

Ai GROUP SUBMISSION

Inquiry into the Business Experience
in Utilising Australia's Free Trade
Agreements

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Ai Group response to Inquiry into the Business Experience in Utilising Australia's Free Trade Agreements

About Australian Industry Group

The Australian Industry Group (Ai Group) is a peak industry association in Australia which along with its affiliates represents the interests of more than 60,000 businesses in an expanding range of sectors including: manufacturing; engineering; construction; automotive; food; transport; information technology; telecommunications; call centres; labour hire; printing; defence; mining equipment and supplies; airlines; and other industries. The businesses which we represent employ more than one million people. Ai Group members operate small, medium and large businesses across a range of industries. Ai Group is closely affiliated with more than 50 other employer groups in Australia alone and directly manages a number of those organisations.

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Executive summary

The Australian Industry Group welcomes this opportunity to assist the Government in understanding the utilisation of Australia's Free Trade Agreements (FTAs). Given the substantial investment that the Government has committed to negotiating and implementation of FTAs the aim should always be to provide a net benefit to Australian companies, and while much attention is given to exporters, benefits of FTAs should be enjoyed by importers, exporters and investors.

Ai Group's members do use FTA's for import and export, however many exporters do not and in Ai Group's capacity as an Authorised Body under the FTA certificate of origin regime, and as a deliverer of Austrade services under TradeStart, we have a unique perspective as to the reasons why exporters, manufacturers especially, may not be using FTAs.

The reasons for not engaging with FTAs are as varied and complex as the reasons for exporting in the first place, however they include; low levels of understanding how FTAs work; difficulty in accessing information; non-tariff barriers have a great impact on manufactured exports, and FTA's not meeting exporters needs.

Information and Advice

The first and most significant barrier, particularly for Small to Medium Enterprises (SMEs) is accessing information. While the recent efforts of Austrade and the Federal Government to conduct outreach seminars on the North Asian FTAs are welcome, as is the recent funding announcement in the Budget, they still lack the granular level of information that companies require to adequately utilise an FTA.

The significant benefit of all FTAs is the reduction of tariffs. The information on the rate and scale of tariff reduction is organised using Customs Harmonised System Tariff (HS) codes, as are the rules that companies must meet to qualify for Australian origin. In Ai Group's experience, very few exporters know what the HS code for their product is, or where to find it. While the HS code data is captured by Australian Customs at export, it is only used for statistical purposes and is often entered by freight forwarders, with no consequences for inaccuracy.

For exporters of horticultural or commodity products, the HS code is usually quite simple, but for manufacturers of elaborately transformed goods classifying goods takes some consideration. While the Australian Customs Service promotes itself as being the agency to help Australian importers to understand and access FTAs, they do provide some limited assistance to exporters who need help with classification of their products. However this is an incomplete service and as a correct HS code is the legal basis of FTA compliance, not entirely satisfactory.

The regional FTA architecture also causes confusion for exporters. For example, once the Trans Pacific Partnership (TPP) is in force, exporters will have three different FTAs to use to export to Malaysia. When presented with this information, the first question from exporters is: "Don't they cancel each other out?"

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The answer of course is that they don't. It is the responsibility of the exporter to analyse which FTA provides the best benefit for their product. Currently this information is contained in the respective texts of each FTA. When responding to a snap poll, the most common reason given by members for not using FTAs, was that they thought that the benefits applied automatically which means that many companies may not even be looking for this information.

Along with different tariff rates and rules of origin for each product across each FTA, exporters must also understand the different administrative requirements for each agreement. Ai Group has long been in favour of providing companies with the option of self-declaration to determine origin, not mandate Certificates of Origin certified by a third party. As an organisation authorised to issue Certificates of Origin for preferential agreements Ai Group is able to witness firsthand the administrative stress and time pressures that the mandatory regime puts on companies, particularly SMEs.

While Ai Group assists our members to go through these many steps, there is a need for a comprehensive service that all exporters can access. In the aforementioned snap poll, members indicated that other than Ai Group, they would expect to receive this service from either DFAT or Austrade.

