HOUSE OF COMMONS

International Trade Committee

Oral evidence: UK-US Trade Relations, HC 481vi

Wednesday 28 February 2018

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Watch the meeting

Members present: Angus Brendan MacNeil (Chair); Mr Nigel Evans; Mr Marcus Fysh; Mr Ranil Jayawardena; Mr Chris Leslie; Julia Lopez; Stephanie Peacock; Faisal Rashid; Catherine West; Matt Western.

Questions 310-354

Witnesses

I: His Excellency the Hon Alexander Downer AC, Australian High Commissioner to the UK

Examination of witness

Witness: Alexander Downer.

Q310 **Chair:** Good morning and welcome to this meeting of the International Trade Committee, where we have the Australian High Commissioner. Could you please introduce yourself for the record?

Alexander Downer: I'm Alexander Downer, the High Commissioner of Australia to the United Kingdom.

Q311 **Chair:** Thank you. You have the opportunity to make a brief statement if you would like, or we can go on to questions.

Alexander Downer: You are welcome to go pretty much straight to questions. I will say, by way of introduction, that since the 1980s Australia has been very committed to the trade liberalisation paradigm that has been strongly supported by both the major political parties that have formed Government during that period—the Labor party and the Liberal party, which is more or less the Australian equivalent of the Conservative party here. So this has had widespread political support. It has not always had widespread public support. There have been reservations about the trade liberalisation agenda, in particular among people working in industries that have been directly affected by reductions in tariffs and quotas over the years.

Nevertheless, our experience has been that the overall economic impact has been extremely positive. It is one of the reasons why we have had a constant process of microeconomic reform in Australia. Companies have to readjust to changes in the international marketplace and investment flows to the more efficient sectors and away from the less efficient sectors. This has helped to keep unemployment low and it has helped to maintain steady rates of economic growth. Australia has had over 26 years of continuous economic growth without a recession, and at this stage we are confident that will continue. We attribute opening our market to the outside world as being an important contributory factor to that successful economic performance.

Q312 **Chair:** Was any adjustment made within Australian society or the Australian political system to help the losers, in the short term, of those agreements with their fiscal transfers? What was the deal? When the country gained overall, individual actors were losing in the economy. What was done on that?

Alexander Downer: Both the Federal Government and state Governments in the states directly affected by the adjustment process have provided financial support, and have sometimes directly provided retraining programmes, for workers affected by businesses closing. How effective those schemes have been might be debatable. I come from Adelaide in South Australia. One of the economic drivers of the South Australian economy has been the automotive industry. At one stage, we had two major automotive manufacturers there: Mitsubishi and General Motors Holden. As a result of, you could say, reducing tariff protection, but also as a result of a lack of sufficient productivity and poor model choices by those manufacturers, both of those businesses have closed in South Australia.

There have been retraining programmes for some of those workers, though to tell you the truth, older workers in that industry retired and younger workers found it relatively easy, in most cases, to find alternative employment. So the overall level of unemployment in South Australia, even though the automotive industry has completely shut down there—the last car built in South Australia was built in November last year—is still pretty low.

Q313 **Chair:** So when you say that there has been 26 years of continuous economic growth, has that been 26 years of continuous economic growth in each state, province or territory—however you define it?

Alexander Downer: I'll have to check that. In South Australia and Tasmania there might have been two consecutive quarters of negative growth. It is possible. In Western Australia after the mining boom ended they certainly had one, and might have had two, quarters of negative growth. I couldn't tell you for every state, but it is true that in some states there have been downturns, owing typically to vagaries in the international marketplace, but it has varied.

Q314 **Chair:** A final question from me on Australia's mechanisms. Does that mean there has been any fiscal extra from the Federal Government to states, provinces or territories that have felt any heat from those economic changes?

Alexander Downer: The short answer is no. There is a Commonwealth Grants Commission, which allocates grants to the state Governments based on a formula, which is a bit like the formula you use here for the Governments of Scotland, Wales and Northern Ireland—it is a somewhat similar mechanism. Most of the money that is distributed by the Commonwealth Grants Commission—the Commonwealth is not to be confused with the Commonwealth of Nations; the Commonwealth of Australia is the name of the country, so the Federal Government is often referred to as the Commonwealth Government.

Above all, the Commonwealth Grants Commission allocates the VAT revenue to the states. The VAT is collected nationwide and it is a state tax in the sense that all the revenue from the VAT, which we call GST, is redistributed to the states according to a formula. A state such as mine, South Australia, is a poorer state, so it gets a proportionally higher share of the GST revenue than—a particularly controversial issue—the state of Western Australia, which has benefited from the huge mining sector and gets a much lower proportion of GST revenues than, I think I am right in saying, any other state. That is how it works.

That is a simple answer. In reality, the Federal Government have allocated work to states or parts of states—not necessarily whole states—that are struggling. For example, the naval shipbuilding programme has been more and more concentrated into South Australia as it has struggled, as I mentioned earlier, with the closure of its automotive industry and a substantial restructuring. From the second world war to the 2000s, South Australia was very much a manufacturing state, and that manufacturing has pretty much gone, so naval shipbuilding has been a big focus in South Australia.

Q315 **Matt Western:** I want to pick up on that point, which is of interest. You said that there has perhaps been some public resistance to the reduction of tariff barriers and so on, which had seen the closure of two car plants, and you finished by saying that South Australia has gone through a tougher time since the 2000s. Are you aware of average incomes in South Australia having fallen, pro rata, compared with other states as a result of those closures?

Alexander Downer: Not necessarily as a result of those closures—that would be very hard to establish—but for many years, South Australia's per capita GDP has been lower than that of most other states, with the exception of Tasmania.

There are all sorts of factors at play. South Australia became heavily dependent on subsidised manufacturing. By subsidised I mean that a substantial part of the subsidy came through tariff protection, quotas—which we had as well—and very high tariffs. As a result, those protected industries did not sufficiently invest or modernise, because they could survive without doing so.

