

February 2018

Free Trade Agreement Utilisation Study





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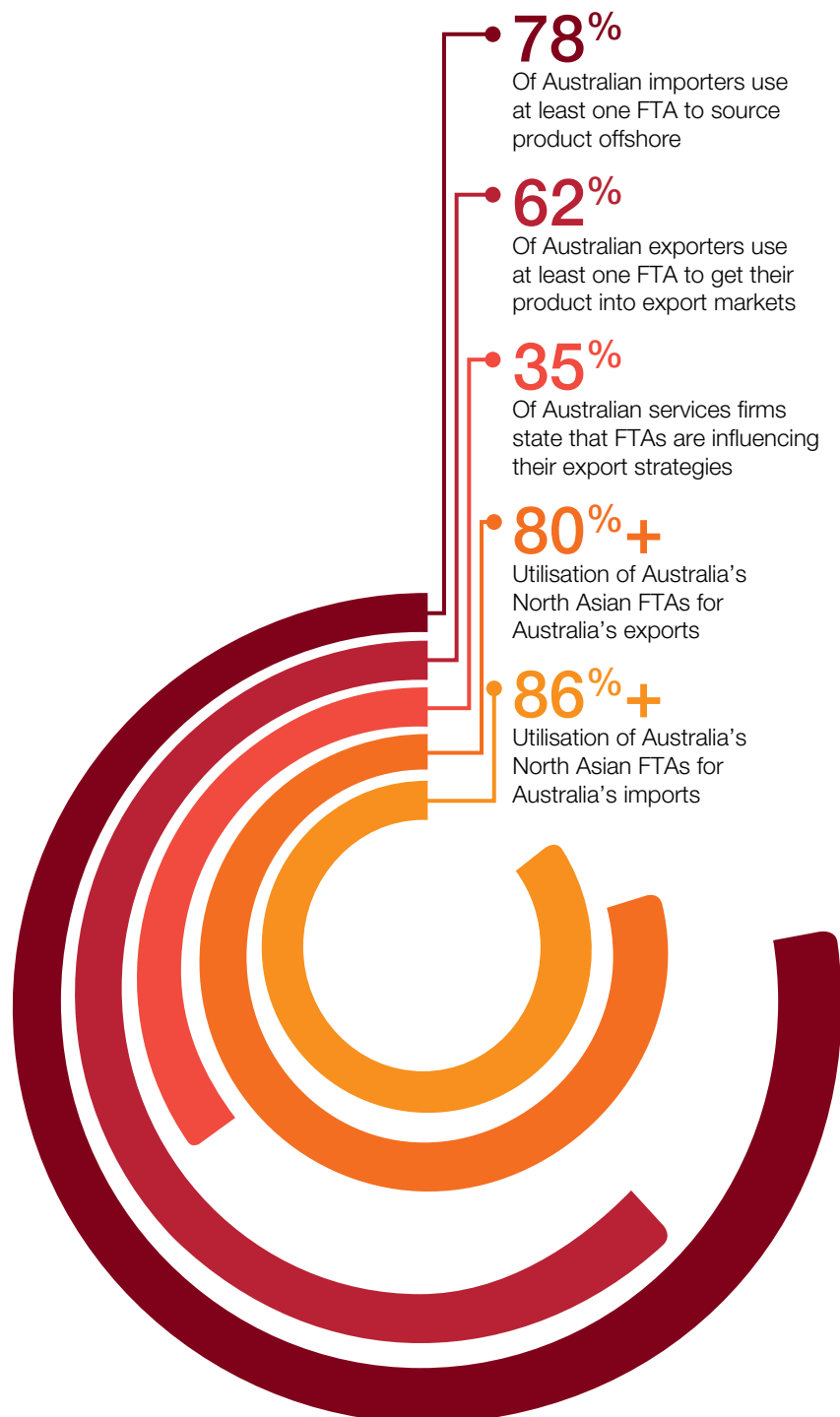
Executive summary

We asked Australian businesses to tell us their experience with using Australia's Free Trade Agreements (FTAs), particularly with the three North Asian countries. They did this through a series of focus group sessions, one-on-one in-depth interviews and an online business survey.

Our business survey received over 530 responses from businesses who interact with FTAs across trade in goods, services and investment.

The overall awareness of FTAs among the Australian business community is high. Businesses have been quick to take advantage of the benefits available from the North Asian FTAs (i.e. the FTAs with the People's Republic of China (China), the Republic of Korea (South Korea) and Japan) when buying and selling goods in these markets. The main benefits Australian businesses are enjoying from the North Asian FTAs are improved price competitiveness and lowered landed cost of goods.

The research found that:



Australia's FTAs with these leading economies in Asia are generally more advanced than their FTAs with other parties, and provide an important platform for further expansion of trade and investment between them and Australia.

Our research reveals that Australia's FTAs contribute to Australian business confidence and impact positively on business activity. There is evidence that businesses are integrating FTAs into their business processes and planning. Australian businesses engaged in trade are generally aware of FTAs and the agreements are being used to support their trade and investment activities across a range of sectors. To date, the greatest impact of Australia's FTAs has been in merchandise trade. Our research showed generally high two-way utilisation rates for Australia's FTAs across both imports and exports. FTAs are also contributing to the expansion of services trade and international investment, although the full benefits in these areas are yet to be realised (and these outcomes are harder to measure than goods outcomes). Early signs indicate that FTAs have promoted investment in Australia and the level of investment is increasing.

The effects of FTAs are also indirect. There are businesses reporting increases in domestic demand for goods and services from businesses trading internationally. Not surprisingly, small- and medium-sized enterprises (SMEs) lag behind larger businesses in FTA utilisation, and continued outreach and education is required for these businesses to maximise the opportunities available to them from Australia's FTAs.

The Australian Government, peak bodies and trade intermediaries all have a role in further broadening the uptake of FTAs. Government outreach efforts are contributing to raising understanding and utilisation of FTAs, and these efforts should continue and be reinforced by peak body education programs. Existing mechanisms within FTAs to review or renegotiate them are an important avenue to explore solutions identified around the origin of goods, compliance and regulatory barriers. These efforts should be informed by an ongoing agenda of research into FTA utilisation, particularly to monitor services and investment outcomes.

We have identified six principal findings from our research:

01 Australia's North Asian FTAs have high utilisation rates for merchandise trade.

Internationally-engaged Australian businesses are aware of the North Asian FTAs and view them favourably. Understandably, appreciation of the detailed requirements of FTAs, along with their applicability based on industry or product and the process for obtaining FTA preference, varied among businesses, especially at the SME level.

02

03 FTAs are influencing business activity, confidence, strategy, expansion planning and international investment, including in the services sector. However, they are not viewed as a silver bullet by industry, but are regarded as complementary to business strategy.

While FTAs provide greater regulatory certainty for Australian service providers and investors in partner markets, these commitments to liberalise services are still new territory for businesses. The full services market access outcomes of Australia's North Asian FTAs will take time to bear fruit, and will become evident over future years.

04

05 Options to optimise business utilisation of FTAs include streamlining origin documentation arrangements, reducing compliance costs, digitising forms, providing further education and advocacy (particularly for SMEs), and implementing measures to foster improved understanding of services and investment commitments in FTAs. Existing review mechanisms in FTAs could help to enhance and align their benefits.

Along with the Australian Government, industry associations and business groups play an important role in assisting businesses understand and utilise Australia's FTAs. Trade intermediaries also have an important role in assisting businesses to utilise FTAs effectively.

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About the research

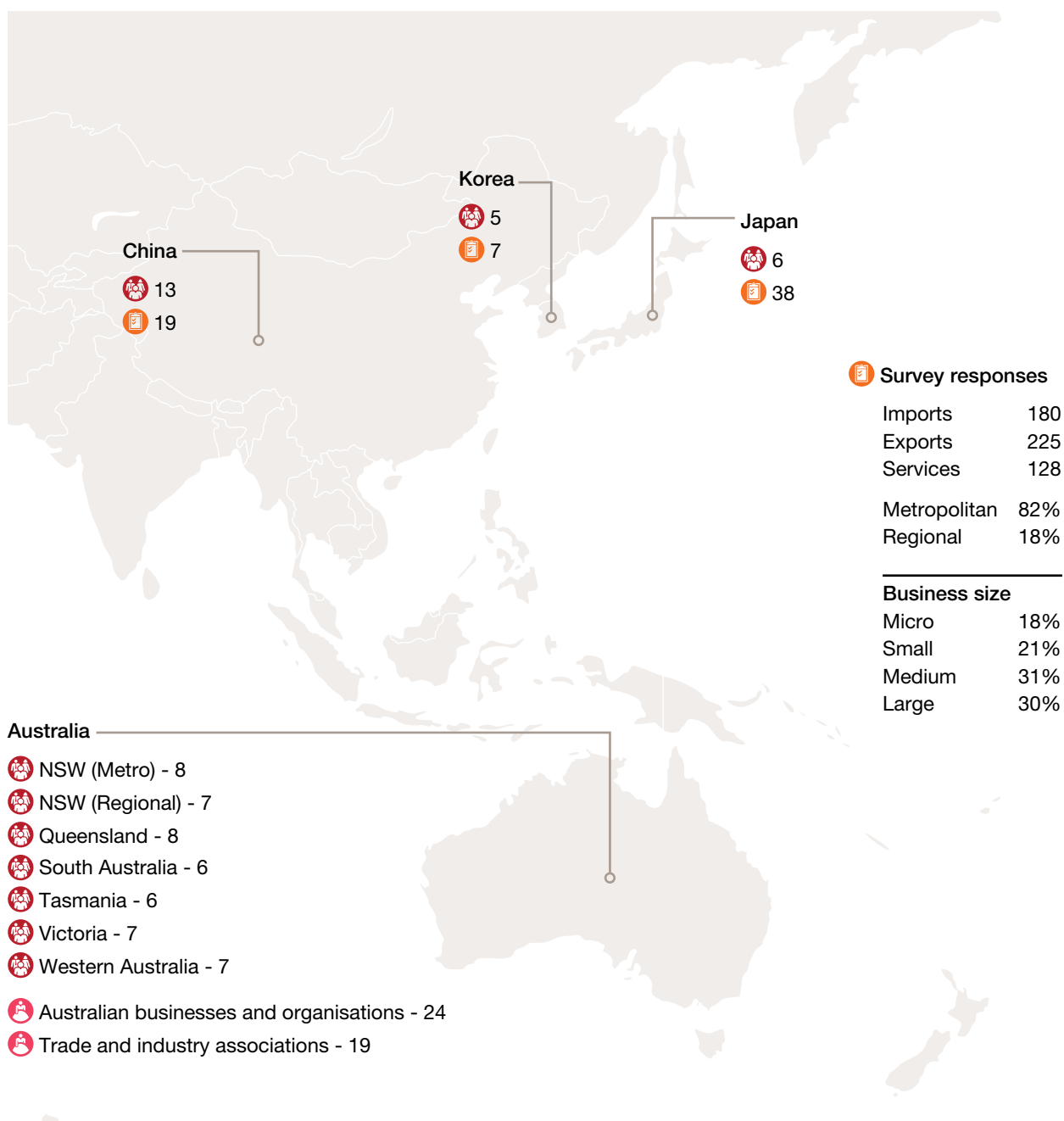
PricewaterhouseCoopers Australia (PwC) and our subcontractor, ITS Global, were engaged by DFAT to provide this independent FTA Utilisation Study. Our study aims to deliver analysis and findings that serve the needs of both DFAT and the Australian business community. This evidence base seeks to ensure trade policy and advocacy can continue to deliver benefits to Australian businesses. The findings of this report are based on a comprehensive literature review

– we also conducted interviews with 19 industry associations; focus groups in Australia, China, Japan and Korea; in-depth interviews; an online survey with a representative sample of Australian businesses; and an economic analysis of trade clearances data. The size and scale of the qualitative research undertaken (over the period April-July 2017) as part of this study is illustrated in the diagram below which shows the locations and number of participants involved.

