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Submission for the parliamentary inquiry into Australia's trade and investment relationship with the UK

This submission addresses the following term of reference for the inquiry:

- *Possible implications for Australia's trade and investment relationships with the UK and the European Union consequent to the UK's exit from the European Union.*

Summary

The UK's so called 'hard Brexit' line is going to negatively impact the Australian economic position in the global value chains that rely on ease of trade and investments in the European single market.

The aggregation of trade and investment data on market complementarity and financial exposure with the UK and the EU (minus the UK) indicates that it is in Australia's best economic interest to prioritise a preferential partnership with the EU over a new free trade agreement with the UK.

In the aftermath of Brexit, this submission recommends setting up a non-binding and non-preferential economic cooperation forum with the UK aiming at unilateral liberalisations in targeted sectors with clear growth margins for trade and investment complementarity.

This approach of concerted unilateralism with the UK and preferential bilateralism with the EU is best placed to limit disruption in the post-Brexit global value chains that impact Australia's economy.

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Economic assessment

This section follows the steps of the 2010 Australian Government's Productivity Commission Report on Bilateral and Regional Free Trade Agreements [BRTAs], which found that preferential trade and investment arrangements "can significantly increase trade flows between partner countries, although some of this increase is typically offset by trade diversion from other countries".

This submission relies on the Productivity Commission's conclusion that increased trade flows per se produce only a modest improvement in national income and commercial benefits, because "the main factors that influence decisions to do business in other countries lie outside the scope of BRTAs".

In 2015 the UK ranked as Australia's 8th largest merchandise export destination (2.9% of total) and 10th largest source of merchandise imports (2.8% of total).

Similarly, the UK ranked as Australia's 3rd largest export destination for services (7.2% of total) and 2nd largest source of imported services (9.4%).

Table 1 below also shows the amount of foreign direct investment (FDI) stocks as of 2015, with a combined total of approximately A$ 850 million.

The EU in the 2015-2016 financial year accounted for 6.7% of total merchandise exports, 18% of total merchandise imports, 15.3% of total export of services and 25.7% of total imports of services, as tallied by the DFAT European Union (EU) Fact Sheet.

However, the primacy of the UK in Australia's economic relations with the EU is further demonstrated in table 1 above. The UK alone contributes between 15 to 47% to the composition of Australia's trade relationship with the EU as a whole.

In order to gauge the possible implications for Australia's trade and investment relationships with the UK and the EU, the following sections assess key market trends in relation to 1) trade in goods; 2) trade in services; and 3) capital investments.

The aggregated analysis of these three areas assess Australia's trade and investment relationship with both the UK as an individual economic partner and the EU as a single market without the UK, hereafter referred to as EUBrex.

Table 1: Snapshot of Australian Economic Relations with the UK in 2015

	UK
GOODS	
Merchandise Exports (A$ millions)	7158
Merchandise Exports (Rank)	8
Merchandise Exports (% of Total)	2.9
Merchandise Exports (% of EU)	44.1
Merchandise Imports (A$ millions)	7584
Merchandise Imports (Rank)	10
Merchandise Imports (% of Total)	2.8
Merchandise Imports (% of EU)	15.5
SERVICES	
Commercial Services Exports (A$ millions)	4911
Commercial Services Exports (Rank)	3
Commercial Services Exports (% of Total)	7.2
Commercial Services Exports (% of EU)	47
Commercial Services Imports (A$ millions)	7316
Commercial Services Imports (Rank)	2
Commercial Services Imports (% of Total)	9.4
Commercial Services Imports (% of EU)	36.7
FOREIGN DIRECT INVESTMENT	
FDI Inward Stock to Australia (A$ millions)	499930
FDI Inward Stock to Australia (% of EU)	50.5
FDI Outward Stock from Australia (A$ millions)	353204
FDI Outward Stock from Australia (% of EU)	59.9

Sources: Australian Department of Foreign Affairs and Trade Fact Sheets and authors' calculations

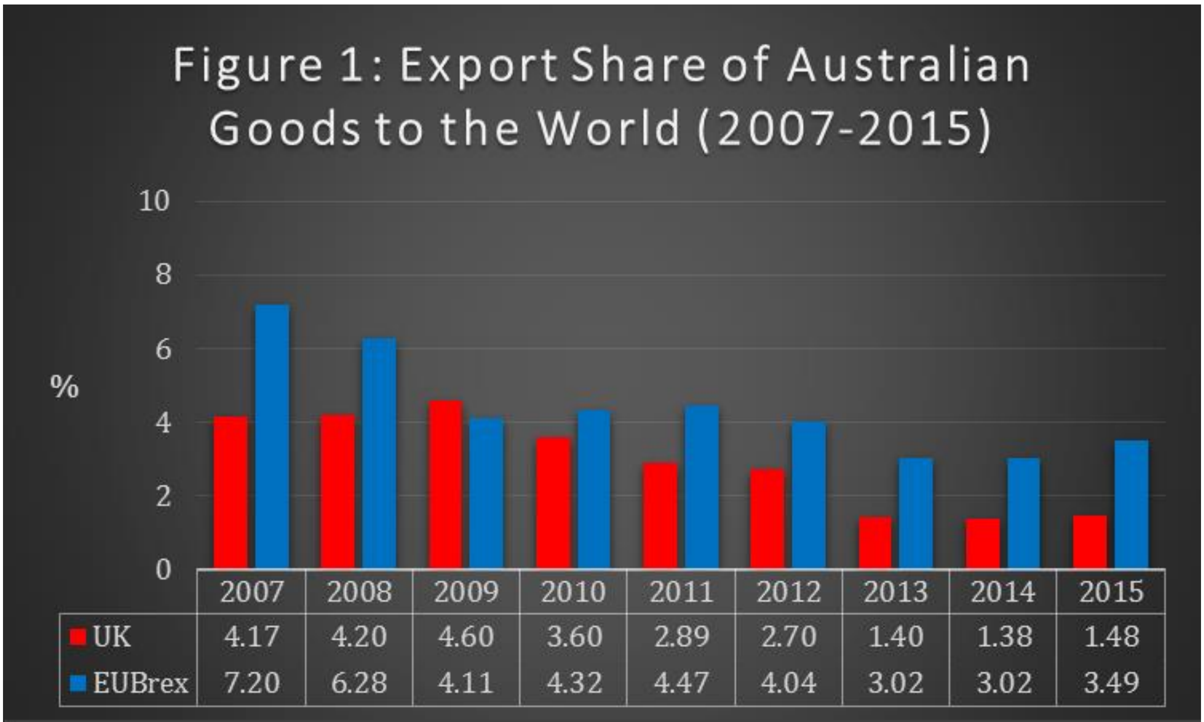
Four indicators of trade in goods with the UK and EUBrex were compiled for the period from 2007 to 2015, namely: a) export share; b) import share; c) export similarity; and d) trade complementarity.

In terms of **export share**, as indicated in figure 1, the importance of the UK as an export destination has on the whole been in the decline since 2007, peaking in 2009 at 4.6% and falling to 1.48% by 2015.

A similar downward trend is identified for the EUBrex as trading partner with general downward trend in export share from a high of 7.2% in 2007 to 3.49% in 2015.

The UK and EUBrex do not appear to be sizeable individual markets for Australian exports contributing less than 10% of total Australian exports.

Overall, with the exception of 2009, the EUBrex has consistently exceeded the UK as an export destination.