Even before the tariffs all started coming down in the 1980s, those industries were really starting to struggle. At that stage, the Federal

Government were not only into providing tariffs and quota protection, but some direct financial support. In more recent years, the Federal Government have provided direct financial support to the automotive industry to no avail—it does not seem to have worked; they did not build cars at the right price that people wanted.

Per capita GDP would be lower in South Australia than other parts of Australia. It would be lower in Tasmania, which has never had a manufacturing sector. There are all sorts of other factors at play in Tasmania.

Q316 **Matt Western:** So the point is that it was already low. It has not deteriorated relatively since the early 2000s.

Alexander Downer: Well, South Australia has suffered from some other factors as well, which are more controversial. As a civil servant, I dare not weigh into the political controversies, but there is controversy over energy policies in South Australia and relatively high energy prices—that is an unrelated issue to do with the international marketplace.

Q317 **Chair:** Specifically on the matter at hand, the US-Australia free trade agreement, what were the major achievements of the agreement, and which sectors were predicted to benefit most from the agreement? Which sectors did Australia and the US seek to protect in the agreement and why?

Alexander Downer: Effectively, we did not seek to protect any sectors. To borrow an expression your Prime Minister likes to use, free trade means free trade. We were pretty much open to American exports coming into Australia duty-free full stop. We were not aiming to—

Q318 **Chair:** Was that a mistake?

Alexander Downer: No, it has worked a treat. I am happy to explain why this is a huge success. The Americans wanted to protect a small number of agricultural industries. In most cases there is a phasing down of tariff protection or quota protection in those industries, such as the beef industry and the dairy industry. The one industry that the Americans refused to provide us any additional access to was the sugar industry, which they explained to us at the time was extremely sensitive politically and while there might have been a good case for us exporting more sugar to the United States, they were not up for it, because if they were to do that, they would never get the free trade agreement ratified by the Senate. We gave up on that, in truth. I think I am right in saying that 94% of our exports to the United States are completely duty-free and 100% of their exports go into Australia completely duty-free.

We have not tried to protect our agricultural industries from United States agriculture, and our agricultural industries have thrived all the same, because they have found export markets in the United States. Despite the fact that the United States is a huge producer of beef, it is one of our largest beef markets, because we have a niche for minced beef. I must be careful, because this is on the record—I was going to say “low-quality”, but I do not think I will concede that point. We produce relatively cheap minced beef, which is used by McDonald’s hamburger stores. It is a huge market for us.

Because you are in the UK, you will be interested in services. We have been committed to opening up our services market to the Americans and we have not done badly in terms of improving our access to the United States services market as well.

Q319 **Julia Lopez:** As we are on services, did you have trouble trying to penetrate state-level service contracts? That is something we discussed when we were in the United States. We might be able to negotiate with the Federal Government, but at state level, how do you get access to those Government contracts?

Alexander Downer: By the way, it is the same with Australia. The Federal Government in Australia cannot commit the state Governments to having open contracting. Nevertheless—I stand to be corrected—over 30 states provide us with access to their contracting system. I think it is 32 states. Our states provide the United States with access to ours as well. The American Federal Government spoke to the States and tried to help us with the States. I suppose that the States did not see Australia as hugely threatening in that area. Obviously, from the point of view of a state Government, if they can make purchases more cheaply from somewhere else, that saves money, which they can spend on something else. So it is quite an attractive proposition for them.

Q320 **Julia Lopez:** You concluded the agreement with the US in 11 months.

Alexander Downer: Fifteen months.

Julia Lopez: Sorry, 15 months. Why did you chose to negotiate so quickly, and should the UK aspire to do that or should we take a little longer to get the right agreement?

Alexander Downer: I cannot find my way through the folder here, but I have a list of how long our free trade agreements have taken to negotiate, so I can tell you various others. There is no particular pattern, because sometimes the negotiations get bogged down and in some cases the Government of Australia changed, and different Governments have different attitudes to these negotiations, so that has led to delays as well.

In the case of the United States, both the Australian Government at the time and the United States Government were very keen to conclude a free trade agreement. We in Australia had pressed George W. Bush very hard for a free trade agreement. He was up for free trade; he said that he was happy to do that. So the political context was that both Governments wanted to make the agreement and wanted to make it as soon as they could. What can delay negotiations is if one side wants to continue to protect particular areas. The more you want to protect, the more your interlocutor will want quid pro quos, and the negotiations can become complex and protracted on that basis.

Our basic view was—it is hard to persuade the public of the economics of this, but it is definitely true—that if we open up the Australian market to American imports, we will be able to buy things more cheaply than we would otherwise be able to do. That will contribute to improving people's living standards and will not only be good for America, I am sure, but very good for Australia. So we did not want to keep out any American imports. We were happy to have them, if they could sell things to us more competitively than we could produce them ourselves. I know that is a bit counterintuitive for a lot of people, but that turns out to be not only good for the macro economy but particularly beneficial to low-income people.

For example, if we can buy motor vehicles from the United States more cheaply, it means that motor vehicles are more available to lower-income people. If we can buy textiles, clothing and footwear more cheaply, the people who benefit the most from that are lower-income people. It is actually highly regressive to have tariffs and protection. Call this controversial, but we like to put the interests of the consumer before the narrow and selfish interests of producers who have access to the media.

Chair: Controversial!

Alexander Downer: Our attitude meant that for the Americans, Australia was not much of a problem. It was much more us going to the Americans and saying, "Do you have to be so difficult on dairy? Do you have to be so difficult on beef?" They agreed to phasing arrangements because they thought, more politically than in reality, that it would be difficult suddenly to allow Australia full access to their beef market, their dairy market or whatever. So we agreed to phasing arrangements, which are still in place.