Acknowledgements

We wish to thank the many individuals and businesses who contributed their time and countless insights to this research. Of particular mention is our research subcontractor ITS Global, and our independent reviewer Andrew Stoler.

Breakdown of our research



Legend



Focus groups



In-depth interviews



Survey

Glossary

AANZFTA	ASEAN–Australia–New Zealand Free Trade Agreement
ABS	Australian Bureau of Statistics
ACIFTA	Australia–Chile Free Trade Agreement
ASEAN	Association of Southeast Asian Nations
AUSTFA	Australia–United States Free Trade Agreement
Austrade	Australian Trade and Investment Commission
ChAFTA	China–Australia Free Trade Agreement
CoO	Certificate of Origin
DFAT	Department of Foreign Affairs and Trade
FDI	Foreign Direct Investment
FTA	Free Trade Agreement
JAEPA	Japan–Australia Economic Partnership Agreement
KAFTA	Korea–Australia Free Trade Agreement
MFN	Most Favoured Nation
MoP	Margin of Preference
MRA	Mutual Recognition Agreement
North Asian FTAs	Collectively, ChAFTA, KAFTA and JAEPA
NTB	Non-tariff Barriers
RoO	Rules of Origin
SAFTA	Singapore–Australia Free Trade Agreement
SME	Small and Medium Enterprises
Study	The PwC FTA Utilisation Study
TAFTA	Thailand–Australia Free Trade Agreement
TCO	Tariff Concession Order
US	United States of America
WTO	World Trade Organization

Overview of Australia's FTA network

Since Australia finalised its Free Trade Agreement (FTA) with New Zealand in 1983, the Australian Government has had an agenda of securing trade agreements with our key trading partners across the Asia-Pacific region. As of today, Australia has 10 FTAs (nine bilateral and one plurilateral) in force¹. Together they account for over 60 per cent of Australia's two-way trade.

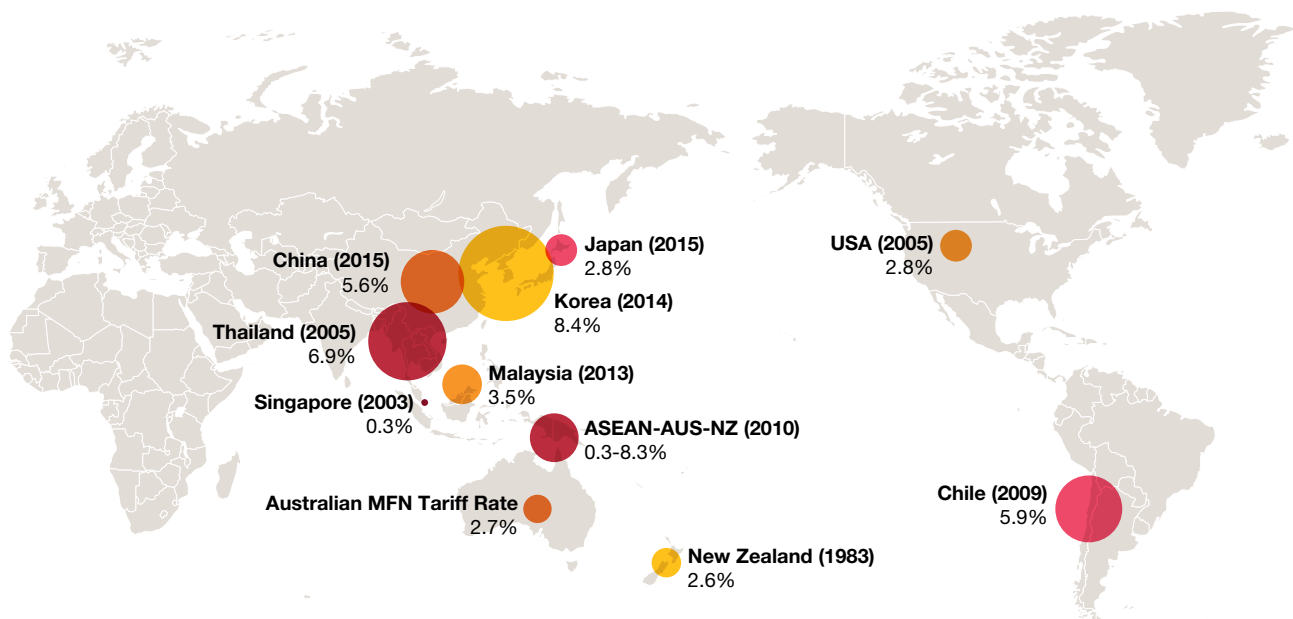
FTAs are negotiated by governments, often over many years. As well as being international

legal agreements they are the foundation of a cooperative economic partnership. FTAs include specific commitments to make trade and investment more open and can encourage and support trade when viewed as a reciprocal endorsement of each party as a preferred trading partner.

Commitments vary between FTAs and encompass a broad spectrum of issues, including tariff reductions (some immediate, others phased in over several years) across a broad range of goods and governed by

a set of qualifying tests known as 'Rules of Origin' (RoO). In particular, at least in respect of trade in goods, FTAs provide more access to the FTA partner countries than is accorded to countries outside of the FTA. Australia's FTAs also include commitments to improve market access for trade in services, foreign direct investment concessions, technical barriers to trade limitations, facilitate access to government procurement contracts, and other measures to foster trade and investment between the parties to the agreement.

Figure 1: Australia's in-force FTAs as of November 2017, including comparison of Most Favoured Nation (MFN) tariff rates*



*Weighted average global MFN tariff rate for the relevant country(ies) for 2015 (except for some countries in the Association of Southeast Asian Nations (ASEAN) where the most recent year of data available for the country is prior to 2015).

Source: Trade statistics information obtained from the World Integrated Trade Solution (WITS) TradeStat database developed by the World Bank (in collaboration and consultation with other organisations). WTO copyright of the original data is acknowledged.

¹ In addition, three other agreements have been signed but are not yet in force (Trans-Pacific Partnership (TPP); Pacific Agreement on Closer Economic Relations Plus (PACER Plus) and Peru-Australia Free Trade Agreement (PAFTA)) while eight others are under negotiation, as well as other sectoral agreements, such as the Trade in Services Agreement, that is also under negotiation.



Key findings from the research

Utilisation of Australia's FTAs

FTA utilisation was a principal focus of our research, particularly in relation to Australia's agreements with China, Korea and Japan. We assessed utilisation through an economic analysis of trade clearance data, and explored business perceptions of utilisation through an online survey, focus groups and in-depth interviews.

For the purposes of this study, the FTA utilisation rate is defined as, where the FTA offers a Margin of Preference (MoP)², the proportion of trade [in value or dollar terms] that enters under that FTA preference. These figures exclude trade under alternate mechanisms for tariff relief (including duty concessions, quotas and temporary tariffs).

In order to analyse utilisation rates of FTAs, we looked at awareness of FTAs, and why importers and exporters opt into FTAs. We found that Australian businesses are generally aware of FTAs and their requirements. We also found that the larger the MoP, the higher the utilisation of FTAs. This supports the proposition that businesses opt into FTAs where it makes commercial sense to do so and there is a clear cost benefit.

Figures 2 and 3 show FTA utilisation rates for Australia's two-way trade with North Asian and other selected FTA partner countries in 2016. Data for the United States, Chile and Thailand³ have been analysed to give a comparison with FTAs which have been in-force for a longer period.

Our qualitative and quantitative analysis shows that, while the uptake across all of Australia's FTAs is generally good for those that trade in goods, the results slide significantly across the small- and medium-sized enterprises, with only 55 per cent of SME exporters (compared to 77 per cent in large enterprises (i.e. those with greater than 200 employees)) and 40 per cent of SME importers (compared to 94 per cent in large enterprises) claiming the preferential rates of duty available under all Australian FTAs.

² The Margin of Preference (MoP) is the difference between the MFN tariff rate and the FTA tariff rate.

³ Chile and Thailand data for Figure 3 was not available.

