

Trade in a Two-Speed Economy: Should Australia protect its industries?

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Should Australia protect its industries?

- Short answer: No.
 - Adam Smith: Prosperity requires ‘peace, easy taxes, and a tolerable administration of justice’.
 - David Ricardo: ‘Foreign trade [is] highly beneficial to a country, as it increases the amount and variety of the objects on which revenue may be expended, and affords, by the abundance and cheapness of commodities, incentives to saving, and to the accumulation of capital ...’
 - Economists have known for 200 years that trade is good.
 - All trade, not just foreign trade, not just ‘fair’ trade.
 - Comparative Advantage – both true and non-trivial (Paul Samuelson).
- Long Answer: Maybe.
 - Is Australia a special case?
 - Does Australia have Dutch disease?

Is Australia a Special Case?

- It is possible that some or other market distortion and/or failure exists meaning that government intervention is necessary to restrict free trade.
 - National Security
 - Income Redistribution
 - Optimum Tariffs
 - Maintain Balance of Trade
 - Job Protection
 - Infant Industries
 - Externalities
 - Strategic Trade Theory
 - Level Playing Field

Is Australia a Special Case?

- National Security

- ‘This is an industry that has enormous effect whether from plastics to steel to aerospace. I mean, it is not just building motor cars here. It is having the capacity to build jet fighters and therefore it is incredibly important that we keep the skills base.’

- Kim Carr, 10 June 2008.

- ‘On the other hand, if a respectable case can be made for maintaining a heavy manufacturing base on the grounds of national security, the inherent value of a diversified economy or the transitional costs of shutting down capital-intensive industries only to start them up again when market conditions change, there needs to be a forum where it can be addressed.’

- Tony Abbott, 30 August 2011.

Is Australia a Special Case?

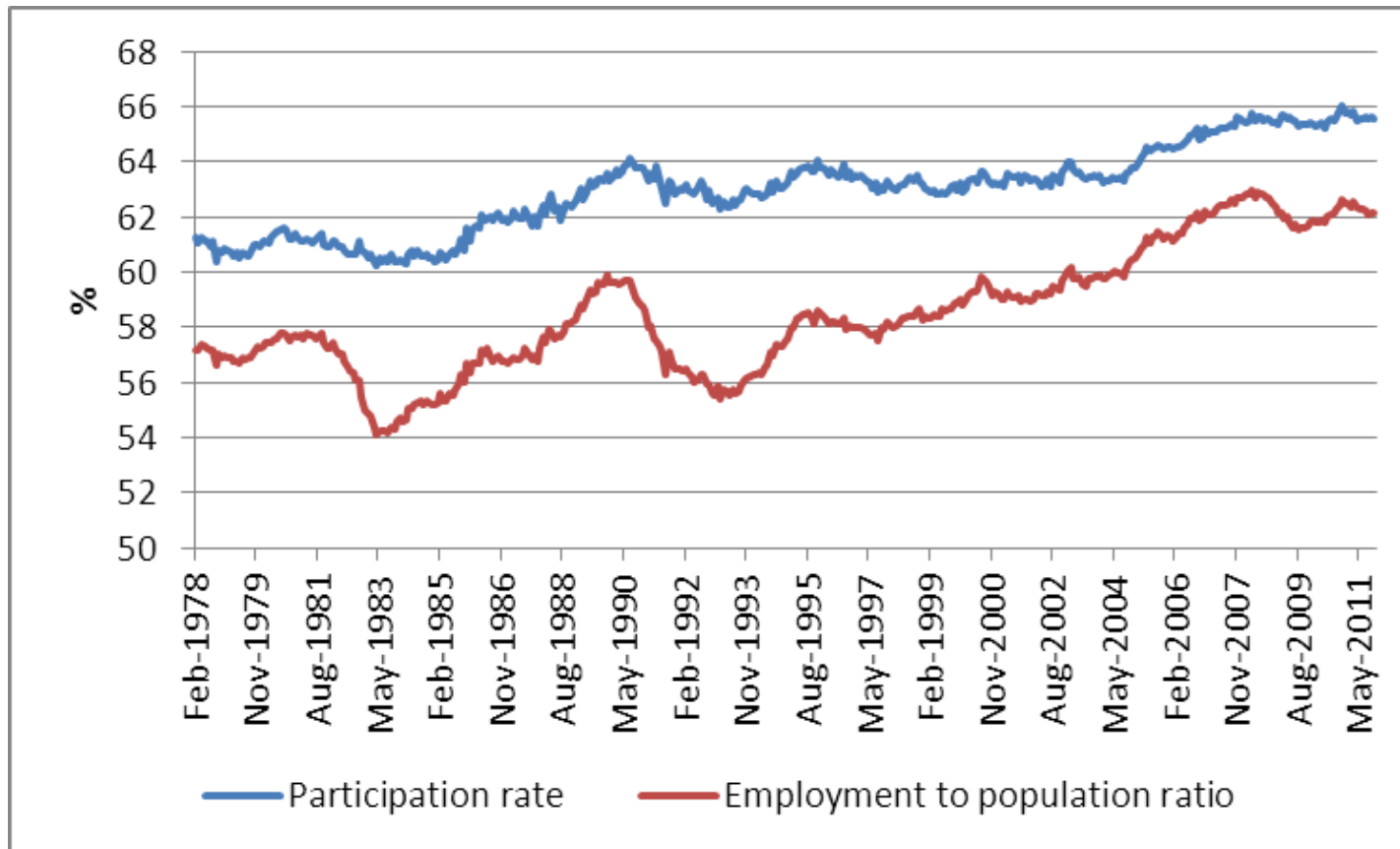
- Income Redistribution
 - The welfare system is best suited for this.
- Optimum Tariffs
 - Australia is a small open economy with little power to impact world prices.
- Maintain Balance of Trade
 - Trade imbalances are not inherently undesirable.
- Job Protection
 - Public Choice argument (see below).
- Infant Industries
 - Mill test: Industry must become successful without need for protection.
 - Bastable test: Industry must generate discounted benefits greater than costs.

