

# Australia–China trade: opportunity, risk, mitigation, ballast – progress?

James Laurenceson and Weihuan Zhou

## Introduction

From the vantage point of the present, it is easy to forget the exuberance regularly evinced in Australia’s discussion of trade with China not all that long ago. Political leaders led the way. In June 2015, at the signing ceremony of the China–Australia Free Trade Agreement (ChAFTA), Prime Minister Tony Abbott addressed the Chinese side that had gathered in Canberra:

What you have collectively done is history making for both our countries, it will change our countries for the better, it will change our region for the better, it will change our world for the better ... We seize this opportunity of more trade and more investment with China ... One day we will be able to say to our children and grandchildren, that yes, we were there the day this extraordinary agreement was signed between our two countries.<sup>1</sup>

Despite bilateral political ties beginning to sour in the second half of 2016, at a joint press conference in September 2019 – one where US President Donald Trump had declared China to be a “threat to the world” – Prime Minister Scott Morrison remained focused on the economic upside: “We work well with China ... we have a great relationship with China. China’s growth has been great for Australia.”<sup>2</sup>

A keen appreciation of the benefits that robust trade ties with China delivered extended to the public at large. In the 2018 Lowy Institute poll, 82 per cent of respondents considered China as “more an economic partner than a security threat”.<sup>3</sup> Just 12 per cent nominated the opposite. The previous year a poll by the United States Studies Centre asked respondents whether they had a more favourable view of increased trade with the United States or China.<sup>4</sup> The proportion choosing China was 10 percentage points higher than the proportion choosing

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1 Abbott 2015.

2 White House 2019.

3 Lowy Institute Poll 2022.

4 Jackman, Flake et al. 2017.

the United States.

That said, almost immediately after China overtook Japan to become Australia's largest trading partner in 2007, this appreciation of the benefits became tinged with worry about what could go wrong. In 2013, the Lowy Institute commissioned University of Sydney academic Jamie Reilly to provide an assessment of the risk "that the Chinese government will manipulate its trade and investment to undermine Australian autonomy or security".<sup>5</sup> While Reilly concluded the worries were "overblown", they persisted. In a moment of candour in November 2014, Prime Minister Abbott told visiting the German Chancellor, Angela Merkel, that Australia's policies towards China were driven by both "fear and greed".<sup>6</sup> From 2017 there was also an up-tick in media reporting alleging that Beijing was disrupting market access for a variety of Australian exports, including beef, wine and coal, in order to send a political message to Canberra.<sup>7</sup> Even if the evidence supporting such claims subsequently proved equivocal, by the time of the 2019 edition of the Lowy Institute Poll, 74 per cent of respondents agreed with the statement "Australia is too economically dependent on China".<sup>8</sup>

But it was events in 2020 that dramatically elevated the frame of risk.<sup>9</sup> First, the COVID-19 pandemic emanating from China in January of that year was followed by shortages of some goods in Australia. Some commentators linked these shortages to Australia's exposure to China as a supplier. In March 2020, the executive director of the Australian Strategic Policy Institute (ASPI), Peter Jennings, claimed that "China locks its factories down and within days Australia faces shortages of medical supplies, building components and consumer products of all types".<sup>10</sup> Second, in May that year Beijing launched a campaign of disruption targeting Australian exports.<sup>11</sup> What started with barley and beef subsequently expanded to around a dozen goods by year's end. While the pace of escalation slowed in 2021, none of the earlier moves had been rescinded as of September 2022. In the face of Australian complaints, Beijing responded by claiming the measures were legitimate and permitted by international trade rules. Nor was the disruption one-sided: Canberra was blocking Chinese investment with increasing regularity<sup>12</sup> and Chinese goods remained the most prominent target of

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5 Reilly 2013.

6 Garnaut 2015.

7 Laurenceson, Zhou and Pantle 2020.

8 Kassam 2019.

9 The background and trigger for the elevation of the frame of risk is discussed in Zhou and Laurenceson 2022.

10 Jennings 2020b.

11 Laurenceson and Pantle 2021.

12 Uren 2020.

punitive Australian anti-dumping tariffs, despite expectations in Beijing that the rules embedded in ChAFTA would result in fewer such cases. The negative impact on Australian public opinion of the above events was revealed in a June 2021 poll found by the Australia–China Relations Institute. The poll found that, despite China remaining the largest customer for Australian goods and services by far, a majority (53 per cent) of respondents agreed with the statement “Australia’s economic relationship with China is more of an economic risk than an economic opportunity”.<sup>13</sup> Only one-fifth disagreed. In a dramatic reversal of the 2018 results, the 2021 edition of the Lowy Institute Poll reported that just 34 per cent of Australians regarded China as “more an economic partner than a security threat”.<sup>14</sup>

