Wynnum 4178
Queensland, Australia
8 September 2010

Review of Trade Agreements Study
Productivity Commission
GPO Box 1428
Canberra City ACT 2601

Dear Productivity Commission

I'm writing to make a submission to the Study.

I wish to make three points.

1. First, I attach as part of this submission an article pointing out the lack of a logical basis for Australia's current trade policies and the damage that the dismantling of trade barriers does to producers in a net importing country. This article has been published in the magazine *Public Administration Today* and is copyright.

2. Second, I urge the Commission to include a section in the report presenting a coherent theory to underpin its analysis. The theory of “comparative advantage”, which is normally cited to support trade liberalisation, is inapplicable when capital is mobile across international borders, as is now universal.

   The heading to Section 8.1 of the report suggests that a theory is to follow, but no such is visible.

   The Draft Report presents the results of econometric analysis and modelling, but these tools are meaningless unless they are grounded in a serviceable theory based upon justifiable assumptions.

3. In several places, the Commission refers to benefit to consumers of cheaper goods. This list should be balanced by an account of the damage done to producers when goods and services that can be manufactured in this country are discarded in favour of debt-fuelled importations.

I would be grateful if you would not release the attached article on your website unless and until I can gain a clearance from the Editor of the journal in which it has been published previously.

I thank the Commission for the opportunity to make a submission.

Yours faithfully

(*Signed*)

Geoff Edwards

Edwards, Geoff. Oct.-Dec. 2008. "Collision Course: PM's Advocacy of International Financial Regulation Confronts DFAT's Free Trade Zeal". *Public Administration Today*. Pp.64-75.

COLLISION COURSE: PM'S ADVOCACY OF INTERNATIONAL FINANCIAL REGULATION CONFRONTS DFAT'S FREE TRADE ZEAL

Pity the Minister for Trade Simon Crean! While he is travelling the globe trying to convince the rest of the world to liberalise markets in goods and services, the Prime Minister is travelling the globe trying to convince world leaders that a new international order is required to regulate financial services. Mr Rudd has observed:

> "But the origins of the current crisis lie in the largely unregulated sectors of our financial markets that brought out the absolute worst in the most extreme forms of capitalism" (Rudd 2008).

Since 1983, Australia has been one of the loudest advocates for eliminating domestic and international checks and balances on trade in financial and other services, making repeated commitments under the aegis of the General Agreement on Trade in Services (GATS) with precisely that purpose.

Indeed, a deregulatory agenda is still, shamelessly, being advanced under GATS at the World Trade Organization (WTO). Trade negotiators are insisting that under the current Doha Round governments should place ever stronger constraints on their capacity to regulate services, financial services in particular. "The world's largest banks, insurance companies, and brokerage houses have dominated trade negotiations on services... Unlike other service sectors, financial services have been under negotiation almost continuously...". (Gould 2008). Meeting as recently as 12 November 2008, the WTO advocated more co-sharing of risks by international financial institutions, meaning, shift responsibility for the mess onto world taxpayers.

A new government has an opportunity to scrutinise the enthusiasms of the previous administration. Minister, I plead with you to reconsider trade orthodoxy.

SETTING THE SCENE

In the previous Government's benchmark White Paper on foreign affairs and trade, *Advancing the National Interest* (Clth 2003), the national interest is defined as "the security and prosperity of Australia and Australians" (2003:vii) — nothing else. The document clearly considers free trade and free investment as being the only pathway (in the international arena) to prosperity, as revealed by the title of Chapter 4: "Building Prosperity through Market Liberalisation" (2003:49ff), the only chapter dealing specifically with economic prosperity. Liberalisation is equated with `free trade'.

The materials that DFAT has published argue only one side of the case, as if there is no alternative. In endorsing free trade uncritically the Department is not alone: it mirrors or is mirrored by the pre-eminent sources of economic advice available to the Government (such as the Productivity Commission and federal Treasury) and consultants such as Mortimer (2008). This chummy mutually reinforcing debate in Australia's policy community is paralleled by pro-free trade policies promulgated internationally by the Bretton Woods economic institutions (WB, IMF, WTO) and the governments of other Anglo-Saxon countries (notably UK, US, Canada, New Zealand). However, the official unanimity does not reflect the evidence of adverse economic effects in countries which have opened their borders to trade, or the critiques by NGOs, or the theoretical critiques in disciplines other than neo-classical economics.

