

AUSTRALIA-CHINA AGENDA 2013

Improving Australia's Investment Environment

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THE AUSTRALIAN Centre on China in the World engages with the public and policy discussion of relations with the People's Republic of China and the Chinese world. Australia-China Agenda 2013 is our contribution to this important election year and the on-going consideration of the bilateral relationship.

This is a relationship that touches on virtually every aspect of our national life. A mature and beneficial engagement of such breadth and depth requires the leadership and support of government at all levels, as well as public stewardship, media understanding, educational enhancement and the strategic involvement of the business community.

Australia-China exchanges are also profoundly influenced by regional and bilateral relationships. Australia and China trade in goods as well as culture, politics and people, ideas and education, community and personalities.

Australia-China Agenda: 2013 brings to the attention of the public and the media, politicians and specialists some reflections and policy ideas authored by specialists with a professional interest and involvement in the relationship.

—Geremie R. Barmé
Founding Director, CIW

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JANUARY 一月

FEBRUARY 二月

MARCH 三月

APRIL 四月

MAY 五月

JUNE 六月

JULY 七月

AUGUST 八月

SEPTEMBER 九月

OCTOBER 十月

NOVEMBER 十一月

DECEMBER 十二月

二〇一四年

TO DEVELOP capital-intensive sectors of the Australian economy, such as mining and infrastructure, foreign investment is a necessity, not an option. Given Australia's small population and vast geography, the domestic savings pool has always been too small to fund large-scale projects in these sectors, at least outright, meaning that foreign savings must be drawn upon if growth and jobs are to be unlocked.

For many decades, foreign investment came overwhelmingly from our traditional economic partners, such as the US, UK and Japan.

In more recent years, however, considerable press attention has been devoted to instances of Chinese firms seeking to invest in Australia. Prominent examples that have reached fruition include China's Minmetals buying most of the assets of OZ Minerals in 2009, and the purchase of Cubbie Station by a consortium led by China's Shangdong Ruyi in 2012.

The stock of Chinese investment in Australia currently stands at just \$22.9 billion, a mere 1.1% of the total stock of foreign investment, and 1.6% of GDP.

Indeed, according to data compiled by the Heritage Foundation, over the period 2005-2012 Australia attracted more large-scale investment attention from China than did any other country, including the US.

Such headlines give the impression that as China's global economic status has risen, Australia has managed to successfully tap its capital markets, in much the same way it did with the US, UK and Japan in earlier times. Given the economic malaise that now exists in traditional source funding countries, China's emergence would seem particularly timely.

Such an impression however is misleading. Other data, apparently less worthy of media attention, suggest that Australia's utilisation of China's vast pool of domestic savings has been surprisingly limited.

Consider this: Over the past decade the US has been one of the world's largest net capital importers. Yet in spite of this, according to Balance of Payments data compiled by the Australian Bureau of Statistics (ABS), Australia managed to play host to an additional \$A330 billion in US investment over the period 2003-2012. The accumulated stock of US investment in Australia at the end of 2012 stood at \$A617.6 billion. Meanwhile, over the same period, in spite of China being one of the world's largest net capital exporters, Australia only managed to attract an additional \$20 billion in Chi-

nese investment. The stock of Chinese investment in Australia currently stands at just \$22.9 billion, a mere 1.1% of the total stock of foreign investment, and 1.6% of GDP.

Balance of Payments data are particularly instructive because they measure capital inflows in net terms. It can hardly be considered that China has become a more important supplier of capital to Australia if large inflows in a given year are matched by equally large repatriations. Balance of Payments data also seek to capture actual capital flows, not mere expressions of investment intent.

Some Chinese capital no doubt also finds its way to Australia through Hong Kong Special Administrative Region, which is listed as a separate source country by the ABS, as well as via tax havens such as the Cayman Islands. But even if allowances are made for this, the basic conclusion remains: Chinese investment in Australia is marginal.

