Submission

By

Business NZ

To

Ministry of Foreign Affairs and Trade

On the

New Zealand – China Free Trade Agreement Joint Feasibility Study Public Consultation Document

18 August 2004

PO Box 1925
Wellington
Ph: 04 496 6555
Fax: 04 496 6550

NEW ZEALAND – CHINA FREE TRADE AGREEMENT
JOINT FEASIBILITY STUDY
PUBLIC DISCUSSION DOCUMENT

SUBMISSION BY BUSINESS NEW ZEALAND
18 AUGUST 2004

1. Introduction

1.1 Encompassing four regional business organisations (Employers' & Manufacturers' Association (Northern), Employers' & Manufacturers' Association (Central), Canterbury Employers' Chamber of Commerce, and the Otago-Southland Employers' Association), Business New Zealand is New Zealand's largest business advocacy body. Together with its 56-member Affiliated Industries Group (AIG), which comprises most of New Zealand's national industry associations, Business New Zealand is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

1.2 In addition to advocacy on behalf of enterprise, Business New Zealand contributes to Governmental and tripartite working parties and international bodies including the ILO, the International Organisation of Employers and the Business and Industry Advisory Council to the OECD.

1.3 Business New Zealand's key goal is the implementation of policies that would see New Zealand retain a first world national income and regain a place in the top ten of the OECD (a high comparative OECD growth ranking is the most robust indicator of a country's ability to deliver quality health, education, superannuation and other social services). It is widely acknowledged that consistent, sustainable growth well in excess of 4% per year would be required to achieve this goal in the medium term.

1.5 International trade is critical for economic growth, particularly for small countries with small domestic markets, such as New Zealand. However, many countries impose significant tariff and non-tariff barriers to trade, which harm the competitiveness of New Zealand exporters. Trade liberalisation is therefore very important for gaining improved access and higher returns for New Zealand goods and services in overseas markets, and so increasing New Zealand's rate of sustainable economic growth.

1.6 Business New Zealand welcomes the opportunity to comment on the proposal for a New Zealand – China Free Trade Agreement. The People's Republic of China is New Zealand's fourth largest trading partner and one of our fastest growing markets for exports and sources of imports. However, rapid growth in bilateral trade in recent years has occurred in spite of significant tariff and non-tariff barriers and these are likely to have impeded further growth in New Zealand exports.

1.7 Many in the business community welcome the Government's intention to negotiate of a free trade agreement with China that would eliminate or at least substantially reduce tariff and non-tariff trade barriers. However, it should also be recognised that others are very concerned about the impact a free trade agreement with China would have on sensitive sectors of New Zealand economy that are sensitive to Chinese imports, most notably textiles, clothing and footwear. Their circumstances must be carefully considered.

1.8 Following a summary of recommendations, the remainder of this submission comments on the key issues arsing from the intention to negotiate a free trade agreement with China.

2. Summary of Recommendations

2.1 Business New Zealand recommends that:

(a) Negotiations for a free trade agreement with China should be a high priority but should not overshadow other high trade policy priorities, such as the:

(i) WTO Doha Round;
(ii) Development of single economic market with Australia; and
(iii) Negotiation of a free trade agreement with the United States.

(b) A free trade agreement with China should provide for a significant reduction or elimination in Chinese tariff levels.

(c) Any negotiated reduction in New Zealand tariffs on imports from China beyond those already announced to 2009 should be dependent on:

(i) Agreement from China that it will significantly reduce or eliminate its tariff and non-tariff barriers;
(ii) The implementation of a phased tariff reduction programme to provide businesses with certainty and time to adjust;
(iii) Greater commitment by the Government to growth promoting policies to improve business productivity and competitiveness; and
(iv) Continued support for the development and implementation of industry strategies that recognise the need for ongoing support for industries in transition and improved funding for training for the existing workforce.

(d) A free trade agreement with China should include agreement for the reduction or elimination of non-tariff barriers.

(e) A free trade agreement with China should include robust rules of origin provisions that are enforceable.

(f) New Zealand should retain the right to take anti-dumping action in respect of trade between New Zealand and China.

(g) A free trade agreement with China should remove or relax barriers restricting trade in services.

(h) A free trade agreement with China should seek to improve the investment climate.

(i) Provisions on protecting intellectual property rights should be included in a free trade agreement with China and China should be encouraged to improve its track record in this regard.

(j) A free trade agreement with China should not include provisions on labour and environmental standards.

(k) A free trade agreement with China should not include a provision on the Treaty of Waitangi.

(l) A free trade agreement with China should include provisions on a disputes resolution process.

3. Business New Zealand's Position on Free Trade Agreements

3.1 Business New Zealand is generally supportive of trade liberalisation policies. Reducing the tariff and non-tariff barriers faced by New Zealand exporters and those wishing to do business offshore are likely to result in significant gains in competitiveness, higher incomes for firms and improved living standards and quality of life for all New Zealanders.

3.2 Business New Zealand's first preference is for trade liberalisation to take place at a multilateral level, such as through the WTO process. A positive, comprehensive outcome to the WTO Doha Round would deliver far greater benefit for New Zealand than putting in the effort to firstly attract potential bilateral partners (no easy feat for a small country) and then undertake separate negotiations with them, with the time and energy that goes into such a process.

3.3 However, the WTO process is a slow one and partially as a result of a perceived lack of progress there has been a proliferation of regional and bilateral trade agreements concluded over the past decade. Business New Zealand's view is that the term 'free trade agreement' is somewhat misleading. A true free trade agreement would effectively create a single economic market between the participants and would also reduce trade barriers with the outside world. In reality most 'free trade agreements' are 'preferential trade agreements', in that they may confer improved market access (but by no means completely open access) for the parties. Providing that the principle of Most Favoured Nation is not compromised, these agreements are usually endorsed as 'WTO-consistent' even when the outside world is excluded from the improvements negotiated by the parties.

3.4 For the purposes of this submission, Business New Zealand will use the term officially adopted for the New Zealand – China negotiations, 'free trade agreement'. However, we consider the term 'closer economic partnership' to be a more accurate representation.

3.5 Business New Zealand agrees that a free trade agreement with China should be a high priority, but we continue to consider progress in achieving a positive and comprehensive WTO Doha Round outcome to be of greatest importance. Also, New Zealand should not in its enthusiasm for China lose sight of the importance of fostering the development of a single economic market with Australia, nor the importance of negotiation of a free trade agreement with the United States.

3.6 *Recommendation: Business New Zealand recommends that negotiations for a free trade agreement with China should be a high priority but should not overshadow other high trade policy priorities, such as the:*

(a) WTO Doha Round;
(b) Development of single economic market with Australia; and
(c) Negotiation of a free trade agreement with the United States.

4. China as an Economic Superpower

4.1 25 years ago the People's Republic of China had only recently emerged from 70 years of almost continuous revolution, war and social instability. The devastating decade-long Cultural Revolution had only recently ended with the death in 1976 of Mao Tse Tung. China was inwardly focused, isolated internationally (by both the West and the Soviet bloc) and its Communist ideology made for a centrally planned economy with private enterprise prohibited. Despite aggressive efforts to develop heavy industry, most of its population was still living in rural poverty.

4.2 In 1978 China's leaders made an explicit decision to reform and open China to the outside world. Although politically it has remained a one-party Communist state, its economic reforms have been significant. As a result, China has averaged 7% GDP growth over the past 25 years, has attracted large flows of foreign investment, has greatly expanded its international trade, and it is now the 6th largest economy in the world – with some suggesting that China could become the world's largest economy within the next 10-20 years[1].

4.3 China has taken a more active role on the international stage in recent years, being a member of APEC since 1992 and the WTO since December 2001 – the latter after 15 years of negotiations. WTO membership is particularly important as it improved market access for goods and services and provided for further reform of its trade policies and practices.

