CASE STUDY OF A SUCCESSFUL NATIONAL INDUSTRIAL DEVELOPMENT PROGRAMME/STRATEGY

AUSTRALIA'S INDUSTRIAL DEVELOPMENT EXPERIENCE

1. The problem or issue addressed:
Since the 1970s, successive Australian governments have instituted significant policy changes that have seen a dramatic shift from protectionism to a more liberalised industry policy environment.

Major microeconomic reforms began in the 1970s with large reductions in tariffs. The rate of microeconomic reform increased dramatically in the 1980s and 1990s as the Australian economy became more open and competitive. These reforms were accompanied by significant labour market reforms which established a stronger link between wages and labour market productivity.

This policy shift recognised the importance of efficient resource allocation, productivity improvement and international competitiveness in sustaining economic growth, employment and improved living standards. As part of this process, industry protection/assistance has been markedly reduced, partly through a reduction in tariffs and quotas, and significantly greater emphasis placed on improving domestic and international competitiveness to support better trade and investment outcomes.

More recently, the policy focus has been expanded to support improved productivity and innovation in the context of better international understanding of the interaction between these and other drivers of sustainable economic growth. In addition, increasing importance has been placed on achieving strong economic growth, low unemployment and improved living standards in a manner which is consistent with principles of sustainable development.

2. Name of the programme:
The activities outlined in this case study encompass a broad range of policy initiatives.

3. Timeframe: Ongoing

4. Status: ☑ Ongoing ☐ Completed in year ___________

5. Main objectives:

- **Macroeconomic stability** – creating a stable environment in which industry can invest with confidence and businesses can build their international competitiveness. The focus is thus on achieving high levels of growth, employment and business investment in a low and stable interest and inflation rate environment.
- **Microeconomic reform** – creating an environment that contributes to improved competitiveness of business in domestic and international markets. Reforms include those to labour and financial markets, to corporate law, taxation, competition and regulation.
- **Specific interventions** – focusing on the key drivers of growth: innovation, investment and international competitiveness.

Current Australian industry policy recognizes the importance of sustainability and the need for economic growth objectives to meet the needs of the present without compromising the ability of future generations to meet their own needs. It promotes productivity growth rather than focusing solely on bringing additional inputs into production as a means of increasing output (economic growth), recognizing the latter scenario is not sustainable where the supply of natural resources is approaching finite limits, or where the overuse of the resource could lead to irreversible environmental damage.

Australian Government policy is that intervention should be undertaken where it is judged that economic, social or environmental objectives cannot be achieved in the marketplace and there is a clear net public benefit in intervening. The rationale for any proposed intervention is considered from the point of view of the economy as a whole, as opposed to specific firms or industries. This is likely to contribute more strongly to economic growth and improved living standards than policies developed with narrow firm or sectoral perspectives. It is important that any intervention is implemented as efficiently and effectively as possible.

Innovation is one of the immediate causes of productivity improvement, and hence the Australian Government actively promotes innovation through specifically targeted incentives.

Investment is encouraged by the Australian Government through creating a macroeconomic environment conducive to domestic and foreign investors and microeconomic reform which reduces costs and improves investment returns.

Similarly, international competitiveness is fostered through maintaining sound macroeconomic fundamentals, undertaking microeconomic reforms and encouraging market forces to operate. Competition encourages innovation, new ideas, better service provision and sustainable industries and often results in more efficient allocation of resources across society.

Australia's Innovation Focus
Historically, the Australian Government directed considerable policy attention towards initiatives designed to encourage Research and Development (R&D) activity. Recently, in the context of better international understanding of the interaction between innovation and productivity and other drivers of sustainable economic growth, the Government has broadened its focus to include innovation. The aim has been to encourage leverage from existing strengths in traditional industries and to develop new high-profit, high-growth industries.

Some key characteristics of the Australian economy which have led to the innovation focus are:

- The Australian economy's scale, visibility and remoteness affect its ability to attract foreign investment, including R&D investment from large international companies;
- Industry structure in Australia is characterised by a large number of small to medium sized enterprises in which R&D is less prolific than in larger companies;
- Reliance on the primary sector is high, and a significant proportion of manufacturing exports are simply transformed manufactures; and
- The experience of the last three decades: the dramatic policy shift over this period placed significant emphasis on improving domestic and international

> competitiveness to support better trade and investment outcomes. As a result, Australian industries became well-placed to compete in the global marketplace. Innovation by firms is recognised as playing a key role in continuing these successes.