Is Australia a Special Case?

- Externalities
 - Arguments tend to be vague. No explanation why externalities are not internalised.
- Strategic Trade Theory
 - Government have a poor track record of picking winners.
- Level Playing Field
 - Foreigners ‘cheat’ by having lower costs or subsidies.
 - Anti-dumping provides make-work for lawyers and economists.
 - Eye of the beholder.
 - Comparative advantage theory does not rely on ‘level’ playing field.
 - Trade is efficient due to difference, not similarity.
 - All arguments about ‘level playing fields’ end in conspiracy theory.

Job Protection

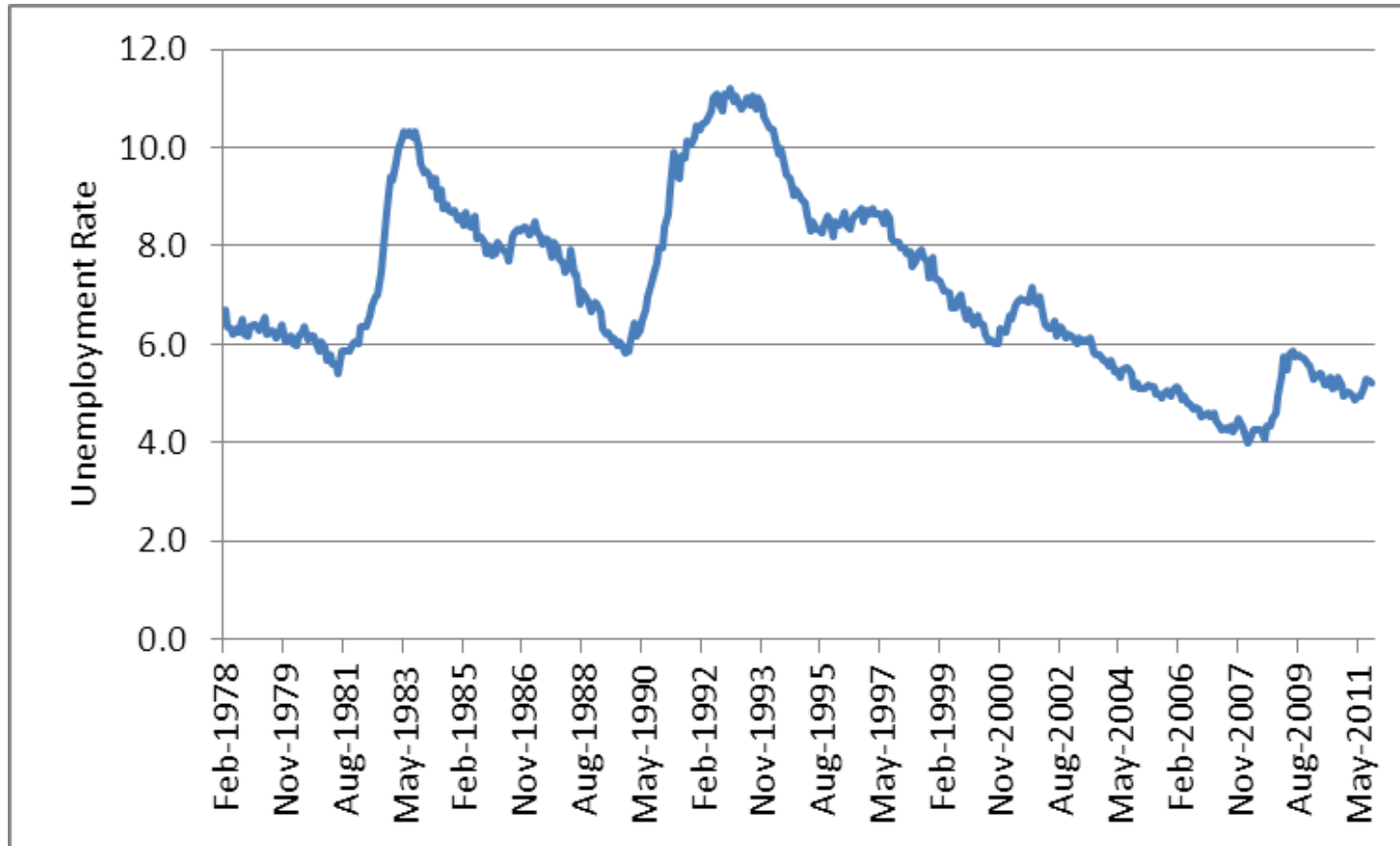
- The economy is creating jobs



• ABS 6202.0 Labour Force, Australia

Job Protection

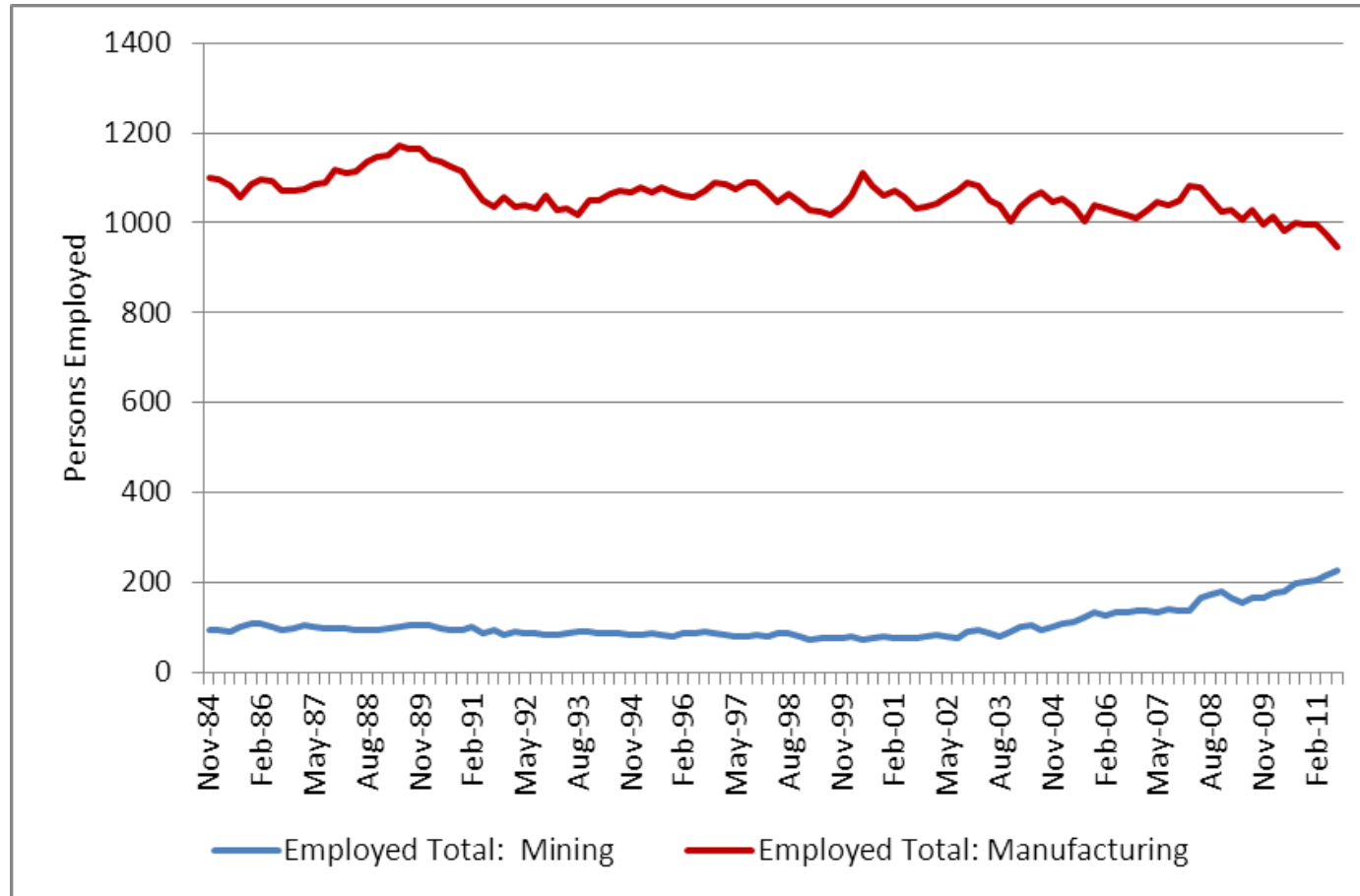
- The economy is creating jobs



• ABS 6202.0 Labour Force, Australia

Job Protection

- The number of manufacturing jobs is falling



• ABS 6291.0.55.003 Labour Force, Australia, Detailed, Quarterly

Is Australia a Special Case?

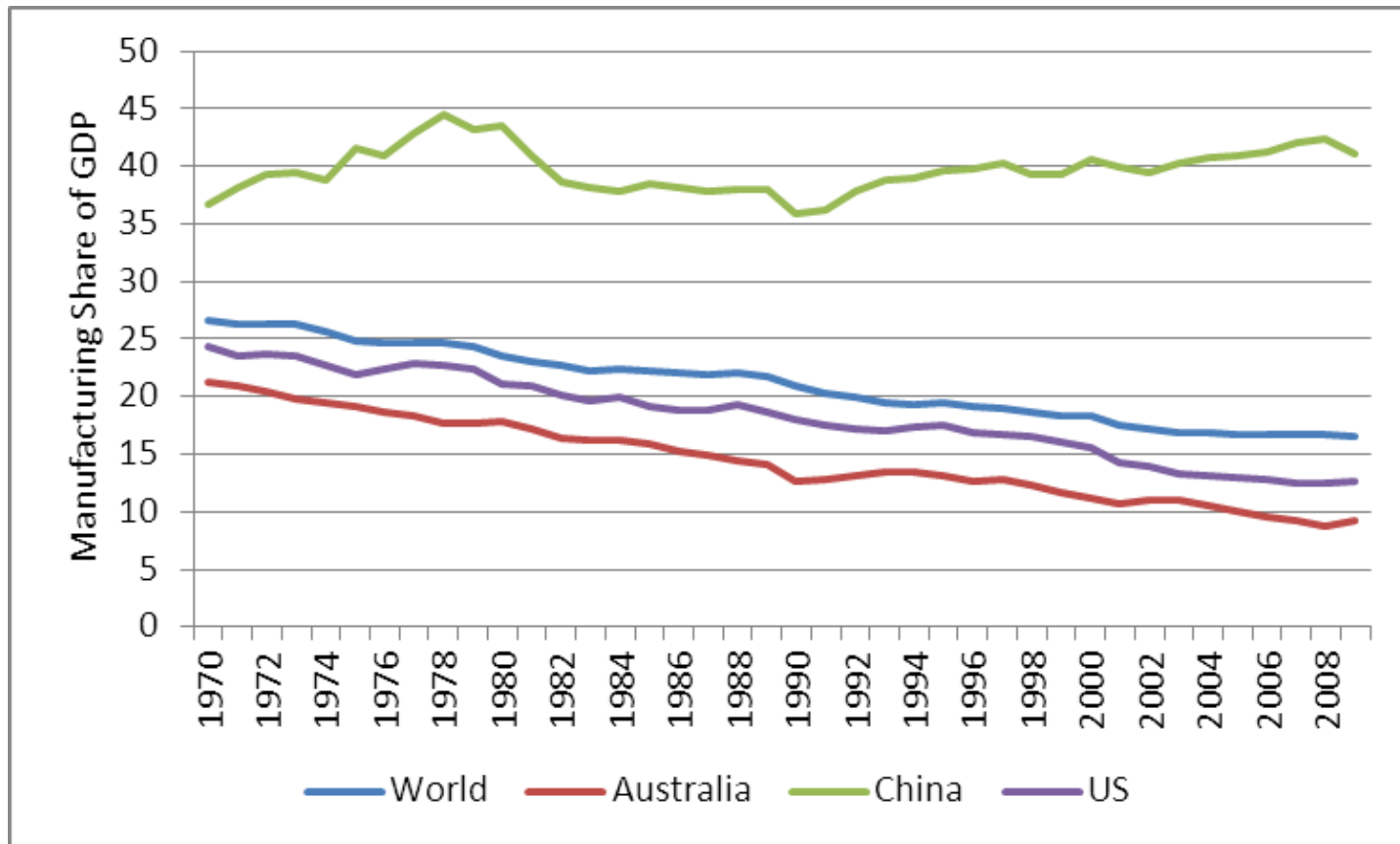
- Job protection.
 - The economy is continuing to generate new jobs.
 - Not manufacturing jobs.
 - Do Australians have a right to a manufacturing job?
- Is Australia a special case?
 - No.