4.4 Although New Zealand was the first country in the world to provide China with 'market economy status', Business New Zealand considers that China still has much to do before it can truly be considered so. The harder tasks of reforming its state owned enterprises, housing sector, financial markets, and developing a social welfare system are significant challenges, as are tackling official corruption and ensuring primacy of the rule of law and a respect of property rights, including those of holders of intellectual property.

4.5 The sustained rapid growth of China's economy over recent years has been staggering (9.1% for 2003). While rapid growth has lifted hundreds of millions of Chinese out of poverty and provides excellent opportunities for exporters, it has not come without problems both for China and the global economy. For example, the Chinese government has been considering how it can contain growing inflationary pressures, although it remains to be seen how successful it will be in applying the brakes, particularly as the government seems unprepared to revalue its significantly undervalued currency to a more realistic level.

4.6 Meanwhile, China's demand for raw materials and intermediate goods has been a significant and growing factor in increased global commodity prices, most notably for oil. While China is becoming an engine for economic growth, particularly in Asia-Pacific, high commodity prices are a double-edged sword (as evidenced by concern over the impact of higher oil prices).

---

[1] For example, in June 2003 BERL suggested that a simple extrapolation of Chinese and American GDP growth rates would see China's GDP overtake that of the United States in 2012.

4.7 While there is much enthusiasm for the opportunities provided by a potential market of 1.3 billion people and an economy growing at 9% per annum, China's GDP per capita in 2003 was only US$1,132, a mere half of Thailand's and just 5% of Singapore's or Hong Kong's. Although it has a large and growing urban middle class, China is still overwhelmingly agrarian, with most of the population subsisting on very low incomes, particularly in the interior western and northern provinces that are a far cry from the booming eastern coastal fringe.

4.8 China is an important trading partner and is likely to become increasingly so over time, but both its immediate prospects and size pose challenges for a small and distant trader such as New Zealand.

5. New Zealand – China Bilateral Trade

5.1 Since 1990, the People's Republic of China has become an increasingly important trading partner for New Zealand, taking an increasing proportion of our exports while also supplying a much greater proportion of our imports (see table 1 below).

5.2 For the year ending December 1990, China and Hong Kong together took around 2.5% of New Zealand exports and were the source of a similar proportion of New Zealand imports. Rapid growth in both exports and imports (but especially imports) since 1990 has resulted in the proportions being 6.7% of exports and 9.4% of imports for the year ending December 2003.

5.3 When considering the historical trade data it is important to recognise that a growing proportion of New Zealand's trade with China is being recorded as going directly to China or coming directly from China rather than via Hong Kong (a traditionally important transit port for products entering and leaving China). The reduction of Chinese tariff rates since its WTO accession in 2001 and greater levels of enforcement at the China – Hong Kong border have been a factor in exports to Hong Kong falling by almost 30% since 2000. Looking solely at direct trade with China will therefore tend to understate the importance of China as a market (particularly in earlier years).

Table 1: Total Trade with China and Hong Kong, years ending December 1990-2003 ($millions)

	1990	1995	1997	1998	1999	2000	2001	2002	2003
Exports	**379**	**1,149**	**1,168**	**1,253**	**1,248**	**1,700**	**2,117**	**2,035**	**1,905**
+ China	151	529	593	659	646	928	1346	1422	1361
+ Hong Kong	228	620	575	594	601	773	771	613	544
Imports	**382**	**980**	**1164**	**1344**	**1610**	**2095**	**2364**	**2731**	**3002**
+ China	190	752	1023	1187	1432	1924	2207	2591	2849
+ Hong Kong	191	228	142	157	179	171	156	140	153

Source: Statistics New Zealand, Overseas Trade Statistics

Exports

5.4 The majority of New Zealand's exports to both China and Hong Kong are based on primary products. In 2003 only 31% of exports to China and Hong Kong were manufactured to any degree (compared to 41% overall) and only 15% to the extent that they could be regarded as 'elaborately transformed' (compared to around 29% overall). The tables 2 and 3 on the following page provide an indication of the major commodities exported to China and Hong Kong over the past three years.

Table 2: Principal New Zealand Exports to China, years ending December 2001-2003

Description	2001 ($m)	2002 ($m)	2003 ($m)	% Change 2001-03	% of Total Exports 2003
Milk	161.4	209.4	267.1	+65.4	19.5
Wool	209.3	172.9	142.2	-32.1	10.4
Logs	85.5	130.2	120.3	+40.6	8.8
Guts, bladders etc	51.6	58.9	73.6	+42.7	5.4
Sheep skins, raw	65.6	47.5	62.6	-4.7	4.6
Sheep meat	42.6	48.6	50.1	+17.5	3.6
Animal Fat	27.8	37.4	49.6	+78.4	3.6
Chemical wood pulp	90.2	59.6	48.0	-46.8	3.5
Sawn timber	33.9	47.4	38.2	+12.8	2.8
Frozen fish	35.8	40.9	34.6	-3.6	2.5
Fibreboard	28.7	44.1	33.2	+15.8	2.4
Flours, meal etc	41.2	34.4	31.9	-22.6	2.3
Wood pulp	39.9	34.7	26.6	-33.4	1.9
Sheep skins, tanned	29.7	32.6	26.1	-12.1	1.9
Dairy spreads (butter)	4.4	13.6	22.2	+402.7	1.6
Aluminium	18.8	17.2	19.7	+5.2	1.4
Kraft paper	38.8	40.4	18.3	-52.7	1.3
Casein	10.3	14.9	12.8	+24.2	0.9
Beef, live	0	0	12.0	--	0.9
Paper and paperboard	17.8	11.7	10.5	-40.8	0.8
Top 20 sub total	1033.3	1096.3	1099.4	+6.4	80.1
Total Exports	**1349.3**	**1430.1**	**1372.4**	**+1.7**	**100.0**

Source: Statistics New Zealand, Overseas Trade Statistics

Table 3: Principal New Zealand Exports to Hong Kong, years ending December 2001-2003

Description	2001 ($m)	2002 ($m)	2003 ($m)	% Change 2001-03	% of Total Exports 2003
Crustaceans, fresh or live	85.2	90.7	82.3	-3.4	14.7
Horses	10.3	18.5	23.2	+124.5	4.1
Beef skins	21.9	17.0	22.3	+1.8	4.0
Milk	104.5	40.5	22.2	-78.7	4.0
Crustaceans, canned etc	37.3	29.6	22.1	-40.8	4.0
Yachts	0.1	0.3	19.6	+20521.0	3.5
Kraft paper	11.7	10.1	19.6	+67.9	3.5
Fish fillets	34.1	30.5	16.2	-52.5	2.9
Frozen beef	26.2	19.5	15.3	-41.8	2.7
Sheep meat	17.4	15.9	14.1	-19.0	2.5
Apples, pears	16.3	9.5	12.2	-25.1	2.2
Cheese	24.4	18.6	11.9	-51.4	2.1
Fur skins	9.9	10.3	11.5	+15.8	2.1
Dairy spreads (butter)	33.6	19.0	10.6	-68.5	1.9
Leather	0	7.5	9.4	--	1.7
Raw hides	14.8	15.5	9.3	-37.5	1.7
Kiwifruit	12.5	10.9	9.2	-26.4	1.6
Ivory	16.1	11.4	9.2	-43.3	1.6
Molluscs	13.2	12.4	8.2	-37.3	1.5
Logs	17.3	18.7	8.1	-53.0	1.5
Top 20 sub total	506.7	406.4	356.2	-29.7	63.7
Total Exports	**786.4**	**629.0**	**559.0**	**-28.9**	**100.0**

Source: Statistics New Zealand, Overseas Trade Statistics

5.5 The top 20 export commodities to China contribute 80% of all New Zealand exports to the People's Republic. This would imply that China is a less diversified market with export activity largely undertaken by the major primary producers. This is particularly so compared to Australia's equivalent figure of 34%, which reflects that country's position as the major market for New Zealand's more diversified elaborately transformed manufactured exports.

