

Assess the impact of domestic movements towards free trade on the Australian economy

Free trade is a trade policy that does not restrict imports or exports. Historically, Australia has been moving towards free trade as since the Hawke Government in 1991 who cut tariffs to 15% or 10% and slowly again in 1996 a further cut to 5% and abolishment of quotas for PMV and TCF industries. Subsequent governments continued the Hawke Government's agenda as by 2010, the average tariffs for manufacturing and agriculture were 4.7%. By 2014, Australia's average weighted tariff was 1.3% and provided subsidies only accounted for 3% of farmer's incomes, making Australia the second lowest level of agricultural protection in the OECD. This movement towards free trade had impacts on standard of living, unemployment, BOGS and achieving higher levels of technical and allocative efficiencies, leading to higher economic growth.

Free trade has allowed for foreign competition to enter the economy. Increased foreign competition will lead to lower import prices as well as incentivising domestic businesses to lower their prices and thus greater consumer choice and raising the average Australian's materialistic standard of living. For example, with the introduction of Uber in Australia in 2012, consumer demand decreased for the taxi industry which was comparatively less efficient and more expensive. This can be seen in Figure 1, where since 2016, demand for Uber has increased

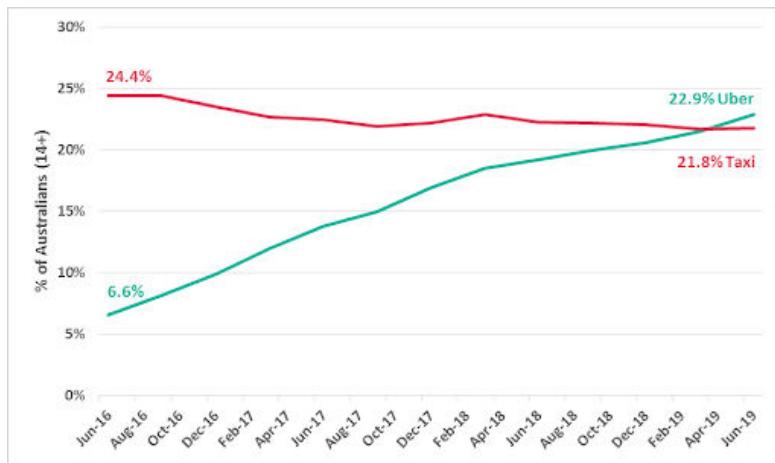


Figure 1 - % of Australians using Uber or Taxi over time

and has exceeded the demand for taxis by April of 2019. The introduction of Uber also paved the way for other international ride-sharing companies such as Ola and DiDi which provides a wider range of consumer choice and its cheaper prices will raise standard of living.

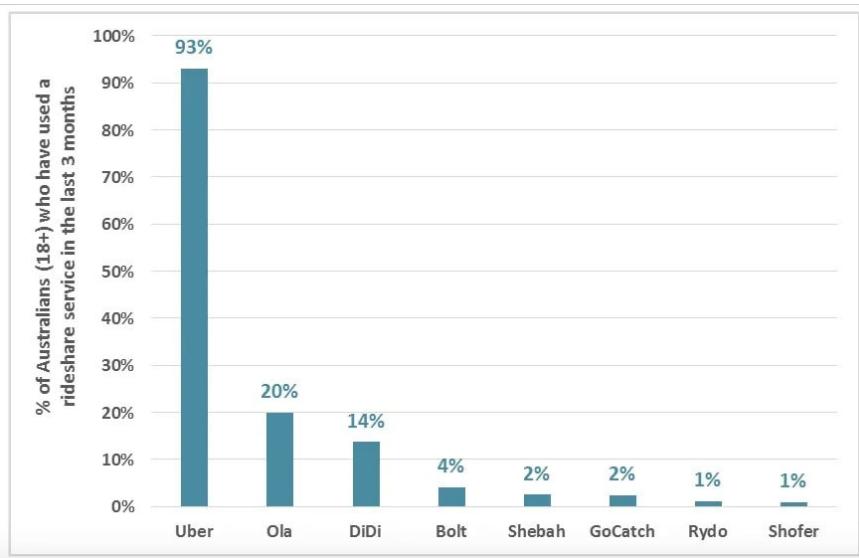


Figure 2 - Column graph showing demand for other ride-sharing services

The increase in foreign competition as a result of free trade has improved standard of living as it has provided greater convenience for lower prices from a range of ride-sharing services compared to when it was only taxis.

