

Trade Opportunities for the Australian ICT Services and Creative Industries sector - Australia's North Asian FTAs¹

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1. What FTAs do

More than just tariffs

Australia's recent FTAs, including those with Korea, Japan and China cover more than just tariffs. They now encompass a wide range of economic activity, including not only tariff reductions for goods, but commitments to reduce investment barriers, some liberalization of services and provisions addressing intellectual property, e-commerce, and temporary movement of labour.

Australia's FTAs with Korea, Japan and China

Korea Australia Free Trade Agreement (KAFTA)

KAFTA is one of our most comprehensive FTAs. It covers goods, services, investment, data processing, temporary movement, etc. KAFTA is modelled on the Australia/United States Free Trade Agreement (AUSFTA) and the (on hold) Trans Pacific Partnership Agreement (TPP). It entered into force in December 2014.

Japan Australia Economic Partnership Agreement (JAEPA)

JAEPA is the most comprehensive and significant bilateral agreement Japan has negotiated to date. JAEPA delivers improvements in access for Australian services providers which is equivalent to or better than that Japan's previous FTAs. It adopts a similar content and structure to KAFTA. It began in January 2015.

China Australia Free Trade Agreement (ChAFTA)

ChAFTA is China's first comprehensive agreement with developed economy and the first covering trade in services. It became operational in December 2015. ChAFTA provides Australian services providers with improved access to the China market (second only to China's agreements with Hong Kong and Macau). For the moment, competitors from other developed financial markets such as the United States, Europe or Japan cannot match this access.

Regulation of services and investment

Regulation of services and investment in FTAs involves legal commitments for regulation. Services businesses and investors 'use' FTAs differently to traders of goods; rather than choosing to receive the benefit of tariff preferences, services providers benefit from FTAs as recipients of changes to relevant laws and regulations arising as a result of formal legal commitments. These commitments change or remove regulatory controls in foreign (and home) markets, distinct from tariff reductions which apply to goods.

FTAs are treaty agreements between governments. They do not set rules for private market activities, though these are affected by government regulation.

¹ Material prepared for Briefing: *Trade Opportunities for the Australian ICT Services and Creative Industries Sector*, Australian APEC Study Centre, RMIT University, 6 September 2017.

FTAs do not grant ‘free trade’ or guarantee a completely open market. The commitments to remove ‘barriers’ can be conditional or may be subject to exceptions. The degree of liberalisation accorded varies among economies, by sector and by agreement. It depends on what has been agreed.

ICT services in FTAs

In the ICT sector, both goods and services are traded. While ICT products include manufactured goods, (e.g.: computers and communications equipment and components), ICT services encompass a wide range of activities. They include telecommunications services, computer programming and information services, data processing, hosting and related activities and computer software as well as wholesaling of ICT products and more broadly content and media services.² Many ICT activities involve both goods and services, such as digital games, digital health products, Edtech and exploration and mining software (EMS). See Annex 1.

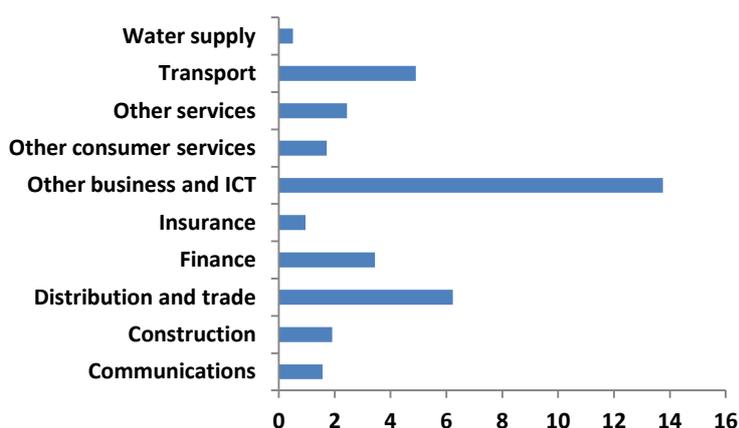
2. Why FTAs matter

ICT is an important Australian industry

ICT services exports are growing. Australian exports of ICT goods and services were just over AUD7bn in 2015/16, or just over 10% of all services exports. ICT services exports are growing faster (14.3% 5 year trend) than the average rate across all services (6.3%) and faster than exports of ICT goods (10.7%).³ Imports were larger (AUD31.2 billion), and mostly goods (25 billion) but are growing at a slower rate than exports (4.4% 5 year trend compared to 12.4% for exports).