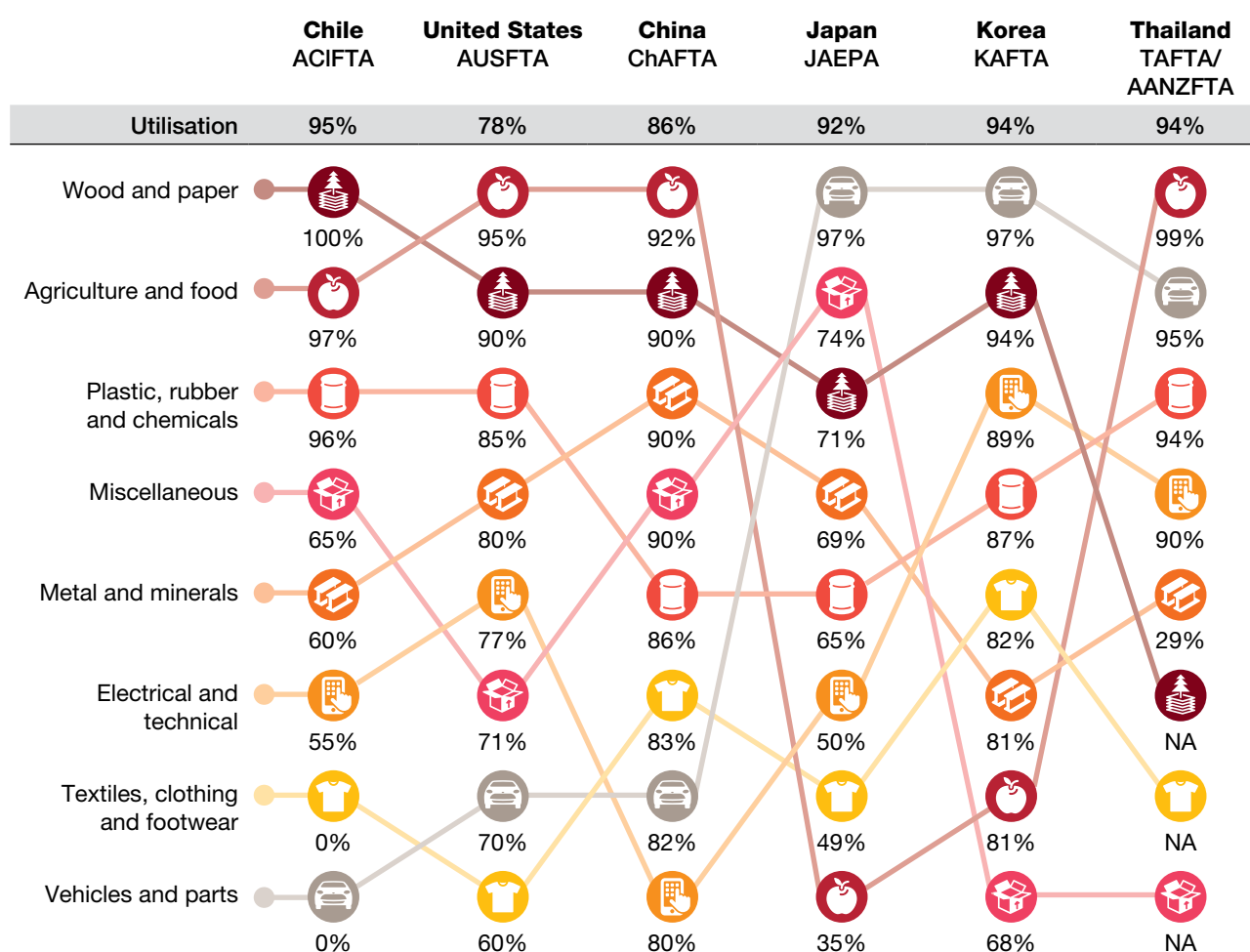
Australia's North Asian FTAs have high utilisation rates for merchandise trade.

In most cases, one or two key commodity groups have the majority of the impact on the total utilisation rates. Where one commodity group makes up the bulk of the dollar value of trade, it also has one of the highest FTA utilisations. This indicates that there may be some economies of scale in utilisation and, additionally, where trade was already commercially important, use of the FTA was by extension more commercially important. Further, a large percentage MoP on a tariff line

with a low dollar value of trade may not be as commercially important as a smaller percentage MoP on much higher value of trade.

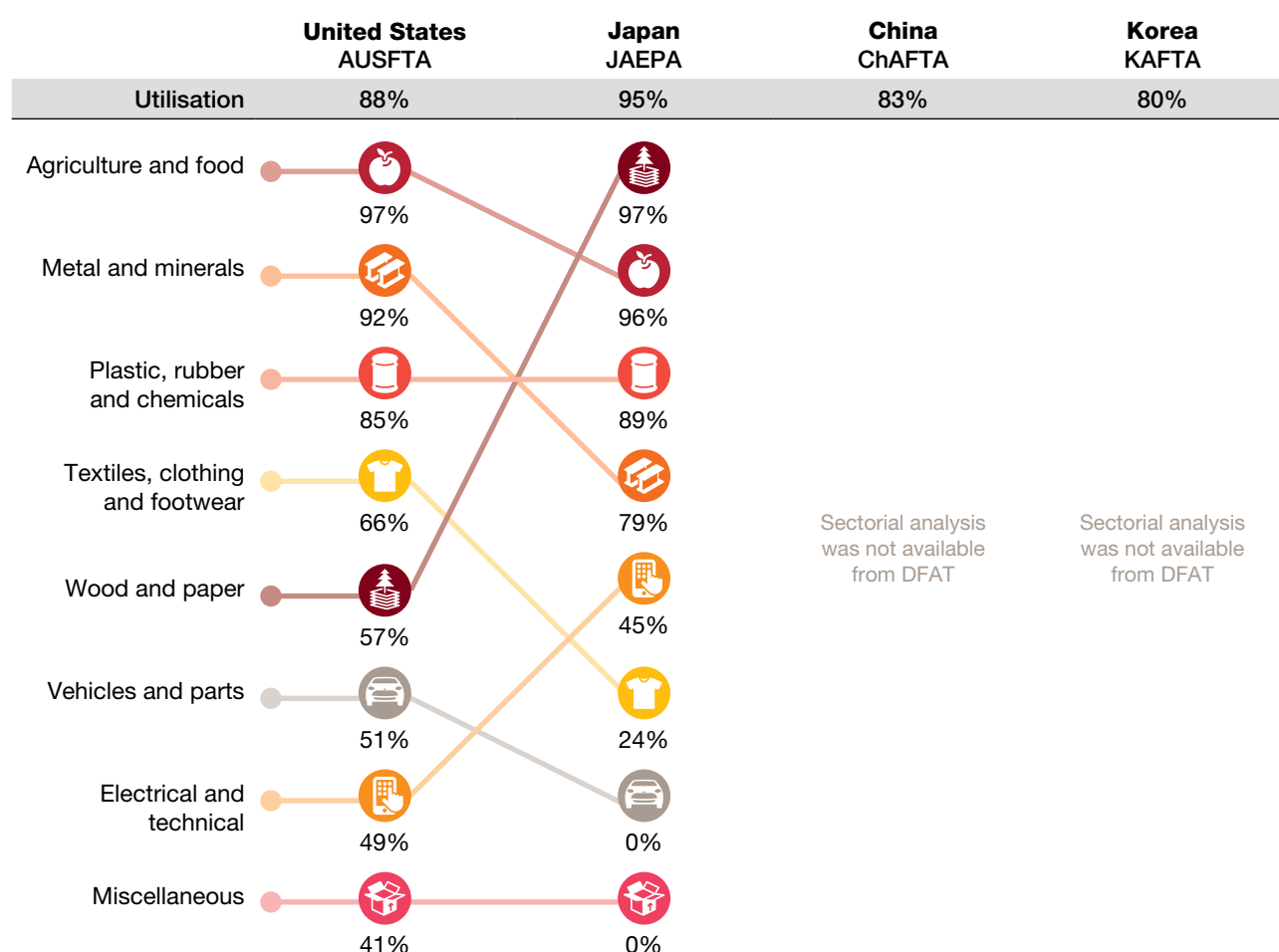
Figure 2 compares the FTA utilisation rates by product group for Australia's imports from the United States of America (US), China, Japan, Korea, Thailand and Chile while Figure 3 compares the FTA utilisation rates by product group for Australian goods imported into Japan and the US. Our analysis of FTA utilisation rates highlights that Australian importers and exporters are making use of FTAs, and ultimately accessing the benefits available.

Figure 2: FTA utilisation rates for imports into Australia, total and by product group, 2016



Source: PwC analysis using ABS Catalogue No. 5368.0 import clearance data (downloaded from the DFAT STARS database). Data provided by DFAT.

Note: Product groups ranked by FTA utilisation rate. Ranking on a value of trade basis may differ. Where 'n/a' indicates that the utilisation was not able to be calculated as the denominator of the equation is zero. This means that there are no applicable imports in that category with a MoP, or all imports in the category with a MoP enter under another preference.

Figure 3: FTA utilisation rates for Australian goods imported into other countries, total and by product group, 2016

Source: PwC analysis using data provided by DFAT and the World Bank Integrated Trade Solution, Official Statistics Japan and the United States International Trade Commission.

Note: Product groups ranked by FTA utilisation rate. Ranking on a value of trade basis may differ.

Our research also showed businesses often use alternative mechanisms for tariff relief (where they are available), although these decisions are likely made on a case-by-case basis, with factors including MoP, administrative and compliance costs, supply chain structure and efficiencies all considerations. For example, some 46 per cent of Australian exporters and 45 per cent of Australian importers viewed the fact that the goods had zero tariffs or were eligible for duty-free entry under a separate concession as significant to their decision not to use FTAs.

A high proportion of Australian importers and exporters (60 per cent and 53 per cent) who indicated they don't use FTAs said they preferred to use alternative duty relief measures (such as duty drawbacks, TCOs and other duty concessions) where available because they are generally less onerous, costly to comply with and have existed as industry assistance mechanisms for much longer than most FTAs. Importantly, there is a sizeable proportion of trade through these mechanisms accessing duty relief without the need to claim FTA preferences. For example:

An Australian focus session participant noted that it claimed some preferences under FTAs on imports into Australia, however this was a relatively small amount in comparison to the duty relief gained under TCOs.

Another participant stated that they did not claim any FTA preferences but instead used duty drawbacks as their main source of duty relief for imported inputs which were later processed in to finished products for export.

A focus group participant in the medical manufacturing industry noted that, although they traded extensively with FTA countries (including North Asian FTA partners), they did not use FTAs because their products were already duty-free in their export markets.

Ultimately, importing Australian businesses are in the advantageous position where they have a range of opportunities to seek customs duty relief, with FTAs making up a growing proportion of the mix.

Business perceptions and awareness of FTAs

Our research analysed the level of awareness of FTAs in the trading community. Through the in-depth interviews, we found that participants were highly aware of Australia's FTAs.

In terms of creating awareness, the survey found that 78 per cent of the Australian businesses that trade in goods obtain information on FTAs from more than one source.

The main sources from which Australian businesses obtain FTA information and advice are government websites, customs brokers or freight forwarders, and industry associations.

Our research found that the gap between business awareness of the existence of FTAs and their understanding of FTA requirements affects a business' ability to

use FTAs and is a key cause of sub-optimal utilisation. For example:

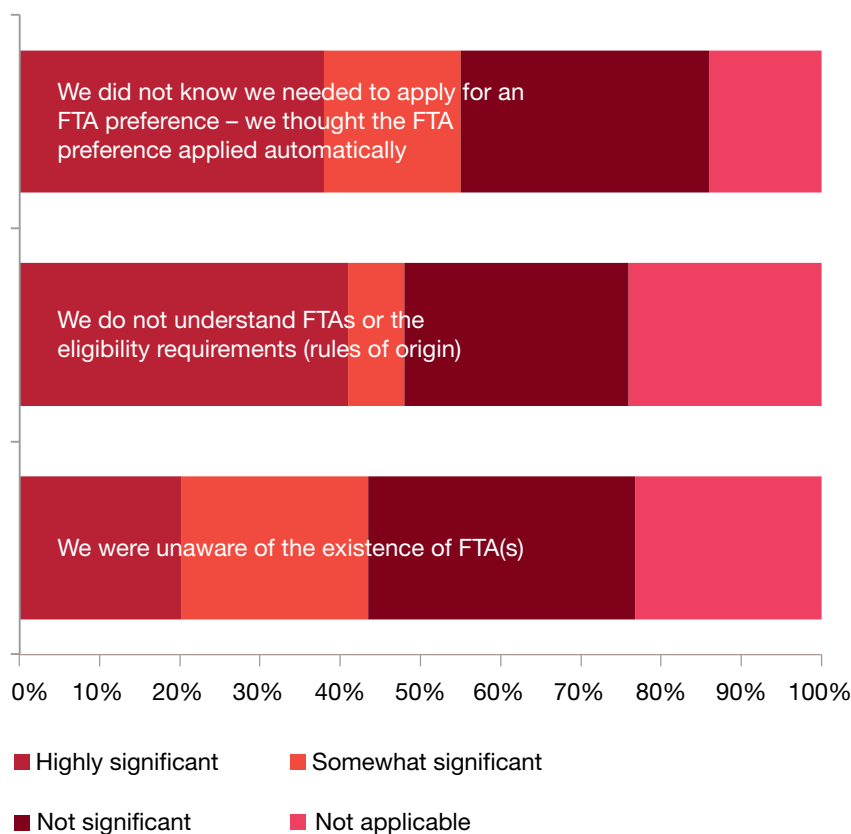
An Australian focus session participant in the retail and consumer industry noted that where they did not claim FTA preferences, one of the key factors was the supplier's lack of awareness.

