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**DISCUSSION PAPER No. 55**

**Australia's Foreign Economic Policy:  
a 'State-Society Coalition' Approach  
and a Historical Overview**

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**Abstract**

This paper aims to explain the historical development of Australia's foreign economic policy by using an analytical framework called a 'state-society coalition' approach.

This approach focuses on virtual coalitions of state and society actors that share 'belief systems' and hold similar policy ideas, goals and preferences, as basic units (policy subsystems) of policy making. Major policy changes occur when a dominant coalition is replaced by another.

The paper argues that, in Australia, there have been three major state-society coalitions in the foreign economic policy issue area: 'protectionists', 'trade liberalisers' and 'optional bilateralists'. The rise and fall of these coalitions resulted in distinctive shifts of Australia's foreign economic policy in the 1980s towards unilateral and multilateral liberalisation and in the late 1990s towards bilateral trade and investment arrangements.

**Keywords**

Australia, foreign economic policy, state-society coalitions, belief systems, changes in dominant coalitions

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## Introduction

In recent years, East Asian states have been intensifying efforts to integrate their economies with each other mainly through bilateral and regional free trade agreements (FTAs). Their efforts, nonetheless, are not confined to the East Asian region. The move towards institutional integration with 'extra-regional' states such as Australia, Chile, India, Mexico, New Zealand and the United States has also gained momentum. Intra- and inter-regional economic cooperation schemes including FTAs are now forming a complicated multilayered structure in East Asia. Focusing only on the 'regional' aspect of integration phenomena will not provide full understanding of what is really happening in East Asia.

This paper aims to explain the historical development of foreign economic policy of Australia, one of such extra-regional states that has been seeking closer economic relations with East Asia eagerly for more than twenty years. Understanding Australia's foreign economic policy and its changes will lay a foundation for better understanding of recent economic integration phenomena in and around the East Asian region.

The paper is divided into two sections. The first section sets out an analytical approach to exploring the formation of, and changes in, Australia's foreign economic policy. The approach contains three major elements. First, the international system is seen as the environment in which a small state like Australia, which alone does not possess the capability to make major impacts on the international system, must operate. Australia is a taker from/user of the international system basically and it is inevitable for a state like Australia that the international environmental factors restrict its foreign economic policy. In most cases, Australia has to react to, rather than try to exercise control over, changes in the international environment.<sup>1</sup>

Second, while the international environment does restrict the foreign policy behaviour of a small state, this does not necessarily mean that the environment forces a state to take one particular approach on particular policy issues. Rather, it can be seen that the international environment provides a certain range of foreign economic policy options that a small state like Australia can practically pursue. Within this range of policy options, a state like Australia

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<sup>1</sup> In fact, no state is totally free from what others do in this era of complex interdependence. The development of economic interdependence has created resources of new, non-military power. The new power of a state depends on its sensitivity and vulnerability. In terms of the cost of dependence, sensitivity means liability to costly effects from outside before policies are altered to try to change the situation. Vulnerability can be defined as an actor's liability to suffer costs imposed by external events after policies have altered (Keohane and Nye 1977: 13). The degree of influence of the international environment, therefore, is relative phenomenon.

attempts to realise its policy goals by choosing a policy (or a set of policies) that it perceives best.

Third, the state's choice of foreign economic policy is influenced by its relations with the domestic society represented mainly by a variety of societal interest groups. State-society relations need to be brought into consideration in the explanation of foreign economic policy formation. As a state tries to implement policies according to contemporary domestic necessities and those necessities in the future, to a certain degree it needs to be receptive to policy demands of the societal interest groups. Nevertheless, the state is not a mere agent of domestic interest groups. It can play a role in forming policy preferences on how best its policy goals can be achieved through certain ideas, knowledge and procedure. The concept of 'state-society coalitions', which share basic beliefs such as policy goals, preferences, ideas, knowledge, norms etc., in the domestic policy process provides a useful approach to state-society relations. The formation of domestic coalitions, changes in dominant coalitions, or internal alteration of a dominant coalition can cause changes in policy goals, ideas and preferences, which in turn will lead to shifts in the state's foreign economic policy.

The second section of the paper oversees the historical development of Australia's foreign economic policy. Since the early 1980s, Australia's foreign economic policy has experienced two distinctive shifts. The first shift in the 1980s was a consequence of the decision to reform the domestic economy. The reform aimed at transforming the traditionally inward-looking, inflexible and excessively commodity-dependent economy into an open, market-responsive economy, and most measures introduced for the reform were related to foreign economic policy. At the same time, the government actively involved itself in multilateral trade and investment liberalisation processes to underpin the domestic reform. The second shift, commencing in the latter half of the 1990s, has been to put more emphasis on bilateral relations than multilateral processes, based on an already significantly liberalised domestic economic regime. Australia has shifted its policy to prioritise concrete and short-term economic benefits it can calculate over somewhat abstract and longer-term nature of the benefits from multilateral liberalisation. The shift has been clearly manifested by the government's inclination towards concluding bilateral FTAs.

These shifts in Australia's foreign economic policy imply that there have been changes in dominant state-society coalitions in the issue area. The newly dominant coalition brought different core beliefs, thus different policy goals and preferences, from the previous one. The shifts also imply that there had been exogenous shocks to Australia's policy subsystems, which eventually led to the changes in domestic coalitional settings. In the foreign economic policy

context, these exogenous shocks are likely to be major changes in the international economic environment. For the dominant coalition to stay in power, it must significantly adjust its policies to accommodate the new environment. Attempts to do so are likely to fail since a coalition's core beliefs are hard to change. If a coalition were to stay dominant long enough to make state-society relations and policy making process institutionalised, the coalition would find it hard to change those institutions as well. Thus, for foreign economic policy to change, it is most likely that the replacement of a dominant coalition with a competing one would be required. In a state like Australia, which adopts parliamentary democracy as a system of government, a decisive replacement of a dominant coalition is likely to occur as a result of a change of government, though it is not a prerequisite.

## **Foreign Economic Policy of Small States: An Analytical Framework**

### **The International System as a Restricting Environment**

The 1970s saw the emergence of structural theories to explain the relations between the international system and individual state's behaviour. 'Structural realists' define the structure of international system in several ways. Bull defines an international system as: two or more states [which] have sufficient contacts between them, and have sufficient impact on one another's decision, to cause them to behave ... as part of a whole (Bull 1977: 9). On the other hand, Waltz defines an international system as: the arrangements of its parts [that] are set by its principal parts, and other states are assumed to act along with these arrangements made by powers (Waltz 1979: chap. 5). Then, they assume that the fundamental principle of the international system is 'self-help', rather than the maximisation of power as traditional realists suggested (Waltz 1979: 126). When 'rational' states decide how to act externally, they do so with consideration and anticipation of how other states react and what consequences it will bring. Relativity of states' capabilities, or distribution of capabilities, will significantly influence states decision making (Waltz 1979: 97). If distribution of capabilities changes, so does states' anticipation and expectation, therefore their foreign policy behaviour.<sup>2</sup> The points of the structural realists' argument is that, under the assumption of self-help, states' behaviour can be explained by distribution of capabilities alone, which is a system-level variable. In other words, unit-level variables such as states' attributes and interactions do (or should) not matter when explaining their foreign policy. Cooperative behaviour from states can only be expected when there is a hegemon that is capable of and willing to provide and maintain 'international public goods'

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<sup>2</sup> Structural realist theories, in fact, do not readily explain how the distribution of power changes.

such as security alliances and sets of rules for international economic transactions (Kindleberger 1973; Gilpin 1981, 1987; Hasenclever *et al.* 1997: chap. 4).

‘Liberal institutionalist’ theories draw on a different explanation of states’ activities though they share major propositions of realist theories: the structure of an international system as a primary determinant of states’ foreign policy, and states act rationally to pursue their individual interests (Keohane 1984: chap. 5). The difference originates from their emphasis on effects of the deepened interdependence among states.<sup>3</sup> The international system consists not only of military/political power but also economic power, which is the distribution of economic activities and wealth.<sup>4</sup> Since the end of World War II, flows of goods, services, capital, technology and information across borders have dramatically increased due to rapid and continuous technological developments in transportation and telecommunication. These flows have significantly deepened economic interdependence among states. Economic interdependence has altered the traditional ways of pursuing national interest in international relations, as it provides states opportunities to demand of others policy change or to invoke sanctions if they continue to be uncooperative. This is possible because, under deepened interdependence, the fate of a state, as well as its economy and society, is intertwined with that of other states (Duffy and Feld 1980). Destruction of economic interdependence would be too costly for any state to contemplate. Each state cannot decide and implement its foreign economic policy and achieve its economic goals without taking the impacts of other states’ policies toward itself into consideration (Morse 1976). The more this restriction on states’ behaviour grows, the less states can pursue their specific (and absolute) interests alone. States will not have much choice other than pursuing ‘common’ (and relative) interest as their foreign policy priority. This argument on rationality in states’ cooperative actions without hegemonic power providing international public goods was developed into liberal theories of international regimes (Krasner 1983; Keohane 1984; Hasenclever *et al.* 1997: chap. 3).

How relevant are these systemic approaches in explaining Australia’s foreign economic policy? The two assumptions that systemic approaches postulate still seem to hold: national governments of sovereign territorial states act as main actors in international relations, and they act to achieve their policy goals. Though the importance of the influence of multinational enterprises and transnational coalitions of environmental, ethnic, religious or other non-governmental organisations on states’ foreign policy decision making has significantly

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<sup>3</sup> Keohane and Nye (1977) defined Interdependence as ‘mutual dependence’ where there are reciprocal – though not necessarily symmetrical – costly effects of transactions.

<sup>4</sup> Cohen (1988:26) pointed out that, since the 1960s, the emergence of new influential states, such as Japan, Korea, Saudi Arabia and others, in international relations had the same characteristics of increased economic power, not military strength.

increased since the 1990s because of economic globalisation and the end of the Cold War (Huntington 1993; Risse-Kappen 1994, 1995; Wapner 1996; Hirst and Thompson 1996), sovereign states are still seen to be the most appropriate agents for improving welfare of their population. Moreover, international organisations, or regimes, cannot function properly without political legitimacy and authority given by states.

Systemic theories seem to be able to explain *general* differences in activities between powers (eg. the United States) and other states (eg. Australia) through capability distributions, as it explains what powers can afford to do that other states cannot.<sup>5</sup> What they do not explain is why foreign policy behaviour of states with similar capability distribution, especially small states, can differ. According to both realist and liberal arguments, states with similar capability should act similarly irrespective of their unit-level differences. Nevertheless, it seems those cases are rare in reality. In most cases, these states' policies are different in substance, levels of commitment and timing.

Several causes can be pointed out for this insufficiency in structuralist theories. First, emphasis has often been placed on theoretical parsimony. Most structuralist attempts to theorise foreign policy behaviour of states have tried to retain, or compete with, the parsimony and scientific rigor of original structural realist models. Second, partly due to the traditional predominance of 'high politics' as the subject of international relations study, theoretical literature tended to focus on great power perspectives. Third, excessive reliance on the 'rational choice' assumption, which can often be seen in game theories, caused incomplete explanations of small states' behaviour. Explaining every state activity only with maximisation of subjective expected utility is not sufficient since it does not provide any insights into the preferences the state had or how those preferences have been developed. While the rationality cannot be totally discarded when analysing states' choice of policies, the problem is that, if too much emphasis is placed on rationality, it would treat states' policy 'preferences' as givens (Richardson 1991: 31), and that would eventually lead to unsatisfactory explanations of small states' behaviour.

To explain differences in small states' foreign policy behaviour in a given environment, unit-level variables need to be brought into the analysis. In other words, states' policy preferences and domestic policy processes matter in explaining their foreign policy activities (Moravcsik 1997). The international environment and its change have strong influences on small states like Australia as Biersteker (1992: 113) argued 'states that adapt their economic policies to respond receptively (both flexibly and favourably) to these changing global conditions will do well, or at least have a better chance of doing well, in the increasing

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<sup>5</sup> The United States' aggressive unilateralism in its trade negotiations with Japan in the 1980s and 1990s and, more recently, its leading role played in the war against Iraq without the support from the United Nations are good examples. It is very unlikely that states like Australia could do the same.

competitive world economy'. But the international environment does not necessarily force a state to take one particular approach towards a respective policy area. Gourevitch (1978: 911) stated:

However compelling external pressures may be, they are unlikely to be fully determining. Some leeway of response to pressure is always possible. The choice of response therefore requires explanation. Such an explanation necessarily entails an examination of politics: the struggle among competing responses.

It should be seen that the international system provides a certain range of foreign economic policy options that a small state can practically pursue. It is more appropriate to see the system as an environment in which small states must operate to achieve their policy goals than as the sole determinant of their foreign policy behaviour.<sup>6</sup> Small states have some choices over some areas of decision. Just how much depends on what areas of decision and what under what circumstances (Gourevitch 1991: 228).<sup>7</sup>

### **The Focus of Domestic Policy Process: State or Society?**

To explain states' foreign policy, examining the impact of the international system alone is not enough. There must be more than one policy choice available to a state at any given time. The arguments about how states choose policies, nevertheless, did not escape the influence of the controversy over whether individual volition or circumstantial constraints are the primary locus of explanation. The former takes states' political, economic and social attributes and policy making processes as independent variables to explain foreign policy outcomes as a dependent variable ('*inside out*' approach, or *second image* in Waltz [1959]); the latter reverses the causal relationship ('*outside in*' approach or *second image reversed* in Gourevitch [1978]). These approaches presuppose that foreign policy and domestic politics are separate phenomena. But as deepening interdependence of intricate domestic and foreign policies occurs, this presupposition does not hold. Analyses of what outcomes come about through what process in these complex interactions need to be focused. Policies are supposed to depend on numerous factors such as

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<sup>6</sup> Sprout and Sprout (1957), Starr (1978) and Papadakis and Starr (1987), among others, discussed an 'environmental' analysis of foreign policy. Their concept of an environment in which states operated, however, included unit-level variables such as governmental, societal and individual factors.

<sup>7</sup> Thakur (1991: 279) argued that size-differentiating theories of state behaviour were subsets of national attribute theory, and how much choice small states could have was specific to the actor, context, issue, region and time.



their priorities and preferences in a given policy area, domestic institutions and the power balance among domestic constituencies.

How then are these factors formed in a state? Traditionally, the major determinant of the formation of domestic policy preferences, priorities and institutions was seen as *either* the state *or* society. The former consists of the structure of political authority (primarily political party(-ies) in power and the state bureaucracy) and the latter consists of societal interest groups which represent the relations of the various arms of production (including industry, finance, commerce, labour and agriculture) (Katzenstein 1978a: 19).

Foreign economic policy can have significant consequences for the material interests of societal groups such as industry organisations and labour unions. Societal interest groups try to influence policy makers as much as possible to make and implement economic policies that serve their interests. In this pluralistic society-centred approach, foreign economic policy is explained as the result of ongoing competitions among domestic societal and political groups (Lindblom 1977; Milner 1988; Rogowski 1989; Rogers 1993; Frieden and Rogowski 1996). State actors are viewed basically as intermediaries, or agents, creating policies according to political pressures, or sometimes threats, exerted by interest groups.

Political leaders involved in the foreign economic policy process have their own bases of potential support such as their electoral constituencies and certain interest groups. Depending on their support bases, leaders' roles, responsibilities, priorities and perceptions can be expected to differ. Policy outcomes would therefore depend on who (and which group the political leader represents) is most influential in the decision making process. Decision making in foreign policy can be seen as a process of bargaining, persuasion and the formation of coalitions among the participants. This intra-governmental process model was applied by Neustadt (1960), Lindblom (1965) and Allison and Halperin (1971), among others. Policies must attract support from those constituencies in the society upon whose votes political leaders ultimately depend. Through his two-level game approach, Putnam (1988) argued that a political leader negotiating an international agreement has to conform to the need of domestic constituencies. In other words, to succeed, any international agreement must fall within a certain range of acceptable contents ('win-set') of domestic constituencies.

In clear contrast to these lines of argument, a state-centred approach does not see the state as a mere agent of societal interest groups. State actors are the main players of the policy process and they decide foreign policy according to their policy preferences and goals, which do not necessarily coincide with domestic sectoral interests. Early realist literature emphasised that decision making and the implementation of foreign policy were conducted by leaders of states.

To realise 'national interests' defined as power, Morgenthau (1949) relied on well-trained leaders and diplomats as independent variables.<sup>8</sup> In this approach, the rationality and human nature of policy makers were taken as the most important factors of foreign policy making. In contrast, Waltz (1959: 80–1) looked at the state as a whole as an important determinant of foreign policy, stating: 'since everything is related to human nature, to explain anything one must consider more than human nature. The events to be explained are so many and so varied that human nature cannot possibly be the single determinant'. Allison (1971) pointed out that the traditional 'rational actor' model, which relies heavily on leaders to make decisions through choosing rationally among available options, is not adequate to provide a full understanding of foreign policy decisions.