The aforementioned increase in foreign competition will also pressure domestic businesses to increase their technical efficiency as those unable to provide an affordable price with relatively low input and relatively high output will not be able to compete. Free trade also allows domestic businesses to source lower input costs from overseas which will lower prices for domestic consumers, lowering inflation which will achieve a higher technical efficiency, increasing aggregate supply.

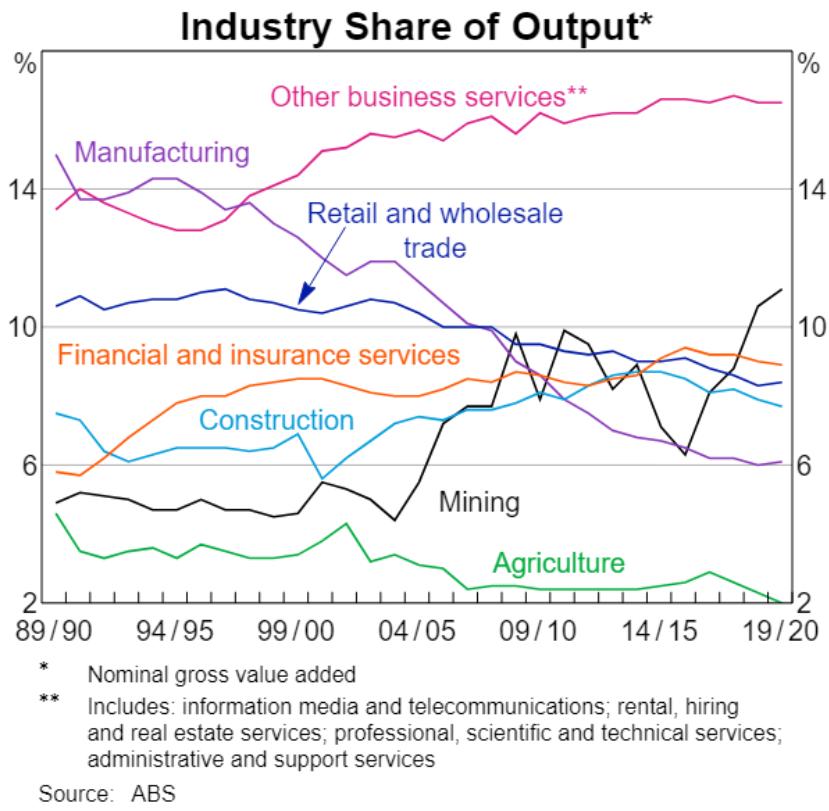


Figure 3 - Industry share of output in Australia

In figure 3, the decline in manufacturing can be seen as overtime, the industry has been inefficient due to its reliance on subsidies as well as input and production costs in Australia are relatively higher than other countries which makes the industry unable to compete with other economies. Its level of technical efficiency is lower than other countries' manufacturing industries whereas there has been a gradual increase in Other business services which include information media and telecommunications etc. which are not affected by Australia's isolated geographical location so the industry's level of technical efficiency is high compared to other economies which allows for the industry to grow and increase Australia's level of aggregate supply.

A short term effect of free trade is the structural unemployment in inefficient domestic industries which are forced to undergo restructuring in order to be able to compete with the foreign industries. Manufacturing in Australia had declined for many decades and one of its largest components was the PMV industry. The PMV industry had struggled to compete with other global economies who had lower labour costs and other input costs which allowed them to be internationally competitive. In 2011, the Australian government discontinued its subsidies, decreasing their government spending in the industry from an allocated \$500 million to \$100,000 million and in the short-term this caused 50,000 workers to become structurally unemployed. This caused the unemployment rate to rise from 5.2% in 2011 to 6.1% in 2013. Since the dismissals tend to be workers with lower skills and thus lower wages, income inequality also worsened as in addition to this, workers with higher wages working for more

efficient industries who had access to global markets would have received more bonuses and growth in wages, further worsening income inequality. Thus, the increased foreign competition will initially cause structural unemployment and worsen income inequality however it will prompt the hysteresis process as well as the industries may start to restructure to be more efficient.