Any robust policy should sit within a conceptual framework that includes a body of *evidence*, a coherent *theory* and disinterested *logical analysis*. These three headings are used to structure the following material.

THE EVIDENCE

Good analysis relies upon honest treatment of evidence. By this test, many of the claims made for free trade are exaggerated, overly optimistic or plain fictional.

Results Domestically Have Confounded Predictions

If Australia's foreign debt does not convince readers that our nation's trade policy is dysfunctional, then the outcomes of recent free trade agreements should be cause for reflection.

First, the debt. Although the leapfrogging price of coal caused the current account balance to tip positive in the June 2008 quarter, this was the first quarterly trade surplus in 25 quarters. Net foreign debt is now an unpayable $600 billion, or 53% of GDP. This is more than twice Argentina's debt of c.$A258 bn during the peak of its economic and political crisis at the beginning of 2002. Only the confidence of creditors stands between our country and a comparable crisis, and our rising dependence on imports of petroleum (self-sufficiency declined by 11% last year) makes Australia's situation terminal.

Second, the performance. Mortimer (2008) in reviewing the Singapore, Thailand and US free trade agreements was forced to concede that "As import growth has outstripped export growth to date, Australia's trade balance with all three countries has deteriorated." He had no choice: in the first 24 months after the agreement with the USA (A-USFTA) came into operation, Australia's trade deficit with the USA *worsened* by $3.25 bn (GTW 2007), confirming the predictions of the critics. So much for assumption-based economic modelling. Somebody in DFAT should say 'sorry' for misleading the public by claiming in advance that there would be a net *benefit* of $2 bn per annum after the first year.

The lame excuses Mortimer offered were in language worthy of Sir Humphrey Appleby: "...unrealistic expectations of what FTAs could deliver...limitations inherent in the instrument...Australia has relatively limited negotiating coin...the benefits...can be eroded by...factors outside...the agreement such as excise taxes."

Despite the collision of trade orthodoxy with reality, Mortimer was remarkably optimistic that further liberalisation would benefit Australia. In doing so he was only conforming to a pattern. Mark Vaile, previous minister in 2003: "The [US] FTA also is an opportunity to...attract additional investment, and therefore more and better paid jobs for Australian workers".

Poking further back into the archives, governments in the 1980s and 1990s promised that trade liberalisation and micro-economic reform would transform Australian exporting into competitive success, especially in sunrise industries. Today Australia is as dependent upon exports of unprocessed raw materials as ever, having knowingly shut down large sectors of manufacturing and applauded firms which shaved costs to themselves by outsourcing IT development to India.

Results Globally Have Confounded Predictions

Engagement with the international economy has featured in the successful economic development of probably all prosperous countries, including Britain, the US, western Europe, Japan — and not least, Australia. However, it has been through *managed* not unrestricted trade (TWN 2001:23,24; Fallows 1993; Ormerod 1994; Rodrik 2001; MacEwan 2002).

Even on its own terms, growth in GDP is not correlated reliably with openness of borders to trade: many growth centres would have been snuffed out in their sunrise stages in the absence of protection. Australia's infant industrial economy found its feet behind tariff fences of a kind which it now seeks to break down for all countries including itself. Chang (2003) explained this process, termed "kicking away the ladder".

An evidence-based report co-sponsored by the UN Development Programme, the Rockefeller Foundation and others (Malhotra 2003) disproves the assertion that trade and investment drive economic growth. "Trade expansion neither guarantees immediate economic growth nor longer-run economic or human development. Internal and external institutional and social pre-conditions largely determine whether and to what extent a country or population group benefits from trade." (2003:21). "...integration with the world economy is an outcome, not a prerequisite, of a successful growth strategy." (2003:28). "Cross-national comparisons reveal no systematic relationship between countries' average levels of tariffs and non-tariff barriers and their subsequent economic growth." (2003:29). "...no country has developed simply by opening itself to foreign trade and investment." (2003:30). "The quality of a country's public institutions is a crucial—perhaps the most important—determinant of its long-term development..." (2003:36). "The only systematic relationship between countries' average tariffs and non-tariff restrictions and their subsequent economic growth is that countries dismantle trade restrictions as they get richer" (2003:41).