Q321 **Julia Lopez:** Were animal welfare issues ever a big political issue in Australia when you were doing the FTA?

Alexander Downer: Of course. All these standards have to be reconciled. We do not adopt American standards, and America is not just going to adopt Australian standards.

There are two things to say about that. The standards are not necessarily all that different. I know that there is a view here that America has very low food safety standards and so on. That is not our experience. I do not think that they are as different from food safety standards that you might have here or in the European Union as you might imagine. Obviously, when we export anything to the United States, we have to meet American standards, and if they export anything to Australia, they have to meet our standards. So the free trade agreement did not mean that we would just abandon our standards.

There were some controversial questions there. Standards have to be supported by science; that is what the WTO says. So if we have particular standards for beef—typically quarantine standards—we have to be able to defend them scientifically. Otherwise they just become another form of protectionism and would be contrary to the spirit, let alone the letter, of a free trade agreement. With the Americans we were able to resolve these issues. I would not say that was without any difficulty, but we were able to resolve them.

Q322 **Julia Lopez:** The Australian Senate Select Committee report expressed concern about "the lack of adequate research being undertaken prior to Australia committing itself to trade agreements." How would you respond to that criticism?

Alexander Downer: Do you mean lack of research on the cost-benefits of a free trade agreement?

Julia Lopez: Yes.

Alexander Downer: We did actually do some work. The Centre for International Economics, I seem to recall, did some work on the likely benefits of a free trade agreement, and showed it would have a positive effect—it would add 0.5% of GDP over 10 years or something like that. These are just illustrative figures, really. They are nothing more than that, because they are based on certain assumptions. I cannot remember for the life of me what assumptions the Centre for International Economics report was based on, now—it was a long time ago—but they are based on certain assumptions.

One of the weaknesses of any of the assumptions of these economic models is that they are static models. They do not take into consideration what changes of policy the Government might make as a result of the free trade agreement coming into force; but, even so, this one study done on the macroeconomic impact of a free trade agreement with the United States found it to be very positive—and it has been, let me assure you, extraordinarily positive. It has led to what could only be described as a huge increase in the investment relationship. Our investment relationship with the United States has grown by 130% since the free trade agreement came into force, and our trade relationship has grown by, I think, around 50%. So it has been hugely beneficial to the Australian economy. The American economy is 15 times larger than the Australian economy, but it has been beneficial to the American economy as well.

Q323 **Catherine West:** I have a question about defence, Alexander, because obviously that is one of the areas that, I think, the UK has put on the table for a number of years with the US, through the EU and so on, but has never managed to have a good conversation about that. I am wondering what the Australian experience is, and if you do those sorts of exports.

Alexander Downer: Defence is a separate thing altogether, in the main, from free trade agreements. We buy a huge amount of American defence equipment; they can't complain. We are in the joint fight striker programme, for example, as you are, right at the moment, and you can imagine the benefit to the United States from our participation in that.

As you would well know, we have the ANZUS alliance with the United States. It has the same sort of obligations as NATO has with the United States. We do not have obligations to buy American defence equipment, and they certainly do not have obligations to buy our defence equipment. We are a fairly poor exporter of defence equipment anyway, and that is not written into the free trade agreement. Nevertheless, they are buying some Australian defence equipment. For example, some vessels for the navy are Australian. They are actually manufactured in the United States but they are Australian vessels and built by an Australian company, so we do have some defence exports there—but it is not a component of the free trade agreement.

Q324 **Catherine West:** Traditionally they are quite aggressive on that, aren't they?

Alexander Downer: Well, the WTO takes this into account: there can be national security considerations. Most countries will take the view that when it comes to their defence industries they want to have some indigenous industries. So even though one could make a very clear argument that it costs you substantially, particularly for Australia—this may or may not be true for the UK, but it is certainly true for Australia that it often costs us more to build ships or submarines, or whatever it may be, in Australia than to just buy them off the shelf; that is pretty much for sure—we do it so that we can have complete control of the project and better capacity to manage the through-life programmes for that equipment. We pay a premium for it in many cases; at the moment we are spending $50 billion on a submarine programme with French-designed submarines. There is no doubt that it would be cheaper for us to just buy the submarines off the shelf and have them built in France, but we are having them built in Adelaide. We want the industry to be indigenous, for national security reasons.

Q325 **Matt Western:** I was struck by the figure that you cited of 130% for growth in investment, compared with 50% growth in trade. Is that in particular sectors? Could you elaborate briefly?

Alexander Downer: Investment from the United States is the largest source—something like 27%—of foreign investment in Australia. They are big investors in services, particularly financial services; in the resources sector; and in agriculture. They have been very big investors in manufacturing. I mentioned earlier that in Adelaide we had the Holden factory, which was owned by General Motors; they are now investing just in distribution in Australia for General Motors parts. It is pretty much across the board.

This is one of the things that is difficult to model. If you have a free trade agreement with a country, it psychologically affects the attitude of businesses to that country. There is a sort of notion—albeit an exaggerated notion—of a single economy. Certainly Australian investors have proved to be more willing to go and invest in the United States since the free trade agreement, and their investors are more willing to come and invest in Australia—even though it might be difficult to point to obstacles that they had before the agreement.

There was one particular obstacle. We have something you do not have, which is called the Foreign Investment Review Board. All foreign investments in Australia of more than $250 million have to be approved by the Treasurer—our equivalent of the Chancellor of the Exchequer—on the board’s advice. In the case of countries with which we have a free trade agreement, such as the United States, that threshold is typically lifted to $1 billion. That means that they can invest up to $1 billion without having to get any approvals from the Australian Government. Again, the approvals are invariably given—not universally, but invariably. But it is a bureaucratic process to go through—a psychological obstacle more than anything else. When you take that away, you are kind of opening the door to investment.