Katzenstein (1976, 1978c) and Krasner (1978a) argued that the state played the central role in policy processes. The main point of their argument is that the state has its own needs and goals, which cannot be reduced to specific societal interests (Krasner 1978a: 333).<sup>9</sup> The state pursues 'national interest' that is related to *general* societal goals, and as such has a consistent ranking of importance over time (Krasner 1978a: 13, 35). Ikenberry, Lake and Mastanduno (1988a: 10) took the state as a whole as an actor in foreign policy process in a broad sense. Political leaders, senior bureaucratic officials, policy advisers and so on are viewed as individual participants (policy makers) within the process. Policy makers are assumed to represent the concept of 'national interest' and participate in the policy making process not so much as agents of any particular groups in the society. Rather, they tend to take actions to achieve the policy objectives that they believe are most beneficial. Furthermore, state policy makers are in the position to be able to make links between foreign economic policy of their own and other states and tie certain policy issues to a larger set of international issues. By doing so, they can bargain to realise the state's overall interests (Ikenberry 1988: 167–71).

It seems that an analysis that depends solely upon either a society-centred or state-centred approach would not be able to grasp the bi-directional nature of influences between the state and society. On the one hand, state actors need to be receptive to the demands of the society, in particular that of their direct constituencies; on the other hand, they are in the unique position that enables them to set policy goals, to form policy preferences for realising the goals and to mobilise support from the society. In fact, Katzenstein (1978b: 308), one of the main supporters of the state-centred approach, more or less admits the need to combine the two approaches to

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<sup>8</sup> Morgenthau (1949) argued that only the workman-like manipulation of diplomacy in a realist way could achieve the national interest (defined as power) and the potential transformation of international politics.

<sup>9</sup> Goldstein (1988: 185) also pointed out that 'the state is the institution which interprets, more or less correctly, national needs'.

explain policy outcomes: ‘government officials do not define policy objectives single-handedly but in conjunction with business and financial leaders’.<sup>10</sup>

One of the attempts to accommodate bi-directionality of influences in state-society relations from the state-centred perspective is to focus on the ‘strength’ of the state in asserting its policy goals and preferences over the society. Krasner (1978a: chap. 3) argued that the strength of the state in relation to its own society can be envisioned along a continuum ranging from ‘weak’ to ‘strong’. Weak states’ foreign policies are dominated and restricted by societal forces such as public opinion, interest groups, and parliament and bureaucracy with members and officials who strongly support their constituencies’ demand. As a result, these states are unable to reflect their own policy preferences, even if they had them in the first place, in their foreign policies. On the other hand, strong states are independent of societal demands and pressures so that they can have autonomy in reflecting their policy preferences in their foreign policies. Actual states are supposed to fall between two extremes of the continuum. The difference between weak and strong states is assumed to originate from their institutionalised political structure such as federalist structure, the system of checks and balances between legislative and administrative branches of government and the network of interest group representation (Müller and Risse-Kappen 1993: 34).

This ‘weak-strong’ state approach has several problems in examining foreign economic policy of a state. First, weak-strong categorisation may be useful for understanding general characteristics of states for comparative purposes,<sup>11</sup> but, as Krasner (1978a: 58, 1978b) admitted, the same state’s ability to assert its policy goals and preferences over the society differs from issue to issue and over time.<sup>12</sup> In explaining shifts in foreign policy, for example, this approach may be able to indicate a strengthened (or weakened) influence of the state (or society) in certain issue areas, but does not necessarily explain why the states’ (society’s) influence strengthened (weakened). Second, this approach seems to rely too much on institutionalised political structures of states. For this reason, it does not pay attention to the question of how particular policy goals and preferences are developed both in the state and

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<sup>10</sup> The ability to influence government decisions is not necessarily limited to business and finance sectors. Other interest groups, such as associations of manufacturing industries and trade unions, can have the same ability. The degree of influence they can exert on the government depends upon the issue at hand and the state’s institutional settings to deal with those issues.

<sup>11</sup> For instance, France seems to be the candidate of a strong state with its centralised political system and the power granted to the president, while the United States can be labelled a typical weak state because of the significantly plural nature of its political structure. Federal Republic of Germany (West Germany) and Japan seems to fall in the category of intermediate (Müller and Risse-Kappen 1993: 34).

<sup>12</sup> Krasner (1978b) showed that it was easier for the US government to assert its policy objectives in monetary policy than in commercial (trade) policy mainly because the beneficiaries and victims of commercial policy in the society are relatively easy to detect while the impact of monetary policy tends to spread wide in the society.

society. Third, the approach still takes the state and society as the two factors which are potentially and directly antagonistic in foreign policy decision making process. As mentioned earlier, a state is in a unique position that allows it to manipulate and mobilise support for its policy goals and preferences from societal interest groups, and interest groups can expect better chances of realising their interests by aligning with appropriate parts of the state. Instead of focusing on *either* the state *or* society, ‘coalition building’ between them should be brought into the examination to better understand state-society relations.

### **An Alternative Approach: State-Society Coalitions as Policy Subsystems**

State-society relations in foreign economic policy making are better understood by certain cooperative structures between the state and society, rather than a continuous power game between them on policy goals and preferences. Approaches from the coalition building perspective between the state and society have been suggested and discussed in foreign policy literature (Katzenstein 1985; Gourevitch 1986; Hagan 1987; Rogowski 1989). Sabatier and Jenkins-Smith (1993) developed the ‘advocacy coalitions’ approach, which was mainly developed to explain US and Canadian domestic public policies such as education, environment and airline deregulation, but Kunkel (2003) showed that its basic framework was useful in explaining how the shifting US trade policy towards Japan in the 1980s and 1990s was formulated.

The advocacy coalitions approach has some unique features. First, it takes several coalitions consisting of actors from a variety of public *and* private institutions in a particular issue area as policy subsystems. By doing so, it avoids traditional ‘either-or’ frameworks. In this approach, the main units that compete for the realisation of preferred policies in an issue area are these coalitions, not the state and society. Second, the approach uses ‘belief systems’, rather than interests, as the basis of a coalition, because beliefs are more inclusive and more verifiable than interests. The set of interests and policy goals, and perceived causal relationships constitute a ‘belief system’. Until the 1980s, studies of international relations, let alone foreign policy analysis, lacked focus on epistemological issues (Richardson 1991: 26). Based on belief systems, this approach provides ‘social constructivist’ perspectives for the study of states’ foreign policy behaviour. Third, this approach hypothesises that policy changes are the products of two interactive forces: changes in dominant state-society coalitions in an issue area and changes external to the subsystems. This assumption seems to suit particularly well an analysis of small states’ foreign policy behaviour, which is inevitably restricted by the international

environment. Overall, it seems that the state-society coalitions approach based on Sabatier and Jenkins-Smith (1993) is applicable to the analysis of Australia's foreign economic policy.

A state-society coalition is a policy subsystem that is the interaction of actors from different public and private institutions in an issue area. Actors include not only state institutions and societal interest groups but also journalists, researchers and policy analysts who are actively concerned with a policy problem and seek to influence governmental decisions in the issue area (Sabatier 1993: 16–17). Members of a coalition share a set of basic beliefs such as policy goals, preferences, causal and other perceptions, and often act in concert in seeking to manipulate the rules, budgets and personnel of governmental institutions<sup>13</sup> in order to achieve these goals over time (Jenkins-Smith and Sabatier 1993a: 5; Sabatier 1993: 16–18).

Though the realisation of welfare (material or otherwise) forms the basis of coalition building, it is assumed that state-society coalitions are built around basic beliefs in 'core' elements such as philosophy of life and cause-effect relationships for welfare realisation. A coalition's policy goals and preferences are derived from basic beliefs. Two or more coalitions are the basic units of analysis engaged in framing debate on policy problems in an issue area and determining the content of state policy preferences. New coalition(s) will emerge when a group of actors become dissatisfied with the neglect of a particular problem by existing coalitions. For instance in the context of foreign economic policy, when protectionist policy is prevailing, those in the state and society who are dissatisfied with the policy might form an alternative coalition that favours free trade, and when multilateralism is prevailing, bilateralist coalition might be formed. Members of a coalition are not necessarily from the same political affiliation.<sup>14</sup>

Public policies can be conceptualised in the same manner as 'belief systems', that is sets of value priorities, important causal relationships, perception of the efficacy of policy instruments, etc. (Sabatier 1993: 17).<sup>15</sup> There are three types of beliefs in the system (Sabatier 1993: 30). First, fundamental normative and ontological axioms that define a person's underlying personal philosophy are called 'deep core' beliefs. By definition, deep core beliefs are hard to change. In

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<sup>13</sup> Governmental institutions here are not only the organisational structure but also a set of laws and rules whether written or unwritten.

<sup>14</sup> This is particularly so in countries like the United States where the 'divided government' – the situation that the presidential power is held by one political party and the majority of Congress is held by another – is norm rather than anomaly, and bureaucratic and private institutions are significantly pluralistic. There is a recent example in Australia, too. The support for the movement for Australian republic in the 1990s attracted support from members of all major political parties.

<sup>15</sup> In the study of international relations, Goldstein and Keohane (1993) argued extensively on the importance of ideas for states' foreign policy decision making. Case studies of the volume covered wide range of states and events where idea mattered, including the Anglo-American negotiations over the post-war international trade and financial regimes (Ikenberry 1993), the Stalinist political/economic policies in China (Halpern 1993), decolonisation by the European states after the World War II (Jackson 1993) and the creation of the European Community's internal market (Garrett and Weingast 1993).

the context of foreign economic policy, beliefs in which economic system is best for the national economy and the promotion of living standards of the people fall into this category. The perception of how the world operates, in other words, to understand the world from either the realist or liberal perspectives, would make significant differences because such perception affects the level of confidence the state-society coalition places on the function of international laws, organisations and regimes such as the GATT/WTO and the United Nations (UN). Second, basic strategies and policy options for achieving deep core beliefs in the issue area are called 'policy core' beliefs. Whether to choose protectionist policy or free trade policy for national welfare purposes, multilateral liberalisation or bilateral, and whether to prioritise short term or long term gains all fall into this category. Like deep core beliefs, policy core beliefs are also hard to change. Once something has been accepted as a policy core belief, powerful ego-defence, peer-group and organisational forces create considerable resistance to change, even in the face of countervailing empirical evidence or internal inconsistencies (Sabatier 1993: 33). Third, a multitude of instrumental decisions and information searches necessary to implement the policy core in the issue area are called 'secondary aspects'. It is assumed that secondary aspects are easier to change especially when a policy compromise with competing coalitions is required.

Focusing on 'shared belief systems' of state-society coalitions brings 'social constructivist' perspectives of the international relations study into the analysis. Social constructivism emphasises the role of intersubjective beliefs, norms and identity of a state (as a basic unit of international relations) in international relations and foreign policy behaviour, which structural realism and liberal institutionalism take as exogenous and given (Wendt 1992, 1994, 1995, 1999; Katzenstein 1996; Ruggie 1998, 1999). The identity and intersubjective beliefs of the same state can change and pull its interests along. In other words, identity and beliefs formulated in cultural and historical contexts can form policy preferences.<sup>16</sup> Constructivists hold the view that the building blocks of international reality are ideational as well as material; that ideational factors have normative as well as instrumental dimensions; that they express not only individual but collective intentionality; and that the meaning and significance of ideational factors are not independent of time and place (Ruggie 1999: 239). These constructivist views are embedded in shared core beliefs in the state-society coalition approach. In explaining Australia's foreign economic policy and its change, identity as a core belief and the perception of how Australia should relate to the region seem to carry significant weight, because of Australia's unique history at the southern edge of Asia.

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<sup>16</sup> For instance, Berger (1996) argued that Germany and Japan today differ significantly from their pre-World War II predecessors. Antimilitarism has become integral part of their sense of self as nations and is embedded in domestic norm and institutions.

State-Society coalitions seek to learn about how the world operates and the effects of various governmental interventions in order to realise their goals over time. This process is defined as ‘policy-oriented learning’: relatively enduring alterations of thought or behavioural intentions that result from experience and are concerned with the attainment (or revision) of policy objectives (Sabatier 1993: 19). Because of resistance to change ‘deep’ and ‘policy’ core beliefs, however, such policy-oriented learning is usually confined to the secondary aspects of a belief system.

Members of a coalition will resist information suggesting that their core beliefs may be invalid or unattainable and they will use formal policy analyses primarily to strengthen and elaborate those beliefs. Changing the core beliefs of a coalition, when it happens, requires the gradual accumulation of evidence over a long period of policy research, so that changes in core elements in policies, more likely than not, need a replacement of one dominant coalition by another in the issue area. In addition, this transition is hypothesised to result primarily from changes in the distribution of political resources of subsystem actors arising from shocks exogenous to the subsystem (Jenkins-Smith and Sabatier 1993b: 42). These exogenous shocks to the subsystem usually comprise changes in socio-economic conditions and the rise of a new system-wide governing coalition. These changes can substantially affect a subsystem, either by undermining the causal assumptions of present policies or by significantly altering the political support of various state-society coalitions (Sabatier 1993: 19–20, 22).

Changes in socio-economic conditions in the context of foreign economic policy are most likely to be induced by major changes in the international economic environment such as economic crises. A dominant coalition at the time may or may not have a set of policies to respond to the new environment. Changes in a dominant coalition take place when its core beliefs are perceived to be no longer valid; thus, so too are its policy goals, preferences and institutions. Nevertheless, the change in dominant coalitions, thus the decisive change in foreign economic policy, is likely to take a relatively long time,<sup>17</sup> because the former dominant coalition tries to hang on to power by accepting alterations in its secondary aspect of beliefs to accommodate the change in the international environment. The core of a governmental program is unlikely to be significantly revised as long as the coalition that instituted the program remains in power.

The rise of a new system-wide governing coalition usually means a change of government. While, as mentioned earlier, the construct of state-society coalitions does not necessarily reflect political affiliation of members, the impact of the change of government can significantly affect

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<sup>17</sup> Sabatier (1993: 16) argued that understanding the process of policy change would require a time perspective of at least several years, and usually a decade or more.

political support and resource allocation among coalitions. This is particularly so for states like Australia which adopted the Westminster style of parliamentary democracy as the system of government. The main state actors (Prime Minister, Ministers for Foreign Affairs and Trade) come from the party, or coalition of parties, that hold the majority of seats in the House of Representatives, and bureaucratic institutions are relatively hierarchic and for the most part have a pervasive culture of collegiality, especially among the senior officials of the various foreign policy institutions (Gyngell and Wesley 2003: 40). A state-society coalition that aligns with them can expect relatively undisturbed dominance in Australia. When a change of government occurs as a result of a general election, the dominant coalition is likely to be swept aside because of the removal of main state actors and the change in the majority in the House of Representatives. Another coalition with different belief systems has a strong chance of being established as the new dominant coalition. This does not necessarily mean that policy change takes place immediately after the change of government. An alternative coalition may take some time to settle in to being dominant enough to initiate policy change.

## **Summary**

The preceding discussions on small states' foreign policy indicate that the analytical framework for Australia's foreign economic policy should incorporate several major characteristics.

The international system is seen as the environment in which a small state like Australia must operate. System-level approaches such as structural realism and liberal institutionalism that focus on distribution of capability and rely on 'rational' behaviour of states do not fully explain small states' foreign economic policies. The international environment does provide constraints on what small states can do so that states like Australia have to react to changes in the international environment. But the environment does not force small states to adopt one particular policy in any particular issue area. Rather, the international environment provides a certain range of foreign economic policy options that a small state like Australia can practically pursue. Within this range of policy options, small states attempt to realise their policy goals by choosing a policy (or a set of policies) that they perceive as best.

Which policy small states actually choose under certain circumstances depends on their policy goals and preferences. Traditionally, either state (governmental institutions) or society (interest groups) tended to be taken as a main setter of policy goals and preferences, but relying on either state or society misses the bi-directionality of influences between them. As an aggregate unit of analysis (policy subsystem) in domestic policy process, the concept of 'state-society coalitions' that consist of both state and private actors and shared core beliefs such



as policy goals, preferences, ideas, knowledge, norms etc., provides a useful approach to state-society relations. The formation of state-society coalitions, changes in dominant coalitions, or internal alteration of a dominant coalition can cause changes in policy goals, ideas and preferences, which in turn will lead to shifts in the state's foreign economic policy.

## **Changes in Dominant State-Society Coalitions and Australia's Foreign Economic Policy**

This section provides an overall picture of the rise and fall of dominant state-society coalitions in Australia, and how the development has affected Australia's foreign economic policy orientation. In other words, this section provides answers to these questions: what coalitions with what core beliefs and policy goals and preferences existed in Australia? how were these core beliefs and policy goals reflected in actual foreign economic policy? and when and why were dominant coalitions replaced with another?

First, it will be pointed out that, mainly because of the historical background to nation building, the state-society coalition with a firm belief in the need to protect almost all domestic industries ('protectionists') established its dominance soon after federation in 1901. The protectionists' dominance had strengthened during the course of World War I, the depression of the 1930s and World War II, and an almost bipartisan support for the coalition continued until the 1960s.

