# Trade Opportunities for Mining Services - Australia's North Asian FTAs[1]

## Australia's FTAs – more than just tariffs

### *A core part of Australia's trade policy*

**Australia now has FTAs with almost all of its major trading partners**. More are on the way. Agreements with Korea, Japan and then China have followed those with first New Zealand, then Singapore, the US, Chile and ASEAN countries. An FTA with Peru has recently been concluded. Bilateral negotiations are underway with Indonesia, Hong Kong and potentially India and the EU. Progress is being made toward the Regional Comprehensive Partnership Agreement (RCEP- involving also New Zealand, ASEAN, India, Korea, China and Japan) and an FTA between Australia and Pacific Alliance countries (Mexico, Chile, Colombia and Peru). The Trans Pacific Partnership Agreement (TPP) was recently concluded (currently without US participation) and is expected to be signed next month.

Australia's North Asian bilateral FTAs are significant in that they are comprehensive agreements which build on existing frameworks to support open trade and investment. The TPP (when it enters into force) will be the most advanced trade agreement in the region. Though it does not include Korea or China, it is generally viewed as a precursor to an eventual APEC-wide FTA, covering all APEC economies.

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, e-commerce, temporary movement, etc. KAFTA is modelled on the Australia/United States Free Trade Agreement (AUSFTA) and the Trans Pacific Partnership Agreement (TPP). It entered into force in December 2014.

**Japan Australia Economic Partnership Agreement (JAEPA)**

JAEPA is the first comprehensive and significant bilateral agreement Japan has negotiated. 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 in a meaningful way. 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*

**Australia's recent FTAs 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.

[1] Material prepared for Briefing: *Trade Opportunities for the Australian Mining Services Sector,* Australian APEC Study Centre, RMIT University, 19 February 2018, Kristen Bondietti, Principal Trade Consultant, ITS Global www.itsglobal.net

**Regulation of services and investment in FTAs is different to goods.** 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 in foreign (and home) markets.

These changes arise from legal commitments in the agreements. Governments agree to treat regulation of services in ways which make it easier for foreign providers to deliver them, either across borders from their home market or in the market of the FTA partner.

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

## Why FTAs matter

### *Mining exports rely on services*

**Mining involves a broad range of economic activity encompassing both goods and services**. There are many services which are incidental to trade in mining products, for example engineering and project management, construction, research and technology, water and waste management, blasting and drilling, to name a few.

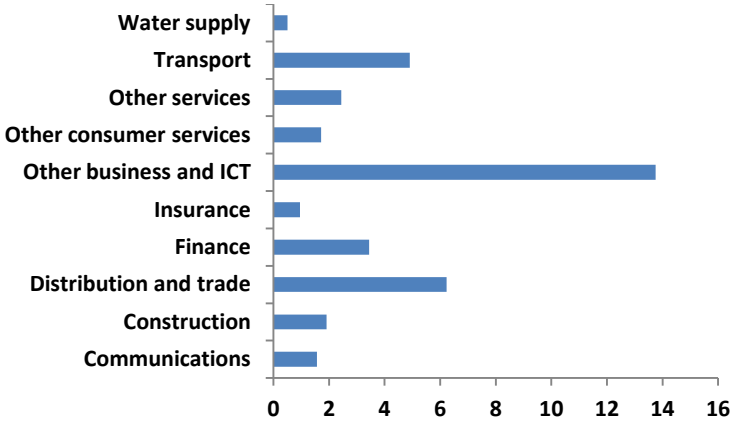
Mining Equipment and Technology Services (METS) provide a wide range of technology and services to mining companies across the mining and resources value chain (including transportation services, equipment manufacturing, project management, communication services, computer design systems and mining support services, and chemical manufacturing).[i] Over 60 percent of METS firms operate in both minerals and oil and gas sectors. Many services are 'embodied' in other traded mining services and products.

