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Foreign Economic Policy Making in Australia: Analytical Framework and the Role of the State

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I. Introduction

In November 1996, the annual Asia Pacific Economic Cooperation (APEC) Ministerial and Leaders' Meetings were held in Manila and Subic respectively. The main product of these meetings was, of course, the "Manila Action Plan for APEC 1996" (MAPA '96) which included the Individual Action Plans (IAPs) of all members for trade and investment liberalisation. Following the Bogor Declaration in 1994 and the Osaka Action Agenda in 1995, the APEC trade and investment liberalisation/facilitation process had entered the actual implementation stage.

While the contents of the IAPs, which represent the level of commitment to the APEC liberalisation process, varied significantly,[1] and while it is not readily possible to measure the "comparability" of each IAP, the overall evaluation of the IAPs seems rather auspicious. The bureaucratic staff and ministers of each member involved in the making and gathering IAPs resolved that it was appropriate for the first year to collect IAPs from all members in the same format.[2]

APEC members agreed to implement their IAPs from January 1997. It was also agreed that, in the future, members would present revised IAPs to the annual Ministerial Meeting. This "rolling" process is planned to be long and continuous and, considering that the contents of IAPs were greatly diversified in 1996, the process will have to overcome difficulties if the APEC liberalisation process as a whole is to be successful. Members will need to respond to "peer pressure" from others to deepen and widen their commitments and, at the same time, they will have to accommodate domestic policy demands that may run counter to liberalisation efforts. For APEC members, the rolling process is a balancing process between international and domestic pressure. Thus, it is becoming more important to understand the policy making process of individual members, and factors affecting policy outcomes.

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[1] The complete document of MAPA '96, including all members' IAPs, can be downloaded from the WWW homepage of the APEC Secretariat (http://apecsun.apecsec.org.sg/).

[2] This view was put by a staff member of the APEC Promotion Office, the Ministry of International Trade and Industry, Japan, at the seminar organised by the IDE APEC Study Center, 18 December 1996. Yamazawa (1997) also suggests that IAPs of 1996 are good as a first step, considering that some of the developing economies such as Chile, China, Indonesia and the Philippines made greater commitment than they did for the

I wrote a working paper last year that deals with foreign economic policy making in Australia (Okamoto 1996). “Foreign economic policy” is defined here to include government action that has an impact on other countries’ economies through the production and distribution of goods and services, and the movement of capital (including foreign direct investment) across national borders. It is utilised by governments to modify what would otherwise be the way that goods, services and capital would flow if a completely free market situation prevailed. It includes not only a state’s policies on multinational or bilateral negotiations such as the General Agreement on Tariffs and Trade (GATT) and other trade agreements between countries, but also policies of export promotion, import restrictions through tariffs or quotas, and deregulation of foreign currency exchange and those investment policies that can be decided and implemented unilaterally (Destler 1980:7, 129-33 and Cohen 1988:3). Thus, the change in foreign economic policy of a state means either: more restriction on international flows of goods, services and capital than the current level, or; deregulation of those flows to secure the operation of a “freer” market.

Australia departed from its traditional protection policy in the 1980s and has become one of the champions of free trade. It has also been an active promoter of the APEC trade and investment liberalisation process. My 1996 paper attempts to explain the major factors that have influenced foreign economic policy making in Australia since the 1980s. The factors examined in that paper are: the international economic environment; interest group attitudes and their relations with the government; results of politics within the government, and; structure of the bureaucratic decision making process.

This paper will concentrate on establishing a general analytical framework for the foreign economic policy making of middle-sized states like Australia. Then, by using parts of this framework, change in the international economic environment and the Australian state’s role in foreign economic policy making will be discussed.

II. The Analytical Framework of Foreign Economic Policy Making

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Uruguay Round and it was only 2 years since the APEC leaders declared their intention for trade and

In the study of international relations, the manner in which one state forms and implements its foreign economic policy has been widely discussed. Many have argued, from different angles, that a distinctive line cannot be drawn between international relations and domestic politics because they are so interrelated. According to this view, both external and domestic factors matter in foreign economic policy making. How, then, given this prevailing agreement, can the changes in Australia's foreign economic policy since the 1980s be approached?

First, the international system/environment can be taken as a primary factor, or an independent variable. The term is defined here as to mean the distribution of power and economic wealth among states, and the spread of dominant ideas for policy practices over states. It is inevitable for small and middle states that international environment factors influence their foreign economic policies. In fact, no state is totally free from what others do in this era of complex interdependence.[3] The degrees of external influence on each state vary, however, depending on the political and economic strength of a state. Australia, being a middle sized state in terms of both its political/military capability and the amount of international economic transactions, cannot create a favourable environment by itself. In most cases, Australia has to react to, rather than control, changes in the international environment.

Second, within the range of policy options, which are set by the international economic environment, governments attempt to realise stable and sustainable growth of, and full employment in domestic economies. The need to adjust domestic industrial structure, again usually induced by changes in the international environment, demand changes in foreign economic policy, too. Governments try to decide and implement economic policies according to contemporary domestic necessities and industrial structures, and for those necessities and structures perceived to be desirable in the future. However, why governments take up certain policies at certain times cannot be fully explained by changes in the international economic

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investment liberalisation in Bogor.

[3] The development of economic interdependence has created resources of new, non-military power. The new power of a state depends on its sensitivity and vulnerability. "In terms of the cost of dependence, sensitivity means liability to costly effects from outside before policies are altered to try to change the situation. Vulnerability can be defined as an actor's liability to suffer costs imposed by external events after policies have altered" (Keohane and Nye 1977:13). Less sensitive and vulnerable states gain power over more sensitive and vulnerable ones. Keohane and Nye called this model "complex interdependence".

environment alone. The International environment does set limits for a government's policy options, but there must be more than one option at any given time. This is why the policy decision making process, such as politics within a government, bureaucratic procedures, and the policy ideas of participants in the process, should be closely examined.

Third, the demand of a society for a certain set of economic policies should be brought into analysis. More or less, governments in power are sensitive and responsive to the pressures of interest groups from which they get their political support. Australia managed to change its traditional protectionist policy during the 1980s and this inclination for liberalisation is continuing in the 1990s. There must have been changes in the attitude of traditional interest groups and/or their relations with the government over this period.

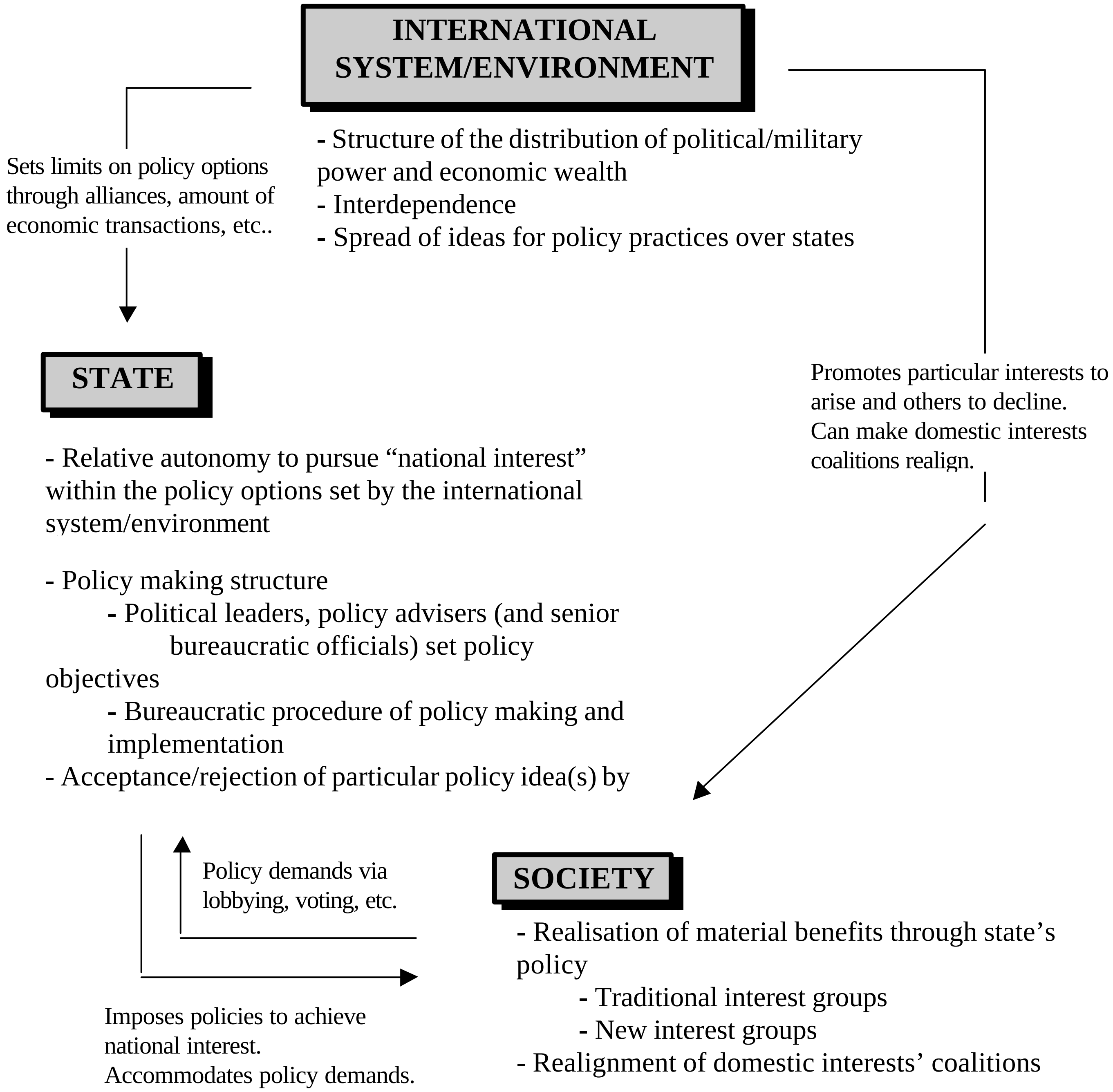
Figure 1 shows a simple framework for analysing foreign economic policy making. Three factors will explain the respective aspects of the change in Australia's foreign economic policy since the 1980s: the changing international system/environment; the government's choice of a certain set of economic policies to respond to the change in the international system/environment and achieve certain objectives, and; the changing policy demands of the society and the state's response. It is essential to put these aspects together to understand the whole picture of the change in Australia's foreign economic policy. It seems that the spread of an idea, that is the revival of neoclassical economic theory in policy practices,[4] over states and international economic organisations in the 1980s can be closely linked to these three aspects. The Australian government and society seem to have accepted the idea of "economic rationalism" over this period as a way to respond positively to the changing international economic environment.