ICT services are ‘embodied’ in most traded goods and services. Export data does not include ICT services which are ‘embodied’ in other services and goods (e.g.: ICT design, development in delivery of other services such as financial, professional, health and in traded goods such as electrical and electronic equipment) – when this is taken into account the value of ICT services in exports is much more significant.

Value added contribution to Australian exports, by services sector (%) 2011



Source: World Bank, WITS, World Integrated Trade Solution

² For example, motion picture, video and television programme activities as well as sound recording and music publishing activities, programming and broadcasting activities, internet publishing, consulting and provision

³ Source: DFAT. Based on OECD definition, ABS and DFAT data 2015/16. See

ICT and other business services embodied as inputs in other sectors' exports, as an industry, contribute the largest share of value added (13.75% in 2011) to Australia's exports.⁴

The industry is a major employer. More than 2.5 million Australian employees (or 22% of the workforce) work intensively with ICT (e.g.: accountants, accounting clerks, advertising, public relations and sales managers).⁵ In Victoria, the industry directly employs 74,700 people, (approximately one third of Australia's ICT professionals).⁶ The exploration and mining sector (EMS) alone directly employs more than 2,500 people.⁷

It is an important contributor to broader economic activity. The Australian ICT market was estimated to be worth over AUD120 billion in 2015 (fifth largest ICT market in the Asia-Pacific region, after Japan, China, India and Korea), accounting for 4.6% of Australia's GDP.

Aside from direct economic activity involving ICT and tech workers, the sector plays an important role in accelerating the rest of the national economy, contributing 4.9% to Gross Value Add (measuring the contribution of ICT services in the production of other goods and services); a larger contribution than mining, education, defence, agriculture and the individual manufacturing sectors.⁸

Open services matter

Services are key to economic performance at the national level and in international markets. Roughly 50 per cent of all services are now considered to be traded, thanks to advances in information and communications technology. Services play a critical role in economic growth due to the extensive role that they play as inputs into all other economic activities. Services now represent fully half of world trade when measured on a value-added basis.⁹

Services will be the next driver of growth in the Asian Pacific region. While the share of GDP generated by services is already relatively high in most developed economies (70% - 80%), in developing and some Asian economies it is much lower (40% - 60%).

Barriers to services are still high, especially in developing countries. Costs for trade in services are estimated to be two or even three times as high (in ad valorem terms) as the trade costs of goods due to these barriers. Barriers to services were cited as the top impediment to ability to trade in the Asia-Pacific, and as one of the top priorities for APEC to address, by respondents to the PECC State of Trade in the Region Report for 2015.¹⁰

Most FTAs of Asian economies have few commitments which advance liberalisation of services.

⁴ Source: World Bank, WITS, World Integrated Trade Solution, accessed August 2017 at <http://wits.worldbank.org/analyticaldata/evad/Country/AUS/Year/2011/Sector/All/group/Services#>

⁵ Deloitte Access Economics (2015) *The Connected Continent II: How digital technology is transforming the Australian economy.* <https://www2.deloitte.com/au/en/pages/economics/articles/connected-continent.html>

⁶ See <http://www.liveinvictoria.vic.gov.au/working-and-employment/victorian-industries/information-and-communications-technology#.WXkxFlUmUk>

⁷ See <https://www.austrade.gov.au/International/Buy/Australian-industry-capabilities/ICT>

⁸ <http://www.investinaustralia.com/industry/ict/ict-industry-australia>

⁹ See Stephenson, 'Benefits of Services Trade Liberalisation in the Asia-Pacific Region', Australian APEC Study Centre Currents Newsletter 2017 accessed at <https://www.rmit.edu.au/news/all-news/2017/local-news/benefits-of-services-trade-liberalisation>