To date, the Australian government has maintained a bipartisan position that it wishes for robust trade engagement with China to continue, albeit engagement that accounts for risk and does not come at a cost of modifying political choices in the face of coercive pressure. When at the end of 2020 one National Party senator called for Australia to place an export tax on iron ore sales to China in retaliation for Beijing’s disruption of other Australian exports, this was immediately rejected by the Minister for Resources and Water.<sup>15</sup> Early on in Beijing’s campaign of disruption, Prime Minister Scott Morrison maintained an insistence that commercial interactions with China involve “a judgement Australian businesses can only make ... those are not decisions that governments make for businesses”.<sup>16</sup> In September 2021, in a speech otherwise calling for businesses to bolster their resilience through greater market diversification, Treasurer Josh Frydenberg acknowledged that many Australian businesses had “worked hard to access the lucrative Chinese market”. This, he said, had “brought great benefits to them and to Australia overall. And they should continue to pursue these opportunities where they can.” In March 2022, even after several months of fanning a narrative that China was a strategic and security threat in the lead-up to a federal election, Morrison continued to back this position: “The ongoing engagement between private industry and business with markets like China is very important and I will continue to encourage that, but obviously the political and diplomatic situation is very, very different...”<sup>17</sup> Nonetheless, the government did send a strong message to businesses regarding the implications of heightened geopolitical risk. In March 2021, Australia’s ambassador to China, Graham

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13 Collinson and Burke 2021.

14 Lowy Institute Poll 2022.

15 McCulloch 2020.

16 Prime Minister of Australia 2020.

17 Hastie 2022.

Fletcher, told a business forum, “You’ve just got to imagine that, unexpectedly, you may lose your China market for no good reason other than that Beijing has decided to send a message to Canberra”.<sup>18</sup> The new Labor government elected in May 2022 has not yet shown any sign of deviating from the above script. Addressing the Australia–China Business Council in September 2022, the Assistant Minister for Foreign Affairs, Tim Watts, said that commercial relationships were seen as “complementary” to the government’s efforts to stabilise the broader relationship and encouraged those in the audience to “stay engaged in the China market, while accounting for risk”.<sup>19</sup>

Yet calls outside government for Canberra to change tack and adopt a more interventionist and prescriptive approach that drives trade ties away from China have not dissipated. In May 2020, ASPI’s Jennings asserted that “economic dependence on China is dangerous” and that “steps must be taken to reduce that dependence”.<sup>20</sup> There is also the possibility that a future US administration, particularly a Republican one, might head in a more radical “decoupling” direction – and pressure Australia to follow. In August 2021, Matt Pottinger, a former senior Trump administration national security official wrote on economic engagement with China: “Elected leaders must now take the next step...Because companies are economic actors, not political ones, it is the government’s responsibility to establish guidelines for engaging with adversaries.”<sup>21</sup> In some quarters the extent of Australia’s trade relationship with China is already seen as an issue for the Australia, New Zealand, United States Security Treaty (ANZUS) alliance . In June 2019, Charles Edel and John Lee of the United States Studies Centre passed on the message: “The United States would like Australia...to lessen its commercial dependence on China”, before themselves going on to advocate for “active diversification”.<sup>22</sup> The Biden administration is putting increased store on self-sufficiency and “friend-shoring”, the latter of which aims to build supply chains between the United States and security allies like Australia, and that have China carved out.<sup>23</sup> There has also been increased discussion of more security-focused arrangements, such as the ANZUS alliance, the Quadrilateral Security Dialogue (the Quad) and the Five Eyes intelligence arrangement, being expanded into the economic realm.<sup>24</sup>

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18 Dziedzic 2021.

19 Watts 2022.

20 Jennings 2020a.

21 Pottinger 2021.

22 Edel and Lee 2019.

23 Condon, Kim and Kim 2022.

24 Laurenceson 2021b.

With this as background, in what follows we argue that calls for Canberra to deploy public policy with the objective of reducing trade with China in order to mitigate risk are, in general, poorly conceived. To be clear, we do not suggest that trade engagement with China does not present risks. Rather, our contention is that most Australian businesses – the actors that overwhelmingly undertake trade – are already acutely aware that geopolitical fallout might affect their operations and that at a firm, industry and national level there exists a variety of mechanisms to mitigate these risks. Mitigation mechanisms stem from both economic and legal sources and collectively they bolster Australian resilience in the face of coercive measures by Beijing. During a period of prolonged breakdown in senior political-level dialogue,<sup>25</sup> trade engagement delivered not only ongoing direct economic benefits but also ballast to the broader relationship. Further, despite bilateral trade disruption, Australia and China have an alignment of interests in supporting regional and global trade architecture, presenting opportunities ripe for cooperation and to positively shape Australia’s external environment.

### **China trade risk: economic sources of mitigation**

A narrative advanced by some Australian commentators, particularly those coming from a strategic or national security background, is that businesses are naive or indifferent to the risk that this engagement with China involves, at a firm or more systemic level or both. This then leads to calls for government intervention to mitigate the risk by reducing trade “dependence”.