The small amount of Chinese investment in Australia is also not simply a matter of China being late to the party, with the trend now being irrevocably upwards. ABS data show that in 2012, net inflows of Chinese investment amounted to \$3.9 billion, not much higher than the average annual value since 2006, and well down on the high of \$7.8 billion in 2009. Net inflows of US investment in 2012, however, were \$43.7 billion. Even if only direct investment is considered, as opposed to also including portfolio investment, net inflows from the US were still four times larger than those from China.

The immaturity of Australia's investment relationship with China stands in sharp contrast to the trade relationship, where China is both our most important export destination and import source.

One reason the inward investment numbers are so small is because China maintains a fairly extensive system of capital controls. For example, any Chinese company wanting to invest abroad must obtain approvals from the National Development and Reform Commission, the Ministry of Commerce and the State Administration of Foreign Exchange. Such a bureaucratic approvals process is likely in particular to discourage overseas investment by Chinese private sector firms.

There is another reason however: disincentives to Chinese investment erected at the Australian end.

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By far the most significant of these is the requirement that, irrespective of size, proposals for inward investment from 'foreign governments', which includes state-owned enterprises (SOEs), must go through a Foreign Investment Review Board (FIRB) approvals process to determine whether they are in the 'national interest'. In contrast, inward investment by privately owned firms only requires FIRB approval if the amount is more than \$248 million, and in the case of US and New Zealand firms, the threshold is raised further to \$1.08 billion.

What these rules mean in practice is that nearly all Chinese inward investment must go through a lengthy and uncertain approvals process, while only a fraction of investment from other countries must do so.

Joint work by KPMG and Sydney University estimates that nearly ninety percent of the Chinese investment that has made its way to Australia has come from SOEs. This is consistent with the pattern of China's overseas investment globally.

Research by the Australia-China Business Council has reported a widespread perception amongst Chinese investors that they did not feel as welcome in Australia as they did in some other host countries.

Further complicating matters is that having ultimate say on whether a proposed investment is in the 'national interest' is the Commonwealth Treasurer, a popularly elected official. Amongst the Australian public, there is a well-documented widespread distrust of foreign investment. A 2013 Lowy Institute Poll found that a majority of Australians (fifty-seven percent) felt, 'the Australian government is allowing too much investment from China', a staggering finding given the small actual numbers involved.

The justification for the acute attention paid to 'foreign SOEs' – which more often than not means Chinese SOEs – is the assumption that they are more likely to have 'non-commercial' or 'external strategic' motivations as compared to private sector firms. Suspicions surrounding Chinese SOEs were clearly evident in Opposition Leader Tony Abbott's statement in Beijing last year that: 'it would rarely be in Australia's national interest to allow a foreign government or its agencies to control an Australian business'.

Not surprisingly then, research by the Australia-China Business Council has reported a widespread perception amongst Chinese investors that they did not feel as welcome in Australia as they did in some other host countries.

What Can We Do?

1. Reduce the relevance of ownership type when determining whether proposed foreign investment should attract special FIRB attention.

To the extent that the current inward investment regime acts to deter investment by Chinese SOEs, it is clear that there will be high costs to the national interest in terms of the growth of the capital stock, and therefore in terms of labour productivity and job creation.

What is less clear is how the inward investment regime benefits our national interest in some broader sense.

The most basic point to note here is that any firm operating in Australia, whether they are domestic or foreign (and if foreign, whether they are state-owned or private), is subject to a comprehensive set of laws and regulations that aim to promote fair competition based on commercial principles and transparent reporting. There also exist rules and regulations to guard the integrity of the tax base, the industrial relations system and the environment. If these laws are inadequate in some way, then they will be inadequate for all firms, from domestic privately-owned firms to Chinese SOEs.

All too frequently we see other issues being conflated with investment by Chinese SOEs. For example, much angst has been expressed regarding the purchase of Australian farms by Chinese SOEs for the purposes of minerals exploration. But this is clearly a land use question, not a foreign investment one, and whether land currently used for agriculture and livestock production can be used for mining purposes in the future is a decision that resides exclusively with Australian governments, not Chinese SOEs.