Recommendations:

- *That DFAT's new FTA outreach service includes staff with Customs expertise to assist companies with classification and rules of origin.*
- *That the proposed FTA portal provides information arranged by market rather than FTA.*
- *That the outreach activities are delivered in a variety of modes and with enough detail to assist SMES in making informed decisions.*
- *That DFAT continue to pursue modern self declaration regimes under all FTAs.*

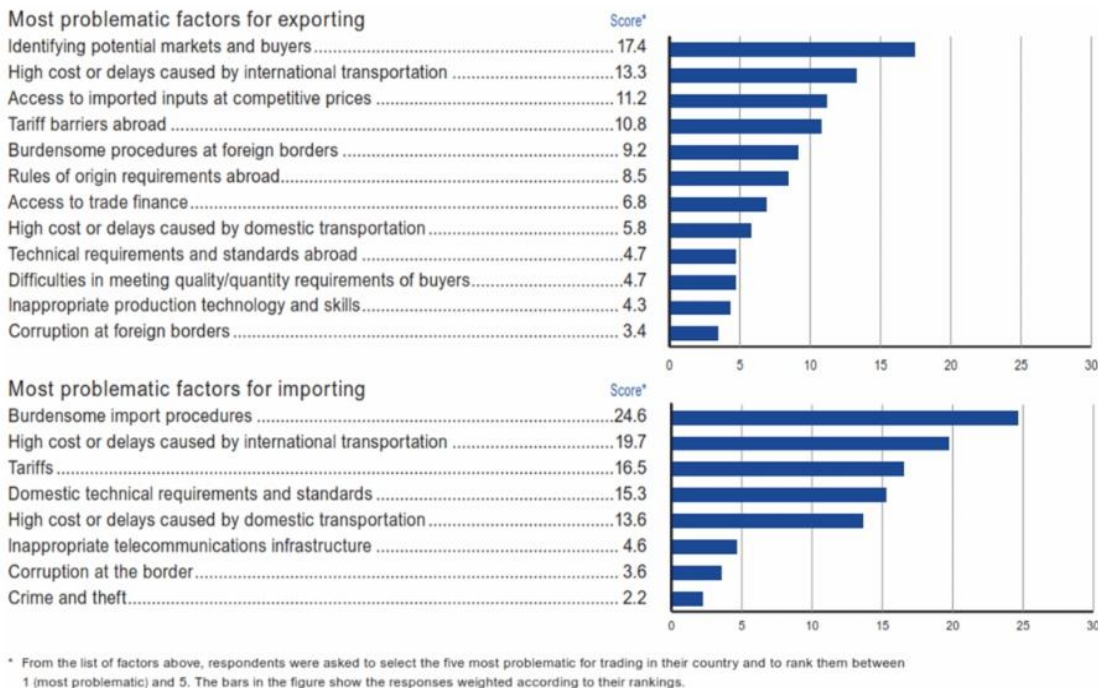
FTAs aren't delivering a competitive advantage to manufacturers.

In a recent poll of members, the second most cited reason for not using FTA's was that companies are not sure what the benefits are. As outlined above, the process for companies to find this information is currently quite onerous. However, many companies also offered that non-tariff barriers were a more significant barrier to export than tariffs.

This is supported by the data from last year's World Economic Forum's (WEF) Global Enabling Trade Report that showed that Australia's relative performance on global trade facilitation has deteriorated since 2008. When asked to nominate the most problematic factors in inhibiting exports, tariffs didn't make the top three problems.

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Table 1: Problematic factors for Australian exporters and importers in 2013

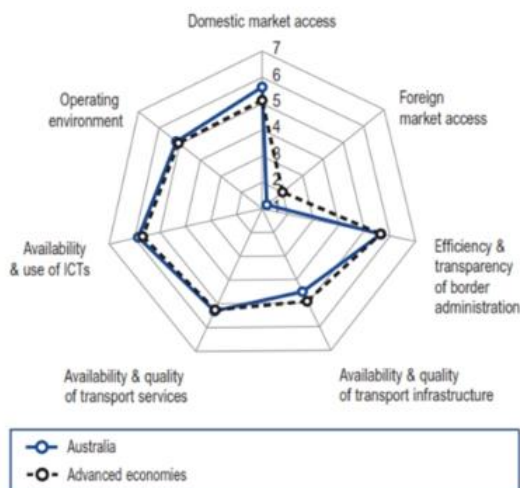


While Australia's Enabling Trade Index (ETI) has declined only marginally over the past six years, many other countries have improved their performance on cross-border trade facilitation. This has resulted in Australia's global ETI ranking slipping from a peak of 14th in 2009 to a poor 23rd in 2014.

