

GLOBALISATION: Keeping the Gains

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Australia has been called the lucky country. But countries like people really make their own luck. It's not luck Australians' economic fortunes rose as we embraced globalisation and reformed our economy.

Despite our success, globalisation has become a controversial issue.

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Firstly what do we mean by globalisation? These are two definitions, but really globalisation is just an extension of the personal freedoms and free markets we enjoy in our own economy to the whole world, with a resulting expansion of the benefits.

Today I want to briefly highlight the main findings of our new report *Globalisation: Keeping the Gains* by trying to answer three major questions often asked about globalisation.

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- Are Australians gaining from globalisation?

- Are the rest of the world, including developing countries gaining?
- and what can we do to keep and spread these gains, both in Australia and in poorer countries.

Our first major finding is that Australia and other countries, including developing countries, that have opened up to international trade and investment have benefited considerably from globalisation.

Our second major finding is that free trade and investment are necessary but not sufficient for communities to benefit. To keep and extend the gains from globalisation, countries also need effective economic policies and institutions.

Let's look first at how Australia has fared

Our report gives a wealth of evidence that Australians' living standards have improved rapidly since we re-opened our economy and undertook other economic reforms in the 1980s and 90s.

In fact, historically Australia was a highly globalised economy, with a much higher ratio of exports to GDP than the world average.

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But Australian governments turned away from globalisation during the depression, raising trade barriers. We also adopted inefficient labour and capital market policies and high levels of state ownership. Australia's experiment with de-globalising was not a big success. From having the highest per capita income in the world in 1913, Australia dropped to 15th place in 1990. Our human development index ranking dropped accordingly.

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However, over the last two decades, Australian governments turned away from protectionism and reduced trade barriers dramatically. Effective rates of protection fell from an average of 25 per cent to 5 per cent. Only textiles, clothing and footwear and cars still attract higher tariffs.

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Governments also undertook a whole range of other reforms I'll discuss later. Australia now is one of the most open and efficient economies in the world.

In the 1990s, due to freer trade and other economic reforms, Australian's average real income per person rose rapidly, by over 55 per cent, from about A\$23,000 in 1980 to A\$36,000 in 2002.

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And as we saw before, as a result of embracing open trade and investment, and a raft of other important economic reforms, our ranking in world GDP per capita are rising, back to eighth and our human development indexes rankings reached 4th in the world in 2002.

So Australia has definitely gained from globalisation.

But what about developing countries?

Many people think that while developed countries like Australia may be gaining, globalisation is making poor countries poorer.

However, the evidence is very convincing that developing countries that globalise grow and reduce poverty faster than those that do not.

For example, recent study of 72 developing countries shows in the 1990s, globalising developing economies' real incomes and output grew faster, on average about 4 times faster, than inward looking economies' output.

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Developing globalisers also are growing about twice as fast as developed countries, closing the income gap with them.

Looking at our own region, many of our East Asian neighbours are some of the biggest gainers from globalisation.

From the 1960s on, most East Asian economies became increasingly export oriented and globalised, lowering their tariffs and expanding their exports and imports.

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They also provided their populations with education and infrastructure and generally sound governance. As a result, capita income grew strongly in most East Asian economies' over the last 20 years.

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Most of the ASEANs also grew despite setbacks during the Asian crisis.

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And as incomes grew, the proportion of East Asian populations living in poverty fell dramatically.

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Over the last 20 years, while the world's population increased by 2 billion, the numbers living in poverty fell by 200 million due entirely to falling poverty in globalising countries, particularly in China and the rest of East Asia. However, the numbers living in poverty in inward looking and poorly governed Africa increased.

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So both Australians and people in globalising developing countries are gaining from more open trade and investment.

But what can we as Australians do to keep and spread these gains for ourselves and people in developing countries?

This question leads naturally to the second major finding of our report, that while globalisation is necessary, it is not sufficient to guarantee communities gain from globalisation. To keep and spread the gains, governments must not only reduce barriers to international trade and investment, they also must get domestic policies right.

Looking at Australia's experience, why have we gained so much from globalisation when some other economies like Argentina have not?

