# INDUSTRY POLICY AND THE AUSTRALIA-JAPAN COAL TRADE

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The industry policy debate in Australia has consumed a great deal of the energy of progressive academics, leading trade unions and government bureaucrats.[1] In combating such advocacy there has been a similar effort by orthodox economists - from academia, business, the media and also from within government. From the labour movement's viewpoint, the industry policy initiatives of the Australian Labor Party in office federally in the period 1983-1996 were limited to begin with and gradually fizzled out altogether. Recent analysis (Bell, 1996) has suggested dismal results for what little industry policy there was.

This article seeks to contrast the industry policy of Australia with that of Japan, it's major trading partner. It does so in relation to the coal trade rather than manufacturing, the traditional focus of industry policy in Australia. It seeks to demonstrate the gulf that exists between the two nations in the practice of government policy and its relationship with capital. Whereas trade and industry are seen as two sides of the same coin in Japan, and immense effort has been put into securing raw materials on an advantageous basis, in Australia trade policy has been largely divorced from industry policy and to the extent that it has been integrated it has been mostly with regard to manufacturing. The minerals trade, easily the largest component of Australia's trade with the world, has received scant attention from the advocates of industry policy.

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* The comments of Dick Bryan, Evan Jones and Frank Stilwell are gratefully acknowledged.

1 See, for example, *Journal of Australian Political Economy*, Special Issue, Australia Reconstructed: Ten Years On, No. 39, June

The final result of this lack of policy attention has been major losses to the Australian community from the exploitation of its natural resources, and a deepening of the structural crisis in Australia's economic position which constrains options for future economic development.

## Why Does it Matter?

It has been consistently argued that Australia's balance of trade is crucial to the capacity of the Australian economy to support improvements in the standard of living and in employment levels. The argument is roughly as follows:

- that Australian society has, at various times, had a tendency to import more than it exports, and this contributes to the Australian economy being in debt to the rest of the world. The trade imbalance arises at least in part because Australia exports low-value primary commodities and imports high-value manufactured goods;
- that unless addressed this tendency results in spiralling public and private sector net foreign debt, leading to international pressure to cut public sector spending and to limit wage levels in order to restrict consumption and therefore imports;
- that the way to overcome this problem is to restructure Australian industry so that more is exported, redressing the trade imbalance, eliminating or at least reducing the current account deficit, reducing foreign debt and removing constraints on the ability of wages to grow and the public sector to spend.

It is further argued that the current account deficit, now running at 3% of GDP per year (OECD, 1997), is a limit on the rate at which the economy can grow because, unless Australian industry is better able to supply a range of manufactured goods and services to its own community, any economic growth feeds directly into increased imports, increasing the problems stated above. The limits on the rate of growth of the economy then restricts the possible growth in employment.

It is not necessary to accept this reasoning in order to agree that improving the capacity of Australian industry to generate greater income is a good idea. Employers with stagnant sales, fixed or declining markets and falling prices for their output do not easily agree to wage rises. Their tendency to avoid, evade and oppose taxes is also likely to increase, and so will that of their employees, leading to limits on the public sector and to spending on social security, public health and education.

Two critiques of this type of position are that it is nationalistic; and that in accepting the need for continuing economic growth and further international trade it is pursuing a competitive goal that can never be won and which is environmentally unsustainable. The latter argument is rejected on the basis that zero growth economies will inevitably be accompanied by spiralling unemployment and cuts in living standards, both of which are unacceptable to most people. The task for those who recognise the need for further economic growth but also the constraint of environmental sustainability is to devise paths of economic growth that enable wealth creation whilst not increasing natural resource use - a difficult task that is beyond the scope of this article.

As for being nationalistic, that is certainly a feature of policies which benefit Australian-based capital at the expense of foreign capital. The case presented here seeks to avoid such a position. The ownership of Australian industry is regarded as immaterial; capital is capital and will generally move to where it makes the most profit. The issue for Australians is the terms on which capital is invested here, and whether ordinary Australians benefit sufficiently from it. Hence the issue in this paper is that a profitable coal industry will afford the potential for greater community benefits than an unprofitable one, especially if that profitability is secured by increased export prices rather than worsening working conditions in the coal industry. In the absence of concrete mechanisms for the global working class to work together, it is important to ensure that the Australian community gets a fair deal from its increasing integration with the rest of the world. To reject all Australia-focused trade and industry policy as nationalistic is to leave Australian working people and the community without the tools to ensure improved living standards and employment from further globalisation.

## Coal: Some Background

Coal is "out of sight, out of mind" for the vast majority of Australians. However, at 10% of merchandise exports, coal exports dwarf all other export industries (ABS, 1997), including service sector industries such as tourism. Australian reliance on coal exports reflects a much greater reliance on the primary industries in general. Mining and minerals processing account for over 40% of Australian merchandise exports; with the addition of the products of agriculture the proportion exceeds 65%. Even with the recent increased significance of manufacturing exports, a comprehensive approach to addressing the current account deficit would still seek to ensure that income from mineral and agricultural sources was maximised. However, successive Australian governments have put little emphasis on the coal trade, assuming that it would look after itself. This blasé approach has not been shared by the Japanese counterparts to the trade, who have deployed immense effort and resources into securing the trade on favourable terms to Japanese industry.