In particular, when the China–Australia Free Trade Agreement (ChAFTA) was implemented, there were problems with suppliers and Chinese issuing agencies either not being aware of the need, or else not being ready to issue a Certificate of Origin (CoO) in order to meet FTA requirements. In another Australian focus group session, an exporter said “we thought that the FTA benefit was automatically applied and I would have expected my service provider to advise me that I required a CoO”.

As indicated in Figure 4, a lack of understanding of the technical requirements of FTAs may contribute to sub-optimal utilisation by Australian-importers.

Figure 4: Responses to survey question – How significant were the following factors in you not claiming reduced customs duties for goods imported into Australia?

Although internationally-engaged Australian businesses are generally aware of FTAs and view them favourably, an understanding of the detailed requirements of FTAs, along with their applicability based on industry or product, and the process for obtaining FTA preference, was not consistent among businesses.



Source: PwC FTA Business Survey.

From a trade in services perspective, specific knowledge and understanding of how FTAs impact services industry sectors and individual businesses is not widespread. We found that the level of awareness is generally highest among larger businesses with a regional Australian presence, but even these firms are sometimes unaware of the detail of FTAs. Previous research has found that awareness of bilateral FTAs is generally higher than for plurilateral FTAs, because it is clearer to businesses what concessions have been granted.

FTAs have also led to improved perceptions of Australia's business environment

An indirect benefit of FTAs is described variously as the 'head turning' or 'halo' effect; successful trade agreements with China, Japan and Korea have contributed to the positive perception of Australia as a place to invest and do business. This awareness can translate to greater interest on the part of firms and investors in FTA partner countries to explore Australian opportunities.

FTAs have raised the profile of Australia and Australian businesses in FTA markets, particularly in the financial, legal and education services industries. The agreements are also reported to have promoted interest in Australia as a place to invest.

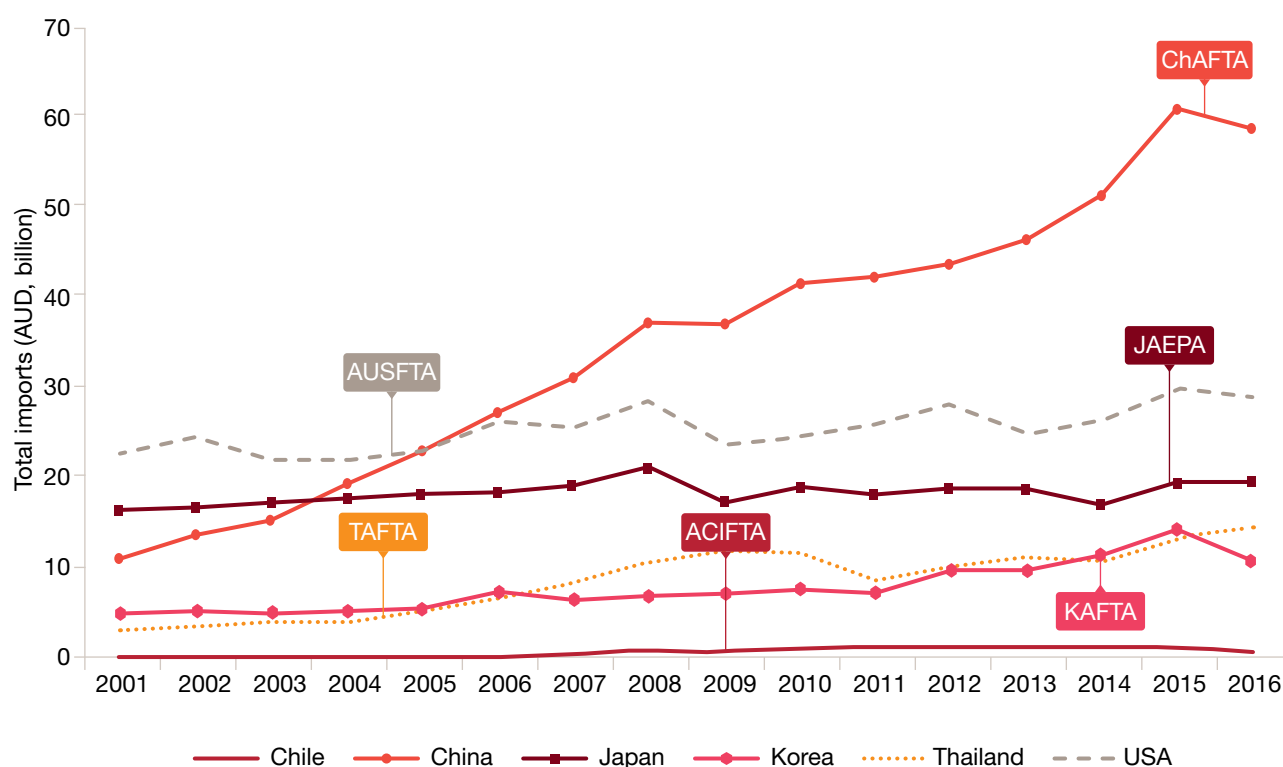
Impact on business activity and processes

FTAs are influencing business activity, confidence, strategy, expansion planning and international investment, including in the services sector. However, FTAs are not viewed as a 'silver bullet' by industry, with their impact being largely complementary to other commercial considerations.

Market engagement has improved between Australian businesses and their partners in FTA countries following the entry into force of Australia's FTAs. Higher usage of FTAs correlates with a strengthening trading relationship (and therefore likely relative increases in the levels of imports and exports, taking

global economic and trading conditions into account). The research demonstrated that FTAs have indirectly facilitated trade between Australia and FTA partner countries. Figure 5 shows the flow of goods imports into Australia from selected partners over the last 15 years (encompassing the introduction of the relevant FTAs). Across this period, Australia had a trend of increasing imports from all these partners. However, it is not possible to draw causation between the trade flows and the entry into force of the North Asian FTAs.

Figure 5: Australian goods imports from selected partners (2001-2016)



Similar to imports, Australia had a trend of increasing or steady exports to Chile, China, Japan, Korea, Thailand and the US; although we were unable to determine direct causation with the FTAs. However, for both imports and exports higher usage of FTAs is correlated with a strengthening trading relationship (and therefore likely relative increases in level of imports and exports, taking global economic and trading conditions into account).

Survey responses by Australian exporters indicated that utilising FTAs had resulted in sales to new customers in FTA markets or increased sales to existing customers. There was also some support for the idea that FTAs stimulated Australian exports to FTA markets, with 42 per cent of Australian exporters citing improved price competitiveness in export markets as a key outcome from utilising FTAs. Further, 33 per cent of Australian exporters indicated that utilising FTAs had resulted in sales to new customers in FTA markets while 31 per cent of Australian exporters indicated increased sales to existing customers.

Focus group participants who export goods were generally positive about the influence of FTAs, with 63 per cent of Australian participants indicating that they have exported greater quantities of products under the FTAs.

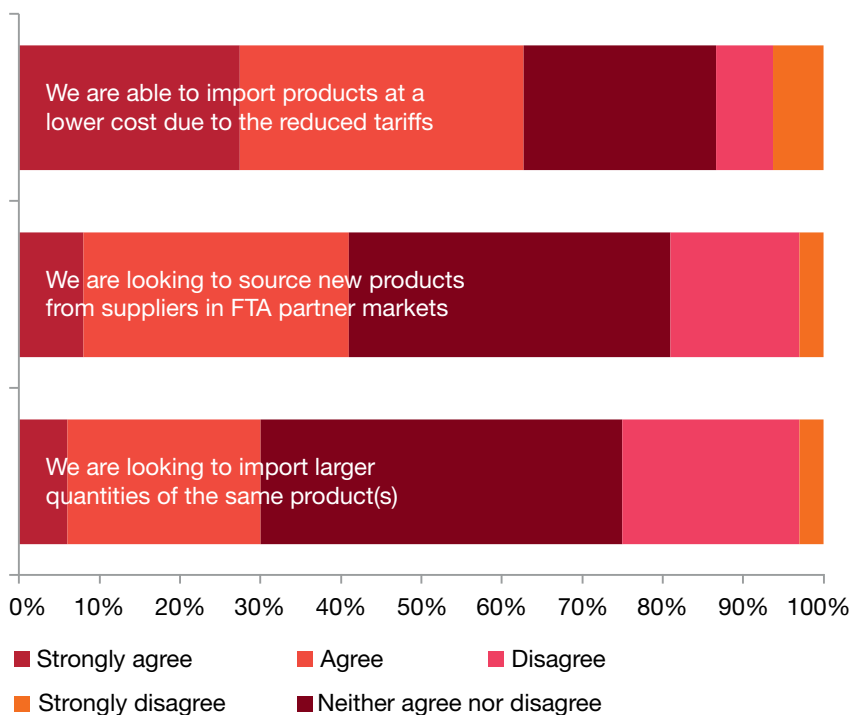
Reduction of tariffs

We found that the biggest impact FTAs have on importers' business activity is their ability to import products at a lower cost due to reduced tariffs. Results from the FTA Business Survey at Figure 6 show that 31 per cent of Australian respondents surveyed indicated they are looking to import larger volumes in the future, and 41 per cent of Australian respondents stated that they were looking to source new products from suppliers in FTA markets.

These results indicate that Australian businesses believe FTAs may facilitate an increase in the import of goods from FTA partners in the future. However, this is strongly affected by commercial considerations such as demand and supply chain planning.



Figure 6: Responses to survey question – How has utilising FTAs on your imports into Australia impacted your business strategy for the future?



Based on the business survey results (refer Figure 7), 29 percent of exporters indicated that reduced tariffs under FTAs have resulted in an increase in exports to FTA markets. However, 25 per cent of Australian exporters indicated that this was *not* the case, with the remaining respondents neither agreeing nor disagreeing. We got similar results when asking exporters to indicate whether they believed FTAs had resulted in their business exporting a wider range of products to FTA markets.

