Australia in the Asian Century
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Australia China Business Council: Submission to the White Paper on Australia in the Asian Century

1.1 Executive summary

Australia’s current terms of trade boom stems from China’s unprecedented demand for our bulk commodities.

In 2010-11, Australia and China engaged in over $113 billion of two-way trade. With China becoming our largest trading partner in 2007-08, increased bilateral trade and investment was instrumental in sparing Australia from the worst effects of the global financial crisis.

Our relationship with China reflects the highly complementary nature of the two economies — with Australia being a prime provider of bulk commodities to an expanding Chinese market.

Notwithstanding our current fortuitous set of circumstances, Australia’s long-term political and economic engagement with China risks falling behind other major economies such as the United States, Canada, the United Kingdom, Brazil, Germany and the European Union.

Excessive reliance upon minerals export capacity distorts the character of the emerging and potential relationship and overshadows other emerging business opportunities.

Government must work proactively across industry, the media, state and local governments and indeed the wider community to construct a comprehensive China engagement strategy to prepare the economy for the next phase of China’s development. This will be characterised by high value designed-in China goods, rather than low value made-in China goods and the flow of high value services form China to Australia. This changes the paradigm for Australian business.

This submission will focus on a range of areas including:
- The benefits to Australian households of trade with China
- China’s role in the future of Australia’s manufacturing industry
- China’s role in Australia’s regions
- Bilateral infrastructure cooperation
- The future of two-way investment flows
- Australia’s diplomatic deficit.

1.2 Recommendations

The Council’s Submission makes a number of important policy recommendations including:
- Consider the introduction of government subsidies and incentives to high-tech and low carbon manufacturers prepared to enter local joint ventures with Chinese companies such as
  - Double the Export Market Development Grant (EMDG) for manufacturers in high-tech and low carbon industries
  - Provide additional funding via Australian Research Centre (ARC) linkage grants to universities that develop partnerships with Chinese counterparties in high-tech and low carbon industries
  - Lower the threshold for EMDG eligibility so that smaller SMEs are given the opportunity to expand into this market. This will also offset the impact of a consistently higher Australian dollar.
  - Develop a comprehensive fully funded export and investment promotion strategy utilising shared networks of government agencies including Enterprise Connect and peak business bodies such as the Australia China Business Council

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1.3 Broader strategic questions for the White Paper Taskforce

- What are Australia’s key performance indicators for measuring the effectiveness of its China engagement strategy over the short, medium and long-term?
- Should the Australian Government impose a deadline for concluding negotiations towards a comprehensive Australia China free trade agreement?
- What are the key areas of growth in the Chinese economy beyond the 12th five year plan and how can Australian business effectively source these opportunities?
- What is the Australian Government’s strategy to expand Australia’s diplomatic footprint in China as well as strengthen China expertise across government?
- How should the Australian Government most effectively work with state, territory and local governments in developing a comprehensive China engagement strategy?
- Does Australia possess sufficient tourism infrastructure to service the forecast growth in Chinese tourist arrivals?

- Establish a government funded regional development initiative to increase Chinese investment and in-market awareness of core infrastructure priorities and community services in rural and regional Australia.
- Provide additional funding via ARC linkage grants to academic institutions that develop partnerships with Chinese counterparties focused on research and development in rural and regional Australia.
- Improve capacity of foreign investors and joint venture partners to secure skilled labour in major resources projects to address capacity constraints and manage wider inflationary pressures.
- Secure increased access for companies in major infrastructure projects as part of any bilateral infrastructure memorandum of understanding or free trade agreement.
- Establish a formal government to government infrastructure working group with representation from the business community.
- Strengthen policy and legislative mechanisms to support a greater role for Chinese capital in major infrastructure projects.
- Maintain Australia’s proactive foreign investment attraction program tempered by transparent approval processes and increased liberalisation.
- Execute a bilateral investment framework as part of any Australia China free trade agreement.
- Establish a fully funded China Market Readiness Initiative to increase awareness among Australian companies and facilitate greater Australian investment in China.
- Formalise the Australia China Economic and Trade Cooperation Forums (ACETCF) at a government to government level.
- Strengthen the Australia China Joint Ministerial Economic Commission (JMEC) through the creation of a formal business dialogue.
- Establish an Australian consulate-general in Chengdu or Chongqing.
1.4 About the Australia China Business Council

The Australia China Business Council (ACBC) is the premier organisation for the promotion of trade and investment between China and Australia. ACBC is a national organisation with branches in New South Wales, Northern Territory, Queensland, South Australia, Victoria and Western Australia.

The membership of ACBC comprises a broad cross section of over 1000 large, medium and small companies from a diverse range of industries – all united by a commercial interest in China.

ACBC is widely regarded as a thought leader on matters affecting Australia’s commercial relationship with China and maintains excellent relationships with both Chinese and Australian governments at the highest levels. ACBC has been a respected host for visiting Chinese leaders including Hu Jintao, Wu Bangguo, Xi Jinping, Wen Jiabao and Li Keqiang.

ACBC organises flagship conferences and events combining first class networking opportunities with major Chinese companies and forums for discussion of significant policy issues. ACBC has been the official organiser of the flagship Australia China Economic and Trade Cooperation Forums for the past two years.

