

Chapter 3

Trading links between Australia and China

Background to Australia's trading relationship with China

3.1 Australia and China have long-established trading links that have grown closer and of greater significance to both countries over recent years. In the trading sense, the two economies are often referred to as 'natural partners'.¹ Indeed, one commentator described the relationship as 'a natural economic affinity'.² This chapter briefly examines the current state of Australia's trading relationship with China and the developing trends in trade between the two countries.

Diplomacy and trade

3.2 Chinese and Australian politicians speak of their desire to strengthen and deepen trade and economic relations between their two countries.³ Such words do not express empty sentiments. Concrete actions, including a series of reciprocal high-level visits, demonstrate a commitment by both sides to furthering the relationship.

3.3 In March 2002, the Chinese Foreign Minister visited Australia, the first visit by a Foreign Minister since 1992. In the following May, the Prime Minister, the Hon. John Howard, visited China. In August 2003, he made another visit to China to meet Chinese leaders including President Hu Jintao and Premier Wen Jiabao. President Hu paid a reciprocal visit to Australia in October 2003 during which he addressed a joint sitting of the Australian Parliament. Most recently, in April 2005, Mr Howard conducted a visit to China, his fifth to that country since becoming Prime Minister. This political and diplomatic engagement is developing alongside strengthening trading links between the two countries.

3.4 During the President's visit in 2003, Australia and China entered into an agreement, the Australia–China Trade and Economic Framework, which set in place the foundations for closer commercial ties between the two countries.⁴ This agreement, designed to liberalise trade and investment between the two countries, was a significant step forward in building closer economic and trade links. It included a commitment by both governments to 'undertake a detailed joint study into the

1 See for example, Ambassador Fu Ying, address to the National Press Club, 28 July 2004.

2 Graeme Thomson, Principal Graeme Thomson and Associates, 'Trade Policy Issues', Australia–China Free Trade Agreement Conference, Sydney, 12–13 August 2004, p. 3.

3 The instances are too numerous to list here but see for example, Dr Ashton Calvert, Secretary, Department of Foreign Affairs and Trade, Opening Speech, 'Strategic setting: Common future', Australia–China FTA Conference, Sydney, 12–13 August 2004, p. 1.

4 Australian Bureau of Statistics, *Year Book Australia*, 2005, International Relations: Australia's bilateral relationships, Catalogue no. 1301.0–2005.

feasibility and benefits of a free trade agreement between Australia and China'. Since that agreement was reached, further positive measures have been taken toward a formal free trade arrangement.⁵ In March 2005, the Australian Department of Foreign Affairs and Trade (DFAT) and the Chinese Ministry of Commerce released a joint feasibility study into an Australia–China free trade agreement. The following month, Premier Wen and the Australian Prime Minister agreed to commence negotiations on an Australia-China Free Trade Agreement.⁶ While this top level dialogue has and is taking place, trade between the two countries forges ahead.

China's growing importance as a trading partner

3.5 China is currently one of Australia's major trading partners.⁷ During the decade leading to 2003, China moved from being the tenth to the third largest merchandise trading partner with Australia.⁸ During 2004–05, China became Australia's second largest merchandise export market and the second largest source of imports. Australia is China's eighth largest trading partner for goods.⁹

3.6 The following figures show the steady growth in Australian exports to China from 1991 to 2001. Over this period it quadrupled to become Australia's fifth largest export market rising from tenth in 1991–1992.

Table 3.1: Australia's export market to China 1991–2001

1991– 1992 \$m	1992– 1993 \$m	1993– 1994 \$m	1994– 1995 \$m	1995– 1996 \$m	1996– 1997 \$m	1997– 1998 \$m	1998– 1999 \$m	1999– 2000 \$m	2000– 2001 \$m
1,458	2,268	2,590	2,964	3,781	3,584	3,872	3,948	4,966	6,846

Taken from Australian Bureau of Statistics, International Merchandise Trade, Australia 2002, International Accounts and Trade, Feature Article—Australia's export markets, 1991–92 to 2000–01.

3.7 More recently, the trend in exports to China has continued on its upward trajectory and China in 2003–04 was Australia's third largest export market. In 2003

5 The Hon. Mark Vaile, MP, Deputy Prime Minister and Minister for Trade, Media Release no. MVT85/2003, 24 October 2003.

6 Prime Minister of Australia, John Howard, Media Releases, 'Announcement of Free Trade Agreement Negotiations between Australia and China', 18 April 2005.