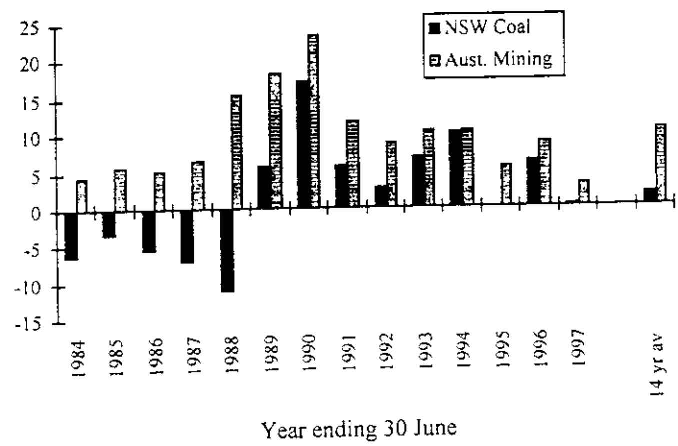
Whilst enjoying continued growth, the Australian coal industry has suffered from low profitability in comparison to other Australian mining industries even whilst remaining the largest section of the industry. Figure 1 shows profitability of the NSW coal industry. (Figures are not available for the national industry.)

This low profit matters because businesses which do not make profits do not pay taxes, depriving the community of a return for the use of its natural resources.[2] Whilst there are royalties payable which are based on the tonnage of coal mined or its value, these are set at a low rate and do not make up for low or non-existent corporate income taxes from unprofitable coal companies. Moreover, continuing low profits leads to continued pressure by business on governments to further lower royalty

2 Whether community returns from the mining industry are equitably distributed is an important question; it cannot be assumed that improving the profitability of, and then revenues to government from, the industry will automatically benefit most Australians. This is a problem for all discussions of the taxation of capital and space constraints prevent it being canvassed more fully here.

rates, to lower other charges on the industry (such as rail freight rates and port charges) and to pressure on the workforce to produce more coal for less wages. Figure 2 shows that the NSW coal mining industry (around one half of the total industry) is steadily reducing its community returns measured as a proportion of its own gross revenues.

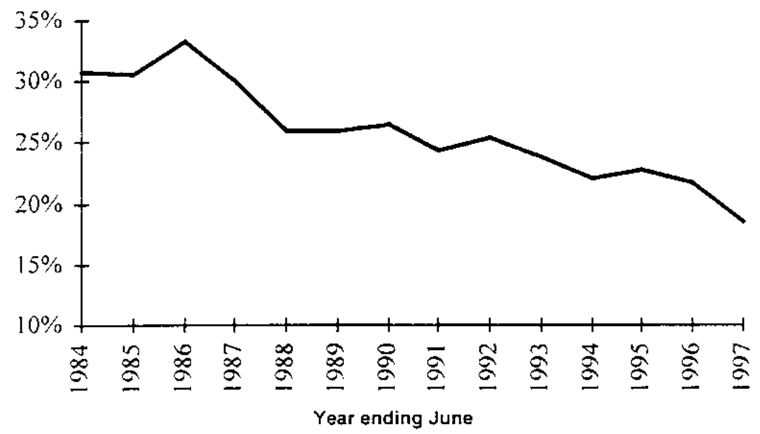
**Figure 1 Coal industry profits, NSW**




Source: Coopers and Lybrand (1998) and previous issues.

An industry which is failing to increase its contribution to the community, despite its increasing size and production, calls into question its legitimacy in terms of its right of access to Australian natural resources. Whilst opponents of mining *per se* might regard this as desirable, it also means that the Australian community is left deprived of what it should have received for the exploitation of its resources, and further reduces the capacity of the community to pay its way in the global economy. How this situation has come about is examined through a description of industry and trade policy in Japan, and through the subsequent Australian response.

**Figure 2 Total payments to governments as % of coal industry revenues, NSW**




Source: Coopers and Lybrand (1998) and previous issues.

## Trade and Industry Policy in the Japanese Steel and Power Industries

> Nothing has been more important for Australia in Asia than the Japanese game in the resources trade. Yet very little is said in the 1990s about this most important of all games. Perhaps one reason is that the Japanese resources game brought with it such stunning uncomfortable reality that Australia has still not fully recovered, decades after the play began. (Byrnes, 1994, p65)

In spirit, if not in practice, most developed nations adopt the orthodox economic maxims of the benefits of free trade and competition, in both domestic and international markets. This formal commitment to free trade is often carried through into domestic policy. In many developed countries, and certainly in Australia and the United States, legislation such as the Australian *Trade Practices Act* (1974), seek to proscribe co-operative arrangements amongst companies in the same industry on the basis that this is a breach of competitive principles and is likely to be disadvantageous to consumers.

The Japanese situation is *not* similar. There is indeed competition between rival firms in Japan, and the economy is dominated by private capital.[3] But this competition takes place within a framework which is characterised by a consensus on the national interest, and there is substantial evidence of co-operation amongst Japanese firms to achieve mutual benefits with respect to foreign suppliers and/or competition.