These events have been collectively attended by two Australian Prime Ministers, five federal ministers, the Chinese Vice-President and Vice-Premier, and by more than 1000 company executives on both sides of the bilateral relationship.

The Council has a rapidly growing program in China and organises trade missions to key Chinese jurisdictions, high-level policy dialogues and opportunities for its key stakeholders to engage directly with senior Chinese businesspeople and officials.
2.1 The benefits to Australian households of trade with China*

Ordinary Australian households have benefited considerably from Australia’s increased trade and investment with China. The benefits of trade impact households in a variety of ways:

- Higher company tax receipts allow the government to invest in core community infrastructure and services such as roads, schools and hospitals
- Greater employment opportunities in rural and regional Australia
- Stronger Australian dollar means more competitive pricing for consumer goods
- Terms of trade boom means continued growth in real wages across a number of sectors.

In 2010-11, Australia and China engaged in over $113 billion of two-way trade (total of imports and exports). This relationship reflects the highly complementary nature of the two economies — with Australia being a prime provider of inputs to an expanding Chinese market.

In 2010-11, the average value of trade per household was just over $13,400, up around 30 per cent from last year and 93 per cent since 2006-07. Over the last five years, the average value of two-way trade per household increased by about 18 per cent per annum.

Australia’s resource and commodity exports to China continue to be bountiful. However, tourism and education are two service-oriented exports with growing Chinese markets.

Since 2007-08, China has been Australia’s largest trading partner for both exports and imports.

Trade with China has allowed Australia to consume cheaper manufactured imports, helping to facilitate previously uneconomic projects while exporting resources and commodities whose prices have been rising. In 2010-11, exports per household amounted to $8,370 and imports per household were $5,100.

Chinese investment in Australia has been growing, reaching $19.5 billion in 2010. Investments have not been limited to the resources sector – services, research and development, agriculture, and retail investment have been growing over the years.

* This section draws extensively on the 2012 update to the ACBC’s report prepared by the Allen Consulting Group titled The Benefits to Australian Households of Trade with China
2.2 Household Trade: Across the States and Territories

All States & Territories across the country have benefited from trading with China.

China’s growing demand for resources and commodities is beneficial for resource rich states such as Western Australia and Queensland, where trade per household is $58,300 and $6,500 respectively.

Trade in services — especially tourism and education — continues to grow.

New South Wales and Victoria are the two largest importers of Chinese goods, mostly importing manufactured consumables from China. Trade per household in New South Wales is $9,000 and in Victoria it is $7,000.

Australian States & Territories are either net exporters or net importers in terms of their trading relationship with China. For most States & Territories, China is their largest trading partner. China is the largest two-way merchandise trading partner for New South Wales, Victoria, South Australia, Western Australia and Tasmania, and the second largest for both Queensland and the Northern Territory, coming just behind Japan (DFAT 2012).

Western Australia engaged in the highest level of trade with China ($50.5 billion). On a per household basis, China is also the largest trade partner for Western Australia, with $58,300 of trade per household. While the Northern Territory engaged in one of the lowest levels of trade with China ($1.2 billion), this equated to about $16,900 per household — the second highest compared to other states, and ahead of New South Wales, Victoria and Queensland (DFAT 2012).

Key exporting states to China include Western Australia and Queensland. These states principally export resources, commodities and raw materials. Western Australia exported about $50.5 billion and Queensland about $10.9 billion of goods to China. For Queensland, this equates to about $6,500 of trade per household. Households in exporting states have benefitted directly from rising incomes — although household spending in resource rich states are distributed throughout the economy through the multiplier effect as well.

New South Wales and Victoria are two major net importers of China’s goods, mainly importing manufactured consumables such as furniture, sporting goods and clothing. New South Wales imported about $20.5 billion worth of Chinese goods, with total trade per household at $9,000. In Victoria, the second largest importer of Chinese goods, trade per household is about $7,000. While households in net importing states have benefitted from cheaper Chinese imports, the benefits are not limited to those states. These manufactured imports are distributed to the rest of Australia, benefitting households overall.
2.3 China is a major consumer of Australian products

In 2010-11, China consumed over $70 billion of goods and services produced in Australia — about $8,370 per household. Exports to China also included $5.7 billion of services.

The market share for Chinese exports is almost 24 per cent, and the value exported to China is almost four times that of India’s ($18 billion) and about five times that of the United States ($14 billion) (DFAT 2011). Exporting to China benefits Australian households in a number of ways — such as providing more job opportunities (both directly and indirectly), increases in share prices and dividends, improved terms of trade and new business opportunities.

Australia’s major export items to China include iron ore and concentrates, coal, copper ores, other metal ores, crude petroleum and wool. Exports to China outpaced Japan in 2009-10 and 2010-11 to become Australia’s top export market. However, the services sector provides significant opportunities for export trade as well — in 2010-11, Australia exported about $5.7 billion of services to China. This is a 58 per cent increase from 2006-07 ($3.6 billion) (DFAT 2011).

In addition to the increased incomes generated mainly by the mining sector, households also profit from the business and employment opportunities that result from trade in the service sector.