	2007	2008	2009	2010	2011	2012	2013	2014	2015
UK	4.17	4.20	4.60	3.60	2.89	2.70	1.40	1.38	1.48
EUBrex	7.20	6.28	4.11	4.32	4.47	4.04	3.02	3.02	3.49

Notes: 1. Geometric Mean (UK) = 2.65% ; 2. Geometric Mean (EUBrex) = 4.26%
Source: UNCTAD Stat Database and authors' calculations

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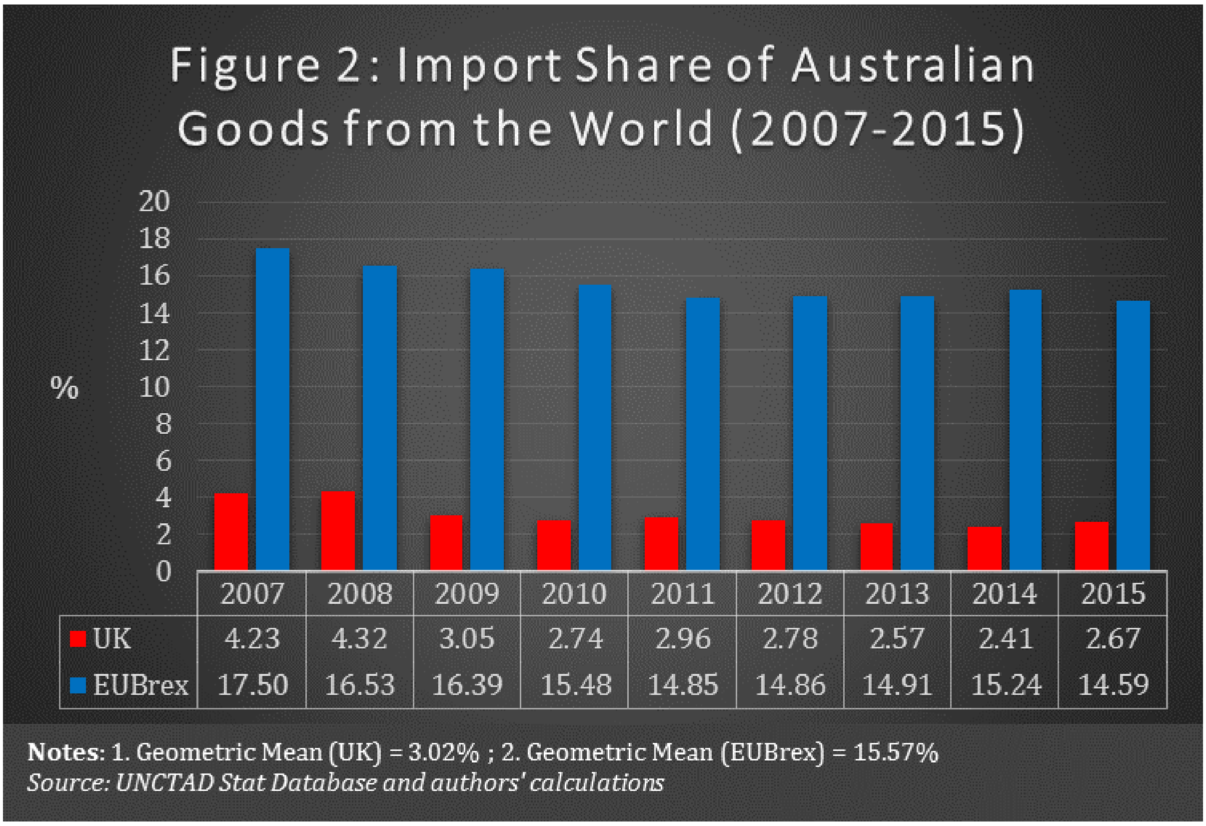
As figure 2 indicates, a similar pattern is observed with **import share** of the UK and EUBrex declining over time.

The UK import share has been below 5% over the period of observation, whereas the EUBrex has been consistently above 14.5% over the same period.

In contrast to the exports, the EUBrex should be regarded as a major source of Australian imports.

Consequently, export and import shares of the UK and EUBrex with Australia permits further investigation as to export similarity and trade complementarity between each trading partner.



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Export similarity measures competition for worldwide export markets between trading partners – i.e. the higher the percentage of export similarity, the higher the degree of competition.

As figure 3 shows, export similarity between Australia and the UK has fluctuated since 2007 in a general downwards trend, averaging 45.99%.

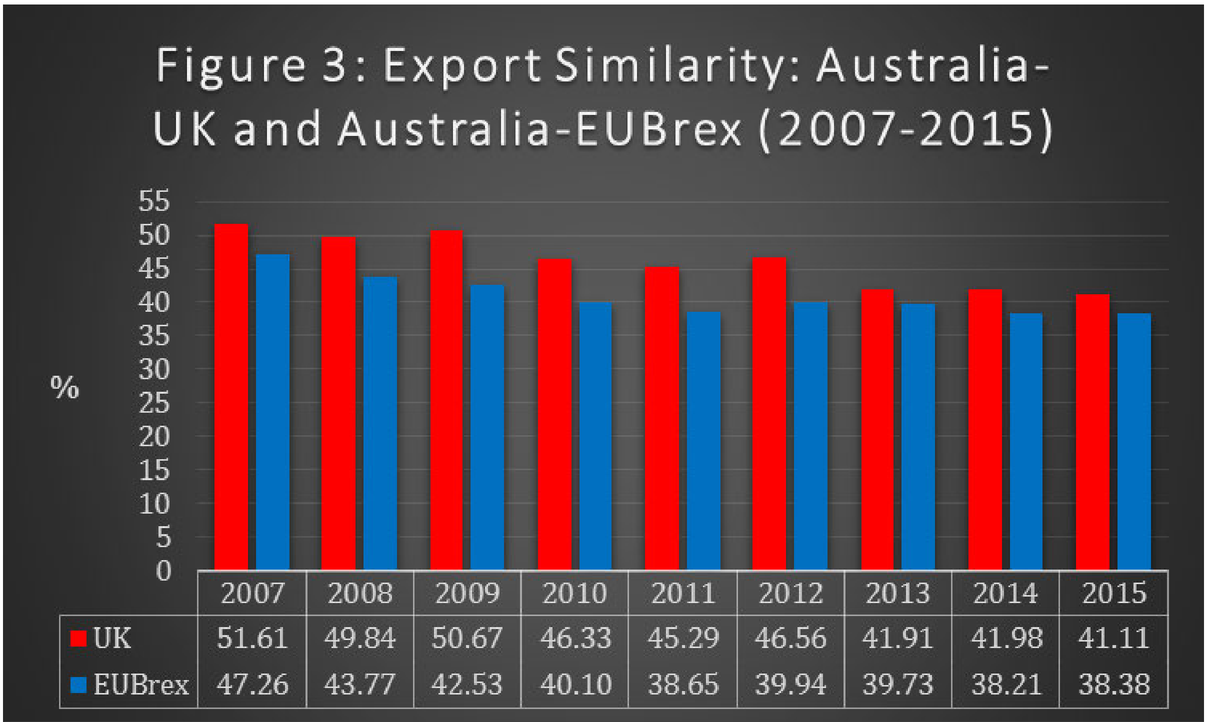
In comparison, the export similarity between Australia and the EUBrex has followed a similar pattern of fluctuation and downwards trend in since 2007, but has averaged 40.86%.

In both cases, the UK and EUBrex demonstrate a sizeable (above 40%) match in global export markets.

This in itself is not too surprising a feature, as all three trading partners are major global trading nations.