¹⁰ *Ibid.*

Investment is a key driver of global growth

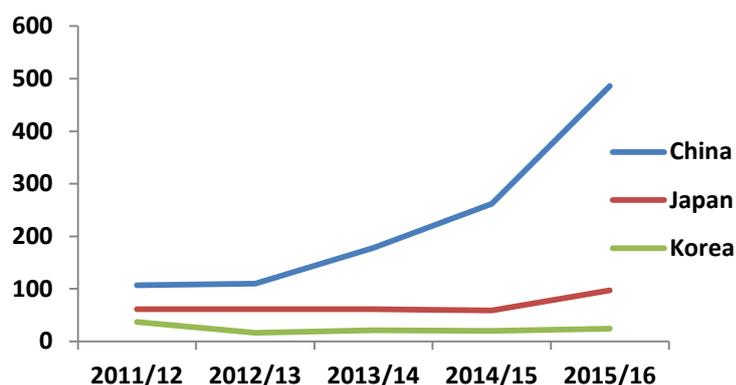
Investment is now a key driver of growth. Businesses are establishing operations in foreign markets rather than exporting. Equally, Australia depends on foreign investment to expand its ICT sector, including strategic investment by global ICT corporations such as IBM and Canon. Software and processes are built and adapted here and often rolled back into the global product development environment for use by customers worldwide.¹¹

But barriers are still high. Work by the OECD assessing the restrictiveness of policy on foreign direct investment shows that investment restrictions are higher on services (than on goods) and in many cases by a very significant amount.¹²

North Asian markets are important to Australia

ICT exports to North Asia are growing. There has been significant growth in ICT exports (goods and services) to China (85.5% growth 2014/15 – 2015/16) and Japan (64.4%) since conclusion of the FTAs. This is faster than growth in exports to major export markets (US, EU, NZ – 31.1%; 15.4%; 10.9% respectively), albeit off a much smaller base.

Australia's ICT exports (goods and services) to North Asian FTA partners (AUD million)



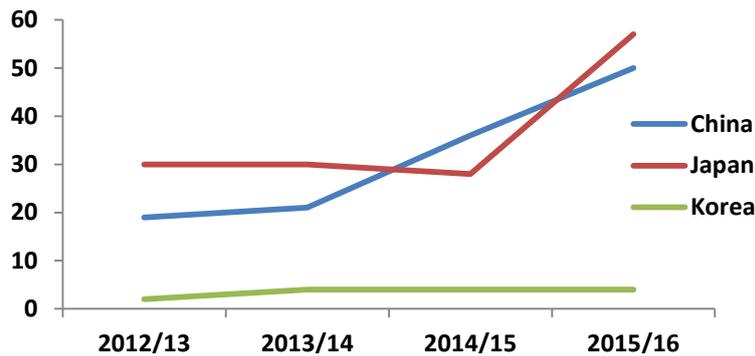
Source: DFAT, based on DFAT, ABS and unpublished data

ICT services exports to Japan and also China have grown since 2014 (103.6% and 38.9% respectively), but are still dwarfed by exports to US and EU in total value terms.

¹¹ See <http://www.investinaustralia.com/industry/ict/ict-industry-australia>

¹² See Note 9.

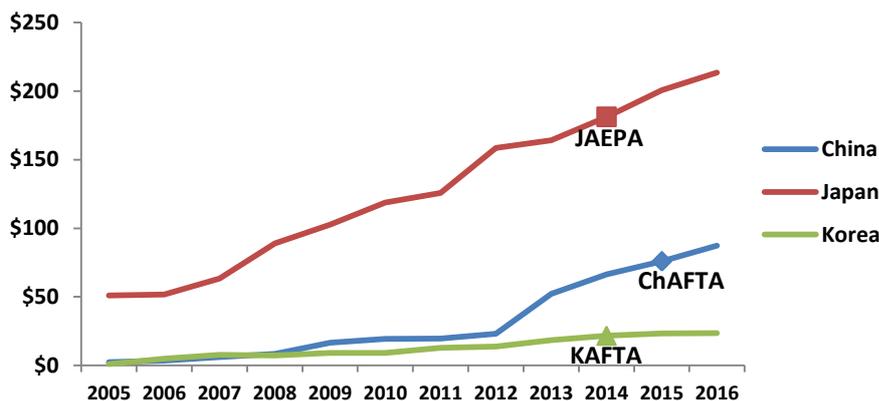
Australia's ICT exports (services) to North Asian FTA partners (AUD million)



