

Protection in Australia

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Multiple Choice Answers

1	C	6	A	11	C	16	A
2	A	7	D	12	C	17	A
3	C	8	C	13	B	18	C
4	A	9	B	14	D	19	C
5	B	10	C	15	C	20	A

Short Answer Questions

Question 1

- Free trade is a situation where there are no artificial barriers to trade imposed by governments for the purpose of shielding domestic producers from foreign competition.
- Australian tariff levels have steadily decreased over the past few decades, falling from highs of 36 per cent in 1968-69 to 3 per cent in 2005.
- Australian tariffs are relatively high compared to those of other high income economies, which have generally eliminated all tariffs as part of the WTO and other trade agreements. However, Australian subsidies are very low compared to other high income economies – particularly in the agricultural sector where the US and EU maintain high levels of protection.
- A reduction in protection exposes protected industries to foreign competition. The industry is forced to either restructure or close. If the firm is able to restructure, it will be forced to increase productivity in order to generate more output with the same imports. If the firm closes, the resources in the economy which were previously used by the firm can be applied to more productive areas of economic activity, leading to an improvement in productivity in the economy overall.
- A reduction in domestic levels of protection would harm import-competing firms which relied upon protection to remain profitable. These firms would be forced to restructure or close. However, a reduction in protection levels would benefit firms which use the protected import in their production activities. For example, a decrease in tariffs in the passenger motor vehicles industry would reduce the cost of buying a company car, and that cost saving can be passed on in the form of lower prices. Individuals who were previously employed in an import-competing industry would find themselves structurally unemployed due to the lack of jobs available in the industry. However, consumers would benefit from lower prices and greater choice of goods and services from overseas. The government, in the short term would experience a loss of revenue if the protection were tariff-based, or a reduction in expenditure in the case of a subsidy. However, in the long run, lower protection should generate higher levels of economic growth, leading to an increase in company tax revenue. The government may, however, experience political obstacles to removing protection, particularly in industries with a large amount of domestic employment.

Question 2

- a) The textiles, clothing and footwear (TCF) industry and the passenger motor vehicles (PMV) industry.
- b) The share of rural exports in Australia has steadily declined over the past two decades due to persistent global protection levels. The share of minerals and metals exports, on the other hand, has remained consistently high, increasing by 2007-08 due to a global commodity price boom.
- c) A reduction in protection should improve Australia's export performance. In the short run, a reduction in protection will reduce production costs for any firm which uses imports as a production input, allowing exporting firms to lower their prices and increase their global market share. In the long run, inefficient import-competing firms will be forced to close, freeing up resources for use in industries in which Australia has a comparative advantage, increasing exports.
- d) A reduction in protection would worsen the current account balance in the short term. A reduction in protection would result in less domestic production of import-competing products as inefficient domestic firms are forced to close or restructure. The price of imports would be lower, encouraging higher import consumption, worsening the balance on goods and services and worsening the current account. However, in the long run, resources will flow from inefficient import-competing industries to efficient export industries in which Australia has a comparative advantage. In addition, those import-competing firms which restructured may find niche export markets in which to specialise. This will increase exports, improving the balance on goods and services and improving the current account balance.

Question 3

- a) Global subsidy levels have remained persistently high over the past two decades in high income economies, accounting for between 25 and 40 per cent of farm income.
- b) Subsidies are less inflationary than tariffs, since tariffs directly increase the price of a product, whereas subsidies are merely a payment to producers. Secondly, subsidies provide a guaranteed source of income to producers, which is particularly important to the agricultural sector, whereas tariffs merely artificially decrease the competitiveness of imported products.
- c) The WTO provides a form for negotiating multilateral free trade agreements. The Uruguay round of negotiations, which founded the WTO, provided significant reductions in tariff protection over most manufactured products. The WTO also resolves trade disputes between nations to ensure that trade agreements are complied with. The WTO allows trade disputes to be ended without countries needing to resort to the use of retaliatory tariffs.
- d) Global protectionist policies harm Australia's trade performance and impede the process of structural change in Australia. Global protectionist policies in the agricultural sector prevent Australian exports from increasing their market share in large overseas export markets such as the EU and US. Also, the use of subsidies in agricultural protection also drives down global prices for agriculture which lowers the price Australians are able to charge for their agricultural exports, decreasing export revenues. As a result, Australians face low global prices and low export volumes. In recent years, Australia has unilaterally reduced protection in most industries to less than 5 per cent. In the short run, this worsens the current account deficit due to the increase in imports, however in the long run, new export industries should emerge in areas where Australia has a comparative advantage, increasing exports and improving the current account deficit. However, persistent global protection prevents Australian exporters from increasing their market share, impeding the process of structural change and worsening the current account deficit.