Does Australia have Dutch Disease?

- Has the mining boom led to a decline in Australian manufacturing?
- Dutch Disease
 - Resource boom leads to manufacturing decline.
 - Demand for Australian resources shifts factors of production from manufacturing towards mining.
 - High exchange rate makes it difficult for Australian manufactured goods to compete in international markets.
 - Price Competition only
 - Price.
 - Product.
 - Place.
 - Promote.

Does Australia have Dutch Disease?

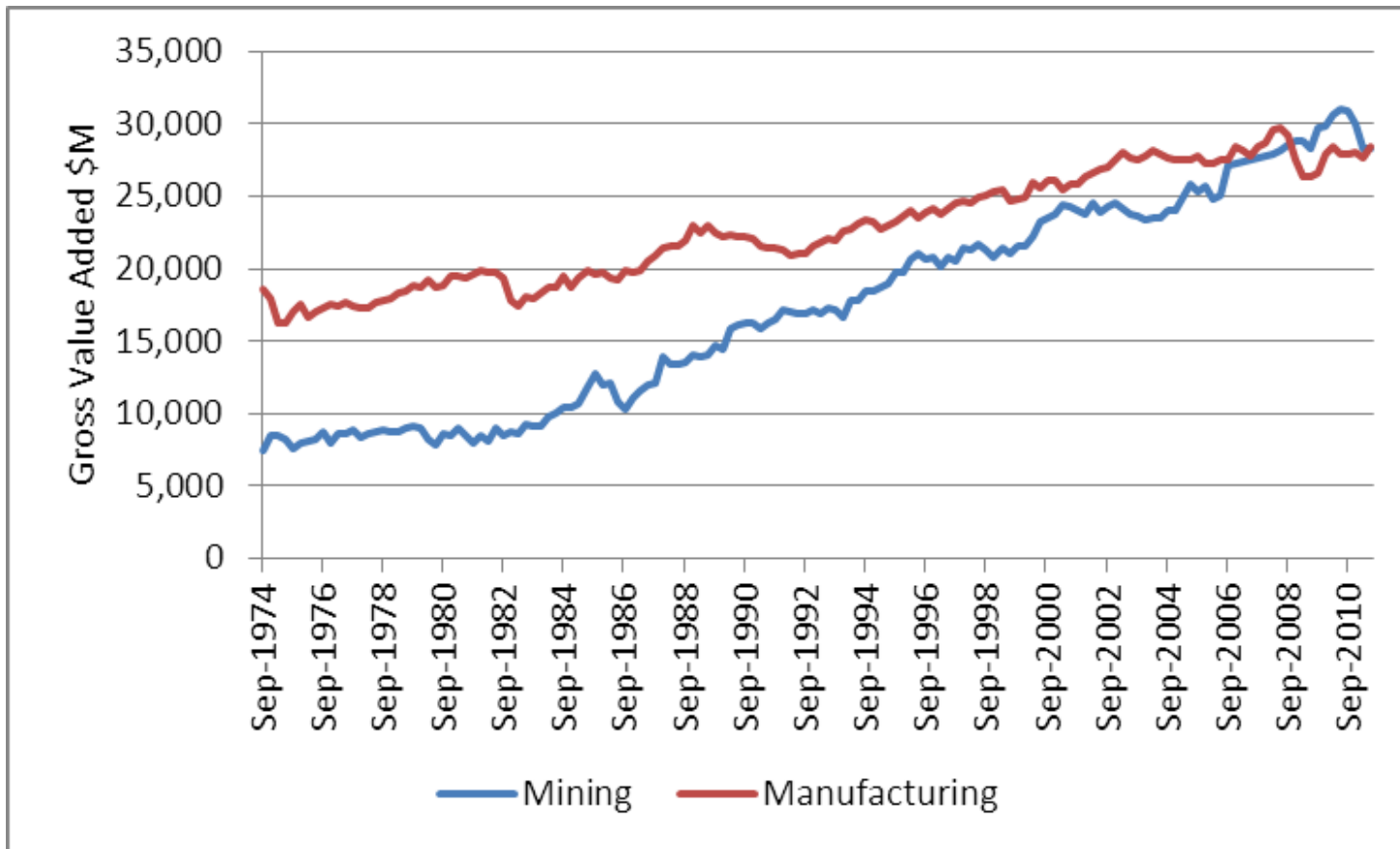
- Has the mining boom led to a decline in Australian manufacturing?



- <http://mjperry.blogspot.com/2011/04/decline-of-manufacturing-is-global.html>

Does Australia have Dutch Disease?

