Submission No 6

Inquiry into Australia's trade and investment relationship with Japan and the Republic of Korea

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Mr Paul Zinkel
Inquiry Secretary
Joint Standing Committee on Foreign Affairs, Defence and Trade
Trade Sub-Committee's
Parliament House
CANBERRA ACT 2600

By email: jscfadt@aph.gov.au

Dear Mr Zinkel,

The Australian Industry Group (Ai Group) welcomes the opportunity to contribute the views of industry to the inquiry by the Trade Sub-Committee of the Joint Standing Committee on Foreign Affairs, Defence and Trade into Australia's trade and investment relationship with Japan and the Republic of Korea (Korea).

Ai Group, with over 10,000 members, is a leading national industry body representing various sectors including manufacturing, engineering, construction, automotive, food, transport, information and communication technology, call centres, labour hire, printing, defence and aerospace, mining equipment and supplies, and other related service industries.

Ai Group has national, regional and local profiles with offices located in Adelaide, Brisbane, Canberra, Sydney and Melbourne, as well as regional centres and an affiliated office in Perth. Ai Group is closely associated with more than 50 other employer groups and has long standing links with over 80 international organisations. Together, Ai Group and its affiliates represent the interests of approximately 60,000 businesses which employ in excess of 1.2 million staff across Australia and the world.

In its role as representative of Australian industry, Ai Group fully appreciates that international trade is fundamental to Australia's on-going growth, development and prosperity. In this regard, Australian industry relies upon all levels of government to foster an environment that delivers appropriate domestic and foreign policy settings to promote an internationally competitive and sustainable economy.

Japan

Japan is Australia's second largest export market. Australia is a critical supplier to Japan of clean and safe food products and energy and mineral resources, representing Japan's third-largest source of merchandise imports after China and the United States.

In 2010, two-way goods and services trade between Australia and Japan was valued at $66.1 billion, an 11.8 per cent increase on 2009. Exports to Japan in 2010 increased by 13.7 per cent to $45.6 billion, representing approximately 18 per cent of Australia's total exports.

In 2009-10, Australia's key exports to Japan included coal ($12.9 billion), iron ore ($6.0 billion), beef ($1.7 billion) and copper ($1.2 billion). Japan was Australia's largest export market for beef, fish, animal feed, coal, LNG, aluminium, beef, dairy products and cereals other than wheat.

Australia is also an important market for certain Japanese consumer and industrial products. Last year, passenger vehicle imports increased by 26.8 per cent to $7.0 billion, representing Australia's largest import item from Japan. Other significant merchandise imports from Japan include: tyres ($571.9 million in 2009-10), civil engineering equipment ($533 million), chemicals ($477 million) and office machines ($450.1 million).

Beyond merchandise trade, two-way trade in services is valued at over $4 billion. Underpinned mostly by the tourism and education sectors, services trade represents a balanced mix of imports ($2.1 billion) and exports ($1.9 billion), making Japan Australia's sixth-largest services trade partner (in 2009-10).

Japan is Australia's seventh-largest destination for foreign investment. At the end of 2010, Australia's stock of investment in Japan was $29 billion. In return, Japanese investment in Australia (our third-largest investor) is significantly higher with an investment stock of over $118 billion.

In terms of indirect investment, Australia is now one of the largest recipients of offshore investment by Japanese mutual funds, receiving 12 per cent of all such funds being invested offshore. Japanese direct investment (44 per cent of total investment) has contributed significantly in the development of Australia's iron ore and coal sectors.

Japanese investment has also been important for the development of Australia's export-oriented manufacturing sector. For example, Toyota Motor Corporation Australia has invested heavily in manufacturing and car design facilities since the mid 1990s. Japan has also made substantial investments in Australia's food sector, including the acquisition by Asahi Breweries of beverage maker Schweppes Australia, and the purchase of Dairy Farmers and Lion Nathan by Japan's largest brewing company, Kirin. There has also been direct investment by the major dairy company, Snow Brand, in dairy ingredients in Victoria and Nippon Meat Packers in cattle-raising, feed-lotting and processing in Eastern Australia.

There is no doubt that Japan is one of Australia's most important and significant trading partners. The relationship is robust and already facilitates an enormous amount of bilateral trade and investment with efficiency. However, beyond the largely tariff free resources sector, Australian industry has experienced difficulties penetrating the Japanese market.

Significant tariff barriers remain for Australian exporters when attempting to enter the Japanese market. While Japan has a relatively low, simply applied tariff, its tariff regime is skewed heavily towards protection of its agricultural sector. In addition, there is an existing practice of heavy agricultural subsidisation.

