Discussion Paper

Chinese investment in Australia: How much is too much?

Natalie Cope

Foreign direct investment (FDI) is an important pillar of Australia's economic development. As a country with a small population and low savings base, foreign capital has provided employment, allowed higher rates of economic growth and a higher standard of living than Australia could otherwise expect from domestic sources of investment. Yet despite the importance of FDI to economic development, Chinese investment in Australia is a contentious topic. Over the last year, several cases involving the sale or lease of privately and publicly owned Australian assets to Chinese investors have attracted criticism. But is the political and emotional backlash that reverberates in the public narrative warranted?

While Chinese foreign investment into Australia has steadily increased since 2007, China remains only the fifth largest source of foreign investment in Australia, behind the United States, the UK, Japan and the Netherlands.

Considering the context of Australia's history, the anxious response to Chinese investment seems to bear an uncanny resemblance to the nation's discomfort during other waves of foreign investment from the US in the 70's and in particular Japan in the 80's. It pays to remember that the Foreign Investment Review Board (FIRB) and the Treasurer's "national interest test" were established in this environment, and designed principally to quell public concerns and protect national interests. To date, this has been an effective means of managing investment and allaying public anxieties.

The issue at stake seems not so much whether the current review framework is effective, but whether Chinese investment poses a particular threat to national security (with some viewing China as an increasing security rival to the US), and thus should be subject to stricter regulatory and political review. It seems this issue stems from a broad lack of awareness about the drivers of Chinese outbound investment and a misunderstanding about the role the Chinese government currently plays in the decisions by both state owned and private enterprises regarding invest abroad. While state-owned enterprises continue to play a figurative role in outbound investment, they do so under increasingly competitive market conditions and are often at arm's length from central powers. Over time, investment by private Chinese enterprises has increased. In the calendar year 2015 private entities accounted for 78 per cent of all Chinese FDI.[1]

Australia is a liberal, rules based investment environment with a robust legal framework. This allows for rigorous inspection of any foreign investment; particularly when that investment is destined for what could be classified 'Australian assets of strategic or national significance'. Australia should treat Chinese investments the way it treats any other

[1] KPMG & China Studies Centre Survey 2015

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investors, and should have confidence in its own rules and procedures. Exceptional treatment for any partner is never a good thing. Indeed it could adversely affect national interests.

Notwithstanding the above, the question of whether there is a threshold – either quantitative, or based on certain criteria, such as strategic importance – beyond which the Australian government should not accept Chinese investment (or any other foreign investor) is worth considering. As a matter of principle there need to be limits to foreign investment in any country. In Australia, applications are currently reviewed by FIRB in consultation with other government agencies on a case-by-case basis. In the current context, if an application made to FIRB is perceived as problematic to national security, the Treasurer can decide to approve the transaction subject to conditions and safeguards, or decline the application altogether (Interestingly, there is currently no legislative definition of what is 'national security').

However, any limits that are imposed, even when on a case-by-case basis, must be applied uniformly to all foreign and domestic investors. If we are not consistent we risk losing our reputation as a stable and transparent destination for investment.

Another question is reciprocity, and whether Australia should prohibit foreign investment into sectors that Australians are not permitted to invest in China. This is a popular argument in major powers such as the United States and the European Union. For Australia however, reciprocity is not relevant, and would be harmful to our interests. Why should Australia delay or deny benefits to its own communities just because the Chinese government has not liberalized certain sectors of their economies?

What if a major deterioration in Australia-China ties were to occur? How should the Australian government manage Chinese investments in critical infrastructure? If a major deterioration were to occur Australia should maintain its principle of open, fair and stable markets (whomever involved). Doing so will create an environment that best allows for the resolution of conflict. Punitive retaliation would be extremely counterproductive. It is probably more useful to ask whether we need a strategy for dealing with existing investment in the case of a crisis in relations. In this context, it is worth noting that in the event of a conflict or war with China, the Australian political leadership and security agencies already have the power to appropriate, where necessary, assets that compromise national defence.

The injection of foreign capital into our local economies results in job creation, infrastructure development and the transfers of knowledge, goods and technology between counties. Chinese investment is an opportunity from a commercial and strategic perspective (as is all foreign investment). In a very real example, if the Government proceeds with plans foreshadowed in the White Paper on Developing Northern Australia, there will be a need to attract large volumes of strategic foreign investment, including from China. Thus we need to become comfortable with investment from foreign sources. This makes us stronger, not weaker. While it makes sense for Australia from time to time to take stock of its foreign investment review framework, its regime should evolve being mindful of eliminating any nationality-based discrimination.