**CHINA HAS OUTPACED AUSTRALIA’S OTHER TOP TWO MARKETS FOR INTERNATIONAL STUDENTS**

![Graph showing CHINA HAS OUTPACED AUSTRALIA’S OTHER TOP TWO MARKETS FOR INTERNATIONAL STUDENTS](image)

*Source: Department of Immigration and Citizenship (2011), Student visa program trends 2004-05 to 2010-11.*

**AUSTRALIA’S EXPORTS TO CHINA RELATIVE TO MAJOR TRADING PARTNERS**

![Graph showing AUSTRALIA’S EXPORTS TO CHINA RELATIVE TO MAJOR TRADING PARTNERS](image)

*Source: Department of Foreign Affairs and Trade (2011), Composition of Trade 2010-11.*

The tourism and education markets are key growth sectors for export to China. In 2010-11, China was the top source country for international students with almost 50,000 student visas granted to Chinese nationals (DIAC 2011). The chart below left shows that international Chinese students have outpaced Australia’s other top two source countries for international students, India and South Korea. Although the number of Chinese students dropped by 10 per cent from 2008-09 to 2010-11, this was part of a broader trend where total visas granted for international students dropped by 22 per cent for the same period.

Tourism is also a growing market — China is one of the top three visitor origins for tourism in Sydney, Melbourne, Gold Coast and the Australian Capital Territory. In 2010-11, Sydney had about 277,000 Chinese visitors, followed by Melbourne (233,000 Chinese visitors), the Gold Coast (118,000 Chinese visitors), and the Australian Capital Territory (18,000 Chinese visitors) (Tourism Research Australia 2011).
2.4 China is a major supplier of cost-competitive consumer products

Imports from China provide access to cost-competitive goods and improve consumer choice. Australia imported close to $43 billion of Chinese products in 2010-11. This is about $5,100 per household.

These have mainly been manufactured goods such as telecommunication equipment, clothing and computers. In 2010-11, Australia imported close to $43 billion of Chinese products. The average Australian household purchased about $5,100 worth of Chinese imports — a 16 per cent increase from the previous year.

Manufactured goods consumed by Australian households typically include telecommunication equipment, textiles, computers, furniture and other consumables such as clothing and footwear. Australian households benefit from access to Chinese goods due to lower prices and improved consumer choice, ultimately increasing the welfare of households. The purchasing power of households would have been considerably lower if not for the availability to cheaper manufactured goods from China.

Trade with China has helped keep inflation low. As illustrated in our previous report, over the past few years significant increases have been observed in the prices of sectors such as housing, health and education products. However, price deflation has been evident in telecommunication equipment and clothing — two significant imports from China. From June 2007 to June 2011, telecommunications equipment import prices decreased at an annual average rate of 10 per cent, while clothing import prices decreased at 0.6 per cent. This compares with an increase in the consumer price index of 3.2 per cent within the same period.

### Principal Imports From China By Category, as Million

<table>
<thead>
<tr>
<th>Product category</th>
<th>2006-07</th>
<th>2007-08</th>
<th>2008-09</th>
<th>2009-10</th>
<th>2010-11</th>
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<tbody>
<tr>
<td>Telecom equipment &amp; parts</td>
<td>2,081</td>
<td>2,606</td>
<td>3,121</td>
<td>3,359</td>
<td>4,209</td>
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<tr>
<td>Textiles, footwear &amp; clothing</td>
<td>4,207</td>
<td>4,321</td>
<td>5,255</td>
<td>4,675</td>
<td>5,245</td>
</tr>
<tr>
<td>Computers</td>
<td>2,249</td>
<td>2,530</td>
<td>2,795</td>
<td>3,524</td>
<td>4,033</td>
</tr>
<tr>
<td>Prams, toys &amp; sporting goods</td>
<td>1,404</td>
<td>1,632</td>
<td>2,197</td>
<td>1,909</td>
<td>1,764</td>
</tr>
<tr>
<td>Furniture, mattresses &amp; cushions</td>
<td>1,205</td>
<td>1,373</td>
<td>1,620</td>
<td>1,537</td>
<td>1,639</td>
</tr>
<tr>
<td>Other</td>
<td>15,994</td>
<td>18,532</td>
<td>22,056</td>
<td>21,371</td>
<td>24,219</td>
</tr>
<tr>
<td>Total imports</td>
<td>27,140</td>
<td>30,994</td>
<td>37,044</td>
<td>36,374</td>
<td>41,109</td>
</tr>
</tbody>
</table>

3.1 China’s role in the future of Australia’s manufacturing industry

3.2 Procurement of Chinese Equipment*

The procurement of Chinese equipment in Australian resources projects has become an issue for certain stakeholders with an interest in the local manufacturing industry and has generated significant media coverage.

Specifically, manufacturing unions are actively lobbying the Commonwealth to introduce incentives for resources companies that provide preferential procurement treatment to local Australian firms. This protectionist posturing not only risks the viability of resources projects; it contradicts the basis of the past three decades of Australia’s trade policy and threatens the continued development of productive relationships with our major trading partners.

Research by the Minerals Council of Australia demonstrates that procurement of local equipment for resources projects in Australia stands at 89%.

Resources companies must be given the flexibility to procure cost-effective Chinese equipment where appropriate. Given the scale of many current resources projects, prudent procurement decisions are vital in ensuring projects are kept within budget and completed to schedule – thus reducing unnecessary inflationary pressures on the broader Australian economy.

The savings on Chinese procured equipment are significant and can be found in a wide range of areas including:
- Steel structures
- Coal handling equipment
- Crushers
- Stackers
- Reclaimers
- Power generation equipment.