Second, another coalition that argued against protectionist policies from the viewpoint of economic efficiency ('trade liberalisers') began to emerge in the latter half of the 1960s. The end of the long post-war boom of commodity exports in the early 1970s inevitably revealed the vulnerability of Australia's traditional economic structure. As a result, the 1970s saw the growth of the trade liberalisers and the protectionists had to start policy oriented learning seriously and give compromises, but the decisive shift in Australia's foreign economic policy had to wait until the early 1980s when Australia suffered another massive deterioration in its terms of trade.

Third, while trade liberalisers gained dominance by the mid 1980s and significantly shifted Australia's foreign economic policy orientation in the 1980s and 1990s, they also aimed at liberalisation of regional and global trade and investment. As Australia was not capable of realising multilateral liberalisation alone, governments tried to use the Asia Pacific region, in which Australia's most important economic partners were concentrated, as a springboard for multilateral liberalisation. In this sense, the trade liberalisers had a strong tendency towards an 'Asia Pacific regionalist' policy approach.

Fourth, after consecutive failures of regional and multilateral liberalisation initiatives in the late 1990s, the government opted to pursue the bilateral route as an imperative option to realising Australia's 'national interest'. At first, most society actors such as industry organisations were sceptical about the government's initiative, but by the time a bilateral FTA with the United States came into sight in 2001, support for the government initiative grew. The 'optional bilateralist' coalition has emerged as a force, though it seems that it is yet to be established as firmly as preceding state-society coalitions (protectionists and trade liberalisers) were at their peak of influence.

This section also points out that each of these coalitions that formed the basis of Australia's foreign economic policy and its shifts were closely associated with particular perceptions of how the world operated. In general, the protectionist shared a power-based 'realist' worldview that emphasised the need of defence for a small state like Australia against adverse political, military or economic influences from overseas. The trade liberalisers shared a more 'liberal' view of the world in which multilateral cooperation was not only possible but also inevitable in the era of deepened interdependence. The newly emerging optional bilateralists share a more realist perception than the trade liberalisers and are sceptical about the effectiveness of multilateral cooperation. The view (perceptions) of the world held by each coalition was in part a product of the times and the coalitions used their respective perceptions for the purpose of backing up the rationale for their policy orientations and driving concrete policies forward.

## **The Protectionist Tradition**

### *The Origin*

The formation of the first state-society coalition in the area of the foreign economic policy issue in Australia inevitably reflected how the state was formed: at the beginning of the twentieth century, the six colonies of the British Empire (New South Wales, Queensland, South Australia, Tasmania, Victoria and Western Australia) in the remote continent at the south-western edge of the Pacific, together became a 'sovereign' country, effectively forming a customs union. With federation in 1901, the politics of 'domestic defence' emerged as an exercise in nation building (Castles 1988: 91). 'Domestic defence' naturally meant the maintenance and promotion of national security, but it also meant the protection of domestic economic activities. Already by

that time, Australia as a whole achieved one of the highest standards of living in the world.<sup>18</sup> ‘The nation was founded not in war, revolution or national assertion, but by practical men striving for income, justice, employment and security’ (Kelly 1992: 1). It was natural then that the ‘protection’ of people’s everyday lives became a government priority. According to Castles (1988: 93), the values institutionalised by successive governments were the protection of manufacturing industry through tariffs and other trade restrictions (and assistance for primary industry), the conciliation and arbitration of industrial disputes, the control of immigration, and a residual system of income maintenance for those outside the labour market. Kelly (1992: 2–13) referred to them as the ‘Australian Settlement’ characterised by White Australia, industry protection, wage arbitration, state paternalism and imperial benevolence, but what Castles and Kelly described were in fact the same phenomena. The protectionist economic policies were in large part ‘defensive’ strategies, designed to preserve the high standards of living reached during the late nineteenth century (Kenwood 1995: 40).

Anderson and Garnaut (1987: 28–39) pointed out that a variety of rationales for economic protectionism existed and explained how Australia’s state and private beliefs and policy goals had integrated. First, a belief in ‘infant’ industry protection was widely accepted as a policy to stimulate new manufacturing industry. It was argued that protection was necessary to ensure entrepreneurs would risk their investment before the industry could stand on its feet. The argument was appealing in a state like Australia, which had competitiveness in primary industry like agriculture and mining rather than in manufacturing.

Second, a belief that protection raised real wages, or allowed a larger work force to be employed at a given real wage, played an important part in moulding public opinion in favour of protectionism. This proposition was incorporated into a major official report on the Australian tariff, set up by Prime Minister Stanley Bruce in 1927 (Brigden *et al.* 1929). The Brigden report argued that protection of import competing manufacturing industry raised demand for labour and the increased demand for labour could attract immigration (mainly from the United Kingdom, Ireland and the continental Europe). Successive governments regarded an increase in population as vital for Australia not only as an economy of scale matter but also as a political/security issue. Also, the report’s proposition was very influential during periods of high unemployment such as in the 1930s.

Third, because protection was assumed to encourage an increased labour force at a given wage, it was considered to be an adequate policy to address unemployment. This was especially

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<sup>18</sup> For instance, Australia’s per capita GDP in 1890 was US\$ 1,680. This figure was well above those of the United Kingdom (US\$ 1,200) and the United States (US\$ 1,160) in the same year. This trend continued until the end of the 1920s. See Anderson and Garnaut (1987: 16).

so in Australia where real wages tended to have downward rigidity because of the institutionalised system of compulsory arbitration.

Fourth, in more general terms, there was a widely shared conception that Australia should develop a 'balanced' economy. This is not a phenomenon peculiar to Australia: almost all other states consider that their economies should not rely on specific industrial sectors and have protected their import competing industries more or less. Australia relied heavily on imports of both consumer and capital goods, which it either could not produce for itself or could produce only at excessive cost. To pay for these necessary imports, Australia produced a range of primary products both agricultural and mineral. Recognising the vulnerability of this structure through the experiences of supply shortages especially during the period of world wars, governments tried to promote import competing (or substituting) industries using protection.

Coupled with material incentives held by protected industries and labour unions, all these beliefs and factors, whether or not based on economic theories or empirical evidence, supported the expected outcomes and contributed to the formation of a strong protectionist coalition. The Free Trade Party, mainly supported by the state of New South Wales, existed in the early years of federal politics but, by the end of the first decade, lost a significant number of its seats in the Parliament and formed an anti-Labor Party coalition with the Protection Party. By 1906, the Labor Party became convinced of the advantages of a protectionist policy for wage earners and their employment, and it supported protection of the manufacturing industry in general (Kenwood 1995: 69). Support for the Country Party, which was formed in 1920 (becoming the National Country Party in 1975, then the National Party in 1982), was based on rural industries but it too joined the protection consensus. Until after World War II, because more people worked in labour-intensive agriculture – such as sugar, dairy, fruit and tobacco – mainly for domestic sale than in land-intensive production of wool and meat, the Country Party tried to represent the interests of the former more by providing financial and other assistance and protection from import competition (Anderson and Garnaut 1987: 42–3, 47). In other words, the Country Party preferred to advocate 'protection all round' rather than no protection at all (Kenwood 1995: 70).

### ***The Development before World War II***

The first uniform tariff introduced in October 1901 was a compromise between the Protectionist and Free Trade Parties in the Parliament. The result was continued protection at various levels according to type of industry but lower on the average than had ruled in Victoria where the

Protectionists were dominant. While it contained highly protectionist elements in some parts, it was basically a revenue tariff aimed at providing the Commonwealth government with sufficient funds to fulfil its financial obligations to the various state governments (Kenwood 1995: 69). From then on, Australia's tariff rates on manufactured imports maintained an upward trend. After several tariff increases including the Lynne Tariff of 1908 and the Greene Tariff of 1921, Australia's protectionist tendency was already clear in the early decades of the twentieth century. Table 1 shows average manufacturing tariff rates of some industrialised and industrialising states in the early twentieth century. Though tariff rates are not necessarily the best indicators of levels of protection because governments can employ other means, such as quantitative import restrictions, they more or less illustrate the trend. Table 1 demonstrates that, by the mid 1920s, Australia's average tariff rate for manufactured products was already higher than any others, except for the United States.

**Table 1 Average Manufacturing Tariff Rates in the early 20<sup>th</sup> Century (Selected States)**

	1902	1913	1925
Australia	6	16	27
Belgium	13	9	15
Canada	17	26	23
France	34	20	21
Germany	25	13	20
Japan	10	20	13
Netherlands	3	4	6
United States	73	44	37

Source: Anderson and Garnaut (1987: 7).

The impacts of the world depression in the 1930s and World War II in the 1940s helped the protectionist coalition grow even more dominant. The depression in 1929 caused a sharp increase in unemployment and there was a strengthening of support for a tariff increase. In addition, the depression forced Australia's export earnings to drop sharply, thus bringing the current account deficit problem to the economy in the early 1930s. Aiming for securing employment and reducing the trade deficit (and by so doing, financing payments to foreign debt), the government introduced the Scullin Tariff in 1930 and devalued the Australian pound in 1931. The Scullin Tariff increased tariff rates even higher and also imposed quantitative restrictions on imports. These two measures were introduced primarily to ease the current

account deficit and unemployment problems, but they also had the effect of raising protection of manufacturing industries.

In parallel with protection of manufacturing, assistance and support for rural industries also grew. On the one hand, the importance of rural products such as wool, wheat and sugar to Australia's exports had been critical since the early stages of federation. Given the limited capacity of manufacturing industries, Australia was heavily dependent on these rural industries to provide exports necessary to pay for imports of manufactured goods. On the other hand, as mentioned earlier, more people worked in the production of labour-intensive sugar, dairy, fruit, tobacco and grain industries, which sold a higher proportion of their production in the domestic market. Governments intended to raise (and stabilise) the incomes of these farmers as well. As a consequence, successive Commonwealth and state governments were always prepared to provide financial assistance and other support measures for rural industries such as the payment of various subsidies and/or bounties, import restrictions on wheat, sugar, butter and others, and income tax concessions. Stabilisation of rural incomes was mainly pursued through the control of prices and output of products, rather than by acting directly on farm incomes. The principle of a higher domestic price for farm products than on overseas markets was established in the early stage of federation. Marketing boards for individual products like sugar, wheat, wool, dairy, rice, butter, cheese, milk, eggs, cotton, fruit and vegetables, meat, fish were established from the early 1920s and monopolised the sale of these products. To maintain high domestic prices, governments from time to time introduced production quotas and restriction on volume of inputs such as land and water. Through this 'two-price' scheme, farm incomes were increased by the higher prices paid for rural products by domestic consumers (Kenwood 1995: 49). Many rural industries had become heavily dependent on government assistance but generally increasing manufacturing protection had given justification for this assistance under the argument of a geographically and sectorally 'balanced' economy (Kenwood 1995: 44).

One exception to the increasing level of 'protection all round' was the provision of preferential treatment to British imports. During most of the nineteenth century, most Australian colonies were prepared to give preferential access to their markets to British imports, in return for gaining reciprocal treatment for their exports on the large British market, though whether or not they got the actual implementation of reciprocal preferential arrangements was largely affected by the British trade policy of the time (Cleary 1934: 1–5). After federation, the Commonwealth government voluntarily granted preferential treatment to British imports for the first time in 1908 and subsequently increased the margin of preferences during the course of World War I (1914–18) and at the outbreak of the world depression (1929), without securing much reciprocal action from the United Kingdom. The United Kingdom, because of its superior

capacity for manufacturing exports and its need to secure cheap imports of foodstuffs and raw material, had maintained its 'free trade policy' since the mid nineteenth century. But by the end of the 1920s, with its manufacturing exports declining as other states gained competitiveness and they tended to protect their domestic industries through high tariffs, the argument for preferences for intra-Empire trade grew in the United Kingdom. Further adverse impacts of the depression on trade in the early 1930s pushed the UK government to search for an imperial preference system, and at the Imperial Conference in Ottawa in 1932, a series of bilateral and reciprocal preferential trade agreements were concluded between the United Kingdom and its Dominions. The UK–Australia agreement assured preferential access of Australia's exports (especially important agricultural products for Australia such as wheat, dairy and dried and canned fruits) to the UK market, while Australia also provided much reduced tariff rates to virtually all British imports than to those from other states.<sup>19</sup> The responses to the Agreement from the private sector in Australia were somewhat mixed. For instance, the Australian Industries Protection League, which was established in 1919 to promote protection and assistance for domestic primary and manufacturing industries, did *not* oppose the idea of providing preferences to the 'Mother Country'.<sup>20</sup> The League, nevertheless, argued against the preferential margins given to British *manufacturing* imports, which might induce severe competition in the domestic market (Hume-Cook 1938: 37–9). The Agreement obtained Parliamentary approval without amendments. The basic framework of reciprocal provision of preferences between the United Kingdom and Australia was to be maintained until the early 1970s, when the United Kingdom joined the EEC and realigned its tariff structure to suit the customs union.

### ***The Post-war International Economic Regime and Australia's Protectionist Policy***

World War II strengthened the power of the Commonwealth government to intervene in domestic economic activities to manage the wartime emergency circumstances. This experience had provided a cogent demonstration of Keynesian theory in practice and, by the early 1940s, the Keynesian economic policy was well underway in Australia (Capling 2001: 19). At the same time, World War II had worked to strengthen the core beliefs of the protectionist coalition. Domestic industries must be protected and assisted by government policies to maintain

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<sup>19</sup> At the start of the preferential agreement, the Australian government provided: at least 15 per cent less tariff rates to British imports on products that attracted less than 19 per cent tariff duties from other states; at least 17.5 per cent less tariff rates on products that were subject to 19 to less than 29 per cent; and at least 20 per cent less tariff rates on products that were subject to 29 per cent or more (Cleary 1934: 25).

<sup>20</sup> In fact, the League's secondary objective was stated as 'the extension and retention of a system of Tariff Preferences to Great Britain on all classes of goods and commodities' based on 'patriotism and goodwill' (Hume-Cook 1938: 16, 36).

sufficient supply of various products, not only for increasing the standard of living of the Australian population but also for preparing for times of emergency when essential imports might be significantly reduced. The beginning of the Cold War immediately after the war further strengthened the protectionist coalition's 'realist' view of the world so that governments further emphasised the need to defend national sovereignty and protect the domestic economy from penetration by cheaper products (Kenwood 1995: 38).

The designing of the post-war international economic regimes had already started during the war. The United States played a major role in this process to set the concept of free trade at the centre of the new regime, realised as the establishment of the IMF, the International Bank for Reconstruction and Development (IBRD, World Bank) and the GATT. The United States provided critical wartime assistance to the United Kingdom based on the 'Agreement on Mutual Aid against Aggression' concluded between them in 1942. The Article VII of the Agreement stated that both states would commit themselves to 'the elimination of all forms of discriminatory treatment in international commerce, and to the reduction to tariffs and other trade barriers' (Crawford 1968: 9). This pledge laid a foundation for the post-war negotiations for the establishment of the international economic regime, especially the GATT. The negotiations were revolved around the US proposal to introduce two principles into the new regime, 'non-discrimination' and the 'unconditional MFN treatment', as they were considered to assure freer trade in the world.

The Australian government had some serious concerns in accepting these principles. First, Australia wanted to maintain the British Imperial (Commonwealth) Preference system. It was not only for the reason of emotional imperial ties but also for practical reasons. Under the preferential system, the Commonwealth members, especially the United Kingdom, had become significant markets for Australia's exports such as sugar, dried and canned fruits, beef and dairy (Capling 2001: 16).<sup>21</sup> Second, as explained earlier, the Australian government believed that states should be able to keep their right to protect its domestic industries from import competition whenever they thought necessary. The US proposal did not recognise economies like Australia, which were dependent on the production and export of primary commodities, but had ambitions to develop a diversified manufacturing sector. 'The United States proposals promoted tariff reductions at precisely the time that Australia more than ever before was committed to the use of interventionist measures to promote industrialisation' (Capling 2001:

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<sup>21</sup> Domestic support for the maintenance of the preferential system was not without opposition. Parts of Departments of Commerce, Agriculture and External Affairs believed that the system had not only outlived its usefulness but also had become detrimental to Australia's trade interests, as it had made Australia overly dependent on the British and Commonwealth markets (Capling 2001: 16). Nevertheless, the opposition did not attract enough support to influence the government policy on this matter.



18). Third, the government was sceptical about being able to get a sufficient level of market access for its exports, which consisted mainly of primary commodities, in return for tariff and other concessions it would make. The government particularly doubted the ability of the United States, already the largest economy in the world, to open its primary commodity market to Australian exports (Capling 2001: 16–17).

Thus, during the negotiations for the International Trade Organization (ITO) Charter and the GATT, the Australian government insisted the following points. First, the government strongly argued that the ITO Charter must include a provision that ensure an international collaboration to promote full employment in the major developed economies. Full employment in the major developed economies was seen as ensuring growing demands for Australia's exports (Crawford 1968: 7). In addition, it would support greater stability in prices for primary commodities (Crawford 1968: 31). Second, the government sought the active promotion of production and productivity in relatively under-developed economies, and maintained the need for industry protection. J. J. Dedman, Minister for Post-War Reconstruction, identified Australia as being in the middle stage between developed and developing economies and argued in the Parliament that:

A country in a process of rapid industrialization cannot give up its choice between protective tariffs, quantitative restrictions on imports, and payment of production subsidies as means of fostering its industrial growth. Australia found it necessary to press for concrete recognition of our right to use such protective measures and clear provision for their use in appropriate circumstances.