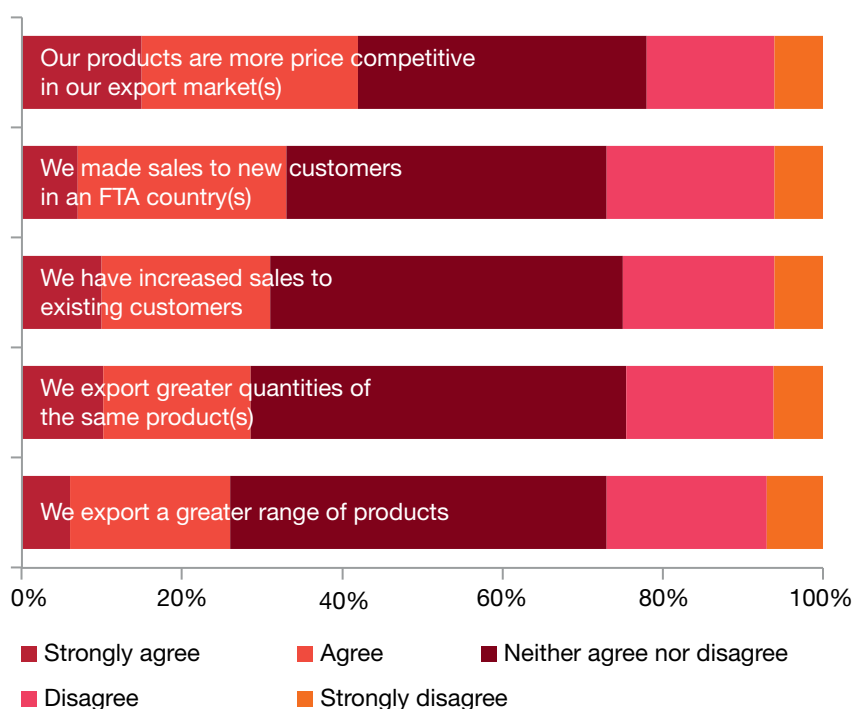
Business decisions and strategy

The research also found that FTAs have an impact on future business strategy. For goods traders, the survey found that:

- 43 per cent of respondents said, going forward, they were looking to increase exports of specific product(s) that had become more price competitive due to reduced or eliminated tariffs under FTAs
- 45 per cent of respondents indicated that they were looking to expand the range of products exported from Australia
- 46 per cent of respondents were exploring new export markets facilitated by Australia's FTAs.

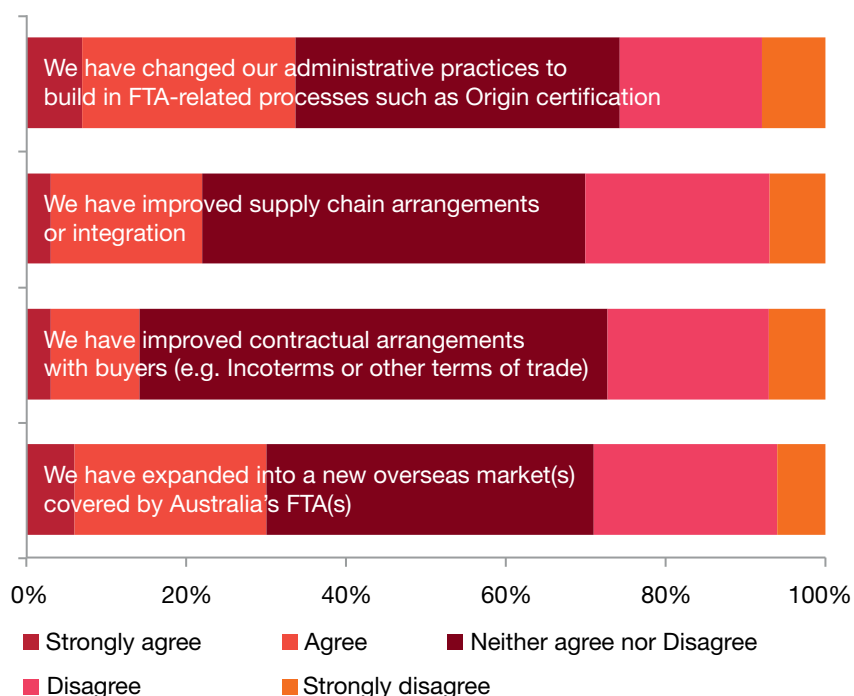
In terms of how utilising FTAs impacts business strategy for the future, as Figure 8 indicates, FTAs can lead to Australian businesses developing new business networks and supply chains. However, despite these operational changes, Australian businesses did not comment substantively on the strategic impacts of FTAs across our focus groups and interviews. This suggests that FTAs are one of many considerations which inform business decisions on sourcing of products or assessment of export market access. A variety of other factors form the primary focus for businesses (for example, cost of labour, quality of products and inputs for importers, or size and proximity of market for exporters).

Figure 7: Responses to survey question – How has utilising FTAs for your exports from Australia impacted on your business activity?



Source: PwC FTA Business Survey.

Figure 8: Responses to survey question – How has utilising FTAs for your exports from Australia impacted on your business activity? (Business Decisions and Strategy)



Source: PwC FTA Business Survey.

Services businesses and investors however, use FTAs differently to traders of goods. Unlike goods exporters, for whom FTAs offer reductions in tariffs or expanded quotas, service providers benefit from FTAs through changes to relevant laws and regulations as a result of formal legal commitments. This indirect process means that businesses may be unaware of these improvements.

On average, 35 per cent of services businesses survey respondents reported that FTAs have had some or a substantial influence on their decisions to export and trade. This includes decisions to establish abroad, to sell a wider range of services or conduct a broader range of business activities in the FTA market, to engage in offshoring or outsourcing, and to bid for government procurement contracts in FTA markets.

Our research shows that increased trade in goods between Australia and FTA partner countries – and even increased interest in exploring possibilities for goods trade on the part of many businesses – has driven an increase in demand for some Australian services companies. Increased interest from Japanese, Chinese and Korean investors in exploring opportunities in Australia has also spurred demand for support services (eg legal and financial advice) from Australian providers.

Overall, most services businesses we surveyed and interviewed recognised that it is too early to gauge the full impact of the services commitments contained in the North Asian FTAs.

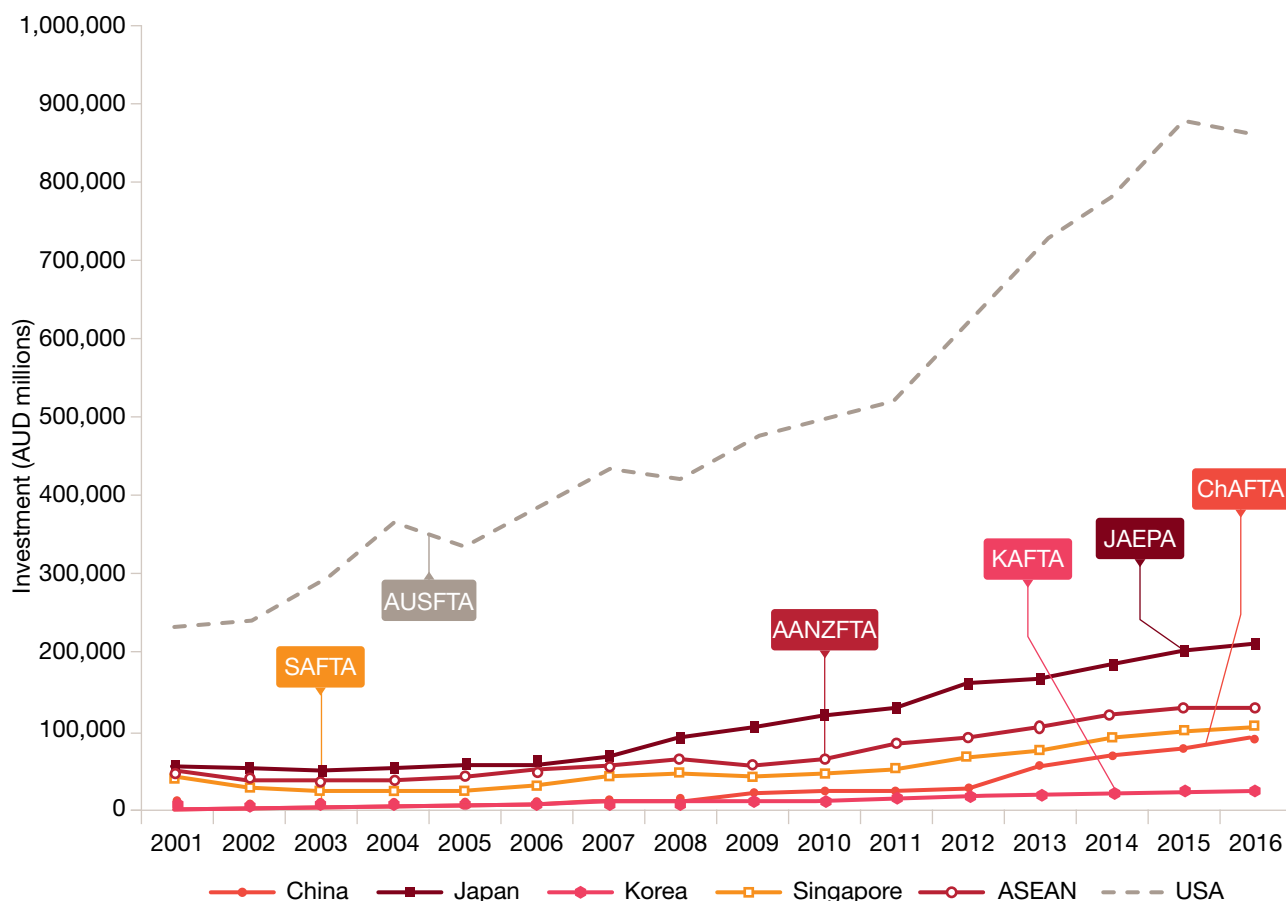
Despite this, early signs indicate that FTAs have promoted investment in Australia and the level of investment is increasing. Figure 9 shows investment from Japan has risen by