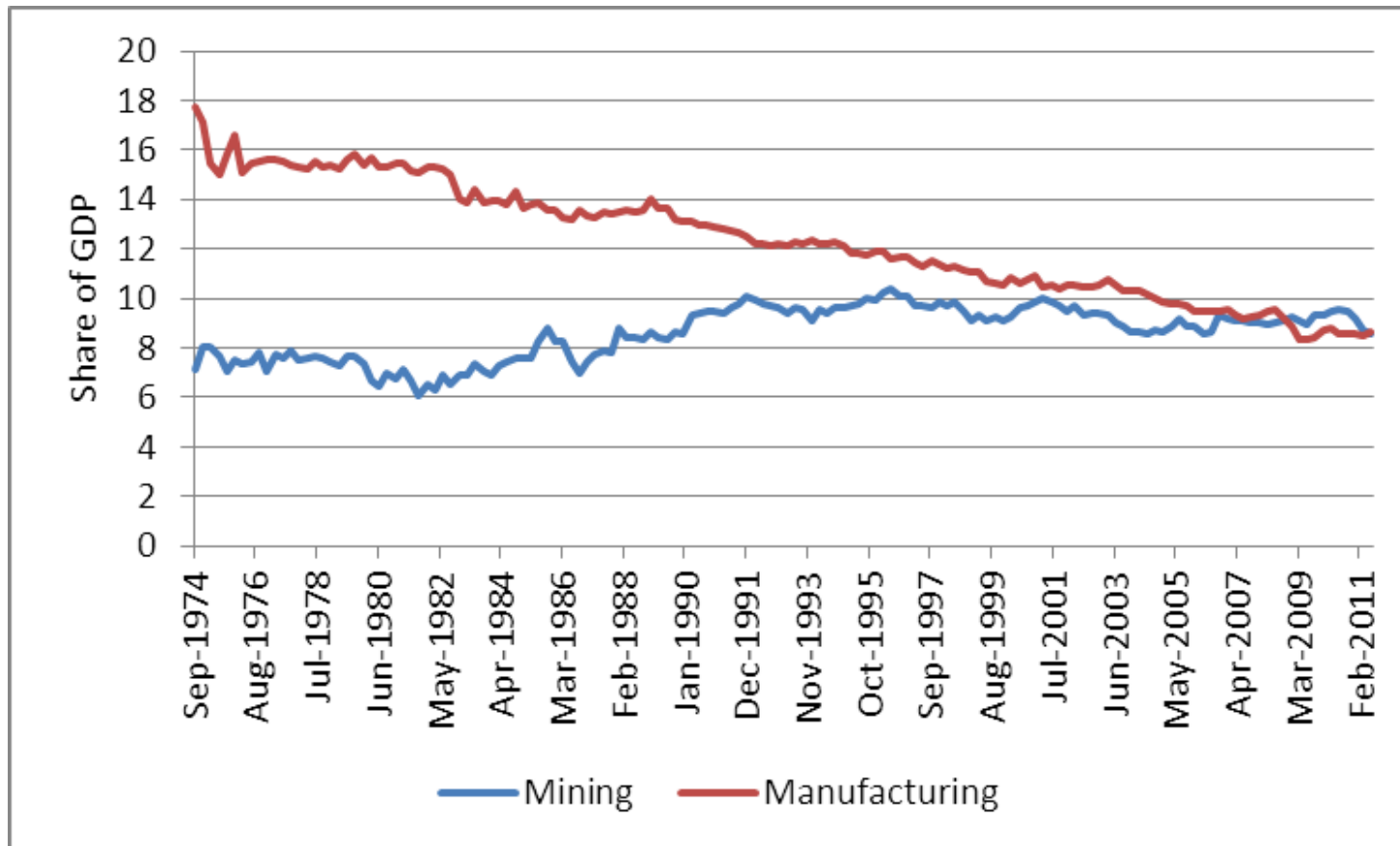
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• ABS 5206.0 Australian National Accounts: National Income, Expenditure and Product (Chain volume)

Does Australia have Dutch Disease?