In the following sections, this analytical framework, or the influence of the above three factors on foreign economic policy making, will be explored in detail. How those factors interact in the policy making process will also be examined.

[4] It is important to note that using neoclassical economic theory in policy practices does not necessarily mean that the actually implemented policies are exactly in line with the theory. States have their own characteristics in their domestic economic situations and policies may be modified accordingly.

Figure 1

Image of the Analytical Framework for Foreign Economic Policy Making in Middle-sized States



II.1 The International System/Environment as an Independent Variable

II.1.1 Structure of the International System and Its Change

> *Governments are not free agents. International facts, ..., prevent them, often in the most unexpected ways.* (Butler 1973:84)

The structure of the international system came into focus in the 1970s as the primary factor that influence the foreign policy of a state. Bull (1977:9) described the international system as "[t]wo or more states [which] have sufficient contacts between them, and have sufficient impact on one another's decision, to cause them to behave ... as part of a whole". According to Waltz (1979: chapter 5), the structure of the international system is defined by the arrangements of its parts, and these arrangements are set by its principal parts (i.e. great powers). Other states are assumed to act along with these arrangements made by great powers. The difference between great powers and other states are their "capabilities", and all the states are said to seek to increase their capabilities through domestic and foreign policies.

The international system consists of not only military/political power but also economic power, that is the distribution of economic activity and wealth. Since the end of World War II, flows of goods, services, capital, technology and information across states' borders have dramatically increased due to rapid and continuous technological developments in transportation and telecommunication. These flows have created economic interdependence among states.[5] Economic interdependence has altered the traditional ways to pursue power in international relations and settle disputes.[6] External factors derived from this international system can improve, alter or interrupt states' domestic and foreign economic policy according to their stronger/weaker position relative to others. However, economic interdependence sets limits on

[5] "Interdependence, most simply defined, means mutual dependence. ... where there are reciprocal (although not necessarily symmetrical) costly effects of transactions, there is interdependence" (Keohane and Nye 1977).

[6] Cohen (1988:26) pointed out that, since the 1960s, the emergence of new and influential states in international relations has had the same characteristics: increasing economic power, not military strength. He gave Japan, South Korea, Saudi Arabia and others for examples.

what states can do in terms of foreign economic policy. This is because destruction of economic interdependence would be too costly for any state to contemplate. Duffy and Feld (1980) state: "[w]hat is important is the perception by the population of a state that their fate, as well as, their economy and society, is somehow intertwined with that of neighbouring states, and this knot cannot be extricated without extremely harmful consequences". Each state cannot decide and implement its foreign economic policy and achieve its economic goals without taking the impacts of other states' policies toward itself into consideration (Morse 1976). Gourevitch analysed the question of foreign economic policy of a state from the economic aspect of the international system (Gourevitch 1978). He looked at various approaches that explain the international economic system such as product cycles, Wallerstein's world system and economic interdependence,[7] and conclude that the system constrains an entire range of domestic behaviours, from policy decisions to political regimes.

The change in the international system since the late 1970s has been one of the most significant since the end of World War II. As Biersteker (1992:113) argued, "[s]tates that adopt their economic policies to respond receptively (both flexibly and favourably) to these changing global conditions will do well, or at least have a better chance of doing well, in the increasing competitive world economy". The international system should be seen as a primary factor in influencing foreign economic policy, especially for small and medium sized states.

II.1.2 Spread of Economic Ideas over States

Change in the international system should be seen as a precondition for states, but it alone cannot readily explain why particular changes in states' foreign economic policy takes place as they do. There must be more than one policy option available at any time. To explain why particular economic policies are employed by states to respond to the changes in the international economic system, it is useful to examine the dominant ideas influencing international policy formulation at the time.

Foreign economic policy makers of states can utilise a variety of different ideas to deal with the international economic environment and its changes. Ideas can vary on aspects such as

[7] See Gourevitch (1978:882-96). For respective approaches, see Gerschenkron (1963), Wallerstein (1974) and Keohane and Nye (1977).

the theory of international trade, the balance of payments adjustment process, and the causes of economic development (Cohen 1988:7). Why a state takes up a particular idea for policy making can be explained by asking how policy makers of states perceive changes in the international economic environment. A new environment (external shock) might force policy makers to decide how much more, or less, they should integrate with the world market of goods, services and capital. This is particularly true if traditional policy is thought to be incapable of coping with the new environment.

The way policy makers perceive the international and domestic economic situation can be influenced by dominant policy ideas at the time, which also can be seen as part of the international economic environment. If major economic powers adopt certain ideas to form their economic policies towards a new environment, other states might try to emulate their policies (policy bandwagoning). Furthermore, if to change policies along with those of economic powers becomes a condition to join and get benefits from prevailing international regimes in which those economic powers have a strong say (such as the GATT, International Monetary Fund (IMF) and World Bank), policy bandwagoning is more likely to be a dominant phenomenon.

The spread of economic ideas and the policy practices according to them are based on: the widespread publication of relatively standardised textbooks; the growth and homogenising tendencies in advanced graduate training; the worldwide readership of the leading journals; the increasing mathematisation and quantification of economics which helps overcome language barriers; the expanded mobility of students, professors and experts across borders, and; the international network built among leading institutions (Coats 1989:113). In this ways, certain ideas for economic policy formation can spread over states in the world in a certain period of time, and can be implemented accordingly.

In sum, the impact of the international system and its changes are given and primary factors for states, especially small and medium-sized ones, in making their foreign economic policy. However, this does not mean that the international system forces states to take a particular policy approach. Rather, it limits what states can do and provides certain range of policy options. Gourevitch (1978:911) added that "[h]owever compelling external pressure may be, they are unlikely to be fully determining. Some leeway of response to pressure is always possible. The choice of response therefore requires explanation. Such an explanation necessarily entails an examination of politics: the struggle among competing responses". Waltz (1959, 1979) also has reservation in asserting that the international system is the dominant determinant of states' foreign policy.

If one is seeking to explain a single state's foreign economic policy making and implementation, examining the impact of the international system alone is not enough. There must be more than one policy choice available to a state at any given time. After all, it is the state that perceives opportunities and disadvantages set by the international economic environment and translates these perceptions into foreign economic policy.

II.2 Role of the State in Foreign Economic Policy Making

II.2.1. Development of an Analytical Framework for the Role of the State

Early realist literature emphasised the struggle among states for national interests in the anarchical situation where there is no one to serve as a mediator or arbitrator. Decision making and the implementation of foreign policy were conducted by leaders of states. To realise national interests, Morgenthau (1949) relied on well-trained leaders and diplomats as independent variables, in the area of foreign policy decision making.[8] The rationality and human nature of policy makers were taken as the most important factor of foreign policy making in this approach. Waltz (1959) looked at the state as an important determinant of foreign policy decision making, saying, "[s]ince everything is related to human nature, to explain anything one must consider more than human nature. The events to be explained are so many and so varied that human nature cannot possibly be the single determinant" (Waltz 1959:80-1).[9] He argued that the state functions are determined by the need of the society, which can include the liberal market economy (*laissez-faire*), as well as protection of domestic industries and the management of aggregate demand (*Keynesianism*). Allison (1971) pointed out that the traditional "rational actor" model, which relies heavily on leaders to make decisions through choosing rationally

[8] Morgenthau (1949) argued that only the workman-like manipulation of diplomacy in a realist way could achieve the national interest (defined as power) and the potential transformation of international politics.
[9] Waltz (1959) focused on the state as the "second image" of international relations. The "first image" was the same as the traditional realist's.

among available options, is not adequate to provide a full understanding of US foreign policy decisions. By introducing the "organizational process" (bureaucratic procedure) model and the "governmental politics" model, both of which deal with the political process within the government, he explained different dimensions of the US and the Soviet decision making processes that could not be explored by the traditional model.