2. We need to appreciate that Chinese SOEs are acutely aware of their position as ambassadors of China abroad. They are cognisant of the fact that any misstep in terms of contravening Australian laws and regulations will be latched upon by a local press that is hungry for controversy, and politi-

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cians willing to exploit such controversy. It is largely for this reason that Chinese SOEs such as Minmetals and Yancoal have preferred to appoint locals to senior management positions. This ambassadorial role is likely to be felt far more keenly by Chinese SOEs than Chinese privately owned firms.

3. When designing rules that so clearly impact upon inward Chinese investment, we need to consult extensively with Australians who have direct experience in such matters. A small but growing number of Australian business leaders now operate in companies that have Chinese SOE parents. Figures such as Andrew Michelmore, CEO of MMG Limited, are able to quickly dispel myths such that since his company became majority-owned by a Chinese SOE, his day to day decision making has been impacted upon by Communist Party officials sitting in Beijing. Such people are also able to elucidate upon the distinct benefits that having a Chinese SOE parent can bring. For example, Michelmore has noted that the stable funding base afforded by China's Minmetals has allowed him to focus on executing the long term strategic goals of the company, which is publically listed in Hong Kong, rather than being preoccupied with frequent trips into volatile global capital markets.
4. Work with China to fast track formal agreements such as last year's Memorandum of Understanding on infrastructure cooperation to tangible projects.
5. Take opportunities as they arise to press the case to China that loosening capital controls at home will bring mutual benefits for both countries. For Australia, it would help to facilitate more inward investment by Chinese privately-owned firms.
6. The government of the day needs to communicate an unequivocal line on the net benefits afforded by Chinese inward investment. Presently we have an incongruous situation where amongst the general public there is a general reticence towards Chinese firms wanting to invest in Australia, while at the same time decisions by other foreign companies such as Mitsubishi and Ford to abandon their Australian operations are greatly lamented. As former Commonwealth Treasury Secretary, Ken Henry, put it so aptly last year: 'They don't want them to come, it appears, but they don't want them to leave either.' The need for strong leadership is obvious.

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AUSTRALIAN CENTRE ON CHINA IN THE WORLD

The Australian Centre on China in the World (CIW), College of Asia & the Pacific (CAP), The Australian National University (ANU) is an initiative of the Commonwealth Government of Australia in collaboration with ANU, a university with the most significant concentration of dedicated Chinese Studies expertise and the publisher of the leading Chinese Studies journals in Australia. CIW is a national research centre that is jointly managed by a body of academics that includes scholars of China at universities in Adelaide, Brisbane, Hobart, Melbourne and Sydney.

The Centre is a humanities-led research institution that is engaged with the broad range of social sciences to produce academic work that, while relevant to the full spectrum of demands of international scholarship, also relates meaningfully to those in the public policy community, and to the broader interested public, both in Australia and overseas. It values a New Sinology, that is an intellectual, cultural and personal involvement with the Chinese world (be it in the People's Republic, Hong Kong, Macau, Taiwan or globally) that is underpinned by traditions of academic independence, local fluency and disciplinary relevance.

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CIW sites

<http://ciw.anu.edu.au>

<http://www.thechinastory.org>

CIW publications (also available online)

China Story Yearbook 2013: Civilising China, October 2013

China Story Yearbook 2012: Red Rising, Red Eclipse, August 2012

Stephen FitzGerald, *Australia and China at Forty—Stretch of the Imagination*, 澳大利亚与中国已届四十年—舒展的想象力, February 2013

Australia and China: A Joint Report on the Bilateral Relationship 中国和澳大亚：关于双边关系的联合报告, with the China Institutes of Contemporary International Relations (CICIR), February 2012

CIW journals

China Heritage Quarterly

(<http://www.chinaheritagequarterly.org>)

East Asian History

(<http://www.eastasianhistory.org>)

The China Journal, co-published

(<http://ips.cap.anu.edu.au/chinajournal/>)

Danwei, affiliated

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