Australia's Innovation Policy

Australian innovation policy has historically preferred market driven prioritisation, rather than an approach of 'picking winners' or 'top-down' direction-setting within the research sector. There has been a preference for enabling organisations to exercise considerable autonomy in deciding what research to pursue, with research funding provided in block grants to research institutions and universities with little centralised direction, but allocated on the basis of competitive project quality.

Australia's innovation policy is articulated in two key action plans: *Backing Australia's Ability: An Innovation Action Plan for the Future* (2001) and *Backing Australia's Ability: Building Our Future Through Science and Innovation* (2004). The former provided the strategic framework for innovation and included the establishment of new programs and activities or enhanced existing ones, while the latter built on this, following evaluation of the programmes delivered under the 2001 Statement. It deals with some gaps and takes on board a number of developments that further defined the direction of innovation policy. Together they form the backbone of Australia's innovation action plan. In both statements the Australian Government committed to funding major initiatives to stimulate innovation to the combined sum of AU$8.3 billion over 10 years.

This focus on innovation, in conjunction with the establishment of Australia's National Research Priorities (an environmentally sustainable Australia; promoting and maintaining good health; frontier technologies for building and transforming Australian industries; and safeguarding Australia) which cover the activity of all publicly funded research agencies plus those allocated government research funding, is a move towards taking a more strategic approach.

Framework for Industry Policy Development

A Framework for Industry Policy Development (FIPD), finalised in 2005, is an example of a tool for making industry policy decisions, and a framework that explicitly considers environmental and social aspects in industry policy decision making. It provides a framework for thinking through the issues involved in policy development in a consistent way, and ensures that any government intervention is based on a transparent and well considered analysis of the net benefits, structured in the most efficient and effective manner. It thus aims to increase the consistency of advice and promote greater transparency and accountability in the policy-making process.

The FIPD emphasizes the need for wide consultation across government and with other stakeholders and is based on a 'whole of government' approach to policy development and program delivery. This aims to ensure that policy advice from one Department is consistent with other elements of the Government's policies and with Australia's international obligations, and that departmental officers seek solutions in the national interest rather than defending their specific portfolio interests.

The *National Strategy for Ecologically Sustainable Development* (NSESD) is explicitly recognised in the FIPD, to ensure that social, environmental and economic issues are all taken into account when developing industry policy.

The FIPD aims to facilitate well-considered analysis of the short and long-term, social, environmental and economic costs and benefits, and distributional effects of any government intervention. If a need for intervention is identified, the FIPD provides guidance on the form the intervention should take; general design issues (including international obligations); identification of net benefits from intervention (for example, utilising cost-benefit analysis), and program delivery.

National Competition Policy

Australia's National Competition Policy is an example of a policy to promote open markets domestically but which also has flow on effects to its international competitiveness and attractiveness to investors.

The Australian Government initiated extensive economic reforms in the 1980's to remove policy-related inhibitors to growth (including liberalisation of capital market controls, abolition of import quotas and phased reduction in tariff assistance). As the reform program gathered pace, it became apparent that aspects of Australia's wider competition policy framework were impeding performance across the economy and constraining the scope to create national markets for infrastructure and other services.

In April 1995, the Australian Federal, State and Territory Governments reached agreement on an ambitious plan to promote enhanced competition in Australia. The resulting *National Competition Policy* (NCP) is underpinned by three intergovernmental agreements: the *Competition Principles Agreement*; the *Conduct Code Agreement*; and the *Agreement to Implement the National Competition Policy and Related Reforms (Implementation Agreement)*. The three agreements outline the reforms which governments undertook to put in place under the NCP process.

The key objective of NCP is to develop a more open and integrated Australian market that limits anti-competitive conduct and removes the special advantages previously enjoyed by government business activities, where it is in the public interest to do so. NCP is based on an explicit recognition that competitive markets will generally serve the interests of consumers and the wider community, by providing strong incentives for suppliers to operate efficiently and be price competitive and innovative. A key principle of NCP is that arrangements that detract from competition should be retained only if they can be shown to be in the public interest.

Specifically, NCP provided for: the extension of the *Trade Practices Act* (TPA) to previously excluded businesses; governance and structural reforms to government businesses to make them more commercially focused and expose them to competitive pressure; regulatory arrangements to secure third-party access to 'essential' infrastructure services and, more generally, to guard against overcharging by monopoly service providers, especially in the infrastructure area; and a process for reviewing, and where appropriate amending or rescinding, a wide range of legislation which restricted competition. NCP also incorporated previously agreed reform programs for the electricity, gas, water and road transport sectors.