The access to global markets will grow already existing efficient industries and as they expand, they would absorb the jobless workers from inefficient industries and this shift of structural unemployment will lead to higher levels of allocative efficiency and thus greater levels of aggregate supply.

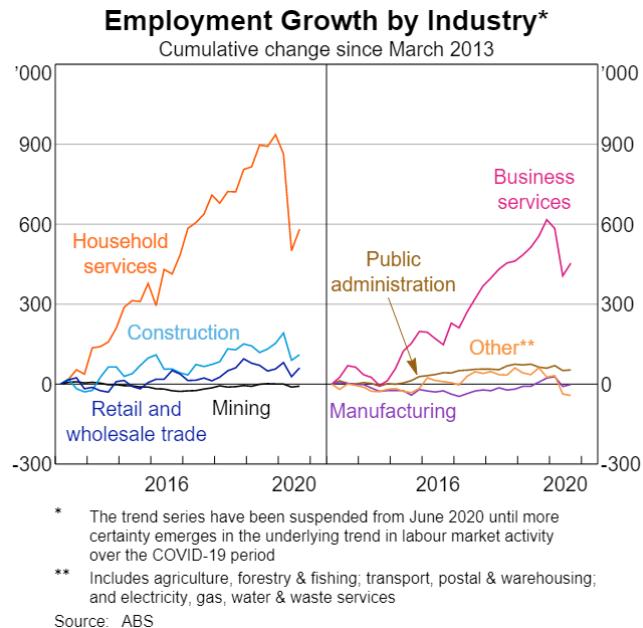


Figure 4 - Employment growth by Industry

As seen in figure 4, mining, retail and manufacturing industries have experienced job losses as they are inefficient in comparison to foreign industries, meanwhile, more efficient industries such as services have experienced significant employment growth (with the exception of 2020 due to COVID-19). This shows that despite the initial increase in unemployment, in the long-term, unemployment will decrease as domestic industries become more efficient as they are pressured from global industries. The unemployment rate has steadily decreased from 2014-2019, decreasing from 6.06% in 2014 to 5.18% in 2019, showing that employment will benefit as workers will update their skills to better meet the demands of both the domestic and global markets.

Another impact of free trade is increased economic growth. The aforementioned increase in levels of technical and allocative efficiency will lead to higher levels of aggregate supply which increases economic growth. The Productivity Commission in Australia has estimated that Australia's movements towards free trade has led to a \$4 billion increase in Australia's GDP which will continue to increase over the next decade. Furthermore, a study done in 2012, named 'Does free trade result in higher GDP per capita? An international perspective',

conducted by scholars from Deakin University, found a correlation between a country's trade freedom index and their GDP per capita.