5.6 However, China's figure of 80% is broadly comparable to other significant export markets such as the United States (70%), Japan (78%), Germany (89%), the United Kingdom (80%), Korea (84%), Taiwan (84%), Malaysia (73%), France (91%), and Italy (92%). In fact, for markets such as the United Kingdom (sheep meat), Germany (sheep meat and casein), and France (sheep meat), only one or two products dominate total exports.

Imports

5.7 98% of New Zealand's imports from China are manufactured products. Table 4 shows that the main products entering New Zealand from China are overwhelmingly elaborately transformed manufactures. Table 5 on the following page shows a similar picture for imports from Hong Kong.

Table 4: Principal New Zealand Imports from China, years ending December 2001-03

Description	**2001 ($m)**	**2002 ($m)**	**2003 ($m)**	**% Change 2001-03**	**% of Total Exports 2003**
Computers	89.5	132.5	178.3	+99.2	6.3
Apparel, ladies	82.1	95.3	100.3	+22.2	3.5
Toys	65.4	71.5	73.4	+12.4	2.6
Knitted apparel, jerseys etc	83.9	74.0	71.4	-14.9	2.5
Footwear	58.0	69.4	69.7	+16.7	2.4
Knitted apparel, T-shirts etc	62.0	64.4	63.8	+2.9	2.2
Transmission apparatus	12.3	29.8	61.1	+395.3	2.1
Electric equipment	47.1	59.0	60.3	+28.1	2.1
Plastics articles	51.7	53.4	54.0	+4.5	1.9
Apparel, mens	57.8	56.1	50.7	-12.3	1.8
Television apparatus	35.7	38.7	50.3	+40.9	1.8
Games	13.9	11.6	49.7	+257.9	1.7
Linen	30.7	39.7	40.3	+31.2	1.4
Machinery, parts	24.8	34.5	40.0	+61.7	1.4
Underwear	32.4	31.3	39.9	+23.2	1.4
Seats	17.7	24.9	38.0	+114.6	1.3
Electric apparatus	20.8	39.8	36.0	+73.3	1.3
Photocopying apparatus	20.7	32.8	35.8	+73.0	1.3
Telephone equipment	21.9	33.2	35.7	+63.2	1.3
Lamps	26.3	34.1	33.0	+25.5	1.2
Top 20 sub total	854.5	1026.3	1181.7	+38.3	41.5
Total Imports	**2207.4**	**2590.6**	**2848.5**	**+29.0**	**100.0**

Source: Statistics New Zealand, Overseas Trade Statistics

Table 5: Principal New Zealand Imports from Hong Kong, years ending December 2001-03

Description	2001 ($m)	2002 ($m)	2003 ($m)	% Change 2001-03	% of Total Exports 2003
Machinery, parts	11.1	9.2	16.8	+52.1	11.0
Printed matter	12.9	10.3	9.5	-26.9	6.2
Computers	9.0	5.1	6.7	-26.0	4.4
Toys	2.0	3.0	4.2	+108.0	2.7
Gold	0	1.3	4.0	--	2.6
Electrical apparatus	1.0	2.7	3.9	+287.2	2.6
Unrecorded media	2.2	1.6	3.2	+48.9	2.1
Trunks, etc	2.7	3.6	2.9	+10.9	1.9
Stoves, ranges, etc	0.2	0.9	2.9	+1076.6	1.9
Jewellery	1.1	2.1	2.8	+166.3	1.9
Newspaper	2.5	2.8	2.7	+9.2	1.8
Video recording	0.4	0.6	2.5	+564.2	1.6
Radio-telephony, etc	1.2	1.2	2.3	+96.7	1.5
Watches	5.0	4.2	2.3	-54.3	1.5
Knitted apparel, jerseys etc	1.9	1.3	2.0	+7.1	1.3
Sauces	1.8	2.2	1.9	+5.6	1.2
Transmission apparatus	1.0	0.6	1.6	+68.5	1.1
Diodes etc	2.5	2.7	1.6	-33.9	1.1
Insulated wire, etc	1.3	1.0	1.6	+22.1	1.0
Apparel, women's	1.8	1.5	1.5	-18.2	1.0
Top 20 sub total	61.4	58.0	76.9	+25.3	50.2
Total Imports	**156.4**	**140.1**	**153.4**	**-2.0**	**100.0**

Source: Statistics New Zealand, Overseas Trade Statistics

5.8 Considering the increasingly wide range of products China manufactures and exports, it should not be any surprise that Chinese imports into New Zealand are significantly more diversified by product than New Zealand exports to China. Only 41.5% of imports from China (and 50% of imports from Hong Kong) make the top 20 products. However, this proportion is similar to many of our other significant import sources, including the United States (41%), Australia (42%), Italy (42%), the United Kingdom (47%), Germany (53%), and Taiwan (55%). Japan (78%), Malaysia (70%), France (69%) and Korea (62%) all have rather higher proportions.

5.9 Taken at face value, and ignoring for now the competitive implications for domestic industry, economic theory would imply that the two economies complement each other and that a free trade agreement reducing barriers and costs for each country's exports would make sense both for exporters and consumers.

6. Tariffs on New Zealand Exports to China

6.1 Although tariff rates have been significantly reduced in the wake of China's accession to the WTO, China still imposes significant tariffs on imports, particularly on goods for final consumption. We also understand that unlike most other countries (including New Zealand), which use FOB ('Free On Board') as the basis for valuing for assessment of customs duty, China uses CIF ('Cost Insurance Freight'). Using CIF to value imports for duty results in a higher tariff being paid than would have been the case were FOB used.

6.2 Table 6 below indicates tariff rates for the top-20 commodities exported to China in 2003, both at the time of WTO accession (December 2001) and as they will stand by 2005.

Table 6: Tariffs on Principal New Zealand Exports to China

Description	Tariff Code	Bound Rate at Date of WTO Accession, Dec 2001	Final Bound Rate (Implemented to 2005)	Exports 2003 ($m)
Milk	0402	15-36.7%	10%	267.1
Wool*	5101	38%	38%	142.2
Logs	4403	1%	1%	120.3
Guts, bladders etc	0504	18-20%	18-20%	73.6
Sheep skins, raw	4102	7-9%	7-9%	62.6
Sheep meat	0204	18.6-23%	12-23%	50.1
Animal Fat	1502	8%	8%	49.6
Chemical wood pulp	4703	0%	0%	48.0
Sawn timber	4407	1-5%	1-5%	38.2
Frozen fish	0303	11.7-16%	10-12%	34.6
Fibreboard	4411	8-13.8%	4-7.5%	33.2
Flours, meals and pellets of meat, fish etc	2301	2-5%	2-5%	31.9
Wood pulp	4701	0%	0%	26.6
Sheep skins, tanned	4105	10-14%	10-14%	26.1
Dairy spreads (butter)	0405	36.7%	10%	22.2
Aluminium waste, scrap	7602	3%	1.5%	19.7
Kraft paper	4804	8-11%	2-5%	18.3
Casein	3501	10%	10%	12.8
Beef, live	0102	0-10%	0-10%	12.0
Paper and paperboard	4810	11-11.3%	5-7.5%	10.5

Source: WTO, Statistics NZ Overseas Trade Statistics

* The final bound rate listed for wool is the out of quota tariff rate. The quota quantity for wool was set at 287,000 metric tonnes in 2004. The in-quota tariff rate is 1%, the out-of-quota rate 38%.

6.3 A free trade agreement that eliminated or significantly reduced tariffs would be of benefit for many of New Zealand's major exporters to China, particularly dairy, sheep meat, frozen fish, and manufacturers of some wood-based products. However, the gains of tariff reduction would probably be negligible for exporters of raw materials and intermediate goods such as logs, sawn timber, wood pulp, and aluminium. Wool would benefit providing China's import quota for wool was increased or removed.

6.4 It is also worth considering tariffs on commodities that are not listed above. Some examples are listed in Table 7 below.