In 2004, the Australian Government initiated an inquiry into NCP reforms (*Review of National Competition Policy Reforms*, 2005), particularly focusing on the impacts of NCP and related infrastructure reforms undertaken to date on the Australian economy and the community more broadly; and on areas offering future opportunities for significant gains to the Australian economy from removing impediments to efficiency and enhancing competition. The results of this review are outlined in the 'Results Achieved' section of this case study.

Reform of the Automotive Sector

The objective of the Government's automotive industry policy is to provide transitional assistance to encourage competitive investment and innovation in the Australian automotive industry in order to achieve sustainable growth, both in the Australian market and internationally, in the context of trade liberalisation. This policy is supported by strategies that are designed to minimise disruption to production and employment during the transition period.

In the late 1970s, tariffs on passenger motor vehicles (PMVs) peaked at nearly 60 per cent, underpinning quotas which restricted imports to 20 per cent of the market and a local content scheme to promote the use of domestic components. These arrangements, designed to stimulate the development of viable automotive manufacturing in Australia, also served to insulate the industry from external competitive forces. However, in 1985, the focus of automotive policy, consistent with broader changes to industry policy, shifted to one of exposing firms to greater import competition. Reductions in assistance have proceeded gradually and steadily since.

Tariffs on PMVs and derivatives and components for these vehicles dropped to 10 per cent on 1 January 2005, and a staged phase out will continue, with tariffs dropping to 5 per cent on 1 January 2010. As a means to facilitate the transition to lower assistance, the Australian Government has operated the *Automobile Competitiveness and Investment Scheme* (ACIS) since 2001. The scheme provides eligible participants with tradeable import duty credits based variously on their production, R&D and investment activities. Duty credits can be used by the firm to which they accrue, or by other importers who have purchased duty credits, to discharge customs duty on vehicles and components. Some key results and impacts of automotive sector reform are included in the 'Results Achieved' section of this case study.

Support to Small Business

A healthy small business sector is vital to the Australian economy. There are 1.1 million small businesses in Australia, which represents over 96 percent of businesses. The small business sector generates around 30 percent of Australia's economic activity and 3.3 million jobs. Small businesses are not located only in major metropolitan centres: approximately 35 percent of small businesses operate in regional Australia.

Small businesses are defined in Australia as businesses with less than 20 employees. Due to their size, small businesses do not generally have professional managers. Instead, the business owner typically handles the administration burden as well as running the business. As a consequence small businesses have little scope to absorb the impact of additional regulatory burden, and the task of communicating with small businesses is made more difficult by the strong competition for the operator's attention from other aspects of the business. The challenge in communicating with small business is to deliver information that is useful, easily obtained and imposes minimal compliance burdens on small business when they obtain it.

The Government's objective is to secure improvement in the economic environment for small business, promoting greater economic and employment growth in this vital sector. It has to this end taken efforts to reduce administrative procedures and costs related to business start-up and operation, by firstly establishing the Office of Small Business (OSB).

The OSB is a focal point for the development and consideration of small business policy issues within the Australian Government. It is responsible for promoting and maintaining links across the Federal departments and agencies responsible for implementing elements of the Government's plan for small business.

The OSB's interest in environmental issues is largely driven by concerns to avoid imposing an unnecessary regulatory burden on small businesses. The OSB must be consulted in developing proposals for Cabinet consideration which will impact on small business. OSB will make an assessment of whether the impact of a measure is negligible, low, medium or high (considering the number of businesses affected and the degree of impact on individual businesses).

OSB has policy responsibility for components of the Small Business Assistance Program and the Regulation Reduction Incentive Fund (RRIF). The latter, an AU$50 million fund launched early in 2005, aims to reduce the 'red tape' burden faced by small business, particularly home-based businesses, at the local government level. From mid 2005, local governments will be able to compete for payments from the RRIF based on their proposals to reduce red tape, regulatory complexity and compliance requirements for the small and home-based business sector. The RRIF is envisaged to encourage best practice and the use of technology by local government to deliver real benefits to small businesses.

A final example of an initiative to facilitate better business interface with government is the Business Entry Point (BEP) which was established in 1997 to provide Australia's small businesses with an online entry point to government information and services. Its role is to aggregate information and transactions from all three levels of government and to provide business with an online discovery mechanism for this content. The BEP is unique in that it crosses jurisdictional boundaries to provide a whole-of-government portal that provides information on planning, starting and running a business.