(Statement, 27 February 1947, quoted in Crawford 1968: 56)

The government also sought permission to use defensive measures, such as quantitative restrictions of imports, at the time of economic emergencies. Third, the government stated that it would not eliminate or reduce already existing tariff preferences except in return for a sufficient level of compensating concessions.

The result of international negotiations in the latter half of the 1940s was basically favourable to Australia. The 'full employment' and 'economic development' provisions were included in the ITO Charter. The tariff reduction negotiations in 1947, which led to the birth of the GATT, allowed the already existing preferential systems to stay, making the structure of the British Commonwealth Preference system largely remain intact (Crawford 1968: 36). The GATT also permitted to use quantitative import restrictions for defending the balance of payment as an exception to general rules. Tariff concessions offered to Australia in the negotiations covered almost all principle products that Australia exported or could expect to

export. What was significant for Australia was the US concession to reduce its tariff on wool by 25 per cent, in addition to the reduction of its tariffs on beef, mutton, lamb and butter (Crawford 1968: 75). While Australia had to offer concessions in return in the form of certain reduction of the British Commonwealth preferences and general tariffs, the government concluded that the deal was good enough for the Australian economy as a whole to sign, and Australia became one of the original signatories of the GATT in 1947. The unexpected failure to establish the ITO, chiefly because of the US Congress' rejection to ratify the Charter, meant that the 'full employment' and 'economic development' provisions were not transferred into the GATT fully, but the Australian government resolved that it was more beneficial for its economy to stay in the GATT.

A good result of the GATT negotiations in 1947, nevertheless, was not automatically reflected in practice in following years. Some tariff concessions gained from European states and the United States in 1947, especially for Australia's foodstuffs and raw materials, were being nullified by the operation of non-tariff devices, protective in effect and often in intention (Crawford 1968: 129). At the GATT review process in 1954–5, the Australian government strongly criticised the lack of genuine reciprocity in the operation of the GATT articles, but it became apparent that it was not going to be practicable to treat trade in agricultural products in the same way as trade in most manufactured products. The prospects for an effective reciprocity of MFN treatment in the Australian tariff were not greatly advanced (Crawford 1968: 131). In this circumstance, the government opted for securing its right to protect domestic industries because reducing or maintaining low tariffs and other trade restrictions on manufactured products without receiving reciprocal return in agricultural commodities was totally inconsistent with the protectionist coalition's belief system and was not acceptable. At the GATT review meeting in 1951, John McEwen, Minister for Commerce and Agriculture, stated:

My Government would want to be satisfied that, when necessary, action could be taken to protect Australian domestic industries, particularly those in early stages of development. ... there is no provision for emergency action where a contracting party finds that a developing industry will face critical circumstances unless it is placed in a competitive position in the domestic market. Australia, as a rapidly developing country, must have sufficient freedom in this regard.

(Speech at the Ninth Session of the Contracting Parties of the GATT, 9 November 1954,  
quoted in Crawford 1968: 150)

As a result of the review process, the members that were heavily dependent upon a few primary commodities for their export income and relying on their tariff as an important aid for diversifying their economies were permitted to enter into negotiations for the adjustment of 'bound' tariff rates on selected items (Crawford 1968: 160). By this amendment, combined with the original right to raise (or impose new) tariffs on 'non-binding' items, Australia had effectively secured the freedom to raise any tariffs for protective purposes.<sup>22</sup>

Australia's somewhat uncomfortable relations with the GATT continued through the 1950s and the 1960s. It was mainly because agricultural products, on which Australia's interest was concentrated, were virtually excluded from the negotiation agenda. Though prepared to participate in meetings, McEwen was always sceptical about the merit of multilateral organisations such as the GATT and the United Nations Conference on Trade and Development (UNCTAD). He believed that the power and interests of major powers would usually prevail over small states' like Australia, and accepted it as reality (Golding 1996: 150).

While being sceptical about the ability of multilateral liberalisation processes to deliver Australia's interests, the Liberal/Country government pursued bilateral routes for export promotion more vigorously and flexibly because it would be easier to ensure reciprocal actions from partner states. A good example is the negotiations with Japan in the 1950s, which culminated in the commerce agreement between the two states in 1957. At the time, Australia's exports to Japan were steadily increasing reflecting Japan's growing demand for commodities such as wool and foodstuff for its post-war reconstruction, and the trade balance was heavily in favour of Australia. On the other hand, since the end of World War II, exports to the United Kingdom, traditionally Australia's main export market, were decreasing and the United Kingdom had already expressed its intention to join the EEC, which meant the eventual termination of preferential access of Australia's agricultural products to the UK market. While Australia was maintaining preferential tariffs to the imports from the United Kingdom and applying MFN tariff rates to most other states, punitive tariff rates were applied to Japanese imports as an exception according to Article XXXV that allowed Australia not to assume GATT obligations towards Japan, even after the latter's accession to the GATT in 1955. To reduce MFN tariff rates and apply them to Japanese imports to secure better access to the Japanese market, which was far more promising than the British one, the Australian government faced

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<sup>22</sup> The subsequent and frequent actions by the Australian government to unbind 'bound' tariff rates were not popular because other GATT members whose interests were adversely affected were rarely satisfied with the alternative concessions that Australia offered. Crawford (1968: 133) warned that excessive use of this right would reduce respect for Australia's complaints on other matters. He added that this would be more and more the case with developing states if Australia unbind tariff rates of significance of their trade.

two difficult problems. First, the agreement with the United Kingdom still set the obligatory margins of preference on British imports. Thus, without a new arrangement, if Australia were to reduce MFN tariffs, it also had to further lower the preferential tariffs on British imports. By that time, the Australian government saw the preferential arrangement with the United Kingdom was unfairly favouring the United Kingdom with the result that it did not have any intention of providing further benefits to the United Kingdom. Second, domestic opposition to providing MFN treatment to Japanese imports was robust among labour-intensive import competing industries and labour unions that would face increased competition with cheaper imports from Japan (Anderson and Garnaut 1987: 118). Trade Minister McEwen and some senior officials from the Department of Trade, particularly John Crawford, provided strong leadership to counter these problems. After tough renegotiations with the United Kingdom, Australia was successful in 1956 in cutting the obligatory preferential margins on British imports, reducing them from levels of 17.5 per cent to levels of 10 and 7.5 per cent, and promptly reduced MFN tariff rates on hundreds of items (Capling 2001: 60). At the negotiation with Japan, which ran concurrently with the one with the United Kingdom, Japan demanded MFN treatments on all its exports. While Australian farmers argued strongly for an end to any discrimination against Japanese imports – they did so to obtain greater access to Japanese markets for their products in return – opposition from manufacturing industries and labour unions was very strong as was to be expected. To lead the negotiation to success, after intense discussions in the cabinet and despite opposition from the Labor Party, the Liberal/Country government decided to comply with Japan's demand and concluded an agreement in 1957 that exchanged MFN status.<sup>23</sup>

### *Institutionalisation of the Protectionist Policy Preferences*

As the protectionist state-society coalition had dominated the foreign economic policy agenda for such a long time, its policy idea and goals were deeply institutionalised in the policy making process. Especially after 1949 when the long reign of the Liberal/Country parties' government started, the trade related bureaucracy<sup>24</sup> became the Country Party's power base (Capling 2001: 55–7). Since that time, the ministerial post of the Department has become a reserved seat for a senior leader of the party whenever the Liberal and Country (later National) parties are in power. John McEwen, who held the trade minister's post from 1949 to 1971, was given by

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<sup>23</sup> Australia's decision to abolish all discrimination against imports from Japan in the early stage of bilateral negotiations was not expected by the Japanese negotiators. The Japanese government expected much tougher negotiation so that it could not believe the Australia's offer on the spot (Golding 1996: 193).

<sup>24</sup> Originally the Department of Agriculture and Commerce, reorganised as the Department of Trade in 1956, again reorganised as Department of Trade and Industry in 1963.

Prime Minister Robert Menzies almost total responsibility regarding trade policy (Golding 1996: 179). McEwen, who himself was a farmer under the soldier settlement scheme and experienced hardships to survive after World War I before becoming a Member of Parliament (Golding 1996: 41–3), was a champion of protectionism. In addition to the need to protect the manufacturing industry for the purpose of workers' welfare, he stated:

Primary producers needed government assistance because they operated in an economy where wage earners were protected by arbitration and manufacturers were protected by tariffs. Some equivalent form of protection for primary industry was needed to ensure that efficient operation carried with it a reasonable prospect of profit.

(John McEwen, quoted in Golding [1996: 140])

As the protectionist coalition's belief system was firmly institutionalised in the foreign economic policy making process and successive trade related departments enjoyed relative autonomy in this area, some detriments seemed to have emerged by the 1970s. The 1976 report by the Royal Commission that enquired into the efficiency and effectiveness of the Australian government administration pointed out that foreign policy and other public policies needed more coordination and integration (Royal Commission 1976: chap. 10, 4.10–12). Emphasising that the Department of Foreign Affairs should be the principal bureaucratic coordinator of all official activities and policies that affected the international policies of the government, the report recommended several reform measures, which were centred on enhancing efficient interdepartmental coordination. It recommended, for instance, regular briefings by the Department of Foreign Affairs officials to those from other departments participating in international negotiations, frequent interdepartmental exchange of information relevant to foreign policy and the establishment of task forces, study groups and interdepartmental committees to review particular aspects of policy in relation to particular countries, groups of countries, or to problems of more general significance (Royal Commission 1976: chap. 10, 4.7, 15, 18). These recommendations imply that the two Departments in charge of external relations, Foreign Affairs and Trade, did not have sufficient policy coordination between them. Collins (1976: 395) argued that it was neither only nor always the foreign ministry which was the obstacle. Autonomy held by the Department of Trade in foreign economic policy issues and its reluctance to change sometimes caused uncoordinated and inconsistent overall foreign policy.

### **Trade Liberalisers' Indictment and Protectionists' Resistance**

### *The Emergence of the Trade Liberalisers Coalition*

The growth of the domestic economy during the long post-war boom period had relied on the export growth of primary commodities and the redistribution of income to other sectors. Australia's protectionist policy was designed to shelter its domestic manufacturing, services and domestic-oriented agricultural sectors from international competition. In protecting these sectors against imports, the Australian government was effectively discriminating against much more competitive industries like export-oriented agriculture and mining. If this dominance of the protectionists were to be reduced so as to shift the foreign economic policy orientation, an alternative state-society coalition that favoured less protection and freer trade and investment regimes must be firmly established. In addition, exogenous shocks were most likely to be required to replace the protectionists.

The opposition to protectionist policy from those disadvantaged, such as export oriented mining and agricultural industries and manufacturing that relied heavily on imported materials, in the post-war period was in fact consistent, if not strong enough to influence the protectionist coalition. The criticism against protectionism also came from economists who argued that the policy was not founded on economic theories and that governments were actually wasting scarce resources by misallocating them as a result of protectionist policies. There has been a string of people like Heinz Arndt, Max Corden, H. C. (Nugget) Coombs, Peter Drysdale, Ross Garnaut, Fred Gruen, Stuart Harris, Richard Snape and others who, as academics and government members, have argued for liberalisation and deregulation. For instance, Corden argued as early as 1958 for abolishing the import quota system and introducing a uniform and low tariff rate on all imports<sup>25</sup> and wrote:

When a firm is not doing well, instead of being forced to reduce its cost or improve its product, it has the more fruitful avenue open to it of stopping or hindering its competition. The energies which might better go into competing on an economic basis are put into pressing for higher protection.

(Corden 1958: 340).

By the late 1960s, these economists advocated trade liberalisation with near unanimity. An important development in the process was the increasing sophistication of the analysis of the effects (or costs) of protection, and especially of attempts at establishing new measures of

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<sup>25</sup> Corden suggested gradually replacing import restrictions with tariffs, then establishing a standard tariff rate for all imports. The standard tariff rate could be varied according to the balance of payment situation. Corden based his suggestion on a fixed exchange rate.

measurement (Anderson and Garnaut 1987: 67). Their argument for liberalisation and deregulation, with more persuasive evidence of costs of protectionism and benefits of liberalisation, induced the beginning of the 'policy-oriented learning' process by the protectionist coalition, but the process turned out to be very gradual and it took more than a decade before decisive change in foreign economic policy was made.

In 1963, the government appointed a committee to research the general state of the domestic economy, to point out problems and advise on measures to respond to them. The committee headed by J. Vernon produced a report in 1965 (Vernon *et al.* 1965), which dealt with protection policy in detail. The report accepted the benefits of protectionist policy, especially its effect on employment. At the same time, it recognised that the level of protective measures given by the government to some industries might have been too high and be having growth-inhibiting effects (Anderson and Garnaut 1987: 70–1). Also, from the resources allocation point of view, the report pointed out that disparities in the levels of protection afforded to individual industries were more damaging than the high protection given to domestic industries as a whole (Kenwood 1995: 79).

In the mid 1960s, the Tariff Board (later reorganised as the Industries Assistance Commission in 1974, reorganized again as the Industry Commission in 1990 and since 1998 known as the Productivity Commission) started their review of Australia's tariff structure. The Tariff Board was established in 1921 for the purpose of advising the government on tariff policy. Though the Board was allowed to inquire into any matter relating to tariff policy on its own initiative, it had confined itself to much narrower roles (Kenwood 1995: 70). Until the mid 1960s, the Board's main role was to handle government requests to review the level of tariff protection afforded to specific manufacturing industries and advise government whether the protection provided was appropriate. This procedure contained a bias towards increased protection, since governments generally referred matters to the Board in response to pressures from manufacturers seeking additional assistance. In 1967, the Board began a systematic review of tariffs on manufacturing industries. The Board intended to advise the government to reduce tariffs of excessively protected industries as the first step towards tariff reform (Rattigan 1986). The Board's initiative was supported by primary industries such as agriculture and mining, some financial journalists and even by some members of the Liberal Party, which was then in power.

While the Vernon report's moderate implication of the need for reducing excessively protective tariffs and the Tariff Board's broader initiative of tariff restructuring were both backed strongly by the financial press like *the Australian Financial Review* which was the only national financial paper (Anderson and Garnaut 1987: 72; Golding 1996: 202, 211), they both

met with opposition from the members of the protectionist coalition such as manufacturers' organisations, trade unions and parts of the government (especially from the Department of Trade and Industry). As a result, the government effectively shelved the moves for the time being. These episodes in the 1960s showed that an alternative state-society coalition that shared a core belief in liberalisation and a freer trade and investment system began to emerge. Nevertheless, the 'trade liberalisers' coalition had to wait exogenous shocks to the policy subsystem that favoured them before they could become a dominant force.

### ***Changes in the International Economic Environment and the Failure of the Whitlam Experiment***

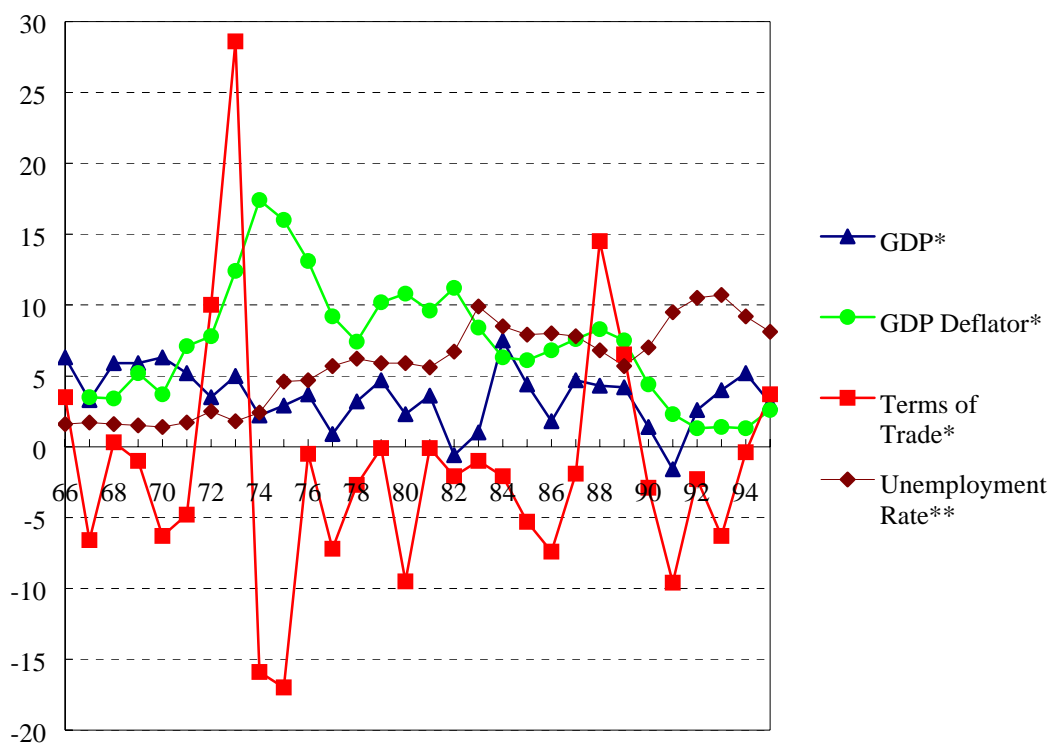
The first exogenous shock to foreign economic policy subsystem came from the international economic environment in the early 1970s. Accompanying the mineral resources boom in the early 1970s, Australia recorded a large current account surplus in 1972/73. As a result, pressure on the Australian dollar to appreciate grew significantly. The government always had the power to control the exchange rate, which was principally fixed but adjustable, but it avoided appreciation of the exchange rate then to maintain the provision of 'exchange rate protection' to domestic industries that produced tradable goods. The appreciation was seen to have adverse effects on both exporting agricultural and mineral industries and import competing manufacturing industries. The perception that the Australian dollar was undervalued led to large capital inflows and growth in the domestic money supply, resulting in growing inflationary pressure.

