SUMMARY

1. Since the global financial crisis and its previous Trade Policy Review in 2011, Australia, one of the most open economies in the world, has performed well relative to many other advanced economies due, *inter alia*, to its broadly appropriate macroeconomic policy mix. Following a period of expansion resulting from the boom in mining investment driven by improved terms of trade, which reached a historic peak in 2011, growth slowed down to below its trend rate of 3%. As resource investment peaked and the terms of trade declined, the economy entered a transition period towards mining production and exports as well as to broader-based drivers of activity in non-resources sectors. Australia's declining position among the most competitive economies in the world reflects only minor improvements in average multi-factor productivity (MFP). Inflation has been within or slightly above (2010/11) the central bank's 2% to 3% target. The unemployment rate has remained relatively low, albeit rising gradually from 5% in 2010/11 to 5.9% in 2013/14.

2. Structural policy reform, aimed at improving Australia's MFP and thus its international competitiveness, has been ongoing in certain areas. To facilitate the transition towards non-resource sector growth by supporting domestic demand, the central bank has cut its policy interest rate by 225 basis points to 2.5% since November 2011. During the review period, the fiscal deficit narrowed considerably to 1.5% of GDP, but then rose again in 2013/14 to 2.4%. Australia's budget strategy now includes a Temporary Budget Repair Levy and requires that new spending measures be more than offset by reductions in spending elsewhere.

3. The responsiveness of the freely-floating exchange rate to economic developments contributed to the maintenance of macroeconomic stability and containment of external vulnerabilities; it has helped the economy to absorb a sharp increase in terms of trade without leading to overheating and a spike in inflation. Despite some depreciation over 2013 and a subsequent decline in the terms of trade, the Australian dollar still remained relatively overvalued, to the detriment of Australia's export competitiveness. Reflecting the narrowing structural saving-investment gap, Australia's current account deficit dropped considerably in 2010/11 and thereafter rose gradually before dropping again in 2013/14. The merchandise trade account turned to surplus in 2010/11 and 2011/12 driven by the peak in the commodity price cycle; subsequently, it returned to a deficit as commodity prices moderated, and in 2013/14 it moved back towards surplus on the back of increased commodities production. Australia's international (foreign exchange) reserves have risen. Net external debt increased, largely held by the private sector, especially non-financial corporations.

4. Despite the openness of the Australian economy, international trade in goods and services continue to account for only around 40% of GDP. The share of commodities – the main traded goods – in total merchandise exports rose further. Developments in international trade and foreign direct investment (FDI) patterns during the review period continue to reflect the rising importance of China as Australia's main export market (especially for mining products), and the EU, the United States, and Japan as its major sources of FDI. Mining investment has risen while non-mining investment has been weighed down by, *inter alia*, excess capacity and an overvalued exchange rate. While maintaining an open stance towards foreign investment, Australia continues to screen large investment projects to ensure they are in the national interest. FDI proposals subject to screening are rarely rejected, but often have conditions attached. Foreign equity caps remain in the areas of airports, civil aviation, maritime transport and telecommunications. Restrictions on foreign direct investment in residential real estate and agricultural land are also in place.

5. While there have been few changes to the institutional framework for formulating and implementing trade policy, a change in Government in 2013 has resulted in policy shifts in many trade-related areas. Additionally, a key focus of the new Commonwealth Government over the review period has been to drive forward reforms to cut costs, provide more efficient and effective government services and create a less burdensome regulatory environment for businesses and citizens. It has also launched discussions on reform of the Australian Federation with a view to ensuring its efficient and effective functioning.

6. Australia's trade policy continues to be based on the premise that trade openness, economic growth and improved living standards are strongly linked; emphasis is placed on improving international competitiveness and market access overseas. Australia pursues a combined multilateral, regional, bilateral and unilateral approach to trade policy, and is exemplary in the transparency of its trade regime. It remains an active Member of the WTO and contributes a

significant amount of its official development assistance to aid for trade funding. It has maintained a strong record of notifications, with few outstanding. Since 2011, Australia has been involved in several WTO dispute settlement cases in different ways, including as a respondent in five cases relating to plain packaging requirements applied to tobacco products. Simultaneously, Australia has been actively pursuing new RTAs. Over the review period, RTAs with Malaysia and the Republic of Korea have entered into force, an RTA with Japan has been signed, and one with China has been concluded. Australia is negotiating three additional bilateral RTAs as well as four plurilateral ones.