Table 2: Australia's ETI results in 2014: detailed sub-indexes

Enabling Trade Index 2014

	Rank (out of 138)	Score (1-7)
Enabling Trade Index 2014	23	4.9
Subindex A: Market access (25%)		
Pillar 1: Domestic market access	18	5.6
Pillar 2: Foreign market access	134	1.2
Subindex B: Border administration (25%)		
Pillar 3: Efficiency & transparency of border administration	22	5.6
Subindex C: Infrastructure (25%)		
Pillar 4: Availability & quality of transport infrastructure	24	4.5
Pillar 5: Availability & quality of transport services	20	5.3
Pillar 6: Availability & use of ICTs	15	5.9
Subindex D: Operating environment (25%)		
Pillar 7: Operating environment	19	5.2



Australian manufacturers have been competing in a very low tariff environment domestically for a number of years, and this has forced them to compete on innovation and quality, rather than price.

The Australian Bureau of Statistics recently published its survey of IT use and innovation by Australian businesses for 2013/14 and reported that positive trends are evident, particularly among advanced

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manufacturing businesses, medical technologies and pharmaceutical firms. In particular it found that 52% of all Advanced manufacturing businesses were innovation-active in 2013-14, while 35% had innovative-activity still in development as at 30 June 2014 (well above the average for all industries). This sector includes “any manufacturing process that takes advantage of high-technology or knowledge-intensive inputs as an integral part of its manufacturing process”. In these data, this sector includes the manufacture of chemicals, medicines, vehicles, transport, professional and scientific equipment, computers, electronics and other specialised machinery and equipment.

This drive for innovation means that for some companies products, a 5% tariff saving is not worth the administrative burden. As one manufacturer of specialised equipment for the oil and gas industry responded to the news that his products could land in Indonesia 5% cheaper under AANZFTA: “They will buy it anyway.” While this response may surprise some, it is easy to understand the answer by looking at the way that FTAs work. The paradox of many of our FTAs is that the benefit is realised by the party that pays the import duties, usually the importer, however the administrative responsibilities lie with the exporter or producer. This does not reflect the common business practices of Australian Exporters. In Ai Group's experience, most Australian exporters export using the Incoterm FOB, Free on Board. This means that once the goods pass the imaginary ship's rail in Australia, exporters are no longer responsible for the costs of shipping the goods, including any concern with the import costs or procedures. Using an FTA forces them to be far more engaged in the import process than they have traditionally been. In the early days of implementation of an FTA, Ai Group will receive as many calls from overseas importers as we do from Australian exporters.

However, in some cases, there is no tariff for manufacturers to overcome. Prior to the signing of the recent Japan Australia Economic Partnership Agreement (JAPEPA), the tariff chapters that are relevant to Australia's Advanced Manufacturing sectors are largely already at zero, see Table 3.

Table 3 Japan's import tariff rates for advanced manufacturing from all countries

Chapter number	Product Descriptions	Number of products lines with a tariff rate of 1% or above.
Chapter 84	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof.	0
Chapter 85	Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and	10

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	accessories of such articles.	
Chapter 86	Railway or tramway locomotives, rolling-stock and parts thereof; railway or tramway track fixtures and fittings and parts thereof; mechanical (including electro-mechanical) traffic signalling equipment of all kinds.	0
Chapter 87	Vehicles other than railway or tramway rolling-stock, and parts and accessories thereof.	1
Chapter 88	Aircraft, spacecraft, and parts thereof.	0
Chapter 89	Ships, boats and floating structures.	0

An unintended consequence of both innovation and, in some cases, free trade, is that exporters face incredible non-tariff barriers, particularly in the areas of standards and product registration as well as nationalistic procurement policies. These barriers are particularly difficult to overcome as they are usually presented as safety or security measures, not barriers. However this isn't limited to manufactured products, agricultural products can lose all tariff reduction benefits through changed regulations as demonstrated in Table 4.