DFAT's website cites a WTO report claiming that trade helps countries out of poverty, but then the boosterist WTO would say that. UNCTAD's more balanced evidence does not find a direct relationship between poverty and trade. Poverty has deepened in the poorest countries although they have opened their borders. There is nothing new about these findings: Pettman reviewed literature and evidence in 1982 and found that economic growth and free trade are correlated with increasing inequality and retarded development. Pettman's analysis is striking for its modernity: his description of the camps occupied by "marketeers" and their critics would apply today. Neo-liberal trade and development orthodoxy has held sway despite contrary evidence for more than 25 years.

THE THEORETICAL BASIS OF TRADE POLICY

The intellectual case for free trade traces its origins to the theory of `comparative advantage', expounded by classical economist David Ricardo in 1817. *If certain pre-conditions are satisfied*, two countries can both benefit from trade if they specialise in manufacturing or growing those goods which they can produce most efficiently. Gains arise mathematically from the differing opportunity costs of capital within each country. For trading to be gainful to both parties, it is neither necessary nor sufficient to demonstrate 'absolute advantage' in endowment of resources or other intrinsic capacities (Lipsey et al 1981).

Ricardo's comparative advantage remains at the centre of modern theories of trade, despite subsequent refinements such as the neo-classical Heckscher-Ohlin-Samuelson formulation (see Shaikh 2003). Ricardo's theory however rests critically upon pre-conditions additional to those common to mainstream economics generally. (Trade theory shares a theory of micro-economics with other branches of economics). Various authors express the trade-specific assumptions differently: Stretton (1999) for example listed six; here are three:

Employment is full. The labour or capital displaced by imports can be readily absorbed by more `efficient' enterprises, both before and after the trade, in all participating countries. This assumption is invalid. Through mechanisation and the drift of rural labourers to the cities, most countries now have surplus labour. There is no point in saving labour internationally through specialisation, if workers at home are left idle (Schumacher 1943:6). The International Labour Organization (ILO 2007) has reported that "the number of people unemployed worldwide remained at an historical high...of 195.2 million...in 2006 despite strong global economic growth."

Labour and capital are not mobile across international borders. This is partly valid for labour, which is inherently relatively immobile. For capital, however, the assumption of immobility does not hold under conditions of free foreign investment where liquid money chasing fractions of a percent advantage is transferred around global financial markets at the speed of electronics.

Transaction costs such as transport are negligible. Indeed, through containerisation costs of transport have been low enough to facilitate rapid growth in trade (Rees 2002). Transport costs scarcely feature in the trade literature, but when fuel prices rise after oil production peaks and emissions trading kicks in, this pre-condition will be unattainable.

Alongside these basic assumptions is a requirement that countries do not run persistent trade deficits. In reality producer countries with high production costs tend to suffer enduring trade deficits funded by inflows of capital. The margins that a country can gain by internal specialisation are dissipated in servicing external debt. "Thus free trade does not make all nations equally competitive, as is argued within standard trade theory.

Rather, it exposes the weak to the competition of the strong” (Shaikh 2003). Now, conversely, countries are forced to export in order to service the debt that previous unbalanced trade has created (Rees 2002).

Free trade economists slip illegitimately between classical Ricardian analysis (in which countries appear as a unit of analysis) and modern neo-classical economics grounded in the notion of the self-interested rational consumer (and in which countries have an elusive status — Jones 2002). Modern factors of production include technology, intellectual capital (Schumer and Roberts 2004) and fossil energy which do not behave in the same way as classical factories. Ricardian `old' trade theory has been accompanied in the past two decades by `new' trade theory which admits that a country may gain from trade even if it does not enjoy comparative advantage, simply through economies of scale and niche opportunities when competition is imperfect (Palley 2003). This explanation however seems like patching old wineskins, for it contradicts the assumption of aggregation lying at the core of micro-economics (that an economy is the sum of the actions of numerous rational agents). If there is such a thing as economy of scale, then aggregation cannot hold.

Consequences of the Assumptions

If just one of its assumptions is found invalid, a theory collapses. At least two of the three foundations of trade theory mentioned are insupportable. Comparative advantage is a special case in which unemployment does not exist in either trading partner and capital is immobile: the pre-conditions are tight (Batra 1993). The weaknesses are not merely market failures in an otherwise sound theory, they are inherent (Keen 2001; Palley 2003; Daly 1993). The lack of an adequate theory does not invalidate a policy or specific actions derived from it. However, it does invalidate the theory as an organising principle. Without an adequate theory, success or failure becomes a matter of trial and error, with no guarantee that what worked in one circumstance will work somewhere else.