Source: DFAT, based on DFAT, ABS and unpublished data

Investment from North Asia is increasing. Recent years have seen rising levels of investment from Japan and China in particular (though in value terms this is still dwarfed by investment from the US, UK and NZ).

Stock of investment in Australia from China, Japan, Korea, 2005-2016 (AUD million)



Source: ABS database

Policy agendas create growth opportunities

China, Japan and Korea all understand their economies need reform. The Trans Pacific Partnership (TPP) Agreement and bilateral FTAs have provided justification for domestic reform. China has triggered review of an APEC wide FTA.

China's domestic policy is also focused on reorienting the economy away from its reliance on infrastructure and manufacturing toward domestic consumption, services and technology. A core part of this is expanding investment in research and innovation. It is driven by a broader strategy to replicate Japan, South Korea and Taiwan's path to technology powerhouse success.¹³

¹³ <http://www.innovationaus.com/2015/07/ChAFTA-misses-ICT-opportunities/>

3. Opportunities for business – FTAs with Korea, Japan and China

i. Deliver commercial opportunities to expand trade

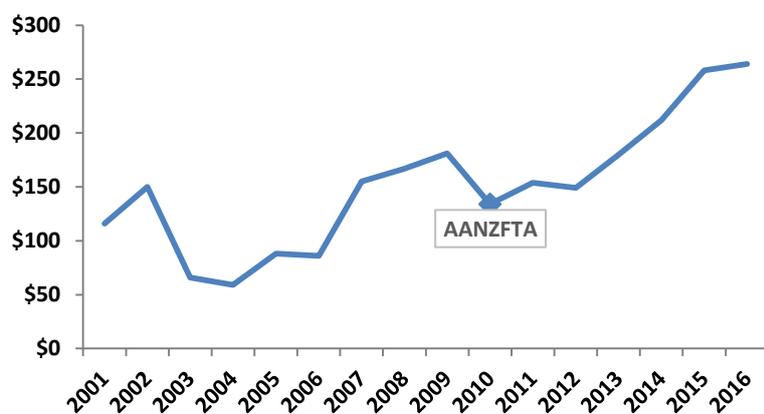
Business will benefit directly from greater market access. FTAs deliver new rights for Australian firms to establish and deliver ICT services in FTA markets. This also creates opportunities for Australian ICT subsidiaries to support other industry players, including education and health services, all of which are underpinned by ICT. See Annex 2 for examples.

There are indirect benefits from expanded trade. FTAs can be beneficial in facilitating trade and investment flows that create demand for more services activity. Businesses can leverage FTAs to create new opportunities to help expand services offered in the region for traders and investors. This is most notable for providers of services which are embodied in goods exports, particularly ICT.

There is evidence of expanded trade. FTAs have coincided with rising cross border services exports to FTA markets. For example, Australia's ICT services exports to ASEAN member states accelerated following the ratification of AANZFTA in 2010, almost doubling from AUD134 million in 2010 to AUD264 million in 2016.

ICT exports to North Asian partners have also grown significantly since the FTAs were concluded (14.3% over the last 5 years, and about 12% between 14/15 and 15/16.¹⁴ But it is still early days.

Australia's Cross-border ICT services exports to ASEAN member states (AUD million)



Source: ABS 5368.0.55.004 (AUD millions)

The 'real' value of ICT in trade is understated. Reported trade flows do not include ICT services which are embodied in other services and goods (e.g.: ICT design, development in delivery of other services such as financial, professional, health and in traded goods such as electrical and electronic equipment).