7 Australia China Business Council, *Committee Hansard*, 29 June 2005, p. 19.

8 Australian Bureau of Statistics, *Year Book Australia*, 2003, International Relations: Australia's bilateral relationships, Catalogue no. 1301.0–2003; DFAT *Submission P19*, p. 6.

9 *Submission P19*, p. 6. See also Allan Gyngell, 'Australia's Emerging Global Role', *Current History*, vol 104, no.680, March 2005, p. 102.

Australia exported goods and services worth \$9b and \$1b respectively to China.¹⁰ Imports from China are also steadily increasing.

Table 3.2: Merchandise Exports and Imports by selected countries

Country	Exports			Imports			Balance of Trade	
	2001–02 \$m	2002–03 \$m	2003–04 \$m	2001–02 \$m	2002–03 \$m	2003–04 \$m	2002–03 \$m	2003–04 \$m
Japan	22,796	21,727	19,798	15,461	16,337	16,101	5,403	3,697
USA	12,008	10,365	9,453	21,488	22,494	19,945	-12,127	-10,492
China	7,816	8,803	9,212	11,275	13,789	15,339	-4,999	-5,427
Republic of Korea	9,818	9,115	8,473	4,722	4,753	4,878	4,363	3,595
New Zealand	7,669	8,127	8,080	4,740	5,019	5,056	3,101	3,024

Extracts from Merchandise Exports and Imports, By country and country group, Australian Bureau of Statistics, Year Book Australia, International accounts and trade; International merchandise trade, Catalogue no. 1301.0–2004, p. 816 and Australian Bureau of Statistics, Year Book Australia, International accounts and trade; International merchandise trade, Catalogue no. 1301.0–2005, p. 834.

Complementarity in trade

3.8 The Chinese and Australian economies are complementary with expectations for further growth and development.¹¹ China is in the early growth stage of economic development where low cost manufacturing is a central driver of economic growth. As it moves away from its traditional rural base to becoming an industrialised country, China's demand for resource commodities and energy will increase significantly. With

10 Merchandise Exports and Imports, By country and country group, Australian Bureau of Statistics, *Year Book Australia*, International accounts and trade; International merchandise trade, Catalogue no. 1301.0–2004, p. 65.

11 Many commentators remark on this feature of Australia's trading relationship with China. See for example Alan Oxley, Director ITS Global, Melbourne Australia, Chairman, Australian APEC Study Centre, 'Good FTAs should be like share prices—anticipate future developments: Trends in trade and investment between China and Australia', presentation to the China Australia FTA Conference, Sydney, August 2004, p. 7.

its abundant resource commodity and energy stores, Australia is well placed to gain from China's growing industrialisation. Australia is a major exporter of primary commodities to China; currently exporting iron ore, wool, aluminium, copper, and flat rolled iron.¹²

3.9 Many commentators referred to the complementarity between the two economies and the enormous scope for Australia to deepen its economic and commercial ties with China.¹³ Importantly, the complementarities extend beyond Australia's natural and rural resources. DFAT submitted:

The Australia–China commercial relationship reflects comparative economic strengths. Australia predominantly exports unprocessed rural and resource commodities and some high value manufactures and services to China. Australian businesses also invest in a variety of high value manufacturing and services industries in China. China in turn predominantly exports labour intensive or processing–derived manufactured goods to Australia and invests in a variety of Australian resource, processing, manufacturing and services ventures.¹⁴

3.10 The services sector in particular holds great promise for China and Australia. China's services sector is underdeveloped. On the other hand Australia is an advanced economy with the services sector having a predominant place in generating economic growth.¹⁵ As noted earlier, in 2003, Australia exported goods and services worth \$9b and \$1b respectively to China.¹⁶ In the opinion of Mr Alan Oxley, Director ITS Global:

In the longer term, the economic relationship will broaden and will retain special characteristics, including some that do not traditionally headline bilateral economic relationships—namely tourism, education and

12 See the findings outlined in 'China's Growth and Integration into the World Economy: Prospects and Challenges', Eswar Prasad (ed.), *IMF Occasional Paper* 232, p. 13.

13 See for example, Ken Henry, Secretary to the Treasury, 'Australia China Economic Directions—Long Term Trends in the Australian Economy', Australia China Free Trade Agreement Conference, 13–14 August 2004, p. 2.

14 *Submission P19*, p. 13.