Etherden (2005) argued that the defect in trade theory goes deeper than Ricardo, to English philosopher Bentham (1748-1832). The notion that both parties to a trade gain Benthamite `utility' or else the trade would not occur — that markets are self-regulating — disregards the prospect of unequal power. The theories developed by the classical political economists of the 1700s and early 1800s were based on observations of village-scale transactions among craft-based participants, so lack a theory of power adequate for analysing international trade by global corporations (Nell 1988).

Modern village peasants with large debts to a local moneylender and forced to penury by falling prices for their cash crops cannot bargain with companies buying on behalf of wealthy western countries on remotely an equal basis. Nations are in a comparable predicament. Not even a developed country can negotiate a free trade agreement on an equal basis with the USA. Australia tried, but was comprehensively out-negotiated (Weiss et al 2004).

Ironically, globalisation does not make free trade inevitable, it negates its basis. Advocates of free trade (e.g. Oxley 2003) set out to remove barriers to movement of capital and labour when this very practice invalidates the theoretical foundations on which trade policy relies.

If comparative advantage does not apply because of the inapplicability of its pre-conditions, the default position of absolute advantage prevails. In practice, this plays out as benefiting the well-endowed countries at the expense of the weak; and their advantage accumulates.

Space does not allow pursuit of this fundamental defect here but it can be said in summary that modern trade policy lacks an adequate theoretical justification, even within the framework of orthodox neo-classical economics.

ANALYSIS

In this section, some aspects of trade policy and the process by which it is formulated are analysed to assess whether a policy of free trade makes any practical sense.

Trade Activity — To What End?

Most official expositions such as DFAT's submission to the Senate Committee on Foreign Affairs in 2003 portray the goal of trade as increased growth and the goal of growth as increased standard of living. WTO language elevates trade as an end goal: for example, it defines a country's regulation as an unnecessary obstacle to trade if its objectives can be achieved by less trade-restrictive measures.

There is a circularity in these arguments. The promises of free trade depend upon global economic growth, but growth depends upon free trade. The practical case for free trade rests on its argued capacity to increase the throughput of goods and services, by accessing cheaper or better products.

Economic Efficiency

Australian producers are urged to become `internationally competitive' if they are to succeed on world markets. But competitiveness is a variable, not an objective standard. The prices for which goods and services can be sold internationally depend on several diverse ingredients, notably:

1. The *direct costs of production* and the `efficiency' with which the producer uses input resources.
2. *Factors influencing supply and demand* – balanced by the market – for example, consumer preferences, natural disasters, advertising...
3. *Domestic wage-price cost structure* – affecting purchasing power within a country – for example, proximity of resources, taxes, interest rates and institutional constraints...
4. *Inter-country differences* in natural conditions – comparative factor endowment – item 3 played out on a global canvas.
5. *Exchange rates* of the relevant currencies.
6. *Tariffs or subsidies*, cartel or governmental quotas on production, transfer pricing by corporations and tax evasion.

The marvel of the market *for consumers* is that these factors are smoothed out invisibly before goods and services appear in the shops for purchase. But *for producers* in a mixed economy only the first two ingredients are reasonable variables. To require them to compete on the others is unjust and anti-intuitive.

In common language, 'efficiency' refers to capacity to produce a good less wastefully, confining the term to the first ingredient. Traditionally, efficiency referred to the number of labour hours spent in making a product (Morris 1993:145). But in economics, `efficiency' refers to capacity to market something at a lower price, embracing all ingredients. `Economic efficiency' is achieved when goods transact in pure competitive markets. Many economists define it in terms of `value of output for given value of input resources', which sounds as if it approximates the first, but in fact embraces all because in economics `value' is measured by price.

Sanders (2004) contrasted `ecological efficiency' — "extracting the maximum amount of service from a given quantity of natural capital" — with `economic efficiency' — "achieved when prices at which goods and services are marketed are at a minimum. Economic efficiency biases all values to the present (because of discounting) thus breaching the condition of inter-generational equity which is inherent in any notion of sustainability. Defining `efficiency' in a resource-based rather than market-based manner fundamentally changes the implications for public policy."

The six factors listed above are considered in turn.

Direct costs of production
There is nothing normative or absolute about costs. The prices of raw materials, labour, services, fees, transport and all other inputs are variously subsidised or taxed in a mix unique to each polity or industry and continuously changing.

