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# ViewPoint

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## New Zealand under the China Trade Agreement: More than China's Farm?

The dust is settling in the wake of the signing of the Preferential Trade Agreement (PTA) with China.

There have been the celebrations and the criticism, but now the deal is all but done. What started as political intent will now play through to the economy, mixing the terms of the deal with our ability to make it work for New Zealand in the medium to long term. Putting the obvious human rights, freedom and labour issues aside, we are compelled to focus on the challenges and implications for our companies when trading with a large, low cost country. We also need to consider what approach our own Government must take to maximise the competitiveness of New Zealand's companies.

Once ratified, the trade agreement will, over a decade or so, almost eliminate all tariff gaps and open the Chinese market to New Zealand agricultural commodities. However, our success in being more than China's farm depends on our ability to work this agreement in the area of trade in elaborate products and recognise how other major trends will impact global trade.

We appear to be reaching and end game watershed: oil at over $110 a barrel variable and rising, higher Carbon, climate and energy costs in general, freight and food costs are increasing quickly as global resource competition intensifies. Labour costs are increasing in some developing countries, and environmental pressure and awareness is growing, even in China. All these things probably mean that New Zealand wins on food and maybe improves on labour cost differences, but comes up short on transport and travel costs and what that implies in trade and tourism.

For many, the attraction of a trade agreement with China is the eye-wateringly large market that might open for New Zealand trade. New Zealand has a first mover advantage over other nations, who are yet to conclude a deal of their own. Companies are now encouraged to engage further with their Chinese markets and take advantage of the new opportunities.

However, the reality of making the agreement work for trade to our gain has a few challenges. Being first is not all upside – having done the first deal we now have to make the first deal work for us against the background on the global trends mentioned. China is our most able competitor and Chinese governance can, and does, take a long term view of the world. It is important to recognise that the agreement process manifests itself through the fact, that in China, when the ink is dry the deal is done, in New Zealand, the deal is subject to Parliamentary ratification.

New Zealand is going to have to work hard and smart to keep what we have come to see as our place in the world. New Zealand's trade deficit with China is increasing rapidly, having grown from NZ$1.4 billion in June 2004 to NZ$3.4 billion in June 2007. On current trends, the deficit will run out at NZ$3.9 billion to June 2008. Perhaps, some deficit is inevitable due to economies of scale and economic focus of the two countries, but how to minimise the deficit is a key question. China may well be the source of a trade but it could also become the financial 'tsunami' that has the capacity to swamp our economy.

Nationally, what are the strategies and policies that need to be put in place to help our firms compete with a China that demands high quality, but retains low cost profile?

Currently, "Made in China' is a reality for many products in New Zealand, but often 'recognition' goes to the local brand, not the Chinese firm. New Zealand seeks to retain its position by holding the intellectual genesis and control of the brand here. However, once China gets 'branded' (IBM to Lenovo) it will begin to assert control throughout the entire supply chain. Once this happens, Chinese industry sectors, backed by a large long term capital base, will have the right products, top class design capability, and as this transition gains momentum, their companies will enter the New Zealand acquisitions market and their own with increasing leverage.

Therefore, the focus for our Government should be more than "the deal is done, off you go". The Government must reduce the competitive differences between China and New Zealand and implement a framework that delivers more exports across a growing, not contracting, number of export classification codes. Otherwise, we will export activity and capability, leaving us with ever fewer export classifications and regressing to become simply China's farm.

Support or oppose this trade agreement, China is a force that we have to learn to live with now and in the future. However, supportive policy from Government and pragmatic and forward thinking by New Zealand companies are necessary if we are to maximise our position.

If New Zealand's monetary policy continues to counter inflationary pressure in a manner that drives the cost of borrowing and exchange rates upwards, then the benefits to our firms from the trade agreement might be lost or a best severely damaged. Add the growing number of cheap imports that erode domestic markets into the mix, along with heavy compliance costs, and there is less incentive for mobile companies to take root and grow in New Zealand.

If we end up down this road, our simplifying exports and present policy framework will mean that our companies and economy will not fare so well under this trade agreement after all.

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