Japan also imposes high tariffs on a number of food products, including processed foods. Key areas of high tariffs in this sector include meat, dairy products, cereals and preparations, processed foods, sugars and confectionery, wine and other beverages and tobacco. For example, honey from Australia faces a minimum tariff of 30 per cent.

Japan also maintains some unwarranted non-tariff barriers, such as: standards unique to Japan, both formal and informal (eg. list of food additives, which limits the use of specific food additives on a product-by-product basis, is inconsistent with international practice); official regulations that favour domestically produced products and organisations; and licensing powers which limit membership and market access. Australian exporters would also benefit from greater transparency surrounding import insurance and airport clearance fees, as well as streamlining of Customs clearance procedures.

Given the depth and scope of the relationship, there is a clear mutual interest in the two countries further liberalising their trade and investment links. Ai Group supports the negotiation between the Australian and Japanese Governments of a Free Trade Agreement (FTA). A high quality, liberalising FTA would provide an important opportunity to further develop Australia's trade with this key market, providing industry with the mechanisms to address regulatory impediments and other non-tariff barriers to Australian exports and investment.

However, to date FTA negotiation progress has been slow with twelve rounds held between April 2007 and February 2011. On 11 March 2011, Honshu on Japan's northern Pacific coast was devastated by a tsunami causing great loss of life and enormous structural damage. Recovery efforts, naturally, have distracted the Japanese Government and contributed to further delays in FTA negotiation efforts. It is important that these negotiations are reinvigorated immediately, with a view to delivering a highly liberalised, comprehensive free trade agreement as soon as possible.

Korea

Korea is Australia's fourth-largest overall trading partner and was our third-largest goods export market in 2010. Our total two-way trade relationship is worth over $25 billion. Key Australian exports include crude petroleum, iron ore, coal and beef.

Although primary commodities feature greatly in the bilateral relationship, trade is also important across a range of industries. Our major exports of manufactures to Korea are automotive engines and pharmaceutical products but also include automotive parts, biotechnology and information and communications technology. Beyond beef and wine, our food and beverage exports also include dairy products and seafood.

In 2010, Korea was our ninth largest import source country, with imports valued at over $7 billion. Our major imports are finished products such as cars, electronic equipment and computers, as well as refined petroleum. There has been a 42.2 per cent year-on-year increase in the value of passenger motor vehicle imports.

Beyond merchandise trade, Australian services exports to Korea were valued at $1.9 billion underpinned by recreational and education-related travel services. Education exports have been particularly successful, with Korea ranked as Australia's third largest source of foreign enrolments. Tourism is also very important with almost 200,000 visitors from Australia to Korea and over 40,000 Australian tourists visiting there.

Investment ties between Australia and Korea are growing modestly from a comparatively low base. In 2009, the stock of Australian investment in Korea totalled $6.3 billion while Korean investment in Australia totalled $8.7 billion.

Major Korean investments in Australia include Korea Zinc's investment in the Sun Metals Corporation refinery in Queensland, and POSCO's investment in BHP-Billiton's iron ore resources in Western Australia. Currently, ROK investors are involved mostly in resource development (including in Queensland coal-seam gas and New South Wales coal mines) or in import and distribution (e.g. Hyundai, Daewoo, Kia, LG and Samsung). Macquarie and ANZ banks have a significant Korean presence active in funds management and infrastructure investment.

Australia's trading relationship with Korea is important and has the potential to grow substantially in the coming decade. However, beyond the resources and education sectors, Australian industry has also experienced difficulties entering the Korean market.

Like Japan, significant tariff barriers remain for Australian exporters when attempting to enter the Korean market. Liberalisation will benefit Australian exporters with obvious gains to be made from reductions in Korean agricultural trade barriers. The Australian agricultural sector would benefit from improved Korean market access in meat, dairy, grains, sugar and, if achievable, rice.

One example is pork which is Korea's most consumed protein. By addressing existing Korean trade barriers, an Australian-Korea FTA could provide an opportunity to realise market access gains for Australian pork exports.

However, along with any negotiated market access for agricultural products, there will also need to be accompanying outcomes on sanitary and phytosanitary (SPS) and other technical barriers. Clear rules and agreed mechanisms able to effectively resolve SPS and other technical barriers will be essential to realising any benefits of the negotiated market access outcomes.

Beyond the agricultural sector, in a suitably comprehensive agreement, gains for Australian manufacturers could also be expected. Tariff reductions in areas such as automotive engines, pharmaceutical products, chemicals and wine where Korean tariffs are more modest but the bilateral trade is growing and important, would deliver benefits.