ASPI’s Michael Shoebridge, writing in April 2020, is a typical example.<sup>26</sup> After the initial economic shock caused by the COVID-19 pandemic, Shoebridge warned that Australians should “expect myriad calls to restart our economic relationship with China as it was before”. These calls would come “from treasury types in Western governments as well as those with deep self-interest – a lot of wealthy people and leaders sprinkled across our corporate and university landscapes”. He exhorted, “we must discount them as we make decisions”. This was because “the Chinese state has created unacceptable risks for the rest of us and it will continue to do so unless it changes or until we reduce our dependence on activities within its jurisdiction”.

Anecdotes of Australian businesses seemingly making poor decisions with respect to

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<sup>26</sup> Shoebridge 2020.

China trade engagement are not hard to find, particularly with the benefit of hindsight. But arguments like that advanced by Shoebridge struggle at a first-principles level. The Australian government's Productivity Commission emphasises that a starting point for effective mitigation is the proposition that risks are best managed by those with direct incentives and capabilities to assess and respond to them, and typically this means businesses, not bureaucrats.<sup>27</sup> The owners of the Australian businesses that engage with China, either as a customer or supplier, do so with their own money on the line. When Beijing effectively blocked Australian barley with tariffs of around 80 per cent in May 2020, it was farmers who faced the fallout: there was no taxpayer-funded bail-out in the offing. Given this, the suggestion that businesses would gloss over risks is a puzzling one. That Australian businesses engaged in trade with China, in fact, take risk seriously was confirmed in a report authored by journalist Glenda Korporaal in December 2021.<sup>28</sup> Korporaal interviewed a dozen business leaders operating at the coalface of trade with China, revealing a sharp appreciation that geopolitical risk was rising. At the same time, oftentimes it still ranked below other challenges in their risk matrix, such as the impact of unexpected shifts in Chinese government regulations. Businesses have also exhibited creative strategies in handling geopolitical risk. When bottled wine from Australia was hit with prohibitive anti-dumping tariffs in late 2020, Treasury Wine Estates pivoted to sourcing product from the United States and France, as well as investing in China's own domestic vineyards.<sup>29</sup> And in any case, the overall level of risk still needed to be compared with the expected returns from engaging with China versus the risk/return equation presented by alternative markets. In August 2021 the chief executive officer of trans-Tasman dairy manufacturer, A2, told investors:

There's no avoiding the fact that the China infant nutrition market is – even though it is challenging at the moment – by far the largest and most interesting opportunity for us. So it is both the biggest risk and the biggest opportunity for us that we must embrace. We have to invest in that to capture that opportunity going forward.<sup>30</sup>

In a November 2021 survey by the Australian Trade and Investment Commission, the Export Council of Australia and the University of Canberra, a higher proportion of businesses looking to diversify to South Korea and Japan, along with other regularly touted alternatives to China such as Taiwan and Vietnam, reported experiencing more barriers in these markets

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<sup>27</sup> Productivity Commission 2021.

<sup>28</sup> Korporaal 2021.

<sup>29</sup> Korporaal 2022.

<sup>30</sup> Lynch 2021.

than did business looking to diversify to China.<sup>31</sup>

It is the case that privately-owned businesses do not seek to eliminate risk entirely. Rather, when deciding whether to perform additional risk assessment and mitigation, they compare the expected benefits and costs from doing so. Society might, therefore, insist that a limited number of supply chains are closer to fail-safe than private-sector decision-making delivers and be prepared to incur the costs this necessitates. But this can only serve as justification for highly targeted interventions and is a far cry from the vague calls cited above.

One claim made with particular stridency is that Australian businesses might embrace political lobbying as a tool of risk mitigation, either in the form of demanding taxpayer-funded bail-outs if their China bets go wrong or by putting pressure on Canberra to shift its political positions to ones more agreeable to Beijing. In May 2020, ASPI's Jennings said that business leaders had advocated for a "just shut up and take money from China" approach.<sup>32</sup> After leaving office, former prime minister Malcolm Turnbull also complained:

An Australian prime minister who ends up in conflict with China cannot expect any support or solidarity from the Australian business community. Overwhelmingly, they're totally invested in the economic benefits of the relationship and they'll always blame their own government if problems arise.<sup>33</sup>

Again these assertions struggle once subject to cursory scrutiny. First, in a liberal democracy like Australia, businesses are entitled to press their interests, just as other groups are entitled to push back against such advocacy. Second, while business interests are not the entirety of the nation's interests, they are not in contradiction to it. In June 2020, former director-general of the Australian Security Intelligence Organisation (ASIO) and secretary of Defence Dennis Richardson advised corporate executives that when they are slurred as unpatriotic for emphasising the value of the China trade relationship, "they should punch their accuser right on the nose...figuratively that is".<sup>34</sup> He then suggested they remind their critics of the employment that their business provides and the tax it pays. Third, the weight of evidence suggests that after Beijing began disrupting trade, rather than amplifying their criticism of Canberra, businesses did the opposite in recognition of the fact that amplification would only invite more frequent pressure in the future.<sup>35</sup> Finally, and perhaps most

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31 Australian Trade and Investment Commission (Austrade), Export Council of Australia and the University of Canberra 2021.

