes, focussing on rushed negotiations, inferior outcomes, outcomes which make subsequent multilateral agreements more difficult and outcomes which introduce new trade distortions. They conclude their analysis with the comment that:

> "The absence of detailed consideration of the likely welfare effects of the preferential trade agreements that Australia is negotiating has been a striking feature of Australia's trade policy formulation over the last 15 years." [3]

Noting that, as at noon on 22 September, there is only one submission to the committee, and that respected academic trade economists are not aware of the enquiry, I strongly recommend that the committee treat the Capling and Ravenhill analysis as an important submission to this enquiry, together with other materials referenced in this submission. I also recommend that the Committee invite some of our senior trade economists, and representatives from the Australian Competition and Consumer Commission to discuss these issues with them.

Stakeholders and the national interest

The role that interested parties play in determining public policy is well known. Regulatory capture occurs in most societies and its strength differs at different times. How it works has been spelled out in numerous studies, the most famous of which is probably Mancur Olsen's theory of public choice. How such private interests operate, and the very substantial funds they use to ensure their private interests trump the public interest,[4] is a massive problem for elected representatives.

Over the past several decades the parties which have the greatest private interests in the government decisions have managed to re-frame themselves as "stakeholders". This apparently innocuous term disguises their vested interests.

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[3] Ann Capling and John Ravenhill, 2015, "Australia's flawed approach to trade negotiations: and where do we sign?", **Australian Journal of International Affairs**, 69:5, 496-512, page 509.

[4] For example the extensive 2010 advertising campaign waged by the minerals industry against changes to how resources are taxed.

Having vested interests is not wrong nor a bad thing – for example all Australian have a vested interest in their government managing the economy well. But companies and corporations have very substantial funds at their disposal[5] and can use these for privileged access to government and privileged influence over decision making.

Stakeholder language hides the fact that important groups and interests are poorly considered – sometimes never considered – when it comes to determining trade policy and to negotiating individual trade treaties. There is no well resourced group representing consumer interests that is able to act as a watch-dog in respect of Australian trade policy.

In determining overall trade policy goals the pre-eminent interest has to be impediments to competition in the domestic economy. While interest groups, including foreign trade negotiators, can point to specific non-competitive issues (e.g. coastal shipping, high charges for managing investment and superannuation funds), the major roles should lie with public authorities rather than interest groups. Our competition authorities and bodies such as the Productivity Commission should be resourced to scan, analyse and advise on restraints to competition that should be addressed and removed.

In 2009, when G20 leaders were looking at how to resist protectionist influences, three of Australia's leading economists put forward an agenda where Australia could have shown leadership in developing an active trade agenda. This proposed agenda, endorsed by many others, built on the need for each country to focus on its own domestic reform agenda, using as a model Australia's experience.[6] Australia missed an important opportunity when it did not take up this proposal. It is not too late to do so now.

The focus in the terms of reference for this inquiry on "stakeholder consultations" ignores the fact that there is little to no analysis of the impact on consumers of trade negotiation goals in general nor of particular treaty elements in particular. This contrasts strongly with the 2011 Government Trade Policy Statement. The Howard government introduced a new National Competition Policy, but this was short on specific follow-up reforms. Subsequent governments have also given lip service to the need for robust economic reform, but have been light on actual delivery. An issue that needs particular attention in the light of supply-constraint elements in the current resurgence of inflation,[7] is the limited number of major suppliers in many markets and the impact this has on competition generally.

Finally the use of the term stakeholder rather than special or vested interest allows advisors and decision-makers to avoid recognising that most of the input with regard to trade treaties is from those operating on sectional rather than national interests.

The government, and DFAT in particular, also needs to come to terms with the fact that trade treaties are poor vehicles for pursuing international strategic goals. The USA developed this approach and has, since its bilateral treaty with Israel in 1985, negotiated treaties with many countries, especially those which are very small in comparison to the size of the US economy. The 1974 US Trade Act not only strengthened the role of the US Trade Representative (USTR), but also established Advisory Committees allegedly reflecting both public and private interests. However, as history shows, these now largely reflect purely the interests of major

[5] Funds which are tax-deductible and therefore subsidised by ordinary Australian taxpayers.

[6] Bill Carmichael, Saul Eslake and Mark Thirlwell, 2009, Message to the G20: "Defeating protectionism begins at home", **Lowy Institute Policy Brief**, https://www.lowyinstitute.org/sites/default/files/pubfiles/Thirlwell%2C_Message_to_the_G20_1.pdf.