7. The tariff remains one of Australia's main trade policy instruments, albeit a minor source of tax revenue. As a result of the introduction of the HS2012 tariff nomenclature, the average applied MFN tariff rate dropped slightly, from 3.1% in 2010 to 3% in 2014. Unilateral reductions on apparel and certain finished textile articles were implemented at the beginning of 2015. Some 96% of applied MFN tariff rates continue to be in the range zero to 5%. In line with long-standing, though decreasing, sectoral support to textiles, clothing and footwear (TCF) and passenger motor vehicles (PMV), the applied MFN tariff rates on the latter products (PMV) remain considerably higher than the average. The tariff structure has remained unchanged. Most tariff rates (99.7%) are *ad valorem*, which contributes to the transparency of the tariff. By contrast, the few non-*ad valorem* rates tend to conceal relatively high tariff rates, particularly those on used vehicles, although these seem to be rarely applied. The pattern of tariff escalation remains unchanged, which means that effective rates of MFN tariff protection can be considerably higher than nominal rates. Some 97% of tariff lines are bound, thereby imparting a high degree of predictability to the tariff. However, applied MFN tariff rates continue to fall short of bound rates by an average of about 7 percentage points and up to 55 percentage points for clothing items. While the consequent gap between bound and applied MFN rates provides considerable scope for the authorities to increase applied tariffs within bindings, this has not occurred.

8. During the review period, documentation requirements have remained minimal, and computerized customs clearance has facilitated virtually all imports and exports. Trade facilitation efforts included the simplification of Australia's duty concessions scheme, the enhancement of international cooperation, efforts to ratify the WTO Trade Facilitation Agreement and commitment to fund assistance to partner countries in this area. Customs valuation legislation was amended to ensure consistency with the WTO Agreement on Customs Valuation, and transfer pricing policy practices have been clarified.

9. Import prohibitions and restrictions, in the form of generally strict quarantine or technical requirements, have remained in place to preserve, *inter alia*, human, animal or plant life or health, the environment, safety, or security. During the review period, reforms were undertaken to develop a modern and responsive system that facilitates trade while managing biosecurity risks. Whereas technical standards and many other regulations are, by and large, subject to cost-benefit analysis, this is still not the case with SPS measures. The share of national standards that are identical or "modified adoptions" of international standards remains at 38% (or 97% of applied standards). During the review period, significant changes have been made to the legislative, institutional and procedural framework for anti-dumping and countervailing measures. Recourse to anti-dumping and countervailing action has been increasing in Australia, the WTO's fourth largest user of the former in 2013, with most initiations and measures relating to items originating in Asia. Two safeguard investigations were initiated, but no new safeguard measures were adopted.

10. Export controls or quantitative restrictions implemented by public sector entities affect certain primary and therapeutic goods to ensure, inter alia, adequate domestic supply, and to enforce standards; however, a permit requirement for wheat exports was repealed. The Rice Marketing Board for the State of New South Wales, an export monopoly, was the only state-trading entity operating during the review period. Export assistance, consisting of direct grants (e.g. through export market development grants) and tax concessions (e.g. Tradex), has been maintained and in certain areas is focussed on Asian markets. In addition to local content requirements, export finance is, *inter alia*, conditional upon "national interest" criteria. Export credit terms seem to be in line with OECD guidelines.

11. Support for domestic production and trade has been provided through tax and non-tax incentives, with increased emphasis on R&D spending as well as regulatory restrictions on competition in certain activities. Some industry-specific programmes (e.g. steel, TCF) were terminated or amended during the review period. The special Luxury Car Tax, which affects both

domestic and foreign cars, but seems to fall disproportionately on imports, has been retained. The effective rate of combined assistance (i.e. tariff, budgetary, agricultural pricing and/or regulatory assistance) continues to be relatively high for motor vehicles and parts, TCF, and forestry and logging. The State remains involved in the economy through government trading enterprises (GTEs) which provide services in key infrastructure sectors (e.g. water, electricity, ports, rail, urban transport), though not always on a fully commercial basis. Efforts to streamline state participation in areas where Commonwealth Government involvement is necessary included "bonus" payments to state governments that sell public assets and use the proceeds for infrastructure projects.