From the latter half of the 1970s, focus on the role of the state in the foreign economic policy making process evolved into a new dimension. The quantity of literature whose emphasis was on the influence of the international system and societal groups in policy making grew. Katzenstein (1976, 1978a) and Krasner (1978a), among others, argued, however, that the state continued to play the central role in policy making, and that much more attention should be paid to the state's role. The main point of their argument is that the state has its own needs and goals which cannot be reduced to specific societal interests (Krasner 1978a:333).[10] The state pursues "national interests" (policy objectives) which must be related to *general* societal goals, and as such have a consistent ranking of importance over time.[11] (Krasner 1978a:13, 35). The actors in the state and society influencing the definition of foreign economic policy objectives (national interests) consist of political groups and the major interest groups. The former are derived from the structure of political authority (primarily the state bureaucracy and political parties), and the latter represent the relations of the various arms of production (including industry, finance, commerce, labour and agriculture) (Katzenstein 1978b:19). Though constrained by the international system and the domestic societal pressure, the state has relative autonomy in pursuing policy objectives and they cannot be pursued by any particular societal groups.

The development of the above approach saw the emergence of two broad aspects (Ikenberry, Lake and Mastanduno 1988:10). First, the state as a whole is taken as an actor in foreign economic policy making in a broad sense and political leaders, senior bureaucratic officials, policy advisers and so on are viewed as individual participants (policy makers) within

[10] Goldstein (1988:185) also said that "the state is the institution which interprets, more or less correctly, national needs".

[11] "For any single decision it is possible to impute a rank-order of objectives, but if this changes from day to day or even year after year, it would be misleading to use the term 'national interest'. One would better look to bureaucratic preferences or societal pressures to understand the actions taken by central decision makers" (Krasner 1978:14).

the process. In this case, as mentioned earlier, policy makers are assumed to represent the concept of "national interest" and participate in the policy making process, *not so much* as agents of any particular groups in the society or governmental institutions as other approaches may suggest. Rather, policy makers tend to take actions to achieve their policy objectives by pursuing the public policies that they believe are most beneficial.

Lake emphasised the relative autonomy of states in his article on US trade policy making at the turn of the century. He focused on the role of the "foreign policy executive"[12] who was seen as the sole authoritative foreign policy maker, and argued that this "executive" led society and mobilised support for trade policy making (Lake 1988:56-7). Katzenstein also wrote that the direction of influence between the state and society goes both ways and "[p]ublic policy can shape private preference" (Katzenstein 1978b:18).

The policy preferences and actual choice of the state can often differ from the demands of interest groups because private interests tend to be narrow without considering the state's economic strategy and rarely take the economic policies of other states into account. Furthermore, state policy makers are in the position to be able to make links between foreign economic policy of their own and other states' and tie certain policy issues to a larger set of international issues. By doing so, they can bargain to realise the state's overall interests (Ikenberry 1988:167-71).

Second, the state can be viewed as an institution or a set of laws and rules, whether physically established as an organisation or not. Policy making is the process within the institutional settings of the state that is shaped by experience from previous events. Thus, the way in which the state and the society are actually linked is historically conditioned (Katzenstein 1978b:17). Once set up, the institutional settings are hard to change and tend to remain in existence much longer than the cause they originally served. It is important to understand the history of the state which formed the current institutional settings because they influence, lead, redirect and constrain policies to be made and implemented. Some kind of crisis situation is needed to change or reshape current institutional settings of the state.

[12] "Foreign policy executive" is defined as high-ranking bureaucrats and elected executive officials charged with the overall conduct of defense and foreign affairs (Lake 1988:36-7)

II.2.2 Impact of Ideas on the Foreign Economic Policy Making Process

When policy makers make foreign economic policy, they need some guide to understand the current international and domestic economic situation, available policy options and the expected results of those policies. Economic ideas play a significant role in this area, and why and how they matter should be explained.

Goldstein and Keohane (1993a) and the contributors of their edited book discussed the impact of ideas on foreign policy making,[13] and their case studies cover a wide range of policy decisions taken by various states.[14] All of them argued that ideas did matter when the crucial policy decisions were made, by explaining the relations between certain ideas and respective states' specific historical development, institutions, central policy makers and so on. They explained the relations between ideas and policy decision making as follows. Goldstein and Keohane (1993b) categorised ideas into three different dimensions: world views, principled beliefs and causal beliefs. Among them, *causal beliefs* are the ideas about the cause-effect relationships. Causal beliefs guide individuals on how to achieve their objectives. Changes in causal beliefs occur more often than the other two as the knowledge of theories and new technologies evolve. Specific policy changes can often be traced by such changes. Second, they explained how ideas had impacts on policy decision making. If policy makers cannot predict exact results of certain policies, they make decisions according to the expected results.[15] The idea that policy makers have becomes an important causal factor here. When a set of certain ideas is employed by policy makers, it limits the possibility for alternative policies to be picked. Moreover, if a set of ideas comes to influence policy decisions for a long period of time, they may be built into political institutions such as standard operating procedures of administrative departments, ministries or agencies. This process makes it more difficult to change the policy preferences of a state. Changes in institutionalised ideas may occur in a crisis situation, otherwise, they tend to last even if the interests and/or power that promoted them cease to exist.

[13] See also Goldstein (1988).

[14] The case studies include: the Anglo-American negotiations over the postwar international trade and financial regimes (Ikenberry 1993); the Stalinist political/economic policies in China (Halpern 1993); decolonisation by the European states after the World War II (Jackson 1993), and; the creation of the European Community's internal market (Garrett and Weingast 1993).

[15] It is not unusual for policy makers not to know exact policy results as they cannot avoid imperfect information during the policy making process.

Hall (1989:369-75) suggested some conditions for *new* economic ideas to be taken up and incorporated into policies. First, naturally, the validity of economic ideas in policy making depends upon their perceived capacity to achieve goals and to solve the problems at hand. A relevant set of economic problems are needed to exist for ideas to be taken up. In other words, ideas should be at the right place at the right time to be adopted by policy makers. Second, the reception of new economic ideas is influenced by the institutional settings of a state and its prior experience with related policies. If the new economic idea, and the policies it suggests, are totally different from previous ones, the change in policy will occur gradually, if it happens at all, unless something happens to change those institutions drastically. Third, ideas must win support from not only policy makers within the state but also from broader bases including societal groups, because economic polices are ultimately directed towards them.

II.2.3 Structure of the Policy Making Process within the State

Political Leaders and Policy Advisers

Changes in the international economic environment and the worldwide spread of particular ideas over states' policy making units can explain the reason why a state changes its foreign economic policy. However, it cannot readily explain why changes happen in different time periods, or why the substance of change differs from state to state. A straight forward answer for this question is: because each state has different policy makers and institutions. The domestic structure of foreign economic policy making is historically founded. The contemporary structures are rooted in some of the major historical transformations of the past (Katzenstein 1978b:323).

In the case of parliamentary systems of government like Australia, once the Cabinet makes policy decisions, the approval from the parliament, if needed, can be expected. On the other hand, for political leaders in the government, the process prior to a Cabinet decision becomes important. This process includes negotiation, persuasion and bargaining within their own political party and with the opposition party(s), to get support for a particular set of economic policies.[16] If the ability of the elected political leaders to define policy objectives (national interests) is

[16] In Australia's case, the major actors in the area of foreign economic policy making are: the Prime Minister; the Minister for Foreign Affairs; the Minister for Trade; the Treasurer, and; other economic ministers depending on the issues. Policy advisers (official or private) for respective ministers and senior officials in respective Departments also play important roles.

strong, it will reduce the capability of bureaucracy and societal groups to intervene and alter the original objectives for their interests.

To analyse the foreign economic policy decision making process of a state, an understanding of the perceptions of the participants is also essential, especially in the period of policy change. It is necessary to question what are perceived to be problems and the causes of problems, and what are believed to be solutions for these problems. Maybe more importantly, it is necessary to ask when and how do policy makers formulate ideas on problems and solutions.

The initial acceptance of certain economic ideas, and the subsequent request for leaders of government to take certain policy options, may come from domestic circles, such as academic and bureaucratic economists. However, if these domestic circles do not have channels to make close contact with policy makers like ministers and high ranking bureaucratic officials, their requests stand a good chance of being declined, if heard at all. This may be true even if their argument is perceived to be correct. On the other hand, those domestic policy circles which keep closer contact with leaders may act as policy advisers,[17] and have a greater chance to influence leaders in policy making.[18] In this case too, however, the ideas that are forwarded to leaders do not necessarily exert their influence immediately (Halpern 1993:110). An appropriate economic situation, or a change in the situation, is needed for those ideas and subsequent policies to be taken up, especially if those ideas and policies are different from preceding ones.