¹⁴ This is faster than all services as an average which grew at 6.3% and 9% respectively. Source: DFAT. Based on OECD definition, ABS and DFAT data 2015/16.

ii. Improve the business operating environment

FTAs can positively alter the regulatory landscape and improve business to business links. All agreements include provisions to support transparency in regulation and decision making. There are specific provisions to address anti-competitive practices and ensure transparency in telecoms regulation, digital products and e-commerce.

Enhance protection of intellectual property rights. Intellectual property (IP) provisions in the FTAs generally guarantee international treaty protections under the WTO TRIPS Agreement and various IP treaties. However, under ChAFTA China has given certain assurances covering respect for intellectual property, including agreeing to make its IP databases publicly available on the internet.

Facilitate temporary movement of people. All agreements provide temporary entry for business and qualified personnel to FTA markets. There are specific access commitments for qualified ICT professionals.

Australia has granted access for lower skilled workers in Australia¹⁵ and in some cases agreed not to apply labour market testing. These provisions are designed to assist business by addressing skill shortages in the Australian market.

See Annex 2 for examples.

iii. Expand investments in FTA markets

FTAs enhance legal protection of Australian investments. Enforceable legal protections strengthen the security of investments in FTA markets (e.g.: protection from expropriation). In KAFTA, private investors can enforce these rights through international arbitration under the investor state dispute settlement mechanism (ISDS). There is no ISDS available in JAEPA. Australia and Japan have agreed to consider its inclusion in the future.

Outward investment in ICT is growing. Australian FDI in information and communications industries abroad (including FTA partners) was AUD3.46 billion in 2015, up 44.8% from 2014. But it comprises only a tiny share of total FDI abroad in services industries (0.6%).¹⁶

iv. Encourage foreign investment in Australia

Direct investment opportunities in Australia from North Asia will become more attractive. The FTAs quadruple the Foreign Investment Review Board's screening threshold for investments from Korea, Japan and China in non-sensitive sectors (from AUD252 million to AUD 1,094 million.)¹⁷ This is equivalent to treatment given to the US and New Zealand under previous trade agreements.

FTAs can enhance perceptions of Australia as an investment destination –'head turn' effect. There is some evidence to suggest that FTAs have raised the profile of Australia and Australian companies in FTA markets. This is particularly so for Korea, where the investment and services trade relationship is not longstanding. This can support greater investment in Australia.

¹⁵ Investment Facilitation Arrangements (IFA) permits Chinese-owned companies registered in Australia undertaking large infrastructure development projects above \$150 million to negotiate increased labour flexibilities for specific projects.

¹⁶ DFAT, *International Trade in Services 2015-16*.

¹⁷ The FIRB will continue to screen all direct investments, new business proposals and acquisitions of interests in land (including agricultural land), by Chinese state-owned enterprises, regardless of transaction size. ChAFTA does not change these arrangements.

v. Promote economic reform in FTA markets

FTAs set 'standards' for more open services markets. Over the longer term, the creation of binding legal commitments for liberalisation will help set 'standards' to support more competitive services in the region. It is important in current times of increased protectionism and uncertainty in global trade.

4. Securing opportunities

While it is governments that negotiate FTAs, it is business that trades and invests. FTAs can provide commercial opportunities, but the benefits must be realised by business.

The impact is limited. Why?

- It takes time for the impacts of regulatory changes to be factored into business decisions. The North Asian FTAs are relatively new – in many cases it is too early to gauge significant impacts.
- Second, the 'benefits' are difficult to measure. Gains from services trade are particularly complex, not readily quantifiable and tend to be 'dynamic' throughout the economy.
- Furthermore, other issues which are beyond the scope of FTAs do and will continue to impact on business (e.g.: cultural and language barriers, data privacy regulation and censorship etc).

What can FTAs do? FTAs as 'living agreements.'