This is particularly so with respect to the Japanese steel and power industries. O'Brien (1992) argues that the entire post war history of the Japanese steel industry is one of the seeking of consensus between the bureaucracy and business on strategic long term goals. The bureaucracy in the form of the Ministry for International Trade and Industry (MITI) and the Ministry of Finance (MoF) has sought to first rationalise the industry and then to stimulate its rapid expansion with new technologies to achieve economies of scale. This was achieved initially through the heavy-handed mechanism of the allocation of concessionally-priced funds, and later through 'administrative guidance'. In the most substantial evidence of co-operative activity in the national interest, Japan's two biggest steel makers, Yawata and Fuji, merged to form Nippon Steel Corp. with the encouragement of MITI. It was done in the interests of avoiding 'unnecessary competition' that risked squandering economic rents[4] from the international steel trade.

The situation in the Japanese power industry is similar. The industry consists nominally of nine major private utilities. However, they were set up by government decree in 1951, and a large part of their construction finance has been provided at below-market interest rates from the public sector (Hein, 1990). The continuing co-operation of business and the state in the supposedly private power industry is evidenced by the Electric Power Development Corporation, a joint

3 In fact, the Japanese state is a smaller player in the national economy than in most OECD nations, accounting for only 6% of employment and 27% of expenditure (OECD, 1997).

4 'Economic rents' are defined as super or excess profits arising from exclusive access to resources or dominance of a trade or industry.

venture of the Japanese Ministry of Finance and all nine electricity utilities. The task of the EPDC is to develop and commercialise new technologies and undertake other projects that are too risky for individual companies. With 70% of the equity provided by the state, and debt finance on a concessional basis also from the public sector, most of the risk is being carried by the public sector.

The close involvement of the Japanese public sector continues into the activities of the power utilities in overseas investment: the group of ten are all involved in the Australian coal industry through investment vehicles EPDC (Australia) Pty. Ltd. and Japan Coal Development Australia Pty. Ltd.

The industry policy effort in Japan is indivisible from trade policy; achieving success in trade is one of its central purposes. Crawford *et al* (1978) contrast the outward focus of Japanese industry policy with the inward-looking, protectionist stance of most Australian industry policy until the 1980s:

> Japan's structural adjustment policies have been comprehensively directed to fostering new activities in a period of high growth for the manufacturing sector and have been formulated in a long-term indicative planning frame. This has not been the approach in Australia where, until recently, measures to assist declining industries have been concentrated in protection policy. (ibid., p149)

Japan's outward dependency on natural resources has long been recognised, and a substantial policy effort has been directed towards reducing this vulnerability. Japanese business and the state share a fear of resource vulnerability that is hard for more resource-rich nations to understand:

> Mineral resources are the lifeblood which sustains the life of the people and their industrial activity. Japan depends almost entirely on imports for its mineral resource requirements. What is more, deposits of mineral resources are concentrated in a few areas of the world . . . Owing to this peculiar set of circumstances, the availability of mineral resources could pose a short term sporadic threat or a protracted industrial menace to the

> economic security of Japan (*MITI White Papers* 1981-82, cited in Kolenda, 1985, p257)

It is from this basis that joint government and business activity in foreign resource markets begins, especially in coal, oil and natural gas.

## Japanese Government Support of Overseas Investment

Government-assisted finance for coal mining investments began in the 1960s, but it was formalised in the 1970 MITI White Paper that promulgated the 'Development-for-Import' or *kaihatsu yunso* policy. The primary focus of the policy was to improve security of oil supplies, and the greatest effort went into oil projects in the Middle East and elsewhere. However, coal was also a significant component, with the goal of diversifying energy supplies, diversifying their sources and improving security of supply.

The primary vehicles of participation by the Japanese state in the *kaihatsu yunso* policy have been the funds of the Japan Development Bank, the Export-Import Bank, and the Agency of Natural Resources and Energy in the Ministry of International Trade and Industry. The Japanese state has access to substantial investment funds through its Fiscal Investment and Loan Program (FILP), which has as its funding base savings accounts and insurance schemes operated through post offices. FILP funds were equivalent to 13% of all loan funds in Japan in 1955 and 11.8% in 1990 (JDB & JERI, 1994).

The bulk of FILP funds go to domestic programs - infrastructure, housing, local government, small business, etc. But a significant portion is allocated to international trade and investment. In 1990 the Japan Development Bank and the Export-Import Bank received just over 20% of all concessional finance, and the Export-Import Bank allocated 35% of its funds to overseas investments or import programs. The total of funds allocated to subsidising overseas investments in 1990 was ¥1,401.7 billion - about A$12.6 billion at the then prevailing exchange rates. This is a substantial public sector commitment to assisting business in overseas ventures that is not related to any aid program. That assistance is provided because the overseas investments, where they fit within the development-for-import policy or similar program, are seen as being in the national interest.

There are further sources of funds from the public sector. MITI's Agency of Natural Resources and Energy has a budget for coal-related programs. Much of this budget is administered by the New Energy and Industrial Technology Development Organisation (NEDO). NEDO operates as a subsidiary of MITI, and is funded by both MITI and the various steel mills and power utilities. It is a standard example of the way in which business and the state work together in Japan to achieve mutually-shared goals. NEDO works to facilitate the development of coal mines for the Japanese market in a number of ways, including the provision of debt guarantees for loans for mining investments by the Export-Import Bank or from commercial banks. In providing bank debt guarantees, NEDO removes all or most of a bank's risk exposure in such loans, with the effect of encouraging bank lending to mining projects of marginal or uncertain profitability. This shouldering of risk by NEDO is not as real as it seems. Two NEDO-assisted projects in Australia - the North Goonyella and Ensham mines, projects which were considered by the merchant bank BZW (1993) to be of dubious commercial merit, have been awarded long term contracts by major Japanese buyers. Similar security has not been given to other suppliers, who are generally on annual contracts. There seems to be a happy coincidence between the action of NEDO in backing a project and in the awarding of coal supply contracts by major Japanese businesses. This coincidence results in more coal mines and greater coal supply than would otherwise be the case.