Table 7: Tariffs on other New Zealand Exports to China

Description	Tariff Code	Bound Rate at Date of WTO Accession, Dec 2001	Final Bound Rate (Implemented to 2005)
Beef, frozen	0202	31.8-35%	12-25%
Fish fillets	0304	23.3-24%	10-12%
Cheese	0406	34.8-36%	12%
Frozen vegetables	0710	11.8-13%	10-13%
Other fresh fruit, inc kiwifruit	0810	27.1-39%	12-30%
Prepared meat	1602	19.8-21%	12-15%
Food preparations	2106	5-50%	3-35%
Wine	2204	44.6-50%	14-30%
Crude oil	2709	0%	0%
Medicaments	3004	5-10%	3-6%
Cosmetic and toiletries	3304	26.7%	6.5-15%
Plastic packaging	3923	12-16%	6.5-10%
Leather	4104	5-8.4%	5-8.4%
Printed matter	4901	0%	0%
Carpet	5703	21-25%	10-14%
Knitted apparel, jerseys etc	6110	25%	14-16%
Apparel, women’s	6204	21-25%	14-20%
Linen	6302	20-25%	14-16%
Footwear	6403	19-24.5%	15-24.5%
Stainless steel products	7220	10-11.7%	10%
Aluminium structures	7610	26.7%	25%
Agricultural machinery	8433	4.7-10%	3-8%
Electric equipment	8516	8-35%	8-35%
Motor vehicle parts	8708	6-35.7%	6-25%
Aircraft	8802	1-5%	1-5%
Vessels	8901	5-9%	5-9%
Medical and vet instruments	9018	6-11%	5-8%
Furniture	9403	14.7%	0%

Source: WTO, Statistics NZ Overseas Trade Statistics

6.5 This list above shows that although tariffs in most product classifications have been significantly reduced since China’s WTO accession, there is still scope for gains from tariff reduction or elimination for many New Zealand exporters that currently do not export to China to a significant extent.

6.6 Hong Kong does not impose tariffs on its imports so New Zealand exporters do not face any tariff barriers into that territory.

6.7 Business New Zealand agrees that there are likely to be significant gains for many exporters from a free trade agreement with China that reduced or removed Chinese tariffs. While we would support such an outcome, we consider it critical to ensure that issues such as non-tariff barriers are adequately addressed and that New Zealand’s remaining tariffs are not surrendered for minor gains on the Chinese side.

6.8 *Recommendation: Business New Zealand recommends that a free trade agreement with China should provide for a significant reduction or elimination in Chinese tariff levels.*

7. Tariffs on Chinese Imports into New Zealand

7.1 In keeping with the wider economic reforms in the 1980s and 1990s, New Zealand tariffs were either eliminated or significantly reduced. By 1999, 95% of imports were entering New Zealand tariff-free and those remaining tariffs were scheduled for removal by 2006. However, in 2000 the incoming Labour-led Government froze tariffs at existing levels pending a review of tariff policy. Following the completion of this review in 2003, a programme of phased tariff reductions was announced as set out in table 8 below.

Table 8: Tariff Reduction Programme 2006-2009*

Current tariff	July 2006	July 2007	July 2008	July 2009
17-19%	17%	15%	12.5%	10%
10-12.5%	10%	7.5%	5%	5%
5-7.5%	5-7.5%	5-7.5%	5%	5%

Source: Ministry of Economic Development

* On 1 July 2005 alternative specific tariffs (which apply almost solely in the clothing area) will revert to the apparel ad valorem tariffs.

7.2 It is important to consider the level of tariffs on significant imports from China, particularly in any assessment on their effectiveness in protecting New Zealand industries. Table 9 below shows existing normal tariff rates and those that will be in place in 2009. However, China is currently classified as a 'less developed country', so it is subject to preferential tariffs for a number of these products, such as electric equipment, lamps, toys, games, seats, and plastic articles. Nevertheless, it would appear that a significant proportion of Chinese imports into New Zealand are subject to tariffs of varying levels.

Table 9: Tariffs on principal New Zealand Imports from China

Description	Tariff Code	Current Tariff Rate	Tariff Rate July 2006	Tariff Rate July 2009	Imports 2003 ($m)
Computers	8471	0%	0%	0%	178.3
Apparel, ladies	6204	19%*	17%	10%	100.3
Toys	9503	0-7%	0-7%	0-5%	73.4
Knitted apparel, jerseys etc	6110	19%*	17%	10%	71.4
Footwear	6403	0-19%	0-17%	0-10%	69.7
Knitted apparel, T-shirts etc	6109	19%*	17%	17%	63.8
Transmission apparatus	8525	0-7%	0-7%	0-5%	61.1
Electric equipment	8516	0-7%	0-7%	0-5%	60.3
Plastics articles	4202	0-7%	0-7%	0-5%	54.0
Apparel, mens	6203	19%*	17%	10%	50.7
Television apparatus	8528	0%	0%	0%	50.3
Games	9504	0-7%	0-7%	0-7%	49.7
Linen	6302	0-12%	0-10%	0-5%	40.3
Machinery, parts	8473	0%	0%	0%	40.0
Underwear	6212	0-19%*	0-17%	0-10%	39.9
Seats	9401	7-17%	7-17%	5-10%	38.0
Electric apparatus	8517	0%	0%	0%	36.0
Photocopying apparatus	9009	0-5%	0-5%	0-5%	35.8
Telephone equipment	8527	0-10%	0-10%	0-5%	35.7
Lamps	9405	0-7%	0-7%	0-5%	33.0

Source: NZ Customs Service, Statistics NZ Overseas Trade Statistics

* Also includes an alternative specific tariff for some products within this classification group. These will revert to ad valorem tariffs in July 2005.

7.3 Table 10 shows the tariff rates for significant imports from Hong Kong. Hong Kong is not considered to be a less developed country, so tariffs on all of its products will be at the full normal rate. It would appear that a significantly lower proportion of Hong Kong imports are subject to tariffs when entering New Zealand than is the case with respect to Chinese imports.

Table 10: Tariffs on principal New Zealand Imports from Hong Kong

Description	Tariff Code	Current Tariff Rate	Tariff Rate July 2006	Tariff Rate July 2009	Exports 2003 ($m)
Machinery, parts	8473	0%	0%	0%	16.8
Printed matter	4901	0%	0%	0%	9.5
Computers	8471	0%	0%	0%	6.7
Toys	9503	0-7%	0-7%	0-5%	4.2
Gold	7108	0%	0%	0%	4.0
Electrical apparatus	8517	0%	0%	0%	3.9
Unrecorded media	8523	0%	0%	0%	3.2
Trunks, etc	4202	0-7%	0-7%	0-5%	2.9
Stoves, ranges, etc	7321	0-7%	0-7%	0-5%	2.9
Jewellery	7113	0-7%	0-7%	0-5%	2.8
Newspaper	4902	0%	0%	0%	2.7
Video recording	8521	0%	0%	0%	2.5
Radio-telephony, etc	8527	0-10%	0-10%	0-5%	2.3
Watches	9102	0%	0%	0%	2.3
Knitted apparel, jerseys etc	6110	19%*	17%	10%	2.0
Sauces	2103	0-6.5%	0-6.5%	0-5%	1.9
Transmission apparatus	8525	0-7%	0-7%	0-5%	1.6
Diodes etc	8541	0%	0%	0%	1.6
Insulated wire, etc	8544	0-17.5%	0-17%	0-10%	1.6
Apparel, women's	6204	19%*	17%	10%	1.5

Source: NZ Customs Service, Statistics NZ Overseas Trade Statistics

* Includes an alternative specific tariff for some products within this classification group. These will revert to ad valorem tariffs in July 2005.

7.4 The remainder of this chapter discusses related issues around China's growing share of manufactured imports, the growing share of Chinese imports in New Zealand markets, the impact on price levels, the impact on enterprise growth, and the impact on employment growth. The section concludes by discussing whether tariffs on Chinese imports should be reduced or removed and makes several recommendations about tariff reduction.

