

THE IMPORT-REPLACEMENT THEORY

THE theory of import-replacement is one of the most serious fallacies in Australian economic thinking since the war.

The theory is based on the assumption that the great development taking place in the manufacturing field will reduce the dependence of the economy on imports. With one or two exceptions it is admittedly hard to find explicit affirmations of this idea. But that it has been implicit in much of our economic thought and policy there can be no doubt, and, in the years following 1952, when import restrictions were first introduced, import-replacement almost assumed the proportions of a national dogma. It was widely believed that a solution to the balance-of-payments deficiency could eventually be achieved by the progressive substitution of local production for imports. Under the influence of this notion, the test to be applied to a projected new industrial development was not so much the basic economic criterion of cost as the technical feasibility of producing the article in question in Australia.

But over the last few months there have been signs that opinion is shifting and that the hopes which were held that the external problem could be solved by the process of substituting home production for goods previously imported, are being abandoned. The Prime Minister himself, and at least one of his senior Cabinet Ministers, have expressly stated that a programme of industrialisation far from reducing the total import requirements of the economy, inevitably increases them. In November, addressing the South Australian Chamber of Manufactures, the Rt. Hon. John McEwen, Minister for Commerce and Agriculture, said: "There is no record in history of any nation which has expanded its industrial structure without at the same time constantly increasing its import demands. That goes for the United Kingdom, the United States, for Germany, for Japan, and for every modern industrial nation".

Economists, too, are today less confident in the doctrine of import-replacement than they were a comparatively short time ago. Confidence in the doctrine is being destroyed by the hard fact that despite a doubling of output and the employment of 30% of the working population in the manufacturing industries—as against 20% two decades ago—Aus-

tralia's imports, in quantity, have risen by nearly 100%. Even on a per capita basis, imports, in 1954/5, were around 40% greater than before the war.

There are, admittedly, two, although extremely limited, senses in which the doctrine of import-replacement may be said to be valid. The first is the obvious one that if a nation launches the production of a certain article, previously imported, on a scale sufficient to supply all, or a good part of, the total demand it has thereby reduced or removed the need for importing that article. If, for instance, as a consequence of developments since the war we were now meeting our entire requirements for, say, domestic refrigerators from our own production, then it follows that we would have removed the need to buy refrigerators from other countries. In the narrow sense, import-replacement would have occurred. We would have replaced imported refrigerators by the product of local factories. It is wrong, however, to deduce from the simple technical fact that we are now making something we did not make before, that we have thereby necessarily rendered the economy as a whole less dependent upon imports. With some forms of production there may be a real net saving of imports; but with others, particularly perhaps those which have to import the major part of their raw materials and components, this may not be so.

There is a second limited sense in which import-replacement may be said to have taken place. This is where, as a consequence of our manufacturing development, we are meeting the demands of our greatly expanded economy for a commodity or material which we would otherwise have to import, or to import in greater quantity, than is, in fact, the case. For instance, the Australian economy today requires a great deal more steel than before the war. If, in the interim, steel production had not been increased by around a million tons a year, then to maintain the present level of the economy's requirements of steel, we would have had to import an additional million tons.

IN this sense, import-replacement has of course occurred over a wide field. Indeed, it is on this aspect of import-replacement that the supporters of the doctrine have largely rested

their case. They have pointed out that if the capacity of Australian manufacturing had not been vastly expanded then we would have been compelled to import in infinitely greater volume to sustain the present population at its existing standard of living. This, of course, is indisputable. Unfortunately for its advocates, the argument is wholly beside the point.

From the standpoint of achieving a balance in overseas trading, the only test of import-replacement that matters is whether the industrialisation that has occurred has resulted in an over-all reduction in the economy's import requirements. On the facts—to which we drew attention above—it is perfectly clear that industrialisation has not produced this result. It has not produced it in terms of absolute quantities of imports, nor has it, so far, produced it in relation to the general size of the economy. Imports, and related payments, today amount to over 25% of national income (even with restrictions) as compared with under 20% in the pre-war years. The only test of import-replacement that means anything, so far as the balance of payments is concerned, is whether, at this point of time, we require less imports than we did last year, or five years or ten years ago.

THE supporters of import-replacement have overlooked three vital considerations.

First, as Australian industry must import quite a large proportion of its requirements of raw and semi-processed materials, essential component parts and capital equipment, the direct net gain, if any, in replacing imports by home production is not nearly so great as it may at first sight seem. To take the example of steel again: It is wrong to claim—as the advocates of import-replacement sometimes do—that because steel production has expanded by one million tons we are thereby saving each year imports to the value of one million tons of steel. To get the true direct import-saving there has to be deducted the additional imports of materials and equipment made necessary by the expansion of the capacity of the local industry. Moreover, even this only covers the net position in the industry itself. What is frequently overlooked is that to produce, or expand, the production of a given article

in Australia requires not only the establishment of a factory to manufacture it, but a whole range of auxiliary activities—for instance, other local industries must be expanded to provide equipment and materials, transport, power and other services. An expansion in the capacity of an industry such as steel leads to an increased demand for the products and services of all the other industries on which the steel industry depends. To cater for these increased demands, these industries must in turn expand their capacity and, in the process of doing so, they will add to their requirements of imports.