## Co-ordinated Intervention in World Markets

The relationships between Japanese business and state organisations, as described above, are clearly very close. Whilst the oft-stated policy goal is simply improved resource security through diversification of supply and encouragement of capacity development there is a harder and more calculated edge to the strategy.

In *The 1989 Fiscal Year: Survey for Foreign Coal Import Infrastructure Promotion* (1990)[5] NEDO bureaucrats published consensus views on how the coal trade relationship between Australia and Japan should be handled. The trading relationship was seen as necessarily extending to investment issues. With regard to annual coal contract negotiations, supposedly the exclusive preserve of the steel and power companies[6], NEDO offers the following advice:

> .... the United States can be introduced as the major counter-supplier to check Australia. That is, in contrast to price negotiations in which Australia took the initiative and reflective of Australian intention on coal prices, Japanese thermal coal users would be able to take a new advantageous turn in these negotiations (through the new supplier); Japan can check Australia. (p9)

With regard to the role of investment the advice offered is:

> The second problem is, as was pointed out in the process of making a supply forecast, that the demand and supply relationship in the international thermal coal market will shift to a tight base. The price of thermal coal will rise. The relative price of thermal coal against that of oil in the year 2000 will approximate the worst period of the 1986 counter-oil shock: about 0.6. The price of thermal coal must be reduced, as must its relative price against oil and plans must be made to enlarge usage of thermal coal. For this, an enlargement of the thermal coal supply is needed.
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> In Australia, which has the largest share of the thermal coal supply, interest rates are very expensive ...... To solve this problem, Japanese firms need not only assume ownership rights and interest in Australian coal mines, but also to invest and

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5 This document was not published in English, which perhaps explains its remarkable frankness. The Construction, Forestry, Mining and Energy Union in Australia obtained a translation through the commissioning of research in Tokyo.

6 Various Japanese authorities have expressed the view that there should not be government intervention in the coal contract negotiations, and were unhappy at the existence of Australian export controls. See, for example, Hartcher (1994).

> finance these via low interest loans from Japan. ..... Through the dimensions of reduction of interest and refund duties and the enlargement of supply by the promotion of new development, the price of thermal coal will be stabilised at a lower price.[7] (Section 9.2)

These extracts provide clear evidence of Japanese business investment and price bargaining that is co-ordinated by or with government. This degree of state / business co-ordination should not be seen as surprising. Resource security is of paramount concern to business and government alike. That mutually shared goals should be achieved through co-operation rather than simply untrammelled competition is central to the way in which economic activity is organised in Japan. As the recently published *Policy Based Finance: the Experience of Post War Japan* by the Japan Development Bank (1994) makes clear, this approach is entrenched in Japan and will remain, despite the hostility to it of other OECD nations and the OECD secretariat. It is an approach in sharp contradiction to that which has dominated in Australia.

This multi-faceted, pragmatic and nationalistic approach by Japanese business and the state has paid off handsomely. The cost of coal imports for Japanese industry has fallen dramatically in real terms. Figure 3 shows the trend in coking coal (for steel-making) and steaming coal (for power generation) over the last 16 years. Prices are stated in F.O.B. terms - the price for coal loaded on ship at point of departure from Australia.

This is the standard price in Australia-Japan coal contracts. Some of this fall in price can be attributed to the overall appreciation of the Yen against the Australian dollar and other currencies, and the overall trend for technological change to lower the cost of mineral commodities. Even so, the price change is dramatic. Moreover, with Australia as Japan's largest coal source and the Australia-Japan coal price setting the benchmark for the world coal trade, the falling price repercusses throughout the coal industry globally.

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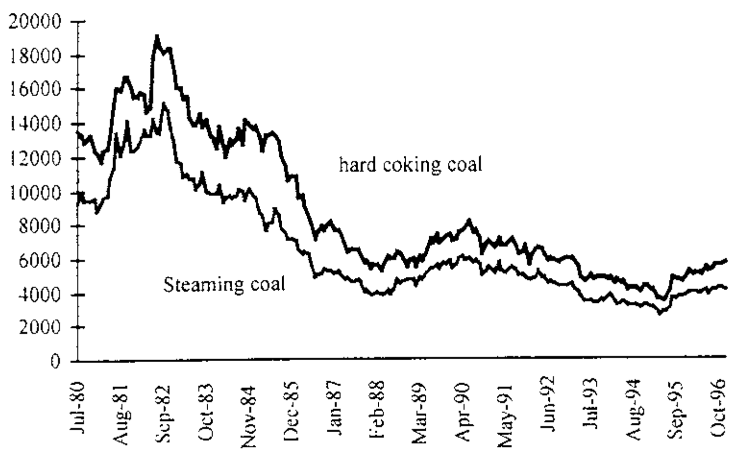
7 'Thermal coal' is another name used to describe steaming coal.