Much of these types of equipment is now manufactured by western companies under OEM arrangement. There is no evidence to support assertions that Australian companies are forced into procuring Chinese equipment in return for securing offtake agreements. Australian companies will make prudent procurement decisions based on cost efficiencies, productivity gains to projects, and are often motivated to obtain finance through the several buyer credit related facilities in exchange for purchase of Chinese-manufactured industrial goods.

Chinese companies are keen to deliver lead engineering roles in Australia as platforms for the deployment of Chinese manufactured goods. The Australian Government and all stakeholders ought to encourage, at every opportunity, Chinese companies to enter into joint ventures with Australian partners to deliver projects in Australia.

3.3 Research and Development Investment in China

Notwithstanding the pressure on Australia’s manufacturers stemming from a high Australian dollar, weakening demand from traditional markets and the continued rise of competitive Asian alternatives, China has an overwhelmingly positive role to play in the future of Australia’s manufacturing industry.

China has surpassed Japan as the globe’s second largest spender on industrial research and development (R&D) and is slated to overtake the United States before the close of the current decade (WIPO 2011). China’s total R&D investment accounted for 12.8% of global spending in 2009, compared with only 2.2% in 1993.

China has embarked on the largest investment in R&D in human history. The 12th Five Year Plan aims to increase total R&D spending to 2.2% of GDP by 2015, an increase from 1.75% in 2010 and 1.3% in 2005 (Economist Corporate Network 2011). Significantly, this will mean 3.3 patents for every 10,000 Chinese citizens. These ambitious targets have been met by significant government support and tax concessions for investors.

Such investment in R&D can be leveraged to attract further investment into R&D in a number of sectors in Australia.

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* See Glasson, Speech to NDRC WA Government MOU Introduction, Perth, Western Australia, 3 February 2012
3.4 Targeted Sectors

The Chinese Government has targeted the following focus points and sectors for investment:

- Energy and resources
- Material Science
- Biotechnology
- Space Technology
- Earth Science
- Nanotechnology
- Agriculture
- Equipment
- Environment protection
- Information and communications technology.

3.5 Implications for Australia

Australia has much to gain as China transforms its own manufacturing base from one geared at servicing traditional export markets and their appetites for consumer goods to one based on higher value, low carbon, high-tech industries.

While concerns over intellectual property have long stood in the way of further collaboration, as China develops patents, innovates domestically and enters overseas markets, greater incentives will emerge to develop a national comprehensive intellectual property protection system. This will in turn provide greater certainty to international companies seeking to develop strategic partnerships with Chinese companies and academic institutions.

The emergence of this new market of such an enormous scale provides a further incentive for Australia to gear industrial policy to encourage manufacturers to widen its value chain and focus on R&D and the key sectors articulated by its largest trading partner.

Australia needs to reduce government subsidies for traditional sectors unless companies are able to demonstrate a willingness to either export to emerging markets or form strategic partnerships and joint ventures with parties in a position to invest in new skills and research in industry sectors geared for the Asian Century paradigm. Governments should examine incentives to encourage manufacturers to enter into joint ventures with companies and provide increased industry assistance to Australian companies prepared to invest and export to emerging markets.

Australia needs to balance the need for fiscal conservatism and the need for cost savings in the federal budget on the one hand, with good industry and export development assistance on the
other. The Commonwealth’s decision to halve Export Market Development Grant (EMDG) entitlements is placing considerable pressure on exporters already feeling the effects of a high Australian dollar. The EMDG is a vital component of industry assistance in developing market access into China and the diversification of Australia’s export earnings outside of traditional sectors of the economy.

Australia’s higher education sector, in its bid to increase our national research output also stands to benefit significantly from establishing partnerships with Chinese universities, the Chinese Academy of Sciences as well as Chinese companies.

3.6 Recommendations

- Consider the introduction of government subsidies and incentives to high-tech and low carbon manufacturers prepared to enter local joint ventures with Chinese companies
- Double the Export Market Development Grant (EMDG) for manufacturers in high-tech and low carbon industries
- Provide additional funding via Australian Research Centre (ARC) linkage grants to universities that develop partnerships with Chinese counterparties in high-tech and low carbon industries
- Develop a comprehensive fully funded export and investment promotion strategy utilising shared networks of Enterprise Connect and peak business bodies such as the Australia China Business Council.

CASE STUDY – Wollongong University innovation campus

The Wollongong University Innovation Campus is the type of institution that could benefit significantly from increased collaboration between Australia and China.

New South Wales’ Illawarra Region reflects the challenges facing Australia’s manufacturing sector as well as the wider Australian economy. With steel production driven offshore, the region’s structural composition as well as and the local workforce’s skills base must adapt to the Asian Century.

The Campus’ website and prospectus is in both English and Simplified Chinese. The Campus has a full-time team dedicated specifically to creating research partnerships between the centre and potential Chinese partners.

The following extract from the campus’ website shows its mission statement and vision:

Our vision is to enhance the economic and cultural wealth of iC participants by providing the best environment in the Asia-Pacific region for people and organisations to exchange and develop ideas and deliver innovative outcomes.

The Innovation Campus (iC) aims to provide an environment for commercial and research entities to co-locate with University of Wollongong teams and establish successful productive partnerships.