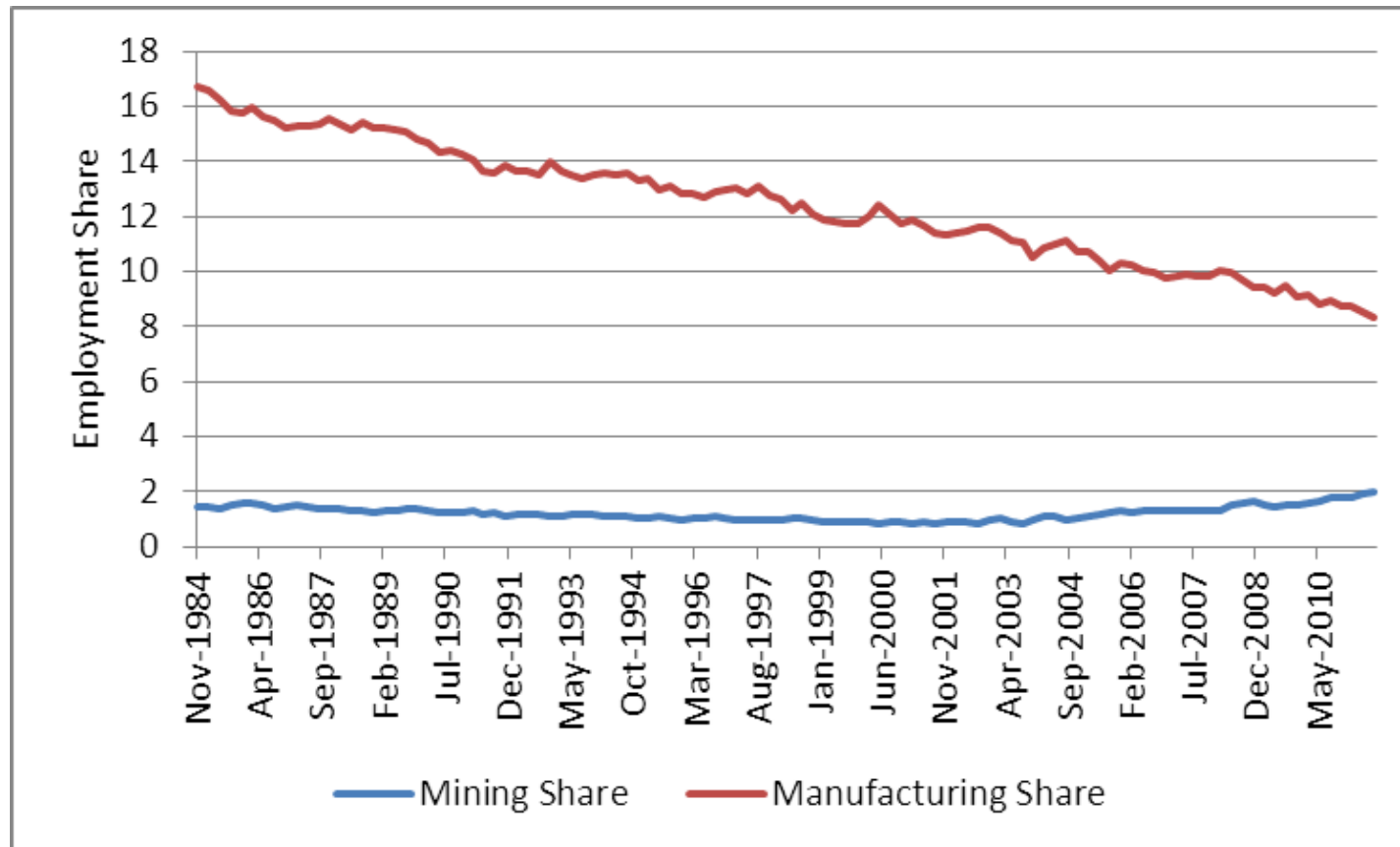
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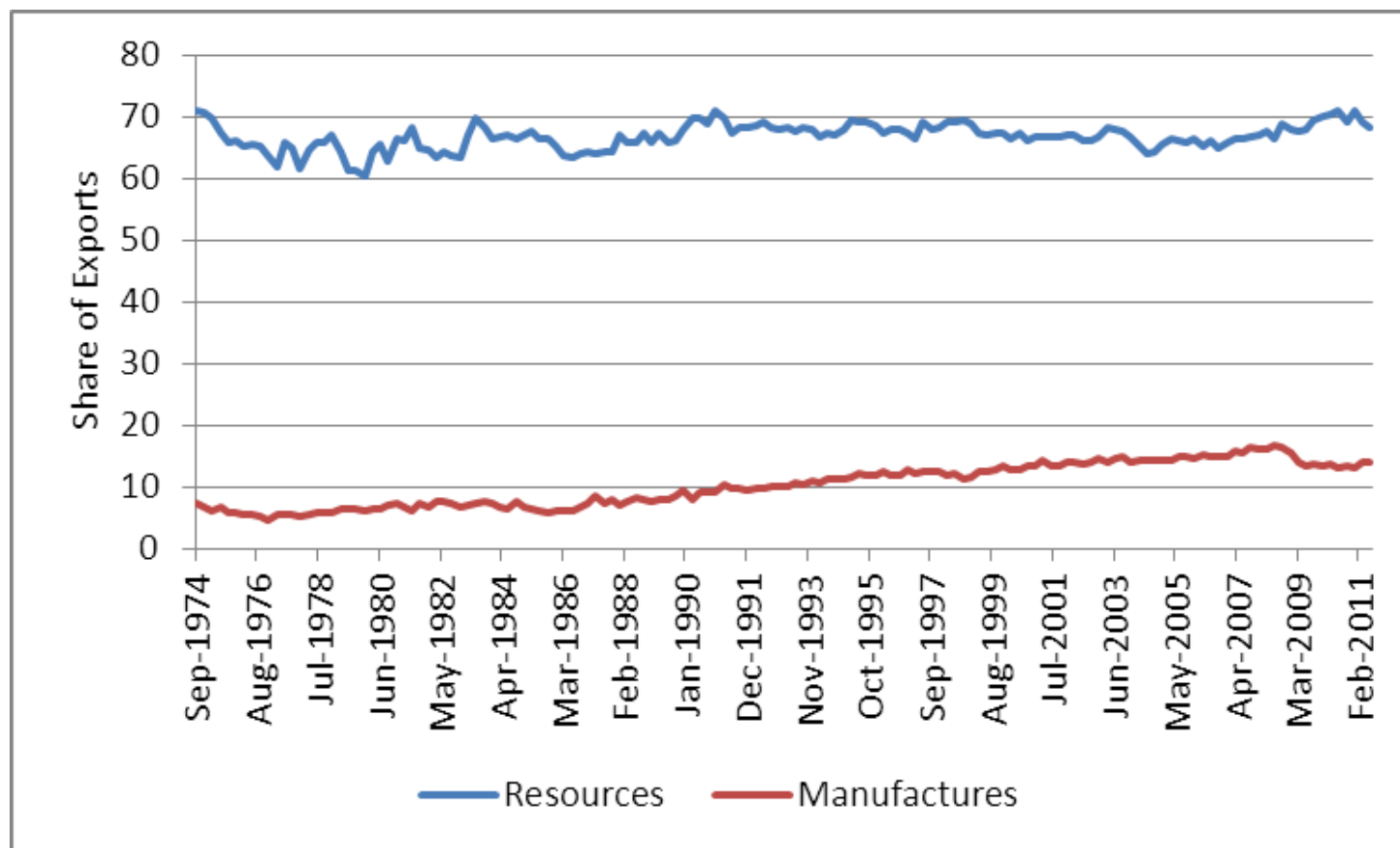
- Has the mining boom led to a decline in Australian manufacturing?



- ABS 6291.0.55.003 Labour Force, Australia, Detailed, Quarterly Table 05. Employed persons by State and Industry

Does Australia have Dutch Disease?

- Has the mining boom led to a decline in Australian manufacturing?