**Figure 3 F.O.B. coal prices in 1990 Yen**




Source: Australian Coal Report

## The Australian Policy Response

Australian policy-makers have long been aware of perceived problems in the coal trade since its rapid development in the mid 1960s. Depending on the mixture of political and economic forces at the time, responses of varying degrees have come forth. Yet policy responses to coal trade issues have taken place in a manner isolated from broader policy debate about industry policy. Moreover, this latter debate itself has resulted in extremely limited policy action.

The Australia-Japan coal trade is clearly a bilateral trade issue. It therefore sits uneasily within a policy approach of the last decade that has been increasingly dominated by the rhetoric of 'free trade' and multilateralism. Further, the distribution of responsibility for the regulation of the various trading and investment practices amongst a number of Federal Government departments has prevented the development of any coherent position. It has even acted to prevent recognition that Japanese bargaining practices in relation to coal prices and investments in coal mining are related issues.

National interest concerns in relation to coal have had various guises. There has historically been a concern to ensure adequate coal supplies for domestic use, with concern about the availability and cost of essential raw materials dominating minerals policy in the early post-World War II period. Exports of iron ore were banned from 1938 until 1960 when the discovery of large deposits in northern Western Australia removed any scarcity concerns (Bowen and Gooday, 1993). In the coal industry, the enactment of special joint legislation by the NSW and Federal Governments established the Joint Coal Board in 1946 which had wide-ranging powers to regulate what was considered an essential industry.

With the opening up of the central Queensland coal fields in the 1960s, the emphasis of national interest concerns changed as the coal industry came to be perceived as both a profitable investment sector and an export earner. Regarding the former there have been policy concerns about the level of foreign ownership; and regarding the latter there has been concern that export prices are 'fair and reasonable'. However, policy weight has only been given to such concerns periodically, and the record of the last decade is one of increasing indifference to even the possibility of 'problems' warranting policy intervention. Moreover, not only is policy attention to coal infrequent, it is also restricted to the issues of foreign ownership and prices - issues which by themselves are not the key to ensuring community gains from the Australia-Japan coal trade, and the industry generally.

## Foreign Ownership Concerns

The concerns about foreign ownership in the mining industry began with the almost inevitable entry of foreign-based corporations as coal and iron ore mining developed into internationally-oriented capital-intensive industries. Concern about foreign ownership in major resource industries reached its height relatively early in the development of the international trade in coal and iron ore; the Whitlam Labor Government of 1972-75 saw a strong policy focus, including attempts to marshal funds to 'buy back the family farm'. Since that time concern has generally been decreasing, though there have been concerns about particular, highly visible, areas of foreign investment such as in tourism, aviation, Central Business District property and the media. The current guidelines for foreign investors (Treasury, 1992) strongly encourage foreign investment, but display some sensitivity to public concerns in the above areas, by imposing limits on market share and corporate control, or by requiring specific approval processes in certain cases. There is now little regulation of foreign investment in the mining industry. Projects involving more than $50m in investment must be submitted for approval, which will be given unless there are compelling national interest concerns.

The nationalist concern about ownership of the 'family farm' rests implicitly on a notion that Australian companies hold the interests of the Australian community at heart, and that foreign-based transnational companies do not. It is not the experience of trade unions in the mining industry that Australian-based companies should be so favourably regarded; Australian bosses have not been noticeably better than foreign bosses and often a great deal worse. But nationalism remains a powerful emotive force in most communities and Australia is no exception; public policy-makers are often compelled to respond to nationalist concerns.

### Price-setting / Market Dominance Concerns

The demand, and pricing, for the products of the Australian coal industry has always been dominated by the Japanese Steel Mills, joined later by the Japanese Power Utilities, leading to periodic concerns about price-setting. These concerns were held most strongly by the Whitlam Labor Government of 1972-75, which introduced a new regime of export price controls using Customs (Prohibited Export) Regulations made under the Customs Act 1901.[8] All mineral exports were subject to scrutiny to

8 It should be noted that, due to restrictions in the Australian constitution which delegate control of land to the States, and foreign policy issues to the Federal Government, the latter can only intervene unilaterally in the coal industry via controls on exports.

ensure fair and reasonable prices before permission to export was granted. The then Minister for Minerals and Energy, Rex Connor, went further and personally intervened in coal price negotiations in Tokyo in 1974 that he considered to be biased against Australian interests (Byrnes, 1994). He succeeded in getting substantial price rises, though at the cost of a cut in the volume of coal sold.

With the demise of the Labor government, export controls were scaled back but not abolished. Their retention reflected concerns of the junior coalition government partner, the (then) Country Party, about getting a fair deal for rural industries. This concern came to the fore in 1978, when Doug Anthony, leader of the Country Party and Minister for Trade and Resources, toughened the application of export controls because of concerns about co-ordinated bargaining depriving Australian producers of fair returns (Bowen and Gooday, 1993). At that time the controls were applied to coal, iron ore, bauxite, alumina, petroleum products, tin, salt and uranium. Anthony's intervention caused tensions within the Federal Government, and the full force of the controls was never implemented.