However, the persistent level of competition for global markets between Australia and the UK, and between Australia and the EUBrex is likely to hinder future trade negotiations, as it will be difficult to prove significant commercial advances from preferential bilateral agreements.

Given the higher degree of Australia's trade competition with the UK than with the EUBrex, this concern is expected to play a larger feature in future negotiations with the UK.



Notes: 1. Geometric Mean (UK) = 45.99% ; 2. Geometric Mean (EUBrex) = 40.86%
Source: UNCTAD Stat Database and authors' calculations

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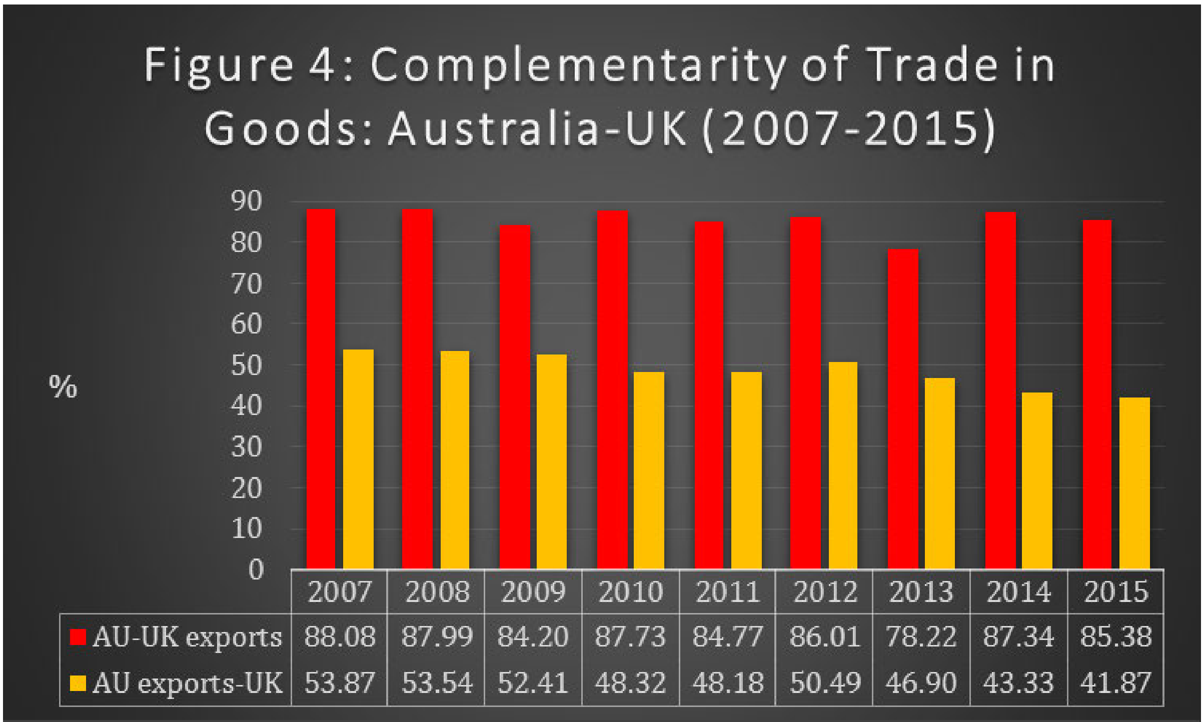
In contrast to export similarity, **trade complementarity** measures the overlap from one import market to the export market of another across different sectors, i.e. the higher the percentage of overlaps, the higher the degree of complementarity.

From the perspective of Australia and the UK, figure 4 shows that the Australian imports are well served by the UK exports (more than a 78% overlap), however the UK imports are less well served by Australian exports (no more than a 53.87% overlap).

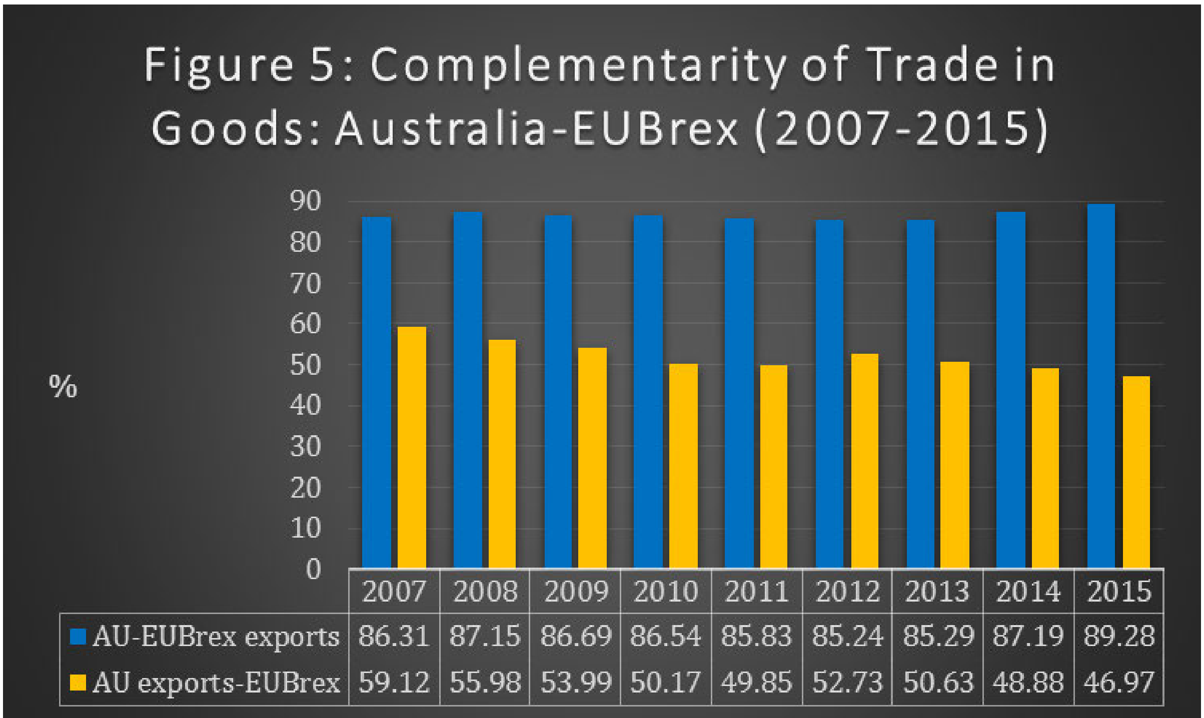


Notes: 1. Geometric Mean (AU-UK exports) = 85.47% ; 2. Geometric Mean (AU exports-UK) = 48.60%
Source: UNCTAD Stat Database and authors' calculations

The significant differences in trade complementarity between Australia and the UK imply that it will be difficult to establish mutually beneficial trade arrangements.

In particular, such differential in trade complementarity between Australia and the UK shows that the UK exporters are poised to benefit significantly more than Australian exporters from a preferential bilateral FTA.

In comparison with the UK, as indicated in figure 5 on trade complementarity between Australia and the EUBrex, Australian imports are better served by the EUBrex exports (more than an 85% overlap), and the EUBrex imports are better served by Australian exports (no more than a 59.12% overlap).



Notes: 1. Geometric Mean (AU-EUBrex exports) = 86.60% ; 2. Geometric Mean (AU exports-EUBrex) = 51.92%
Source: UNCTAD Stat Database and authors' calculations

Nonetheless, sizeable differences in trade complementarity between Australia and the EUBrex imply that it will still be difficult to establish mutually beneficial trade arrangements, as Australian exporters would gain less than the EUBrex exporters, however less so than in comparable arrangements with the UK.

