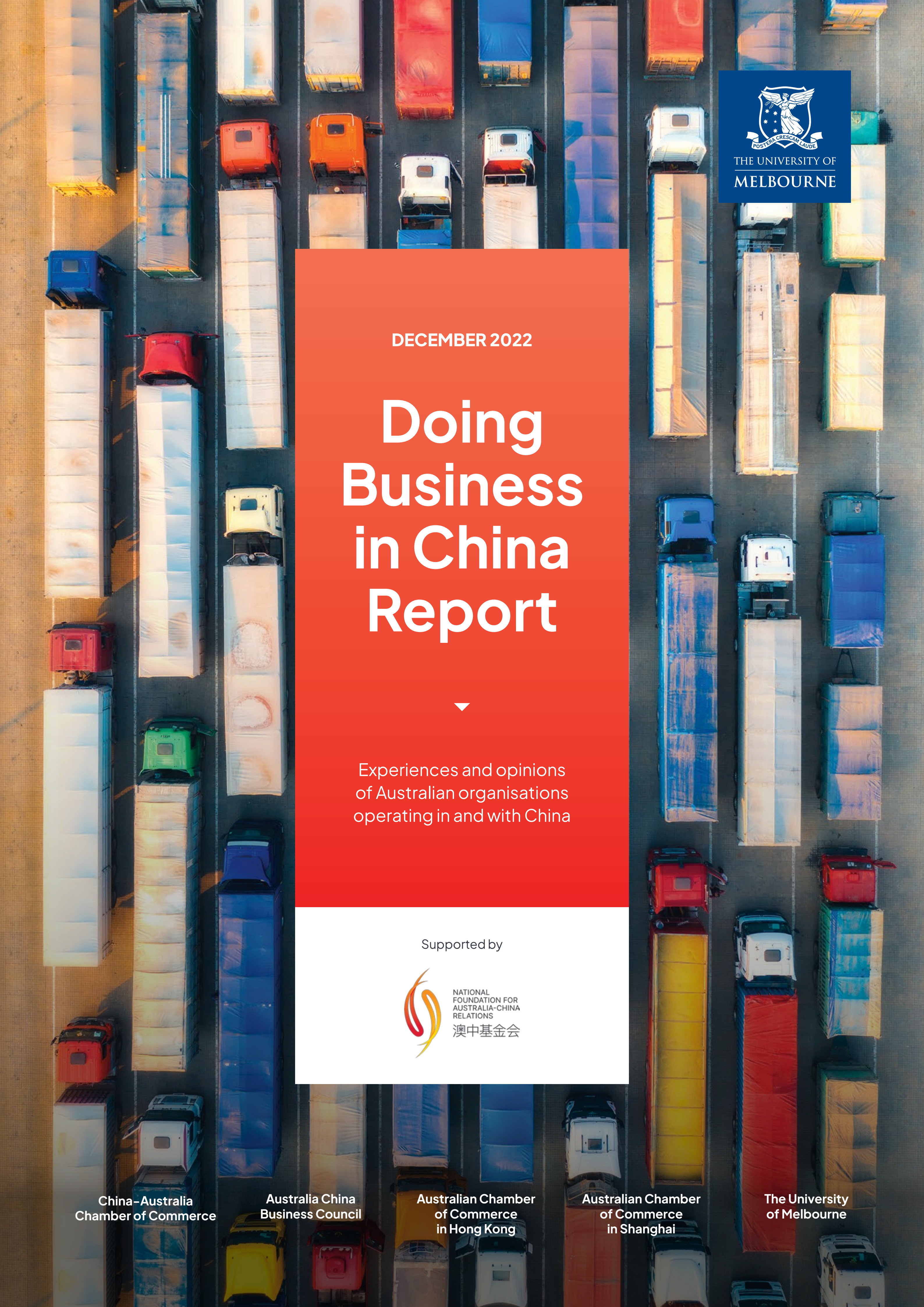

THE UNIVERSITY OF MELBOURNE

DECEMBER 2022

Doing Business in China Report

Experiences and opinions of Australian organisations operating in and with China

Supported by

NATIONAL FOUNDATION FOR AUSTRALIA-CHINA RELATIONS
澳中基金会

China–Australia Chamber of Commerce

Australia China Business Council

Australian Chamber of Commerce in Hong Kong

Australian Chamber of Commerce in Shanghai

The University of Melbourne

Message from the Chairs

As we approach the 50th anniversary of the establishment of diplomatic relations between Australia and China, this report provides reason to be cautiously optimistic about the future of business relations between the two countries.