12. Australia has continued to use government procurement as an instrument of economic policy aimed at fostering industrial development in certain sensitive areas (e.g. real estate property or accommodation, inputs to R&D services, and motor vehicles) that are exempt from mandatory rules applying to procurement above certain thresholds. Procurement rules were amended, *inter alia*, to redefine procurement methods and adjust to new legislation's terminology. The target of sourcing at least 10% of purchase value from small and medium-sized enterprises (SMEs), as well as preference margins for local suppliers and local-content requirements by certain state governments have been maintained and, in certain areas, revised. However they are applied in line with RTA commitments. Foreign participation in the bidding or the granting of duty concessions may require the submission of an Australian Industry Participation Plan, an element also used for the granting of duty concessions under the Enhanced Project By-Law Scheme. Whereas Australia remains an observer to the WTO Committee on Government Procurement (GPA), it intends to initiate work to possibly accede to the GPA. Comprehensive chapters on government procurement in a number of its RTAs reflect its commitment to respect principles of transparency and non-discrimination in the conduct of its government procurement.

13. Australia has further strengthened protection of intellectual property rights by passing new legislation, considered as its biggest IP system overhaul in twenty years, by amending existing legislation in several areas and expanding its international commitments. The competition policy framework, which remains characterized by a long list of special regimes and exemptions, including at state or territory level, will be comprehensively reviewed with a revised compliance and enforcement policy being released in 2013. A recent legislative amendment is aimed at strengthening protection in the area of consumer credit protection and enforcement at the national level.

14. Despite its relatively small contribution to GDP (2.4%), Australia's market- and export-oriented agriculture remains of fundamental importance to the economy; its MFP has risen and a strategy to raise the sector's competitiveness is under consideration. During the review period, sectoral policy developments have focused largely on ensuring a sustainable, productive and resilient agricultural base, supported by measures on drought relief, water and land management, farm finance and rural research. The average level of applied MFN tariff protection for the sector (excluding forestry) remained negligible, at 1.4%, compared with 3.3% for manufacturing. However, some sensitive items (e.g. cheese, certain vegetables, certain oils and fats) continue to receive considerably higher tariff protection with tariff-rate quotas affecting certain types of cheese and curd. A generally strict quarantine and inspection regime remains in place, while biosecurity reform has proceeded. Exports and/or production of certain commodities (e.g. certain dairy products, grain, horticulture, livestock, and wines/grapes) continue to be subject to levies earmarked mainly for R&D. Single-desk arrangements (i.e. monopolies) continue to affect rice exports. Changes were made in areas such as: exceptional circumstances arrangements; export certification requirements; wheat export arrangements; and, the livestock supply chain. Despite a wide range of assistance programmes, the sector's overall level of support, as measured by various indicators, has remained low, with budgetary assistance declining in value terms to about 0.1% of GDP. This assistance continues to be delivered in the form of non-trade distorting (Green Box) budgetary outlays and remains within Australia's *de minimis* WTO commitments. A range of initiatives and measures have continued to improve fisheries' management and thus the sustainability of fish stocks for the long-term viability of the sector.

15. Mining (8.6% of GDP), which continues to operate in a seemingly competitive market environment with no apparent industry-specific restrictions on foreign investment and overall little government support compared with other sectors, remains critical to Australia's economic performance. Its average MFP growth rate dropped further but mining output, set to increase strongly in the coming years, is expected to give a boost to productivity. The sector's Mineral

Resources Rent Tax on iron ore and coal was applied from 2012 to late 2014, while the Petroleum Resource Rent Tax has been extended to virtually all onshore (as from 2012) and offshore oil and gas projects.

16. During the review period Australia, *inter alia*, reviewed its future energy needs, passed a comprehensive package of clean energy proposals, including a carbon price mechanism (repealed in 2014), and set mandatory minimum efficiency performance and energy rating label requirements. A new coherent and integrated approach to energy policy is under consideration. Electricity generation, transmission, and distribution remain subject to geographical and regulatory segmentation. Generation capacity is largely government-owned or controlled and retail electricity rates' regulation is maintained in all states and territories other than Victoria, South Australia and New South Wales. Tariffs are set by independent energy regulators or governments. Budgetary assistance to the electricity, gas, water, and waste services industries was the highest among all sectors. The Fuel Tax Credits Scheme continued to reduce the cost of liquid, gaseous and blended fuels for certain business uses; domestic producers of ethanol, biodiesel and renewable diesel used in transport also continued to receive a government subsidy, although subsidies for ethanol and biodiesel are to be gradually repealed.

