**I'm not a protectionist, but …**

*(Article by Saul Eslake, Director of the Productivity Growth Program at the Grattan Institute, published in the Melbourne* Age*, and in the online edition of the* Sydney Morning Herald*, on Wednesday 31st August 2011)*

The online *Urban Dictionary* defines "I'm not a racist but …" as "something an idiot says before making a comment that proves that the idiot is, in fact, a racist".

I'm not going to be so arrogant or rude as to insinuate that anyone of the surprisingly large number of people who have prefaced their demands that the government 'do something' about 'the crisis in manufacturing' with the phrase "I'm not a protectionist, but …" is an idiot. It's entirely understandable that the owners of managers of manufacturing businesses, and union officials representing workers employed at manufacturing businesses, are concerned about their future.

And to the best of my knowledge, no-one in a position of influence has seriously suggested that Australia should start imposing high tariffs on imported goods, in the way that we did for much of the 20th century. That form of protectionism forced Australian consumers to pay higher prices than they would otherwise have done, for a narrower range of what were often poor-quality goods, in the name of 'protecting' jobs (at what were often foreign-owned businesses) and of ensuring that Australia 'made things', and it's been rightly rejected by the Government.

But there's not much difference between that traditional form of protectionism and the idea that businesses should be forced to buy Australian-made products in preference to imported goods that are cheaper, or which more readily meet the purpose for which they are required. At various times in Australia's protectionist past, governments forced Australian businesses to buy locally-made inputs, even though they could have obtained cheaper, more suitable or better-quality products from abroad. And of course 'quotas' (limits on the amount of particular products that could be imported each year) were widely used during the 1950s, and again in the late 1970s and 1980s, to force Australian consumers to buy Australian-made cars, clothing and footwear, more often than not at higher prices than they would have paid for equivalent (and usually better-quality) imports.

Needless to say, people who are in favour of forcing Australian consumers or businesses to pay higher prices for a narrower range of often poorly-made goods never couch their ideas in those terms. Forcing 'struggling' Australian households to pay higher prices for kids' clothes, or businesses 'doing it tough' to pay higher prices for things they use in their production processes, that would be a hard sell. But 'protecting Aussie jobs', who could object to that?

There's no denying that Australia's manufacturing sector is experiencing particularly difficult trading conditions at the moment, as a result of the persistently strong Australian dollar, rising input prices, heightened competition from other countries, or weaker domestic demand. Manufacturing employment has declined by almost 10% since the onset of the global financial crisis, and that was before the announcement of some 1,400 job losses at Bluescope Steel. Of course manufacturing isn't the only sector experiencing significant difficulties: Qantas and Westpac have also announced big job losses in recent weeks. But somehow job losses in manufacturing always seem to cause more wailing and gnashing of teeth than job losses in services sectors.

The difficulties faced by the manufacturing sector are, in part, a by-product of the 'mining boom' that has been gathering strength over the past seven or so years, apart from a brief interruption associated with the global financial crisis.

And if it were really likely that the 'mining boom' will turn out to be a 'flash in the pan', there might well be a case for somehow seeking to 'hold it back' in order to minimize the adjustment pressure on other sectors of the economy.

However, it's much more likely that the 'mining boom' will last at least until the end of this decade, and possible into the early 2030s. If the history of other countries is any guide, China won't begin to move out of the commodity-intensive stage of economic development associated with urbanization and industrialization (which typically begins when per capita income exceeds US$2-3,000 in 2011 prices, and continues until per capita income exceeds somewhere between US$18,000 and US$25,000, depending on the distribution of income) until 2019 at the earliest, and possibly not until 2024. India, which only entered this stage of development in 2007, won't begin to exit it until 2032 at the earliest.

And although there are many things which could alter that timetable, any decision by Australia to 'hold back' the rate of growth in our own resources sector isn't going to be among them. If we were to decide to restrain the speed with which the mining sector expands, China and India would get the resources we were unwilling to supply from somewhere else, possibly at a higher price (at least initially), and we would forego for all time the income we would otherwise have obtained.

Moreover, over the time scale that the 'mining boom' seems likely to last, our own history suggests that there will be an ongoing decline in manufacturing in any event, so that attempts to preserve manufacturing jobs by imposing higher costs on other sectors of the economy or on consumers will only delay, rather than prevent, inevitable (and from the standpoint of overall national income desirable) structural change.

It's an inescapable truth that for as long as the share of Australia's GDP generated in the mining sector is larger than the average for other 'advanced' economies, and for as long as Australians want to spend a similar share of their incomes on services (which are inherently less tradeable than goods) as people in other 'advanced' economies, manufacturing is going to be a smaller share of GDP in Australia than in other 'advanced' economies. The sum of agriculture, mining, manufacturing, construction and services as a share of GDP can't exceed 100%.

The best thing that the Government can do to assist businesses and workers in the manufacturing sector, or indeed in any other part of the economy that is on the wrong end of the side-effects of the 'mining boom', is (as the Productivity Commission pointed out in the context of the retail sector) to assist them in improving productivity – and hence in maintaining their profit margins in the face of adverse (for them) influences such as a strong Australian dollar.

The Government should also be seeking to extract the highest share it can of the proceeds of the exploitation of Australia's natural resources, without deterring the investment required for those resources to be exploited, and using the revenue flow over time to enhance Australia's productive capabilities, through well-targeted investments in infrastructure and skills formation.

Seeking to preserve, as if in aspic, the composition of Australian economic activity and employment as it was in some year gone by is not the way to ensure that Australia makes the most of the once-in-human-history opportunity presented to us by the industrialization and urbanization of the two most populous nations on the planet.

*(Saul Eslake is a Program Director with the Grattan Institute. The views expressed here are entirely his own).*