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- As we saw before, throughout the 1980s and 1990s, Australian governments reduced trade barriers dramatically.
- While some believe cutting tariffs hurt Australian industry, the evidence does not support this.
- A recent study of Australian industry through the 1980s and 1990s shows on average cutting an industry's tariffs by 1

per cent permanently increased these industries' output by 0.15 per cent.

- This is because increased international competition and other economic reforms transformed Australian industry, encouraging firms to adopt new technologies and seek out new export markets, increasing their output and productivity.
- Australia governments also freed up interest rates, the exchange rate and prices for electricity and other utilities, reformed taxes and decentralised wage setting.
- All these reforms make our markets work more efficiently, so now we mainly devote our labour, capital and land to producing those goods and services we can sell for the highest returns on world markets, and import goods and services we can't produce competitively, including from developing countries.
- This makes us richer as a community and richer as individuals. It also helps our developing neighbours grow out of poverty.
- As well, our economic institutions generally work well.
- The Treasury and RBA provide a stable macroeconomic policy environment.

- The ACCC makes sure our firms act competitively, and our prudential controllers ensure our financial institutions are generally sound.
- This allowed us to weather the Asian financial crisis unscathed. Despite HHH, our corporate governance is generally strong.
- Our legal system protects property rights and creditors, as well as personal freedoms.
- Our education system seeks to give all children access to a quality education. This means Australian workers and school leavers can take up high skilled, better paid jobs in growing industries and leave lower skilled, lower paid jobs in declining industries.
- Firms also can find the skilled workers they need to adopt new technologies and keep ahead of international competition.
- Australian governments generally ensure we can access reasonably priced and efficient infrastructure services so producers can remain competitive.
- Finally, Australian governments have spread the gains from globalisation by ensuring all can access quality education, social services and a social safety net.

- Despite the rapid increase in Australian's incomes over the last two decades, inequality has remained roughly the same.

All these reforms have helped Australians gain much more from globalisation than countries like Argentina, which have at least as many resources but weaker institutions and policies.

What about developing countries? What can we do to help them gain more from globalisation?

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Certainly the main thing developed countries can do to help developing countries gain from globalisation is to reduce their trade barriers to developing economy exports like labour intensive manufactures and agricultural products.

For example, the US Agriculture Department estimates high agricultural trade barriers and subsidies of around US\$1 billion a day cut prices for all agricultural output worldwide by a massive 12 per cent each year.

Hence, these agricultural support policies could cut low and middle income East Asian and Pacific economies agricultural output value by over US\$37 billion each year or about 5 times the US\$7.7 billion these economies receive in aid annually.

These trade barriers not only hurt developing country exporters but also efficient developed country agricultural producers like Australia.

The World Bank estimates developing countries would gain about US \$100 billion a year if developed and developing countries removed all their trade barriers against developing country exports.

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This far exceeds the US\$57 billion developing countries get each year in aid.

So to keep and spread these gains, further trade reform is important, both for developing countries and Australia.

Australia already has removed most trade barriers, except in the autos and TCF sector and removed all tariffs for least developed country imports in July this year.

Australia also is working hard in the WTO's Doha Round of trade negotiations to reduce global trade barriers, particularly to agricultural exports. Doha is called the development round because it is seeking to reduce barriers to developing economy trade and getting them access to cheaper medicines for major diseases like AIDS.

But to gain from globalisation, opening to international trade and investment is necessary but not sufficient. Developing countries also need to ensure labour, financial and product markets are working and their populations have access to adequate education and infrastructure services.

Recent studies show strengthening economic governance and institutions is an important method of boosting growth.

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Hence, another important way we can help developing countries benefit from globalisation is through our development assistance, helping developing countries strengthen key economic and legal institutions, improves market efficiency, upgrades infrastructure, education and health delivery and encourages participation in global markets. Australia's development assistance increasingly prioritises economic and legal governance activities.

So summing up – Slide 16

The evidence strongly shows Australia and open developing countries are benefiting significantly from globalisation.

However, for Australia and developing countries to keep the gains from globalisation all countries must continue to lower trade barriers and implement sound domestic policies. Australia has succeeded because of its economic reforms and strong

institutions and also is helping its developing neighbours to benefit through trade reform and aid.