32 Packham 2020.

33 Turnbull 2021.

34 Richardson 2020.

35 Power 2020.

importantly, even to the extent that some business owners may continue to engage in such lobbying, in the end it is elected officials who get the final say. And the survey evidence since 2020 shows that the public opinion has swung in behind the firm position that Canberra has adopted towards Beijing. The fact that in the 2022 Australian federal election campaign the opposition Labor party was overwhelmingly in agreement with the government's policies towards China makes the point that it saw no electoral advantage in advocating for positions that Beijing might prefer.<sup>36</sup>

The campaign of trade disruption unleashed by Beijing since May 2020 also provides an instructive case study to gauge the scale of systemic risks that Australia's exposure to China as a customer creates. In its breadth and duration, this campaign is unprecedented in the history of modern Chinese economic statecraft. Yet the first outcome to emphasise is that the aggregate value of Australia's goods exports to China in 2020 was steady – and in 2021 jumped by 21 per cent to hit a record high of A\$177 billion.<sup>37</sup> Similarly, the value of Australia's imports from China rose by 7 per cent in 2020 and a further 8 per cent in 2021 to hit a record high of \$91 billion. That total goods exports and imports reached record levels during a campaign of trade disruption reflects the mitigating factor of China's own self-interest, as well as a fortuitous increase in global commodity prices: between April 2020 and December 2021 the Reserve Bank of Australia's commodities price index jumped by 37 per cent.<sup>38</sup> Exports to China of big-ticket items like iron ore, liquefied natural gas, wool and more have continued to flow unimpeded. This is because China is as reliant on Australia as a supplier as Australia is on China as a customer. It is here that claims Australia is “dependent” on China butt up against the economic reality of there being a mutual dependence. New research shows that the resilience of Australia's exports to China to shocks emanating from the political realm is not only a contemporary phenomenon but stretches back ever since the take-off in the 2000s.<sup>39</sup>

Next, many of the industries hit with disruption were able to effectively mitigate the fallout. An Australia–China Relations Institute study<sup>40</sup> in September 2021 estimated that, for nine of the 12 export goods affected, the value of export losses amounted to less than 10 per cent of total export value. The mitigation mechanism most commonly available for Australian

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36 Collinson 2022.

37 Department of Foreign Affairs and Trade n.d.<sup>40</sup>.c.

38 Reserve Bank of Australia n.d.

39 Galley et al. 2022.

40 Laurenceson and Pantle 2021, 1.



exporters has been access to competitive global markets. Even for goods like cotton, where three-quarters of Australian exports went to China prior to market access being lost, global markets supported local producers redirecting their production to other customers quickly and at low cost. When Beijing blocked goods from Australia, Chinese importers had to source supply from elsewhere. In turn, this created an opening for Australian exporters in those markets that China's new suppliers previously serviced. Another mitigation mechanism available for exporters of affected goods such as lobsters has been "grey markets". This involved local producers first exporting their product to separate customs territories such as Hong Kong before it was then trans-shipped to the Chinese mainland. Some exporters of agricultural and forestry goods also engaged in product transformation to avoid sanctioned categories, such as turning logs into woodchips.<sup>41</sup>

Australia has yet to experience import disruption, albeit some nationalistic Chinese tabloids appear to have enjoyed preying on local fears that it might.<sup>42</sup> China's self-interest again helps to mitigate the risk. Not only would Chinese exporters lose sales to Australia but it would also damage China's reputation as a reliable supplier globally and so provoke a mitigating response. In 2010, Japanese officials perceived that Beijing was threatening to cut off the country's supply of rare earths, albeit the details of the case are contested.<sup>43</sup> Predictably, this triggered a supply chain resilience-building exercise by Tokyo, including investing in the establishment of alternative suppliers.

Nonetheless, the fear of being targeted by Beijing on the import side of the equation loomed sufficiently large such that in May 2021 Treasurer Frydenberg tasked the Productivity Commission with reviewing Australia's supply chain vulnerabilities. The resulting study began by clarifying that, contrary to some commentary, "Australia's supply chains proved generally resilient in response to the COVID-19 pandemic".<sup>44</sup> It then found that around one-fifth of Australia's import product lines (1327 out of 5862) were "highly concentrated" – a situation where the main supplier accounted for over 80 per cent of Australia's imports of that product. Yet, as the above discussion showed in the case of exports, there is also no simple relationship between exposure and risk when it comes to imports. In the event that Beijing disrupted supply, what matters is whether alternative sources are available. To make this point the Productivity Commission's study cited the example of the chemical chlorine:

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41 Ferguson, Waldron and Lim 2022.