China's Growing Share of Manufactured Imports

7.5 Table 11 on the following page shows shares for imports from China and Hong Kong (combined) for manufactured products for 1998, 2002 and 2003. It shows that since 1998 China has significantly increased its share of New Zealand imports for almost all categories of manufactured product. China is the overwhelmingly dominant import source for clothing and footwear and has become a major import source for textiles, household appliances, and furniture, as well as for 'other manufacturing'.

Table 11: China and Hong Kong shares of total manufactured imports, years ending December

Product	1998	2002	2003
Food processing	1%	2%	3%
Beverages and tobacco	1%	0%	0%
Textiles (excluding carpets and rugs)	17%	23%	26%
Carpets	2%	2%	3%
Clothing and knitting mill products	51%	69%	72%
Footwear	39%	56%	60%
Leather tanning and fur dressing	2%	5%	10%
Sawn timber and wood products	6%	7%	8%
Paper, paper products and printing	3%	4%	4%
Industrial chemicals and petroleum products	2%	4%	5%
Synthetic resins	0%	1%	1%
Other chemical products	2%	2%	3%
Rubber products	3%	6%	6%
Plastic products	7%	10%	11%
Non-metallic products	8%	14%	16%
Iron and steel	2%	2%	3%
Non-ferrous metals	1%	2%	4%
Metal product manufacturing	8%	15%	17%
Transport equipment	1%	1%	1%
Electronic equipment	6%	13%	16%
Household appliances	14%	24%	25%
Electrical equipment	6%	13%	13%
Agricultural machinery	1%	1%	1%
Industrial machinery and equipment	2%	4%	4%
Furniture	10%	20%	25%
Other manufacturing (incl. confidential items)	30%	28%	39%
TOTAL	**6%**	**10%**	**11%**

Source: Statistics NZ/Business New Zealand

7.6 Chinese products face tariff rates of up to 19% on textiles, clothing, footwear and 7% on furniture. The rates on these products seem particularly high compared to the zero tariffs imposed on imports from Australia, Singapore, the Pacific Islands, and the 'least less developed countries' (LLDC)[2]. However, despite the tariffs China has a large and increasing import share for these and other products.

7.7 An interesting development is China's increasing share of more sophisticated products such as electronic equipment, electrical equipment, and industrial machinery and equipment. As well as having a price advantage, the variety and quality of Chinese manufactured products appears to be widening and improving. A form of 'import substitution' is likely to be occurring, with Chinese imports beginning to displace those from other countries.

Growing Share of Chinese Imports in New Zealand Markets

7.8 When considering the impact of tariffs and their usefulness in protecting local industry, it is useful to consider the market share imported products have in local markets. The following tables 12-14 provide an indication of import penetration overall and for two of New Zealand's most sensitive sectors: (1) textiles, carpet, clothing, footwear, leather and (2) furniture. The tables also

[2] Providing they meet the relevant rules of origin.

show more specifically the growth in market share for imports from China and Hong Kong over the period 1998-2003.

7.9 Table 12 shows that after peaking in 2000, overall import penetration rates have fallen. This is partly due to New Zealand's higher exchange rate since late 2000 reducing the prices of both exports and imports in New Zealand dollar terms[3]. However, New Zealand manufacturers may also have shifted some of their production away from exporting in order to supply the strong domestic economy and reduce their exposure to the higher exchange rate[4]. However, despite these wider trends, China and Hong Kong's share of the domestic market has been growing – from 2.5% in 1998 to 4.3% in 2003.

Table 12: Import Penetration of Domestic Market – All Manufacturing

Year Ending December	New Zealand Manufacturers' Sales for Domestic Market ($m)	Total Manufacturing Imports ($m)	Estimated Domestic Market ($m)	Import Share of Domestic Market (%)	Total Manufacturing Imports from China/HK ($m)	China's Share of Domestic Market (%)
1998	31,531.4	20,967.4	52,498.8	39.9%	1,307.2	2.5%
1999	32,339.3	24,330.0	56,669.3	42.9%	1,573.5	2.8%
2000	33,560.2	26,943.4	60,503.6	44.5%	2,048.8	3.4%
2001	35,061.1	27,883.1	62,944.2	44.3%	2,290.2	3.6%
2002	39,083.3	28,255.4	67,338.7	42.0%	2,673.1	4.0%
2003	41,572.2	27,730.0	69,302.2	40.0%	2,945.8	4.3%

Source: Business NZ/Statistics NZ

7.10 Table 13 tells a similar story for the textiles, carpet, clothing, footwear, and leather (TCCFL) sectors. Despite the anecdotal evidence of an industry in difficulty, the domestic TCCFL industry has picked up overall market share against all TCCFL imports. Again, the higher dollar will have reduced the prices of TCCFL imports when expressed in New Zealand dollars, and the exchange rate and strong domestic trading conditions may have encouraged a more domestic focus[5]. However, once again China and Hong Kong's share of the TCCFL market has bucked these trends and risen from 18.8% in 1998 to 26.0% in 2003.

Table 13: Import Penetration of Domestic Market – Textiles, Carpet, Clothing, Footwear, & Leather

Year Ending December	New Zealand TCCFL Manufacturers' Sales for Domestic Market ($m)	Total TCCFL Imports ($m)	Estimated Domestic TCCFL Market ($m)	TCCFL Import Share of Domestic Market (%)	TCCFL Imports from China/HK ($m)	China's Share of Domestic TCCFL Market (%)
1998	1,277.6	1,650.3	2,927.9	56.4%	551.8	18.8%
1999	1,445.5	1,803.2	3,248.7	55.5%	652.4	20.1%
2000	1,450.5	2,042.7	3,493.2	58.5%	846.3	24.2%
2001	1,678.6	2,077.7	3,756.3	55.3%	928.0	24.7%
2002	1,908.1	2,061.1	3,969.2	51.9%	981.8	24.7%
2003	1,824.7	1,964.3	3,789.0	51.8%	987.0	26.0%

Source: Business NZ/Statistics NZ

[3] Between November 2000 and February 2004 the New Zealand Dollar appreciated by 80% against the US Dollar and 48% against the Trade Weighted Index.
[4] Although this isn't shown in the table, our statistics indicate that total manufactured exports as a percent of total sales have fallen from 44.4% in 2001 to 36.6% in 2003.
[5] TCCFL exports as a percent of total TCCFL sales have fallen from 44.3% in 2000 to 37.7% in 2003.

7.11 Table 14 shows that the furniture industry is becoming increasingly exposed to imports, albeit off a much lower base than either the TCCFL sector or overall manufacturing. Import market share has risen consistently since 1998, despite the local furniture industry more recently reducing its already relatively low exports in order to supply the strong housing-led domestic market[6]. China and Hong Kong's share of the domestic furniture market has increased from 1.4% in 1998 to 4.7% in 2003.

Table 14: Import Penetration of Domestic Market – Furniture

Year Ending December	New Zealand Furniture Manufacturers' Sales for Domestic Market ($m)	Total Furniture Imports ($m)	Estimated Domestic Furniture Market ($m)	Furniture Import Share of Domestic Market (%)	Furniture Imports from China/HK ($m)	China's Share of Domestic Furniture Market (%)
1998	1,009.1	156.2	1,165.3	13.4%	16.1	1.4%
1999	1,143.7	190.2	1,333.9	14.3%	22.4	1.7%
2000	1,009.2	215.2	1,224,4	17.6%	31.9	2.6%
2001	1,016.3	221.2	1,237.5	17.9%	37.1	3.0%
2002	1,165.1	253.3	1,418.4	17.9%	50.9	3.6%
2003	1,199.5	282.4	1,481.9	19.1%	69.7	4.7%

7.12 These statistics indicate that despite gains in market share for New Zealand manufacturers against total imports, China has continued to grow its individual share of New Zealand markets. This strong growth has been in spite of high tariffs.