Price in market transactions is disconnected from the quantum of flows of materials and from non-commodified public goods. This works against husbanding a society's patrimony of natural resources. Markets regard natural resources as the free gift of nature until some human agent has commodified them, so do not prepare for their exhaustion and do not signal under-pricing. By definition, in a sustainability-conscious era, a non-renewable resource like oil is underpriced if it is cheaper than the renewable alternatives such as solar or wind power.

Although the transport between countries of similar goods produced by similarly competent suppliers may be economically `efficient' if it brings cheap goods to the importer, it is wastefully `inefficient' in use of resources in any material sense. For goods other than those unique to the trading partners, this amounts to spending fuel to promote brand competition between alternative suppliers. The apparent efficiency is a fiction of accounting (Palley 2003). A similar principle applies to human capital: free markets disregard the cost to the state of educating future employees or the welfare expenditure on rehabilitating poisoned or injured workers, or the waste if able workers are made redundant.

The National Farmers Federation, an early and relentlessly vocal advocate for free trade, has helped to place Australia's farmers in their current predicament. Under free trade, domestic prices are capped by international prices, so to survive farmers must reduce costs. Reducing costs means reducing investment in maintaining and regenerating their productive asset – their land resource – the condition of which doesn't appear in the market. Governments are then obliged to pay drought aid, land care, FarmBis, welfare and other schemes to ensure their survival. Hardly an 'efficient' method of remunerating the nation's food producers. As Parliamentary Secretary Sharman Stone (2003) observed in referring to corporate competition:

> “A community that pays less than the total cost of production, in particular, for food and beverages, will ultimately pay the price through degraded natural resources and human capital. ...sustainability is under threat when retailers use their market power to force prices to suppliers close to or below their full cost of production.”

Supply & demand

Supply and demand are balanced more or less effectively by the market. The consequences sometimes may seem unfair, such as when a hail storm destroys a battling farmer's uninsured ripening crop, but so long as Providence or lack of business skill can be blamed, producers tend not to blame the trading system.

Domestic purchasing power

Producers contribute through various taxes and charges to Australia's high level of civic amenities — such as libraries, universal education, research such as by CSIRO, public transport, the Australian Broadcasting Commission and the social welfare net. Trade-fuelled pressure to reduce costs tends to squeeze `overheads' such as taxes and fees out of the cost of doing business. The end result can only be a decline in the quality of civic life — and, ultimately, in exporting, which also benefits from these forms of infrastructure because they are public goods under-provided by the market. Quiggin (1997) referred to the “naive mercantilism common in the business sector, where community services are seen, not as a pillar of our economic well-being, but as a cost burden detracting from `competitiveness' on export markets.”

Under free trade in financial services, this problem compounds itself as businesses trading internationally become unaccountable to the community from which they have severed themselves (Terry 1995:165) but which have nourished them by civic services, education and public infrastructure. Our Government even abets this by joining the international race to the bottom through downgrading corporate taxation scales, free-trade agreements and deregulation under GATS.

Inter-country endowment

Climatic factors, disease conditions and suitability of natural resources such as rainfall, soil fertility and topography vary widely between countries. While it is not unfair to allow competitive markets to pit farmers within the same bio-geographic area against each other, it is unfair to expect farmers to remain competitive with remote farmers enjoying more benign conditions. *Prima facie*, it cannot be in the national interest to allow the global market to preside over the fortunes of a country's food producers in this way.

Exchange rates

The fourth factor brings an international lottery into trade practice. Official exchange rates have been floated for about half the national currencies. The touted reason for floating — by which the exchange rate is set by balances in foreign currency transactions — is to allow currencies to reflect genuine financial fundamentals rather than the potentially misguided policies of governments. But the *financial* markets are connected only indirectly and weakly with the national *production* markets which determine national prices. Ninety-six percent of world transfers of funds are not supporting transfers of tangible goods and services. Over and above fundamentals, financial trades are a complex resultant of uncertainties such as geopolitical deal-making, wars, corruption, hedging by futures traders, `herd instinct', Greenspan's "irrational exuberance", computerised selling and `momentum trading'.