At the time when the survey was completed, before the Federal Election this year, government-to- government relations between Australian and China had plunged to the lowest level since diplomatic relations were first established in 1972. Despite the state of bilateral relations, media reporting and public sentiment; despite the challenges caused by epidemic prevention and management policies in China and the impact of sanctions and tariffs on some of Australian trade with China; and despite the risks associated with heightened geopolitical tensions and economic decoupling, Australian businesses operating in China are clear-eyed about the importance of the China market and most are either maintaining or increasing their commitment here.

In China for the long term

Three in four of the 160 companies which responded to this year's survey have been operating in China for more than ten years, an increase since the last survey in 2018. A further 13 percent have operated in China for between 6 and 10 years.

Optimistic about the future

For 58 percent of companies, China is either the top or one of the three top markets and more than half the companies are optimistic about opportunities over the next two years.

At the time of the survey, the percentage of respondents maintaining or increasing investment levels was more in 2022 than in 2021, with 66 percent planning to return to or exceed pre-pandemic levels of investment.

More than half the survey respondents were optimistic about market opportunities and growing profitability in China over the next two years. Expanding into new cities and regions; leveraging perception of "Brand Australia" as being safe and high quality; and improved market access were cited as the top three areas of opportunity being focused on.

One third of respondents said that China's actions toward achieving carbon neutrality will create opportunities for their companies to sell products, services, and solutions in China.

It was encouraging to see the percentage of Australian companies sourcing or producing goods and services in China for the Chinese market has more than doubled to 46 percent. Investing, partnering and doing business in country allows Australian companies to potentially earn more than under a pure export model, and helps increase the resilience of the earnings from and exports relating to such business.

Reflecting the impact of trade sanctions and tariffs, this optimism can no longer be attributed to the China Australia Free Trade Agreement with only 20 percent of companies having benefited over the two years prior to the survey as compared to more than 50 percent in 2018. Interestingly, more companies were optimistic about the Regional Comprehensive Economic Partnership (RCEP) and the benefits of China joining the Comprehensive Progressive Agreement for the Trans-Pacific Partnership (CPTPP).

Resilient in the face of headwinds

The percentage of respondents saying the investment environment in China was deteriorating more than doubled to 52 percent. Not surprisingly, the pandemic and trade sanctions made up the top two challenges for Australian businesses in China.

COVID-19 caused sales and profitability to decrease significantly compared with 2019 levels. 36 percent of respondents reported a reduction in headcount and 31 percent a reduction in investment in China. 90 percent reported a negative impact of travel and border restrictions in Mainland China on their China business.

70 percent of business leaders were not satisfied with the Australian government's management of the bilateral relationship in the two years up to May 2022. In 2018, 84 percent of respondents said that bilateral relations had a strong or moderate impact on business.

45 percent of respondents have not taken any actions because of the negative impacts of bilateral relations on their business. Of those that did take actions, considering new markets, increasing investment in new markets, and reducing headcount in their China business were all preferred over reducing investment. Only four companies said they have or will cease their China business.

Looking forward

The opportunity to improve and normalise relations is highly welcome by the Australian business community. We support efforts to resume the healthy and stable development of Australia-China trade and economic relations. Elimination of sanctions and tariffs on Australian trade with China would be a win-win outcome for Australian exporters and Chinese importers and end-consumers and would presumably make it easier for Canberra to support China's application to accede to the CPTPP.

A key theme of collaboration between Chinese and Australian companies will be complementing existing areas of traditional strengths in goods export with emerging opportunities in services and investment. With climate change a key priority for the new administration in Canberra, this is an area ripe for fostering greater collaboration between China and Australia. Across multiple sectors, collaboration in the development and use of cost-effective low emissions technologies and solutions promises to yield new business opportunities for Chinese and Australian companies.

No doubt the impacts of China's zero-COVID policy on the movement of people and goods will continue to challenge companies, employees, and their families. With China's international borders having been closed since March 2020, the experience and perspectives of 160 Australian companies operating in China are a valuable reference for Australian political leaders, policy makers and business leaders alike.