Ideas for policy change need a good environment, such as a major external shock, a perceived failure of past policies, domestic promoters, and a change in the policy demands of society, to be taken up and kept as a basis for a new set of economic policies. (Biersteker 1992:126). Economic crises provide policy makers with an opportunity to introduce new policies: dissatisfaction with past policies creates a new willingness of political leaders to

[17] Those policy circles are often called “epistemic community” (Biersteker 1992:121). Hall (1989:378) pointed out that the distribution patterns of this community varied from state to state. In some states, policy advice comes mainly from bureaucratic officials, and some states actively invite experts into the official or unofficial policy making process as members of public commissions and policy advisers for individual politicians.

[18] This statement does not imply that the policies finally implemented by the government always agree with what original ideas suggested. Solow (1989:80-2) argued that, by the time economic ideas reach policy makers, they are transformed into such cruder forms that it is fair to say that they become a different doctrine. He pointed out the reason for this as: original economic theories are too complicated to be fully explained in

re-evaluate their interests and goals; disruptions and the breakdown of rules and institutions by crises create a need for non-incremental decision making, and; the collapse of old political coalitions as the result of crises requires a search for new coalitions (Ikenberry 1993:83). They provide policy makers opportunities to try something different.

Bureaucracy

In policy making, inputs from bureaucracy can usually play an important role. Policies are not simply made at the top of the ministries or at Cabinet level. Much of policy substance originates way down within the bureaucracy and is modified, refined and reshaped repeatedly as it moves up to the highest decision making level.[19] Also, the bureaucracy plays a significant role in actual policy implementation. Bureaucracy does this often through interpreting and adapting decisions to fit changing economic and other situations. Policy makers cannot foresee all these changes (Coats 1989:111).

Bureaucratic actors are charged with worrying about different dimensions of foreign economic policy according to their respective policy jurisdictions, and it is their interest to have as much influence as possible in enhancing their viewpoints and containing opposing positions (Cohen 1988:38). Each bureaucratic actor considers its dimension, or that of the organisation to which he/she belongs, to be very important. Each will pursue a relatively consistent set of perspectives under any conventional organisational arrangement. Bureaucratic actors seldom bring a common vision of how best to react to a new issue (Cohen 1988:42-3). Thus, in the bureaucratic dimension of policy making, the primary process is how the different goals, perspectives, self-interests and ideas of the participating bureaucracies are to be introduced and assigned priorities. The success or failure of a bureaucratic organisation's attempts to maximise its values will be a function of the extent to which the governments' decision-making process listens to and takes seriously the various bureaucratic inputs.

As mentioned earlier, if a particular set of policies is adopted for a long time, the relations between political leaders and bureaucracy, and among bureaucratic organisations in this policy

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a short time or sentences, while policy makers are not interested in the finesse and complexity of theories but simple and confident prescriptions.

[19] Salant (1989) pointed out that, in some cases of economic policy, bureaucratic economists could have more important influences on economic policy than political leaders, political parties and interest groups.

area, will become institutionalised. Thus, for political leaders to introduce a totally new set of policies, they need to depart from the prevailing institution and create a new one. There are several ways to do so. First, if the political party in power changes as the result of an election, there is a great chance for new government to depart from the previous institutions. Second, even if the government does not change, stronger political leadership and consultation with policy advisers from outside of the bureaucracy can confine the organisational interests. Third, with or without a change in the government, an organisational re-arrangement (administrative reform) can change the pattern of negotiation and bargaining between political leaders and bureaucracy, and of course, among bureaucratic organisations.[20]

II.3 Policy Demands of the Society: Relations between the State and Interest Groups

By the late 1950s, the close relationship between domestic politics and foreign policy making received greater recognition. Economic policy has important consequences on the material interests of societal groups such as industry organisations and labour unions. Taking trade policy for instance, imports can provide both a positive and negative impact on the domestic economy. They can offset local shortages of goods and services, and provide competition to local import competing industries. Competition with imports can give incentives to local import competing industries for more efficient production and marketing. At the same time, if those industries fail, competition induced by imports can displace jobs and, in the worst case, force firms to bankrupt. Thus, societal groups try to influence policy makers as much as possible to make and implement economic policies which serve their interests. In this pluralistic approach, foreign economic policy is explained as the result of ongoing competitions among domestics societal and political groups. Policy makers and bureaucracy in the government are viewed basically as intermediaries, or passive actors, creating policies in deference to political pressures, or

[20] In addition, as Weir (1989) suggested, changing the procedure of recruitment can have an impact on the degree of openness and hierarchy in bureaucracies that will eventually lead to change in the institutionalised relations.

sometimes maybe threats, exerted by special interest groups on behalf of their economic interests.

Rosenau (1969:45) argued that the linkage between domestic and international politics, defined as "any recurrent sequence of behaviour that originates in one system and is reacted to in another", should be closely analysed in research on foreign policy decision making. He emphasised that domestic politics plays an important role in the linkage. Lindblom (1977) pointed out that, because of its significance to the economy, private business, especially large corporations, tends to enjoy privileged power over policy making. Putnam (1988) argued through his two-level game theory that analysts should look at state structures such as political parties, interest groups, elections etc., because political leaders negotiate with their counterparts in other states and make decisions not only to pursue national interests but to fulfil demands of domestic interest groups, which form the basis of their political support. Policies must mobilise support from coalitions in the society whose votes elected political leaders ultimately depend upon. Frieden (1988) took the US inability to take leadership in the international political economy in the inter-war period, and explained it by the unevenly distributed economic interests within US society.[21]

Political leaders involved in the foreign economic policy decision making process have their own bases of potential support (electoral constituencies, interest groups, bureaucratic organisations they lead, etc.). Depending on their support base, leaders' roles, responsibilities, priorities and perceptions can be expected to differ. Policy outcomes will therefore depend on who (and which group that the political leader represents) is most influential in the decision making process. Decision making in foreign policy can be seen as a process of bargaining, persuasion and the formation of coalitions among the participants. This intra-governmental process model was applied by Neustadt (1960), Lindblom (1965), Allison (1971) and Allison and Halperin (1971), among others.

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[21] By the end of World War I, the United States became the world's biggest overseas investor. However, those who had interests in international economic activities were a powerful but small part of the entire society, namely the financial sector and some industries such as mining and automobiles. Other sectors remained virtually isolated, having no international transactions, and saw the world economy primarily as a competitive threat. These two distinctively different parts of the society formed "internationalist" and "isolationist" blocs but neither was powerful enough to prevail. The result was the contradictory and volatile US foreign policy during the period.

The statist approach, too, admits, more or less, the influence of the demands of society on foreign economic policy. Katzenstein, one of the strong supporters of this approach, writes that "[g]overnment officials do not define policy objectives single-handedly but in conjunction with business and financial leaders" (Katzenstein 1978c:308). The ability to influence government decisions is not necessarily limited to business and finance sectors. Other societal groups, such as associations of manufacturing industries and trade unions, can have the same ability. The degree of influence they can exert on the government depends upon the issue at hand and the state's institutional settings to deal with those issues.

To deal with societal groups, the strength of the state to assert its policy objectives differs from issue to issue,[22] and state to state. Krasner (1978a: chapter 3) argued that the strength of the state in relation to its own society can be envisioned along a continuum ranging from "weak" to "strong". This categorisation is useful for grasping the general character of states in comparative purpose. However, as Krasner himself admited (Krasner 1978a:58, 1978b), the same state's ability to assert its policy objectives to society differs from issue to issue. For analysing foreign economic policy and its change in a single state, it is more beneficial to explore actual relations between the state and the society and its change in detail, than to seek to label the state as "weak" or "strong".

Then, how *change* in foreign economic policy of the state can be examined from the aspect of the state-society relations? There are three possibilities can be thought.

> *Possibility 1*. Because of the impact of changes in the international system on domestic economy, traditional coalitions become less able to assert their interests. Principal private interests in the past may have sought state intervention, or non-intervention, in their economic activities, but they are increasingly turning away from that general mode of

[22] Krasner (1978b) showed that it is easier for the US government to assert its policy objectives in monetary policy than in commercial (trade) policy mainly because the beneficiaries and victims of commercial policy in the society are relatively easy to detect while the impact of monetary policy tends to spread wide in the society.

relations with the state. Thus, the state becomes relatively free from the traditional pressures on its foreign economic policy

Possibility 2. Societal groups with new interests that agree with the government's new set of policy objectives increasingly come forward to challenge the bases of traditional coalitions. They eventually take over as dominant coalitions to influence the government. If the new coalitions are sustained for a certain period of time, their influence on the state will be institutionalised within the foreign economic policy making process.

Possibility 3. The traditional interest groups change their attitudes, actively or passively, towards policies to accommodate changes in the international system. They find that policy reform by the government could be beneficial to themselves in the long run, or that there is no other choice. They might form new coalitions with groups whose interests agree with the new policy objective of the state.

These three possibilities can happen independently or concurrently. In any case, new institutional settings in the relations between the state and society will be created. If the new set of policy succeeds in providing good results, both for the state and the society, this policy will be able to create domestic interests to defend itself.