At this point, it becomes clear that for Australia a preferential bilateral FTA with the EUBrex is more desirable than one with the UK, and the cross-check of trade complementarity with trade competition further confirms this reasoning.

In fact, the likely benefits of potential arrangements for Australian exports so far has been understood to be a relative gain.

However, little is indicated as to whether the gain achieved for Australian consumers of imports will be achieved at the expense of the Australian producers of exports.

To assess whether potential arrangements are likely to be beneficial to Australian producers of exports, it is necessary to compare measures of complementarity (with exports from Australia) to those of export competition.

The logic of this approach is that the current gains achieved by Australian producers of exports occur under the constraint of competition, and that cooperation reduces market rivalry.

Therefore, trade complementarity must exceed trade competition if producers of exports are to gain from trade cooperation.

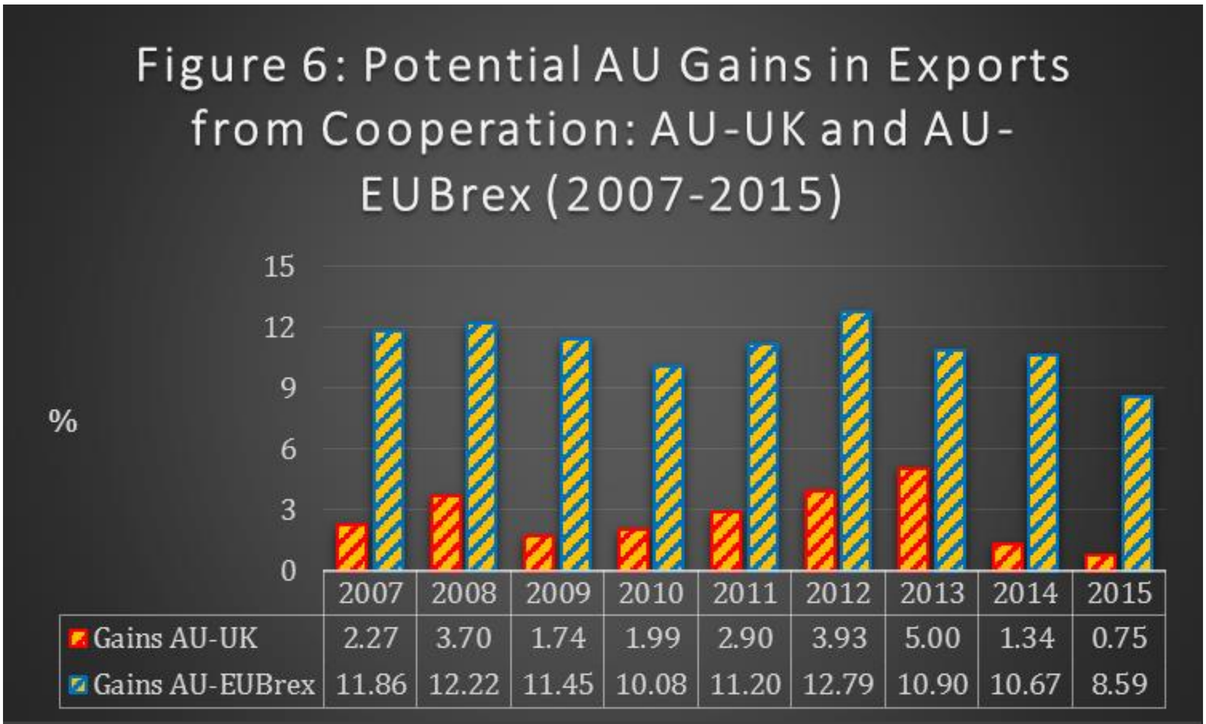
Figure 6 shows that gains from cooperation for Australian producers of exports would have been positive over the period 2007 to 2015 if potential trade arrangements with the UK and EUBrex had been in place.

However, the gains for Australian producers of exports would have been considerably greater from an arrangement with the EUBrex than from a comparable cooperation with the UK.

According to this analysis, entering into preferential trading agreements with the UK and EUBrex will be, on aggregate, beneficial for Australia.

To understand which sectors will be winners or losers from such arrangements needs further investigation.

For this very reason, given the political uncertainty of post-Brexit negotiations between the UK and EU, Australia's economic diplomacy should be mindful of sequencing its own negotiations in ways that maximise trade complementarity and limit trade competition with the various European partners.



	2007	2008	2009	2010	2011	2012	2013	2014	2015
Gains AU-UK	2.27	3.70	1.74	1.99	2.90	3.93	5.00	1.34	0.75
Gains AU-EUBrex	11.86	12.22	11.45	10.08	11.20	12.79	10.90	10.67	8.59

Notes: 1. Geometric Mean (Gains AU-UK) = 2.28% ; 2. Geometric Mean (Gains AU-EUBrex) = 11.02%; 3. Gains in exports are defined as the difference between complimentarity (AU exports) and export similarity with the trading partner
Source: UNCTAD Stat Database and authors' calculations

Consequently, an area for further consideration is to what extent a hard Brexit will reduce the value of Australia's exports and imports due to the disruption of the global value chains that rely on ease of trade between the UK and EUBrex.

In order to make such an assessment, the calculation for selected years captures the dollar value add of manufactured goods from Australia or the EUBrex passing through the UK, and with the final destination of either the EUBrex or Australian markets – refer to table 2.

Although further analysis is still needed, the data from the OECD EBOPS 2010 Database on the intermediate and final trade in manufactured goods indicate two potential outcomes under a hard Brexit:

a) On average up to US$0.47 billion of value per annum of Australian exports can be disrupted, thus potentially reducing Australia's industrial output; and

b) On average up to US$1.37 billion value of imports to Australia per annum could become more expensive, thus increasing the cost of domestic production and consumption.

Table 2: Maximum Potential Reduction of Australian Manufactured Goods Exports and Imports: Global Value Chains under a 'Hard' Brexit (2005 and 2010)

AU Exports				**AU Imports**			
Year	*AU Domestic Value Added by Gross Exports with UK (US$ mil.)*	*EU share of UK Domestic Value Added (% of Total)*	*Max. Reduction AU Domestic Value Added (US$ mil.)*	*Year*	*AU Foreign Value Added by Gross Exports with UK (US$ mil.)*	*EU share of UK Foreign Value Added (% of Total)*	*Max. Reduction AU Foreign Value Added (US$ mil.)*
2008	1317.34	43.90%	578.31	2008	2773.03	51.42%	1425.89
2009	908.87	43.67%	396.90	2009	2230.85	48.81%	1088.88
2010	1062.01	40.82%	433.51	2010	2522.01	48.11%	1213.34
2011	1124.65	40.87%	459.64	2011	3514.57	49.31%	1733.03
Average	1103.22	42.29%	467.09	Average	2760.12	49.40%	1365.29

Source: OECD Stat EBOPS 2010 Database and authors' calculations

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2. Trade in Services

Sectoral level data on trade in services is traditionally inconsistent or incomplete. Given these limitations, two indicators of trade in services with the UK and EUBrex were compiled for the period of 2007 to 2015, namely: a) export share; and b) import share.

As for trade in goods, export and import shares indicate the importance of a trading partner in terms of worldwide Australian exports and imports.

Export and import shares are represented as a percentage of the total Australian exports and imports, and provide a means to track the relative importance of a trading partner over time.