The boundary of the METS sector is constantly evolving, with new players entering from non-traditional sectors. For example, traditional oil and gas or defence services companies now provide key technologies and services to mining, and telecommunications providers have moved beyond communications to providing mining software and data services.[ii]

**METS are an important export industry in their own right.** The METS sector generates over $90 billion annually in revenue, employs around 400,000 people and exports to more than 200 countries. Over sixty percent of Australian METS companies export products and services, worth approximately $15 billion annually. The industry is seeking to grow exports in future.[iii]

The value of METS in mining exports is much more significant when METS embodied in traded goods and services are considered. Official export data does not account for the value-add component of METS to broader trade. The chart below illustrates the value-added contribution of services to Australian exports of goods and services, particularly ICT, transport and distribution.

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




*Source: World Bank, WITS, World Integrated Trade Solution*[iv]

**And an important source foreign investment in Australia.** Foreign investment is important for the Australian minerals sector which is capital intensive due to the large scale and technologically advanced nature of mining and resources development projects. The sector relies on access to funds, technology, know-how and market links through foreign investment, in particular foreign direct investment (FDI).[v] In 2016, 39 percent of the total stock of FDI in Australia (or $310.6billion) was in the mining industry.[vi]

## *Open services matter*

**Services are key to economic performance at the national level and in international markets**. Roughly 50 percent of all services are now considered to be traded. 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.[vii]

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%).

## *Investment is a key driver of growth*

**Investment is now a key driver of growth**. Businesses are establishing operations in foreign markets as well as exporting. In 2015 over half of exporting METS businesses had offices or operations offshore.[viii]

Equally, Australia depends on foreign investment to expand its mining sector and grow exports. FDI in the mining sector is significant and growing. FDI flows in mining grew by more than 18% over 2015-2016, with levels rising by 6 percent to over $300 billion.[ix]

In addition to providing an additional source of capital funds, foreign direct investment also benefits the Australian mining and METS sector as an important mechanism through which new technologies, equipment and knowledge can be transferred between jurisdictions.[x]

## *But barriers are high*

**Barriers to services and investment 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 are cited as the top impediment to ability to trade in the Asia-Pacific and as one of the top priorities for APEC to address.[xi]

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.[xii]

**Barriers impact on the mining industry**. Regulatory requirements cover all stages of mining activity (from grant of tenure, exploration, extraction, processing, transport and mine closure through to relinquishment of tenure) and impact on the wide range of METS delivered (e.g.: engineering, construction, accounting, legal and computing services). They include for example, limits on equity participation, controls on service delivery in foreign markets, recognition of professional and vocational qualifications, and movement of people. Their wide nature reflects the multidisciplinary nature of the METS industry.[xiii]

Most FTAs of Asian economies have few commitments which advance liberalisation of these barriers. Regulatory controls still impede business. China is identified by the METS industry as a difficult country in which to do business.[xiv]

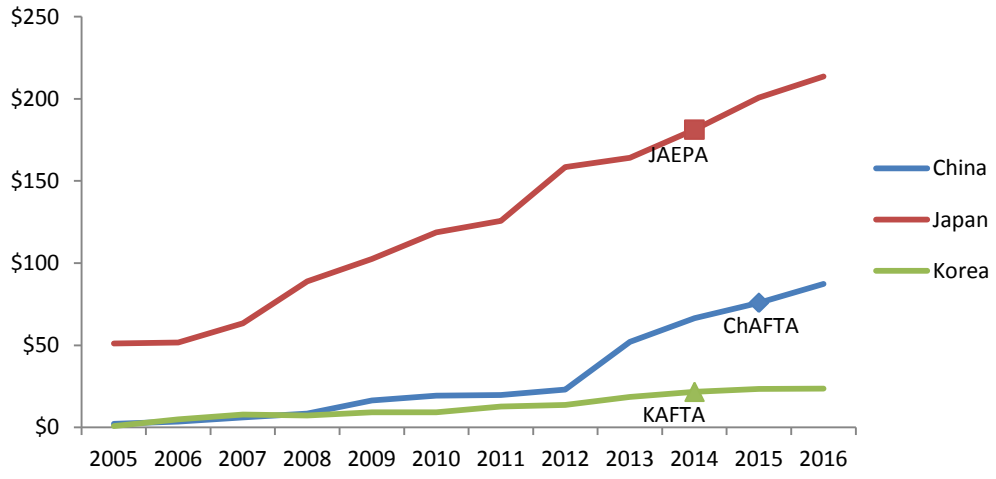
## *North Asian markets are important to Australian mining*