Second, the additional demands on imports made by the increasing population, a big proportion of whom are employed in the "import-replacement" industries themselves. This increased population gives rise directly to increased demands for imports of consumer goods, such as tea and coffee, not produced in Australia; and indirectly, by encouraging an expansion of investment and output in local industries, it leads to additional imports of the equipment, raw materials and parts required by the enlarged industrial structure.

Third, the increasing demands for imports as real incomes and living standards rise.

A good example of these processes is to be found in the manufacture of locally-produced cigarettes and tobacco. In 1954/5 we produced 44.8 million lbs. of tobacco and cigarettes, as against 23.3 million lbs. in 1938/9. Over the same period the increased local production necessitated an increase in imports of unmanufactured tobacco from 23 million lbs. in 1938/9 to 43 million lbs. in 1954/5. Even so, in spite of the greatly increased local production, the greater population and higher standards of consumption per head gave rise to an increase in imported cigarettes and tobacco from $\frac{1}{4}$ million lbs in 1938/9 to over 3 million lbs. in 1954/5.

Indeed, over a wide range of commodities, examples of which are given in the two Tables, a similar process has taken place; a considerable expansion of local production has been accompanied by a rise in imports (see Table I). Table II gives examples of how increases in local production have compelled large increases in imported raw materials.

TABLE I.
Imports and Local Production in Australia—Pre-War & Today

	Unit	1938/9		1954/5	
		Local Prod.	Imports	Local Prod.	Imports
Copper—refined	tons	17,500	72	31,800	28,000
Newsprint	thous. tons	—	178	73.1	214
Steel Bars & Rods	thous. tons	387	5.9	416†	74.5
Steel Sheet—plain	thous. tons	138	39.9	230†	116.2
Electric Motors	thous.	32	146	1,185	261
Cotton Cloth	mill. sq. yds.	5.4	198.1	35.1	305.7
Cotton Yarn	mill. lbs.	11.7	4.8	41.2	6.4
Cigarettes & Tobacco	mill. lbs.	23.3	0.7	44.8	3.2
Gloves	thous. doz. prs.	62*	437	330	510
Socks & Stockings	thous. doz. prs.	3,800	40	5,200	501
Whisky	thous. gals.	271	523	451	609

* Excluding dress gloves which, in 1954/5, were nearly ird of total output.
† 1953/54.

Sources:—Production and Oversea Trade Bulletins.

TABLE II.
Output of Finished Products and Related Importation of Raw Materials.

Industry	Unit	1938/9	1954/5
Motor Vehicles			
New Vehicles—registered	thous.	79	233
Imports			
Built-up Vehicles	thous.	2	43
Motor Bodies	thous.	1	38
Unassembled Chassis	thous.	75	124
Parts	mill. lbs.	4.1	51.4
Motor Spirit Produced	mill. gals.	23	325
Crude Petroleum Imported	mill. gals.	54	927
Rubber Tyres Produced*	mill.	2.2	3.5
Crude Rubber Imported	thous. tons	15	44
Tobacco Manufactured	mill. lbs.	23	45
Imports Unmanuf. Tobacco	mill. lbs.	23	43
Paper Produced	thous. tons	42	79†
Pulp Imported	thous. tons	64	107
Fertilizers & Chemicals			
Superphosphate Produced	thous. tons	1,199	1,964
Sulphuric Acid Produced	thous. tons	490	827
Imports—Phosphate Rock	thous. tons	800	1,084
—Sulphur	thous. tons	115	193
Cement Sheets Produced	mill. sq. yds.	9.5	27.8
Asbestos Imported	thous. tons	92	132
Wirelesses Produced	thous.	164	444
Wireless Valves Imported	thous.	496	905
Cotton Yarn Produced	mill. lbs.	11.7	41.2
Raw Cotton Imported	mill. lbs.	11.9	52.2

* 1938/9 figure includes bicycle tyres; 1954/5 figure is motor vehicle tyres only.
† 1953/54.

Sources:—Production and Oversea Trade Bulletins. Petroleum Information Bureau.

THE astonishing post-war manufacturing development is something of which all Australians can be greatly proud. It has been a magnificent achievement which bears witness to both the enterprise and high technical competence of Australian management and the skill of its workers. That we are on the verge of a great industrial future there can be no doubt. But this future will be the more assured if we concentrate our efforts on those things we can do most efficiently and where our natural advantages are most pronounced.

The final test of whether Australia should attempt to produce commodities or materials previously imported, boils down to a question of real costs. It is not sufficient to have the human and physical resources and even the technical know-how to produce a certain article. The root question is whether we can produce it at a cost which is comparable, or has prospects of becoming comparable, with overseas costs. To squander resources in directions in which there is little hope of achieving near-world levels of productivity would only make the balance-of-payments problem still more intractable as well as reduce the Australian standard of living.

The important thing for Australia now is to make up its mind what things it can do best, to concentrate its efforts and resources in those directions, and to vigorously prospect the export field. Nations much poorer in natural resources than Australia, notably Switzerland, have achieved a high standard of living by realising their own limitations. It should be clear by now that to spread our efforts over too wide a range of production in an attempt at "import-replacement" is to chase a dangerous "will-o'-the-wisp" which would land us in Argentinian economic swamps.