The view of policy advisers and governments has since hardened against the use of export controls. A theoretical justification for this position lay in the postulation of a 'bilateral monopoly' in the Australia-Japan coal trade. This theory was first proposed by Ben Smith (1977) and by 1982 it had been well-publicised and accepted. The two parties to the coal trade were asserted to be equal, and the fact that Australian producers usually had to accept delivered prices substantially lower than other sellers to Japan was explained as the result of a sharing of the freight savings from Australia's lesser distance to Japan. Separately to Smith, the view also developed in the senior Federal departments responsible for macroeconomic policy that governments had little skill in making decisions about prices and were only likely to distort more efficient outcomes that could be achieved by market forces (Green *et al.* 1992). This view of governments as not managerially competent to participate in market matters is not shared in Japan (Johnson, 1982).

## Coal Policy Since 1983

By 1986 export controls on coal had come to be little used. In that year administrative arrangements were slightly altered - business consulted government prior to contract negotiations to form an agreed view on likely prices, with the reasonable assurance that subsequent price settlements would be rubber stamped (Bowen and Gooday, 1993). There was a brief flurry of contract rejections in 1987 when John Kerin as Labor Minister for Primary Industries and Energy departed from the departmental view of the trade.

Export controls in iron ore were abolished by the Federal Labor Government in 1991 and their use in coal became implicitly defunct. In 1992 a *Coal Industry Policy Statement* by the Ministers for Primary Industries and Energy and for Industrial Relations stated that export approvals would only be withheld "where clear and compelling national interest considerations are involved" (Australian Government, 1992, p28). The criteria are not elaborated, but it was clear that export controls could not be seen as an active arm of policy.

The 1992 statement was focused inwards on addressing problems within the Australian industry. Whilst continuous improvement within an industry is essential to maintaining a competitive position, it was hardly a sufficient focus given the external problems of the industry. The statement was effectively a continuation and strengthening of departmental views that the state had little role to play in the industry. The only aspect of the 1992 policy statement which attempted to address trade issues was an attack on production subsidies in Europe via the Uruguay Round of GATT. However, Australian coal exports to Europe are a minor part of coal exports - less than 12% in 1996 (JCB/QCB; 1997) - and always will be because other coal producers (e.g. South Africa and the USA) have lower freight costs to Europe. Priorities appear to be misplaced when a distant and minor market receives policy attention and the much larger and nearer market does not, despite displaying a number of problems.

The last activity of the Federal Labor Government with respect to coal policy was the commissioning of the 1994 'Taylor Report' to the tripartite Australian Coal Industry Council. The Study of the Australian

Black Coal Industry (Queensland and New South Wales) by Rae Taylor, ex-chief executive of Australia Post and former Secretary of the Department of Industrial Relations, recommended to the ACIC that there be a long term objective of the abolition of export control powers, but recognised that this would need to be based on public confidence in the price formation process. Like the 1992 policy statement, the 1994 Taylor Report was noteworthy for its inability to address the overall dimensions of the Australia-Japan coal trade. They are examples of the narrow policy framework which precludes examination of the link between trade and investment practices.

The Taylor Report was essentially a response to appease mineworkers who struck for a total of 12 days in late 1993 and early 1994 over export price settlements they considered unsatisfactory. Recommendations fell into three broad groups: alleviating concerns about price formation, export market development, and encouraging partnership and performance improvement within the industry.

The first of these appeared to be a limited admission that price-setting arrangements in the industry are opaque. In response to a major trade union submission that co-ordinated trading and investment practices might be acting to disadvantage Australian coal producers and the Australian community (CFMEU, 1994), the report said that the way in which prices were achieved did not create confidence in the process.[9] The Report therefore recommended that the Federal Government establish and publish a price series as a means of improving market information and assisting price formation. This recommendation, if implemented, would represent a minor *increase* in the role of the state in the industry (though the price series could eventually be privately-run). It is unclear at this point if the preparatory work for the price series has survived the arrival of the Coalition Government; certainly it has not yet appeared and its prospects must be considered grim.

The market development measures represented a feeble effort to replicate, in reverse, what the major Japanese buying groups have done

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9 The Report declared, at page 95, that it was unable to determine from the available evidence if there was any link between investment practices by Japanese coal buyers and traders and stimulation of over-supply.

for around three decades: lessen the bargaining power of the other party through diversifying markets. The strategy was doomed to failure because neither the Australian coal industry nor the Australian Government have the financial resources to undertake diversification in the manner undertaken by Japanese buyers. In the past the Japanese buyer effort has included the development of high cost mines in western Canada (Byrnes, 1994) and recent efforts include the development of a new export port in Los Angeles to facilitate more coal exports from the mid-west US states to Japan (JCD, 1994). Under any conceivable scenario Japanese buyers will not only remain the major market for Australian coal until well into the next century but will also play a leading role in price-setting for all Asian markets.

The final area in which the Taylor Report made recommendations - encouraging partnership between employers and workers, and performance improvement - was worthwhile. However it was hardly sufficient or relevant in addressing overarching trade problems.

Federal Labor's declining policy action in coal has been continued by the current Coalition Government. The incoming Government attempted to abolish coal export controls shortly after being elected in 1996 but was prevented by doing so through lack of a majority in the Senate. It finally succeeded in May 1997. The spot price for coal subsequently fell dramatically as buyers took more aggressive bargaining positions in the face of an implicit declaration that the Government would not intervene in the industry, regardless of potential or actual losses (ACR, 1997).