Specific outcomes include:

- More productive interface with commercial/ industrial partners
- Diversification of Illawarra economy
- Creation of sustainable employment in the region
- Access to quality office, research, teaching, conference and accommodation facilities
- Growth in the University’s reputation through association with high-profile and/or innovative commercial partners
- Introduction and integration of commercial acumen into University research activities
- Improved research outcomes for students

Source: www.innovationcampus.com.au
4.1 China’s Role in Australia’s Regions

Whilst China’s demand for Australia’s bulk commodities has seen it become a significant importer of resources and an increasingly important investor in rural and regional communities, the development of socioeconomic infrastructure is a major challenge facing the sustainable development of Australia’s regions.

There is a clear business case for greater Chinese investment in Australia’s regions. Securing the foundations for greater investment in regional infrastructure will be vital in ensuring the sustainability of the mining boom and fusing the success of headline resources projects with positive outcomes for regional development.

A 2011 Australian Mines and Metals Association study has shown wages in resource projects increased by more than 40%, leading to projects being reconsidered, refinanced, and there have been significant calls for a large influx of non-Australian labour to facilitate project development. The Australian Bureau of Agriculture and Resources Economics (ABARE) have estimated that Australia will need at least 100,000 skilled workers to complete mining and infrastructure projects.

With the right national interest tests applied, Chinese companies and Sino-Australian joint ventures should be given greater flexibility to balance local employment generation with an appropriate mix of foreign skilled labour where local employment markets are unable to provide labour. Governments must recognise that labour market flexibility is vital in ensuring the viability of major resources projects and managing inflationary pressures in the economy.

Chinese companies have sought publicly to bring large numbers of workers into Australia to complete projects, and have, in some part, been supported by local developers in their quest.

It is difficult to imagine how a large influx of non-English speaking Chinese construction workers would be able to practically execute and EPC arrangement on their own in an Australian context given the differences in design, material, production and safety standards and overall approach to delivering an EPC contract. Chinese have developed an EPC model based on committing human resource to resolve engineering and construction issues as they arise. In contrast to the Chinese model of EPC execution, the Australian model works to reduce human resource input and maximise modularisation.

The answer to labour shortages must lie in co-delivery between Australian and Chinese engineering companies but with the maintenance and deployment of our local standards, English-speaking engineers in senior positions, and genuine integration of management and sufficient support structures to ensure delivery.

Unions ought to bear in mind that if there is no “give and take” in allowing some involvement in the delivery of projects they invest in, China may choose elsewhere and rural and regional employment markets will deteriorate.

Urban development, education and community infrastructure in regions such as the Pilbara, Bowen and Galilee basins are in the fundamental interests of the resources sector – the emergence of sustainable and vibrant cities in our regions will attract more workers and reduce the sector’s dependence on ‘fly in, fly out’ workers and place downward pressure on wages.

Working with industry, communities and across federal, state and local governments, Australia should begin the process of proactively capitalising on China’s interest in our resources sector and focus on attracting greater Chinese capital (as well as collective awareness of Australia’s regional diversity), into our
regions through the creation of a nationwide regional development initiative focused on the following core areas:

- Urban development
- Housing
- Port and rail development
- Education, technology and training (including research and development, indigenous education programs, science and technology, development opportunities for skilled and non-skilled sections of the resources sector, mining and petroleum engineering, photovoltaic engineering, renewable energy).

- Tourism infrastructure (including temporary accommodation, aviation links and airport infrastructure)

A properly resourced regional development initiative could deliver a wide range of qualitative and quantitative outcomes for regional communities as well as industry such as:

- Foundation relationships with relevant Chinese Government agencies
- Foundation relationships with headquarters of Chinese companies with active and/or potential investments Australia’s regions.

**CASE STUDY – Australia China regional investment dialogue**

The Inaugural Australia China Regional Investment Dialogue was hosted by the ACBC in Beijing on Friday 4 November 2011 to coincide with Federal Resources, Energy and Tourism Minister Ferguson’s visit to China.

The dialogue focused on attracting Chinese investment in Australia’s regions and emphasised the importance of infrastructure, tourism projects and housing to the future viability of rural and regional Australia.

The event was attended by the following representatives from various Australian governments:

- The Hon Martin Ferguson AM MP, Federal Minister for Resources, Energy and Tourism
- The Hon Chris Hartcher MP, NSW Minister for Resources and Energy
- The Hon Tom Koutsantonis MP, SA Minister for Mineral Resources and Energy
- The Hon Kon Vatskalis MLA, NT Minister Primary Industries, Fisheries and Resources
- Her Excellency Frances Adamson, Australian Ambassador to the People’s Republic of China
- Mr Drew Clarke, Secretary, Federal Department of Resources, Energy and Tourism

The government representatives were joined by a range of companies including:

- Rio Tinto
- Atlas Iron
- ACCOR Hotels Group
- HRL
- China Railway Materials
- Industrial and Commercial Bank of China
- China Development Bank
- Metallurgical Corporation of China
- Shenhua Group
4.2 Recommendations

- Increased awareness of regional development issues in Chinese Government and industry
- Increased awareness of regional diversity in Chinese Government and industry
- Increased awareness of the role of local governments, indigenous land councils and their interaction with industry other levels of government
- Commitments from Chinese Government and industry to increase engagement with communities
- Increased awareness of local port and rail infrastructure and future development priorities
- Foundation relationships with universities and major companies to support regional R&D initiatives
- Increased understanding of China’s emerging R&D focus related to the energy and natural resources sector
- Increased strategic cooperation between regions and the Chinese higher education sector
- Foundation relationships with Chinese tourism authorities to increase awareness of Australia’s regions
- Foundation relationships with tourism investment platforms to promote investment in regional tourism infrastructure development including hotels and airports
- Promotion of greater aviation links between China and Australia’s regions
- Foundation relationships with urban planning and regional development agencies in China.