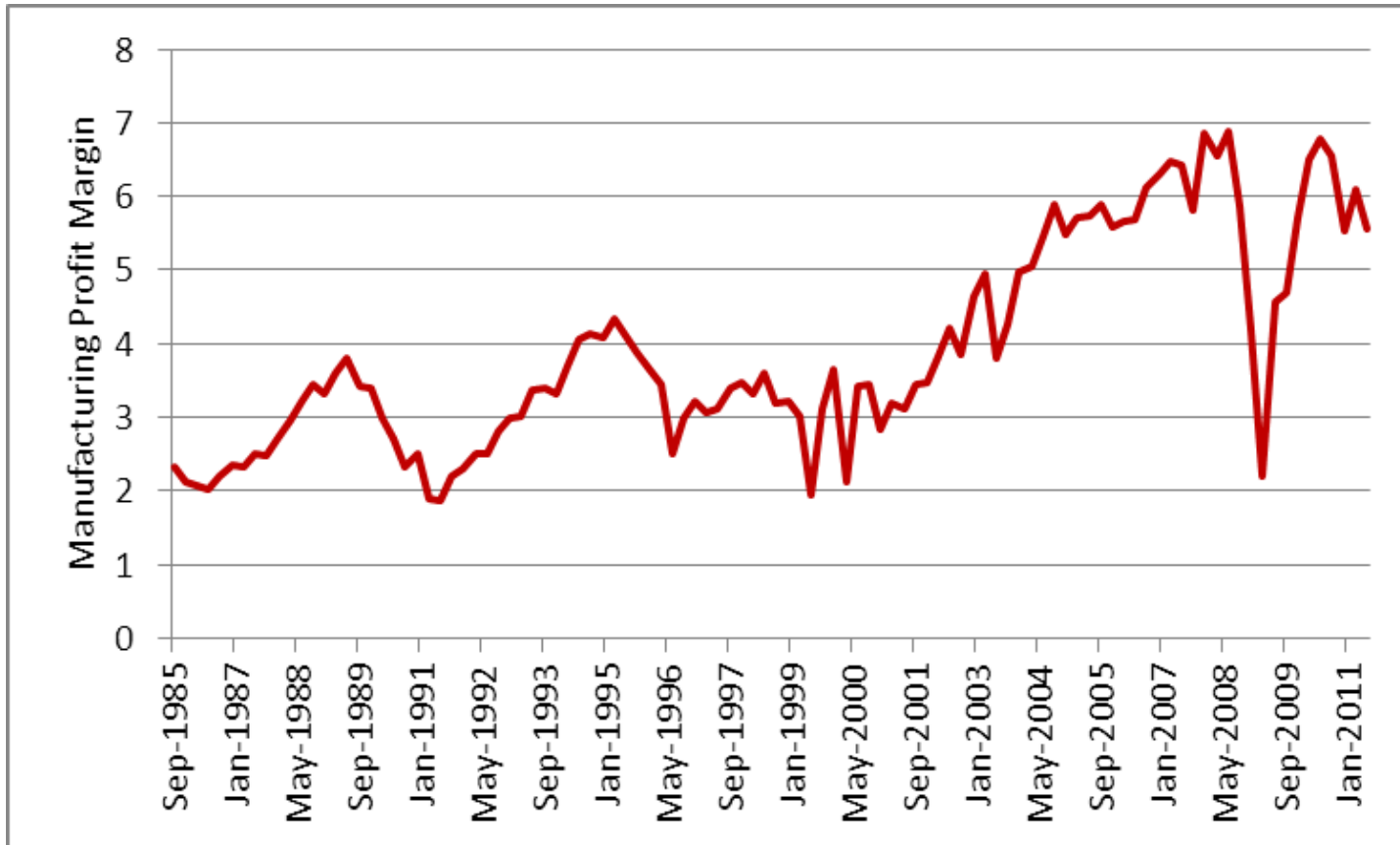
- RBA (Chain volume)

What is going on?

- There are three things happening.
 - Australian minerals boom.
 - Is it really crowding out manufacturing?
 - Creative Destruction.
 - New, low-cost competitors.
 - Improvements in information technology.
 - Internet.
 - Turbulent International Economy.
 - GFC.
 - European debt crisis.
- Increased protection will not address any of these issues.

What is going on?

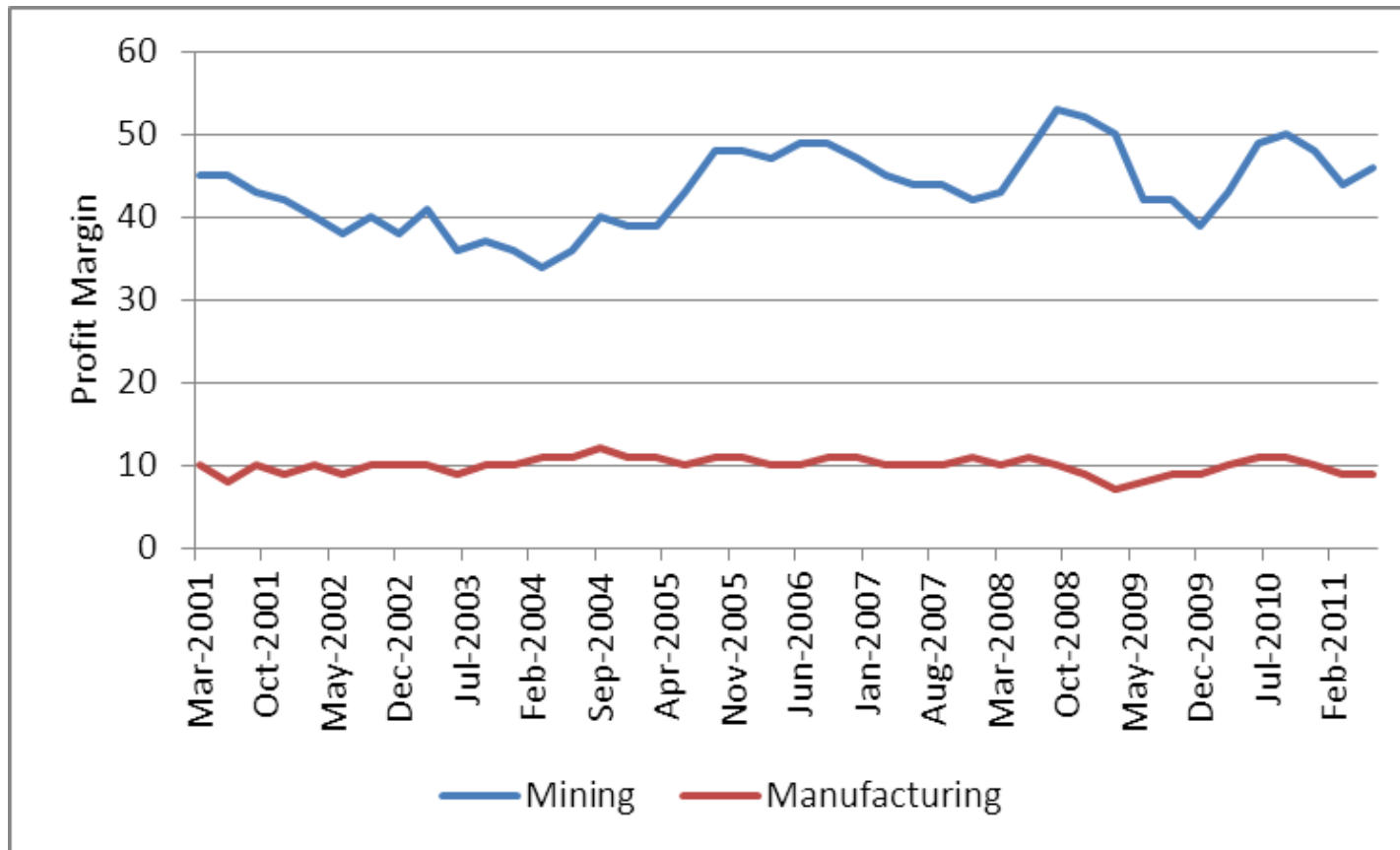
- Profit Margin = Profit before Tax / Sales