In 1997 the Coalition Government issued *In the National Interest*, a White Paper on Foreign and Trade Policy. This was followed by a *Resources Policy Statement* in 1998. The former is concerned with the broad spectrum of issues involved in Australia's relations with the world and so cannot be expected to have much specificity with regard to coal. The latter has no such defence. Neither have anything specific to say about Australia's largest export industry. The latter document confines its discussion with regard to coal to the issue of industrial relations - a perpetuation of the broader view of the conservative parties that labour market 'reform' and deregulation will solve all industry problems. There is some minor shift in emphasis towards greater use of bilateral trade negotiations - perhaps reflecting the preferences of Tim Fischer, the

National Party Deputy Prime Minister. But there is no discussion of any particular focus - on problems or potential advantages - which might benefit from bilateral efforts. The two policy statements seem to reflect a desire by Government in Australia to remain ignorant of the forces at work in the coal industry; to have knowledge would require action or at least an explanation for inaction.

## Institutional and Conceptual Impediments to Alternative Policy

In Japan there are just two government departments which have primary responsibility for trade and industry policy. The Ministry of Finance supervises the Fiscal Investment and Loans Program and the activities of the Export-Import Bank. The Ministry of International Trade and Industry is responsible for facilitating the co-ordination of industry and administrative guidance. Together these two agencies are capable of dealing with Japanese business in all aspects of their international and domestic operations.

In Australia there is a sharp division between senior macroeconomic policy departments such as Prime Minister and Cabinet, Treasury and Finance, and the 'line departments' such as Primary Industries and Energy. This results in different aspects of the coal trade relationship being dealt with by different departments. Whilst there is a Department of Foreign Affairs and Trade, its focus is almost exclusively on multilateral trade issues (Jones, 1994). It has little interest in the vagaries of the Australia-Japan trade. The administration of export controls went from the abolished Department of Trade in 1987 to the Department of Primary Industries and Energy (DPIE) which therefore handles most day-to day issues with respect to the trade.

However, many of the issues examined in this research are not dealt with by the DPIE. Foreign investment is the concern of the Foreign Investment Review Board (FIRB), which is within the Treasury portfolio. The administration of taxation and transfer pricing issues is handled by the Australian Taxation Office, and policy issues arising from them by the Treasury. Trade promotion is handled by Austrade, which is responsible to the Department of Foreign Affairs and Trade. Austrade sees its role purely as a promotional entity and administrator of export facilitation programs. It is not a trade negotiator nor a trading house. The Department of Industry, Science and Tourism (DIST) supervises the Export Finance and Insurance Corporation which provides more direct assistance to emerging exporters. The DPIE also engages in some industry promotion activities.

Issues of competition and fair trading practices are dealt with at a national level through the Australian Competition and Consumer Commission, under the control of the Treasury. At the international level fair trading practices are handled by the Department of Foreign Affairs and Trade. Industry policy is normally the province of DIST but workplace reform components are handled by the Department of Workplace Relations and in some cases by the Department of Employment, Education, Training and Youth Affairs.

One example of the normal micro focus of how the system works is the mechanism whereby foreign investment proposals are reviewed by the FIRB on an individual case basis. The FIRB probably has a capacity to address transfer pricing implications in proposals that would result in vertically integrated industry. However, there is no capacity to assess the impact that the co-ordinated taking up of minority stakes in the Australian coal industry by coal consumers, together with concessional financing and the selective awarding of long term contracts, might have in stimulating supply capacity over what a competitive market situation would provide.

In short, it is not the role or the responsibility of any particular department of government to analyse or respond to the entirety of the Australia-Japan trading relationship in coal. The big picture (otherwise known as macroeconomic policy) is constructed by the senior policy departments as a remote one that has little to do with the sorting out of the policy issues in particular industries. The prevailing view which has come to the fore over the course of numerous reports by the Industry Commission (now the Productivity Commission) is that governments should concentrate on getting the macroeconomic policy settings correct and leave industry development to the private sector. Although the Industry Commission does not determine policy, its position is instructive. With such antipathy to national industry policy by the dominant economic reform advisory body it is no surprise that a strategic industry and trade development approach advocated by the ACTU has been marginalised.

The final outcome with respect to coal is that senior departments do not have the conceptual framework that would enable them to recognise and deal with the type of co-ordinated arrangements employed by Japanese buyers that have reduced the benefits of the international trade to the Australian people. The sophisticated meshing of numerous trading and investment practices by coal buyers and traders are all details of the coal trade which it is not the responsibility of a line department to deal with, and which senior departments choose not to deal with.[10]

One factor which has been especially detrimental to the development of an effective policy response is the Department of Foreign Affairs and Trade's conception of its role. Even if the Australia-Japan coal trade is conceived as a functioning case of bilateral monopoly, there would be seem to be a rationale for DFAT to maintain an active bilateral trade role. Instead, it has pursued a pure multilateralist approach as the solution to Australia's trade problems, with the result that much effort has been put into securing access to protected European coal markets, but little effort in the achievement of fairer terms of trade in the major market. As Jones (1994) has stated, exclusive reliance on multilateralism is the ultimate case of 'picking winners'; it is relying on a theoretical position which has not yet been proven to be a success in world trade.