We thank the member companies who completed the survey, as well as Professor Kofman and the University of Melbourne for their insightful analysis of the results. We also would like to acknowledge the National Foundation for Australia-China Relations for their support of this project and all their work in promoting constructive engagement with China

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Foreword

This 2022 survey of Australian organisations doing business in/with China reveals uncertainty, pessimism, and early signs of disengagement from China. Nonetheless, the survey also shows resilience despite ongoing geopolitical concerns and the challenges resulting from the global pandemic.

The 160 organisations we surveyed suffered direct consequences – including tariffs and compromised supply chains – as well as indirect consequences – like increased regulatory scrutiny and a slowing Chinese economy. Australia's business engagement with China has never been tested like this before. Yet, hidden behind a pessimistic outlook, the survey ultimately reaffirms the appeal of China as a dominant regional economic powerhouse.

This 2022 survey of Australian organisations doing business in/with China reveals uncertainty, pessimism, and early signs of disengagement from China. Nonetheless, the survey also shows resilience despite ongoing geopolitical concerns and the challenges resulting from the global pandemic. The 160 organisations we surveyed suffered direct consequences – including tariffs and compromised supply chains – as well as indirect consequences – like increased regulatory scrutiny and a slowing Chinese economy. Australia's business engagement with China has never been tested like this before. Yet, hidden behind a pessimistic outlook, the survey ultimately reaffirms the appeal of China as a dominant regional economic powerhouse.

This third instalment of the DBIC survey report is conducted in partnership with the China-Australia Chamber of Commerce (AustCham China), the Australia China Business Council (ACBC), the Australian Chamber of Commerce in Hong Kong (AustCham Hong Kong), the Australian Chamber of Commerce in Shanghai (AustCham Shanghai), AustCham China West China Chapter and AustCham China South China Chapter. In 2017, AustCham China and the ACBC recognised the need for a longitudinal survey of Australian businesses to better understand the impact of trade liberalisation and specific trade agreements, as well as the vagaries of general business conditions in doing business in/with China. Optimism and opportunity characterised the initial survey findings. Perhaps not surprising as China declared itself Open for Trade following its accession to the World Trade Organisation in 2001. Steadily adjusting its economy to double digit growth over the next decade, China's trade flow surged. In the wake of the 2008 global financial crisis Australia's trade with China overtook trade flows with its traditional partners, Japan and Korea. To sustain its economic growth trajectory, China's voracious appetite for Australian iron ore, copper, agricultural produce and education grew exponentially. With both countries vested in the benefits of progressive trade liberalisation, the bilateral China-Australia Free Trade Agreement (ChAFTA) came into effect in 2015. The 2017 DBIC survey anticipated the benefits for Australian companies, and the 2018 DBIC survey saw those benefits materialise with strong sales and profits.

Despite its optimism, the 2018 survey also touched on emerging concerns about a possible trade dispute between the US and China. In early 2020, Australia became embroiled in a trade dispute with China, significantly affecting Australian companies exporting coking coal, barley and wine, among other goods and services. To make matters even worse, in March 2020, the COVID-19 pandemic hit trade flows worldwide. And soon after, many countries closed their borders to prevent people movement – extending to within-country lockdowns – severely disrupting businesses.

