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PRIME MINISTER

**TRANSCRIPT OF THE PRIME MINISTER, THE HON P.J. KEATING MP
QUESTION AND ANSWER SESSION FOLLOWING LECTURE TO THE
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Q: I notice when you were talking about the focus of Australian trade you spoke of the Asia-Pacific and including the United States, but India was not included. Now, India is a country of 600 or 800 million now with projections to be quite possibly the fifth largest economy in 20 years, you did not refer to that, is that intentional or ...

PM: Well, India is not a part of APEC, not that the talk was solely or exclusively about APEC. I think there are substantial opportunities in India, but I think that it is a market, probably, we have been a bit late in accessing and one can't deduce from that that the opportunities have gone. I'm sure that is not true and some Australian companies are drifting there, as you know, one of our banks has got a major banking facility there. But, it is only, I suppose, in recent times that the Indian economy has started to really open up and that is probably where the interest is starting to come. We have had Indian Prime Ministers and Ministers coming to Australia periodically and periodically we have had these commitments and declarations of interest in one another, but they tend to fade away and change as Prime Ministers change. Therefore, to get the consistency of interest there is, I think, quite a challenge and would require a very large effort on behalf of the government and on behalf of the private interests in this country. It just seemed to me that for as far as I am concerned the more immediate and obvious place to start this sort of effort in the region was with Indonesia which is strategically more significant to us and one which, I think, politically had languished over the years.

So, there has been that focus, the focus on ASEAN because it is part of ASEAN and we trade with Singapore and Thailand et cetera and we have got the big established trading linkages with Japan, Korea and increasingly with China. And, the fact that APEC in some respects defines them too has, if you like, sharpened our focus. But, it is not to say that I don't think there are opportunities in India or that we won't be exploiting them. But, I do think that working closer to home as we are

and working within the framework of APEC is a case of prioritising one's effort I suppose.

Q: Prime Minister, I wonder if we could publicly have a response from you to Professor Fitzgerald's response to your speech?

PM: You mean the last part of his remarks about east Asia?

Q: I mean the remarks about the potential for new and alternative groupings to APEC to appear?

PM: I think what Stephen was speaking of was at some point an emerging confidence in Asia about Asia itself. About an Asian Asia. That is, one where there is a notion of some perpetuality in economic activity, that is, self sustenance about their economic activity within the area we broadly describe as Asia and a more intuitive understanding of culture, cultural differences, even cultural sensitivities within an Asian context. I think that is entirely possible and to some extent that has always been there. APEC is not there because it is the first thing we thought of. It is there because we don't want to see the United States stay at home with NAFTA, we don't want to see the United States become more inward looking, we don't want to see it's Latin agenda overtake its international ambitions and to keep it more strategically engaged in Asia means that we don't see the world drop into three blocs - Europe, the Americas and Asia. So, there is a sense to APEC, it marries the United States to East Asia, it keeps the United States from going protectionist and unilateralist and it gets them involved in a multilateral way, it extends that strategic cover for Japan which keeps Japan away from the development of its own strategic force which, I think, keeps the temperature down in North Asia and at the same time APEC gives Japan a chance to rebuild and change its political structures and find a new place for itself in Asia and the Asia-Pacific. Whereas, I think, an exclusively Asian structure today would subjugate Japanese interest, or attempt to, which is not good for Japan and it is not good for us and it is not good for the United States.

Therefore, APEC fits the bill, I think, in terms of the economic imperative for the Asian economies, the need for strategic peace in North Asia, keeping the US out of home and well and truly on the streets is a very important thing, I think, to be doing at this point and before there will be any notion of an emerging group as Stephen sees it, will be a time further down the trail when China's power as an economic and military power will be greater. Such a region will have a very heavy influence on China and one couldn't be sure that everyone else is going to sign up to that. I'm quite sure the Ambassador would be quite happy for people to be more influenced by China over time which is a completely reasonable national aspiration.

So, with Japan, we often say it and it is worth saying again, Japan is Asian, but it is not part of Asia and before it signs up to be part of Asia there is going to have to be a lot of political change in Japan and it's

not here yet. The very interesting thing is the ... Stephen referred to the Malaysian proposal which has a lot of the antecedence about it that APEC has. But you see Japan won't touch it, because for the reasons, I think, that I am saying and that is that Japan wants to keep US strategic cover and US engagement militarily and economically in the region, though, I am sure it has sympathies with the general proposition which Malaysia has put.

Q: Prime Minister, this is not so much a question as an addition to your comment on India. That is, that now as you said the doors are being opened, Austrade is in the process of establishing three trading places in India for the first time. As you know it all costs money and fortunately you gave me a very generous minister in Bob McMullan and when we submitted to him the need to be represented more directly in India he agreed to meet the bill. But this is happening right now, so I thought you would might like to ...

PM: Interesting for the audience and for me.

Q: Prime Minister, I am delighted at your enthusiasm for APEC which we are all familiar with. As you know we invented it at our research school.

PM: Everybody says that.

Q: That's right, but I think Ross Garnaut and Peter Drysdale would make a claim to it.