Table 4: Examples of non-tariff measures that reduce the benefits of an FTA

Country	Issue
USA (AUSFTA)	Buy America program undermined the access to US Government Procurement that Australian exporters were promised
USA and potentially Mexico and Canada (AUSFTA and TPP)	Recently proposed changes to the security arrangements for air freight to, through and over the USA could increase costs and delays for exporters who use airfreight to the US and other North American countries
USA (AUSFTA)	Change in recognition of standards assessment body meant that Australian manufacturers of wheelchairs could no longer sell into this lucrative market. It is important to note that on this occasion DFAT was able to reverse this decision and the exporter could retain the market.

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Thailand (TAFTA)	Additional excise on passenger vehicles nullified any Australian advantage from the removal of an 80% tariff.
Thailand (TAFTA)	Stone fruit achieved an immediate ZERO duty under TAFTA , but then Thailand changed the quarantine regulations and the market was completely closed for 3 years . At the time of closure all stone fruit and cherries were shipped to Thailand by AIR. This was no longer possible as Thailand insisted on sea freight only.
Indonesia (AANZFTA)	Indonesia is insisting on pre-shipment inspections for certain products which is creating increased costs and time delays for exporters.

A significant win for Australian businesses in the recent China Australia Free Trade Agreement (ChAFTA) is the inclusion of a specific mechanism to review and address Non-Tariff Measures on a case-by-case basis, as raised by Australia or China. A Committee of ChAFTA will be tasked with ongoing work to address NTMs, including preparing a report and recommendations on NTMs in the first year of operation. It is important that Australian exporters are not only made aware of this provision, but also the administrative process that they need to follow to register issues.

Finally, an important factor that determines the success of Australian exports cannot be resolved by an FTA; exchange rates. In this year's Ai Group Business Prospects Survey and in our CEO Surveys in 2014 and 20112 , we asked CEOs to identify the AUD/USD exchange rates at which their own exported goods and services, and those competing against imports, become uncompetitive. The majority of non-manufacturing businesses did not report any exports over each of these years, reflecting their stronger focus on domestic markets. This year's survey results indicate that in 2015, 94% of manufacturing exporters are able to be competitive in export markets at exchange rates of US80¢ or below, per Australian dollar. This outcome is similar to those for 2014 and 2011, when 95% and 93% of manufacturers reported that their exports can compete when the Australian dollar is at or below US80¢. If the Australian dollar trades in a range of 81-90 US cents however (as it did through much of 2014), then only 63% of manufacturing businesses would remain competitive against exports in 2015 (around the same proportion as in 2011), and 66% would be able to compete with imports (up from 45% in 2011). With the further depreciation of the Australian dollar since September 2014, prospects have improved for a pickup in competitiveness among manufacturing exporters

Recommendations:

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- *That DFAT's new FTA outreach service collects information on non-tariff measures that can be addressed under the arrangements of the respective FTAs*
- *That DFAT dedicate resources to educating Austrade and State Government front line trade facilitation staff in the provisions of the ChAFTA NTM review body and actively seek input for issues to address.*

Strategy on selecting FTA partners.

The Australian government has negotiated agreements with eight of our top ten trading partners and more recently, three of our top five trading partners. This raises the question, what is an FTA improving upon? While they may create new opportunities for sections of Australian industry, there may be other factors that will prevent companies from converting those opportunities into exports. Market selection is rarely is made on tariff rates alone.

If we want the investment of an FTA to pay off, we should be looking at markets with potential, but aren't strong trading partners yet, for example, emerging African or Latin American countries. These countries also have not undertaken the trade liberalisation measures that other markets have and have the potential for greater gains.

Conclusion

While we know that there are many businesses using FTAs to improve their competitiveness, there are complex reasons for utilisation levels not meeting expectations. While better communication will improve take up among SMEs, it won't address all the barriers to trade that extend beyond tariffs.

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