42 GT staff reporters 2021.

43 Johnston 2013.

44 Productivity Commission 2021.

Australia sources chlorine primarily from China, but the global market for chlorine is not concentrated and China is not the leading exporter of chlorine. This suggests that Australia could source chlorine from another economy in the event of a disruption to Chinese supply.<sup>45</sup>

After taking alternative sources of supply into account, it was concluded that just 5 per cent (292 of 5862) of Australia's imported product lines could be considered "vulnerable", with China supplying two-thirds of this number. Even then, fewer than half of all "vulnerable" imports (130 of 292) were found to be used in industries that could be regarded as "essential". Many of these were "unlikely to constitute critical inputs" with examples cited including "women's swimwear from China". In the end, the study highlighted a number of chemicals and personal protective equipment (PPE), such as face shields and isolation gowns, as being examples of goods worthy of further investigation into how supply chain resilience might be enhanced. Such a sober conclusion was in stark contrast to reports by think tanks and statements by politicians seemingly more intent on generating alarmist headlines.<sup>46</sup>

Finally, given that public policy resources are finite, and interventions are not cost-free, any measures aimed at bolstering systemic-level resilience must be chosen with effectiveness rather than political expediency in mind. The mitigation mechanism most frequently privileged in policy circles and public commentary is promoting greater customer and supplier diversification. But it should be recognised that a medium-sized economy like Australia will inevitably develop significant exposures to much larger economies, like China and the United States. Benchmarked against peer economies, for the most part Australia's overall export exposure to its single largest customer does not, in fact, stand out. What does mark Australia as an outlier is the degree of product concentration found in the export basket.<sup>47</sup> The real diversification challenge for Canberra is not so much convincing other capitals to further prise open their markets to the goods that Australia currently exports but rather in enhancing the domestic economy's ability to competitively supply a broader basket of goods and services internationally.

Further, if policymakers obsess on diversification – of either the market or product variety – then other, potentially more effective or less costly mitigation options, or both, can be missed. For example, despite an iron ore price boom adding billions of dollars to federal government coffers since 2020, there have been no additional injections into the Treasury's

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45 Productivity Commission 2021.

46 Laurenceson 2021a.

47 Laurenceson et al. 2021.

Future Fund. An opportunity to self-insure against the income loss that might result from a future shock to exports has been missed. Similarly, measures to encourage supplier diversification must be weighed alongside other supply chain resilience options such as maintaining government stockpiles, mandating or subsidizing private stockpiles or subsidizing domestic production.<sup>48</sup>

## **Trade risk: legal sources of mitigation**

Legal sources of risk mitigation carry particular weight in the case of Australia and China because, even in their bilateral disputes, both countries cite World Trade Organization (WTO) rules in justifying their actions, such as WTO provisions around dumping, and sanitary and phytosanitary protocols,<sup>49</sup> while also continuing to demonstrate a willingness to submit to adjudication by its resolution processes. The risk mitigation the WTO affords is far from perfect. The litigation process itself can stretch to years. But its independence can act as a circuit-breaker in what might otherwise become an increasingly acrimonious bilateral dispute. And even if a party refuses to comply with a WTO decision, it still conveys reputational consequences that other members will factor into their dealings with that party.

Canberra has now initiated cases at the WTO with respect to Chinese tariffs on Australian barley<sup>50</sup> and wine<sup>51</sup>, while Beijing has done likewise with respect to Australian tariffs applied on Chinese wind towers, deep-drawn stainless-steel sinks and railway wheels.<sup>52</sup> The case brought by Beijing is of particular consequence because it involves a matter of long-standing disagreement: specifically, Australia's treatment of China as a non-market economy in its application of anti-dumping measures to Chinese goods.<sup>53</sup>

It is also significant that in the absence of a functioning Appellate Body at the WTO – owing to the United States blocking the appointment of new judges as the terms of serving judges expired – in May 2020 both Australia and China, along with around 20 other countries, voluntarily committed to an interim appellate review procedure known as the

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48 Productivity Commission 2021.

49 WTO, Committee on Sanitary and Phytosanitary Measures, "Notification of Emergency Measures, 6/SPS/N/CHN/1194," accessed January 12, 2021.

50 WTO, "China — Anti-Dumping and Countervailing Duty Measures on Barley from Australia," accessed April 19, 2022, [https://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds598\\_e.htm](https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds598_e.htm).

51 WTO, "China — Anti-Dumping and Countervailing Duty Measures on Wine from Australia," accessed April 19, 2022, [https://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds602\\_e.htm](https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds602_e.htm).

52 WTO, "Australia — Anti-Dumping and Countervailing Duty Measures on Certain Products from China," accessed April 19, 2022, [https://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds603\\_e.htm](https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds603_e.htm).

53 Zhou 2015.

multi-party interim appeal arbitration arrangement (MPIA).<sup>54</sup> The two sides adhered to this procedure in their ongoing disputes concerning China's anti-dumping duties on Australian barley<sup>55</sup> and Australian tariffs on the above bundle of Chinese goods.<sup>56</sup> This contrasts with China's confrontational approach against non-MPIA parties, particularly the United States. In a recent dispute, China appealed "into the void" after the WTO panel found in favour of the imposition of safeguard measures by the United States on certain Chinese crystalline silicon photovoltaic products.<sup>57</sup> China's different litigating strategy can be seen as an attempt to dissuade the United States from continuing to block the appointment of Appellate Body members, an end that Australia supports.<sup>58</sup>