6. Lead institution:
Australian Government, State and Territory Governments.

7. Other implementation arrangements and stakeholders involved (public, private, NGOs, CBOs, international support, etc.):

8. The results achieved:

Economic performance
While direct causal links are somewhat difficult to establish, a compelling case can be made that policy changes which resulted in a successful combination of macroeconomic fundamentals, microeconomic reforms (including tariff reduction and reforms of the labour market, financial market, infrastructure, taxation and competition), increased privatisation and deregulation, and carefully targeted Government intervention have delivered impressive improvements in Australia's overall economic performance since the 1970s. Australia experienced consistently strong GDP growth from the mid 1980s, and since the mid 1990s, both Australia's economic growth and GDP per capita performance have improved significantly compared with the domestic experience of the 1970s and 1980s and compared to the performance experienced by other developed economies over the same

period. Australia also experienced a significant improvement in productivity growth during the 1990s.

National Competition Environment

The 2005 *Review of National Competition Policy Reforms* found that the NCP had delivered substantial benefits to the Australian community which, overall, greatly outweighed the costs. It had contributed to the productivity surge underpinning 13 years of continuous economic growth, and associated strong growth in household incomes; directly reduced the prices of goods and services such as electricity and milk; stimulated business innovation, customer responsiveness and choice; and helped meet some environmental goals, including the more efficient use of water.

Benefits have flowed to both low and high income earners, and to country as well as city Australia, though some households have been adversely affected by higher prices for particular services and some smaller regional communities have experienced employment reductions.

Key lessons learnt from the Review:

- A broadly-based reform program improves the prospect that those who might lose from a specific reform still gain overall. This can make it easier to progress reforms that might be difficult to implement on a stand-alone basis.
- A reform framework which embodies agreed principles, while providing for some flexibility in implementation, is well-suited to a multi-jurisdictional reform agenda.
- Reform is likely to progress more effectively where commitments are specified in advance and there is prioritisation of the reform task.
- An effective public interest test is essential to secure beneficial reform and to enhance community acceptance of the reform process.
- Independent and transparent review and assessment processes are critical to secure good outcomes, especially on contentious issues; prevent backsliding; and promote public understanding of the justification for reform.
- In any reform program, the potential adjustment and distributional implications should be considered at the outset, with decisions about transitional assistance guided by appropriate principles.
- Where reforms involve the establishment of new regulatory arrangements, it is important that those regulations be well scrutinised in advance and periodically reviewed to ensure the benefits continue to exceed the costs.
- Providing financial incentives for jurisdictions to follow through with agreed reforms can be very useful in promoting effective outcomes, although the rationale and value of such payments clearly depend on the nature of the reforms.

Automotive Sector

Key results and impacts of automotive reform identified in the Productivity Commission's 2002 report, *Review of Automotive Assistance* include:

The Australian automotive industry has embraced the challenges provided by reductions in motor vehicle tariffs, and has become leaner and more export oriented. Reductions in assistance to the industry have also encouraged automotive firms to improve their productivity performance. Improvements in quality have been achieved by the local manufacturing plants, resulting in parent companies of the local manufacturers awarding more export contracts to the local subsidiaries.

Further, consumers and user industries have benefited. Reductions in automotive tariffs have contributed to real price declines for motor vehicles despite a weakening of the Australian dollar. This has benefited private and commercial users and improved the transport options available to the less well off in the community. Consumers have also benefited from greater choice.

The import share has risen and the industry has turned to export markets. As tariffs have declined, the share of imports has increased from around 15 per cent of total PMV sales in 1985 to around 60 per cent in 2001. Faced with a rising share of the domestic market going to imports, the industry has increasingly sought out export markets as a source of growth. This has enabled vehicle producers to sustain their output. Exports of vehicles and components increased tenfold between 1985 and 2001. Moreover, a number of home-grown multinational component firms have emerged, with a presence offshore, and others are deriving income from licensing technologies to overseas firms. Vehicle and component producers have not only revealed a capacity to adjust, but also demonstrated strong competencies in world competitive niche manufacturing.

Industry employment has declined but productivity has increased. Industry rationalisation has brought with it significant reductions in employment. Total automotive manufacturing employment declined by about 30 per cent over the decade to 2001. Nearly all this decline occurred in vehicle manufacturing. The maintenance of production levels in the face of declining employment has contributed to the substantial improvements in labour productivity across the entire automotive sector. Notwithstanding the significance of this decline in employment, industry rationalisation has been relatively orderly.