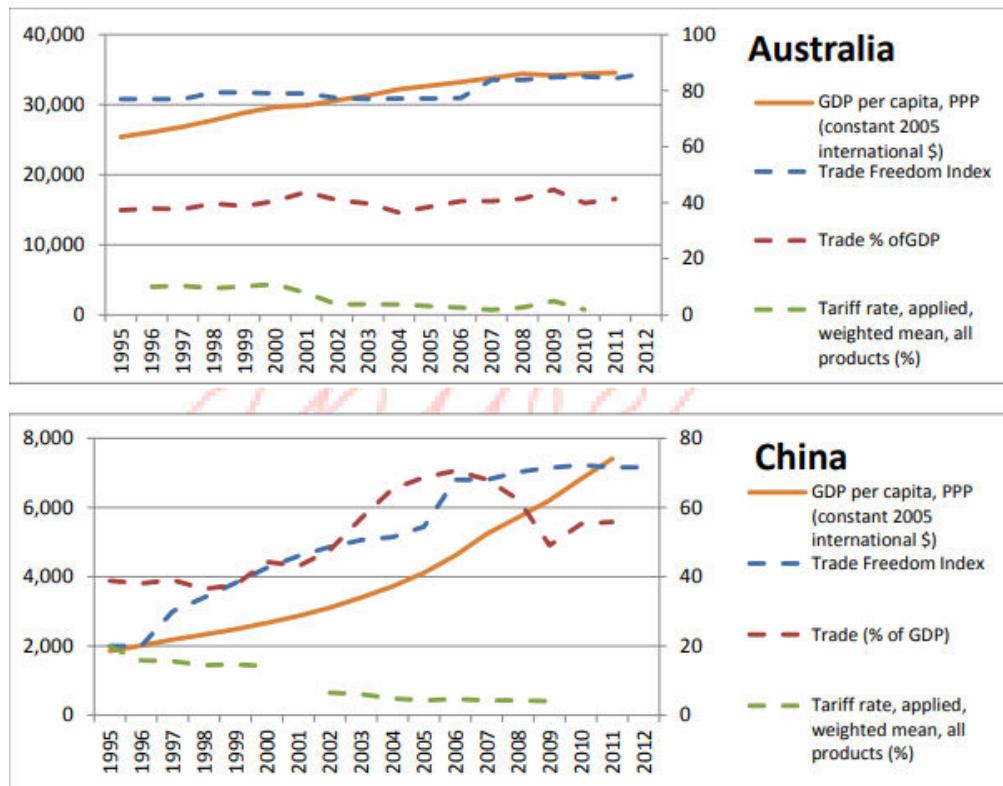


Figure 5 - Graph of Australia and China's TFI and GDP per capita

The graph in figure 5, shows this relationship as the trade freedom index increases, GDP per capita would also increase. This relationship not only applies to Australia and China but also a multitude of other countries as seen in figure 6. Hence, free trade will lead to higher economic growth.

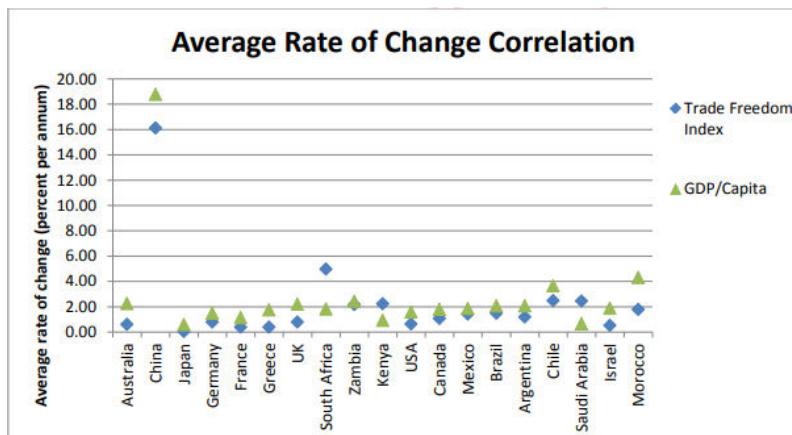


Figure 6 - Graph of average rate of change correlation

The aforementioned increase in aggregate supply would also increase Australia's international competitiveness which will increase exports and improve BOGS. This is because with an increase in aggregate supply, there will be reduced input costs, allowing for domestic industries to compete with foreign industries as prices will now be relatively similar. Free trade agreements such as the Trans-Pacific Partnership (TPP) will boost Australia's level of aggregate supply as input costs such as tariffs are reduced. The TPP is an agreement between Australia, New Zealand, Canada, Japan and Vietnam which totals to 32.6% of Australia's trade. The agreement would reduce 98% of tariffs on Australian agricultural exports which resulted in Japan being able to accept a further 6000 tonnes of Australian rice each year, estimating a \$3.67 billion increase in Australian exports. There were also cuts to tariffs on iron ore, copper and nickel and a reduction in service barriers in areas such as finance, tourism and education. Its effect can be seen in the change of composition of Australia's trade since 1989-90 as in that year, mining made up 40% of Australia's trade but in 2018-19, it had increased to 60% while industries such as manufacturing went from 14% to 6% and rural went from 26% to 10%. This caused Australia's BOGS to enter a surplus of \$83 billion.

Therefore, the domestic movements towards free trade impacted the Australian economy in terms of its standard of living, unemployment, BOGS and its ability to achieve higher levels of technical and allocative efficiencies resulting in economic growth.