**North Asia is a major export market for Australian energy and minerals.** China, Japan, Korea are Australia's top three export destinations for minerals and energy exports. In 2016-17 exports to China were worth $78.1 billion, followed by Japan ($35.5 billion) Korea ($16.1 billion) and then India ($10.9 billion).[xv]

**It is a growing services export destination**. North Asia is an important and growing market for METS exporters. In a 2015 Austmine survey, 23 percent of companies identified North East Asia as a key market. In Australia's International Business Survey 2015, respondents ranked China as within the top five global markets for METS, and as one of the most important new markets. However, exports to North Asia still lag significantly behind other markets in Asia Pacific. Key export regions are South East Asia and South and North America.[xvi]

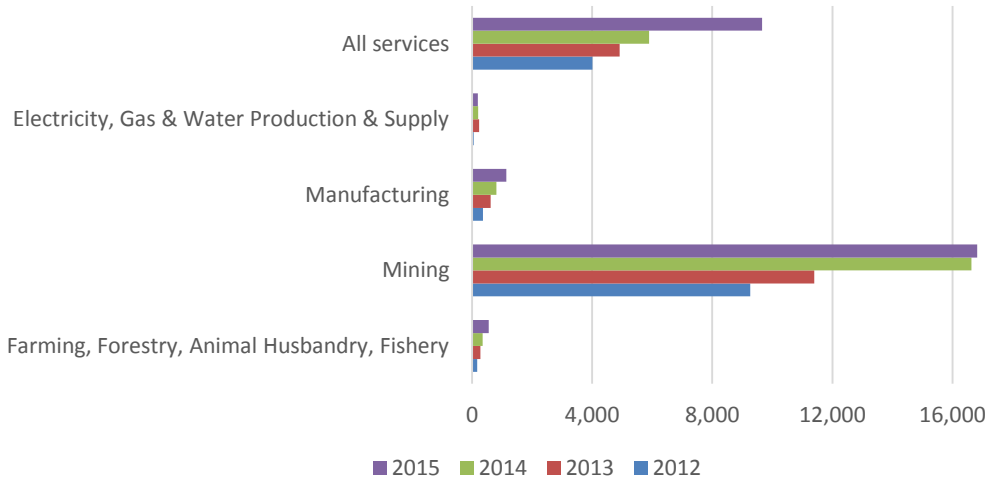
**And an important source of foreign investment**. Recent years have seen rising levels of investment to Australia from Japan and China in particular (though in value terms this is still dwarfed by investment from the US, UK and NZ). In 2015-16, China was also the largest source of foreign investment approvals (put to the FIRB) by both value and number, with $1.5billion of investment in mineral exploration and development approved.[xvii]

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




*Source: ABS database*

Stock of Chinese investment in Australia by sector, 2012-2015 (US$ million)




*Source: CEIC 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 in FTA markets. 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. All of these factors present opportunities for more open services markets, and increased business activity in future.

## Opportunities for business – FTAs with Korea, Japan and China

### *Deliver commercial opportunities to expand trade*

**Business will benefit directly from greater market access arising from FTAs.** The North Asian FTAs deliver new opportunities for Australian firms to export METS to FTA markets through granting of new legal rights, which improve upon previous access arrangements guaranteed under WTO.

For example, ChAFTA permits mining-related services (for oil and gas exploration) to be delivered through a commercial presence in China, in cooperation with Chinese partners. It allows Australian services suppliers to provide technical consulting and field services related to iron, copper, manganese, coal bed methane and shale gas exploitation.[xviii] Australian suppliers are also able to provide mineral resources exploitation services in the central and western regions of China.