- Establish a government funded regional development initiative to increase Chinese investment and in-market awareness of core infrastructure priorities and community services in rural and regional Australia
- Provide additional funding via ARC linkage grants to academic institutions that develop partnerships with Chinese counterparties focused on research and development in rural and regional Australia
- Improve capacity of foreign investors and joint venture partners to secure skilled labour in major resources projects to address capacity constraints and manage wider inflationary pressures in the economy
- Formalise the Australia China Regional Investment Dialogue (ACRID) at a government to government level.
### 5.1 Bilateral Infrastructure Cooperation

#### 5.2 Australia

In Australia, infrastructure bottlenecks remain the most significant challenge confronting our energy and natural resources sector and removing heat in the resources aspect of the bilateral relationship through increased supply and an easing of bulk commodity prices. Infrastructure issues continue to contribute to damaging cost blowouts, supply issues and place inflationary pressure on the broader Australian economy.

The business community strongly supports a greater role for Chinese involvement in Australia’s infrastructure. The ACBC has long advocated the utilisation of Chinese engineering with local Australian engineering support and standards, Chinese cost-competitive equipment, Chinese financing, and the institutionalisation of infrastructure entities with domestic or joint ownership, under local management, giving fixed returns to financiers in a win-win model for both economies.

Producers want to develop infrastructure to provide greater certainty and increase productivity levels, expeditiously delivers product to market, and provides the ability to respond to changes in buyer demand in a timely fashion.

The 2011 University of Sydney-KPMG Australia China Future Partnerships Report cited recent research by the China Council for the Promotion of International Trade (CCPIT), and noted that ‘Chinese companies prefer to invest in in well-developed countries with a large market size and a favourable institutional environment’ such as Australia. Given Australia’s abundance of natural resources, we are especially well placed to benefit from China’s growing interest in infrastructure projects offshore.

The University of Sydney-KPMG report points to Australia’s well established Public Private Partnership (PPP) model, coupled with continued strong pipeline of private investment in infrastructure and generally strong regulatory framework as significant additional contributing factors to China’s interest in Australian infrastructure.

Chinese companies from both the state owned and private sectors have a potentially significant role to play in big ticket infrastructure items such as:

- Transport infrastructure such as bulk-commodity rail, high-speed passenger rail, highways, ports, and airports
- Power generation/energy and utilities
- Upstream, midstream and downstream assets in the oil and gas sectors
- Tourism assets
- Telecommunications
- Educational institutions and R&D ventures.

Generally speaking, Chinese companies find it difficult to win infrastructure opportunities in countries such as Australia because they are used to infrastructure projects that are negotiated on a national level rather than won through local market savvy. Australia needs to recognise the many commercial advantages of collaboration with Chinese parties, and provide the public policy settings to work with Australian companies in the co-execution of EPC contracts, bringing cost competitive equipment, engineering muscle, production capacity, and funding.

To date, there has been limited engagement by government with the bilateral business community specifically on a comprehensive bilateral framework for infrastructure cooperation specifically. The business community would welcome the establishment of a formal government to government infrastructure working group with representation from the business community, supported by a memorandum of understanding to consolidate cooperation to date and set out the framework for future public policy settings.

The nation could benefit considerably from the execution of a comprehensive bilateral agreement with a relevant Chinese Government agency such as the Ministry of Commerce (MOFCOM) and/or the National Development and Reform Commission (NDRC). There are significant lessons to learn from the recently concluded infrastructure agreement between the Western Australian Government and the NDRC.

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* See Glasson, Speech to NDRC WA Government MOU Introduction, Perth, Western Australia, 3 February 2012
5.3 China

China's 12th Five Year Plan places a renewed emphasis on a range of infrastructure priorities and placed ambitious investment targets on sectors including*:

- Energy
- Energy conservation
- Housing infrastructure
- Healthcare (and associated services such as insurance)
- Transportation and logistics
- Aviation.

China's new focus on reducing carbon emissions presents immediate synergies with emerging investment in Australia's clean energy sector associated with the implementation of a price on carbon emissions and the Federal Flagship Funding Program.

China's efforts at developing public housing infrastructure will continue to bode well for the energy and natural resources sectors, whilst concurrently opening new opportunities for Australian architects, construction firms, engineers, urban planners and financial services providers.

Australia's aviation industry stands to benefit considerably from China's continued investment in airport construction as well as capacity increases aimed at catering for projected forecasts in domestic and international passenger volumes.

China is forecast to construct an additional 45 airports and invest more than $232 billion in the nation's civil aviation industry as part of the 12th five year plan (Centre for Asia Pacific Aviation). Passenger numbers are expected to almost double to 450 million by 2015 and Chinese aircraft manufacturers are looking to commercialise the rollout of a single aisle jet over the same period (Centre for Asia Pacific Aviation).