PM: No, I think the people that make a claim to it ... I could tell you where APEC came from. It came from Sandy Hollway in Bob Hawke's office and it came from someone in the department. That's where it came from and the Heads of Government meeting came from me and that is the end of the story.

Q: As a professional historian I find it very interesting to watch history being created. The question I was going to ask was when we look at APEC, of course, we are all inclined to a great enthusiasm and optimism. But, there are those who look at our region and see other more worrying things on horizon in particular there are some people very concerned that about extensive defence modernisation programs in the region, whether or not one feels this really constitutes an arms race. Certainly there are offensive capacities being built and I wonder if you would like to speak for a few minutes about your picture of the strategic environment of our region over the next few years?

PM: That is a very tough subject, I think, to be crystal ball gazing about or to be talking prescriptively about how that will change. I don't find it too difficult to understand that with the cold war, bi-polarity taken away and some of the regional tensions becoming more manifest that people take some defensive steps in terms of their own strategic capacity. It doesn't surprise me. We are seeing some substantial expenditures in

the area, but again, where it matters in North Asia the Japanese political system is largely confining its interests again to a self defence force. It still spends a substantial proportion of its GDP on it, but again, it is a very clear political commitment to maintaining the force as a self defence force without an offensive capability. China is spending a substantial proportion of its national income on modernisation of its defence force. This, countries generally do. There is some concern in the region about the extension of Chinese maritime capacity. I'm sure everyone will continue to keep an eye on that. The nuclear capacity of North Korea is a matter of concern, but again, I think the agreement which has been brokered with the United States will go a substantial way to coming to terms with that and I think the other sub-regional expenditures within ASEAN and those other places are such as I think probably most countries with any financial capability will choose to upgrade their armed forces and to select modern and appropriate equipment. I think the change in the capacity of countries in this region to improve their military capabilities is, in fact, a function of their wealth. As their wealth has risen so has their capacity to do things. Not everyone has done it well as you know. There is a lot of junk around the world and the thing not do is buy junk because in the end if what modern conflicts are showing us is that it is the razor's edge that matters. But, because the strategic environment is so quiet, I think, people can see the effective life of the stuff through and they'll come out the other side during a phase when, I hope, Australia will be a substantial supplier of defence products.

So, I don't find a remarkably uncertain or inexplicable development on our hands.

Q: Prime Minister, I just wonder if I could ask you a question about the forthcoming APEC summit. There was a report that China has rejected the notion that APEC should promote binding agreements that it would only agree to a general goal rather than any binding agreement. My question is in two parts. Do you see the APEC leaders producing a binding agreement or merely a loose declaration of a general goal and what is your position, in principal, on the debate about whether APEC liberalisation should be on a Most Favoured Nation (MFN) basis or on a preferential basis?

PM: The very nature of the APEC meeting is that it is unstructured - that the leaders meet themselves without officials. And if one looks at the success in Seattle with the adoption of a second meeting therefore giving the APEC leaders some form as a forum, and the adoption of trade investment, investment agreements, trade facilitation issues et cetera, I think, the lesson from that is that the leaders when they get together, if they wish, can get things done and that is what I hope will happen at Bogor.

Again, this will be a very fluid thing and it will be fluid right until the moment it meets. It is a most ambitious undertaking. Two years ago, let me tell you this, I first raised the notion of the APEC area meeting

at heads of government or leaders level with George Bush when he came to Australia on new years day 1992. That is to answer my friends question here, that is where it started. I then opened it up with President Soeharto, with President Kim Young Sam and others around the region. That was just a couple of years ago, but already we have got it to the point where we have been able to have a first meeting at President Clinton's invitation where it has gone to a second meeting at the behest of President Soeharto and where we have already adopted a substantial trade liberalisation agenda. Now, this is taking APEC a long way in a very short time, but, I think, Australia has been hungry for change and ambitious for it. We have supported President Soeharto in his attempt to move the agenda to trade liberalisation. There is now quite a deal of support for that. One of the things that surprised me is how quickly this has been internalised in Australia. People have stuck that in their pocket as though it is a fait accompli: 'oh that's that bit done, what's next?' The sort of rampant naivety of this and I am not suggesting this is your view Greg (Sheridan) because it isn't, but the rampant naivety of this is ... I mean it is a terrible thing in the Australian media that everything has such a short span of attention now, that serious and complex issues are dealt with quickly: one night on television, a follow up story in the day's paper - done - that's it. Well, big issues like this just go on and on and I hope that we can get to a declaratory position at Bogor. At this stage, it looks like there is every possibility that we will, but let's get there first before we accept it and internalise it and take it as part of the commercial wall paper of the region.

So, there is that about it. When leaders meet and decide something like this, it is not a loose or waffly declaration, it will mean something. When you sit half the world's population and half the world's GDP down and they agree to something, what greater authority needs to be brought to bear to make it firm? Now, what happens then in its facilitation is a different question, but that's an entirely subordinate question to the primary one about the doing of it in the first place.