The accession to power of the Australian Labor Party (ALP) in December 1972 after twenty-three years in opposition coincided with this economic situation. The government, led by Prime Minister Gough Whitlam, decided to appreciate the Australian dollar to reduce the balance of payment surplus, thus countering inflation, but the effects of the appreciation quickly disappeared under the impact of the resources boom still going on in 1973 (Anderson and Garnaut 1987: 83). An alternative measure to reduce the balance of payment surplus was considered to be the promotion of imports. The committee set up by Whitlam to advise him on ways to increase imports recommended a reduction of tariffs on all imports by 25 per cent under the conditions of the fixed exchange rate system (Rattigan *et al.* 1973). The government promptly responded and implemented a 25 per cent 'across the board' tariff cut in July 1973. Despite these efforts to contain inflation, the government at the same time implemented public policies that effectively nullified them. As a political party based on support of wage earners,



the ALP government supported the demand of labour unions for a wage increase.<sup>26</sup> Also, by spending more budget expenditure than the previous government in areas such as healthcare, education and culture (Dyster and Meredith 1990: 269), it did not refrain from pushing forward its social programs and welfare reforms. The net result was an unprecedented increase in the inflation rate (Figure 1).

**Figure 1 Australia's GDP Growth Rate, GDP Deflator, Terms of Trade and Unemployment Rate, 1966–95 (per cent)**



Notes: \* Percentage points change over the previous year. \*\* Per cent at August each year.  
 Source: IMF, *International Financial Statistics Yearbook 1996*; Reserve Bank of Australia (1996: 202).

The Whitlam government faced more serious economic problems when its major trade partners, the United States, Japan and the EC were pushed into recession after the first oil crisis. As the terms of trade suffered massive decline in 1974 and 1975 (Figure 1), Australia's export earnings suffered significantly, while manufacturing industries lost competitiveness due to the large increase in relative costs reflecting the appreciation of the Australian dollar and rapid increase in

<sup>26</sup> Average weekly wages grew at 12 per cent in 1974, while award wage rates grew at 19 per cent for males and 27 per cent for females (Anderson and Garnaut 1987: 83).

real wage. The unemployment rate also increased rapidly and by 1975 it hit the five per cent mark (Figure 1), which was the highest level since the depression in the 1930s (Anderson and Garnaut 1987: 84). This rapid decline in exports, manufacturing outputs and employment in the mid 1970s provided renewed grounds for demands for protection.

The Whitlam government was ousted in the most unusual and controversial way in the history of Australia's federal politics. In addition to economic difficulties, the government suffered the 'Overseas Loans Affair' scandal in 1975.<sup>27</sup> In October 1975, the opposition controlled Senate blocked the Supply bills, which were necessary for the government to execute the national budget, and urged the government to call a general election. To counter this move, the government controlled House of Representatives passed a motion of confidence in the government. After three weeks of deadlock, on 11 November, the Governor General John Kerr dismissed Whitlam and commissioned Malcolm Fraser, the leader of the Liberal/National Country opposition, as a caretaker Prime Minister. Fraser immediately sought a double dissolution and Kerr dissolved the Parliament on the same day.<sup>28</sup>

Fraser chose to make the ALP's 'mismanagement' of the economy a major issue in the 1975 electoral campaign. Both Liberal and National Country parties went into the campaign with policy platforms that contained typical protectionist elements (Liberal Party of Australia 1974; National Country Party of Australia 1975). In the policy speech during the campaign, Fraser argued:

We will give Australian industry the protection it needs. We would sooner have jobs than dogma. ... Under Labor, there have been disruptive changes in exchange rates, tariffs and other protective devices.

(Fraser 1975: 6, 22).

As one of the election pledges, the opposition promised to provide sufficient protection to maintain employment in the textile, clothing and footwear (TCF) industries (Anderson and Garnaut 1987: 93). In the end, the Liberal/National Country won the general election of 13 November with a big margin.

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<sup>27</sup> The Whitlam government tried to raise an overseas loan of four billion Australian dollars to finance a number of natural resources and energy projects. The loan was sought not from the traditional US or European sources but from the Middle East where 'oil dollars' were abundant following the sharp rise of the petroleum price since 1973. Rex Conner, Minister for Minerals and Energy, used a Pakistani broker for the deal but, in the end, no loans were obtained and no commission were paid (Website: 'whitlamdismissal.com', [<http://www.whitlamdismissal.com/loans/>], last accessed on 7 April 2005).

<sup>28</sup> The dismissal of Prime Minister by an 'unelected' vice-regal representative is remembered as the major constitutional crisis in Australian federal politics. The event has been documented in many publications. For instance, see Kelly (1995).

Though the 25 per cent tariff cut across the board was introduced basically as a macro-economic management measure to reduce the balance of payment surplus and to counter inflation, rather than directly target a reduction in levels of protection towards domestic industries, it marked one of the first major moves to reverse protectionist policies. It has been pointed out that Whitlam was a liberal and 'anti-protectionist' who had a firm statist belief that government's policy decisions should not be influenced by pressure from interest groups (Anderson and Garnaut 1987: 80). The tariff cut decision was made as a result of factors such as advice from a policy advisory committee and key ministerial advisers (Charles and Farrell 1975: 95). This indicates, on the one hand, that the Whitlam government was actually relatively free from the pressure of the protectionist coalition. On the other, it also indicates that the Whitlam government did not attempt to consult with the dominant protectionists coalition to persuade them to support its policy reversal. An alternative coalition of trade liberalisers, which might have strongly supported the tariff cut, had just begun to emerge in the latter half of the 1960s and were still far from dominant in the early 1970s. As a result, the Whitlam government's liberalisation had a weak and unstable support base if any, and when the international economic environment became worse for the Australian economy, the opposition from the protectionist coalition returned strongly and liberalisation policy could not be sustained.

### ***The Protectionist Returns with Some Policy Oriented Learning***

The Liberal and the (National) Country Parties returned to government in 1975 and so was the protectionist coalition in the centre stage of policy making in the foreign economic policy area. The 1970s as a whole, nevertheless, was to become the decade of more policy-oriented leaning for the protectionists, steady growth of the trade liberalisers coalition and policy compromises of the former to the latter.

First, policy reform for agriculture had started even before the ALP came to office in 1973 and was continuously pursued through the 1970s. The government already felt in the 1960s that regulations and support for agriculture had resulted in inefficiencies in the sector. Nevertheless, since agricultural products still remained major sources of export earnings, fundamental restructuring of agricultural assistance and support were hard to undertake. The mineral resources boom of the late 1960s and early 1970s provided the catalyst for agricultural reform as it reduced Australia's dependence on agriculture as its major foreign exchange earner. The government set out to improve agricultural efficiency through a program of rural reconstruction, which aimed at rationalising the agricultural sector so as to concentrate production in economically viable farming units. Rural adjustment schemes commenced in 1971 when farm

reconstruction became a permanent feature of Australia's agricultural policy. Restructuring and rationalisation of rural industry became even more pressing in 1973 when the large UK market with preferential access for Australian agricultural products was removed following the United Kingdom's entry into the EC (Kenwood 1995: 44). In December 1973, the Whitlam government appointed a committee to inquire into broad aspects of agricultural policy and the committee produced a report in May in the following year. The report ('Green Paper') pointed out that the Commonwealth government still maintained a great variety of intervention measures in the rural sector (Harris *et al.* 1974: Appendix Table A2.13), and strongly advised the government that the policy goal should be redirected to enable the sector to adjust effectively to market needs and opportunities. As a consequence of the Green Paper, a new rural adjustment scheme was introduced in 1976, consolidating most of the existing schemes.

Second, the Industries Assistance Committee (IAC) was set up in 1974, replacing the Tariff Board. The establishment of the IAC was not merely a change of name. It significantly strengthened its function as a research agency. The IAC had a much broader mandate than the Tariff Board, being able to carry out inquiries into agricultural, mining, services industries as well as manufacturing, and was not restricted to tariff matters but could examine any form of direct or indirect assistance to producers. The most significant contribution of the IAC was probably its sophisticated measurement of the extent of protection provided to individual industries. The effective rates of assistance were calculated for individual products, taking into account not only tariff protection but also other means of governmental assistance and support, and was made readily available to the public. These visible and objective measurements played an important role in notifying and educating the public, especially those in exporting industries, how much (or less) protection their industries were getting from the government compared with others.<sup>29</sup>

Third, a series of reports produced by government appointed committees in the 1970s all indicated the need to restructure manufacturing industry by reducing the level of protection. In mid 1974, in response to the rapid decline in manufacturing output and after the 25 per cent tariff cut across the board, the Whitlam government appointed a committee to advise on policies for manufacturing industries in general. The report (Jackson Report) recommended tariff reduction for manufacturing industry in principle (Jackson *et al.* 1975). The Fraser government published the White Paper on manufacturing industry in 1977 to follow up the issues raised by

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<sup>29</sup> For instance, along with the idea publicised by the Green Paper that farmers as export producers were put at a disadvantage by tariffs, the disparity in levels of assistance among industries caused discontent in rural exporting industries. Initially, this criticism sparked an argument for tariff-compensating assistance to farmers (and other exporters), but following a number of heated debates on the desirability of using tariff compensation, rural groups came to see their interests as being advanced the most by general trade liberalisation (Anderson and Garnaut 1987: 72).

the Jackson Report in the previous government. The White Paper recognised the need for reduced protection in the context of encouraging a more specialised, trade-oriented manufacturing sector (Commonwealth of Australia 1977). The Fraser government set up another committee of inquiry into the issue of economic structural change, this time as a direct response to ASEAN members' criticism about Australia's protectionist policy. The committee released its report (Crawford Report) in March 1979 (Crawford *et al.* 1979) and indicated the need for a strategy to deal with adjustment problems. To achieve a desirable industry structure, the report encouraged industry to become more import competitive and more export oriented through lower protection. While all these reports and the White Paper stated the desirability of a reduction in the level of protection, they all took a gradualist approach as well. The most likely reason for it was the recent experience of the Whitlam government's 25 per cent tariff cut that worsened the economy, which had already been struggling with inflation. The White Paper stated that a time of lower economic activity – such as in the latter half of the 1970s when the terms of trade did not pick up, inflation rate fluctuated at high percentage and the unemployment rate remained at over five per cent (see Figure 1) – was not an appropriate time for reducing protection. The Crawford Report also recommended that, in addition to the necessity to provide positive industrial development incentives, the procedure to reduce levels of protection should be gradual and be introduced only when the unemployment rate was low and stable.

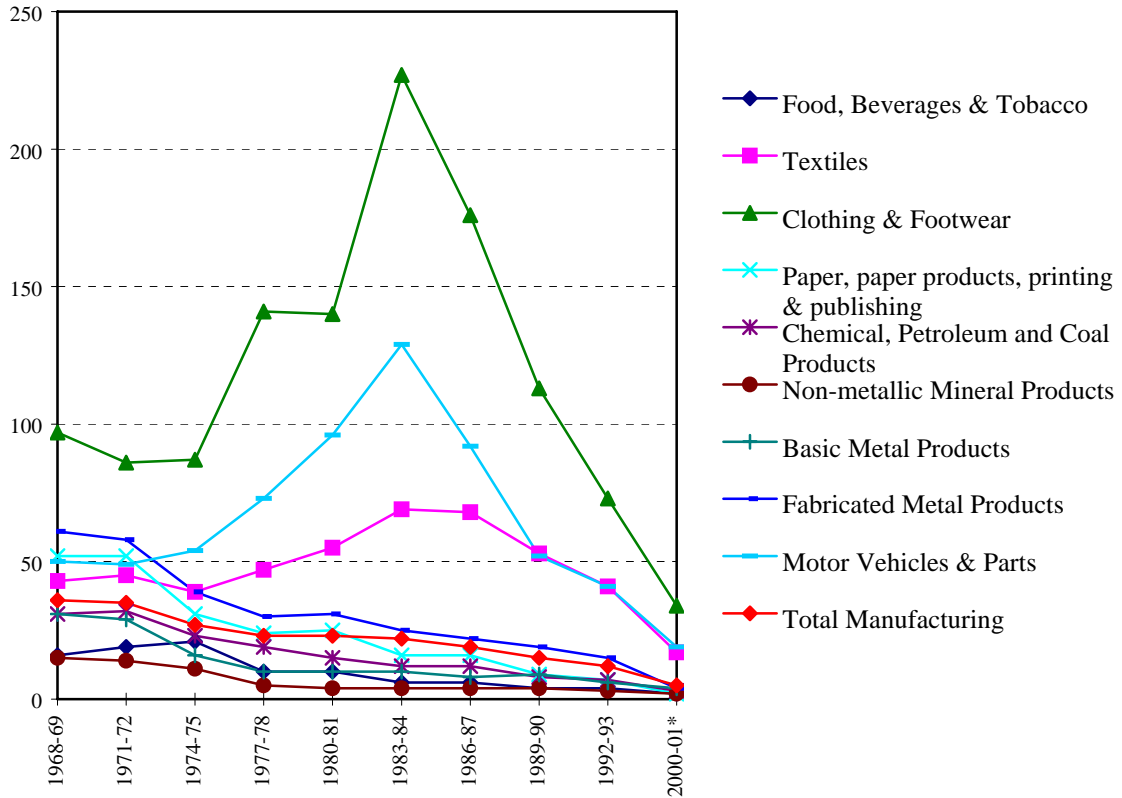
In this situation, the Liberal/National Country government kept its election promise to provide sufficient protection for TCF and passenger motor vehicles and parts (PMV) industries. The TCF industries were the most affected by the 25 per cent tariff cut in 1973 because they were already enjoying the highest levels of protection at the time. These industries also experienced the largest increase in nominal wages in the mid 1970s.<sup>30</sup> Furthermore, TCF industries were the most vulnerable to imports from developing economies. The government had a strong incentive to protect labour-intensive TCF industries, as their decline due to increased import competition would escalate the problem of unemployment. The government reaffirmed the continuation of protection of these industries during the 1977 election campaign giving a further guarantee that the protection would not be reduced for a subsequent three years (until 1980). In July 1979, prior to the 1980 election, the government announced that the commitment would be extended for a further year, to mid 1981. The government preferred import quotas rather than tariff increases to protect TCF and PMV in this period and, as a result,

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<sup>30</sup> Between 1972–73 and 1975–76, nominal wages of TCF industries rose 91 per cent, compared with an average of 74 percent for other manufacturing industries (Anderson and Garnaut 1987: 88).

the average effective rates of assistance for these products rose sharply from the mid 1970s until the early 1980s (Figure 2).

**Figure 2 Average Effective Rates of Assistance, 1968/69 to 2000/01 (%)**



Note: \* forecast figures in 1995.

Source: Industry Commission (1995), Tables A6.3 and A6.6.

It seems that the government and protectionist coalition had to make policy compromises in industries other than TCF and PMV, in addition to the rural adjustment scheme that had been ongoing since the early 1970s. At the GATT Tokyo Round of trade negotiations (1973–9), though the Fraser government disassociated itself from formula-based general tariff reductions<sup>31</sup> because they did not extend to agricultural products (Capling 2001: 90), it decided in 1977 to bind some tariff rates realised by the 1973 tariff cut and to reduce a range of tariffs further on

<sup>31</sup> Before the Kennedy Round (1964–7), tariff reduction was negotiated bilaterally with reciprocity, then generalised on an MFN nation basis. Since the Kennedy Round, the formula-based approach, with negotiated exceptions, has been adopted to achieve wider coverage of products for tariff reduction and avoid free riding. Either way, MFN treatment was applied to all members, thus Australia was a potential beneficiary even it did not fully participate in rounds (Snape 1984: 2; Corden 1995: 11).

non labour-intensive manufactures. Figure 2 shows that the average effective rates of assistance to most manufactured products other than TCF and PMV gradually declined during the 1970s. Nevertheless, the figures for total manufacturing decreased only slightly between the mid 1970s and early 1980s during the period of the Fraser government, because of the sharp increase of TCF and PMV protection.