- **Improve outcomes for business over time.** FTAs have built in mechanisms to facilitate improvements in market access over time. There is evidence this is occurring with the Australia/Singapore Free Trade Agreement (SAFTA). ChAFTA includes a commitment to review services and investment chapters. Both governments have recently (March 2017) agreed to begin this process. In this respect, ChAFTA provides a starting point for a new process of services liberalisation with China.
- **Establish a platform to address and reduce barriers.** Various committees are set up by the agreements which are tasked with bringing regulators together to monitor implementation of the agreement and discuss any trade concerns. The agreements also set out various areas for future cooperation, electronic commerce regulation, for example.
- **Spread the benefits of liberalisation.** The FTAs include a Most Favoured Nation (MFN) clause which means that Australia will receive the benefit of any future liberalisation commitments Korea, Japan or China¹⁸ makes in subsequent FTAs.

But domestic policy is a stronger driver of regulatory reform than FTAs. The majority of the potential gains to be derived from structural reform in services will be realized from unilateral action rather than FTAs. For all APEC economies, more than 60 percent of the gains derive from their own reforms rather than those of others.¹⁹

¹⁸ The MFN clause is more limited in the case of China but applies to computer and related services.

¹⁹ See Philippa Dee, *Priorities and Pathways in Services Reform*, Part I: Quantitative Studies, Singapore: World Scientific Publishing Company, 2013, extracted in Stephenson, 'Benefits of Services Trade Liberalisation in the Asia-Pacific Region', Australian APEC Study Centre Currents Newsletter 2017 accessed at <https://www.rmit.edu.au/news/all-news/2017/local-news/benefits-of-services-trade-liberalisation>.

Annex 1- The ICT services sector

What are ICT goods and services? (OECD definition)

ICT manufacturing industries

- Manufacture of electronic components and boards; computers and peripheral equipment; communication equipment; consumer electronics; magnetic and optical media.

ICT trade industries

- Wholesale of computers, computer peripheral equipment and software; electronic and telecommunications equipment and parts.

ICT services industries

- Software publishing;
- Telecommunications, including wired telecommunications activities; wireless telecommunications; activities; satellite telecommunications activities; other telecommunications activities;
- Computer programming, consultancy and related activities;
- Data processing, hosting and related activities; web portals;
- Repair of computers and communication equipment.

Source: OECD (2007) *Information Economy. Sector Definitions Based on The International Standard Industry Classification (ISIC 4)*, Directorate For Science, Technology And Industry, Working Party On Indicators for the Information Society, DSTI/ICCP/List (2006)2/FINAL

The Australian ICT services sector

The Australian ICT sector remains diverse and fragmented. Large players (mostly multi-national, excluding the carriers) generate the bulk of revenues while it is the smaller companies (mostly domestic) who are innovators and exporters.

The industry encompasses a broad (and becoming broader) product spectrum from software and media content providers to electronics manufacturers. Telecommunications generates more than 40% of the industry's revenues.

Larger companies are present in the Australian market for product development (R&D) facilities, content development, technical assistance centres and global sourcing of skilled analysts. Key players include Acer Computer Australia; Alcatel Australia; APCS IT; Canon; CSC; Datacom; EDS; EMC; Hewlett-Packard; IBM; InfoSys; Techex Communications; WestNet.

The sector is expanding:

- Creative digital industries generates revenue in excess of A\$23 billion;
- Software industry is worth A\$2.7 billion;
- Healthcare IT market estimated at \$1.20 billion (estimated market value of \$2.21 billion by 2020);
- EMS generates more than A\$600 million a year of mining related revenues, more than A\$240 million of exports;
- Edtech market is expected to grow to A\$1.7 billion by 2022.

Source: InvestinAustralia (www.investinaustralia.com); Austrade (www.austrade.gov.au)