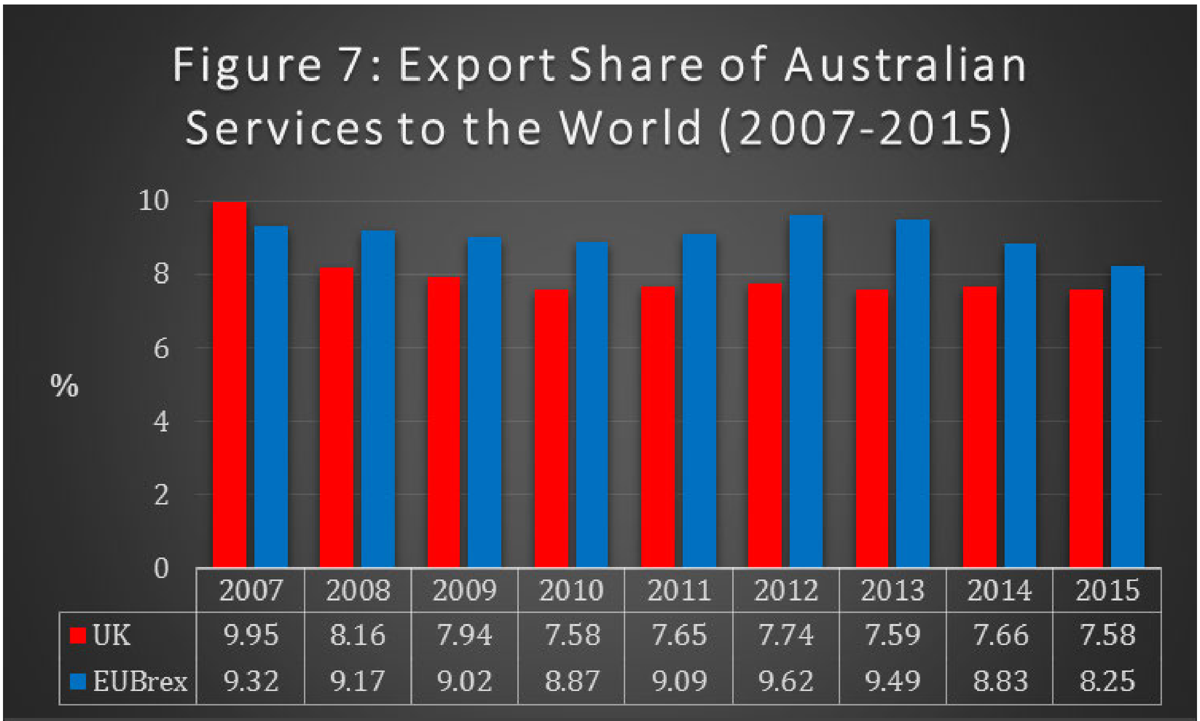
In terms of **export share** in services, figure 7 shows that the importance of the UK as an export destination declined considerably from 2007 to 2009 before settling to approximately 7.7% thereafter.

A much milder decline in EUBrex as a destination for Australian services was experienced during 2007-2009, but it has maintained a more stable average of 9.06% over the entire period under analysis.

Albeit similar in scale, the UK and EUBrex do not appear to be sizeable individual markets for Australian services exports, contributing less than 10% of total Australian exports in this regard.

Nonetheless, the stability of exports to EUBrex, especially post global financial crisis, points toward the EUBrex being a more robust market for Australian services exports after Brexit.

Accordingly, the EUBrex as a market for export of Australian services is likely to remain a more significant partner than the UK.



Notes: 1. Geometric Mean (UK) = 7.95% ; 2. Geometric Mean (EUBrex) = 9.06%
Source: OECD EBOPS 2010 Database and authors' calculations

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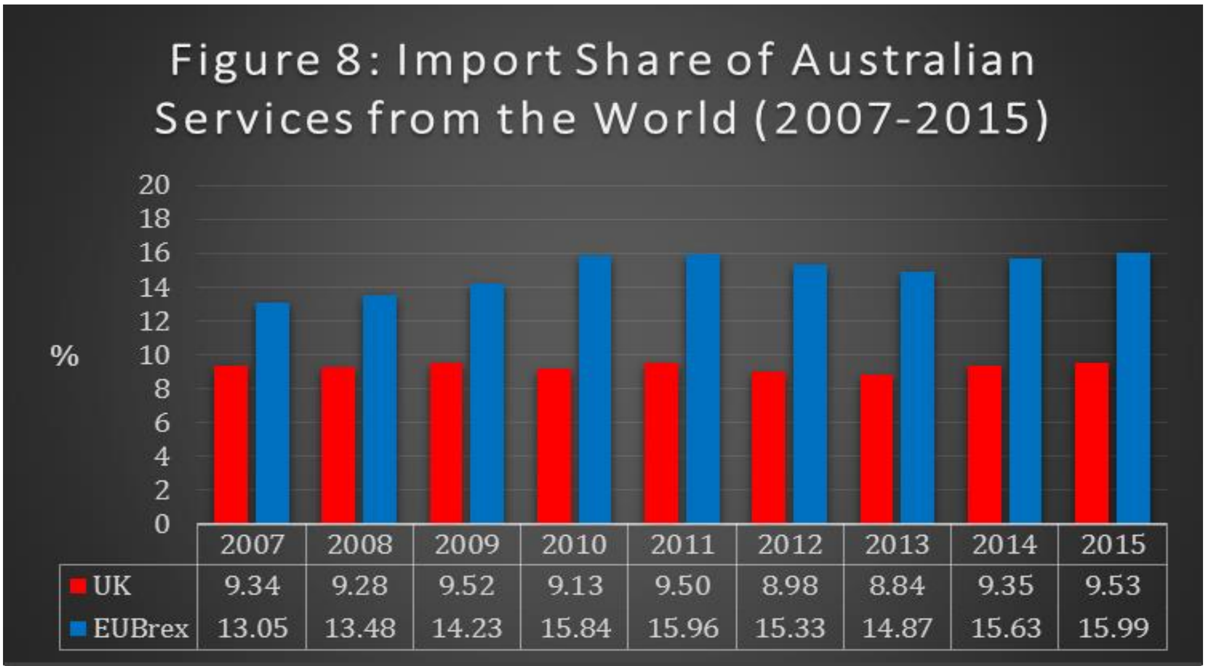
Similarly to the export share, figure 8 shows that overall rising fluctuations have occurred in the past decade with the **import share** of the UK and EUBrex.

The UK import share has demonstrated less variability than the EUBrex, and has been below 10% over the period of observation.

This pattern contrasts with the EUBrex, whose import share of Australian services has greater variability and has been consistently above 13% over the same period.

With the average import share above 10%, the EUBrex should be regarded as a major source of Australian services imports.

Given the long-established difference in magnitudes between services imports from the UK and EUBrex, the latter is likely to maintain this primary import position also post Brexit.



Notes: 1. Geometric Mean (UK) = 9.27% ; 2. Geometric Mean (EUBrex) = 14.89%
Source: OECD EBOPS 2010 Database and authors' calculations

As was the case with the trade in goods, an area for further consideration is to what extent a hard Brexit will reduce the value of Australia's services exports and imports due to disruption of the global value chains that rely on ease of trade and investment between the UK and EUBrex.

In order to make such an assessment, the calculation for selected years captures the dollar value add of business services from Australia or EUBrex passing through the UK, and with the final destination of either EUBrex or Australian markets – table 3.