It is not readily known whether the state or interest groups initiate this change. If one takes the statist approach, the state should be seen as the prime mover of coalition changes. Policy makers can initiate change "by offering a compelling interpretation of events that interest groups are unable to make sense on their own" (Krasner 1978a:75). The state is also able to define problems and policy objectives in ways that appeal to the general concern of citizens rather than particular groups within society. On the other hand, if one takes the pluralistic approach, coalition change and subsequent institutional change is brought about by interest groups themselves as the state (political leaders and bureaucracy) are thought to be just intermediaries who are unable to take their own initiatives.

It seems that, to examine state-society relations during a period of foreign economic policy change, it is better to take the state as an initiator of the change, because it is highly unlikely that interest groups would voluntarily drop the benefits they have been long enjoying through traditional policies. They might realise that the changing international system will not allow them to maintain the traditional benefits, but they would wait to publicly change their attitudes until the government actually starts changing policies. By so doing, they may be able to seek modification of the new policy implementation to make it less harmful by pressuring the government. If the influence of those interest groups towards the government is still remaining, the government has to compromise and find a "not-too-drastic" measure in policy implementation. This measure can be gradual implementation of a new policy to give traditional beneficiaries time to adjust, different time schedules for different policy areas like macro and micro economy, or packaging the new policy with compensation for sectors of the society that will be disadvantaged.

III. Foreign Economic Policy Making in Australia: Changes in the International Environment and the Role of the State

A general framework for analysing foreign economic policy making in middle-sized states is set in the previous chapter, and now it will be applied to the Australian case. This paper, however, only focuses on the international environment and state factors of Australia's foreign economic policy making. It deals only with how the Australian government set foreign economic policy objectives (national interests) under the changing international economic environment, and how it made and implemented policies in accordance with these objectives.

III.1 Review of Change in the International Economic Environment and Foreign Economic Policy in Australia

Australia's foreign economic policy changed over the 1980s, especially after the Australian Labor Party (ALP) gained power in 1983. This was a consequence of the changing international economic environment, with the direct trigger for a change in policy orientation being the sharp deterioration of Australia's terms of trade after the second oil crisis in 1979. To respond to the situation, the ALP government aimed for domestic economic reform based on minimal government intervention in the market (economic rationalism).

Until the 1970s, Australia enjoyed strong trade growth based on traditional exports of primary commodities to rapidly developing East Asian countries (especially Japan). The growth of the domestic economy during the long post-war “boom” period had relied on the export growth of primary commodities, and the redistribution of income to other sectors. Australia had traditionally adopted a policy of protection which was designed to shelter the country’s domestic manufacturing and services sectors from international competition. In protecting these sectors from imports, the Australian government was effectively discriminating against much more competitive industries like agriculture and mining. By the 1980s, it was realised that creating export opportunities for primary commodities alone would not generate enough income to provide Australia’s increasing population with a rising standard of living (Garnaut 1989:205). The country needed policies to advance international competitiveness, not only in the traditional primary commodities sectors but also in the manufacturing and services sectors, and to promote these sectors’ exports.[23]

III.1.1 The Changing Economic Environment in the Asia Pacific Region

Under the GATT regime, economic interdependence among countries in the Asia Pacific region has developed steadily since the 1960s. Drysdale (1988) identified some of the factors behind this development. One was the impact of Japan’s economic growth. Japan was the first country in East Asia to develop its economy, and by the 1980s its GDP had become one of the world’s largest. Rapid economic growth of Japan brought about a huge increase in its demand for minerals and foodstuffs from the region. At the same time, Japanese exports of manufactured goods, as well as the flow of capital and technology transfer, into countries in the region experienced unprecedented growth. Another major factor was the development of other East Asian economies. Resource-rich countries such as Indonesia, Malaysia, Thailand and Australia enjoyed large export earnings while economies like Korea, Taiwan, Hong Kong and Singapore

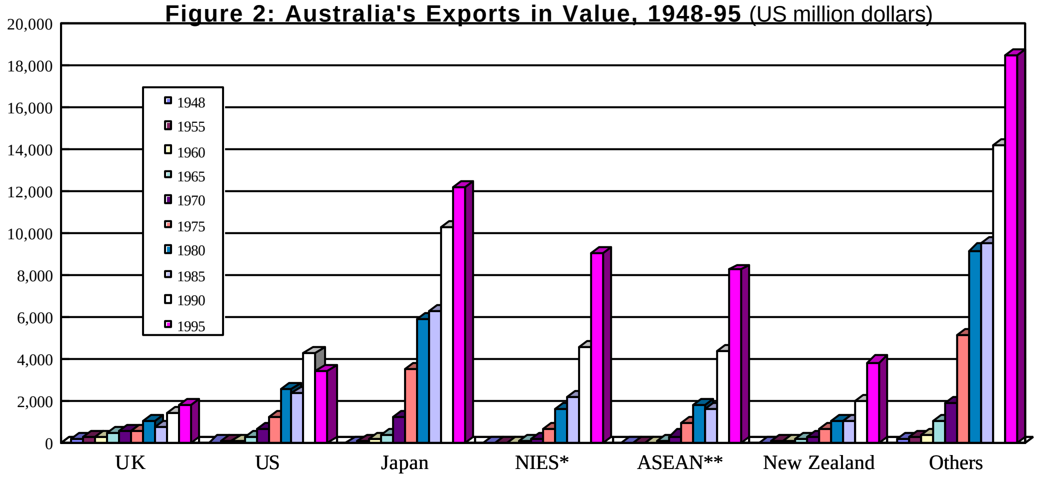
[23] In 1989, the Hughes Committee reported that Australia’s merchandise exports were about one-third lower than they would be in an internationally-oriented economy. See Hughes *et al.* (1989).

followed the Japanese path by adopting outward-looking, trade-oriented industrial strategies. By the late 1960s, Southeast Asian countries were intent on emulating their success. Their economies developed steadily throughout the 1970s and began to grow rapidly in the latter half of the 1980s.[24] Flows of capital, including foreign direct investment, from Japan, Korea, Taiwan, Hong Kong and Singapore to Southeast Asian countries increased sharply in the 1980s; capital flow is now heading for China, Vietnam and Burma. Southeast Asian countries also started to invest overseas during this period. In short, East Asian countries have been providing Australia with investment and export opportunities for the past 30 years.

Figure 2 and 3 illustrate the growing importance of East Asian countries as Australia's trade partners. Figure 2 confirms that Australia has been drastically increasing its exports to East Asia, including Japan, Newly Industrialising Economies (NIEs = Hong Kong, Korea and Taiwan) and the Association of South East Asian Nations (ASEAN = Indonesia, Malaysia, the Philippines, Singapore and Thailand). It also shows that Australia's exports to Japan started to increase rapidly in the mid 1960s. Japan became the largest single export destination in the latter half of the 1960s and remains so. Exports to NIEs and ASEAN started to grow quickly in the mid 1970s. From 1980 to 1995, the fastest growing export destination was NIEs with a more than 450% increase over the period, followed by ASEAN with a 360% increase.

[24] In 1988, 1989 and 1990, Thailand's real GDP grew at a rate of 13.2%, 12.2% and 11.6% respectively, and it has been continuing the trend in the 1990s with annual growth rates over 8%. Malaysia's and Indonesia's real GDP also grew rapidly in 1988, 1989 and 1990: at a rate of 8.9%, 9.2% and 9.7% in the case of Malaysia and 5.8%, 7.5% and 7.2% in the case of Indonesia. They have also been keeping their growth trend with annual rates around 6 to 9%. See IMF, *International Financial Statistics*.

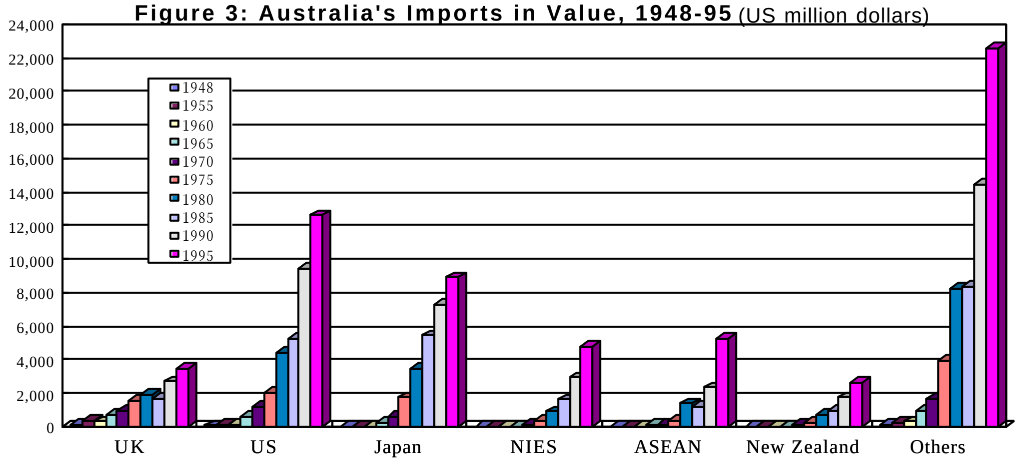
Figure 2: Australia's Exports in Value, 1948-95 (US million dollars)



* Hong Kong, Korea and Taiwan. ** Indonesia, Malaysia, the Philippines, Singapore and Thailand.

Source: International Monetary Fund (IMF), *Direction of Trade Statistics Yearbook*, various issues.