Whilst these priorities present a range of potentially lucrative opportunities for Australian businesses, there are a range of policy challenges and risks associated with gaining entry to the market. The immediate barriers to entry have been identified as follows:

- The risk of new environmental taxes and increased cost compliance associated with the energy sector
- Regulatory discord between provincial and central governments delaying Beijing's health policy reform and increased cost compliance associated with new legislation
- Limited capacity for developed economies to engage with China's freight and logistics sector as well as considerable gaps in infrastructure quality across jurisdictions
- Restrictions limiting the capacity for foreign airlines and infrastructure consortiums to establish joint ventures with Chinese airlines and civil aviation companies
- Under resourced Australian diplomatic/trade and investment promotion footprint in China.

5.4 Recommendations

- Secure increased access for companies in major infrastructure projects as part of any bilateral infrastructure memorandum of understanding or free trade agreement
- Establish a formal government to government infrastructure working group with representation from the business community
- Strengthen policy and legislative mechanisms to support a greater role for Chinese capital in major infrastructure projects.

* See University of Sydney-KPMG Australia & China Future Partnerships Report, pp 24-27 for a comprehensive overview of China's emerging infrastructure priorities and implications for Australian business
6.2 China’s Role as an Emerging Investor in Australia

While trade flows dominate the China-Australia relationship, two-way investment is a smaller but increasingly important component of the relationship. Trade tends to be an important prelude to inward and outward investment, as importers and exporters form increasingly mature supply relationships and growing confidence in each others’ markets. Benefits from trade in ‘goods and services’, while easier to identify, tend to obscure the very real benefits of foreign investment or ‘trade in assets (ACBC ACG Benefits to Australian Households of Trade with China, 2009’.

In the context of increasing negative public commentary concerning perceived excessive levels of Chinese investment in Australia, it is crucial to note that whilst Chinese investment is growing, China is the 10th largest source country of Foreign Direct Investment (FDI). The following table, whilst not including special-purpose vehicles data, demonstrates that China still ranks significantly behind a raft of Australia’s traditional trading partners:

Australians households benefit directly by way of new job creation and increased incomes and less directly through the redistribution of company taxation and royalties revenue by governments. The benefits of direct ‘bricks and mortar’ investment can be more sustainable and less subject than trade to adverse developments in the world economy. This is because it involves a substantial commitment to Australia by the investor.

Australia has historically been heavily reliant on FDI to meet a shortfall between domestic saving and domestic investment. FDI continues to be vital for supplementing local savings. It takes the form of purchase of real estate; joint venture/acquisition of existing enterprises and creation of new companies. It has assisted Australia achieve higher rates of economic growth and employment.

Foreign purchase of Australian assets frees up additional funds for spending by Australian residents. In addition, when these assets are purchased at higher prices than Australians are willing to pay, the Australian owners create additional income for themselves for investment or consumption. Without foreign capital flows, reliance on domestic savings, would tend to put upward pressure on long term interest rates. This obviously significantly impacts Australian households.

Australian households have also been direct beneficiaries with expanded employment opportunities generated by a more competitive export-oriented industrial structure. This flows

| Stock of FDI in Australia by Major Markets (A$ Million) |
|-----------------|-----------------|-----------------|-----------------|-----------------|
| Country         | 2004            | 2005            | 2006            | Share % Rank in 2009 |
| United States of America | 145,130         | 75,554          | 66,599          | 106,511 99,758 99,161 22.7% |
| United Kingdom  | 43,572          | 52,501          | 55,822          | 64,458 61,390 63,177 14.5% |
| Japan           | 18,110          | 21,403          | 23,819          | 31,100 33,576 44,953 10.3% |
| Netherlands     | 17,937          | 21,365          | 24,633          | 25,273 28,691 33,610 7.7% |
| Switzerland     | 9,540           | 11,821          | 16,646          | 16,363 19,512 17,543 4.0% |
| Germany         | 8,418           | 9,754           | 10,555          | 17,515 13,057 15,389 3.0% |
| Singapore       | 5,137           | 4,201           | 5,590           | 14,189 19,419 19,826 3.6% |
| France          | np              | 9,148           | 11,743          | 12,514 12,644 12,608 2.9% |
| Canada          | 6,499           | 6,070           | 7,651           | 10,992 9,456 10,037 2.5% |
| People’s Republic of China* | np | np | 559 | 3,043 9,167 2.1% |
| Hong Kong (SAR of China) | np | np | 4,755 | 7,211 9,093 5,464 1.2% |
| Total all countries | 337,535 | 237,641 | 336,855 | 396,552 359,510 436,029 100.0% |

*Chinese FDI has tripled to A$92 billion, while FDI from Hong Kong fell 40 per cent to A$5.5 billion which indicates FDI is coming more directly from China. FDI therefore from China (including Hong Kong) equated to 2.4 per cent of total FDI stock in Australia in 2009 up from 1.2 per cent in 2008.

from the tendency of foreign investors to bring capital, new technology and innovation to Australia as well as enhanced access to global supply chains for Australian partners. The increased labour productivity that results allows for higher wages than would otherwise be the case.

China invested $19.5 billion in Australia in 2010. From 2006 to 2010, Chinese investments in Australia increased at an average of 50 per cent a year.

Over $39 billion of investments have been approved by the Foreign Investment Review Board in 2009-10.