[7] Isabella Weber, 7 September 2023, "The economics and politics of seller's inflation", Australia Institute webinar available at https://australiainstitute.org.au/event/the-economics-and-politics-of-sellers-inflation-with-isabella-weber/.

corporations. Their influence dominates US trade policy and thus global trade policy. How this has worked out in practice in regard to "intellectual property" is well documented.[8]

The fact that DFAT clearly still focuses on geostrategic issues as a driver for trade treaties is enabled by the lack of proper analysis of the outcomes of existing trade treaties. I am not talking here about economic models, but rather about detailed analysis of the specific elements of specific treaties and assessments of just what their impacts have been and who has been affected both positively and negatively.

Transparency

I'd like to address this issue at two levels – transparency with respect to setting overall trade goals and transparency with respect to specific elements in trade treaties and how this impacts on Australian businesses.

Australia was instrumental in setting up the Cairns group of agricultural fair traders and through that exercised strong global leadership in ensuring positive outcomes from trade negotiations. Since the AUSFTA, however, Australia has followed the US lead and refused to talk about trade goals except in very general terms. Such a non-transparent process has now been challenged by the European Union (EU), which has a new process of making initial negotiating texts publicly available. Australia has been slow to follow this lead and it is notable that the DFAT website for the Australia-EU trade negotiations has no links to draft treaty texts, but the EU website does.[9]

In a sense it is difficult for Australia to talk clearly about its trade goals. In some areas the policy is purely defensive – for example with respect to "intellectual property" Australia's policy is strictly defensive – it will accept provisions that do not require changes to current domestic settings (see Productivity Commission, 2010: 259). It is unfortunate that Australia has not adopted a more positive agenda, actively rejecting the inclusion of anti-competitive provisions in trade treaties.

More broadly it is difficult for DFAT to talk convincingly about trade goals as it sees these in political terms or in terms of exports, not in terms of improving the operations of the domestic economy. Indeed this may be why it is hard to identify clear trade policy goals – outside of agriculture, Australia seems to be reactive rather than proactive. Given the long and honourable performance of the Productivity Commission and its predecessors this is sad.

At a micro level I would like to draw the committee's attention to a rather nasty situation that seems to be emerging with respect to the EU's agenda for geographic indications (GIs). The EU is insistent that Australia provide restraint of trade privileges to 166 food product names. If such names were put forward after treaty agreement, producers would be able to challenge them at the Trade Marks Office and there would be an evidence-based assessment as to whether the privileges should be granted. But it appears that the government will, following New Zealand, deem DFAT's call for comment on the proposed names as meeting all scrutiny obligations. Although many producers, and some consumers and intermediaries, have put forward objections, none have received any response and there has not yet been any opportunity for a proper, legally-based review of the evidence. It appears that there will be

[8] Peter Drahos, 2002, **Information feudalism: who owns the knowledge economy?**, London: Earthscan; and Susan K. Sell, 2003, **Private Power, Public Law: The globalization of intellectual property rights**, Cambridge: Cambridge University press.

[9] https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions/australia/eu-australia-agreement/documents_en.

no proposals for any such transparent and fair processes. It seems there will be no proper legal processes before restraints on trade are handed out by the government.

Bi-lateraterals, multilaterals and non-trade chapters

As the committee would be well aware, the reason why multi-lateral agreements are strongly preferred to bilateral agreements is that they set a global level playing field, fostering improved competition for all parties. In contrast, bilateral treaties can be trade diverting rather than trade enhancing, reducing the chances that they promote welfare and in some cases even leading to a reduction in welfare. In such situations it is better to have no treaty. Armstrong's assessment of the AUSFTA queries whether the AUSFTA has achieved any net economic benefits.[10]

There do not seem to be any proper processes for assessing the goals in specific treaties nor the outcomes achieved against principles of returning to a multi-lateral trading system nor to ensuring that treaty outcomes are not trade diverting. The clear principles enunciated in 2011 in response to the Productivity Commission report seem to have evaporated.[11]

Many so-called free trade agreements are in fact **preferential** trade agreements and run strong risks of being trade distorting.

While lip service is always paid to the greater importance of multi-lateral rather than bi-lateral or regional trade negotiations, the very active agenda of bilateral and regional negotiations suggests this priority is forgotten on a daily basis. Nor does there seem to be an active screening of the content of trade negotiations to avoid issues that will impede future multi-lateral negotiations.

As the committee is aware, many issues in international trade are contentious. The area where Australia has continually expressed greatest concern is agricultural protectionism. Some genuine progress was made through the Cairns Group and the GATT Uruguay Round, though many issues remain. Countries with protectionist agricultural policies are usually able to avoid addressing these in bilateral trade negotiations.[12]

For lower income countries one of the most contentious issues is "intellectual property" (IP).

