News and Features

What's the big deal?

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John Garnaut cuts through the politics of the free trade agreement with the United States to find the winners and losers.

MARK Vaile arrived in Washington in the aftermath of the Iraq war knowing that no American administration had ever owed so much to an Australian government. The Trade Minister planned to spend a week talking with America's Trade Representative, Bob Zoellick, and return home with an historic trade deal.

What followed was a lesson in George Washington's "great rule" of international relations: political connections with foreign nations will be trumped by commerce.

Vaile wanted to quickly end American protectionism on sugar, dairy and beef, in that order. These alone would account for the majority of benefits Australia might hope to gain from any bilateral trade deal with the United States.

High on his list was for the US to push aside the Jones Act, a curious legal anachronism preventing foreign boats from navigating between any two American ports. It was this trade barrier that meant Tasmania's world class superferries could never find a market in the US.

Vaile also wanted a commitment from Zoellick to relax work visa requirements for Australian accountants, engineers and other professionals (and their spouses), allowing them to effectively sell their services to the US.

These five goals were all towards the top of Vaile's negotiating list. But after two exhausting weeks the Americans had hardly budged on any of it.

Despite Vaile's scurrying between his Washington hotel and the Trade Representative's office, the to-do list was as long as when he had arrived.

Importantly, Zoellick insisted on provisions involving the Pharmaceutical Benefits Scheme (PBS), local media content and quarantine - all of which Vaile had previously promised would not be affected by any trade agreement. But some Australians stood to benefit. It was a question of weighing competing interests.

On February 8, after just 11 months of negotiations, the Prime Minister, John Howard, picked up the phone to George Bush and sealed the deal.

HOWARD'S trade deal with the US split his negotiating team. It has since split farmers, business people, the Labor Party and the free trade community. Political commentators and editorial writers have lined up mainly in support, economics editors have mainly opposed.

Business people have attacked public interest groups, economists have attacked each other's work, film stars have cried in front of politicians and the Government has been praised and pilloried from all directions.

Howard says the deal will set Australia up for the next 50 years. One study, by the Centre for International Economics for the Department of Foreign Affairs and Trade, estimated the deal was likely to add $58 billion to the economy over 20 years, measured in today's dollars.

A study by the National Institute of Economic and Industry Research, for the Australian Manufacturers Workers Union, found the deal was likely to reduce economic output by $47 billion over the same period.

The distance between the two conclusions is a cool $105 billion - equivalent to the annual economic output of Queensland.

Most independent economists, such as Philippa Dee, who recently left the Productivity Commission to join the Australian National University, estimate the economic reality to lie about halfway between the two.

It may be instructive that the Government overlooked the commission when seeking experts to evaluate the deal.

Ian Macfarlane, governor of the Reserve Bank, ducked a broad question about its worth at a parliamentary hearing in June.

But when asked specifically about changes to investment laws, which the Centre for International Economics says would create most of the benefits from the deal, he said: "I do not know about these little movements at the margin."

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WHATEVER the economic and sovereignty concerns, debate is now shifting towards the larger political picture.

"The nature of these agreements is more about building strategic relationships than the net dollar value," says Mark Thirlwell, program director for international economy at the Lowy Institute.

If negotiating the bilateral deal has damaged Australia's multilateral trading credentials, as some economists argue, then that is a "sunk cost" which won't be made worse by going ahead with the agreement now.

John Edwards, chief economist in Australia for investment bank HSBC, says ratifying the agreement could give Australia a seat at the table of any future Asia-Pacific trading bloc.

"I do think there is a tidal wave of FTA deals within the region and we need to be part of this."

But others, such as Dee, warn that the trade deal contains precedents on agriculture, rules of origin, intellectual property, media and pharmaceutical benefits that could make it more difficult for Australia to protect its interests in other forums.

The Opposition Leader, Mark Latham, will decide, probably next week, whether the deal is to sink or survive. He could use economic and geo-political arguments to support a decision either way, or he could reject the deal for social policy reasons.

However, influential Labor colleagues Stephen Conroy and Kim Beazley are pressuring him to defer instead to domestic politics and evade the anti-American tag that Howard has pinned to his chest so successfully.

AGRICULTURE

Mark Vaile admits he "oversold" the potential benefits of the trade deal to farmers. He promised there would be no deal without sugar, but there was.

He managed an 18.5 per cent increase in beef quotas, but this was confined to manufacturing-grade beef (mainly hamburger mince and pet food) and spread over 18 years. It meant that Australia's share of the American beef market could actually decline, according to Australian projections.

Tariffs for beef are to be phased out over 18 years. But the US has reserved the right to employ "safeguards" to raise them again if the quantity of Australian imports or the price of beef changes suddenly.

The outcome for dairy is more favourable and producers are strongly behind the deal. Dairy quotas will triple

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immediately and then grow by 5 per cent each year. This will allow Australia into US markets for cheese, butter, milk, cream and ice-cream for the first time.