Finally, and most importantly, there is the issue of external pressures on Governments to act. Negotiating over investment, pricing and trading concerns in the coal industry with the Japanese state and industry is a tough task requiring a constituency bringing substantial pressure to bear. There is only some trade union and community pressure on this issue; capital is largely unwilling or unable to advocate an interest. This is

10 If the problem were simply one of a multitude of departments, the administrative solution would be Inter-Departmental Committees (IDCs) which are already used with reasonable effect where there is a desire to do so. But this solution is not implemented with regard to coal because of the prevailing conceptual view of the industry.

because of the fragmented nature of capital in the Australian coal industry; there is substantial participation by Japanese coal buyers and traders (around 20% of total production) and by other multinational capital. The considerably divergent interests of capital in the industry prevent there being any 'industry view' on the matters raised here (Colley, 1997 and forthcoming).

## A Mistaken Policy Stance

Japanese business and government share an explicitly-acknowledged strategic concern with regard to the coal trade, and co-ordinated activity is undertaken via trading and investment practices. These practices are consistent with the deployment of trade and industry policy by Japanese coal buyers, trading companies and the Japanese state on a co-ordinated basis that has been intended to stimulate supply and, through the achievement of over-supply, depress prices.

The Australian public policy response pales by comparison. Coal policy has been handled solely as a trade issue without consideration of the implications for overall industry development, and policy responses have been further constrained by their limitation to foreign ownership concerns and the use of export controls in monitoring export prices. The use of such controls has waxed and waned since their formal introduction in 1972, and their recent abolition by the Coalition Government was the final point of a trend established by the previous Labor Government. The only constraint on the ability of Japanese business and government to continue their dominance of the terms of the trade is the relative decline in Japan's economic importance in the region as other Asian economies engage in rapid industrialisation and growth (now more constrained since the crises in various Asian countries in 1997-98).

In one of the stronger attacks on the naivety of blind reliance on multilateralism and free trade as the universal panacea to trade problems, Daly (1993, p83) has said that Labor's total focus on these concepts relied on the hope that:

> it will be rewarded for its unsullied purity. In a sense such attitudes leave Australia naked and exposed to the world, and one day we will wonder why we have been raped.

The evidence here does *not* indicate that the Australian community has been 'raped' in the coal trade with Japan. Indeed, given that the pattern of Japanese trading and investment practices described is so overwhelmingly superior to the practices deployed by Australian governments and producers, the question is why the coal mining industry has not been taken advantage of more fully. It would appear that the trade has been 'managed' by Japanese industry and government agencies to give the Australian industry a barely creditable outcome.

## Alternative Responses?

Possible alternatives to the policy debacle described here are not found in any of the traditional left shibboleths of central planning, nationalisation or statutory marketing authorities. Alternative approaches need to be a great deal more pragmatic, and to start from an in-principle position that the Australian community needs to maximise its returns from the use of its natural resources if it is to have any chance of achieving or even maintaining living standards and employment into the next century.

Towards this end it is possible to deploy quite different and possibly hybrid approaches that could contribute to a much better result for the Australian community. In the 'coal price' campaign run by the Construction, Forestry, Mining and Energy Union in 1994, two different policy approaches were put. The first was in line with the economic rationalist and so-called free market predilections of the Federal Labor Government and its departmental advisers. It called for enforcement of a competitive framework in the Australia-Japan coal trade which would have proscribed or penalised the co-ordinated investment practices of the Japanese steel, power and trading companies, and have made illegal the co-ordinated trading and bargaining practices which are also dominated by the buyers and inter-linked with investment practices. Under a genuine competitive market framework the strong comparative advantage that the Australian community has in its coal industry would produce substantially better profits and thence community returns.

The alternative approach would seek to emulate the co-ordination and co-operation between government, business and other stakeholders that has characterised the trade and industry policy approach in Japan. This amounts to an attempt to 'even up' the two sides to the trade or simply to constitute the Australian coal industry as a 'side' at all. Elements of such an approach would have included the establishment of a small unit within the DPIE or DFAT to exercise not only export control powers but also to analyse and make recommendations with respect to overall trading and investment practices. Recognising that the industry is and will continue to be dominated by big business, much of which is transnational, this measure would be complemented by a series of incentives and penalties designed to induce a co-operative approach amongst coal producing companies. Economic rents from the industry could be maximised rather than dissipated through a cut-throat selling competition dominated by monopolistic buyers. [11]

In the 1994 coal price campaign the latter approach was promoted by the union with the exhortation to the coal companies that they 'play as a team because jobs depended on it'. This was an attempt to popularise in sporting terms what was otherwise a complex argument about trade and industry policy. It generated significant public support in the regions where it was deployed and was, in the union's view, a major contributor to a temporary lift in the bargaining performance of the Australian coal producers which saw a billion dollar turnaround in export earnings from the industry in 1995-96.

However, aside from a decision to improve clarity in the price-setting process by publishing a price series, there was no substantive shift in the position of the Federal bureaucracy or the Labor Government with regard to the coal trade. Thus far it appears that the current Coalition Government will continue (and possibly increase) the 'look mum, no

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11 In 1988 and earlier, the union called for the establishment of a 'National Coal Authority' which would have represented a much larger and more direct role for government in the operations of the industry. See Draper and Lee (1988).

hands' approach to an export sector which matters more to the Australian community than any other.

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