Although further analysis is still needed, the data from the OECD EBOPS 2010 Database on the intermediate and final trade in business services indicate two potential outcomes under a hard Brexit:

a) On average up to US$1.47 billion of value of Australian exports can be disrupted per annum, thus potentially reducing Australia's industrial output; and

b) On average up to US$3.36 billion value of imports to Australia per annum could become more expensive, thus increasing the cost of domestic production and consumption.

Table 3: Maximum Potential Reduction of Australian Business Services Exports and Imports: Global Value Chains under a 'Hard' Brexit (2005 and 2010)

AU Exports				AU Imports			
Year	*AU Domestic Value Added by Gross Exports with UK (US$ mil.)*	*EU share of UK Domestic Value Added (% of Total)*	*Max. Reduction AU Domestic Value Added (US$ mil.)*	*Year*	*AU Foreign Value Added by Gross Exports with UK (US$ mil.)*	*EU share of UK Foreign Value Added (% of Total)*	*Max. Reduction AU Foreign Value Added (US$ mil.)*
2008	4068.79	42.32%	1721.91	2008	6728.20	52.11%	3506.07
2009	2997.47	42.15%	1263.43	2009	5724.79	51.09%	2924.80
2010	3636.04	39.91%	1451.14	2010	6537.05	48.85%	3193.35
2011	3687.99	39.56%	1458.97	2011	7768.05	48.88%	3797.02
Average	3597.57	40.97%	1473.86	Average	6689.52	50.21%	3355.31

Source: OECD Stat EBOPS 2010 Database and authors' calculations

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3. Capital Investments

This section investigates capital investments through two channels: a) foreign direct investment (FDI); and b) portfolio investment (PI), with particular focus on the importance of both channels for Australian businesses.

In the context of this submission, **FDI** is initially assessed from the host country perspective in terms of the contribution of inflows from the source as percentage of global inflows since 2009.

Much like import share for trade in goods and services, the percentage contribution indicates the importance of a source nation for its host nation's total FDI inflows.

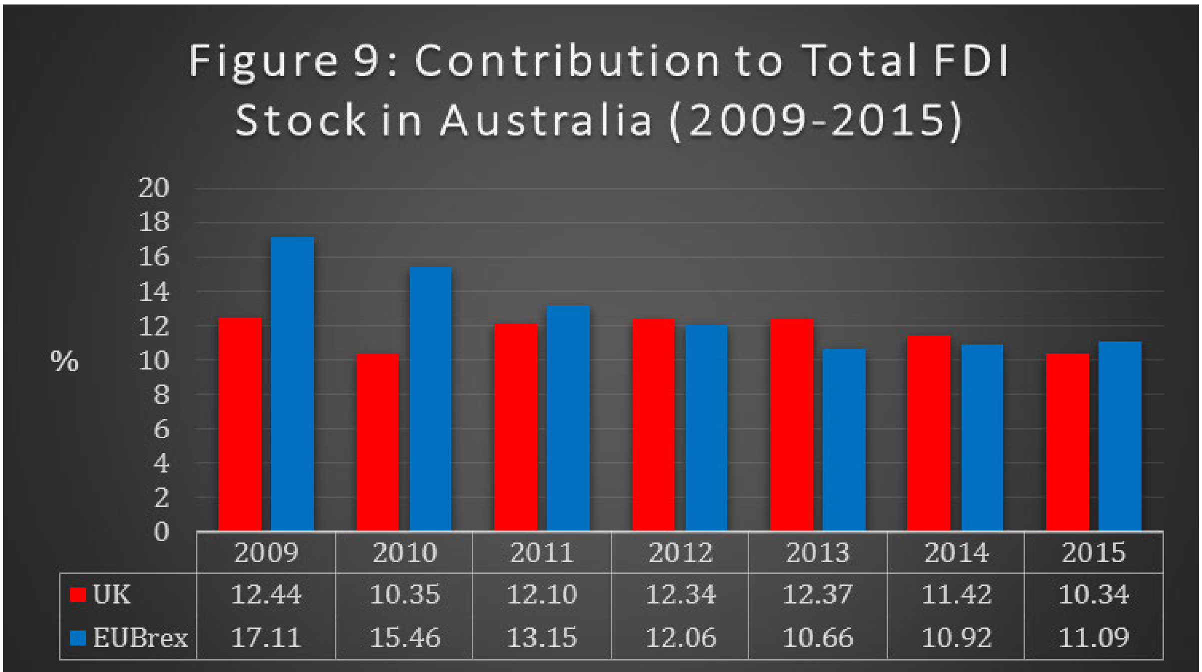
Accordingly, it is necessary to use stock variables, as these are believed to best reflect the activities of multinational corporations (MNCs) operating within the host nation in terms of the influence they have over industrial production and service provision relations.

Figure 9 compares the UK and EUBrex FDI inflows in relation to Australia. Historically, FDI inflows from the UK and EUBrex have jointly contributed more than 21 percent of global FDI inflows to Australia.

Independent FDI inflows from the UK and EUBrex to Australia are similar in recent years, and have since 2009 averaged 11.59% and 12.73% respectively.

The pattern of FDI inflows from the UK appears to be more cyclical than that of the EUBrex, and FDI inflows from both sources have fluctuated over the period under investigation.

In most cases, FDI inflows from the UK and EUBrex are lower in recent years than at the beginning of the period under investigation.



Notes: 1. Geometric Mean (UK) = 11.59% ; 2. Geometric Mean (EUBrex) = 12.73%; 3. FDI stock values based on inward directional principle
Source: OECD Stat Database and authors' calculations

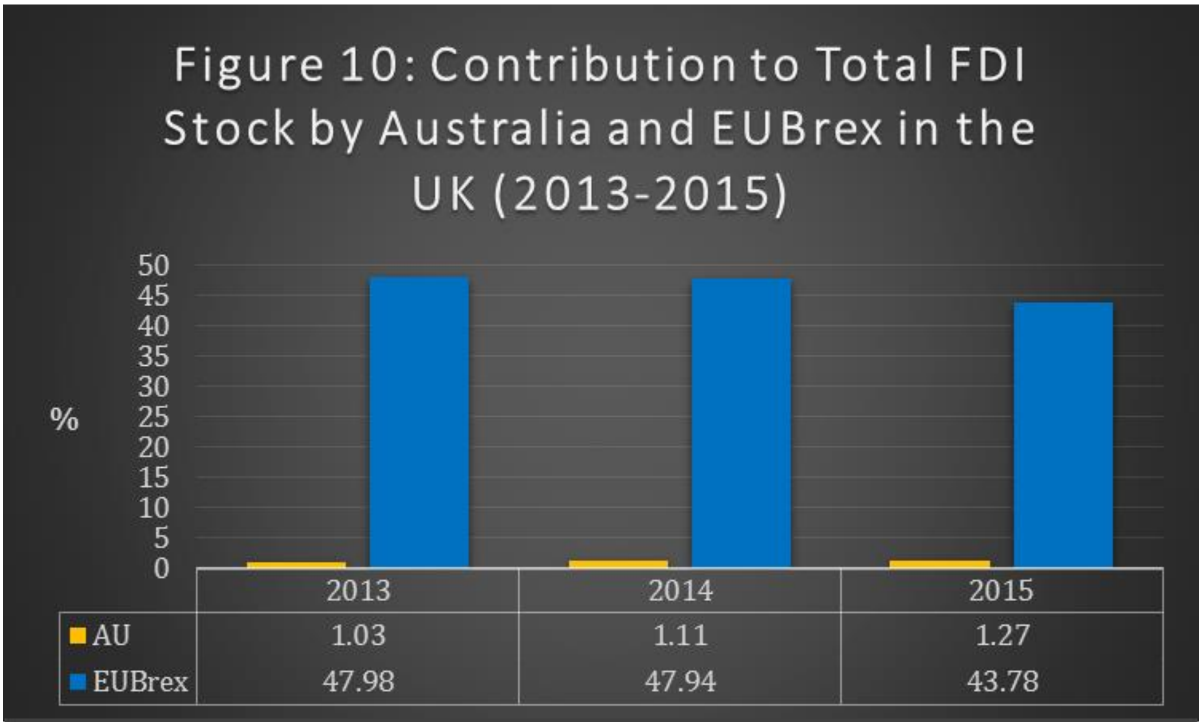
Even with these fluctuations, Australia continues to be a relatively stable market for the direct investments of the UK and EUBrex MNCs.