Impact on Price Levels

7.13 The increase in the exchange rate since late 2000 (which was particularly rapid in 2002 and 2003) and the resulting impact on the prices of imported products (including those from China) has resulted in a fall in 'tradable' inflation, from a peak of +5.4% in late 2000 to -1.6% in early 2004. Tradable deflation over the past year or so has been beneficial from a wider monetary policy perspective in offsetting high and increasing 'non-tradable' inflation, which stood at +5.0% by early 2004[7]. As a result, overall inflation is currently within the Reserve Bank's 1-3% inflation band.

7.14 It is likely that increased imports from low-cost economies such as China have assisted in containing inflationary pressures in New Zealand. This is positive for the economy, in that it should allow for a more accommodating monetary policy than would otherwise be the case.

7.15 Increased imports from China are likely to have benefited not only consumers through lower retail prices, but also those manufacturers sourcing their capital equipment or intermediate goods for production from China: reducing their input costs and making them more competitive (and profitable) both in both domestic and international markets. On the less positive side, anecdotal evidence suggests that competitive price pressures from Chinese imports

[6] Furniture exports as a percent of total furniture sales have fallen from 8.4% in 2001 to 6.5% in 2003.
[7] *Monetary Policy Statement*, Reserve Bank of New Zealand, June 2004.

have squeezed margins for many firms. While this has undoubtedly occurred, the statistical evidence is less clear-cut.

7.16 For example, Statistics New Zealand's Producer Price Index indicates that during the period 1999-2001 a very low New Zealand dollar resulted in both input and output prices rising rapidly. The resulting higher prices for imported capital, intermediate, and consumption goods drove input prices higher than output prices, implying an erosion of firms' margins. However, since 2001 the dollar's appreciation has the opposite effect. As a result, input prices have fallen while output prices have remained relatively stable, implying a rebuilding of margins since late 2001.

7.17 Table 15 below illustrates this change in producer prices for 'all manufacturing' and the sensitive 'textile and apparel manufacturing' sector. It is particularly noticeable how well the latter sector's margins have recovered from September 2001's trough, although it must be recognised that the Producer Price Index is silent on the absolute level of margins, which Statistics New Zealand's Economic Survey of Manufacturing would suggest are lower for the textile and apparel manufacturing[8] compared to all manufacturing.

Table 15: Producers Price Index 1999-2004 – 'All Manufacturing' and 'Textile & Apparel Manufacturing'

	All Manufacturing			Textile & Apparel Manufacturing		
March Quarter	**Inputs Index (Dec 97 = 1000)**	**Outputs Index (Dec 97=1000)**	**Implied Margin v. Dec 97**	**Inputs Index (Dec 97 = 1000)**	**Outputs Index (Dec 97 = 1000)**	**Implied Margin v. Dec 97**
Mar 99	992	1006	1014	939	980	1044
Jun 99	993	1009	1017	946	984	1040
Sep 99	1014	1019	1005	949	986	1039
Dec 99	1031	1040	1009	960	997	1039
Mar 00	1044	1054	1010	972	1003	1032
Jun 00	1065	1069	1004	999	1022	1023
Sep 00	1121	1107	988	1052	1054	1002
Dec 00	1163	1131	972	1083	1076	994
Mar 01	1154	1135	984	1073	1084	1010
Jun 01	1168	1147	982	1092	1096	1004
Sep 01	1213	1145	944	1107	1104	997
Dec 01	1206	1144	949	1088	1101	1012
Mar 02	1198	1145	956	1094	1105	1010
Jun 02	1190	1157	972	1098	1101	1004
Sep 02	1141	1146	1004	1086	1102	1015
Dec 02	1141	1137	996	1089	1112	1021
Mar 03	1124	1134	1009	1076	1102	1025
Jun 03	1118	1138	1018	1082	1108	1024
Sep 03	1114	1129	1013	1074	1102	1026
Dec 03	1112	1126	1013	1035	1088	1051
Mar 04	1101	1131	1027	1008	1080	1071

Source: Statistics NZ Producers Price Index

[8] Statistics NZ's Economic Survey of Manufacturing indicates that while margins between operating income and operating expenditure have averaged around 12% for 'all manufacturing' over the period March 1999 – March 2004, the average margin has been around 10% for 'textile and apparel manufacturing'. However, the Survey does indicate that the sector's margins have improved significantly since December 2001 – averaging 11.7% since that time. This would appear to be consistent with the results for the Producer Price Index.

Impact on Numbers of Enterprises and Employment Levels

7.18 Many factors will have influenced growth in enterprises and employment over recent years. During 1999-2001 a combination of a low exchange rate, good weather and high commodity prices caused an export-led boom and increased consumer spending. As these factors began to wear off after 2001/02, strong net migration gains gave a further impetus to the domestic economy through a buoyant housing market, increased consumer confidence and higher retail sales. Looking ahead, forecasters expect higher interest rates to dampen domestic demand, but that this will be offset by higher commodity prices and a recovering world economy, which will give a further boost via higher exports.

7.19 Import competition and China's influence will have been a factor within these larger trends – albeit a relatively small one overall. However, the influence of Chinese imports is likely to have been considerably more prominent within specific sectors, such as textile, clothing, footwear and leather manufacturing.

7.20 Tables 16 and 17 show growth in the number of geographic enterprises and employment since 1997 for all sectors, all manufacturing, and the TCCFL sector. The tables show that whereas growth in the overall economy has been robust, manufacturing (particularly employment) was weak between 1997 and 2001 before rising in 2002 and 2003, and for TCCFL the situation was particularly grim between 1997 and 1999, with employment being particularly hard-hit. Although the sector's decline appears to have since levelled off, there has yet to be much sign of recovery (particularly for employment).

Table 16: Growth in Geographic Enterprises 1997-2003[9]

As at February	All Sectors	Annual % Increase	All Manufacturing	Annual % increase	TCCFL Sector	Annual % Increase
1997	256,370	--	20,924	--	2,128	--
1998	276,263	+7.8%	21,639	+3.4%	2,112	-0.8%
1999	278,859	+0.9%	21,360	-1.3%	2,018	-4.5%
2000	302,887	+8.6%	22,385	+4.8%	2,095	+3.8%
2001	302,152	-0.2%	22,120	-1.2%	2,007	-4.2%
2002	309,749	+2.5%	22,094	-0.1%	1,999	-0.4%
2003	323,839	+4.5%	22,569	+2.1%	2,018	+1.0%

Source: Statistics NZ Business Demography Statistics

Table 17: Growth in Full-Time Equivalent Employees 1997-2003

As at February	All Sectors	Annual % Increase	All Manufacturing	Annual % increase	TCCFL Sector	Annual % Increase
1997	1,335,180	--	244,510	--	23,470	--
1998	1,360,800	+1.9%	241,740	-1.1%	21,450	-8.6%
1999	1,366,450	+0.4%	232,660	-3.8%	20,470	-4.6%
2000	1,406,300	+2.9%	232,540	-0.1%	20,940	+2.3%
2001	1,418,240	+0.8%	233,930	+0.6%	20,200	-3.5%
2002	1,467,890	+3.5%	242,180	+3.5%	20,230	+0.1%
2003	1,527,200	+4.0%	248,020	+2.4%	19,730	-2.5%

[9] Business demography statistics as at February 2004 are due for release in October 2004.

Should Tariffs be Retained?

7.21 The key question that all this boils down to is: 'should New Zealand remove its remaining tariffs on Chinese imports faster and by more than the decisions made by the Government in response to its Post-2005 Tariff Review'?

7.22 Tariffs impose costs on the economy, although it would appear that these costs are now relatively low. A report by Infometrics for the Ministry of Economic Development found that GDP would rise by only 0.1% in the event of tariffs being removed[10]. The report suggested that New Zealand had already secured most of the possible gains from lower import protection.

7.23 Not surprisingly, the report also observed that the clothing and footwear industries would incur the greatest output losses under a tariff free environment, with the reductions in output being about 8% in each case. On the other hand, it was expected that 'small gains' would accrue to industries such as forestry, dairy and meat processing, base metals, and machinery and equipment.