These are hard things to prove or model, but the fact that we have created that economic relationship with the United States seems to have been a substantial stimulating factor to investment flows between our countries.

Q326 **Faisal Rashid:** Thank you very much for coming, High Commissioner; your input is very valuable and useful.

What is the role of the Australian Parliament in the trade deal process, including the scoping, ratification and negotiating stages?

Alexander Downer: The Australian Parliament has had a Joint Standing Committee on Treaties since the late 1990s—I established it myself, by the way. It is a Joint Committee because it includes both Houses: the Senate and the House of Representatives. Before ratification of treaties, they have to be tabled with the Committee, which holds public hearings and—in certain circumstances—hearings in camera. NGOs, civil society, Government Departments and so on, go before the Committee, which produces a recommendation to the Federal Government on ratification of the treaty. This has happened with just about all the treaties or treaty-status documents that we have negotiated with other countries since—I think it was established in about 1998; it was ’97 or ’98. That is the main role that the Parliament has in what you might call the ratification process. Our ratification processes are the same as yours. The Queen, or the Governor-General in the name of the Queen, technically speaking, ratifies a treaty. That means the Executive decides on the ratification or non-ratification of a treaty.

The other thing to say about that, though, is that many agreements—trade agreements are particularly germane to this—require legislative change. If you enter into a trade agreement with another country, you might have to change some of your tariff rates for that particular country, and that requires legislation. All that legislation goes through the Parliament. When it came to the Australia-US free trade agreement, which is the one we are focusing on, that agreement did not have to be ratified as a treaty, but legislative changes, incorporated in a Bill, had to go through Parliament.

There was some controversy about that at the time. The Labor party was in opposition in those days and raised reservations about—I think these were not opposed in the end—some aspects of the free trade agreement, particularly in relation to pharmaceuticals and intellectual property. If memory serves me well—I'm doing this from memory—it had some concerns. We have what is called the pharmaceutical benefits scheme, whereby the Government subsidises public access to pharmaceuticals—a bit like the system you have here. There was a question about the extent to which, under the intellectual property provisions of the free trade agreement, the Australian pharmaceutical benefits scheme would have access to generic drugs rather than branded drugs. That was resolved to people's satisfaction, but I am just making the point that the Parliament was certainly very involved, and of course the Parliament is very involved in the political process. Question Time is conducted slightly differently in Australia from here. Ministers are constantly being required to answer questions, and the Prime Minister as well, in dealing with these issues.

Q327 **Faisal Rashid:** There was a report from the Senate Select Committee on the Australia-US FTA, and they concluded that there was "insufficient consultation and community involvement in the treaty-making process and inadequate opportunities for parliamentary scrutiny". How has Australia's approach to these issues evolved, and what lessons can the UK learn from this?

Alexander Downer: The Government doesn't have a majority in the Senate; that is one thing I should explain. Does that help to explain the Senate Committee report? You're all politicians. *[Laughter.]* In the Government of the day I was the Foreign Minister at the time, so I am entirely familiar with this period. In 2004, I guess—yes, leading up to the 2004 federal election—the free trade agreement with the United States was a third or fourth-order issue.

Everything needs to be understood in its context. The context here was that this was in the wake of the Iraq war, the invasion of Iraq, in 2003. This had been a pretty vigorously debated issue in Australia, as it obviously was here. It played into the 2004 election year environment, and so did the free trade agreement with the United States. There was some partisan bickering, some partisan warfare, on this issue. I would say that the Parliament was pretty extensively consulted, but it sounds to me, going by my recollection, as though no amount of consultation was ever going to be enough.

Chair: I will now turn to Ranil Jayawardena and remind everybody of time. Time is always the enemy of Committees, so can we have briefer questions and briefer answers, please?

Mr Jayawardena: So long as the High Commissioner is willing to answer, I am delighted—

Alexander Downer: I try to answer questions.

Q328 **Mr Jayawardena:** I am delighted to keep going all morning, if the High Commissioner is willing to answer.

I am delighted that you are here. It is great to have your expertise, as someone who has done an FTA. On a visit to London, your Foreign Minister said that Australia is very keen to pursue negotiations for an FTA with the United Kingdom. She thought that that would be precluded if the United Kingdom were to join the customs union. Your Prime Minister has said that Australia is ready to enter into a free trade agreement with the United Kingdom as soon as we are able to do so. Given that Australia wants a trade deal with us, that President Trump also wants a UK-US trade deal for the future and that we want to do trade deals with countries such as Australia, do you agree that the Labour party's position of wanting to remain in a customs union—in other words, of ruling out a free trade agreement with the US, Australia and other markets—would be a betrayal of our friends and UK consumers? It supports a position that rejects ambition and rules out FTAs.

Chair: Not that you're being led anywhere.

Alexander Downer: Not that I am a career diplomat and I cannot see where that question is coming from. I am not going to get involved in a partisan debate. We would say to you that whether you want to stay in a customs union with the EU, or you want to leave, is something you must debate among yourselves. If you remain in the EU customs union, obviously we will not be negotiating with you, but with Brussels. We have begun that process of negotiating a free trade agreement with the EU—we began it quite a long time ago—and we would like to conclude an agreement with the EU. Obviously you would not be involved in that. As they like to say, you would be rule takers.

At the moment, in the context of the Australia-EU FTA, London has been one of our first ports of call, because you are part of the EU and part of the decision-making process. You have people in the Commission but, more importantly, you are part of the European Council's decision-making process. When you leave the EU, you will not be, obviously, and what is more, if you remain in the customs union, the Council will still be there but you will not be part of it.

Mr Leslie: If we leave.

Alexander Downer: If you leave the EU. Well, you say you are leaving the EU and your public say you are leaving the EU. I am just a simple dairy farmer's son from the Adelaide hills, so I don't know. That you were not leaving the EU would be confusing even for me.

Chair: Can I ask Ranil for the next leading question?