Beyond tariff reductions, it will be essential to acknowledge and address the use of non-tariff barriers (NTB) such as discriminatory taxes, burdensome regulatory and safety compliance requirements for imports. These measures have been employed to protect certain Korean industries, in particular the automotive sector. The Korean automotive market is almost exclusively dominated by domestically produced vehicles. Dissimilarly, the Australian automotive market is very open with a high import penetration.

Sensitive Sectors

Reducing trade barriers through comprehensive liberalisation of bilateral trade and investment under comprehensive free trade agreements should eliminate tariffs immediately on all but a minimum of sensitive items to which transitional tariff reduction arrangements should be applied. Ai Group acknowledges that certain items within manufacturing will require a phased tariff reduction period.

Ongoing and extensive consultation with industry is necessary to develop the narrowest scope for items requiring transitional arrangement. Nonetheless, Ai Group analysis to date indicates transitional arrangements may be necessary for items such as certain TCF (textile, clothing and footwear), automotive, and machinery and equipment products.

Certainly the import sensitive industry sectors of automotive and TCF are currently dealing with restructuring in the face of unilateral tariff reduction (in line with Australian Government policy) and may require phased tariff reduction. It is essential that Australian vehicle and components manufacturers be provided with equitable access to the Japanese and Korean markets.

Such an approach would not preclude the possibility of equitable zero-for-zero tariff arrangements being suitable on certain items within these manufacturing sub-sectors. Further, any margin of preference allocated by Australia on Japanese and Korean goods on items with retained tariffs should be matched by both nations. In addition, strategies to remove non-tariff barriers to Australian exporters into the corresponding Japanese and Korean automotive markets must be included in the negotiated outcomes.

Export Promotion and Facilitation

In preparing this submission, we contacted member companies currently exporting to Japan and/or Korea. Their market-specific comments have been incorporated above. Beyond the need for greater access to export markets through reduction of tariff barriers and addressing non-tariff measures, Australian exporters need more assistance from the Government to successfully compete internationally.

Like any foreign market, Australian exporters must be well prepared and cognisant of the local business culture which will help build confidence through solid relationships and assist in reducing misunderstandings. This is especially important in markets such as Japan and Korea, which rely on developing business relationships through in-person contact and require a high level of cross-cultural sensitivity.

The Export Market Development Grants (EDMG) Scheme, administered by Austrade, is an effective support mechanism which provides financial assistance to small and medium Australian enterprises (SMEs) to develop new export markets. The Scheme provides critical funding to many SMEs during the costly and complex initial phases of identifying and establishing new export markets through the reimbursement of up to 50 per cent of their expenses incurred on eligible export promotion activities.

This year has seen a lower than expected level of EMDG claimants. Our analysis suggests this is, in part, due to ongoing uncertainty surrounding the EDMG Scheme. Recently there have been annual adjustments to the eligibility criteria and allowable expenses. This, as well as the inability to fund a fixed return percentage, has led to increased uncertainty for the Scheme users and created a growing aversion among SMEs to invest their limited funds to develop export markets. This trend, should it continue, may prove a bellwether for the ongoing health of the non-mining SME export sector going forward.

While understanding the current fiscal pressures on the Government budget, it is imperative that support for exporters is expanded.

Maintaining Competitiveness

Through the last two decades of unilateral trade liberalisation, Australia has become one of the most open economies in the world with average tariffs at less than 3.9 per cent. This domestic structural change has contributed to the liberalisation of the Australian economy, providing increased market access to importers and an almost free flow of imported goods and services.

In the current patchy economic times, Australian exporters are also carrying the burden of a post-float high Australian dollar. These factors are compounded by increased domestic cost pressures and interest rate sensitivity. Given global economic settings and expected continued high commodity prices this situation is not expected to change in the near future.

Therefore it is critical that industry gains greater, unimpeded access to export markets and, furthermore, that this access provides Australia with competitive positioning in the complex system of international trade agreements.

As our trading partners continue to negotiate agreements with our trading competitors, the timely completion of highly liberalised, comprehensive, World Trade Organisation consistent free trade agreements with both Japan and Korea would go some way to assist supporting Australia’s international competitiveness.

The final negotiated outcomes of agreements with Japan and Korea must deliver a balance of benefits that is in Australian industry's favour (with equitable, reciprocal Japanese and Korean market access) and deliver Australia a competitive advantage, or at the very least, equal rights to other countries with preferential access to the Japanese and Korean markets.

After implementation, for such agreements to be effective, the Government must also strengthen the linkages between market access negotiations, trade and investment facilitation and market development, strategic consultation and resources for Australian companies to better realise these opportunities. In this increasingly competitive global environment, it is critical that the Government reduces barriers to Australian competitiveness where possible.

Yours sincerely

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