That foreign goods are cheaper or dearer than domestic equivalents is partly an artefact of the currencies' relative exchange rates. This is unfair to producers, who can meet best practice employment, technological and marketing standards but can still be beaten by shifts in exchange rates over which they have no influence. Mining house Pasminco collapsed in September 2001 because its hedges against the Australian dollar turned sour. Trade advantage can seesaw. Since 2000, the Australian dollar has swung from about 50c to about 96c to about 60c to the US dollar. These swings can disrupt planning by firms. Efficiency is harmed by placing investment in infrastructure and factories with lead times of years at the mercy of capricious financial flows with lead times of minutes.

Also, and more subtly, when two countries trade, the higher-wage partner is able to buy goods at prices less than their true (domestic) cost. Intuitively, this is unsustainable. It is also unfair, because the lower-wage partner does not share the windfall. International trade obliges poor countries to purchase their sophisticated imports such as machine tools, computers, armaments and northern expatriates at prices profitable to industrialised producers, but they can sell their commodities only in competition with other poor countries, driving prices down and allowing rich countries to pick bargains. The disparity is growing: prices for primary commodities have fallen relative to prices for manufactures for decades (Rees 2002). The result is that domestic production closes down. This is not the pathway to prosperity.

Trade forces poor, non-industrialised countries to sell their birthright of natural resources cheaply, as international trade in commodities is competitive (and they lack market power). Trade causes countries to dedicate their raw materials, labour, infrastructure, industrial capacity and in part their educational system to producing goods and services for the benefit of countries other than their own. Australia imports doctors and Nile Perch from doctor- and protein-starved Africa. Could we do anything more cruel?

The food trade between continents is promoted heavily in negotiations within WTO, because the export of food from developing countries can earn them foreign exchange, which they need to repay debts to the (mainly) First World and to purchase sophisticated inputs to maintain basic health, education and other public services.

International free trade obliges employees in the subject industries to compete with the poor of the world for jobs and wages (Daly 1993:128). Every farmer and production worker is thrown into competition with workers in every signatory nation (Morris 1993:159).

Tariffs and protection

One traditional purpose of tariffs has been to even out the differences in the value of money across borders, so that producers can compete equitably on the basis of cost of production. Accordingly, it cannot be true that tariffs and similar instruments distort trade by protecting `inefficient' producers from competition. No matter how hard the WTO and governments try to eliminate tariffs, quotas and subsidies, the domestic cost-price structure and exchange rates will always be variables. This establishes a *prima facie* case for tariffs to smooth out what would otherwise be a distorted playing field, shielding a nation's producers from volatility in exchange rates and predation.

If an industry is subsidised in its home country (directly by production subsidies or indirectly by income support, export incentives, research grants or tax deductions) it can engage in predatory pricing overseas. So its imports can penetrate the target country and compromise the local competitor industry. Any country (such as Australia) which abolishes tariffs unilaterally without obtaining reciprocal guarantees is simply a sucker.

Consumers are also Producers

A paradox is the emphasis by advocates of trade on reduced cost to consumers and the corresponding lack of concern about the effects on producers. Consumers are said to benefit from the low prices that international competition brings. The corollary of low prices paid by consumers is low prices paid to producers. That low prices can be of economic benefit to both is, as a generality, a logical impossibility. Even though trade advocates argue that low prices have the beneficial effect of forcing *producers* to become more efficient (that is to waste less labour and other inputs), it could equally be claimed that low prices encourage *consumers* to be less efficient (that is, to waste more products).

Trade can alter distribution within a country and it cannot be assumed that the changes average out. A survey of 84,000 households (WB 2005) found a “sharp 6-per-cent drop” in living standards of rural households because of agricultural imports and increasing cost of consumer durables since Beijing's accession to the WTO in 2001.

The notion that Australia can improve its economy by sourcing services offshore (EAU 2001) is anti-intuitive. Certainly, costs might be reduced, but `costs saved' actually means `investment forgone' — on Australian jobs and development of local capacity. In any case, it is only an assertion that the best interests even of consumers lie in reducing costs. Low prices inhibit craftsmanship and encourage planned obsolescence. Under severe competition firms cut corners with product standards or after-sales service. Low margins work against research and development which in any case is generally under-provided by the market. The expectation of future profit is the basis for future investment and a major source of material progress in a capitalist economy.

For example, low oil prices in the 1980s discouraged energy conservation, new generation technology and, of course, exploration for new reserves. It led to a decline in the `human capital' in the form of a network of skilled petroleum geologists able to assist with a transition to a new era (Fleay 2001).