15 See for example, Alan Oxley, Director ITS Global, Melbourne Australia, Chairman, Australian APEC Study Centre, 'Good FTAs should be like share prices—anticipate future developments: Trends in trade and investment between China and Australia', presentation to the China Australia FTA Conference, Sydney, August 2004, p. 2.

16 Merchandise Exports and Imports, By country and country group, Australian Bureau of Statistics, *Year Book Australia*, International accounts and trade; International merchandise trade, Catalogue no. 1301.0–2004, p. 65

migration—that will generate a case for deeper economic integration through an FTA.¹⁷

3.11 The Chinese assessment of the trading relationship also foresees a much broader trading relationship of strong mutual benefit. The Chinese Ambassador to Australia, Madame Fu, stated:

Australia has rich reserves of energy and mineral resources while China has growing demand and the volume of resources products it imported from Australia in 2003 has reached 3 billion Australian dollars; Australia has a mature agriculture [sector], especially a strong dairy sector and China has an expanding market for dairy products as the living standard of the people is raised; Australia has many excellent scientists who make constant progress in their research and China has a huge manufacturing sector eager to adopt science and new technology. Australia's strong services sectors such as education, tourism, finance and legal consulting can easily find demand in China.¹⁸

3.12 Clearly the complementarity between the two economies offers enormous opportunities for growth and development. Trading relationships, however, particularly with a country that is developing rapidly, do not necessarily remain static. China's continuing economic development and integration in the world economy has the potential to reshape its trading patterns. The trading dynamics between Australia and China will change over time and the degree of complementarity is bound to shift.

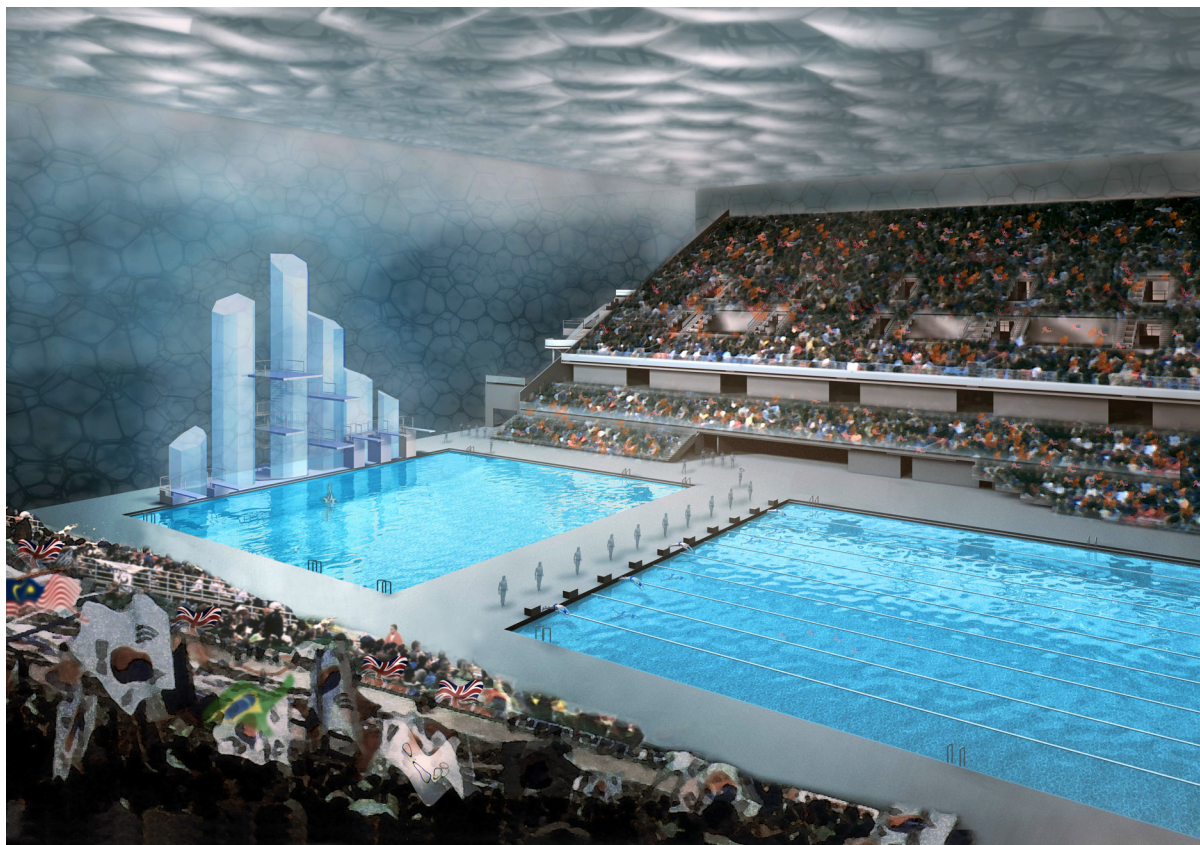
3.13 The current trend suggests that Australia is well placed to build on the solid trading base already established and to tap into the opportunities presented by the changes occurring in China. Indeed, the complementarity between the two economies is posed to broaden. Madam Fu cited the cooperation between the two nations in designing the Beijing Olympic Swimming Center to highlight not only their comparative economic strengths but the potential for further similar partnerships.