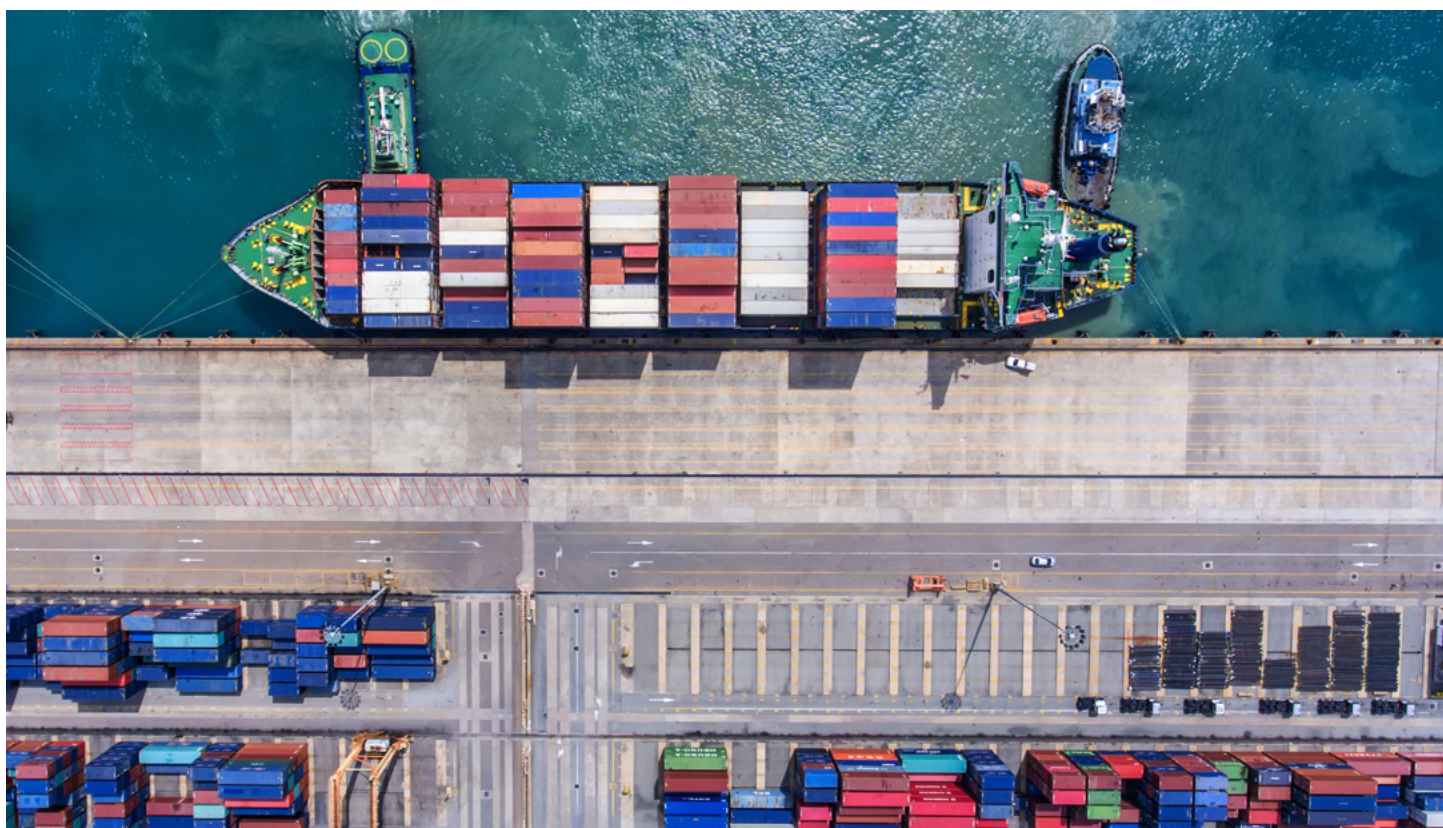
18 per cent since the JAEPA came into force in 2015, and investment from China grew by 15 per cent in the first year following the ChAFTA coming into force at the end of 2015. By contrast, total direct investment in Australia from all countries in 2016 had risen by 5 per cent since 2015 and by 14 per cent since 2014.

The trend towards long-term growth in two-way investment with longstanding investment partners (the US and Singapore) since commencement of FTAs shows that FTAs can also support growth in investment with key trading partners in the longer term.

The stock of inward investment from the US has grown since the AUSFTA (by 158 per cent), while investment from Singapore has increased by 344 per cent since the Singapore-Australia Free Trade Agreement (SAFTA) came into force.

Figure 9: Stock of investment in Australia from China, Japan, Korea, Singapore, USA and ASEAN (2001 to 2016) (AUD millions)





Government procurement

A number of Australia's FTAs contain commitments to ensure transparency and facilitate open participation by businesses in government procurement processes. In general, government procurement provisions in FTAs tend to include details on the government entities covered or not covered, threshold values of in-scope procurements, and any specific exemptions. Given that government procurement provisions only appear in certain FTAs, and some procurements (for example defence procurement) are excluded from the provisions, there is a limited number of entities able to benefit from these provisions.

Six per cent of Australian survey respondents indicated that utilising FTAs had resulted in overseas procurement contract opportunities, compared to 45 per cent who disagreed or strongly disagreed. Furthermore, 9 per cent of Australian exporters agreed or strongly agreed that they were looking to pursue government procurement contracts in FTA partner countries as a result of the FTA.

These responses from the survey and focus group participants suggest that FTAs have facilitated some improvement for the cohort of businesses seeking government procurement opportunities.

In particular, a significant proportion (43 per cent) of the respondents who indicated that they were looking to pursue government procurement contracts in FTA partner countries identified government procurement contract opportunities as an outcome of their having utilised FTAs historically. This suggests FTAs have started to facilitate the award of government procurement contracts to Australian businesses for which government procurement forms part of their business strategy.

Business travel

Australia's North Asian FTAs include some improved visa conditions for Australians travelling to partner countries. Access commitments facilitating business travel in Australia's FTAs – particularly the North Asian agreements – have been limited to date.

However, over 30 per cent of survey respondents agreed that FTAs had increased the number of business trips taken to FTA markets to seek out new business opportunities and 34 per cent reported that FTAs influence business decisions to send staff to FTA markets, either on secondments or on a 'fly in, fly out' basis.

Some respondents agreed that FTAs had enhanced the capacity of management and personnel to work in FTA markets (29 per cent) or to access opportunities as contractors (21 per cent). Few (11 per cent) felt access to working visas for spouses or dependents had improved.

Analysis of arrivals and departure data shows that FTAs have had some impact on the flow of business people travelling to and from FTA markets, although this appears to be due to increased business activity rather than specific commitments to improve entry/access.

Mutual recognition agreements

FTAs have facilitated greater cooperation between Australia and FTA partners on regulatory initiatives through mutual recognition agreements (MRAs). FTAs have facilitated mutual recognition of regulatory approaches in financial and professional services industries.

The benefits of these have yet to be determined – our research showed mixed views on the value of MRAs and some concerns that mutual recognition has not been sufficiently reciprocated in terms of the benefits delivered to Australian firms (vs foreign counterparts). Across the education sector for example, the general view was that more could be done to broaden the scope for recognition of degrees and training placements in Australia and Asian markets.

Nevertheless, there is recognition that provisions in FTAs can create dialogue to address specific barriers to certain professions. For example, the AUSFTA includes a mechanism to promote cooperation among counterpart peak professional bodies, reporting back to a joint committee composed of representatives from both national governments. This has provided the mechanism for Australian legal professionals to engage with US legal professionals at state level on issues of market access. Consequently, Australian lawyers have a good practical level of access into significant US jurisdictions.

Market access and regulatory certainty

Services – rather than goods – now offer the greatest opportunities for increasing gains from trade. This is because, with a few exceptions, international trade in goods is already largely liberalised. The World Bank calculates that the global average applied goods tariff is less than three percent.

In contrast, services industries in most countries are characterised by significant barriers to entry for foreign operators. The inclusion of services in recent free trade agreements – including Australia's North Asian agreements – has raised hopes that liberalisation of world trade in services may begin to gather speed. This process of liberalisation is underway, however results differ greatly between sectors.

FTAs have improved access for Australian firms in FTA markets however, the removal of barriers and impediments to services trade and investment in FTA partner markets is still in its early stages.

The full market access outcomes of Australia's North Asian FTAs will take time to bear fruit, and will become evident over future years.

In addition, services exporters face different hurdles to goods exporters when accessing markets, particularly if they seek to deliver in-market. While FTAs may provide regulatory certainty and safeguards, realising the benefits of market access outcomes requires time and commitment. Setting up a commercial presence overseas can be complex, in an FTA partner market or otherwise.

Despite this, our research revealed that there are cases where services businesses have directly benefited from FTAs due to the removal or reduction of specific regulatory controls. For example, ChAFTA has provided positive results for some education providers. Also, Australian fund managers consider cross-border access for managed funds in the Korea-Australia Free Trade Agreement (KAFTA) and JAEPA to be generally beneficial.

Forty-five per cent of survey respondents agreed (21 percent agreed and 24 per cent strongly agreed) that FTAs had made it easier to access overseas markets by removing or reducing restrictions to entry, or by removing or reducing controls on activities (eg on marketing, solicitation and authorisation).

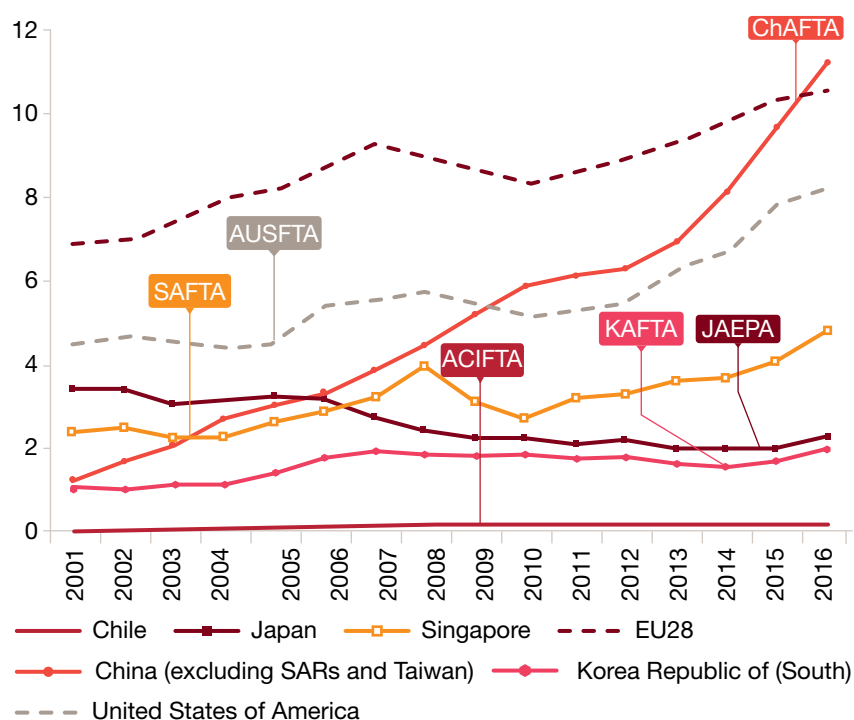
Cross-border exports of services to FTA partners are increasing. FTAs have coincided with rising cross-border services exports to almost all FTA markets. When compared with Australia's services exports to the European Union (EU) – the largest market with which Australia does not have a FTA – Australia's services exports to most FTA partners have performed strongly. Since the SAFTA came into force between Australia and Singapore, Australia's exports of other business services have rapidly increased, rising by 450 per cent to AUD2.2 billion between 2003 and 2016.