Annex 2- Examples of commitments relevant to ICT in Australia’s North Asian FTAs

Opportunity	Commitment/right	FTA example
Establish and operate in FTA markets more freely	Rights to establish in FTA markets to deliver services	ChAFTA: Wholly Australian-owned enterprises can: <ul style="list-style-type: none"> establish and supply value-added telecommunications services in the Shanghai Free Trade Zone (domestic multi-party communication services, application store services, store and forward services, and call-centre services); establish and deliver software implementation and research and development services in China establish joint ventures (up to 55%) to undertake on-line data and transaction processing services (for profit e commerce). Must be registered in SHFTZ and have facilities located there.
	Freedom to invest	KAFTA: <ul style="list-style-type: none"> Australian telecommunications providers can own up to 100% of the voting shares of a facilities-based telecommunications service supplier in Korea, and be licensed to provide public telecommunications.
	Improved conditions for distribution of Australian product	KAFTA: <ul style="list-style-type: none"> Audiovisual Co-production Annex sets out principles for the approval of co-production arrangements (films, animation, broadcasting, digital format production) and accords approved productions in the other party the same rights accorded to national productions (as permitted under laws). It also permits temporary stay for nationals for the purpose of co productions, subject to some requirements.
Deliver services from Australia (cross border trade)	WTO rights guaranteed	ChAFTA: <ul style="list-style-type: none"> Australian firms can supply a range ICT services from Australia - computer and related services, software implementation, data processing, input preparation, data processing, and time-sharing services.
Ease burdens/impediments to doing business	Licensing and registration	ChAFTA: <ul style="list-style-type: none"> China will ensure telecoms licensing requirements are not overly trade restrictive; provide advance notification of regulatory decisions and consult with Australian industry participants in China.
	Freedom of data transfer	All FTAs: <ul style="list-style-type: none"> Freedom of international transfers and payments for current transactions relating to trade in services.
	Treatment of E-commerce	JAPEA: <ul style="list-style-type: none"> Non-discriminatory treatment of digital products and regulation of electronic commerce (covering electronic signatures, online customer protection, paperless trading etc).
Enhance certainty of business environment	Transparency	ChAFTA <ul style="list-style-type: none"> China will ensure publication of laws and regulations and notify changes in laws and rulings affecting electronic commerce.
	Investment	JAPEA: <ul style="list-style-type: none"> Japan will not to make prior notification requirements for telecoms investments under the Foreign Exchange and Foreign Trade Law more restrictive in future.

	Intellectual property	<p>ChAFTA: China will:</p> <ul style="list-style-type: none"> • make its IP databases publicly available on the internet (including for patents, utility models, industrial design, plant variety protection, geographical indications and trademarks) • provide opportunities to address Chinese IP protection which may have been inappropriately granted to trade mark squatters and copycat products.
	Dispute resolution	<p>KAFTA:</p> <ul style="list-style-type: none"> • Australian investors in Korea can enforce FTA rights through international arbitration under the investor state dispute settlement mechanism (ISDS). • Recourse to a telecommunications regulatory body and judicial review of determinations for resolution of telecommunications disputes in Korea.
Ease movement of people and skills across borders	Temporary movement of personnel	<p>All FTAs:</p> <ul style="list-style-type: none"> • Entry commitments for services providers, spouses and dependents in all FTAs. <p>ChAFTA:</p> <ul style="list-style-type: none"> • Specific entry commitments for qualified ICT professionals in China (computer services personnel, engineers and consultancy services related to the installation of computer hardware; software R&D-based implementation services; data management services and data system services). • Access for lower skilled workers in Australia (e.g.: 457 Visas, IFAs).
Create frameworks to address barriers to trade	Committees	<p>ChAFTA:</p> <ul style="list-style-type: none"> • Committee on Intellectual Property provides a framework for raising intellectual property rights issues of interest to private stakeholders, discussed at request of either Australia or China. <p>All FTAs:</p> <ul style="list-style-type: none"> • Trade in Services Committee established • (Sub) Committees on Telecommunications in KAFTA and JAEPA.
Mechanisms to improve outcomes over time	MFN clauses	<p>KAFTA and JAEPA</p> <ul style="list-style-type: none"> • Most Favoured Nation (MFN) clause means that Australia will receive the benefit of any future liberalisation commitments Korea or Japan makes in subsequent FTAs. • KAFTA includes a 'ratchet mechanism' which prevents parties from imposing more restrictive measures in the future.
	Built in review mechanisms	<p>ChAFTA</p> <ul style="list-style-type: none"> • Built in work program to advance liberalisation of services and investment commitments. Agreement in March 2017 to commence review.