

Session II Discussion Paper

Australia needs PRC investment. But how to deter PRC control, especially in critical infrastructure?

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Australia's critical infrastructure is creaking, and needs investment. Projections vary, but most agree it will cost around A\$1 trillion to get it up to scratch.

As has been the case since Federation, some of the money needed to fund this investment will come from foreign sources. As the world's pool of surplus savings shifts eastwards, these funds will increasingly come from investors from the People's Republic of China (PRC).

The PRC may not be the largest source of foreign investment coming into Australia, but it is highly visible and often controversial. As investment from the PRC increases, so too do concerns about the risks associated with PRC control. Understandably, PRC investors want a say in how their money is used, including a desire to have board seats, greater sway over areas of operations, and as a result, access to a range of information. In some cases, PRC control gives rise to genuine national security concerns. But for the most part, public opinion is the greatest concern: annual polls show that between 50-57 per cent of Australians surveyed believe that there is already too much PRC investment.

Critical infrastructure (telecommunications, electricity, water and ports) has become the front line of the battle between the economic need for investment and the worries about the national security implications associated with PRC investment.

But not all critical infrastructure is equally worrisome. It is easier to regulate and segregate PRC control over ports and water for example, but much harder to mitigate the risks associated with PRC control over energy distribution or telecommunications assets. However, technology and the risks of access to data is a worry that unites all areas of critical infrastructure, and a worry that is difficult to fully mitigate. Inevitably, foreign investment will not be possible in some assets, no matter where the investor is from.

A Critical Infrastructure Unit (CIC) was created within the Attorney-General's Department in early 2017 following an uproar over investment by a privately-owned PRC company in the Port of Darwin. The CIC's role is to 'increase the resilience of Australia's critical infrastructure to threats of coercion, control or sabotage', as well as to provide 'more comprehensive, coordinated and timely advice on national security considerations for any prospective investment'.

The CIC's broader role beyond mere investment review provides possibilities for business and government to work together to mitigate some of the concerns associated with PRC control. The CIC can work with business (or state governments) on assets prior to any sale

or any call for investment. While this does not ensure that the investment will pass review, it should improve investor confidence. PRC investor confidence is very important, not least because PRC investors are sometimes willing to pay more, particularly where they can obtain control of the asset.

The idea of investor confidence is central to the issue of public perception. PRC investment is rarely popular. But in the case of a government asset sale, the extra monies that PRC investors are willing to pay help fund essential public services. This greater value is rarely recognised, nor publicly expressed.

Part of the issue with perceptions is that the ultimate decision maker on investment decisions is the Treasurer. As such, s/he must be mindful to be seen as an impartial arbiter and is thereby constrained in making a public case about the importance of PRC investment. The government should consider making either another minister or a department (most likely the Department of the Prime Minister and Cabinet) responsible for making the case for investment. Business should publicly support the government in this venture.

Another part of the perception problem is inconsistency in decision making. Neither the public nor the investor community can possess full information about the government's national security considerations. But everyone, including PRC investors, needs to have confidence in the decision making process.

The benefits of flexibility in decision making on the part of the Financial Investment Review Board and the Treasurer provided by vague guidelines may be outweighed by the cost of reputational damage to Australia as an investment destination.

Public confidence may be improved by providing greater information as to why investments were rejected. Appropriately sanitised intelligence judgments should be made public. The government should consider key levers at its disposal, such as blocking or limiting appointments to key management roles or board seats, or ensuring that firms meet regularly-assessed risk mitigation standards, and apply these measures consistently.

These measures may not eliminate the concerns about PRC investments but they can help to encourage PRC investment that is desirable, and to reassure the public.

Questions:

What precisely are those sceptical of PRC investment in critical infrastructure afraid of?

Does it matter whether the investor is a (passive) financial investor or an (active) operator and whether the investor is a PRC state-owned enterprise or private enterprise?

Would Australia be better off with stricter upfront rules that constrain foreign investment in critical infrastructure but provide more clearly defined, if more limited opportunities to foreign investors?

Who should be responsible for managing public perceptions of the benefits from, and the challenges of, PRC investment?

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