Jointly and separately, UK and EUBrex MNCs are indeed likely to maintain a sizeable influence on industrial production and service provision relations in Australia.

In contrast, within the constraints of limited data availability in the analysis of FDI inflows from Australia and the EUBrex, figure 10 shows that, although Australian FDI to the UK has been increasing over the 2013-2015 period, Australian FDI inflows only average around 1.1% of global FDI inflows to the UK market.

The global FDI inflows in the UK market originating from the EUBrex are far greater, at an average of 46.53%, albeit on a declining trend.

On this basis, it can be argued that Australian MNCs have little direct influence or leverage on industrial production and service provision relations in the UK.



Notes: 1. Geometric Mean (AU) = 1.13% ; 2. Geometric Mean (EUBrex) = 46.53%; 3. FDI stock values based on inward directional principle
Source: OECD Stat Database and authors' calculations

Consequently, due to the considerable scale of influence of the EUBrex MNCs on industrial production and service provision relations in the UK, it is likely that the future operational ability of the EUBrex MNCs in the UK market will take centre stage in post-Brexit negotiations.

Broadly, there are two possible outcomes of the post-Brexit negotiations in terms of the EUBrex MNC operations in the UK services market:

1) The UK and EU will finalise an agreement before the two-year term set by Article 50 of the EU Treaty; or

2) Without a timely agreement, the UK and EU will revert by default to the non-preferential multilateral system under the rules of the General Agreement on Trade in Services (GATS) by the World Trade Organization (WTO).

Australia's services sector is poised to lose from both outcomes, particularly without counteraction in terms of further investment cooperation, liberalisation and domestic reform.

Indeed, the first outcome will further embed Australia's services market subordination, whereas the second outcome is expected to indirectly hit the operations of Australian MNCs in the UK and those of foreign MNCs operating within the Australian services market. This is an area in need of more detailed investigation.

The second channel of capital investments on focus is **portfolio investments** (PI), understood in terms of equity and debt instruments that are tradable on financial markets.

The importance of financial markets to businesses relates to the influence these markets have in financing the consumption of consumers on the one hand, and the production of the businesses on the other hand.

Accordingly, two measures calculate PI in the context of this submission:

a) Exposure of domestic held (Australian) portfolios to the UK and EUBrex financial markets that capture consumption implications; and

b) Exposure of the Australian financial market to the UK and EUBrex portfolios that gauge production implications.

Both measures are expressed as a percentage, i.e. the higher the value, the greater the exposure.

The exposure of Australian portfolios to the UK and EUBrex is determined by the percentage of Australian portfolios held in either market after making adjustments for home-bias, which is the tendency for investors to invest in a large amount of domestic financial assets, despite the purported benefits of international diversification.

Figure 11 shows the exposure of Australian portfolios for the period 2007 to 2015, and indicates that exposure to both markets fell sharply around the start of the global financial crisis before increasing.

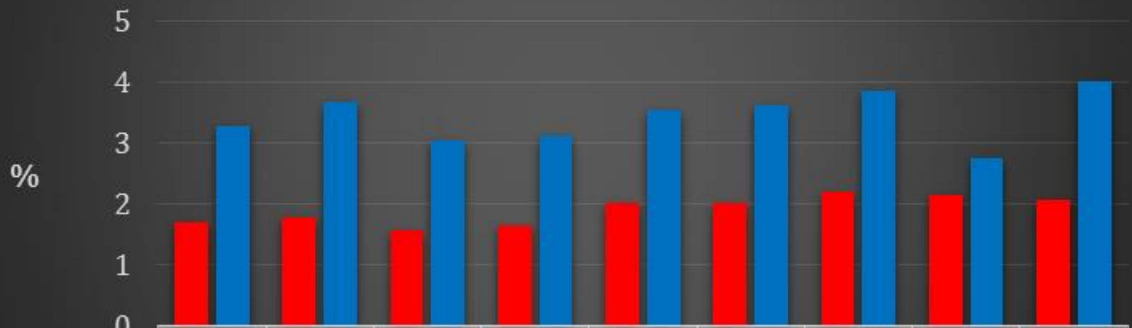
A notable exception was the considerable reduction in exposure to the EUBrex financial market in 2014, which was subsequently followed by a record high exposure in 2015.

Although average exposure for the period under investigation was 1.8 times higher in the EUBrex market (3.42 percent) to that of the UK market (1.89 percent), the average combined exposure was less than 6%.

The rise in exposure of Australian portfolios to the UK and EUBrex financial markets implies that market volatility created through a hard Brexit will have influence on Australian portfolios.

However, given the low overall exposure of Australian portfolios to both the UK and EUBrex financial markets, a significant direct loss in overall wealth is likely to be limited.

Figure 11: Exposure of Total Value of Australian Portfolios to UK and EUBrex Financial Markets (2007-2015)



	2007	2008	2009	2010	2011	2012	2013	2014	2015
UK	1.70	1.79	1.58	1.65	2.01	2.02	2.19	2.15	2.08
EUBrex	3.29	3.68	3.06	3.14	3.55	3.63	3.86	2.76	4.02

Notes: 1. Geometric Mean (UK) = 1.89% ; 2. Geometric Mean (EUBrex) = 3.42%
Source: IMF CPIS Database; World Bank World Development Indicators and authors' calculations