Q329 **Mr Jayawardena:** Thank you, Chairman. I am delighted you are opening up to my way of thinking. High Commissioner—

Alexander Downer: We will negotiate with Brussels, but you will not be part of those negotiations, as I understand it.

Chair: That is a very powerful message.

Mr Jayawardena: Yes, a very powerful message against remaining in the customs union. High Commissioner, I think it was last weekend on "Westminster Hour" that you said that it is up to us, but that "Australia would never contract out its trade policy or the regulations for the management of its internal economy." Given what you have just said, that if we were in a customs union with the EU they would decide trade policy and we would not have a seat at the table, do you stand by those comments? What do you think we can learn from the recent comments on trade policy made by your Prime Minister, who said, "We move quickly…Australians are fleet of foot, we don't muck around"?

Alexander Downer: We are intensely practical people, first, which is how we have been able to conclude free trade agreements relatively swiftly with a range of different countries. We have an approach to trade that I hope I have described reasonably clearly—a free trade approach. We are easy to negotiate with. People say that Australians are tough negotiators and so on, but, in a sense, we are very easy to negotiate with because you are welcome to flog your Jaguars, Range Rovers, Bentleys, whisky or whatever it is—whisky? *[Laughter]* That's your constituency, Mr Chairman. I was in Scotland the other day and it was pouring with rain, and a Scotsman said to me, "It's rain today, but it'll be whisky tomorrow!" That is apropos of absolutely nothing to do with your question—I just thought it was funny.

The point I would make, secondly, is that Australia—as a sovereign country—would not contract out our trade policy to the Association of Southeast Asian Nations or to the East Asia Summit. The public in Australia would absolutely insist they had a say if we were starting to pull down tariffs and so on.

If we contracted out our trade policy to someone else, and through a trade agreement they reduced tariffs from, say, Russia, and people in some industry in northern New South Wales were upset about that, we would have to tell them, "It doesn't matter who you vote for at the next election, that's decided by someone else." It's nothing to do with the UK—you can do what you like here. But in Australia, this just wouldn't happen. Try and tell the Australian punters that—good luck with that.

Q330 **Mr Jayawardena:** I am so pleased that there is a plethora of sources to look at, High Commissioner. In your article in *The Sun* two weeks ago, you mentioned that in the '80s, when Britain first went into the European Community, as it was at the time, it was, as I understand it, when your father was High Commissioner here in London. And Australia put up barriers and tariffs, thinking that they would protect your businesses, but the policy did not help anyone. Your consumers had to pay more.

In that thinking—and you have demonstrated just in your last answer that Australia now is a free-trading country that wants to build relationships with the world—what economic modelling produced during the FTA negotiations was taken on board? And what role do you think such modelling would have in our considering whether we should enter into FTA negotiations on a whole range of industries or on specific sectors?

Alexander Downer: Economic modelling is one thing, and economic models depend on the assumptions that you make. We do some economic modelling. I mentioned that with the Australia-US free trade agreement we got the Centre for International Economics to do some modelling. Modelling has been done from time to time—often, models disagree with each other on different trade agreements. I can't recall off the top of my head economic modelling that was done in relation to the free trade agreement we have with China, but surely some of it was done.

I think there is a bigger point—in the end economic models are static, but it is very hard to make assumptions about changes in behaviour. If you assume behaviour is static—sort of ceteris paribus assumptions—then the economic model is not going to turn out to be particularly valuable.

You either have an instinct for these things or you don't. Our Secretary to the Treasury uses the term, "an intuitive economist". Do you think that reducing tariff protection is going to be good for microeconomic reform, more efficient flows of investment in your economy and reducing costs for low and middle-income people? You can model it and make some assumptions in your model, but we would say, over and above economic models, "We reckon that's gonna work". And what's more, our experience is that that really has worked incredibly well for us.

So, you're in the EU. In the EU, you have an average of something like 17% tariff protection on footwear imported into the EU. We used to have that kind of thing. And that means poor people are paying a hell of a lot more for their shoes, because they will be importing their shoes mainly or substantially from Asia; certainly in the case of Australia, we do that.

Q331 **Chair:** What about shoes that might come from Russia, because you said you have high tariffs on Russia?

Alexander Downer: We don't. No, I was just using that as a hypothetical example. We import almost nothing from Russia, by the way; maybe a little bit of vodka. *[Laughter.]* We have very low tariffs—

Q332 **Chair:** Where do you have high tariffs? Who do you have high tariffs with—?

Alexander Downer: We don't.

Q333 **Chair:** With nobody?

Alexander Downer: We don't have high tariffs full-stop.

Q334 **Chair:** So anybody at all can export into Australia?

Alexander Downer: We have tariffs, but our tariffs are relatively low, compared to the rest of the world. Our average level of tariff protection is about 5%, I think; it might be slightly less than that. Something like 4%. For example, for textiles, clothing and footwear, it's nothing like 17%.

This is what we have learned. Of course we have a footwear industry in Australia. It is a high-quality footwear industry—a lot of people are familiar with R.M. Williams boots and that kind of thing. They are expensive. They are top end. For footwear for low-income people and cheaper footwear, that is almost all imported. We import it more cheaply than we would have otherwise done.

Q335 **Mr Jayawardena:** I'm taking away from this that tariffs are bad, free trade is good and models are models.

Alexander Downer: That's pretty well summed up. You can produce models to prove your argument, whatever argument you want to prove, in our experience.

Mr Jayawardena: Exactly.

Alexander Downer: Believe me, in Government, we certainly talked about producing models to—

Chair: If they don't prove your argument, you keep them secret.

Alexander Downer: That's right.

Q336 **Mr Jayawardena:** We can simply ask economists for another opinion.

I would like to ask a qualitative question. What lessons can the UK learn from Australia's experience with the US? What is the best way that we might want to approach it, given that we are a different economy, but taking on board your insight in this sector?