Figure 3: Australia's Imports in Value, 1948-95 (US million dollars)



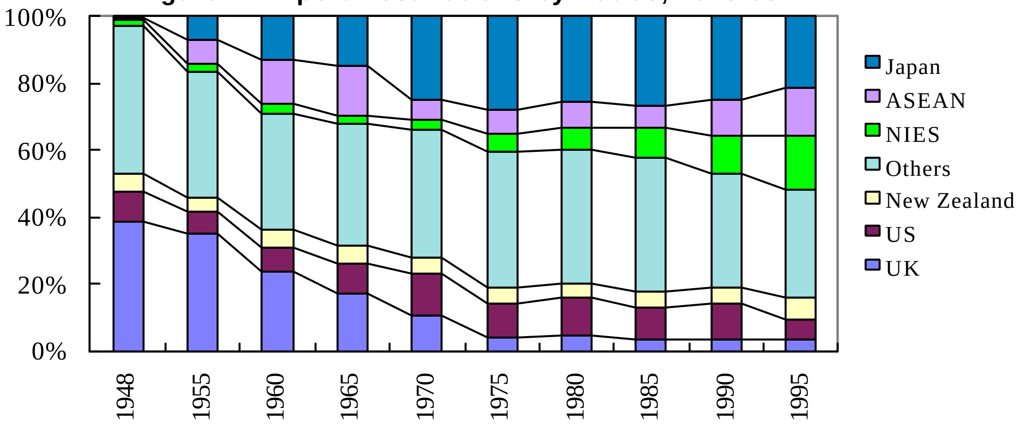
Source: IMF, *Direction of Trade Statistics Yearbook*, various issues.

According to Figure 3, the United States remained as a major import source for Australia. The imports from East Asian economies have also been steadily increasing since the 1970s. The timing of the beginning of the rapid growth of imports from each East Asian economies differed by country/area. Again, imports form Japan started to grow earlier than those from other East Asian countries. The fastest growing import sources over the period from 1980 to 1995 were NIEs with an increase of more than 430%, then, New Zealand with a 286% increase, closely followed by ASEAN with a 278% growth.

It is interesting to note that, among the economies in Figure 2 and 3, Australia has been accounting trade deficits with the United Kingdom and the United States for almost the whole post-war period, while it has been recording trade surpluses with the East Asian economies. Since the 1970s, the trade surplus with East Asia has almost offset the deficits with the United Kingdom and the United States, with an exception in the mid 1980s. For instance, Australia's combined trade deficit with the United Kingdom and the United States in 1990 was US$ 6,440 million and the surplus with East Asia was US$ 6,592, and the same figures in 1995 were US$ 10,860 and US$ 10,484 respectively.

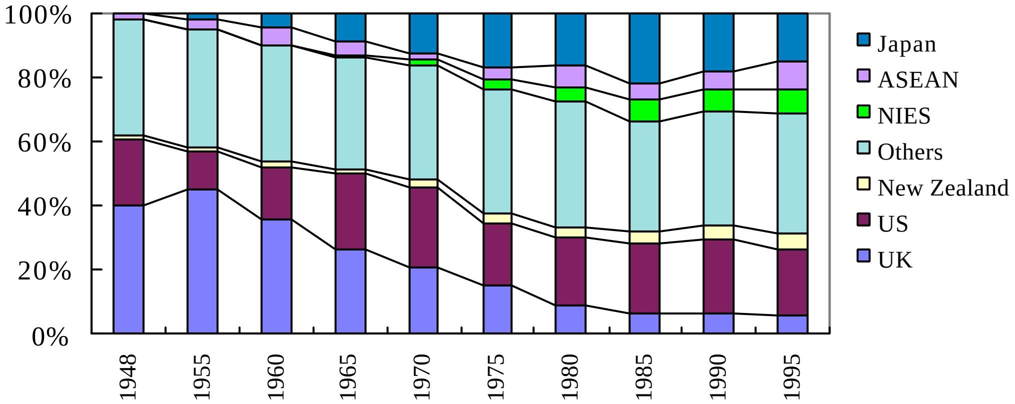
Figures 4 and 5 show the growing importance of the East Asian countries for Australia's trade more clearly from a different angle. These Figures indicate the changes of the share of respective countries/areas to Australia's total exports and imports over the post-war period.

Figure 4: Export Destinations by Ratios, 1948-95



Source: IMF, *Direction of Trade Statistics Yearbook*, various issues.

Figure 5: Import Sources by Ratios, 1948-95



Source: IMF, *Direction of Trade Statistics Yearbook*, various issues.

Both Figures show almost the same trend. First, since the 1960s, the decline of the United Kingdom as Australia's major trade partner is quite notable. In 1948, shortly after the war, the United Kingdom accounted for 38% of Australia's total exports and 40% of imports. However, 47 years later in 1995, those figures had decreased to only 3% and 6% respectively. It can be seen that the special tie between the United Kingdom and Australia, which was brought about by their history as a suzerain power and a member of its empire, and later as members of the Commonwealth, had disappeared over the period in terms of trade relations.[25] Second, the US share in Australia's total exports seems to have reached its peak in the early 1970s (13% in 1970), and since then, the figure has been gradually decreasing. It dropped to 6% in 1995. For imports, again the US share reached its peak in the early 1970s (25% in 1970) but has been stable since then, accounting for just over 20% of the total. Third, Japan started to occupy a meaningful share in Australia's trade since the 1960s.[26] In 1948, its share in total Australian exports and imports were negligible, but by 1965 these figures increased to 17% in exports and 9% in imports. The figures reached almost 30% in exports and 25% in imports in the mid 1980s, but started to decrease gradually in the 1990s. Fourth, the growth of the share of NIEs and ASEAN cannot be disregarded. As a whole, they accounted for only 3% of Australia's total exports and just more than 1% of imports in 1948. However in 1995, the figures reached 32% and 17% respectively due to the rapid economic growth of NIEs and ASEAN over the period. Moreover, if the figures for Japan, NIEs and ASEAN are combined as "East Asia", it is found that the figures have grown to 55% of Australia's total exports and 32% of imports, starting from just 4% and 1% respectively in 1948.

In sum, the change in the international economic environment in the Asia Pacific region over the post-war period has been characterised by the rapid economic development in East Asian

[25] The period between the first UK application to join the EEC in 1961 and its actual accession to the EC membership in 1973 can be seen as a watershed also in terms of Australia's formal trade relations with the United Kingdom. The UK engagement to Europe inevitably meant the reorganisation of the traditional preferential tariff scheme. In the same period, the UK decision to withdraw its military presence from east of Suez in 1967, without full consultation with Australia, lessened their security tie which had already been decreasing since World War II.

[26] The conclusion of the trade agreement in 1957 guaranteed reciprocal provision of the most favored nation status and the abolition of import licensing and can be seen as the basis of the following development of trade relations between Australia and Japan.

countries. Their economic growth have been accompanied by an increasing amount of international economic transactions that have created highly enmeshed interdependence in the region. Being a middle-sized state and traditional exporter of primary commodities, Australia has inevitably been involved in the process of this deepening interdependence. In the process, the relative importance of some traditional economic partners such as the United Kingdom and the United States has declined, and East Asian economies have emerged as new and growing partners. This process has been promoting the re-orientation of Australia's foreign economic policy toward the region.

III.1.2 Policy Reorientation from Traditional Protectionism to Liberalisation

The protection of domestic industry in Australia is a deeply entrenched ideal. With Federation in 1901, the politics of "domestic defence" (Castles 1988:91) emerged as an exercise in nation-building. "The nation was founded not in war, revolution or national assertion, but by practical men striving for income, justice, employment and security" (Kelly 1992:1). It was natural, then, that the protection of citizens' everyday lives became a government priority. According to Castles, the values institutionalised by government were the protection of manufacturing industry through tariffs and other trade restrictions, the conciliation and arbitration of industrial disputes, the control of immigration and a residual system of income maintenance for those outside the labour market (Castles 1988:93). Kelly (1992:2-13) referred to them as the "Australian Settlement" characterised by White Australia, Industry Protection, Wage Arbitration, State Paternalism and Imperial Benevolence, but what Castles and Kelly describe is in fact the same phenomenon. It is not hard to imagine that to abandon these institutions after eight decades would be a challenging task. The protection of domestic industries was virtually kept intact until the early 1980s.

The first move from within government to re-organise protection policy came from the Tariff Board (later called the Industries Assistance Commission and now known as the Industry Commission) in the latter half of the 1960s. Initially, the Board's main role was to handle requests from manufacturers for rises in tariffs, and to advise government, after research and consideration, how far protection on particular products should be increased. In 1967, however, the Board began a systematic review of tariffs on manufacturing industries. The Board intended to advise the government to reduce tariffs of excessively protected industries as the first step towards tariff reform (Rattigan 1986). Although the reform was supported by primary industry sector such as agriculture and mining, and even by some members of the Liberal Party, which was then in power, opposition from manufacturers' organisations, sections of the government (especially the Department of Trade and Industry) and trade unions was vociferous. As a result, tariff reduction had to wait until 1974, when the ALP gained power for the first time in 23 years.