China has guaranteed access to Australian companies established in the SFTZ that are undertaking joint construction projects with Chinese counterparts in Shanghai. Companies operate in the SFTZ in a more open environment which permits delivery of a wider range of projects.

Australian METS providers also benefit from Chinese commitments for environmental services. CHAFTA grants market access for waste disposal services by wholly Australian owned businesses, as well as environmental consultation services, which improve upon access China has granted in its previous FTAs.[xix] KAFTA similarly allows for Australian firms to deliver some environmental services on better terms than Korea permits under WTO (e.g.: for remediation services and waste disposal services).

**There are also indirect benefits from expanded trade**. Greater opportunities for METS exports can be expected to flow from expanded trade and investment in the minerals sector. FTAs can be beneficial in facilitating trade and investment flows that create demand for more services activity. METS businesses can leverage FTAs to create new opportunities to expand their services to traders and investors. This is particularly the case for providers of services which are embodied in mineral exports (e.g.: communications, design, accounting, engineering etc).

FTAs can also help strengthen commercial associations and increase the visibility of Australian services providers. This is particularly so in Korea where the trade relationship is not longstanding.

### *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 services regulation and decision making. For example, JAEPA has provisions to support transparency of regulatory measures affecting energy and mineral resources, for parties to exchange information on existing measures and provide prior consultation on proposed measures.

**Discipline behaviour of SOEs**. FTAs also now seek to discipline anti competitive behaviour of state owned enterprises in domestic services markets. JAEPA and CHAFTA both include disciplines on monopolies and exclusive service suppliers to ensure they act consistently with the agreement and don't abuse their position in the market.

**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. Under ChAFTA China has given certain assurances covering respect for intellectual property.

**Facilitate temporary movement of people.** All agreements provide for temporary entry of business and qualified personnel to FTA markets. The FTAs also include provisions or arrangements to encourage the mutual recognition of professional qualifications.

Australia has granted access for lower skilled workers in Australia 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.

Mechanisms to facilitate labour mobility

**Access to skilled workers** - JAEPA grants temporary entry for investors, contractual service suppliers, intra-corporate transferees, their spouses and dependents. Specific access of between 1-3 years is granted to qualified persons with specialised knowledge in engineering and accounting for example. Similarly, KAFTA provides for temporary entry of one year for some highly skilled workers in certain professions, including some engineering services (e.g.: data systems services).

**Recognition of professional qualifications** - A Professional Services Working Group is established under KAFTA to encourage mutual recognition in certain sectors, including engineering.Since the inception of the agreement, Engineers Australia has concluded an MRA with the Korean Ministry of Science, ICT and Future Planning to facilitate greater mobility of engineering professionals between the two countries.

**Address labour shortages** - CHAFTA Investment Facilitation Arrangements (IFA) permit Chinese-owned companies registered in Australia undertaking large infrastructure development projects above $150 million to negotiate increased labour flexibilities for specific projects.

## *Expand investments in FTA markets*

**FTAs enhance legal protection of Australian investments.** Enforceable legal protections strengthen the certainty and 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), and also in China (though in more limited circumstances).[xx] There is no ISDS available in JAEPA. Australia and Japan have agreed to consider its inclusion in the future.

Additional protections for investors and better access to North Asian services sectors, combined with increased visibility of Australian business, may encourage increased Australian direct investment in these markets from their current low levels.

## *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.)[xxi] This is equivalent to treatment given to the US and New Zealand under previous trade agreements. It should create greater certainty for FTA partner investors and lead to more direct investment over time.

**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 also support greater investment in Australia.

### *Improve outcomes for business over time*

**FTAs establish a platform to address and reduce barriers**. Various committees are set up by the agreements which are tasked with bringing regulators together to address specific trade concerns. They also serve to strengthening government and business links, particularly where there is access for private sector involvement.