There is scope for enhanced cooperation in dealing with bilateral disputes under the WTO framework. For example, in 2005 the Australian government promised recognition of China as a non-market economy as a precondition for free trade agreement negotiations.<sup>59</sup> Later that year, a Senate committee supported the move and made clear what effect the non-market economy designation was expected to have: "Chinese imports will now be judged no differently for anti-dumping purposes to imports from the US and the EU".<sup>60</sup> This is not what eventuated in practice. At the very least, Australia's anti-dumping authorities could extend more meaningful opportunities for the Chinese government and Chinese exporters to demonstrate that market forces play a decisive role economy-wide or in the industries and economic sectors involved and then make a decision on a case-by-case basis upon an objective assessment of the evidence.<sup>61</sup> While this approach would entail more work for Australian authorities, over time this approach could meet China's concerns about Australia's (ab)use of anti-dumping or countervailing measures, or both. With Australia reconfirming China's market economy status, this approach also has potential to contribute to a thawing of bilateral political tensions. The opposite – that is, if Australia maintains its current approach –

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54 WTO, "Statement on a Mechanism for Developing, Documenting and Sharing Practices and Procedures in the Conduct of WTO Disputes, JOB/DSB/1/Add.12," accessed April 30, 2020.

55 WTO, "China — Anti-Dumping and Countervailing Duty Measures on Barley from Australia, Agreed Procedure for Arbitration under Article 25 of the DSU, WT/DS598/5," accessed August 20, 2021.

56 WTO, "Australia — Anti-Dumping and Countervailing Duty Measures on Certain Products from China, Agreed Procedure for Arbitration under Article 25 of the DSU, WT/DS603/4," accessed September 20, 2022.

57 WTO, "United States — Safeguard Measure on Imports of Crystalline Silicon Photovoltaic Products, Notification of An Appeal by China under Article 16 of the Understanding on Rules and Procedures Governing the Settlement of Disputes, WT/DS562/12," accessed September 20, 2021.

58 For a recent discussion on how to resolve the Appellate Body crisis, see Gao 2021b.

59 Department of Foreign Affairs and Trade of Australia and the Ministry of Commerce of the People's Republic of China 2015. See the Recognition of China's Full Market Economy Status and the Commencement of Negotiation of a Free Trade Agreement between Australia and the People's Republic of China, agreed on 18 April 2005. As a pre-condition for ChAFTA negotiations, Australia agreed to confer China the so-called 'market economy status' in 2005.

60 Senate Standing Committees on Foreign Affairs, Defence and Trade 2005.

61 For a discussion of the recent developments of China's anti-dumping practices, see Zhou and Qu 2022.

is likely to promote a situation in which China adopts similar tactics, imposing more frequent and higher anti-dumping duties against Australian goods.<sup>62</sup>

Widening the aperture away from bilateral disputes, Australia has also been careful to put some distance between itself and the United States on trade matters involving China. For example, after the United States launched its campaign of coercion against China in 2018, in November that year trade Minister Simon Birmingham stated, “[We’ve] been very clear in our position all along that we do not approve or support the US actions of increasing tariffs in a unilateral way on Chinese goods”.<sup>63</sup> In the subsequent disputes that China brought against the United States at the WTO, Australia joined as a third party.<sup>64</sup> This is not to say that Australia does not to some extent share US concerns around China’s adherence to trade rules and the functioning of the WTO, but its approach to dealing with these issues has been to engage with China and not obstruct the WTO’s functioning. When the United States, the European Union and Japan pushed for initiatives that would tighten the rules on Chinese state-owned enterprises and industrial subsidies, Australia also seems to have tried to avoid any official statements that would be seen as supporting the initiatives. In two recent joint statements with Japan and the other Quad countries (the United States and India) respectively, there was no direct reference to China’s state-led economic regime and industrial policies. In its statement on China’s WTO Trade Policy Review in October 2021, Australia criticised China’s non-market practices, state intervention in commercial activities and industrial subsidies. But Australia was careful enough that it did not step further to advocate the development of new rules that singled out China.

Both countries are also proponents for a growing range of WTO initiatives to restructure the nexus between trade, environment and sustainable development, including co-sponsoring an initiative that seeks to tackle plastic pollution in pursuit of environmentally sustainable plastics trade.<sup>65</sup> The WTO’s joint initiative on ecommerce,<sup>66</sup> originally initiated by the United States, the European Union and Japan and now led by Australia, Japan and Singapore, has received support from a majority of the membership with China becoming one of the most active participants in the negotiations over time.<sup>67</sup> Moreover, the fact that the ChAFTA is one

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62 Zhou and Qu 2022.

63 Minister for Trade, Tourism and Investment and Minister for Finance 2018.

64 WTO, “United States — Tariff Measures on Certain Goods from China,” accessed April 19, 2022, [https://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds543\\_e.htm](https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds543_e.htm).

65 WTO, “Launch Event: Ministerial Statements on Trade, Environment and Sustainable Development,” last modified December 15, 2021, [https://www.wto.org/english/tratop\\_e/tessd\\_e/launch\\_event\\_151221\\_e.htm](https://www.wto.org/english/tratop_e/tessd_e/launch_event_151221_e.htm).