Figure 10 demonstrates that services exports to China have almost doubled, rising from AUD 5.9 billion to AUD 11.3 billion since 2010, with a 16 per cent rise in the 12 months following the ChAFTA entry into force in December 2015. Exports to Korea have been growing since 2006 and continued to rise in 2014 following the KAFTA. Financial service exports in particular have increased rapidly since the KAFTA was signed, rising 540 per cent between 2014 and 2016.

While FTAs may provide greater regulatory certainty for Australian services providers and investors over the long term, these commitments are not always immediately well understood by businesses. Barriers still remain.

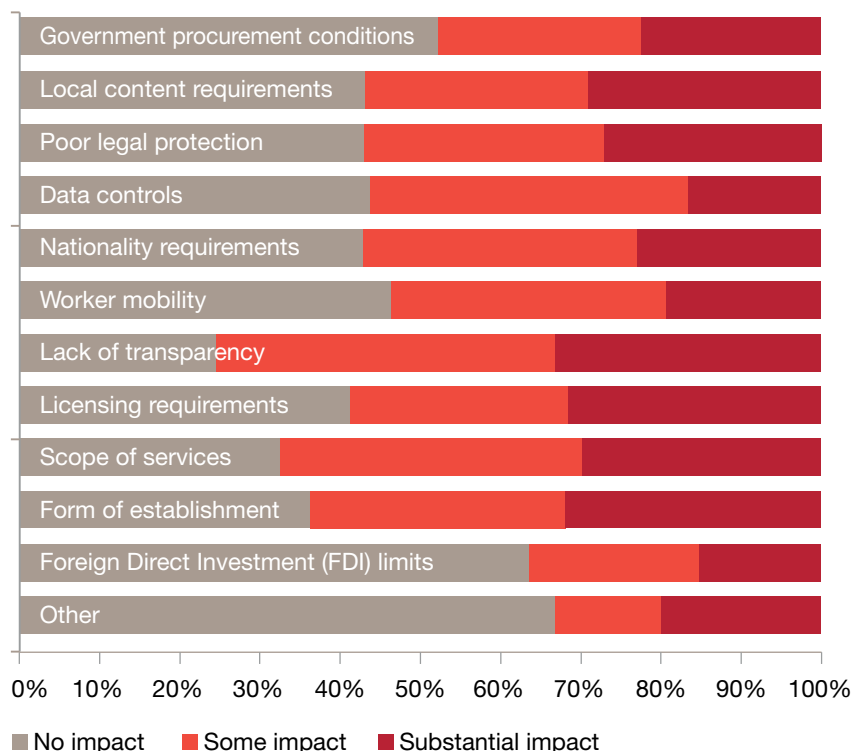
Fortunately FTAs have introduced a process for reducing barriers progressively; for example, through the establishment of intergovernmental working groups and regulation review mechanisms. This process has had a limited impact to date (particularly regarding the North Asian FTAs) as it is still at an early stage. Barriers identified by survey respondents as having the most substantial impact on business include restrictions on type/form of establishment, restrictions on the scope of services and burdensome licensing and qualification requirements. Lack of transparency of applicable laws and regulations was cited as the issue having the most substantial impact on businesses and was the most frequently cited (refer Figure 11).

Figure 10: Cross-border gross services exports from Australia to key markets (AUD billions)



Source: ABS 5368.0.55.004

Figure 11: Responses to survey question – Please describe the impact (if any) of the following factors have on your business's activities or opportunities in FTA markets



Source: PwC FTA Business survey

FTAs can support increased investment flows in two main ways: first, by including commitments and processes that require governments to address existing obstacles and disincentives to investment from FTA partners; second, by promoting goods and services trade, leading to greater business links between the economies.

FTAs have contributed to positive outcomes in the business environment for some investors, for example by easing regulatory constraints on services and addressing 'beyond the border' controls. However, in the main investors believe that the regulatory environment has been largely unaffected by operation of the FTAs.

Between 13 and 16 per cent agreed that FTAs contributed to increased business activity arising from greater certainty of the business environment (eg confidence that regulatory frameworks won't become more trade-restrictive). Between 12 and 20 per cent of survey respondents agreed or strongly agreed that FTAs had a positive effect on various aspects of the business operating environment in FTA partner countries.

The general view communicated by businesses during interviews was that provisions to enhance transparency and decision-making processes in FTAs are positive but are undermined by implementation at the local level. This is particularly the case in economies where services markets are still relatively restricted.

Government's role

Governments can help to optimise business utilisation of FTAs in a number of ways. These include through streamlining origin documentation arrangements, reducing compliance costs, digitising forms, providing further education and advocacy (particularly of SMEs and trade intermediaries), and implementing measures to foster improved understanding of services and investment commitments in FTAs. Existing review mechanisms in FTAs could also help to enhance and align their benefits.

Challenges for business

Rules of Origin and certification

Some Australian importers indicated that the delays in, and administrative costs associated with obtaining CoOs or Origin Declarations (or the inability to do so at all) were a significant factor in their not claiming FTA preference for goods imported from FTA partners. This can be further complicated by difficulties associated with determining whether a particular product satisfies the RoO. In particularly complex cases, importers and exporters often resort to seeking formal advice from Customs authorities on whether a good satisfies the RoO of a particular FTA, which can take some time to obtain. Australian exporters can often miss the opportunity where purchasers/importers do not request a CoO or Origin Declaration – and thereby miss out on the potential savings.

One of the key ways to maximise FTA utilisation among SMEs would be to simplify CoO and RoO requirements, thereby reducing the FTA compliance burden. Moving to self-certification arrangements for FTA use would promote higher rates of utilisation and eliminate the need to engage (often through intermediaries) with certifying bodies. This engagement process, as highlighted through our research, imposed costly administrative processes around claiming of refunds for importers, or higher cost of goods sold for exporters. There was also a call by a number of businesses to increase the number of bodies who are able to issue CoO's.

Regulatory barriers

An area of frustration for businesses was the presence of non-tariff barriers (NTBs) in target FTA markets that undermine benefits afforded by FTAs. NTBs (being all barriers to trade that are not tariffs) include voluntary export restraints, quotas, technical barriers to trade such as domestic standards, and obstacles to the establishment and provision of services. While these measures may be legitimate, the contribution of NTBs to overall trade restrictiveness is significant, and in some estimates NTBs are far more trade-restrictive than tariffs. The identification and removal of NTBs is a key issue in improving the economic integration aspects of both the trade in goods and trade in services provisions of FTAs.



In particular, 25 per cent of Australian exporters stated that NTBs were a greater consideration than FTA benefits in making a decision to enter an export market. The impacts of NTBs include supply chain and distribution restrictions arising from things like licensing and business establishment requirements. Interestingly, 69 per cent of SME respondents indicated that NTBs were a factor in their not seeking to claim preference in regards to goods exported from Australia (compared to 25 per cent for respondents from Australian large businesses). From an industry perspective, Australian businesses from the agriculture, automotive, food and beverage, manufacturing and pharmaceuticals sectors were more likely to identify NTBs as a significant issue in regards to their export operations.

Focus group participants cited limited market access and restrictive phytosanitary measures (regulations on plants and plant products) as more significant to their business decisions and operations than FTAs for the pharmaceutical and processed food sectors. These sentiments represented the broad opinion of participants across all the focus group sessions held across Australia.

The presence of provisions in FTAs that provide scope for (current or future) negotiations relating to market access and regulatory reform has been a notable development in contemporary Australian FTAs and it is clear that there is recognition by negotiators that NTBs represent an area of trade reform that requires significant attention in order to optimise opportunities for Australian businesses. This progress has been recognised by respondents, with the caveat that the rate at which positive outcomes are achieved could be faster. It is also apparent from respondents that there is a complex divide between services and goods when considering NTBs. In light of the various factors evident in the responses, there is a clear need to better define a hierarchy of NTBs for consideration by negotiators in existing FTAs and in drafting the scope and provisions of new FTAs.



Further education, advocacy and ongoing research

There has been considerable investment by the government to inform and educate businesses on the North Asian FTAs, including the development of the DFAT FTA portal which provides business with trade agreement and tariff look up capability based on keywords and Harmonised System codes.

However, ongoing research on FTA utilisation is required, particularly in relation to RoOs and the monitoring of services and investment outcomes of Australia's FTAs with China, Japan and Korea. A structured research program into the utilisation, impact and administration of FTAs should also be a pillar of Australia's FTA policy.

Further research into the broader application of self-certification and other reform options (enabled through technology) across FTAs would likely yield deeper insights into the costs and benefits of the FTA process to business.

Industry's role

Along with the Australian Government, industry associations and business groups play an important role in assisting businesses understand and utilise Australia's FTAs. Trade intermediaries such as customs brokers and freight forwarders also have an important role in assisting businesses to utilise FTAs effectively.

It is clear from our research that trade intermediaries play a role in assisting businesses to access the benefits offered through FTAs. However, there were mixed reports from research respondents about the quality of the support they provide. While a number of businesses said they relied on intermediaries to manage their FTA utilisation, there appears to be a gap between perceptions of the assistance intermediaries give and actual increased FTA uptake. This gap appears to be greatest for exporters and at the SME-sector level.

Results from the business survey found that Australian businesses rely heavily on a number of sources to obtain information and advice on FTAs, with 78 per cent indicating that they use multiple sources of information. Figure 12 provides an overview of these sources.

In terms of intermediaries, 60 per cent of respondents indicated that they obtain information and advice on FTAs from customs brokers or freight forwarders, the second most popular source of information among respondents. Approximately half of respondents (51 per cent) indicated that customs brokers and freight forwarders are a useful source of information in assisting their business to make decisions with regard to FTAs. Further, although 52 per cent of both metropolitan and regional businesses indicated that their import or export team was responsible for FTA management, metropolitan-based businesses

were more likely to also rely on their customs broker or freight forwarder for FTA management compared to those based in regional Australia. The results also indicated that customs brokers were more likely to be responsible for FTA management for large enterprises (62 per cent) compared to Australian SME businesses (30 per cent).

Interestingly, Australian importers appear to rely more on customs brokers and freight forwarders for information and advice on FTAs than businesses that export. Specifically, only 31 per cent of exporters indicated that they obtain FTA information and advice from customs brokers or freight forwarders. This group of respondents overwhelmingly use government websites (81 per cent) as their principal source of FTA information.