Alexander Downer: When we negotiated the free trade agreement with the United States, there was quite a lot of debate in Australia, as I mentioned earlier, about whether it was a good or a bad thing. The American economy is—don't hold me to this—around 15 times the size of the Australian economy, and the Australian economy is slightly more than half the size of the UK economy, so you know how big the American economy is. Some people argued that they were so huge and we were so much smaller that they would just overwhelm us. In our experience, we just haven't found that.

However, all free trade negotiations depend on one thing. They don't really depend on resolving difficult technical questions as much as they do on political will. If the political leadership really wants a free trade agreement, it will happen quite easily. If the political leadership is uncertain about the merits or otherwise, it could be quite a problem and they can be very protracted.

Q337 **Mr Fysh:** In terms of the expectation for the free trade agreement with the US and what the outturn has actually been, what is the order of magnitude to which that free trade agreement has benefited the Australian economy? Is it more or less than people had been saying at the time?

Alexander Downer: It depends who you ask. If you ask the people who were in Government at the time, such as the then Prime Minister, the then Treasurer, the then Foreign Minister—I am the third of those—it has exceeded our expectations. The free trade agreement with the United States has been really great for us. It has worked incredibly well.

Q338 **Chair:** As a percentage of GDP, what do you think it is worth?

Alexander Downer: I'd have to calculate that. I couldn't say. Our largest trading partner is China. You have focused on the free trade agreement with the United States. We have a free trade agreement with China: 93% or 94% of our exports go to China duty-free, and just about all their exports to Australia come in duty-free as well. We have a similar, not identical, agreement with China. I have to tell you that these free trade agreements have been fantastic for us, with a huge boom in our exports to China. These trade agreements have mainly exceeded expectations.

Q339 **Matt Western:** High Commissoner, you have been very positive and expansive on the benefits of the Australia-US free trade agreement, but there have been some commentators, such as ACIL and a professor at the Australian National University, speaking out and saying that this has come at some cost in terms of reducing or diverting trade with the rest of the world. There is a figure of $53 billion lost to other countries. Does that matter to Australia and is the figure correct?

Alexander Downer: I couldn't possibly comment on a figure. You hear this debate less now than you once did. In the mid-1990s there was quite a substantial debate in Australia about the question of trade diversion. We had obviously been hoping that the Doha round would—it sounds a bit glib, but this was the thinking behind it—turn the whole world into a free trade area: a wonderful Elysian vision. We also, being very practical people, realised that was not going to happen. Increasingly, the Doha round has just got bogged down. So the question for us was, "What are we going to do in terms of trade policy? How are we going to get better access to markets and get more stuff more cheaply into the Australian economy?"

We had Cabinet discussions about this and we decided that even though free trade agreements—you have that with the EU, of course: a huge diversion. Some 7% of your exports used to go to Australia in 1960, but I reckon it would be 1% or 2% of your exports now. That is called trade diversion: you have diverted into the EU. Even though these trade agreements do have some diversionary effect for sure, the net benefit is still very substantial. We are better off with a sub-optimal free trade agreement, in terms of there being some diversionary effect, than we would be without it. That is because we are still getting better access to markets than we had without the trade agreement, although we concede that we would ultimately be better off if we had completely free trade with everybody in the world. But I do not know whether that is ever achievable.

The free trade agreement with China that I mentioned—these trade agreements have phasing in them—comes into full implementation in 2029. By then, 99.9% of Australia's resources, energy and manufactured exports will be duty-free into China. I just mention that in relation to China since you have focused on the United States.

Yes, there is some diversionary effect, but nevertheless we are net better off with those agreements than without them.

Q340 **Matt Western:** Could I just follow up with a second question? How could the UK address the potential for trade diversion in its trade negotiations with both the EU and the US?

Alexander Downer: You are asking me to comment on the UK, but I am very cautious just to be commenting on my own country. You already have one huge diversion of trade towards the EU because you have a single market and customs union with the EU. That is diverting trade away from the US, China, Japan and so on. It is up to you whether that is a good or a bad thing.

I will tentatively put my toe in the water here. It is slightly dangerous to do this, but you are probably all going to agree. I assume that if you are able to maintain pretty much free trade with the EU, however it works, and are able to make free trade agreements with other major economies around the world—the United States, China, Japan, Australia and so on—that is a win-win outcome for you. You will have less trade diversion by doing that than you currently have.

You are a trade Committee. We would say to you that one of the things that we really do not want to come out of this Brexit exercise is the erection of tariff barriers and quotas between the UK and the EU. In a sense both of you—not just the UK, but you and the EU—have an obligation not to do that because it will have a negative economic effect on the UK and EU, and it will have a negative effect on the global economy. So if you can have a continuation of free trade, perhaps somewhat qualified, with the EU and you can make free trade agreements with other economies around the world, it seems to me that you will have less trade diversion than you currently have.

Q341 **Julia Lopez:** You talked about the Chinese FTA. In previous discussions I have had with you, we have discussed whether Australian meat is a threat to farmers here. You said that Australia cannot actually fulfil the demand in places like China, and that we should work together with you to fulfil those market demands. Is there any way in which the UK could benefit from the FTA that Australia already has with China in that regard, and by what mechanism do you think we could work together to do that?

Alexander Downer: Well, British businesses would have to go through Australia to then get access to the Chinese market. They can do that; I couldn't quote you any examples, but I guess that some do. That is not very likely to be the case with agriculture, and then there are rules of origin issues and so on that you would have to take into account, so I can't see how that could happen.

However, as you rightly say, our red meat industries are happy to work with your red meat industries in some of these other markets. I noticed that, when your Prime Minister was recently in China, the Chinese announced that they were lifting the BSE ban on British beef.