7.24 Overall, Infometrics recommended that tariffs should be reduced to zero by 2010. However, when it announced its decisions on the Post-2005 Tariff Review, the Government took a somewhat more cautious and measured approach, announcing a phased reduction of tariffs to 2009, as set out in table 8 on page 14. A further review in 2006 will determine tariff rates after 2009.

7.25 In commenting on the Infometrics report and the Government's decisions, we note that Business New Zealand's 2002 submission to the Post-2005 Tariff Review made the following key points:

- Further tariff reductions will contribute little to economic growth if there is not a broader commitment to growth enhancing policies.
- A single focus on tariff reductions will have a greater dislocation impact on tariff sensitive sectors if there is not a commitment to broader pro-growth policies.
- Greater urgency needs to be given to bilateral and multilateral trade agreements that will achieve reductions in tariff and non-tariff barriers faced by exporters.
- The impact of tariffs on the economy is now small and the economy is now very open to imports.
- It is important for there to be a clear linkage with industry strategies that recognise the need for ongoing support for industries in transition and improved funding for training for the existing workforce.

7.26 The Infometrics report was consistent with the assessment made in our submission that the New Zealand economy is already largely open to imports and that the macroeconomic gains of tariff elimination are likely to be relatively small.

[10] *Review of Import Tariffs Beyond 2005*, Infometrics, December 2002.

7.27 Business New Zealand accepts that most firms perceive tariffs to be less important to their business than, for example, the company tax rate, availability skilled staff, business compliance costs, and exchange rate volatility. This is true even for many firms in tariff sensitive sectors, although we note that this does not mean that tariffs are not very important to the viability of some firms, particularly those that are operating on the margin.

7.28 A number of firms in the TCCFL sector have expressed to us the importance of tariffs to their ongoing viability. It is likely that the levelling off in the decline in that sector since 2000 and its relative resilience in the face of import competition has been a result of the 2000-05 tariff freeze and the development of industry strategies providing some medium-term certainty about tariff policy and demonstrating commitment to the sector.

7.29 Business New Zealand agreed with the Infometics report that businesses require certainty and that any programme for tariff reductions should be well signalled with adequate time for adjustment. The Government's announced programme for reductions to 2009 provides such certainty, at least in the medium-term and as such it is welcome.

7.30 Meanwhile, Business New Zealand notes that the Government has made a proposal to the WTO that New Zealand would be willing to eliminate tariffs on non-agricultural products on a reciprocal basis. The Government has said that this goal would be achieved through progressive liberalisation over an (unspecified) implementation period. Business New Zealand supports this ambitious initiative, although we would want to ensure that the impacts on New Zealand's sensitive sectors were adequately considered.

7.31 Further to this point on reciprocity, we also submit that decisions on future tariff levels should also take account of decisions by our significant trading partners (e.g., Australia) on tariff and non-tariff barriers and consideration of developments in multilateral agreements, including WTO negotiations.

7.32 Finally, the Infometrics findings and the Government's subsequent post-2005 tariff decisions do not change our view that a programme of tariff reductions should be considered as part of a wider package of growth enhancing policies and that such a programme should be closely linked with sector strategies aimed at assisting 'industries in transition'.

7.33 Business New Zealand recognises that much useful work is being undertaken on industry strategies to help industries in transition (such as TCCFL and furniture). Wider initiatives such as Growth and Innovation Framework, the Small Business Advisory Group and the Workplace Productivity Working Group have the potential to be useful and the Government's trade policy framework is generally pro-business.

7.34 However, we are not convinced that the Government has made an adequate enough commitment to growth promoting policies, particularly where they would be 'inconsistent with government policy'. In January 2004 Business

New Zealand identified the following key issues for business, which need urgent action[11]:

- High taxes;
- Anti-business employment legislation;
- Holidays Act adds cost and complexity;
- Safe workplaces are not rewarded;
- Electricity costs are escalating;
- Roading infrastructure is failing;
- RMA is obstructing development;
- Local authority rates are rising fast;
- Skill shortages; and
- Negative attitudes to business.

7.35 If tariffs on Chinese imports are to be reduced, then the business community, particularly those in tariff-sensitive sectors, requires action on these key issues to improve productivity and competitiveness both in domestic and international markets.

7.36 Furthermore, Business New Zealand considers that any negotiated reduction in tariffs beyond those already announced to 2009 must be phased to provide certainty to business. More importantly, New Zealand should commit China to a significant reduction or the complete elimination of its tariff and non-tariff barriers to ensure that there is a level playing field for market access in each country. Put simply, New Zealand should not just give away its tariffs unless China agrees to do likewise.

7.37 *Recommendation: Business New Zealand recommends that any negotiated reduction in New Zealand tariffs on imports from China beyond those already announced to 2009 should be dependent on:*

(a) Agreement from China that it will significantly reduce or eliminate its tariff and non-tariff barriers;
(b) The implementation of a phased tariff reduction programme to provide businesses with certainty and time to adjust.
(c) Greater commitment by the Government to growth promoting policies to improve business productivity and competitiveness; and
(d) Continued support for the development and implementation of industry strategies that recognise the need for ongoing support for industries in transition and improved funding for training for the existing workforce.

[11] *10 Key Issues for SMEs*, Business New Zealand, January 2004. While targeted at a small business audience these issues are of equal concern to the wider business community.

8. Non-Tariff Barriers

8.1 In the context of any free trade agreement it will be important to ensure that non-tariff barriers are addressed. While tariffs are the most visible of trade barriers, they are not necessarily the barriers that cause the most distortion and impediment to trade.

8.2 Non-tariff barriers are government requirements that directly or indirectly impact upon trade. They can be many and varied and are often justified for reasons that on the face of it might have very little to do with protectionism. The most obvious non-tariff barriers include:

- Explicit quantitative restrictions (such as import bans and quotas);
- Import licensing or tendering;
- Price controls;
- State trading monopolies (both export and import);
- Subsidies from central and local government for state-owned enterprises;
- Requirements for foreigners to engage local agents; and
- Other restrictions on establishing and maintaining a business presence, particularly in the area of services.

8.3 All of these non-tariff barriers feature in China, although its economic reforms and its accession to the WTO have reduced some of these barriers or put in place a timetable for liberalisation. Nevertheless, any free trade agreement must address these issues in order to make it easier and cheaper for New Zealand businesses to export and do business in China.

8.4 A further issue brought to our attention is that of differing payment systems. We understand that different systems operate between the eastern, coastal provinces and the western, interior provinces. In the coastal areas foreigners are able to successfully transact business providing due diligence is followed and the local party has access to foreign exchange. This is apparently not the case further inland. This potential non-tariff barrier needs to be addressed, particularly as the recently agreed Trade and Cooperation Framework between New Zealand and China places emphasis on 'western China development and the revitalisation of old industrial bases in north-east China'.

8.5 Other less obvious non-tariff barriers include phytosanitary, biosecurity, and trade security requirements, as well as any fees and charges for services relating to such requirements. Most countries, including New Zealand, have such requirements and they are regarded as acceptable providing they do not amount to protectionism, a tax on trade, or impose compliance costs that are overly onerous.

8.6 Last year's SARS outbreak (which most regard to have started in China), New Zealand's vulnerability to imported animal diseases such as foot and mouth, and the impact of exotic insects on trees all highlight the importance of New Zealand remaining vigilant in maintaining a secure border. Business New Zealand would be most concerned if a free trade agreement with China were to compromise the robustness of New Zealand's phytosanitary and biosecurity regimes.

8.7 On the other hand there are strong arguments for considering this country's Import Transaction Fee and further proposed charges for recovering the Government's costs of border security to be taxes on trade. Border security is primarily of benefit to New Zealand as a whole. As such it should be funded from general taxation.

8.8 *Recommendation: Business New Zealand recommends that a free trade agreement with China should include agreement for the reduction or elimination of non-tariff barriers.*

9. Rules of Origin and Anti-Dumping

9.1 Business New Zealand considers it to be very important for the integrity of any free trade agreement with China to include provisions on rules of origin and anti-dumping.