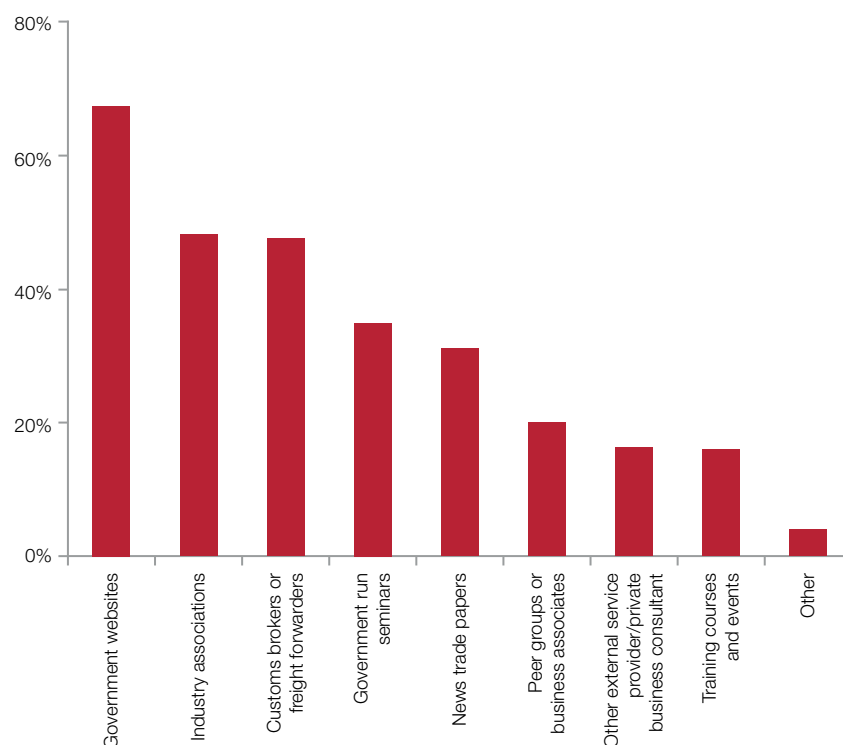
Across the research there was evidence of some reliance on intermediaries (whether customs brokers, freight forwarders or other parties such as trade consultants and industry associations) for assistance with either claiming FTA preferences or managing compliance. For example:

An agribusiness exporting from regional Australia told us their freight forwarder provided an integrated supply chain offering that included completing relevant documentation requirements such as CoOs on the business' behalf.

This service level is an example of best practice, but does not appear to be an industry norm – there were a number of exporters that did not receive this level of support or assumed this support was being provided (when it was not).

A number of businesses remarked that the DFAT FTA portal had been a significant aid to understanding FTA opportunities. Conversely, reliance on intermediaries aligns with evidence of a relatively shallow understanding of the more technical aspects of FTA compliance, such as RoO. In addition, a number of businesses across the focus groups commented positively on the significant assistance that Austrade provides across FTA partner countries. For example, an exporter to North Asian markets said that Austrade was their first port of call when seeking advice on market engagement.

Figure 12: Responses to survey question – Where does your business obtain information and advice about FTAs?



Source: PwC FTA Business Survey

Conclusion

Trade has always been, and will continue to be, vital to Australia's ongoing prosperity. Australia's FTAs play an important role as an enabler to Australian businesses. They represent a key pillar of the Australian Government's trade policy and facilitation agenda, enabling the outbound growth of our business community and attracting innovative new goods, services and investment to our economy. It should be remembered that they are but one part of an overarching global rules-based trade liberalisation framework, with Australia's membership and active participation in the WTO representing the central pillar. They are accompanied by many other policy levers of government that are vital in charting sustainable economic growth for our country.

FTAs represent a strategic imperative of the Australian Government in the drive to broaden the base of our economy, particularly as we transition from a resources-focused mining boom to an agricultural goods 'dining boom'. Demand in Asia for Australia's trusted agricultural produce will continue and Australia's North Asian FTAs provide a competitive advantage across key sectors. They also act as a bridge for the Australian services sector in to new and emerging markets, providing greater certainty and transparency.

To maximise the opportunity that the North Asian agreements present, the Australian Government has accelerated advocacy and education of FTA requirements, representing a clear progression from past strategy. We heard many accounts of the assistance that Austrade had provided business both in Australia and in-market. We also observed significant activity across Australia's trade and industry advocacy groups in the provision of government-supported training and awareness sessions.

Intergovernmental legal agreements are inherently complex – making FTAs complex. There will continue to be a need for international businesses to educate themselves on the intricacies of FTAs in order to optimise the benefits.

Ongoing support for SMEs to grapple not just with the complexity of FTAs, but international business more broadly, will remain a worthwhile and rewarding pursuit for Australian governments and industry bodies. This sector of the Australian economy stands to gain substantially if it can successfully tap in to the opportunities on Australia's doorstep – particularly where it is supported by a network of expanding and ambitious FTAs.

The study represents the first of its kind in Australia, and is an important demonstration by the Australian Government of the value it places on evaluating the impact and utilisation of FTAs and its trade policy agenda. We were asked to consider the utilisation and impact of Australia's FTAs with a specific focus on North Asia. In considering the research question, we sought to deliver insights through layers of enquiry, including quantitative and qualitative assessment in Australia and abroad. The detailed terms of reference and a summary of our research methodology can be found in **Appendix A** and **Appendix B** respectively.

The relative immaturity of the North Asian FTAs presented limitations in terms of assessment of impact, particularly in relation to trade in services. Whilst we were unable to identify causation through our quantitative analysis, there is a correlation between a strengthening trade relationship and FTA usage. Most important of all, it was clear that businesses are utilising the agreements, which demonstrates they are accessing the benefits.

Challenges will persist as a result of the complexity of international business, and of FTAs. Non-tariff barriers and technical barriers to trade remain and should be addressed at a government-to-government level. Our research showed that progress is being made, but business asked for more to be done.

Across our many consultations, meetings, focus groups and our business survey, however, it was clear that the potential benefits presented by Australia's FTAs are flowing through to business and, by extension, the broader community.

Appendix A

Terms of reference

PwC was engaged to conduct an independent analysis of FTA utilisation and the wider impact of FTAs on Australian business activity for Australia's existing agreements, with an emphasis on the FTAs with China, Japan and Korea.

The analysis that was performed encompassed:

- possible barriers to the utilisation of FTAs by businesses, and ways in which FTA utilisation may be able to be optimised
- business perceptions of FTAs and experience of using FTAs, including the impact of FTAs on decision processes
- business intentions on FTA utilisation, noting lag effects inherent in business activities and decision processes.

The study aimed to:

- review relevant Australian and international literature, to ensure the research methodology aligned with Australian and international best practices and considered an evidence hierarchy
- include qualitative and quantitative analysis, on an aggregated and FTA-specific basis, as appropriate, encompassing:
 - focus groups, interviews, case studies and business survey method
 - empirical analysis of available official trade and associated data, including Australian and partner-country customs and trade data

- be framed in the context of Australia's trade trends and economic policies.

The study encompassed the utilisation and impact of FTAs in respect of the following trade and investment activities, noting interrelations where appropriate:

- cross-border merchandise trade
- cross-border trade in services
- supply of services 'in country' through movement of natural persons and commercial presence
- mutual recognition arrangements (and other enhanced professional services cooperation)
- business expansion and investment decisions (including international investment)
- government procurement
- the development of new business networks and supply chains
- other FTA provisions affecting movement of goods, services and people across borders.

The analysis was required to consider the following:

- the processes of international trade and how these may impact on FTA use by businesses
- the role of intermediaries (including aggregators, customs agents, shipping agents and freight forwarders) in the context of merchandise trade and FTA utilisation

- the different forms by which businesses may utilise or otherwise be impacted by FTAs (active, passive, direct and indirect)
- both domestic and offshore aspects of FTAs, including the extent to which Australian businesses are impacted by decisions which may be outside their influence, such as the take-up of tariff preferences outside of Australia by importers or intermediaries in our FTA partner countries.

The completed study and report will provide an evidence base for informing FTA policy and advocacy.

Appendix B

Overview of methodological approach

Literature review

- A literature review of relevant research relating to the utilisation of FTAs was undertaken
- Through this review, we identified a number of initial patterns, trends and challenges in the existing framework that have already been the subject of expert discussion
- An analysis and review of Australia's FTAs to 'map' the nature and type of commitments in the FTAs.

Hypothesis development

- Based on the literature review and desktop analysis, we developed a series of hypotheses to test in order to establish a view of FTA utilisation issues.

Industry association

- We met with nineteen industry associations across Australia to get insights on the perceptions of FTAs, how FTAs were impacting different industry sectors and how they were changing Australian businesses.

Focus group sessions

- We conducted seven FTA focus group sessions across Australia and three FTA focus group sessions in North Asian markets (China, Japan and South Korea) with a select group of importers and exporters to gain insights on FTA usage, how FTAs are changing business activity and strategy.

In-depth interview

- We also conducted a series of in-depth interviews with Australian businesses to gain a deeper understanding of how FTAs impacted on their activities, any barrier they encountered in accessing FTAs and whether FTAs shape sourcing or market selection.

Online survey

- An online survey was created and circulated via several channels, including social media, direct solicitation, industry association websites and newsletters, etc. both in Australia and in offshore markets.
- The survey sought to seek business input and views in respect of trade in goods and services on key measures such as FTA use, impact, strategy and administration. The survey predominantly used the Likert scale to capture a range of sentiments from respondents.
- The survey was completed by micro, small, medium and large businesses in metropolitan and regional Australia, as well as in the FTA markets of China, Japan and South Korea.

Analysis

- Once the data was collected subject-matter experts from PwC and ITS Global analysed, reviewed and provided commentary on the spread of the results and insights gained through the industry association engagement, focus group sessions, depth interviews and on-line survey.
- We performed economic analysis on multiple data sets from Australian and overseas sources, including import/export trade, two-way investment and movement of people data.
- We also performed desktop research analysis of examples of investment opportunities between Australia and FTA Partners, drawing on publicly available information to complement the result of the interview process.

Report

- This report expresses PwC's research, findings and recommendations on FTAs and opportunities to enhance Australian business uptake of FTAs.
- This report also splits our findings between the use of FTAs by Australian businesses and the impact of FTAs on Australian businesses across trade in goods, services and investment.
- Under each category of our report, we have sought to test the hypotheses developed in the initial phases of our Study.

Appendix C

Key references

The following list of reference information is divided into two sections:

- C1. Reference data
- C2. Sources for literature review.

C.1 Reference data

Trade in goods

Methodological sources for economics analysis for trade in goods

Definitions for utility, utilisation and usage. Hamanaka S, *Asian Development Bank Working Paper No. 133 On the Use of FTAs: A Review of Research Methodologies*, 2013

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Data sources for economics analysis for trade in goods

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15. Cross-border gross services exports from Australia to key FTA markets (2000–2016) (AUD billions). Australian Bureau of Statistics, International Trade: Supplementary Information, Financial Year, 2015–16, Cat No. 5368.0.55.003

C.2 Key sources for literature review

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