By the way, we are not worried about that. We are quite happy to compete with British beef in the Chinese market. More than that, we might be able to work together—perhaps more in the sheepmeat area than in beef—in some of these markets, particularly in terms of lobbying and marketing and all those kind of things.

We are not able to fulfil all our orders for beef. There isn't any way that we would see the UK market as a priority for us anymore, even with a free trade agreement.

Chair: Catherine West?

Catherine West: I think our excellent witness has covered the area I was going to ask about, so I think we can probably move on to the next question.

Q342 **Chair:** High Commissioner, some have argued that the UK would need to align its regulations with the US's and diverge from the EU's to agree a comprehensive FTA with the US. How has Australia managed issues of regulatory alignment and co-operation in its FTAs—particularly in the US-Australia FTA? How might Australia address the question of regulatory choice in negotiations with the EU, for example?

Alexander Downer: We already trade with the EU. Remember that, if you take the EU as a whole—including the UK—it is a very significant trading partner for Australia, and within the EU the UK is our biggest trading partner. We meet EU regulations for our exports.

Q343 **Chair:** When it comes to the United States, did you have any alignment issues for the FTA?

Alexander Downer: We have had no difficult alignment issues with the United States that I can recall off the top of my head. People forget that, when we export to the United States, we have to meet their standards, and when they export to Australia they have to meet ours. We have some different standards for, for example, motor vehicles, just as we have different standards from the EU. I am not really arguing that they are better or worse than each other; they are just different.

As a result, cars that are exported from the United States to Australia have to be adjusted for Australian standards. Quite apart from anything else, American cars are left-hand drive and ours are right-hand drive, so that is one regulatory change that they have to adhere to. You pretty much can't register a car in Australia if it is left-hand drive.

Q344 **Matt Western:** Just out of interest, I am keen to know about Australia's experience in its negotiations on the TPP with the previous US Administration, and also what sort of engagement Australian authorities and trade negotiators have had with President Trump's Administration?

Alexander Downer: Well, even our Prime Minister has spoken to President Trump in the last week about this. That is more at the political level and the officials level. To put this into context, when we got to the presidential election in November 2016, both the major candidates—Hillary

Clinton and Donald Trump—said that they would not proceed with the TPP. We were naturally enough disappointed that neither of them would do that.

President Trump won the election and he did pull out of the TPP. He had promised to do that during the election campaign, so while we are sorry that it happened, being Australian, instead of looking into our porridge and shedding tears, we think, "What the hell are we going to do about this?" We have an expression in Australia for when things get difficult: "She'll be right." We will work out something. So we started championing TPP 11—there were 12 originally. The country that came on side early, which was critical in making TPP 11, was Japan. There has been a huge change in Japanese trade policy in recent years, particularly under Prime Minister Abe. I think the plan is that on 8 March we will have the signing ceremony for TPP 11, but the agreement has been made there.

Now, we would like the Americans to come back into TPP. At Davos, President Trump had something to say about this. "Maybe, in different circumstances, we could consider coming back into the TPP"—or words to that effect. But I do not think it is something America is going to do any time soon. If it wanted to renegotiate it, I cannot see how we could do that. The TPP is an open agreement. That means that other countries are in principle—I say this pointedly to a House of Commons Committee—welcome to consider joining it. However, we are not going to change all the provisions of the TPP to allow them to join. That will apply to the United States as well: if it wishes to come and join, that would be fantastic. There are all sorts of geopolitical, as well as economic, reasons why it would be good to have it involved.

Q345 **Matt Western:** Do you think that the UK could possibly join the TPP after Brexit?

Alexander Downer: That depends on how you do your Brexit. It is hard to see how the EU could become part of the TPP, but it is an open agreement. We have said to the British Government—the Japanese position, as I understand it, is somewhat akin to ours—that you have to leave the EU and be in a position to negotiate your own trade policy, but in those circumstances, anything is possible. Certainly, it would not be out of the question. There is a geographic question to it: you are not a Pacific power. However, in a globalised economy your trade can be with anyone, anywhere. The notion—sometimes called in this country the gravity model—that you always trade the most with your nearest neighbours, is not our experience in Australia. Our nearest neighbour is Papua New Guinea and for some reason that is not our biggest trading partner. Yes, there is a reason for it and it is not to do with geography.

Q346 **Matt Western:** Can I just go into one specific area of the CPTPP? The investor-state dispute settlement mechanism apparently narrowed the scope from the original TPP. Why did that change occur, and what inferences, if any, can we draw from this change about the potential of including an ISDS mechanism in future UK trade agreements?

Alexander Downer: Investor-state dispute settlement mechanisms have been quite controversial in a number of countries, including Australia.

Q347 **Matt Western:** Which ones particularly?

Alexander Downer: That is a good question. I would have to take that on notice, but the principle has been a problem. I think the Labor party has been expressing some concern just in relation to the TPP. However, the way the mechanism works in the TPP is that domestic redress is the way investor disputes will be dealt with. The note here says that the scope of application of the original TPP's investor-state dispute system provisions has been limited under the new agreement. That, I think I am right in saying, was particularly at the request of the Canadians, who had some reservations. That is an example of a country that had some reservations about the investor-state dispute mechanisms. "Under the TPP 11 agreement, ISDS"—investor-state dispute systems—"is not available for investors seeking recourse for claims of breach of investment agreements and investment authorisations, and the minimum standard of treatment obligations in financial services sector." It is fairly technical. It is pretty limited in its application, so Governments are able to make domestic changes to policy without triggering some sort of international arbitration.

Q348 **Matt Western:** Finally, in your view what implications are there for the UK in looking at a UK-US free trade agreement, given the experience of the US withdrawing from TPP and perhaps a new attitude in Washington?

Alexander Downer: Gosh, that is a tough question to answer. That really is asking me to think through the Americans' real objections to TPP, which were not to do with investor-state dispute. I think their objections were more political than anything else.