Tariffs imposed by the US will be immediately reduced to zero on products including lamb and mutton, canned tuna and horticultural products such as citrus, flowers and macadamia nuts.

The deepest distortions in US agricultural markets are caused by direct subsidies. But these remain unaffected by the deal.

MEDIA

Mark Vaile says the deal preserves Australia's media content laws. But Bob Zoellick says it contains "unprecedented" new provisions. In a sense they are both right.

Australia will preserve its local content requirements for free-to-air television and pay TV. It has also reserved the right to deliver new subsidies and tax incentives to the industry.

But it has bound its ability to introduce new restrictions. Jock Given, author of American Pie: Culture and Trade After 9/11, says: "At a time when all the talk is about the speed and relentlessness of change we are tightly constraining our policy capacity and we are setting those constraints in stone."

The formidable Motion Pictures Association of America - whose members include Sony, Warner Bros and News Ltd's 20th Century Fox - successfully lobbied Zoellick to restrict Australia's ability to regulate new technology.

Australia has tied its regulatory hands in e-cinema, for example, the technology expected to dominate the cinema distribution and exhibition industries.

This technology is also likely to evolve into use for home entertainment.

QUARANTINE

Some in the banana and pork industries believe a recent loosening in the assessment of the risk of introducing disease through imports, and of the cost of this possible disease is related to the trade deal. US pork producers say the agreement will soften quarantine controls, enabling them to substantially increase exports to Australia.

Bob Zoellick has also given support to these theories. In a Senate committee he credited himself for an Australian import risk assessment that benefited Florida citrus growers.

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But there is little in the text supporting a conclusion that the trade deal undermines quarantine. Broadly, chapter 7 merely affirms that quarantine decisions must be based on science.

Australian farm groups are also concerned that quarantine disputes will be resolved through a trade committee rather than a scientific committee.

MANUFACTURING

Most Australian and US tariffs on manufactured goods are already small and will be cut immediately to zero. Tariffs on cars and textiles will be phased out within a decade. But trade gains between the two countries will be partly offset by trade diversion away from other countries.

Australians will now be encouraged to buy tariff-free goods from the US when they may previously have bought them from lower-cost producers elsewhere. Gains to consumers could be offset by losses in government tariff income.

Rules of origin will complicate exports. The "yarn-forward" rule, for example, will nullify tariff gains by requiring that Australia's globally integrated manufacturers spin their own thread or buy it from the US.

PHARMACEUTICAL BENEFITS SCHEME

Australia's pharmaceutical benefits scheme enables the Government to buy drugs in bulk at some of the lowest patented-drug prices in the world. PBS-listed drugs are chosen by the Pharmaceutical Benefits Advisory Committee. Drug firms have lobbied ferociously against the scheme.

The case that the trade deal has undermined the scheme is mostly circumstantial and the Government says there is nothing that would increase drug prices for consumers.

In the US the Pharmaceutical Research and Manufacturing Association gave $US36 million to the Republican Party in just four years. It has 625 lobbyists in Washington alone. Two top US trade officers in the talks with Australia have since joined the medical products and drug industries. Congressmen have even praised the deal for beginning a campaign to raise medicine prices throughout the world.

But the text of the deal is far more ambiguous. It provides for an "independent review" by an Australian expert of decisions by the PBAC that go against companies wanting to list on the PBS.

The Health Minister, Tony Abbott, released details of the review this week, showing it to have no power to overturn PBAC decisions. David Henry, a professor in clinical pharmacology at the University of Newcastle

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and a former member of the PBAC, is concerned that Abbott's apparently benign model may not withstand a subsequent legal challenge. This is because disputes are to be resolved by a trade panel guided by principles of product innovation, but not necessarily public health. Peter Drahos, a law professor at the Australian National University, fears that intellectual property provisions will allow an increase in medicine cost through a "back door".

INTELLECTUAL PROPERTY

In 2002-03 Australia paid $1.2 billion more in trademark, patent and copyright royalties to other countries than it received. Most of this was paid to the United States.

Mr Vaile said in December that intellectual property was "a very important issue" for libraries and other consumers and he would argue against any changes to existing rules.

But Chapter 17 of the final text shows he lost the argument. It lengthens copyright protection for creative works from 50 to 70 years after the death of the author.

There are few, if any, economists who can support these changes on economic grounds. Milton Friedman and 16 other Nobel prize-winning economists argued in the US Supreme Court that a similar change to US copyright laws could hinder creativity.

Chapter 17 also has provisions to extend effective patent protection for innovators when it could be shown an application was unreasonably delayed. The Government says the patent provisions are inconsequential, which is important because drug companies would have had the most to gain.

For example, proton pump inhibitors (a digestive drug) is a class of drug that could have been affected by such a provision, says David Henry, a professor in clinical pharmacology at Newcastle University. The patented drugs cost about $90 a month per patient. But the patent expired recently and generic drug firms were able to copy it, cutting costs to about $40. Henry says this change has already saved taxpayers hundreds of millions of dollars, but this saving would have been delayed had the drug company been able to extend the patent's life.

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