In sum, the Liberal/National Country government led by Fraser returned to office in 1975 with a protectionist coalition. Its foreign economic policy goals and preferences were clearly reflected in how it dealt with TCF and PMV industries. At the same time, however, the government had to reduce the levels of protection of other industries as policy compromises under growing pressure for structural adjustment through liberalisation. In fact, the Australian economy as a whole did not quite pick up in the latter half of the 1970s: the terms of trade kept declining; the unemployment rate stayed around six to seven per cent; and the inflation rate remained high compared with the figures in the late 1960s (Figure 1). In other words, it had become increasingly obvious that the traditional economic structure was unsustainable under the new international economic environment. Yet, the government was reluctant to redirect its protectionist policies decisively. The protectionist coalition's core beliefs were hard to change. To achieve a recovery in the Australian economy, the Fraser government chose to wait for another export boom to occur. In retrospect, it did not take place until the late 1980s. Instead, another massive deterioration of the terms of trade hit the Australian economy in 1980 after the second oil crisis.

### **Trade Liberalisers' Ascendancy in the 1980s**

As illustrated by the growing pressure for a reduction in protection levels since the latter half of the 1960s, an alternative state-society coalition to protectionism had emerged in the 1970s and been firmly established by the early 1980s. Following the economists' argument against protectionism in the 1960s, the review of the tariff structure by the Tariff Board and the IAC, and a series of reports by government appointed committees that recommended the reduction of protection in principle, the number of Members of Parliament who favoured liberalisation expanded in the 1970s though it had been a small minority on each side of politics in the 1960s. Notably, even the enthusiastic support for 'protection all around' by the Country Party, which effectively dominated Australia's trade policy in the 1950s and 1960s, began to erode in the 1970s, especially after the retirement of its leader and long-serving Trade Minister, John McEwen (Anderson and Garnaut 1987: 80).

The 1970s also saw the emergence of new or reorganised societal interest groups that share liberalisation and deregulation of the economy as their core beliefs and policy goals. These groups became the main actors on the society side of the trade liberalisers' coalition. The rural exporting sector had always stood to gain from less protection for domestic industries, but agricultural organisations tended to be commodity based and it had been difficult to find a common ground against protectionism. The rural reconstruction schemes implemented in the 1970s, which reduced effective assistance for agriculture and preceded any of the similar attempts towards other industries, together with the information from the IAC, encouraged agricultural organisations to form a unified stance against manufacturing protection. In 1979, the National Farmers' Federation (NFF) was established as the national peak organisation for agricultural industries and it made trade liberalisation a prime goal of its political lobbying and public education programs. The NFF, since then, has been seeking the exposure of all industry to market forces and the creation of an internationally competitive Australian economy (Kelly 1992: 43–5). The mining sector had also been severely disadvantaged by distorted resource allocation and economic incentives as a result of protectionist policies. While the sector remained relatively quiet in the argument against protectionism in the 1970s,<sup>32</sup> five large mining companies argued for movement toward a low, uniform tariff in the context of the IAC inquiry on general reductions of protection in 1982 (Anderson and Garnaut 1987: 74). Industrial organisations of the sector had been based in each state and had been slow to establish a national organisation. The New South Wales based Metal Trades Industry Association (MTIA), which was established back in 1873, became an active advocate for liberalisation and deregulation in the 1980s and 1990s. The MTIA was reorganised as the Australian Industry Group (AIG) later in 1998 by merging with the Australian Chamber of Manufactures. Because of the merger and subsequent expansion of the membership, the AIG has come to represent broader industrial interests including manufacturing and services, and has been playing an important role in Australia's foreign economic policy decisions.

Given that the government's protectionist attitude was hard to change, most manufacturing industries with exporting interests traditionally had preferred to seek export subsidies rather than push for trade liberalisation. In part, this was also because they had been benefiting from the protected domestic market. By the late 1970s, a few manufacturers did have sufficiently large exports relative to domestic sales to justify supporting trade liberalisation as part of a major

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<sup>32</sup> The mining sector expanded rapidly in the 1970s, while the manufacturing sector contracted. It can be seen that the mining sector judged that they would attract little public sympathy by exerting political pressures for their own interests and directly against those of the declining manufacturing industries. The large size of the enterprises in the mining sector and the high degree of foreign ownership would also have made it difficult to win public support (Anderson and Garnaut 1987: 74).



reform of the incentive system (Anderson and Garnaut 1987: 74–5). In December 1977, the Associated Chamber of Manufacturers of Australia, the Australian Council of Employers' Federations and some other employers' organisations merged to form a new body: the Confederation of Australian Industry (CAI). The primary objective of the formation of the CAI was to provide a unified front to negotiate with the Australian Council of Trade Unions (ACTU), a powerful peak body of the labour movement in Australia. Also, it aimed at representing business interests to government. These aims, however, were not fully achieved since major member organisations and companies were not ready to give up their independent capacity to lobby the government (Warhurst 1984: 4–5; McEachern 1991: 25). Their representation to the government was made either directly or through another organisation called the Australian Industries Development Association (AIDA). The AIDA in turn was merged with the Business Round Table in 1983 to form the Business Council of Australia (BCA), which consisted of around fifty largest companies and their subsidiaries in Australia. The main factor in BCA's formation was said to be frustration with the CAI. The CAI sought to defend the status quo, or at least the benefits that business gained from traditional arrangements (McEachern 1991: 32). The BCA took a more pro-liberalisation stance because its members were more competitive than other small and medium-sized firms. According to a report by the BCA in 1992, 'exporting goods and services builds wealth, but so can importing if Australia's scarce resources and skills are more productively applied to the products'. The BCA argued in the same report that what the government could do to help industry was 'to remove obstacles and support long term competitiveness to enhance the individual initiatives' (BCA 1992: 64–6).

By the early 1980s, the representation of sectional interests in foreign economic policy evolved to a stage where such organisations had become more national in characteristic, more centralised, more professional and more highly integrated into the federal government (Warhurst 1984: 23). At the same time, an increasing number of state and society actors in the foreign economic policy issue shared a core belief in free trade and a policy preference for liberalisation and deregulation. The trade liberalisers coalition, consisted of these actors, was ready to take over the protectionist coalition as the dominant force. What it needed was another exogenous shock to the policy subsystem that would be a trigger for decisive change in Australia's foreign economic policy.

The exogenous shock again came as a massive deterioration of Australia's terms of trade in the early 1980s. Australia's terms of trade had not improved since 1974, but in 1980, it recorded an almost 10 per cent slide from the previous year (Figure 1). The unemployment rate started to rise sharply in 1982 and reached almost 10 per cent in 1983 (Figure 1). By this time, it was clear

that trying to create export opportunities for primary commodities alone would not generate enough jobs and income to provide Australia's increasing population with a rising standard of living (Garnaut 1989: 205). Australia needed policies to advance international competitiveness, not only in the traditional primary commodities sector but also in the manufacturing and services sectors, and to promote these sectors' exports. Faced with this environment, the Fraser government still found it difficult to completely overturn the core belief of the protectionist coalition.

The ALP, which was re-elected to government in 1983 after eight years in opposition, initiated domestic economic reform. In the same year that it was elected, the government, led by Prime Minister Bob Hawke, who was a member of the committees that produced the Jackson and Crawford Reports in the 1970s, floated the exchange rate and surrendered most of official control over exchange dealings. The government removed restrictions on foreign ownership of merchant banks in 1984, allowed fifteen foreign banks to commence operation in 1985 and removed interest rate control on trading banks in 1986. By the end of 1988, the exchange rate had depreciated by 24 per cent to the level prevailing at the beginning of the decade (Keating and Dixon 1989). The depreciation of the currency was expected to result in an increase in exports and a decrease in the current account deficit and foreign debt, but it did not have this effect immediately. In fact, the economic situation worsened after a brief recovery in 1984. The current account deficit rose to around 4.5 per cent of GDP in 1986 and foreign debt was also still increasing.

The lack of productivity, thus competitiveness against foreign products, in manufacturing industries was perceived to be the major obstacle to a comprehensive reduction of the current account deficit. To increase productivity and competitiveness in manufacturing industries, the government finally decided to expose them to competition in the domestic and world markets and to phase out the protection they, and related parties such as trade unions, had long enjoyed. The Economic Statement of May 1988 announced a general program of phased reductions in protection for all manufacturing industries: tariff levels over 15 per cent were to be reduced to 15 per cent (except for 'sensitive' sectors of PMV and TCF) by 1992, and tariffs between 10 per cent and 15 per cent were to be brought down to 10 per cent by the same year. The Industry Policy Statement of March 1991 declared the continuation of the program stating that tariffs of most imports were to be phased down to five per cent by 1996, the average nominal rate of assistance was to be reduced to three per cent by the end of the 1990s, and the average effective rate of assistance was to be reduced to five per cent by the same time. The government also decided to restructure TCF and PMV industries by exposing them to competition though with a different timetable from other industries. Import quotas for PMV and TCF were abolished in

1988 and 1993 respectively. By 2000, the tariff rates of PMV and most textile and footwear imports would be reduced to 15 per cent, and clothing products would have a flat tariff rate of 25 per cent (Corden 1995:12; Stanford 1992a). These significant measures to reduce protection for manufacturers are clearly depicted by substantial falls in average effective rates of assistance since 1986–87, as shown in Figure 2.

It is important to acknowledge that the decision to diminish protectionism was made unilaterally, not reciprocally with other states, and in difficult economic situations. The recession in 1986 forced the government to realise the desperate and urgent need for structural adjustment of the domestic economy. The famous ‘banana republic’ speech by the then Treasurer Paul Keating was made in May that year.<sup>33</sup> While it is understandable that the government announced its Economic Policy Statement of 1998 at the time of economic recovery,<sup>34</sup> the Industrial Policy Statement to continue structural adjustment was released in 1991 when the Australian economy was in poor condition: GDP recorded minus growth for the first time since 1982, the unemployment rate rose to 9.5 per cent and the terms of trade dropped 9.6 per cent from the previous year. This decisive shift in foreign economic policy could not have been sustained if ‘trade liberalisers’ had not already become a dominant coalition by the mid 1980s.

The uniqueness of Australia’s trade liberalisers was that it was the Labor Party that became a champion of the state side of actors. Traditionally the ALP had the support of the ‘working class’ and was expected to reflect the demands of that part of the society, especially the wage increase. After World War II, Australia’s social structure changed dramatically as the Australian economy experienced the long boom period of the 1950s and 1960s. The number of traditional working class people declined. As a result, the ALP remained in opposition for most of the post-war period, except when Whitlam led the party to the election victory in December 1972 and stayed in office for short three years. The ALP clearly needed to re-think its traditional ideology-driven policy positions and look for alternative policy goals. Dominant figures of the government such as Bob Hawke, Paul Keating, John Dawkins and Gareth Evans who continuously occupied important ministerial posts set the objectives of restructuring the domestic economy by introducing more market oriented policies. These policy makers

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<sup>33</sup> Keating’s remark on the economic situation on a radio program went as follows: ‘I get the very clear feeling that we must let Australians know truthfully, honestly, earnestly, just what sort of international hole Australia is in. ... It’s the price of commodities on world market but it means an internal economic adjustment. And if we don’t make it this time we never will make it. ... We will just end up being a third rate economy ... a banana republic’ (quoted in Carew 1992: 171–2).

<sup>34</sup> GDP growth rate in 1987, 1988 and 1989 were 4.7 per cent, 4.3 per cent and 4.2 per cent respectively. The unemployment rate tended to decline over the period and the terms of trade recorded a better figure than the previous year for the first time in 15 years in 1988.

proclaimed that this 'economic rationalism' would deliver the best material outcomes for the population.

On the labour movement side, the ACTU also altered its stance towards protectionism in the 1980s. In 1986, the ACTU (with the Trade Development Council [TDC]) sent a joint mission to Europe to research the relationship among governments, trade unions and the business communities in the formation and implementation of economic policy. After the mission, the ACTU announced its own economic reform strategy and recommendations in a report called *Australia Reconstructed* (ACTU/TDC 1987). The report covered a wide range of matters ranging from macroeconomic policy to wages in individual firms, and the overall direction was in line with the government's economic reform policy. Employees in the manufacturing and service sectors had been enjoying relatively high standards of living under the protection policy, but the ACTU realised that it was also the main cause of Australia's inability to compete in the new international economic environment. To realise full employment, low inflation and a higher standard of living, ACTU put emphasis on increased investment and productivity rather than protection (ACTU/TDC 1987: 19). The report argued that the manufacturing sector should become internationally competitive and export oriented. Successive post-war governments provided substantial assistance to develop a diverse manufacturing sector aimed largely at supplying a small domestic market. This policy was not without economic and social cost. In particular, the manufacturing sector that developed in the 1950s and 1960s was not, to any significant extent, export oriented. As a result, it was less exposed to international competition and not subjected to adequate pressures for improvements in production and price, which is implied by such competition (ACTU/TDC 1987: 90–1). The ACTU's strong emphasis on productivity and the development of an internationally competitive manufacturing sector was a clear departure from the traditional attitude of Australia's labour movement.

Being in a position to have close relations with trade unions and the labour movement,<sup>35</sup> and sharing the awareness of the need of improved productivity and competitiveness in manufacturing and other industries, the ALP government cooperated with the ACTU on economic reform policy as well. The 'Accord', a policy agreement on wages and prices between the ALP government and the ACTU, stood out as an example. The Accord, which was renewed seven times over the period between 1983 and 1996 when the ALP remained in power, was made with the purpose of controlling the level of real wages within a manageable range, thus controlling one of the major forces of inflation, tackling the problem of unemployment that increased sharply and hit the 10 per cent mark in 1983 (see Figure 1), and reform of industrial

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<sup>35</sup> In addition to traditionally close relations between the ALP and ACTU, Bob Hawke had worked for the ACTU, starting as a research officer and advocate in 1958, and as the president for a decade before becoming an ALP Member of Parliament in 1980.

relations for improved productivity. Successive Accords included measures such as the abolition of full wage indexation to inflation, a two per cent real wage cut, the introduction of a 'two-tier' wage structure in which the 'first-tier' wage gave a flat increase for all workers and the 'second-tier' increase was tied to improved productivity, substantial cuts in personal income tax and the promotion of enterprise bargaining (Matthews 1994: 208).<sup>36</sup> The ALP government successfully and continuously involved trade unions, which had been one of the beneficiaries of the traditional protectionism, in the policy making process.

Another example of major institutional change in Australia's foreign economic policy making was the amalgamation of the Department of Foreign Affairs and the Department of Trade in 1987. As mentioned earlier, the Department of Trade had strong influences over foreign economic policy issues. The Department controlled policies on exports, international trade negotiations, foreign direct investment and imports,<sup>37</sup> under the auspices of the Country Party that was a champion of protectionism.<sup>38</sup> After the retirement of McEwen, however, the number of trade liberalisers in the Department also grew. The division and resultant trade policy stance of the Department of Trade had sometimes conflicted with Australia's foreign policy objectives as a whole. As to be discussed later, since active involvement in multilateral liberalisation processes formed an important part of its economic reform policy, the government was in need of better departmental coordination within the Department of Trade and between the Departments of Trade and Foreign Affairs in pursuit of its policy goals. The government decided to merge the two Departments in July 1987 and established the Department of Foreign Affairs and Trade (DFAT).<sup>39</sup> The establishment of DFAT has been seen as an attempt to integrate Australia's trade policy directly with overall foreign policy orientation (Harris 1989; Pusey 1991: 149).

The leaders of the ALP government were very confident of 'economic rationalism', because other developed states had introduced a similar set of policies several years before with reasonable results. The major changes in Australia's economic policy are parallel to, and closely followed important changes in, economic policy in the leading industrial economies of the world: the United States, the United Kingdom and Germany. Margaret Thatcher came to power

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<sup>36</sup> For more details of the Accord, see, for instance, Stilwell (1986) and Singleton (1990).

<sup>37</sup> For instance, as mentioned earlier, the negotiation process of the Australia-Japan Trade Agreement of 1957 was conducted mainly by the then Minister for Trade, John McEwen and senior officials of the Department of Trade. See Stockwin (1972).

<sup>38</sup> For the political process of the expansion of protection and McEwen's strategy to broaden political support for his Country Party, see Bell (1993), especially chapter 2.

<sup>39</sup> This major restructuring of the department was not confined to the merger of the Department of Trade and Foreign Affairs. The number of Departments was reduced from twenty-seven to thirteen, creating so-called 'super departments' such as the Department of Industry, Technology and Commerce, the Department of Primary Industry and Energy and the Department of Employment, Education and Training.

in the United Kingdom in 1979, followed shortly by Ronald Reagan in the United States and Helmut Kohl in Germany. Although there is much debate about the long-term legacy of each of these political leaders, there is little doubt that they reversed economic policy in their respective states. New policies were supported by neoclassical economic ideas that clearly gained new force worldwide in the late 1970s and early 1980s (Biersteker 1992: 118–19). Ravenhill (1991: 219) pointed out that ‘the 1980s can justifiably be called the decade of deregulation [in Australia]. The domestic agendas that the Reagan and Thatcher administrations pursued inevitably spilled over to other economies not merely through a demonstration effect but also in some instances by compelling foreign governments to offer equivalent latitude to their domestic corporations’.