For example, JAEPA establishes a Sub Committee on Energy and Mineral Resources which serves as a consultation mechanism for dealing with trade issues that arise. The agreement also creates a Sub Committee on Technical Regulations and Standards which serves a similar function for technical barriers for goods trade, as a well as a Sub Committee on Trade in Services to consult and discuss services issues. Similar Committees are set up in KAFTA and ChAFTA. These institutions will be important going forward to address regulatory barriers.

**FTAs are 'living agreements.'** 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 begun this process. It provides a starting point for a new process of services and investment liberalisation with China.

**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 China[xxii] makes in subsequent FTAs. (e.g.: EU/Japan agreement).

### *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 even more important in current times of increased protectionism and uncertainty in global trade.

Demand for Australian resources and mining services will increase as Asia's economies grow and invest in infrastructure, resources and energy-intensive production activities and develop their own mining sectors.

## Securing opportunities

While it is governments that negotiate FTAs, it is business that trades and invests. FTAs can provide commercial opportunities, but they must be realised by business. Caution should be taken when trying to assess the benefits:

**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 barriers, market conditions).

**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.[xxiii]

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[i] Minerals Council of Australia, *New Frontiers South and East Asia*, Trading Nation, 2017.
[ii] CSIRO Futures, *Mining Equipment and Technology Services, A Roadmap for Unlocking Future Opportunities for Australia,* May 2017.
[iii] A survey conducted in 2015 by Austmine found that of the METS companies that are not currently exporting, 16% plan to export in the next 1-2 years. Austmine, *New Realities, Bigger Horizons: Australian Mining Equipment, Technology and Services (METS) National Survey, 2015.*
[iv] 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#
[v] Minerals Council of Australia , *Submission to Joint Standing Committee on Foreign Affairs, Defence and Trade, Trade Sub-Committee Inquiry into Australia's Trade & Investment Relationship with the United Kingdom*, March 2017.
[vi] DFAT, *International Investment Statistics 2017*.
[vii] 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
[viii] Austmine, *New Realities, Bigger Horizons: Australian Mining Equipment, Technology and Services (METS) National Survey,* 2015.
[ix] DFAT, *International Investment Statistics 2017*.
[x] Deloitte Access Economics. *Mining and METS: engines of economic growth and prosperity for Australians, 2017.*
[xi] See Note 8.
[xii] See Note 8.
[xiii] Minerals Council of Australia, *New Frontiers South and East Asia*, Trading Nation, 2017.
[xiv] A survey of METS businesses conducted by the Export Council of Australia found that 23% of respondents identified China as the most difficult country in which they currently do business. See *Australia's International Business Survey 2015: Industry Profile Report: Mining Equipment, Technology and Services*, 2016.
[xv] Department of Industry, Innovation and Science, Office of Chief Economist, *Resources and Energy Quarterly*, September 2017.
[xvi] Austmine, *New Realities, Bigger Horizons: Australian Mining Equipment, Technology and Services (METS) National Survey*, 2015.
[xvii] Investors from China received approval for a number of large value transactions included in the manufacturing, electricity and gas sector, for example TransGrid. While the value of approvals for Chinese investors did increase, it increased by less than 6 per cent since 2014-15. The US is second largest source country for foreign investment approvals by value and the largest investor in non-real estate transactions. See Foreign Investment Review Board, *Annual Report 2015 – 16*, 2017.
[xviii] WTO commitments are limited to petroleum exploitation, with commercial presence for onshore field services limited to cooperative arrangements with CNPC in designated areas approved by the Chinese government.
[xix] Excluding China's FTAs with Hong Kong, Macau and Taiwan.
[xx] The ISDS mechanism in CHAFTA applies only for breach of national treatment with respect to established investments.
[xxi] 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.
[xxii] The MFN clause is more limited in the case of China but applies to engineering services, construction, environmental services, scientific and technical services and computer and related services.
[xxiii] 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.