Low prices for traded goods also skew the relative cost of non-traded services and hence undermine the provision of public goods such as education, health and community welfare, which by their nature are labour-intensive and anchored locally. Right wing pundits observe this and mistakenly rail against the apparent expansion of government.

Within a net food-exporting country, the consequences of trade for consumers can be disastrous. Prices that producers can earn by selling overseas are no doubt higher than they can win at home (or they wouldn't trade). This pulls domestic prices upwards, and can make food unaffordable for the poor. These negative effects are worsened when exports face subsidised competition in the trade partner country, but they arise even in an honest market.

The question of whose interest is served by trans-national trade in food becomes more clear when one disregards the financial economy, which is an artificial construct, and looks instead at the balance sheet in goods. Food moves in one of two ways, both regressive:

- away from producer countries where it is not available for its people to eat; and/or
- into other producer countries where it displaces local production.

DFAT uses the undeniable growth in East Asian economies in the 1980s and 1990s as evidence that `globalisation' brings wealth (EAU 2003). The fact that developing countries can benefit from export to rich countries is clear enough; but the prospect that markets in their countries might be destabilised by reciprocal opening of their markets to foreign goods or services is a necessary corollary.

Not Everyone can Profit Simultaneously

It cannot be possible for every country to run an enduring trade surplus, as world totals must sum to zero (Stiglitz 2003). The trade-fuelled growth of the Asian tigers in the past 20 years has been at the expense of the countries (including Australia, one of the losers) which have run up trade deficits. Trade advantage is about edging out some other country or domestic competitors. If that were not true, international competitiveness would not be an issue in trade circles.

The UN (1997:24) reported that “All countries have a shared interest in an open, rule-based equitable, non-discriminatory transparent and predictable multilateral trading system.” One can agree with this principle, without supporting *free* trade as an ideology.

The fact that a country can increase its economic prosperity through trade doesn't prove the free trade argument: it simply demonstrates that if you sell more goods than you buy, you end up with money in your pocket. Australia jump-started its economy in that way, notably in the gold rush era of the mid-1800s and then the golden era of wool in the 20th century. It simply happens that China is now the country able to thrive by importing capital and exporting goods; but this phase, too, will pass. What eludes the world is a sustainable model of trade (Stiglitz 2003).

By definition a free-trade agreement establishes an anti-free trade cartel which preferentially excludes third parties (Garnaut 2003). DFAT cannot reasonably claim that there are benefits in global integration while also claiming that an agreement designed to discriminate against the rest of the world in favour of one country (Costello 2004) will also bring comparable benefits. If there is a sound theoretical basis for multilateral trade liberalisation, it cannot also justify bilateral trade agreements (unless they are a Trojan horse for deeper liberalisation). Comparative advantage will not serve for both and no other theory seems to be commonly invoked.

World trade in merchandise increased 20-fold between 1950 and 2000 but production increased only six-fold (Dicken 2003:35). This suggests that either similar goods are being swapped or countries are allowing their own production capacity to be superseded by imports, or both. For example, some goods may cross the oceans twice (e.g. once as grain then again as lot-fed meat); or similar produce may be exchanged (e.g. fruits in alternating seasons). These activities will not necessarily help domestic producers overall, though they may be profitable for individual firms or industries.

Certainly, trade and foreign investment can bring systemic benefits such as by permanently increasing a country's stock of knowledge. However, trade does not *automatically* do this. Trade in staples which both countries can produce, and foreign investment which simply gobbles up local viable businesses, are generally wasteful of the human resources of the importing country (UN 2000, Singh 2003).

Foreign direct investment has to increase economic activity sufficiently to service the increased external obligations it creates, perhaps indefinitely (UNCTAD 2003). There is no morally legitimate reason why Australia should live off the assets or lending power of the rest of the world, nor is this sustainable, as in a roundabout way it amounts to selling the nation's family silver (capital resources) to pay for current consumption.

Destroying Sunrise and Other Industries

The DFAT book *India: New Economy, Old Economy* (EAU 2001) offers a glimpse of the world after GATS. The book outlined commercial opportunities that Australian businesses could exploit, such as outsourcing IT software development and data processing to India, which has a high penetration of English but lower labour costs. The report cited approvingly ANZ's outsourcing of 20 per cent of its technology staff to India. Telstra, until recently majority-owned by the Australian people, has shifted some call centre functions to India (Giles et al 2003). This sounds like a recipe for condemning Australia to remain as an exporter of raw commodities.