66 WTO, “Joint Initiative on E-commerce,” accessed April 19, 2022, [https://www.wto.org/english/tratop\\_e/ecom\\_e/joint\\_statement\\_e.htm](https://www.wto.org/english/tratop_e/ecom_e/joint_statement_e.htm).

67 Gao 2021a.

of the few free trade agreements in which China agreed to a stand-alone chapter on ecommerce also provides a solid foundation for China and Australia to advance ecommerce rules on a bilateral basis and then seek to influence the development of the global ecommerce governance at the multilateral level in light of their common position. Another area is trade facilitation. Although the WTO agreement on trade facilitation<sup>68</sup> remains plurilateral at this stage, Australia and China are among the very first group of signatories<sup>69</sup> and both have fully implemented their obligations.<sup>70</sup> This demonstrates their shared vision and commitment to “freer” trade by reducing unnecessary delays, red tape and associated costs at the border. With political will, this shared vision and commitment could extend to re-igniting negotiations to upgrade ChAFTA. This upgrade has long been foreshadowed but negotiations stalled in 2017 along with the deterioration in the political relationship.<sup>71</sup>

Aside from a shared commitment to cleaving to the WTO in bilateral disputes, and to the utility of the WTO more generally, both Australia and China have also demonstrated a shared interest to expanding the rules-based framework beyond it. Both countries were founding members of the Regional Comprehensive Economic Partnership, which entered into force at the beginning of 2022.<sup>72</sup> China has also requested to join the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) in September 2021,<sup>73</sup> an agreement of which Australia is a founding member. Trade Minister Dan Tehan welcomed the opportunity to engage with China in potential accession talks,<sup>74</sup> albeit reiterating that such talks would depend on assessments of China’s compliance with existing trade rules and China’s resort to coercion is evidence of non-compliance.<sup>75</sup> China would also be expected to undertake domestic reforms needed to meet the high standards of the CPTPP. On this point, some trade law experts have argued that China’s ability to meet these standards is more achievable than is generally understood.<sup>76</sup> Meanwhile, some of Australia’s other strategic partners are less inclined to be supportive of its objectives around trade architecture. India withdrew from the Regional Comprehensive Economic Partnership negotiations prior to the deal’s signing, and the Biden administration in the United States continues to show no interest in joining the CPTPP. In

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68 WTO, “Trade facilitation,” accessed April 19, 2022, [https://www.wto.org/english/tratop\\_e/tradfa\\_e/tradfa\\_e.htm](https://www.wto.org/english/tratop_e/tradfa_e/tradfa_e.htm).

69 WTO, “Ratifications List,” accessed April 19, 2022, <https://www.tfacility.org/notifications-ratifications/ratifications-list>.

70 WTO, “Progress on implementation commitments by Member,” accessed April 19, 2022, <https://tfadatabase.org/implementation/progress-by-member>.

71 Department of Foreign Affairs and Trade n.d.a.””

72 Department of Foreign Affairs and Trade n.d.b.””

73 Ministry of Commerce, 2021a””.

74 Tehan 2021.

75 Tehan 2021.

76 Gao and Zhou 2021.

November 2021, Commerce Secretary Rina Raimondo put on the public record that the CPTPP “is not something that America would be part of at this time”.<sup>77</sup>

Finally, there is an opportunity for Australia and China to work together to head off major challenges to the rules-based order around trade, such as the ever-expanding scope of national security to cover unfettered economic interests and preventing the abuse of security-related measures at the cost of trading partners.<sup>78</sup> The unilateral and retaliatory measures on security grounds embarked upon by the United States in its trade war with China,<sup>79</sup> although affecting other countries too, is the most extreme example. A useful starting point would be for Australia to understand China’s evolving approach to national security and the reasons behind it. As of this writing, China’s approaches at international and domestic levels have largely been driven by the actions taken by other key players, particularly the US abuse of economic sanctions on security grounds. At the international level, for instance, China challenged the US trade war measures at the WTO<sup>80</sup> and submitted proposals to reform the relevant WTO mechanisms.<sup>81</sup> In essence, China’s position is that security measures should be subject to close scrutiny by the WTO, must not be abused and can be retaliated if they are applied in bad faith. At the same time, China has also stressed, in its third-party submission in the *Russia – Traffic in Transit* dispute, that WTO’s judicial review of security measures must be conducted with caution so as not to unduly interfere with members’ rights to protect national security.<sup>82</sup> Australia’s position, as reflected also in its third-party submission in the same dispute,<sup>83</sup> is well aligned with China’s insistence on ensuring that the judicial review maintains a proper balance between rights and obligations of WTO members. Accordingly, there is room for Australia and China to take collective actions to influence the future development of security-related laws and practices.

At the domestic level, China has rolled out a series of new laws and regulations to establish a comprehensive framework for the protection of national security. This regulatory effort began with the enactment of a new *National Security Law* in 2015.<sup>84</sup> This law treats all

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77 Takita 2021.