Rules of Origin

9.2 Rules of origin are very important for ensuring that tariff preferences are not abused by companies manufacturing products substantially in third-countries with cost advantages and then representing them as products of the exporting country, so unjustly claiming a tariff preference.

9.3 China has traditionally been a low-cost economy and has had particularly strong labour cost advantages and economies of scale over virtually all other countries. Few countries have been able to compete on price terms alone and as a result the incentive for Chinese manufacturers to locate operations in third countries has been low to minimal. Therefore rules of origin have tended to be designed with countries like China in mind.

9.4 One of the best examples was the case of New Zealand's negotiations with Hong Kong for a Closer Economic Partnership. Hong Kong was unable to reassure New Zealand that its border controls were robust enough to prevent Chinese products from entering New Zealand as 'Hong Kong' products, so claiming a substantial tariff preference. This was the key reason for the stalling of negotiations.

9.5 While China is still very much a low-cost economy, its labour cost advantage is likely to be eroding, particularly for lower cost and lower quality products. The incentives for Chinese manufacturers to locate at least part of their operations in even lower cost countries are likely to grow over time. It would therefore be in New Zealand's interest to include provisions on rules of origin in a free trade agreement with China (of course, China is likely to insist on rules of origin to ensure, for example, that Australian exporters are not able to use New Zealand as a back door to enter China under a tariff preference).

9.6 Enforcement of the rules of origin is critical to their effectiveness. Customs practices and procedures must be robust enough to ensure that the rules of origin are not abused and both countries must be assured that the others' Customs services have the capacity and integrity to enforce them.

9.7 Business New Zealand does not wish to express a preference for any specific rules of origin regime. We consider it to be more important for New Zealand to have a consistent set of rules of origin across all trade agreements. Doing so would help reduce compliance costs.

9.8 *Recommendation: Business New Zealand recommends that a free trade agreement with China should include robust rules of origin provisions that are enforceable.*

Anti-Dumping

9.9 Rules around anti-dumping are an important competitive safeguard to ensure that imports are not sold in a market below cost. Imported products that are sold below cost (i.e., 'dumped' on an offshore market) subject both local industry and imports from other countries to unfair and injurious competition. At its most predatory, dumping can result in the elimination of competitors, leaving the market open to the dumper, which might then price as it wishes to more than recoup any losses incurred while dumping.

9.10 Anti-dumping safeguards have become more important as tariffs and non-tariff barriers have been reduced. According to statistics by the Ministry of Economic Development, products from China have been subject to a number of anti-dumping investigations[12]. Noting that anti-dumping action was removed from trans-Tasman trade in 1990, Business New Zealand considers it to be important for New Zealand to retain the right to take anti-dumping action in any agreement with China.

9.11 *Recommendation: Business New Zealand recommends that New Zealand should retain the right to take anti-dumping action in respect of trade between New Zealand and China.*

[12] *Anti-Dumping Law and Practice in New Zealand*, Ministry of Economic Development website, http://www.med.govt.nz/buslt/trade_rem/guides/adlpinz.html

10. Services

10.1 The services sector is becoming increasingly important in the international economy. New Zealand's services sector is open compared to most other countries, with few barriers to foreign services providers. Providing immigration and qualification requirements are met, national treatment is generally extended to foreign suppliers of professional services.

10.2 China is a very different story, with significant restrictions both horizontally across all sectors and vertically at an industry level. China's schedule of specific commitments on services within its WTO accession documentation lists a multitude of market access limitations and a number of limitations on national treatment.

10.3 A free trade agreement with China should seek to facilitate trade in services between New Zealand and China. Barriers that restrict services trade should be removed or relaxed to improve market access, predictability and transparency. Ideally, such an agreement would also ensure that New Zealand companies are granted the same level of recognition as Chinese companies for government contracts – this would offer significant benefits for New Zealand service providers in what is a very difficult market for foreigners to enter without connections to the 'right people'.

10.4 *Recommendation: Business New Zealand recommends a free trade agreement with China should remove or relax barriers restricting trade in services.*

11. Investment

11.1 Business New Zealand considers that the encouragement of investment should be covered in a free trade agreement with China, although we understand that New Zealand and China already have an investment promotion and protection agreement. We agree that a free trade agreement should seek to improve the investment climate through:

(a) Cooperation and information exchange to improve the climate for two-way investment through enhancing transparency and predictability, improving decision-making processes, and protecting investments and investors; and

(b) Taking action to build linkages between Chinese and New Zealand agencies.

11.2 *Recommendation: Business New Zealand recommends that a free trade agreement with China should seek to improve the investment climate.*

12. Intellectual Property

12.1 A very important issue that must be addressed with some urgency is the protection of intellectual property. Intellectual property rights are an important facilitator for economic growth. Without adequate protection there is little incentive for businesses to undertake costly research and development and receive some reward for the risk of innovating. The return is substantially diminished if ideas and products can be ‘ripped off’ with impunity.

12.2 Unfortunately, China’s track record of protecting intellectual property has been poor (although to be fair it is not alone in this regard). Anyone who has visited China would be familiar with how easy it is to buy cheap imitation products on the street that are of poor quality compared to the original article. A recent example with direct relevance to New Zealand has been the case of counterfeit New Zealand product labelling that has been ‘for sale’ in China. This is serious as it compromises the reputation of New Zealand products in both the Chinese and other international markets.

12.3 As well as make provision for intellectual property rights in any free trade agreement, New Zealand should also work closely with China bilaterally, regionally and multilaterally to improve both its motivation and its capacity to protect intellectual property rights.

12.4 *Recommendation: Business New Zealand recommends that provisions on protecting intellectual property rights should be included in a free trade agreement with China and that China is encouraged to improve its track record in this regard.*

13. Sustainable Development – Labour and Environmental Standards

13.1 Business New Zealand recognises that the Government places a high importance on labour and environmental standards, but we would be concerned if such considerations became the overriding factor in whether to negotiate a CEP with any economy.

13.2 Not withstanding the fact that free trade has proven to be beneficial to developing countries in raising living standards, opponents of free trade have used labour and environmental standards as a smokescreen to mask their inherent protectionism. While on one hand complaining about the gap between rich and poor, the anti-globalisation lobby has restricted their ability to trade and grow their economies by insisting on adherence to strict labour and environmental standards.

13.3 As a matter of principle, we submit that New Zealand should not seek to include labour and environmental standards as part of a free trade agreement with China. We consider that the International Labour Organisation provides a more appropriate mechanism to address labour standard issues on an international level. The framework of multilateral environment agreements provides a similar mechanism for consideration of environmental issues.

13.4 *Recommendation: Business New Zealand recommends that a free trade agreement with China should not include provisions on labour and environmental standards.*

14. Treaty of Waitangi

14.1 Previous negotiations for closer economic partnerships have included provisions for the Treaty of Waitangi. In the case of China, the consultation document states that New Zealand will seek a provision to enable the Government to implement policies related to Maori.

14.2 Business New Zealand is opposed to the inclusion of a Treaty of Waitangi clause into a free trade agreement with China. We would not support any measures that would allow the Government to give any special interest group preferential treatment. This could be construed to be protectionism by another name, and Business New Zealand would be concerned if such a clause were to be viewed by China with suspicion and increased the risk of our negotiations having to make important concessions in other areas.

14.3 There is no mention in the consultation document of what form any favourable treatment would take. If these measures were in the form of non-tariff barriers or subsidies, this could place additional costs on the economy, as well as result in the misallocation of resources.

14.4 *Recommendation: Business New Zealand recommends that a free trade agreement with China should not include a provision on the Treaty of Waitangi.*

15. Dispute Resolution

15.1 Business New Zealand considers it important for a free trade agreement with China to provide for a disputes resolution process. Such a system would be important for addressing problems around market access, non-tariff barriers, intellectual property breaches and trade remedies (e.g., disputes over anti-dumping).

15.2 *Recommendation: Business New Zealand recommends that a free trade agreement with China should include provisions on a disputes resolution process.*