Although the majority of approved investment is concentrated in the resources sector, approved investments in services has been growing as well, reaching over $700 million in 2009-10.

Foreign investment in Australia plays a key role in supplementing domestic savings, supplying capital to the economy and assisting Australia in meeting its overall investment needs. Various types of foreign investment exist in Australia — examples include Foreign Direct Investment (FDI), portfolio investment, financial derivatives and other investment liabilities. Importantly, FDI provides a relatively stable form of capital inflow because investors purchase physical assets such as plant and machinery, as opposed to other kinds of investments which can be more easily withdrawn. FDI has significantly contributed to capital formation in Australia’s mining and resources sectors (Drysdale and Findlay 2008).

In 2010, Chinese investments in Australia totalled $19.5 billion, a 17 per cent increase from the previous year (ABS 2011). In 2006 Chinese foreign investment was just $3.5 billion — from 2006 to 2010, the average increase in investment was 54 per cent.

Looking ahead, the Foreign Investment Review Board (FIRB) approved $39 billion of future investments from China in 2009-10. While the total dollar value of investments have decreased from the previous year, the number of approvals increased by over 1,700. The FIRB also approved substantially more non-mining investments from the previous year, from $345 million in 2008-09 to $4.1 billion in 2009-10. Notably, the approved dollar value of services investment experienced a substantial spike from 2008-09 to 2009-10, increasing by over $660 million.

Although the majority of investments are in the resources sector, China has invested in a variety of sectors in Australia, including financial services and the auto sector, (Australian Trade Commission 2011). For instance, the Industrial and Commercial Bank of China (ICBC), Agricultural Bank of China (ABC), Bank of China (BoC), China Construction Bank (CCB) have established branches in Sydney. Cherry Automobile, a China-based automobile company, has invested in automobile research and development in Australia. Notably, Huawei, a major Chinese telecommunications company and the world's second largest, has emerging business interests in Melbourne and Sydney. More investment from China provides job and business opportunities to households, driving economic growth.

6.3 Australia’s foreign investment footprint in China

While Australian investment in China now stands at $6.3 billion, and this is a three-fold increase compared to 2005 levels - China accounted for only 0.7% of Australia’s FDI output in 2009 (Larum, Lowy Institute). This represents a major imbalance with Australia’s largest trading partner.

Outward bound FDI leading to the provision of Australian financial management services, to take but one example, from within China for a growing Chinese middle class serves to not only balance the investment ledger with China but also diversify and stabilize the Australian economy away from the boom and bust cycle of commodities.

There is much the Chinese and Australian governments can do in terms of attracting and facilitating more Australian investment into China. This is fundamentally in China’s interests – if Chinese investment is to be a welcome feature of Australia’s FDI landscape – the Chinese Government can and must do more in facilitating and promoting Australia’s investment into China.

Whilst conventional barriers and foreign ownership restrictions have been identified as impediments to foreign investment, a range of other non-traditional barriers unique to the China market include:

- Perceptions of corruption and poor governance
- Discrepancy of infrastructure quality between well established eastern seaboard markets and the emerging Chinese hinterland
- Cultural communication issues
- Poor China market readiness and understanding among Australian companies
- Concerns in relation to intellectual property protection

6.4 Recommendations

- Maintain Australia’s proactive foreign investment attraction program tempered by transparent approval processes and increased liberalisation
- Execute a bilateral investment framework as part of any Australia China free trade agreement
- Establish a fully funded China Market Readiness Initiative to increase awareness among Australian companies and facilitate greater Australian investment in China.
Adequate Australian diplomatic representation in China is crucial to extending Australia’s economic and political engagement. Yet Department of Foreign Affairs and Trade (DFAT) officers continue to combat more than a decade of dwindling resources and work in challenging circumstances both in Canberra and on international postings.

The Lowy Institute has conducted a wide ranging inquiry examining the implications of continued funding cuts on Australia’s diplomatic service, which presented a range of very stark findings.

Since 1995, DFAT has declined in size by more than 11% and its overseas missions have contracted by approximately 40%. The 89 Australian Embassies and overseas posts stand far below the OECD average of 150.

This is especially significant in an economic environment increasingly characterized by globalized market forces and the rise of emerging markets such as China and India. Our key competitors have significantly stronger levels of diplomatic representation and Australia has fewer overseas missions than all but four OECD economies.

Of particular importance to the Sino-Australian economic relationship, DFAT’s language training budget has hardly changed in over 10 years.

The Lowy Institute’s report cites a commensurate reduction in resources to the Australia China FTA negotiations with cuts imposed on the department in the 2009-2010 financial year.

With strong continued growth in non-traditional markets outside of the Chinese eastern seaboard centres such as Beijing, Shanghai and Guangzhou, overseas postings and Australia’s representation on the ground in China are crucial to the ongoing development of healthy Sino-Australian relations.

Austrade requires more support in China because of the greater cultural gap that exists in this environment. Austrade should be aggressively scaling up its presence, knowledge and understanding to facilitate the expansion of Australian business in China. Within the next 10 years a population equivalent to the entire population of the US will move from the countryside to the city in China. Austrade cannot continue to operate at its current low resourcing levels if Australia is to enjoy the full benefits of this population and economic shift.

7.2 Recommendations

- Establish a new Australian consulate-general in Chengdu or Chongqing.