78 Cohen 2020; Heath 2020.

79 Bown and Kolb 2022.

80 WTO, “United States — Tariff Measures on Certain Goods from China, Request for Consultations by China, WT/DS543/1,” last modified April 5, 2018; WTO, “United States — Certain Measures on Steel and Aluminum Products, Request for Consultations by China, WT/DS544/1,” last modified April 9, 2018; WTO, “United States — Tariff Measures on Certain Goods from China II, Request for Consultations by China, WT/DS565/1,” last modified August 27, 2018; WTO, “United States — Tariff Measures on Certain Goods from China III, Request for Consultations by China, WT/DS587/1,” last modified September 4, 2019.

81 WTO, General Council, “China’s Proposal on WTO Reform – Communication from China, WT/GC/W/773,” last modified May 13, 2019.

82 WTO, “Russia — Measures Concerning Traffic in Transit, WT/DS512/R,” last modified April 26, 2019, Panel Report.

83 WTO, “Russia — Measures Concerning Traffic in Transit.”

84 President of People’s Republic of China ’2015.

harms or threats to China's fundamental economic principles and system, and to the development of major industries and economic sectors as matters of economic security, and creates a non-exhaustive list of security interests subject to further development according to China's own needs. Faced with the US trade war sanctions, China introduced a series of measures in a short period of time, mainly including Measures on the Unreliable Entity List in 2020,<sup>85</sup> the *Export Control Law* also in 2020,<sup>86</sup> *Rules on Counteracting Unjustified Extra-Territorial Application of Foreign Legislation and Other Measures* in 2021,<sup>87</sup> and most recently the *Anti-Foreign Sanctions Law* of 2021.<sup>88</sup> In all these measures, economic security has become an embedded element of national security acquiring growing prominence. Beijing has also instituted a retaliatory mechanism to authorise the use of a broad range of countermeasures against foreign actions that adversely affect China's economic security. While China's regulatory actions were triggered primarily by US sanctions, they have become part of China's overarching strategy to develop sufficient domestic regulatory tools to combat foreign security actions and to pursue its own security and economic interests. Based on this understanding of China's position, Australia's future engagement with China on security-related issues would wisely be built on the principle of non-discrimination to avoid unnecessary frictions. That is, any actions that Australia takes should target the security risks associated with imports and exports rather than China. Moreover, where there is a need to impose security-related measures on China, there ought to be prior consultations before proposed actions are taken. This would not only show due respect to China's interests but may also lead to a mutually acceptable solution that would avoid countermeasures. Over time, this would also contribute to rebuilding the habits of cooperation so that the two sides can shift their recent focus on political disagreements to one of furthering and expanding mutual economic interests.

## **Conclusion**

Australia has historically viewed trade ties with China through the frame of opportunity. But in recent years, as the bilateral political relationship has broken down, the exposure to China as a customer and supplier has increasingly been seen through the frame of risk. Calls for Canberra to respond by using public policy to drive businesses away from engaging with

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85 Ministry of Commerce, '2020.

86 President of the People's Republic of China' 2020.

87 Ministry of Commerce, '2021b.

88 President of the People's Republic of China' 2021.



the Chinese market have grown louder. Beijing's willingness to disrupt Australia's exports since 2020 means that an increased emphasis on risk is not without cause. Yet, as this chapter has explained, for the most part, deploying public policy to reduce trade exposure to China struggles as a coherent strategy in response.

Geopolitical risk is part of a suite of risks that private business owners already regularly monitor and adjust for. Without any government prompting, some will assess that reducing their exposure to China is an optimal risk mitigation response. Others will elect to maintain an existing exposure, confident in the knowledge that, if access to the Chinese market is disrupted, then they have access to alternative mitigation mechanisms. The scope for public policy to improve outcomes, therefore, is mostly limited to the management of risk at a systemic level. As the evidence raised in this chapter has also shown, the scale of systemic risk that trade engagement with China creates is often exaggerated or misdiagnosed, such as when Australia's diversification challenge is depicted overwhelmingly in terms of exposure to the Chinese market rather than in terms of being exposed to a narrow range of products that the Australian economy can competitively supply on global markets.

While some of the earlier euphoria around trade with China was likely overdone, the key lesson learned from the passage of time is that public policy that does not discriminate against businesses and households getting on with the engagement they regard as mutually beneficial remains consistent with Australia's interests. Beyond the direct economic benefits, robust trade ties provide ballast for the broader bilateral relationship. There is also an alignment of interests in expanding the rules-based framework around trade, including the Regional Comprehensive Economic Partnership, the CPTPP and the WTO, providing an opportunity for Australia and China to cooperate in positively shaping the region they share.

The arrival of a new Australian government in May 2022 and the restart of senior political dialogue the following month has provided further optimism around limiting potential political shocks spilling over to hurt trade. This is not because the structural challenges in the relationship will be resolved – a “reset” in political relations is not in the offing – but a more diplomatic tone from Canberra is readily apparent, as is a commitment to “stabilising” the relationship on the basis of the two countries' Comprehensive Strategic Partnership.

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