- Author's calculations ABS 5676.0 Business Indicators, Australia

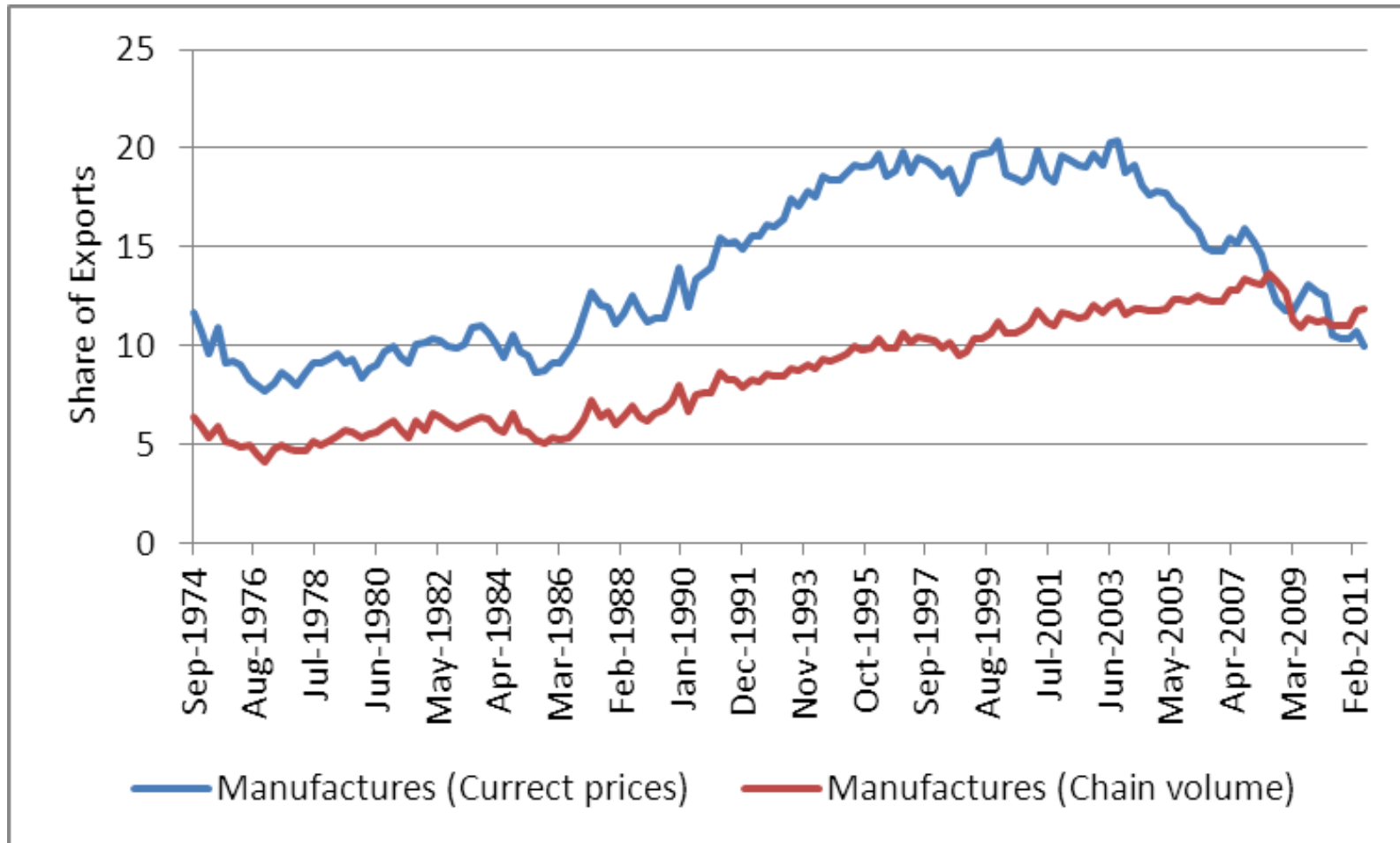
What is going on?

- Profit Margin = Gross Operating Profit / Sales



- ABS 5676.0 Business Indicators, Australia

Things are tough for manufacturing exports



• RBA

Conclusions

- Is Australia a special case?
 - No.
- Does Australia have Dutch disease?
 - No.
- How best to 'protect' the economy?
 - Easy taxes.
 - No carbon tax.
 - No mining tax.
 - Tolerable administration of justice.
 - Deregulation.

Find out more

- Russell Roberts, The Choice: A fable of free trade and protectionism.
- Manuel Ayau, Not a zero-sum game: A paradox of exchange.

- Chris Berg of the IPA has published extensively on anti-dumping and protectionism at The Drum

- I blog at www.catallaxyfiles.com
- I tweet @sincdavidson