A joint team of Australian and Chinese engineers won the bidding with a masterpiece of blue structure called 'water cubic'. Its smart and sophisticated design is regarded as a wonder of physics. It looks like a huge cubic full of blue water, highly modern in shape.¹⁹

17 Alan Oxley, Director ITS Global, Melbourne Australia, Chairman, Australian APEC Study Centre, 'Good FTAs should be like share prices—anticipate future developments: Trends in trade and investment between China and Australia', presentation to the China Australia FTA Conference, Sydney, August 2004, p. 1.

18 Ambassador Fu Ying, address to the National Press Club, 28 July 2004.

19 Ambassador Fu Ying, address to the National Press Club, 28 July 2004.



The proposed Beijing Olympic Swimming Centre. Photograph is courtesy of Arup, architecture firm PTW, the CSCEC (China State Construction and Engineering Corporation).

3.14 The transformation of China's economy has also attracted a wider range of Australian companies keen to trade with China especially in the services sector. Mr Harrowell noted that China is 'no longer the exclusive province of the BHPs and the Telstras; medium-sized companies are able to seriously look at China and establish there'.²⁰

3.15 Hunt and Hunt Lawyers made a similar observation. It suggested that the profile of Australian businesses seeking to work in and with Chinese companies has changed dramatically over the last decade. It noted:

In the last ten years there has been the growth of small to medium Australian businesses seeking to either work with China or in many cases establish their own office in China.

This has been particularly so in the service industries with Australian architects and engineering firms establishing branches in China which are proving very successful with major projects relating to the Olympic Games and capturing work generally because of the demand in the Chinese market for these skills.

20 J. Harrowell, *Committee Hansard*, 29 June 2005, p. 41.

Smaller Australian listed companies are also venturing into China with success for example gold mining companies including Sino Gold NL and recently Golden Tiger Mining NL.²¹

3.16 ACIL Tasman further underlined the growing diversity of firms entering the Chinese market. It referred to several Australian banks, law firms and insurance companies as well as companies involved in mineral exploration and education services now operating in China. It noted that many of these enterprises which have found success in niche markets are small to medium companies.²²

3.17 Proximity is another advantage that assists the trading relationship. Transport and travel distances are not as great and costs are lower to get products to market when compared to some European and American markets.²³ Australia also operates in the same time zone.²⁴

Trade deficit with China

3.18 Australia runs a trade deficit with China. In 2002–03, the deficit in merchandise trade increased by \$1,540 million to reach \$4,999 million. This was due to a \$2,517 million increase in imports but only a \$977 million increase in exports.²⁵ According to the ABS:

Imports of most commodity groups increased particularly office and automatic data processing machines (up \$374m) and telecommunication and sound recording and reproducing equipment (up \$326m). The largest increase in exports were metalliferous ores and metal scrap (up \$254m) and petroleum, petroleum products and related materials (up \$201m).²⁶

3.19 In 2005, the deficit with China rose further and stood at \$5,427 million.²⁷

21 *Submission P24*, p. 11.

22 ACIL Tasman, 'The proposed free trade agreement with China—A commentary and some preliminary analysis', a paper prepared for a Conference on Free Trade Agreements in the Asia Pacific Region at the University of Western Australia, p. 5.

23 *Submission P24*, p. 4.

24 *Submission P24*, p. 4.

25 Statistics taken from Merchandise Exports and Imports, By country and country group, Australian Bureau of Statistics, *Year Book Australia*, International accounts and trade; International merchandise trade, Catalogue no. 1301.0–2004, p. 816 and Australian Bureau of Statistics, *Year Book Australia*, International accounts and trade; International merchandise trade, Catalogue no. 1301.0–2005, p. 834.