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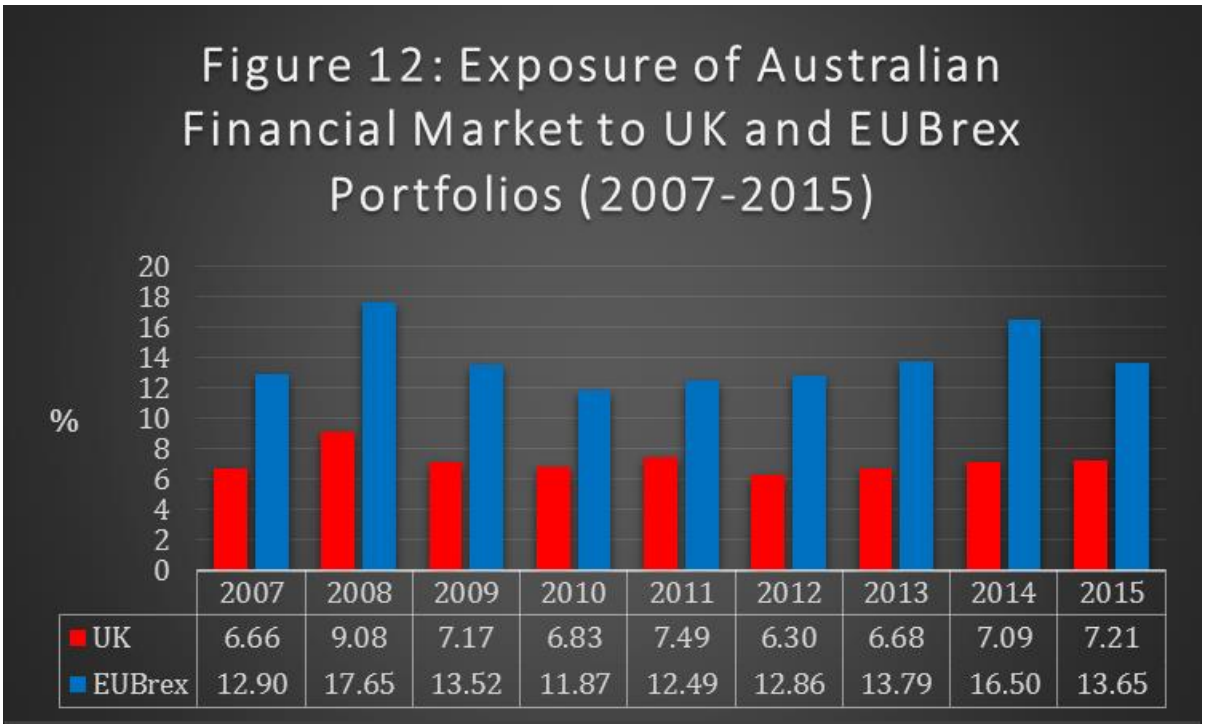
As the second measure of PI, the exposure of the Australian financial market to the UK and EUBrex portfolios is determined by the composition of the Australian financial market that was held in the UK and EUBrex portfolios from 2007 to 2015.

Figure 12 shows that the Australian exposure to both markets appears to follow a cyclical pattern, rising to the highest level around the start of the global financial crisis before falling and then rising once again. Notable exceptions were the UK in 2011 and the EUBrex in 2014.



Notes: 1. Geometric Mean (UK) = 7.13% ; 2. Geometric Mean (EUBrex) = 13.81%
Source: IMF CPIS Database; World Bank World Development Indicators and authors' calculations

The average exposure for the period under investigation was 1.9 times higher to the EUBrex portfolios (13.81 percent) than to the UK portfolios (7.13 percent).

The UK and EUBrex portfolios jointly account for approximately more than one-fifth of all asset holdings in the Australian financial market.

These findings imply that the market volatility created by the hard Brexit will have a significant direct bearing on the Australian financial market and, given the high levels of home bias, a significant indirect bearing on Australian portfolios.

With the significant levels of exposure of the Australian financial market to the UK and EUBrex portfolios, another aspect that requires attention is the importance of London as a financial centre and as a gateway for the UK and EUBrex funds destined for the Australian financial market. The future positioning of London post-Brexit can thus have deeper long-term implications for patterns of financial flows and ultimately for Australia's financial solidity.

Conclusion

In February 2017, the UK's Prime Minister Theresa May presented to Parliament a white paper to explain that her government intends to leave the EU single market, pursue a new strategic partnership with the EU, and secure new trade agreements with other countries bilaterally and in wider groupings.

The clear indication for the so called "hard Brexit" line thus demarcates the possible avenues for Australia's separate trade and investment relations with the UK and EU.

No formal step with the UK can be pursued until the conclusion of its withdrawal process from the EU, when the UK will finally become a separate customs entity, thus being entitled to negotiate international trade agreements.

Considering the present political climate and technical difficulties, it appears unlikely that the UK and EU will finalise an agreement before the two-year term set by Article 50 of the EU Treaty, or even before the advance of the Australia-EU free trade agreement.

Without a timely agreement, the UK and EU will revert by default to the non-preferential multilateral system under the rules of the World Trade Organization (WTO). Essentially, this means that by 2019 Australia, the UK and EU would all be levelled up within a multilateral regulatory framework of trade and investment relations.

This three-way levelling would eliminate the Australia-UK trade and investment subordination to the European single market at the regulatory level, however without discernible improvements in economic outcomes.

As things stand in early 2017 and in projection of 2019, Australia's trade and investment relationship with the UK and the EU could take broadly **four avenues of regulatory framework**.

Based on the economic assessment described above, Australia should consider these four options in the following order of preference (best to worst):

1) ***UK Unilateralism with EU Bilateralism*** – Concerting with the UK non-preferential, non-reciprocal and non-binding trade and investment liberalisations in targeted sectors as soon as the Brexit process concludes, and reassess this strategy upon finalisation of the Australia-EU free trade agreement.
2) ***UK and EU Bilateralism*** - Reciprocating preferential trade and investment concessions with the UK and the EU separately as soon as practicable in the post-2019 UK-EU arrangements.
3) ***Australia-UK-EU Trilateralism*** – Concurrently negotiating Australia-UK and Australia-EU preferential agreements for comprehensive integration with the post-2019 UK-EU agreement.
4) ***Long-term Multilateralism*** – Calling off trade agreements with both the UK and the EU to remain in the fold of the WTO system, and keep the 2019 status quo.

In line with the key points of the 2010 Australian Government's Productivity Commission Report on Bilateral and Regional Free Trade Agreements, this submission urges the Parliament to ensure that any future preferential trade and investment arrangements with the UK and EUBrex will be negotiated in Australia's economic interests with a rigorous and transparent evidence-based approach.

Recommendations

Negotiating with a rigorous and transparent evidence-based approach will require an independent body to conduct comprehensive pre-negotiation modellings based on realistic scenarios in comparison with alternative liberalisation options.

Consequently, further trade negotiations with the UK and EUBrex should eventually enable a full and public assessment of the provisions actually agreed.

Accordingly, this submission recommends to commence, monitor and evaluate the future negotiating processes according to the following guidelines:

I. Australia should not hasten to complete a bilateral free trade agreement (FTA) with the UK immediately after the Brexit process concludes, due to the highly uncertain geopolitical and economic climate that may unravel in the short term.

II. Australia and the UK should set up a non-preferential and non-binding Economic Cooperation Forum (akin to the APEC for the Asia Pacific nations, an AUKEC so to speak) to be in place shortly after the conclusion of the Brexit process in 2019.

III. The so called AUKEC Forum should be designed to buy Australia time to see what happens in the UK and between the UK and EU in the medium term, at the same time providing a strong foundation to conclude a mutually beneficial FTA with the UK for the long term.

IV. In the meanwhile, Australia should prioritise the conclusion of a comprehensive FTA with the EU to capitalise on historically optimal relations, and use it to hedge its subsequent negotiating position with the UK, which is likely to be on a weaker competitive stance with the EU than Australia.

V. Australia should avoid trilateral and multilateral options, as the end game should be at separate bilateral levels with both the EK and EU, in order to eventually achieve more favourable trading terms than the UK can achieve with the EU and vice versa.

VI. The overarching performance indicators of the negotiated provisions with both the UK and EUBrex should be to: a) make Australia’s economy more competitive in the European region; b) strengthen Australia’s geopolitical appeal to the emerging Asian powers; and c) enable more self-reliant postures at a time of uncertain directions for the global security and economic policy of the US.

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Submission for the parliamentary inquiry into Australia's trade and investment relationship with the UK

This submission addresses the following term of reference for the inquiry:

- *Possible implications for Australia's trade and investment relationships with the UK and the European Union consequent to the UK's exit from the European Union.*

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