17. The manufacturing sector contributes 7.1% to GDP. Manufacturing policy has been largely focused on increasing the multi-factor productivity, sustainability and growth of industry as well as creating new high-skilled jobs. Average annual MFP slowdown was reduced. The average applied MFN tariff rate on industrial products remained virtually unchanged. Budgetary assistance from a wide range of policy instruments is estimated to have remained at 0.1% of GDP, albeit decreasing in value terms. The textiles, clothing, footwear and leather industries, as well as motor vehicles and parts activities, have continued to attract high, albeit declining, effective rates of assistance, the highest amongst all manufacturing activities. The automotive industry continues to be assisted by mechanisms such as preferential government procurement policies, tax policy and restrictions on the importation of second-hand vehicles. Assistance continued to be delivered mainly in the form of industry-specific support and was supplemented by a Growth Fund to help adjustment to the end of car manufacturing. Industry-specific support for the textiles, clothing, footwear, and leather industries was drastically cut and the elimination of two remaining programmes is under consideration.

18. Australia's services sector is the mainstay of its economy, accounting for 71% of GDP and 77% of employment. While the financial services sector has performed well over the review period, a recently-released Financial Sector Inquiry has made various recommendations to strengthen and develop the sector, including eliminating distortions to the efficient market allocation of financial resources as well as impediments to competition. Approval is still required for all investments (both domestic and foreign) of over 15% in financial institutions. Banking reforms undertaken since 2011 have included: implementation of new capital and liquidity requirements; strengthened supervision; and winding down of measures introduced to mitigate the impact of the global financial crisis. Recent developments in the insurance sector have included the sale of a major state-owned private health insurer and the closure of the Private Health Insurance Administration Council. The provision of life insurance by foreign companies through branch operations is prohibited, but exceptions to this rule are increasingly being granted through RTAs.

19. Australia has a very high level of information and communication technology (ICT) development and has recently seen a big increase in both fixed and wireless broadband subscriptions and mobile subscriptions. Foreign investment restrictions remain in place for Telstra, the main player in the telecommunications sector, but are not applied to any other provider. The roll-out of the national broadband network is continuing, albeit with a new focus on using a range of different broadband technologies, rather than a largely fibre-to-the-premises approach. Completion is anticipated in 2020. The network is fully state-owned and will operate on a non-discriminatory, wholesale-only basis. Various regulatory steps have been taken to facilitate transition to the new regime and a new framework for providing universal services has been introduced. Australia's television broadcasting industry remains supported by local content measures and film production continues to benefit from various forms of financial assistance by the Commonwealth Government.

20. In the area of transport, budgetary provision has been made for major infrastructural works. While most major government-owned ports and airports are operated by the private sector entities, government involvement in the transport sector remains quite pervasive, and various

foreign investment restrictions are in place. In the maritime transport subsector, reforms have been implemented to make the Australian shipping industry more internationally competitive, increase the size of the shipping fleet and promote employment. These have included tax reforms, the creation of an International Shipping Register, and the implementation of a licensing system to give domestically-flagged ships a first opportunity to cabotage services. However, the cabotage policy is being reviewed by the current Government in light of concerns about its resulting costs and inefficiencies. In air transport, a foreign equity limit on investment in Qantas airline has been removed, bringing FDI restrictions applied to this airline in line with those applied to all others. The review period has seen a big increase in international passenger arrivals by air, the negotiation of several new air services agreements with third countries, and plans to enhance infrastructure. The domestic civil aviation market, which accounts for significantly more passenger arrivals than from international destinations, is dominated by two companies. The tourism sector is fully open to investment, and benefits from little government support. Tourism-related services remain Australia's major services export.

21. Australia's economic growth is expected to pick up to an above-trend pace over 2015/16. Despite its solid economic fundamentals, downside risks to the economic outlook are posed by, *inter alia*, its vulnerability to terms-of-trade shocks due to the increased role of the mining sector, as well as the balance, timing and strength of the decline in mining investment and the pick-up in activity in the non-mining economy. A major economic challenge confronting Australia, with potential trade policy implications, is to formulate appropriate macroeconomic and structural policies to facilitate market-driven adjustment to the effects of its declining terms-of-trade, the appreciation of the Australian dollar and the rising proportion of older people, as well as to enhance economic diversification away from mining. Confronting these challenges will require much faster MFP growth to enable Australia to strengthen its international competitiveness and continue meeting its economic and welfare objectives.