There are some who in this country who argue about this question about MFN (Most Favoured Nation) and preferential, that this needs to be decided first before you can make any declarations. Well, none of these people have ever been around cutting tariffs. I'm the only one in the Australian debate still around who has been in the tariff cutting business and it is a pretty tough caper to be in let me tell you. Therefore, the observation I would make is that when one looks at the very high tariff levels in Asia and the non-tariff barriers, the task of getting them down is so great that what I say is let's get cracking on the task, make sure the task whatever we do is GATT consistent and then worry about whether a particular country wants to extend the preference or not. That is, whether it's MFN or its preferential. But, you would swear blind the way some people speak, we have already got the tariffs down and we are now deciding whether we are going to let the world in to have a crack at it, have a piece of it or are we going to keep it to ourselves. At the moment, the task is untouched. So, I

think the first thing is to in the minds of the APEC leaders, understand that the velocity of trade and investment will be improved by lower tariff and non-tariff barriers, to declare that they wish to bring them down on a phased basis over a period of time and then the third task is to get on and do it and including in that whether in fact countries want to extend the preference outside or to contain it.

Now, for my part, I have said tonight and let me repeat. I don't think that there is any value for us in seeking to develop a bloc in Asia because that is the thing we are trying to avoid. The whole point of putting the Americas together with Asia in APEC is not to produce a preferential area. But, not all countries will take that view. Well, that's all right, the world isn't simple, but some of this academic debate that says we've got to tidy that up first before we can move on with the primary debate is naive and immature in my view. This is a real world tough issue and it is going to take a long time to work our way through, but the end result can be a massive improvement in wealth in this region and we have just got to take the chance and go and do it.

Q: One of the hallmarks, I think, of your Government and Prime Ministership has been the opening up of trade and links with Asia and so on. I think that has been something which is very desirable, but one of the pieces of legislation which has been passed has been the foreign investment funds legislation or FIF, I think, the intention that, quite admirably, is to try and capture the Bonds and Skases of the world, but the way that it has been implemented has been to, on the ground, to greatly restrict the range of choices for ordinary Australians to invest in overseas markets and particularly the Asian markets and I wonder if you'd like to comment. I don't know whether you are aware of that, but the reality is that we now have, the business that I am involved in, an enormously lesser choice available to us as a result of that legislation and I think that the costs of it are far greater than the government would ever earn in terms of tax and whatever was intended to be achieved by the passage of it.

PM: Essentially it was a tax efficiency thing. I mean, the alternative is to run a foreign tax credit system where you bring your dividends home upon which the local tax has been paid and then you top it up to the Australian corporate rate. So, if you pay whatever it is, 18 per cent in Hong Kong or where ever it might be and you bring the dividends home you top them up to 33. Now, the problem for us was that if you look at the OECD area, you have Australian companies in Germany, in France, in Britain running a European business say, where in one country the corporate rate is 36, the rate in another country is 35, in another country it is 38, so there is an enormous accounting task bringing these dividends home and accounting for it if there isn't to be any primary tax paid here. So, what we said was let's make this simple, we'll have a white list, if you bring dividends home from countries on the white list we will assume that the company tax has been paid there and you don't need to top it up here. But, if it is not on the white list it is obviously on the back list. The white list extends

through all of the OECD area, that's the 24 member states of the OECD, and a large part of Asia and we also have an active income test and a passive income test so if you are a hole-in-the outfit in Hong Kong with your name on an accountants door, you don't pass the active income test, but if you are like Pioneer Concrete and you are making concrete in Hong Kong you do pass it. So, even though it may be regarded as tax haven, we don't require a topping up to the corporate tax rate for the dividends here if you are actively involved in that country. But, if people are involved there because it is simply a tax haven or it is low taxed then if it is not on the white list we tax you on an accumulations basis. That is, not even on a distribution, we tax you on an accumulations basis.

If you ask most Australian companies are they better off with that system than a foreign tax credit system, I'm sure they'll answer they think they are better off with that system. Let me say in some places - take Indonesia - where they have specific tax holidays for tax free development zones or in Malaysia where there are development zones, under our double tax agreements we recognise tax sparing. In other words, we regard as legitimate for the purposes of development of those countries, income earned in those particular parts which are free of tax or have very low tax rates. So, if you go through the white list, all the OECD, a large part of Asia, no problem about bringing dividends home. If you are in a tax haven and you can pass the active income test, no problem. If you are in a developing country which has got a development preference, if we give it tax sparing under our double tax agreement you have got no problem either. That means that if you have got an active business somewhere and you believe that the country should be white listed or alternatively that you can pass the active income test, then I don't think it is much of a problem. But, there is no doubt there are some countries that are not on the white list and people can still operate there, it's just that they are taxed on an accumulations basis as they earn their income and they'll get assessments from the tax office as that income is declared.

The alternative is to junk the system and go back to a foreign tax credit system. For major public companies accounting for tax variations of 1 or 2 or 3 per cent across say Europe, or even around this part of the world is, I think, too much of a burden. Largely I thought this system was largely working not too badly. I'm not saying that your example is not without some justice, it may well be, but in all tax things there is no perfection. You have got to make some rule of thumb issues and the rule of thumb in making this work is a white list and if you are not on the white list, well, you know what list you are on.

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