If new-technology jobs such as IT programming are moving to India, there seems no reason why any services other than geographically anchored ones like tourism will be shielded from decamping overseas. Under GATS there is no reason why even core governmental policy analysis won't shift offshore to think-tanks based in the Third World or the USA. Economic analysis can be done in New York or Chicago, since the same neo-liberal consensus prevails in both countries; and since the US has insisted under A-USFTA that domestic favouritism clauses be removed from government procurement policy. So long as a country has a class of educated English speakers, there is no neo-liberal reason why they could not be contracted to do almost any task for which the inputs and outputs can be mailed or e-mailed. Perhaps DFAT should outsource its trade policy analysis to a country that is successful in trade, such as China.

Don Manzullo, US Congressman, in lamenting the shifting of professional positions offshore from the US (a foretaste of GATS) commented: “Increased global trade was supposed to lead to better jobs and higher standards of living... The assumption was that while lower-skilled jobs would be done elsewhere, it would allow Americans to focus on higher-skilled, higher-paying opportunities. But what do you tell the Ph.D., or professional engineer, or architect, or accountant, or computer scientist to do next? Where do you tell them to go?” (Greenhouse 2003).

In addition to snuffing out sunrise industries, international trade destroys mature capital, on a large-scale, often written off (via depreciation allowances) at the expense of the taxpayer. Communities reliant on individual factories are destabilised (Greider 1993).

CONCLUSIONS

For a policy to be well grounded, it must reflect a robust theoretical foundation and be consistent with the empirical evidence. These ingredients seem to be missing from recent analyses by the Government/DFAT, which seem to have been based upon slogans, not logic (Cook 2004). Trade policy has become a substitute for development policy (Parris 2001).

International free trade conflicts with many policies conducive to the public interest. The transport of capital and goods for the purpose of increasing consumption is deemed to take precedence over the sovereignty, well-being, environmental sustainability and culture of local communities (Morris 1993:139).

Those who advocate free trade as a generic policy are, in mathematical language, attempting to solve a multi-factorial equation with a single variable. Factors such as exchange rates, hidden variations in wage-price structure, environmental deterioration, availability of natural resources and political jostling are variables, not absolutes to be assumed away. Under trade, as in competitive markets generally, the strong become stronger and the weak fall further behind. This feature has both theoretical and empirical explanations.

The analysis reveals who benefits and who loses from free trade. The inclusion of currency exchange rates within the calculus of competitive 'efficiency', means that efficiency makes sense only for organisations — notably trading corporations — which can shift their activities around the world, without concern for the effect on farmers, factory workers, domestic consumers and their national governments.

Australia's industries are now feeding on their own flesh. In the 1980s and 1990s tariffs were reduced to force so-called fat and lazy industries to reduce costs. Now manufacturers and farmers are being told that their costs must be reduced in order to match international prices, that is, to maintain low tariffs. This beggar-the-producer policy is now being extended through free trade agreements and GATS to the professions, service industries, investors and administrative classes. International free trade bargains away a country's capacity to feed and tax itself and to develop its own intellectual capital.

Contemporary trade policy in Australia has the hallmarks of a cargo cult, whereby the electorate is regaled with promises of abundance and profit that don't require hard work. The national interest is depicted as lying in free trade in itself, careless of the fate of displaced employees or wasted productive plant, dismissive of foreign debt, and blind to the consumption of natural resources, notably the transport fuel that lubricates the process.

Minister, the fact that most of your advisers are enamoured of free trade and will press you to press that agenda harder does not mean that it is a prudent policy for Australia. Simply repeating a false belief over and over does not make it true. I urge you to ask your Department to trace the logical consequences of free trade for debt, fuel consumption, consumers in developing countries and producers at home. I also urge you to seek briefings from external sources who are sceptical about a free-trade regime that should be consigned by the recent failure of global corporate self-regulation to that filing cabinet reserved for bright ideas that simply didn't work.

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His doctoral thesis (Department of Politics and Public Policy, Griffith University, Brisbane, 2008) examined the concept of 'public interest'.

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ABBREVIATIONS

A-USFTA: Australia-US Free Trade Agreement
DFAT: Department of Foreign Affairs and Trade
GATS: General Agreement on Trade in Services
IMF: International Monetary Fund
UNCTAD: United Nations Commission on Trade and Development
WB: World Bank
WTO: World Trade Organisation.

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