Accompanying the resources boom in the early 1970s, Australia recorded a large current account surplus in 1972/73. The incoming ALP government, led by Prime Minister Whitlam, wanted to encourage imports to counter inflationary conditions, and in July 1974, the Whitlam government reduced overall tariffs by 25%. It was said that this liberalisation measure was a result not of external pressures, but rather of internal factors such as advice from key ministerial advisers and input from the Industries Assistance Commission (Charles and Farrell 1975:95)[27]. However, the Whitlam government soon faced serious economic problems. The Australian economy went into decline in the latter half of 1974 as its major trade partners, the United States, Japan and the European Community were pushed into recession by the first oil crisis. Earnings from exports suffered massively, the inflation rate rose and the government had to squeeze money supply.[28] The timing of the tariff reform worsened the domestic economic situation. Opposition from traditional interest groups returned, and the tariff reform process was stopped, at least for the time being.

After another massive deterioration of the terms of trade in the first half of the 1980s, the ALP, which was re-elected to government in 1983 after eight years in opposition, initiated domestic economic reform. In the same year that it was elected, the government surrendered official control of the exchange rate, deregulated interest rates and allowed the entry of foreign banks. By the end of 1988, the exchange rate had depreciated by 24% to the level prevailing at

[27] Hogan (1974:20-1) argued that the government's longer term objective in encouraging imports might have been the gradual reduction of labour-intensive industries and the re-location of these industries to developing countries, in other words, the restructuring of the Australian economy.

[28] Stagflation in Australia in the mid 1970s was derived mainly from the overseas factor, but the spending and wages policy of the Whitlam government exacerbated the problem. The earlier resources boom created a desire for increased wages and encouraged the government to introduce social reform, larger welfare expenditure, and a higher social wages. The Consumer Price Index rose to 13.1% in 1973/74 and then to 16.7% in 1974/75; government expenditure rose 46% and 22.3% in 1974/75 and 1975/76 respectively. The budget deficit rose to over 4% of GDP. See Dyster and Meredith (1990:269).

the beginning of the decade (Keating and Dixon 1989). The depreciation of the currency was expected to result in an increase in exports and a decrease in the current account deficit and foreign debt, but it did not have this effect immediately. In fact, the economic situation worsened after three years of recovery. The current account deficit rose to around 4.5% of GDP in 1986 and foreign debt was also still increasing.

The strong tendency of both the public and the private sector to spend, thus encouraging imports, and the lack of competitiveness in manufacturing industries were perceived to be the major obstacles to the comprehensive reduction of the current account deficit. To increase competitiveness in manufacturing, the government finally decided to expose industries to competition in the domestic and world markets and to phase out the protection they, and related parties such as trade unions, had long enjoyed. In 1989, the government announced an industry policy that set out a gradual reduction of tariff levels: (1) general tariff levels were to be reduced to 5% by 1996 (except for passenger motor vehicles (PMV) and parts, and textiles, clothing and footwear (TCF)), and; (2) the average nominal rate of assistance was to be reduced to 3% and the average effective rate of assistance was to be reduced to 5% by the end of the 1990s (Stanford 1992). The reduction in protection was announced in a period when the current account deficit was still high and it was made unilaterally.

Forced mainly by the change in the international environment, Australia's foreign economic policy changed over the 1980s. In parallel with this unilateral policy change, Australia's policy behaviour on the stages at international organisations such as GATT and APEC to promote multilateral free trade has become very active.[29] This can be seen as a logical consequence of the domestic policy change.

Australia successfully included agricultural products in the Uruguay Round agenda in 1989 mainly by efforts made at the Cairns Group[30]. Australia had learned when it failed to add agricultural products to the GATT agenda at the GATT ministerial meeting in 1982 that it could

[29] Australia did not participate in the Dillon and Kennedy Rounds of trade negotiations of GATT in the 1950s and the 1960s respectively.

[30] The Cairns Group was established in 1986 by 14 countries that do not have government subsidies for agricultural exports. The group consists of Australia, New Zealand, Canada, Argentina, Brasil Thailand, Indonesia and Hungary, among others, and the their agricultural exports account for about one third of the world total.

not achieve its policy objectives alone in multilateral negotiations (Cooper and Higgott 1990:18). Thus, over the past decade, it has been seeking to form coalitions of like-minded countries to achieve its goals.

When the Uruguay Round seemed to be deadlocked in the late 1980s and early 1990s, the United States opted for the creation of free trade areas (FTAs) with Canada, and then with Mexico, to form North American Free Trade Area (NAFTA), as one of the measures to complement the results of the Uruguay Round. Also, the EC integrated its members' market and became the EU. Economic integration in the areas including economic powers like the United States and the EU made outsiders very cautious of their purposes. Countries in the Asia Pacific region reacted to the US and the EU moves.[31]

Australia and Japan responded by calling for freer trade in the region. Following the footsteps of earlier efforts to form economic cooperation forums (PAFTAD, PBEC, PECC, etc.), the move culminated in the establishment of APEC in 1989.[32] The reason why the APEC initiative came from Australia and Japan is quite understandable. Japan is not a member of any existing FTAs and will be heavily disadvantaged if North America and Europe become trading blocs. For Australia, the Australia-New Zealand Closer Economic Relations Agreement (CER) is the only comprehensive free trade agreements it has made, but it is obvious that the CER alone does not fulfil Australia's needs. Moreover, important trade and investment partners of Australia are located on both sides of the Pacific (East Asia and the United States). APEC is a convenient vehicle to tie members together. It provides a great opportunity to promote economic liberalisation and unite members into one region at the same time.

According to its IAP presented at Manila in November 1996, Australia has made many new commitments to APEC trade and investment liberalisation that go beyond its Uruguay Round commitments. For instance, the tariff reduction plan for the traditionally most sensitive areas of PMV and TCF is as follows: tariff rate for PMV and components will be reduced from 22.5% in 1997 to 15% in 2000; tariff rate for apparel and certain finished textiles will be reduced

[31] One of the responses from the ASEAN countries was the creation of their own FTA, AFTA. However, there were other factors behind the creation of AFTA. At the time, China and Vietnam emerged as attractive FDI destinations for Japan, NIEs and others. ASEAN countries were desperate to keep FDI inflows from them by allowing free trade within the region

[32] There is some literature explaining how APEC was initiated. For instance, see Funabashi (1995), Hatakeyama (1996) and Hawke (1994).

from 37% to 25% over the same period; tariff rate for cotton sheeting and woven fabrics from 25% to 15%; other fabrics from 23% to 15%, and; footwear from 27% to 15%.[33]

III.2 How Did the State Matter in Foreign Economic Policy Change since the 1980s?

Changes in Australia's foreign economic policy since the 1980s can be summarised as: the shift from traditional protection policy to liberalisation and deregulation of domestic economy, thus encouraging domestic industries (manufacturers) to export; putting more emphasis than before on relations with the Asia Pacific economies, especially those in East Asia, to reflect the international economic reality that Australia was facing, and; making efforts in multilateral organisations/fora, mainly by forming coalitions of like-minded countries, for free trade and investment to underpin its domestic economic restructuring. The ALP government, which was continuously in office from 1983 to 1996, had incrementally made the above change as a "grand design" of its foreign economic policy over the period (Viviani 1990:398). It is true, however, that more or less the same re-orientation of foreign economic policy was talked about by previous governments such as the Whitlam-led ALP government (1973-1975), and the Fraser-led Liberal/National Country coalition (1975-1983) when it faced the deterioration of the terms of trade in the early 1980s. The difference is that attempts by the previous governments turned out to be incomplete but the ALP government in the 1980s and 1990s, led by Hawke and Keating, made the changes irreversible. The question here is: how did it make it? Because of the limitation in space, this section will just touch upon important points in terms of the ALP government's role in economic policy making and change, but it still illustrates the significant role played by the government.

III.2.1 Policy Makers: Idea and Leadership in the Policy Making Process

The dominant figures of the ALP government were Bob Hawke, Paul Keating, Gareth Evans, Peter Walsh, John Dawkins and John Button, among others. Over the period that the ALP

[33] Australia's IAP in 1996 is a 71 page document. For other commitments that Australia has made, see its IAP which can be downloaded from http://apecsun.apecsec.org.sg/.

stayed in office, these politicians (policy makers) continuously occupied important posts such as Prime Minister, Treasurer, Ministers for Finance, Foreign Affairs and Trade, and Industry. They set the objectives of restructuring the domestic economy by introducing more market oriented policies that brought liberalisation and deregulation, privatisation of state enterprises and so on. These policy makers proclaimed that this "economic rationalism" delivered the best material outcomes for Australian people. The following speech by Keating (Treasurer from March 1983 to June 1991, and Prime Minister from December 1991 to March 1996), made at the time of the economic recession with huge current account and budget deficits in the mid 1980s, illustrates the determination, more or less shared by policy makers, for restructuring the Australian economy.

> *I get the very clear feeling that we must let Australians know truthfully, honestly, earnestly, just what sort of international hole Australia is in. ... It's the price of commodities on world markets but it means an internal economic adjustment.. . If this government cannot get the adjustment, get manufacturing going again and keep moderate wage outcomes and a sensible economic policy then Australia is basically done for. We will just end up being a third rate economy ... a banana republic*. (Keating on a radio program in May 1986. Quoted in Carew 1992:171-2).