### **Seeking Multilateral Liberalisation through the Asia Pacific Region**

The ALP government’s shift in foreign economic policy was a decisive endeavour to restructure domestic industries, and diversify the range of export products through liberalisation and deregulation. At the same time as these efforts to reform the domestic economy, Australia’s trade structure was experiencing a drastic change: the rise of the Asia Pacific economies as major partners. To underpin the reform, Australia needed multilateral trade and investment regimes, especially the GATT, to ensure that its newly competitive products, as well as traditional export commodities, were traded as freely as possible across borders. The Australian government’s efforts to maintain and promote multilateral economic regimes was focused on its closer relations with Asia Pacific economies, especially the East Asian economies, and using the will and schemes for regional cooperation as a spring board for multilateral liberalisation.

Under the GATT regime, interdependence among economies in the Asia Pacific region has developed steadily since the 1960s. Drysdale (1988) identified some of the factors behind this development. One was the impact of Japan’s economic growth. Japan was first in East Asia to develop its economy, and by the 1980s its GDP had become one of the world’s largest. Rapid economic growth of Japan brought about a huge increase in its demand for minerals and foodstuffs from the region. At the same time, Japanese exports of manufactured goods, as well as the flow of capital and technology transfer, into economies in the region experienced unprecedented growth. Another major factor was the development of other East Asian economies. Resource-rich economies such as Indonesia, Malaysia, Thailand and Australia enjoyed large export earnings while economies like Korea, Taiwan, Hong Kong and Singapore followed the Japanese path by adopting outward-looking, trade-oriented industrial strategies. By the late 1960s, Southeast Asian states were intent on emulating their success. Their economies

developed steadily throughout the 1970s and began to grow rapidly in the latter half of the 1980s.<sup>40</sup> Flows of capital, including foreign direct investment from Japan, Korea, Taiwan, Hong Kong and Singapore to Southeast Asian economies increased sharply in the 1980s; capital flow was then heading for China, Vietnam and Burma. Southeast Asian economies also started to invest overseas during this period. In short, East Asian economies have been providing Australia with export and investment opportunities for the past 40 years.

Table 2 shows the growing importance of East Asian economies as Australia's trade partners.

**Table 2 Australia's Trade Partners, 1960–95 (US\$ millions)**

	1960	1965	1970	1975	1980	1985	1990	1995
<b>Exports</b>								
United Kingdom	221	463	545	541	1,044	778	1,402	1,829
United States	68	237	612	1,210	2,570	2,344	4,283	3,358
Japan	120	396	1,254	3,471	5,871	6,295	10,232	12,184
NIEs*	27	56	144	656	1,612	2,135	4,554	8,986
ASEAN**	28	112	316	927	1,766	1,588	4,366	8,211
New Zealand	14	42	257	606	1,043	1,062	1,952	3,833
Others	325	1,047	1,916	5,094	9,168	9,471	14,128	18,409
Total	803	2,353	5,044	12,505	23,074	23,673	40,917	56,810
<b>Imports</b>								
United Kingdom	295	683	964	1,533	1,895	1,653	2,701	3,452
United States	134	621	1,156	2,040	4,434	5,249	9,424	12,595
Japan	37	232	577	1,759	3,477	5,430	7,308	8,880
NIEs*	5	26	91	376	893	1,626	2,928	4,755
ASEAN**	44	108	102	324	1,384	1,206	2,324	5,242
New Zealand	14	42	107	262	692	956	1,715	2,673
Others	300	941	1,650	3,954	8,252	8,335	14,452	22,534
Total	829	2,654	4,647	10,248	21,027	24,455	40,852	60,131

Notes: \* Hong Kong, Korea and Taiwan. \*\* Indonesia, Malaysia, the Philippines, Singapore and Thailand.

Source: International Monetary Fund, *Direction of Trade Statistics Yearbook*, various issues.

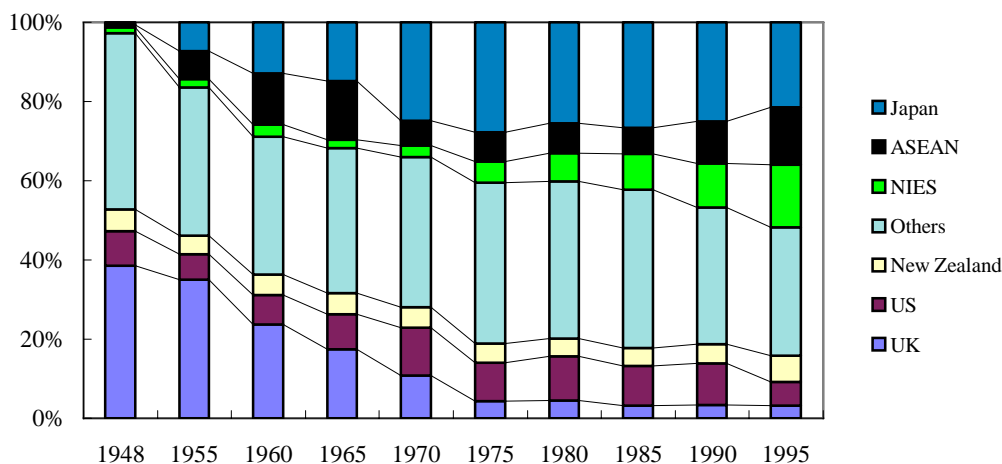
The Table confirms that Australia has been drastically increasing its exports to East Asia, including Japan, Newly Industrialising Economies (NIEs: Hong Kong, Korea and Taiwan) and

<sup>40</sup> In 1988, 1989 and 1990, Thailand's real GDP grew at a rate of 13.2 per cent, 12.2 per cent and 11.6 per cent respectively, and it has been continuing the trend in the 1990s with annual growth rates over 8 per cent. Malaysia's and Indonesia's real GDP also grew rapidly in 1988, 1989 and 1990: at a rate of 8.9 per cent, 9.2 per cent and 9.7 per cent in the case of Malaysia and 5.8 per cent, 7.5 per cent and 7.2 per cent in the case of Indonesia. They have also been keeping their growth trend with annual rates of around 6 to 9 per cent. The International Monetary Fund, *International Financial Statistics*, various issues.

the ASEAN members. It also shows that Australia's exports to Japan started to increase rapidly in the mid 1960s. Japan became the largest single export destination in the latter half of the 1960s and remains so. Exports to NIEs and ASEAN members started to grow quickly in the mid 1970s. From 1980 to 1995, the fastest growing export destination was NIEs with a more than 450 per cent increase over the period, followed by ASEAN with a 360 per cent increase. The United States remained as a major import source for Australia. Imports from East Asian economies have also been steadily increasing since the 1970s. Again, imports from Japan started to grow earlier than those from other East Asian economies. The fastest growing import sources over the period from 1980 to 1995 were NIEs with an increase of more than 430 per cent, then New Zealand with a 286 per cent increase, closely followed by ASEAN with a 278 per cent growth. It is interesting to note that, among the economies in Table 2, Australia accounted trade deficits with the United Kingdom and the United States for almost the whole period, while it recorded trade surpluses with the East Asian economies. Since the 1970s, the trade surplus with East Asia almost offset the deficits with the United Kingdom and the United States, with an exception in the mid 1980s. For instance, Australia's combined trade deficit with the United Kingdom and the United States in 1990 was US\$ 6,440 million and the surplus with East Asia was US\$ 6,592, and the same figures in 1995 were US\$ 10,860 and US\$ 10,484 respectively.

Figures 3 and 4 show the growing importance of the East Asian economies for Australia's trade more clearly from a different angle. These Figures illustrate the changes of the share of respective economies to Australia's total exports and imports over the post-war period.

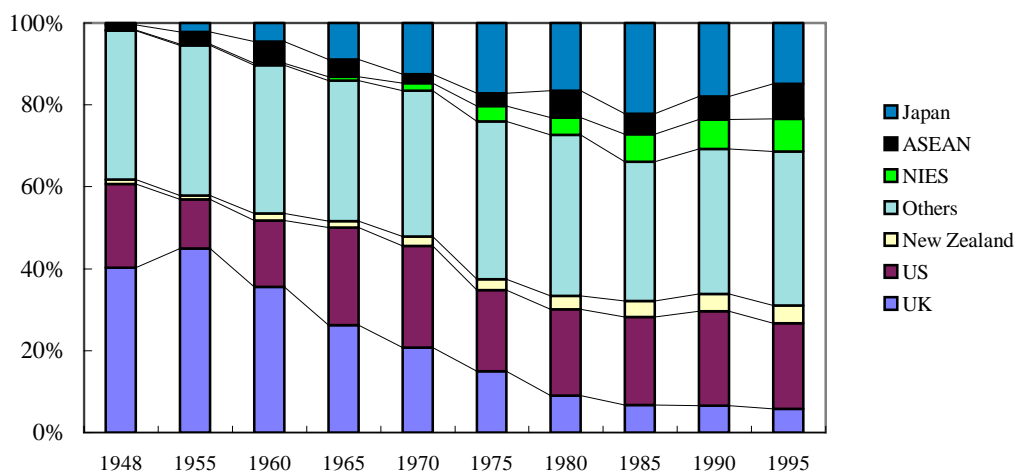
**Figure 3 Australia's Export Destinations by Share, 1948-95**



Source: International Monetary Fund, *Direction of Trade Statistics Yearbook*, various issues.



**Figure 4 Australia's Import Sources by Share, 1948-95**



Source: same as Figure 3.

Both Figures show almost the same trend. First, since the 1960s, the decline of the United Kingdom as Australia's major trade partner is quite notable. In 1948, shortly after the war, the United Kingdom accounted for about 40 per cent of Australia's total exports and imports. In 1995, those figures had decreased to only 3 per cent and 6 per cent respectively. It can be seen that the special tie between the United Kingdom and Australia, which was brought about by Australia's history as a member of its empire, and later as members of the Commonwealth, had disappeared over the period in terms of trade relations. The period between the first UK application to join the EEC in 1961 and its actual accession to EC membership in 1973 was a watershed in terms of Australia's formal trade relations with the United Kingdom. The UK engagement to Europe inevitably meant the phasing out of the traditional preferential market access schemes for Australia's exports (especially agricultural products such as beef, dairy and fruits) to the United Kingdom.<sup>41</sup>

Second, the US share in Australia's total exports seems to have reached its peak in the early 1970s (13 per cent in 1970), and since then, the figure has been gradually decreasing. It dropped to 6 per cent in 1995. For imports, again the US share reached its peak in the early 1970s (25 per cent in 1970) but has been stable since then, accounting for just over 20 per cent of the total.

<sup>41</sup> In the same period, the UK decision to withdraw its military presence from east of Suez in 1967, without full consultation with Australia, lessened their security tie, which had already been decreasing since after World War II.

Third, Japan started to occupy a meaningful share in Australia's trade since the 1960s. In 1948, its share in total Australian exports and imports were negligible, but by 1965 these figures increased to 17 per cent in exports and 9 per cent in imports.<sup>42</sup> The figures reached almost 30 per cent in exports and 25 per cent in imports in the mid 1980s, but started to decrease gradually in the 1990s.

Fourth, the growth of the share of NIEs and ASEAN cannot be ignored. As a whole, they accounted for only 3 per cent of Australia's total exports and just more than 1 per cent of imports in 1948. However, in 1995, the figures reached 32 per cent and 17 per cent respectively due to the rapid economic growth of NIEs and ASEAN over the period. Moreover, if the figures for Japan, NIEs and ASEAN are combined as 'East Asia', the figures had grown to 55 per cent of Australia's total exports and 32 per cent of imports in 1995, starting from just 4 per cent and 1 per cent respectively in 1948.

In sum, the change in the international economic environment in the Asia Pacific region over the post-war period has been characterised by the rapid economic development in East Asian economies. The Japanese economy started its unprecedented growth in the 1960s, while development of NIEs and the ASEAN accelerated in the 1980s. Their economic growth was accompanied by an increasing volume of international economic transactions that had created highly enmeshed interdependence in the region. Being a small state and exporter of primary commodities, Australia had inevitably been involved in the process of this deepening interdependence. In the process, the relative importance of some traditional economic partners such as the United Kingdom and the United States had declined, and East Asian economies emerged as new and growing partners.

The process of deepening interdependence between Australia and East Asia promoted the geographical re-orientation of Australia's foreign economic policy toward the region. To underpin structural reform of the domestic economy, the Australian government needed to realise two policy goals. First, though the economic relations with the region had deepened, as explained earlier, the government perceived an opportunity to increase economic transactions even more, because the growth of East Asian economies, except for Japan, did not show a sign of slowing down until the latter half of the 1990s.<sup>43</sup> Also, though they had a strong interest in liberal economic regimes (Drysdale 1988: 71) and began unilateral liberalisation of their domestic economies in the 1980s, most East Asian economies were still maintaining relatively

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<sup>42</sup> The conclusion of the trade agreement in 1957 guaranteed reciprocal provision of the MFN status and the abolition of import licensing and can be seen as the basis of the following development of trade relations between Australia and Japan.

<sup>43</sup> See Garnaut (1989).

high barriers to international trade and investment. Australia's intention of closer economic relations with East Asia, however, was not exactly matched by existing trade statistics. It was true, as shown in Table 2, that the total value of Australia's exports to Japan, NIEs and ASEAN had rapidly increased over the 1980s but it was also apparent that the share of imports from Australia to the total imports of these economies had decreased over the same period (Drysdale and Lu 1996). At the end of the 1980s, Australia's share in Japan's total imports was less than 6 per cent. The figures for NIEs and ASEAN were even less impressive, recording around only 2 and 3 per cent respectively.

Second, the maintenance and promotion of free and open multilateral trade and investment regimes, most importantly the GATT, has become more crucial for Australia. The international trade regime, however, was fragile in the late 1980s and the early 1990s. Since the early 1980s especially after the Uruguay Round was deadlocked, the United States opted for the creation of an FTA with Canada, and then with Mexico, to form NAFTA. The United States suggested that other bilateral and/or regional arrangements could follow. At the same time, the EC integrated its members' markets and became the EU. Such economic groupings including economic powers like the United States and the EU made outsiders very cautious. For Australia, the Australia New Zealand Closer Economic Relations and Trade Agreement (ANZCERTA, commonly known as CER) was the only comprehensive FTA it had made.<sup>44</sup> The CER emerged as a major factor in the growth of trade between the two countries (see Table 2 and Figures 3 and 4), but it was obvious that the CER alone would not fulfil Australia's needs.

The Hawke government first reacted to the US and the EU moves by considering the need for an Asia Pacific regional bloc but since it was realised that a preferential bloc in the Asia Pacific region would neither be sensible nor successful (Harris 1992: 40), the Australian government set a foreign economic policy objective to promote global free trade and investment using cooperation in the Asia Pacific region as a springboard.<sup>45</sup> In the context of state-society coalitions, the trade liberalisers coalition that had established dominance in the 1980s clearly demonstrated its will to focus on the Asia Pacific region to realise its policy goals. In other words, the coalition also had an 'Asia Pacific regionalist' character. Furthermore, the government's inclination towards multilateral liberalisation through regional cooperation shows

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<sup>44</sup> The original free trade agreement with New Zealand was signed in 1965. The CER became operative in 1983 and was reviewed in 1988. Since then, free movement has been extended to services and thus, CER has become one of the most comprehensive FTAs in the world.

<sup>45</sup> The shift of geographical focus in economic relations towards East Asia was also driven by the protection against imports of agricultural products in the EC, the United States and Japan at that time. For Australia, the EC's Common Agricultural Policy has been severely limiting the access of Australia's agricultural exports to Western Europe. A large export subsidy program (the Export Enhancement Program) by the United States had negative effects on Australia's export markets of agricultural products, particularly wheat, not only in the United States but also elsewhere.

that the government and trade liberalisers coalition had (or maybe had to have) 'liberal' perception of the world: that international cooperation, both political and economic, was not only possible but also inevitable for each state to pursue its 'national interest' under ever deepening interdependence. In other words, if international cooperation were not to function, the trade liberalisers' policy goal of domestic economic reform was to become difficult to achieve. This liberal perception of the world contrasts with the realist view generally held by protectionists, which was quite pessimistic about multilateral cooperation.

Australia successfully included agricultural products in the Uruguay Round agenda in 1989 mainly by efforts made at the Cairns Group, whose members included major ASEAN members: Indonesia, Malaysia, the Philippines and Thailand.<sup>46</sup> Before the start of the Round, the Fraser government had failed in its efforts to add agricultural products to the agenda of the GATT ministerial meeting in 1982. Freer trade in agricultural products, in which Australia had been traditionally competitive, had been an objective of successive Australian governments, but it was not realised before the Uruguay Round. The Hawke government had learned that it could not achieve its policy objectives alone in multilateral negotiations (Cooper and Higgott 1990: 18).