26 Australian Bureau of Statistics, *Year Book Australia*, International accounts and trade; International merchandise trade, Catalogue no. 1301.0–2004.

27 Australian Bureau of Statistics, *Year Book Australia*, International accounts and trade; International merchandise trade, Catalogue no. 1301.0–2004, p. 834.

3.20 According to the Minister for Trade, the Hon. Mark Vaile, MP, Australia's trade deficit with China is expected to improve but will rely on a boost from the export of resources to narrow the deficit. In this case from 2006 the first deliveries of the \$25 billion gas deal between the North West Shelf and Aus/ALNG in Guangdong Province will begin to flow.

3.21 Some have expressed concern at Australia's growing reliance on commodity exports to China to contain the deteriorating balance of trade figures.²⁸ The Australian Manufacturing Workers' Union saw not only the rate of increase but the composition of the deficit as a major problem. It noted that Australia's exports to China are overwhelmingly dominated by primary products while Australian imports from China are dominated by manufactured goods. It submitted:

China's hunger for resources may indeed be a boon for some parts of the Australian economy. However, the successful economies of the future will not be sustained on the exportation of resources. In the face of increasing competition from China, Australia can and must do more to encourage the growth of (strategic) high value added manufacturing.²⁹

3.22 It recommended that states and federal governments work toward improving Australia's trade performance which would involve a commitment to a co-ordinated strategy to ensure the future of the Australian manufacturing industry in a competitive world. In March 2005, Professor Ross Garnaut stated:

The high export prices that have been the dominant element in the recent lift in terms of trade are correctly attributed to the strength of the Chinese demand for energy and metals at a time of reasonably strong global economic growth. They are vulnerable to correction, either with any setback to Chinese economic growth (and we would be prudent to expect China, like all market economies, to have cyclical downturns from time to time), or in other major economies.³⁰

3.23 Clearly, consideration must be given to Australia's growing dependency on commodity exports to China. Chapter 6, which deals with Australia's manufacturing sector, examines this matter. A number of witnesses, however, reminded the committee that while important, China is part of a much broader and complex trading network for Australia. The Australian Chamber of Commerce and Industry (ACCI) noted:

There is little doubt that it [China] will grow in importance over the coming decades. The main challenge, I think, for the Australian government and

28 A number of witnesses also raised concerns about the export of raw materials without value adding to the product in Australia. See paragraphs 6.64–6.66 and 7.34.

29 *Submission P36*, p. 10.

30 Ross Garnaut, 'Breaking the Australian Great Complacency of the Early Twenty First Century', Paper presented at the conference, "Sustaining Prosperity, New Reform Opportunities for Australia", 2005 Economic and Social Outlook Conference, Melbourne Institute and the *Australian*, Melbourne, 31 March 2005, p. 9.

Australian business community is how we position ourselves to best identify and realise those opportunities whilst balancing a whole range of different pressures that come with that. China is important, but it is not the totality of the future. Australian business trades with the whole world. We have to compete with the whole world and that means in Australia and in China.³¹

Committee view

3.24 The committee notes the growing trade deficit with China and Australia's heavy reliance on its exports to China, in particular raw materials, to buttress Australia's balance of trade. This is a development that all state governments and particularly the federal government must take into account when formulating their trade and industry policy. Australia's growing dependency on China as a major trading partner also highlights an earlier observation by the committee that Australia needs to be fully aware of changing circumstances in China and their implications for Australia. It gives further substance to the committee's suggestion that Australia build up a reserve of China analysts ready to advise decision makers on developments in China and trends likely to influence the pattern of trade between the two countries.

Conclusion

3.25 This chapter highlighted the growing importance of China to Australia's economy. It found that:

- both countries desire to strengthen economic ties and have taken definite steps toward a free trade agreement;
- China and Australia's economies are complementary with potential for deepening and broadening the relationship;
- the transformation of China's economy presents opportunities for Australian businesses and is attracting a wider range of Australian companies;
- to take advantage of the opportunities on offer in China and to better anticipate developments in that country, the Australian government and businesses need to have access to China specialists.

3.26 The goodwill that exists between Australia and China and the mutually beneficial nature of their trading relationship does not necessarily mean that the trade relationship is problem free. The following chapter examines the overall business environment in China. It looks at the opportunities available to Australian companies and also some of the main obstacles that hinder trade between them.

31 R. Davis, *Committee Hansard*, 29 June 2005, p. 19.