For policy makers to be so positive on "economic rationalism" and its policy results, the role played by policy advisers from outside the formal bureaucratic decision making process was influential. Though many academics including Corden, Arndt, Gruen, Drysdale and Garnaut opposed protection of the domestic manufacturing industries in the post-war period, and they sometimes had influences on Australia's foreign economic policy making, they were most influential in the 1980s. Following the world wide trend of practicing economic policies of minimal government intervention in the market since the beginning of the 1980s, the ideas of these academics were accepted for realisation of goals not only in the area of foreign economic policy including regional trade initiatives, but also economic policy as a whole. These advisers were also used to meet the argument of the domestic opposition and push policy ideas further than the bureaucrats might wish to take them. (Viviani 1990:403)

III.2.2 Changes in Policy Making Institutions

As it had different political support bases from the previous government, the ALP government was able to change the traditional policy making institutions. Being in a position to have close relations with trade unions and the labour movement, the Accord, a policy agreement between the ALP government and the Australian Council of Trade Unions (ACTU), the peak organisation of labour movement in Australia, stands out as an example of the institutional changes. The ALP government successfully and continuously involved trade unions, which had been one of the beneficiaries of the traditional protectionism, in policy the making process.[34]

The ALP government also tried to restructure the bureaucratic policy making process. Until the 1970s, the Department of Trade (and Industry) was said to have strong influences over foreign economic policy issues. The Department controlled policies on exports, international trade negotiations, foreign direct investment and imports,[35] being a champion of the protection of domestic industries. The Department's policy priorities, however, had sometimes conflicted with Australia's foreign economic policy objectives as a whole.[36] Facing another deterioration of the terms of trade, and a massive current account deficit in the mid-1980s, the government was in need of better departmental coordination in pursuit of its policy objectives. Its major move was taken in July 1987 to merge the Department of Trade with the Department of Foreign Affairs.[37] The establishment of the Department of Foreign Affairs and Trade (DFAT) has been seen as an attempt to relate Australia's trade policy directly with its international relations (Harris 1989; Pusey 1991:149).

In addition to the physical structural reform of the bureaucracy, the ALP government concentrated major policy objectives setting and decision making roles among a small group of

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[34] The Accord was renewed seven times over the period between 1983 and 1996 when the ALP was in office. For details of the Accord and its meanings in domestic politics, see, for instance, Stilwell (1986), Singleton (1990) and Matthews (1994).

[35] For instance, the negotiation process of the Australia-Japan Trade Agreement of 1957 was conducted mainly by the then Minister for Trade, John McEwen and the Department of Trade. See Stockwin (1972).

[36] For the political process of the expansion of protection and McEwen's strategy to broaden political support for his Country (late National) Party, see Bell (1993), especially chapter 2.

[37] This major restructuring of the department was not confined to the merger of the Department of Trade and Foreign Affairs. The number of Departments were reduced from 27 to 13, creating so-called "super departments" such as the Department of Industry, Technology and Commerce, the Department of Primary Industry and Energy and the Department of Employment, Education and Training.

ministers and their policy advisers. For instance, the decision to undertake a major bureaucratic restructuring in 1987 was made by Hawke and his immediate policy circle, and his APEC initiative of 1989 was formulated by only a handful of people, including his policy advisers and senior officials from the DFAT.[38] After Keating became Prime Minister in late 1991, foreign economic policy, and particularly APEC policy, was managed by Keating himself with inputs from his policy advisers, and the Ministers for Foreign Affairs, Trade and some others. This small policy circle decided a basic guideline for foreign economic policy directions and let respective Departments formulate detailed policies. The Department of the Prime Minister and Cabinet played the role of a strong coordinator of policy plans brought up from other Departments. The Department of the Prime Minister and the Cabinet seemed to have power to make other Departments revise their policy plans if they were not quite in line with the original guideline.[39]

IV. Tentative Conclusion

This paper tries to establish a general framework for analysing the foreign economic policy making process in middle-sized states. It also attempts to apply parts of an analytical framework to examine why the major shift in foreign economic policy in Australia took place in the 1980s by focusing only on the change in the international economic environment and the state's response. I realise, however, that this application falls short in some respects. Thus, my conclusions for this paper are necessarily tentative. The aspects of foreign economic policy making in Australia that are untouched by this paper, namely the relations between the state and interest groups and the impact of change in the international economic environment on domestic interest groups, as well as much more detailed analysis of the state's role, remain to be explored in the near future to fully understand the whole picture of Australia's foreign economic policy since the 1980s. The whole picture, when attained, will also be a basis for an analysis of the economic policies of the Liberal/National coalition that was returned to office in March 1996 for the first time since 1983.

[38] See Funabashi (1995).
[39] See Figure 3 in Okamoto (1996) for an image of the bureaucratic policy making structure of the Keating government.

The analytical framework set in this paper can be summarised as follows:

1. The international system/environment, defined as the distribution of power and economic wealth among states, can be taken as an independent variable for foreign economic policy making in middle-sized states. The international environment also includes the spread of dominant idea(s) for policy practices over states in certain periods of time. The system/environment sets the limit to policy options that a state can undertake. Thus, changes in the international system/environment inevitably affect states' foreign economic policy.
2. Under the policy options set by the international system/environment, a state takes up policies to realise its objectives (national interests). To understand why particular policies are taken up among available options in certain periods of time, it is necessary to examine the domestic foreign economic policy making processes of different states. The focus should be set on actors in the process (policy makers) such as Prime Minister and other Ministers according to policy areas, their policy advisers and senior bureaucrats in economic ministries/departments. How do they see the problems at hand and what do they believe to be solutions to achieve their objectives? The structure of bureaucratic process, especially when it is changed by political leaders, should also be closely examined.
3. Even if one takes the "statist approach", that is the state is relatively free from domestic pressures to set its policy objectives (national interests) and implement policies to realise them, the state's relations with domestic societal groups (interest groups) cannot be totally discarded. Depending on the issues at hand, the policy demands of particular groups of a society can have influences on political leaders because those groups constitute their political support bases. When the state makes changes in foreign economic policy, the previous relations between the state and societal groups must have changed somehow because new policies inevitably affect the previous relations. Some parts of the society may be able to gain (and others to lose) from the change. In any case, the government has to adjust their policy objectives and domestic policy demand.

4. As explained above, the international system/environment sets the limit to policy options of a state. It is important to note that the international system/environment can also have an impact on the attitude of societal groups. Changes in the international economic environment may force traditionally powerful interest groups to decline and/or new groups to arise. These changes also make interest groups change their policy demands. Re-organisation of domestic interest group coalitions and changes in their policy demands due to changes in the international environment, thus, will affect a state's foreign economic policy.

The summary of the application part of this paper, which focuses on change in the international economic environment and the role of the Australian state, is as follows:

1. The international economic environment had a fundamental influence on the change of Australia's foreign economic policy in the 1980s. The deterioration of the terms of trade in the early 1980s acted as a catalyst for policy change, and another decline in the terms of trade in the mid 1980s made the process irreversible. Australia turned its economic policy from traditional protectionism to liberalisation and deregulation of the domestic economy. At the same time, the ALP government started to direct the geographical emphasis of economic relations towards the Asia Pacific region, especially East Asia, realising the importance of reflecting economic reality (rapid development of its transactions with economies in the region since the 1960s) in policy practices. In addition, in the 1980s, the world wide acceptance of policy practices according to the idea of the market-oriented economy (neoclassical economic theory) provided a favourable environment for this policy change.
2. The influence of the international economic environment explains why Australia needed to change its foreign economic policy, but does *not* explain why it happened decisively at this particular time. Deterioration of the terms of trade had happened earlier in the 1970s too, and there had been arguments and suggestions forwarded, as well as attempts made, by the previous governments to abandon protection of domestic

industries. Why then was change in the international environment dealt with by policy makers in Australia so decisively from 1983?

The change of government from the Liberal/National coalition to the ALP in 1983 made easier a decisive change in foreign economic policy, even though there were signs of change by the previous government in the early 1980s. To achieve their policy objectives (national interests), including the micro and macro restructuring of the domestic economy, new actors in the policy making process within the ALP government had taken up the idea of market-oriented economy policy practices (often referred as "economic rationalism"). With strong leadership, these actors made and implemented policies accordingly.

3. Actors within the ALP government also restructured policy making institutions. Using its traditional tie with trade unions, the government made policy agreements with the ACTU (the Accord) to pursue its objectives, thus bringing trade unions into the policy making process as an important actor. The government also changed the bureaucratic process of policy making by undertaking a major departmental reorganisation in 1987. In addition to the physical restructuring of the policy making process, the ALP government gave the major role of foreign economic policy objective setting and decision making to a small group of policy makers: Prime Minister and other economic ministers, their policy advisers and senior bureaucratic officials. Their strong leadership, along with the powerful policy coordination role played by the Department of the Prime Minister and the Cabinet, set a firm and irreversible change in Australian foreign economic policy orientation.

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