When the Uruguay Round seemed to be deadlocked in the late 1980s and early 1990s, and the United States and the EU opted for economic integration within their own regions, other states in the Asia Pacific region reacted to these moves. Australia and Japan responded by calling for freer trade in the region. Following in the footsteps of earlier efforts to form economic cooperation forums, such as the Pacific Trade and Development Conference (PAFTAD) series, the Pacific Basin Economic Council (PBEC) and Pacific Economic Cooperation Council (PECC), the move culminated in the establishment of the Asia-Pacific Economic Cooperation (APEC) in 1989. In the early 1990s, APEC consistently argued the importance of the successful conclusion of the Uruguay Round. It is widely acknowledged that APEC's continuous pressure contributed to the constructive conclusion of the Round. Petri (1999: 15) pointed out that APEC played an effective 'cheer leading role' encouraging and supporting multilateral negotiations. Furthermore, APEC's own attempt for trade and investment liberalisation began in the mid 1990s from which Australia could expect significant benefits given its increasing economic relations with East Asia.

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<sup>46</sup> The Cairns Group was formed in 1986 by fourteen states, which claimed not to have government subsidies for agricultural exports, for the purpose of including agriculture in the Uruguay Round agenda and pushing for multilateral liberalisation in agricultural trade. The original members included Argentina, Australia, Brazil, Canada, Hungary, Indonesia, Malaysia, New Zealand, the Philippines and Thailand, and their aggregate value of agricultural exports occupied about 30 per cent of the world total.

Another example of Australia's foreign economic policy engagement with the region was the establishment of the 'AFTA-CER linkage dialogue' process. As Australia tended to be excluded from regional initiatives by ASEAN, the government sought an alternative way to link its economy with them. The ASEAN's initiative to establish its own FTA, the ASEAN Free Trade Area (AFTA), in 1992 caused concern in Australia. The Deputy Prime Minister of Thailand, Supachai suggested in December 1993 the building of closer economic relations between ASEAN and CER members (Australia and New Zealand). Prime Minister Keating responded very positively and was quick in pursuing the proposal (Smith 1998: 242). The ASEAN Economic Ministers Meeting (AEM) in September 1994 agreed to examine possible linkages between ASEAN and the CER. Finally, the Australian and New Zealand Trade Ministers were invited to the annual AEM in September 1995 for consultations on the issue. At the inaugural Ministerial Consultations, the objective of this initiative was set as: finding practical ways of assisting businesses and expanding inter-regional trade and investment, rather than seeking to merge two FTAs – AFTA and the CER – in any formal way (Lloyd 1995: 10). A multi-layered structure for consultation involving ministers, government officials and businesses of ASEAN and CER members also emerged and the whole process came to be called the 'AFTA-CER linkage' dialogue.

### **The Emergence of Optional Bilateralists**

At the general election held in March 1996, the Liberal and the National Parties regained office for the first time since 1983. For a new government that came to power after thirteen years in opposition, it was natural for it to review all policies implemented by the previous governments, and the review, of course, included foreign economic policy. The Howard government completed a review of foreign and trade policy by the middle of 1997 and, in August, published Australia's first White Paper on foreign and trade policy (Commonwealth of Australia 1997).

The essence of the White Paper was the declaration that the new government would pursue every possible measure, including using bilateral approaches, to advance Australia's national interest defined as the security of the Australian nation and jobs and the standard of living of the Australian people. Based on the recognition that the Australian economy's ability to export and the openness of foreign markets are the key to promoting Australia's national interest – more and better paid jobs and higher living standards – and that the multilateral system's capacity to deliver depends inevitably on the will of member states (which is not always uniform), the White Paper stated:

A central feature of the Government's approach ... is the importance it attaches to strengthening bilateral relationships. Bilateral relationships are not an alternative to regional and multilateral efforts.

(Commonwealth of Australia 1997: 53)

While the Howard government declared that it would retain most trade (and foreign) policy objectives of the previous government, including giving the highest priority to the Asia Pacific region and the importance placed on the WTO, there were some indications of more inward looking, short-term and less multilateralism-oriented foreign economic policy than the previous government. First, in June 1997, the government announced the freeze of the tariff reduction schedule for PMV products for five years from 2000. In September, the same treatment was decided for TCF imports.<sup>47</sup> Second, a new favourable stance towards bilateralism, especially FTAs, was emphasised. This stance sharply contrasted to the previous Keating government's that prioritised multilateral liberalisation to bilateral agreements. During his first visit to Japan as Prime Minister in 1992, Keating made clear that Australia saw no overall gain in entering into any trading agreement which discriminated against Japan (Keating 2000: 34). Considering that an FTA with Japan was not even on the policy agenda between the two states at the time, Keating's statement effectively meant that Australia did not see any gain in any bilateral trade arrangement. In addition, the Howard government's stance on bilateralism was also different from the previous Liberal/National (Country) government's and the protectionist coalition. The previous government's bilateral efforts, which were illustrated by negotiations with the United Kingdom and Japan in the 1950s, were principally to *reduce* preferences and discrimination to develop new export markets. In other words, they were attempts to apply MFN treatment that was a principle of the GATT. The Howard government's objective for FTAs, on the other hand, are to *provide* new reciprocal preferential treatment to partners, which is an exception from GATT principles, and to discriminate against outsiders as a consequence. The Howard government's moves can be seen as a shift of foreign economic policy from that of previous governments' supported by protectionist or trade liberaliser coalitions.

Regarding FTAs, the White Paper stated:

Australia will keep an open mind about new approaches, including preferential free trade arrangements. ... The Government recognises that regional trade arrangements offer potential advantages for their participants. ... Compared with global negotiations, they are perceived as

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<sup>47</sup> *The Australian*, 6 June and 11 September 1997.

being able to go further faster, and are more likely to include “new issues” arising from the globalisation of economic activity.

(Commonwealth of Australia 1997: 42)

The *Trade Outcomes and Objectives Statement* (TOOS)<sup>48</sup> released in February 1998 confirmed the government’s stance on bilateralism and FTAs (Commonwealth of Australia 1998: 140). Nevertheless, the government did not argue then that it should establish FTAs with any particular partners.

While the government declared that Australia was open to negotiate FTAs in 1997, this ‘optional bilateralist’ policy idea was not readily accepted by societal interest groups. First, Australia’s export performance in the latter half of the 1990s was good compared with other economies. The nominal growth rates of exports in goods and services in 1997, 1998, 1999 and 2000 were 6.2 per cent, 8.4 per cent, minus 0.4 per cent and 25 per cent respectively (Commonwealth of Australia 1998, 1999, 2000, 2001). Considering that most Asian economies, which usually absorb more than half of Australia’s exports, were facing extreme economic hardship following the Asian financial crisis in 1997, and Japan was still struggling to overcome the long recession, these figures, other than that for 1999, are outstanding. From the trade policy point of view, private businesses did not have particular reasons to rely on bilateral FTAs in this difficult regional economic environment.<sup>49</sup> Second, during this period of strong export growth, there were some good reasons for the private sector (and the government) to prefer multilateral approaches to reducing trade barriers. The previous Keating government actively involved itself in the Uruguay Round to success, particularly in agricultural trade. Private businesses wanted to secure the steady implementation of the results by its trade partners and did not want bilateral FTAs to interrupt the process. At the same time, officials in DFAT who had been directly involved in the Round were sensing the onset of ‘negotiation fatigue’.<sup>50</sup> These legacies of the Uruguay Round and its success did not change just because of the change of governments.<sup>51</sup> In addition, there was a series of multilateral and regional developments from which Australian industries could expect significant trade benefits: the Early Voluntary Sectoral Liberalization

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<sup>48</sup> The Howard government decided to publish the TOOS at the start of every year from 1997 to explain to the Parliament and general public what were achieved in the previous year and what would be the policy targets of the year. Since the TOOS (renamed as *Trade* since 2003) has clearly described the government’s trade policy intentions in each issue, it has become an adequate first reference to see the changes (and/or consistency) in Australia’s trade policy directions.

<sup>49</sup> Interview with the Director of Trade and International Affairs, ACCI (29 August 2002) and the Executive Director of the AIG (5 September 2002).

<sup>50</sup> Interview with a Uruguay Round related official in DFAT, 30 August 2002.

<sup>51</sup> One of the DFAT officials who was involved in the FTA negotiations with Singapore stated that, though the coalition government officially announced that it had an open mind towards FTAs in 1997, some parts of DFAT still remained cautious on bilateral deals. Interview, 28 August 2002.

(EVSL) initiative of APEC (1997–9), the anticipated launch of a new WTO round (1999), and the proposal and feasibility study for the AFTA–CER FTA (1999–2000). Private interest groups expected the government to concentrate its efforts on these initiatives and had not asked the government to pursue bilateral FTAs until 2000.<sup>52</sup>

By 2000, however, all these initiatives turned out to be failures. Every one of these failures effectively worked as an exogenous shock to Australia's foreign economic policy subsystem which was still dominated by the trade liberalisers. The APEC EVSL initiative could not reach an agreement among members and was effectively discarded. Though trade liberalization under the APEC framework looked to be going well in the mid 1990s, the first Individual Action Plans (IAPs) – voluntary liberalization plans by each member – submitted in 1996 to the Ministerial Meeting were, in fact, disappointing for the pro-liberalization members. What most members offered were not much more than they had already committed to in the Uruguay Round (Okamoto 2004a: 1). The EVSL initiative starting in 1997 was an ambitious attempt to dispel this frustration and stimulate APEC liberalization as a whole by accelerating liberalization in selected sectors. The Australian government enthusiastically involved itself in the initiative and was successful in putting food and energy, two of its most important export sectors, into the targets for early liberalization (Wesley 2004). The results of EVSL, which became clear by November 1998, were much less than Australia had expected. Participants in the EVSL could not agree on tariff reductions in the APEC framework because of their different understandings of the concept of 'voluntary liberalization'. The Ministerial Meeting in November 1998 decided to leave the initiative in the hands of the WTO as the 'Accelerated Tariff Liberalization' (ATL) initiative (Okamoto 2004b: 54). The Australian government, along with others like New Zealand, promoted the ATL as a serious agenda item in a new WTO round, but could not gain uniform support from other APEC members. Worse still, while the APEC Leaders and Ministerial Meetings in September 1999 managed to support the launch of a new round, the WTO Ministerial Conference in Seattle two months later turned out to be a mess and failed to launch a new round. As a result, the ATL was forgotten altogether.

In 1998, as the EVSL initiative was heading towards failure, some states in the Asia Pacific region began to move towards bilateral FTAs. In September, New Zealand commenced formal FTA negotiations with Singapore. In December, Japan and Korea, which traditionally favoured multilateralism in trade liberalization and had not been involved in any FTAs before, agreed to start a study on a bilateral FTA at the semi-governmental level. Japan also began similar studies

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<sup>52</sup> Interview with the Director of Trade and International Affairs, ACCI (29 August 2002) and the Executive Director of the AIG (5 September 2002).



with Mexico and Singapore in early 1999 and early 2000 respectively. The United States' intention to create the Free Trade Area of the Americas (FTAA) was clearly stated at the inaugural Summit of the Americas in December 1994. The US drive for the FTAA intensified after the second Summit in Santiago in April 1998 and a draft text for the FTAA was released after the third Summit in Quebec in April 2001. Its negotiation deadline was set for the end of 2004.

Watching its important trade partners' drive for FTAs with other economies, the Australian government must have felt frustrated. What came at this very timing in 1999 was an ASEAN proposal to study the feasibility of an FTA between ASEAN and CER. At the AFTA-CER Ministerial Consultations in Singapore in October 1999, ASEAN proposed to set up a task force to study the feasibility of establishing an AFTA-CER FTA by 2010. A year later, despite the task force's strong recommendation to start negotiations for the FTA immediately, the Ministerial Consultations held in Chiang Mai in October 2000 effectively shelved the initiative indefinitely. At this stage, the Australian government finally decided to take the first step towards bilateral FTAs. The government felt it was already late in taking part in this FTA 'race' and needed to catch up.<sup>53</sup> Just one month after the AFTA-CER Ministerial Consultations that put off an AFTA-CER FTA indefinitely, Prime Minister Howard announced an agreement to start bilateral FTA negotiations with Singapore.

Parts of domestic industries have started accepting this government-initiated 'optional bilateralist' approach for foreign economic policy cautiously, though most of them preferred multilateral liberalisation or regional liberalisation. The Executive Director of the AIG supported the government's argument saying that the main objective of bilateral FTAs was to keep Australian exporters from disadvantageous treatment by trading partners that pursue FTAs with others, and not so much to seek preferential treatment. His emphasis was placed on the point that Australian business was ready to compete with other economies in overseas markets under equal conditions.<sup>54</sup> Growth of support for optional bilateralism by the private sector became more obvious when negotiations for a bilateral FTA with the United States became a real possibility in 2001. A single-issue, inter-industry lobbying group called the 'Australia United States Free Trade Agreement Business Group' was formed in September 2001, consisting of some large industry organisations such as the BCA, the AIG, the Australian Chamber of Commerce and Industry (ACCI) and some of the biggest companies in Australia including News Limited, Telstra Corporation, IBM and BHP Steel. In addition, the NFF, one of

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<sup>53</sup> Interview with officials of the Trade Development Division (30 August 2002) and the Economic Analytical Unit (2 September 2002) in DFAT.

<sup>54</sup> Interview, 5 September 2002.

the strongest advocates of global free trade in Australia, also decided to accept bilateral FTAs as long as agriculture remained at the heart of deals.

By the end of 2005, the Australian government has concluded FTA negotiations with Singapore, Thailand and the United States and all of these FTAs have already come into effect. The government is now negotiating FTAs with China, Malaysia and ASEAN as a whole. It can be seen that the optional bilateralist coalition in the foreign policy issue area has now emerged as a strong force.

## **Conclusion**

From federation in 1901 to the 1960s, a protectionist coalition had dominated Australia's foreign economic policy. Protection and financial and other assistance provided to industries by successive governments covered almost all sectors. Manufacturing industries enjoyed import barriers through high tariffs and quantitative controls, while rural industries received a variety of financial and other assistance. After World War II, economists consistently raised the opposition against protectionism in the context of its resource misallocation and resultant inefficiency in the whole economic activity. The voice gathered momentum in the latter half of the 1960s when the Tariff Board began a series of reviews of Australia's tariff structure, but the protectionist coalition's core beliefs and policy preferences were hard to change after such a long time in domination.

The mineral resource boom of the early 1970s gave an opportunity for the government to reconsider effects of 'protection all round'. Agricultural exports' relative decline as main sources of foreign currency earnings made it easier for the government to aim for restructuring agricultural industry through the implementation of a rural reconstruction scheme. At the same time, the massive balance of payment surplus created by the mineral resource boom caused strong inflationary pressure on the economy. To increase imports to solve the problem, the Whitlam Labor government, which won the general election at the end of 1972, decided to cut all tariffs by 25 per cent in 1973. Though the direct aim for the 25 per cent tariff cut was not to reduce the level of manufacturing protection, it marked one of the initial attempts for liberalisation and deregulation. This could be done because the Whitlam government did not have its support base in the traditional protectionist coalition. On the other hand, an alternative coalition to the protectionist one had not grown to support liberalisation strongly enough. A worldwide recession soon followed the first oil crisis in 1972. The 25 per cent tariff cut, along with the government's expenditure expansion on social and welfare programs, aggravated the

situation in Australia. Because it did not have firm support bases, the Whitlam government lost the general election of 1975 and the Liberal/National (Country) parties returned to power.

Though the Fraser Liberal/National government was protectionist in principle, the international economic environment and domestic opposition did not allow it to return to the protectionism of previous decades. The 1970s were a period of policy oriented learning for the protectionist coalition and the steady growth of a trade liberaliser coalition. As a result, the Fraser government and protectionist coalition had to make policy compromises. Thus, while levels of protection for sensitive industries of the TCF and PMV were significantly increased in the latter half of the 1970s, those for other industries gradually reduced. By the early 1980s, after the reorganisation of industry organisations, the trade liberaliser coalition was firmly established and ready to take over the dominance of protectionists.

A massive deterioration of terms of trade in the early 1980s provided the trigger for a decisive foreign policy change. With the incoming of the Hawke Labor government in 1983, the trade liberalisers finally became dominant. The government first introduced liberalisation and deregulation of the domestic financial sector, then a significant voluntary tariff phase down followed in the late 1980s. As the domestic economic reform had to be underpinned by a favourable international economic environment, the government sought to maintain and promote a multilateral trade system, namely the GATT. To do this, the government targeted the Asia Pacific region, especially East Asia, as a springboard. The trade liberalisers had become Asia Pacific regionalist at the same time.

The Howard Liberal/National government returned to office in 1996, after thirteen years in opposition, with more inward looking, short-term oriented policy preferences in foreign economic policy than the previous government. The government could not return to the protectionism of old, because the liberalisation and deregulation of the economy in the 1980s and 1990s was too extensive to turn back. The Howard government's short-term oriented preferences were reflected in its push for bilateral FTAs. Initially, societal interest groups did not have much interest in the government initiated FTA move, but by the turn of the century when all multilateral and regional liberalisation initiatives that could benefit the Australian economy died down, industrial organisations began to accept bilateral FTAs as options. As an FTA with the United States became a possibility in 2001, the optional bilateralist coalition visibly emerged. By the end of 2005, the optional bilateralists seemed to have taken control of Australia's foreign economic policy subsystem.

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