Matt Western: Protectionist.

Alexander Downer: Yes, exactly. That is what I mean—a more protectionist sentiment. I met a Congressman, who was here in London last week, and he said that in his district, which is on the east coast, prior to the presidential election only 70% of the public supported free trade. Once the election was out of the way only 30% supported free trade. That is because the Democrats and the Republicans had run more protectionist lines—"America first"; "We're being done over by foreigners." That kind of sentiment has certainly caught fire in the United States.

We would say what we always say about these trade agreements. There is the economics of the trade agreements, which I have talked quite a lot about, and then there is the politics of trade agreements. Sometimes the economics seems to be simple, and sometimes the politics is quite difficult. It is easy to play into public fears about the impact of imports on the economy. A lot of that has happened in the United States. However, the politics might be that the United States sees real benefit in free trade with the UK due to sentiment, the special relationship or the UK's leaving the EU—I don't know. That might turn out to make it much easier.

With Australia, the US Senate ratification process in 2004 voted 80 to 16—four of them were away, I guess—in favour of the free trade agreement with Australia. Australia is a big agricultural producer and so is the United States, so how did that happen? There is a lot of emotional sentiment towards Australia in the United States. Americans think that Australia is a very good thing—they are quite right, by the way—so they are kind of pro-Australian. That was also in the context of the Iraq war, in which Australia, like the UK, participated, so there was a positive political sentiment there over that, for right or for wrong.

I think that the lesson I would learn is that if you want a free trade agreement with the United States, our experience shows that that can be done relatively easily, but it will depend on political sentiment. Does your Prime Minister and your Government have a passion for a free trade agreement with the United States? Does the President?

Chair: Let's hope it doesn't involve having to go to war with them. The two final questions are from Marcus and Julia. We will take both questions together, and then the answer afterwards. Marcus first, then Julia.

Q349 **Mr Fysh:** I am just interested in your thoughts on one particular area of TPP and what you think will happen to it. In terms of the automotive industries, it would seem to me that the TPP schedules around rules of origin and so on are quite different in terms of the local content requirement than what is being talked about in the renegotiation of NAFTA, for example. It is around 40% or 45%, as opposed to the proposal, which is 85%. Sixty-odd per cent. is where NAFTA is now. My understanding from many other free trade agreements around the world is that around 60% is pretty normal. What do you think the impact of TPP will be on the competitiveness of the global auto industry and in particular those Pacific nations? Are they going to potentially steal a march on the competitiveness in that industry?

Q350 **Julia Lopez:** Has the liberalisation of the movement of people been part of any of the FTAs that you have concluded so far? In particular, would you consider something like a realm visa with the UK?

Alexander Downer: Okay, visas. I am not sure I can answer your question on precisely what the rules of origin are in the TPP, but from memory you are right that typically rules of origin provisions are around 60%. Is it going to be a problem for the automotive industries? It will not be a problem for Australia, because our automotive industry is completely closed. I think we will have to get back to you on the details of the provisions. Between all of us here, we are not 100% sure.

On the visas question, our trade agreements typically do not involve negotiations on visas and the freedom of movement of people. However, during the negotiations with the Americans on the free trade agreement, we said, "By the way, it does not have to be part of the agreement, but we would like a better visa arrangement for our business and professional people." The Americans agreed to a visa called an E3 visa, which only Australians are eligible for. It provides easy access for Australian business and professional people to work in the United States for two years, and then it can be renewed and renewed. That has been a great deal for us. We have been very pleased with that visa arrangement.

Often visa arrangements are meant to be reciprocal. Countries will typically say, as they do with trade agreements, "We want it to be reciprocal." We have a universal visa system. Everyone who comes to Australia has to have a visa, wherever they are from, although there is some nuance on that in relation to New Zealand. We do not make any exceptions. Under no circumstances are we planning to do that in any negotiations.

With realm visas, we are able to get access to a visa system here called an ancestry visa. If you have a parent or grandparent born here in the UK, which is quite a high percentage of our population, you are able to come here and live and work for five years, and our ticket can be renewed. Then of course there is a pathway to citizenship here. We would not imagine that we would get a much better deal than that. We would imagine more that we could push for something like the American E3 system here. That would be the kind of visa system that we would look at.

Q351 **Chair:** Thank you. I have a final question, and you have the option of commenting on it or not. Norfolk Islanders are here lobbying this week.

Alexander Downer: They have free trade with Australia. They are part of Australia.

Q352 **Chair:** I don't think they have it on their terms. That is their argument. They feel they have been annexed by Australia. What is the Australian point of view?

Alexander Downer: They were annexed by Britain, I think. You need to look in the mirror here; it is British history.

Q353 **Chair:** Norfolk Islanders were against the referendum they have had. How does Australia see the Norfolk Islander view?

Alexander Downer: Norfolk Island became part of the colony of New South Wales. You did that—not us.

Q354 **Chair:** Their argument is that you did that.

Alexander Downer: Well, there you are. When you have joint history, you take joint responsibility—think about that one, Mr Chairman. It is part of Australia. The Australian Government decided a couple of years ago to close down the local Government there. They now have a regional council. The reason for that was that Australia wanted to mainstream all benefits and the tax system right throughout Australia—not have a different tax arrangement or welfare arrangement.

They did not have access to our medicare scheme. Their pension systems and so on were not part of our scheme. Their taxation arrangements were different. They had a 12% VAT rate; we have one of 10%. They had no income tax at all; we do have income tax in Australia. We thought, "These people are Australians—they can get all the benefits that are available to other Australians, and they can pay all the taxes as well."

Chair: I can see clearly where the disagreement is: they see themselves as Norfolk Islanders, and you see them as Australians. Thank you very much for that, and for coming in and explaining to us clearly and expansively US-Australian trade, and the lessons that we might learn in the future. Thank you very much, High Commissioner—it is much appreciated.