Reduced assistance has not been the only factor affecting the structure and performance of the automotive industry. Much of the adjustment since the 1980s coincided with a significant real depreciation of the Australian dollar. This partially insulated the industry from the import price pressure associated with lower levels of protection (it also reduced the extent of the cost savings on inputs used by vehicle and component producers).

The economy-wide microeconomic reforms, including taxation reform, which took place in parallel to the reforms of the automobile industry directly affected the automotive sector by producing more cost-effective transport and reductions in input taxes. They also had more ‘facilitative’ effects that required firms to respond in order to gain the benefits. For instance, wage award restructuring and subsequently the introduction of enterprise bargaining have contributed to the removal of some restrictive work practices, thereby paving the way for productivity improvements. More subtly, increasingly vigorous competition has contributed to changes in culture and attitudes by sharpening incentives to pursue available avenues to improve productivity. For example, competitive pressures have encouraged firms to innovate, to benchmark against international best practice and to adopt new technologies.

9. The relationship of the programme to internationally agreed goals and targets:
This case study of Australia’s industrial development experience over the last three decades supports Paragraph 10 of the Johannesburg Plan of Implementation (JPOI). It does so primarily by sharing a number of lessons learnt with respect to enhancing productivity, the more efficient use of resources and competitiveness, and by highlighting the important role that innovation plays in industrial development in an increasingly interconnected world.

Australia's lessons in reforming, amongst others, the automotive industry to improve productivity and make it internationally competitive, including the progressive reduction in tariffs, could be valuable for developing nations trying to maintain the viability of key industries in the face of globalizing forces. Further, Australia's National Competition Policy reforms are an example of a cohesive package of mechanisms aimed at improving competitiveness within a country that also has flow-on effects to international competitiveness and attractiveness to international investors.

Given the significant proportion of Australia's businesses which are small in size, Australia's experience in developing a suite of mechanisms, largely overseen by the Office of Small Business, to provide an enabling environment for small-scale private enterprise to flourish may be valuable to developing nations where the informal sector is large and small or micro-business dominates rural and urban economies.

Further Information

AusIndustry. Automotive Competitiveness and Investment Scheme. Web: http://www.ausindustry.gov.au/content/level3index.cfm?ObjectID=8A02E067-78E4-4F69-A4FD004D826DDE18

Australian Public Service Commission, 2004. *Connecting Government: Whole of government responses to Australia's priority challenges*. Commonwealth of Australia. Canberra. Web: http://www.apsc.gov.au/mac/connectingsummary.htm

Commonwealth of Australia, 2001. *Backing Australia's Ability*: *An Innovation Action Plan for the Future.* Canberra. Web: http://backingaus.innovation.gov.au/docs/statement/backing_Aust_ability.pdf

Commonwealth of Australia, 2004. *Backing Australia's Ability: Building Our Future Through Science and Innovation.* Canberra. Web: http://backingaus.innovation.gov.au/2001/statement/index.htm

Department of Industry, Tourism and Resources and Department of Small Business and Tourism. Business Entry Point: http://www.business.gov.au/Business+Entry+Point/

Department of Industry, Tourism and Resources, 2005. *A Framework for Industry Policy Development*. Commonwealth of Australia. Canberra.

Department of Industry, Tourism and Resources. Regulation Reduction Incentive Fund. Web: http://www.industry.gov.au/content/itrinternet/cmscontent.cfm?objectid=890ACA7B-65BF-4956-B00E0E099540746D

Department of Industry, Tourism and Resources. Small Business Support. Web: http://www.industry.gov.au/content/itrinternet/cmsindexpage.cfm?objectid=48A33B79-20E0-68D8-ED9772A05DDC83D5

Ecologically Sustainable Development Steering Committee, 1992. *National Strategy for Ecologically Sustainable Development.* Commonwealth of Australia. Canberra. Web: http://www.deh.gov.au/esd/national/nsesd/strategy/index.html

Productivity Commission, 2002. *Review of Automotive Assistance*. Commonwealth of Australia. Canberra. Web: http://www.pc.gov.au/inquiry/auto/finalreport/index.html

Productivity Commission, 2005. *Review of National Competition Policy Reforms.* Commonwealth of Australia. Canberra. Web: http://www.pc.gov.au/inquiry/ncp/finalreport/index.html