"IP" is a bundle of diverse legal privileges. Most either involve monopolies or restraints on trade. They do not therefore belong in treaties whose principle objective is to foster competition. There was a substantial fight over this during the Uruguay Round negotiations. In the event the lower income countries – led by India and Brazil – lost and membership of the World Trade Organization is now not possible without also signing up to the iniquitous Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). Scherer – one of the leading US industry innovation experts – has noted that this agreement was contingent on three benefits that were never achieved (increased agricultural and textile exports and the end of punitive Special 301 sanctions by the USTR).[13]

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[10] Shiro Armstrong, 2015, "The economic impact of the Australia-US Free trade Agreement", **Australian Journal of International Affairs**, 69:5, 513-537.

[11] That bilateral treaties not include elements that would impede subsequent multilateral negotiations and that Australia would avoid seeking preferential treatment for Australian exporters.

[12] For example in the Canada-EU Comprehensive Economic Trade Agreement (CETA) Kerr and Hobbs identified that "little in the way of agricultural trade liberalization was achieved and protectionist interests were maintained". See William A. Kerr and Jill E. Hobbs, 2015, "A protectionist bargain? Agriculture in the European Union-Canada Trade Agreement", **Journal of World Trade**, 29:3, 437-456.

[13] F. M. Scherer, 2006, **"**The Political Economy of Patent Policy Reform in the United States", AEI-Brookings Joint Center for Regulatory Studies, Washington, D.C. I can no longer find this paper on the Brookings website

In large measures the content of "intellectual property" (IP) chapters in trade treaties is drafted by multinational corporations with large holdings of IP privileges. The Productivity Commission rightly recommended that Australia avoid having IP chapters in bilateral or regional trade treaties. If such provisions were essential the Commission strongly recommended they only be included following a rigorous economic analysis (Productivity Commission, 2020: 285). Despite this, Australia has actively pursued IP chapters when it negotiates bilateral treaties with smaller economies and has agreed to set very low standards – that is standards which substantially privilege rights holders and disadvantage consumers – in treaties with larger parties (for example the then Trans-Pacific Partnership Agreement (TPPA), where the agenda was largely driven by US interests).

Trade, health and the environment – managing competing priorities

As a result of strong agitation from civil society Australia at one stage strongly resisted calls for Investor State Dispute Settlement (ISDS) provisions, for example in the AUSFTA. We then went through a phase under the Abbott government where such provisions, which preference the interests of foreign producers over domestic producers and citizens, were readily accepted. The global approach has since moved on and there is now general acceptance that private corporate interests should not be able to restrict the ability of governments to regulate to protect important societal goals such as health and the environment.

There are however further issues with regard to health and the environment where some of the simplistic prescriptions of free trade evangelists are worth challenging. Where, for example, specific products present a serious health risk, governments should be allowed to regulate or ban sales. One also questions whether global trade assessments should include assessment of the energy and emissions cost of transport of such goods. Surely the welfare "advantage" of importing bottled water from Italy or Scandinavia is less than the environmental cost of transporting these goods?

Much of the IP chapters of trade treaties should be challenged in terms of their health impacts (for example pharmaceutical product patents) or their environmental impacts (delaying the spread of new improved energy technologies).

Legislating trade processes – the global experience with the US Trade Representative

The USA has legislated processes for trade negotiations and this have caused great damage in many countries. Particularly iniquitous is the US Special Trade Representative and the use of Special 301 to apply sanctions to exports from countries whose domestic IP policies do not meet with US approval. The Committee would do well to review the US experience before suggesting legislative approaches. Such a review should consider the ways in which this has led to the interests of large scale US corporations dominating the US trade agenda. In many ways this has operated against broader US interests as well as providing real difficulties for smaller trading nations.

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but can provide a copy on request. A revised version was published in the **Journal of Telecommunications and High Technology Law**, 7:2, Spring 2009, pp 167-216, but the concluding section was revised to focus on US domestic concerns.

Final comment

I apologise that I have not been able to make a more substantial contribution to the committee, but I only became aware of the inquiry well after the announcement date. I have checked with fellow economists who publish on trade and they too were unaware of the inquiry. I don't know how you advertise, but I have previously made submissions to the Senate Standing Committee on Foreign Affairs, Defence and Trade (TPPA inquiry and treaty-making process inquiry) and to JSCOT (TPPA, ACTA). I attach as an appendix my earlier submission on treaty making processes, as this seems relevant to your inquiry.

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