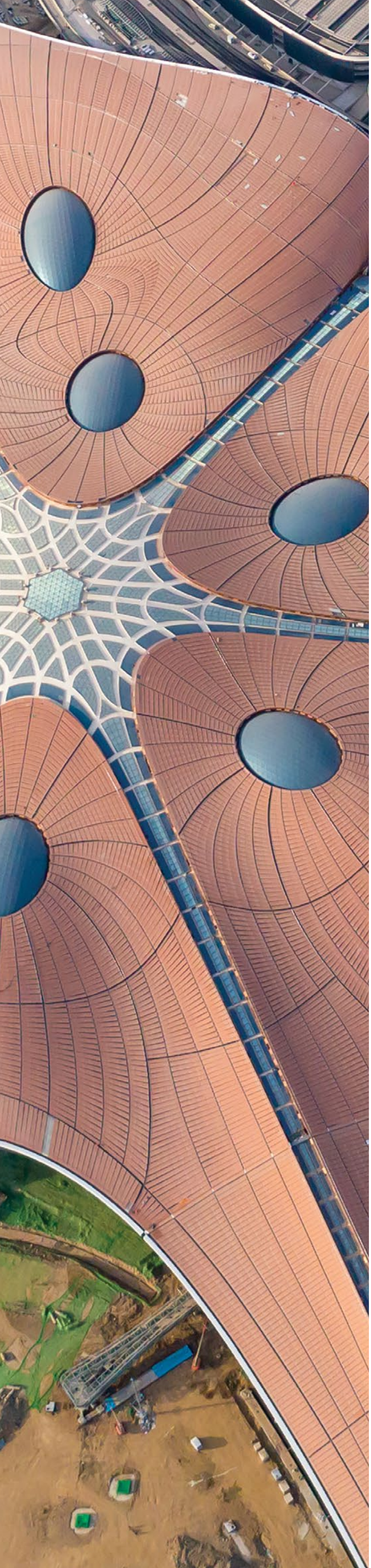
This third annual survey was delayed repeatedly due to the continued impact of COVID-19. In a sense, that delay has been valuable for the responding organisations to step back from their lived experience and reflect more objectively on the full impact of the pandemic and change in bilateral relations between Australia and China. The survey was completed before the federal elections in May 2022.

Paul Kofman

Sidney Myer Chair of Commerce and Dean

Faculty of Business and Economics
The University of Melbourne

The authors of this report gratefully acknowledge grant support received from the National Foundation for Australia-China Relations. The opinions expressed in this report are the authors' only and do not reflect the opinions and positions of NFACR or the Department of Foreign Affairs and Trade.



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Key findings

The 2022 survey results are a synopsis of a tumultuous business environment in China and elsewhere, since the last survey three and a half years ago. Indeed, that November 2018 survey was prescient to highlight the risks and "*importance for companies of Sino-Australian bilateral relations, the impact of media reporting of those relations and the collateral effects of Sino-US trade frictions*."

Intermingled with deteriorating bilateral relations, COVID-19 has overlaid an additional range of challenges. Extended closures of international borders to travel and affected supply chains were particularly disruptive.

Nonetheless, the results of the 2022 survey are witness to the resilience and adaptability of Australian companies doing business in and with China. Compared to 2018, the survey's analysis of respondents' sales, investments and headcounts indicates optimism in 2022, with increasing numbers of respondents expecting growth, following a sharp retraction in 2020 and mixed results in 2021. To weather the business headwinds, many companies have changed their primary strategies, by localising their operations towards sourcing and targeting sales in China or in third-countries other than Australia.

A significant majority of respondents continue to believe that China remains among the top three markets regarding opportunities over the next three years. Yet, uncertainty persists. Australia's new government has an opportunity to recalibrate relations with China towards a normal course, improving the prospects for Australian businesses in the China market.

While respondents noted the reality of a more complicated business environment in China, new areas to engage are found around climate change. China's ambitious carbon targets and policies are opportunities for cooperation where Australian innovation could prove its worth. Overcoming government to government tensions is needed to incubate collaboration in those new market sectors.

Investment Environment

Despite current tensions, 58 percent of respondents still indicated that China is in their top three priorities for global investment plans over the next three years. This was a decline from 81 percent in 2018 and 86 percent in 2017. In the short-term, uncertainty prevails. 39 percent of respondents believe that business in China will rebound faster and stronger during 2022, marginally larger than the 36 percent who considered China will lag other markets. Also, 52 percent see China's investment environment deteriorating, but when asked about total investment in their China business, respondents showed a growing optimism in 2022 compared to 2019 and 2020.

The top-ranking risks affecting investment decisions are China-Australia bilateral relations, the impact of COVID-19 on international travel and new policies and regulatory enforcement.

Business Climate

On the question of ease of doing business in China, paradoxically the percentage of those finding the business environment difficult declined to 58 percent, from 72 percent in 2018. Those finding business easy increased from 3 percent in 2018 to 10 percent in 2022. With no new company entrants to China during recent years, this could be a reflection of the survey cohort's 75 percent with a decade-long or more tenure in China, and now more adept at navigating the Chinese business environment. Also, there were significant shifts with coping strategies to weather the challenges of geopolitical tensions and COVID-19. Those which localised both sourcing and sales in China rose to 46 percent, an increase of 27 percent from the 2018 survey, while those sourcing in China for sales in third countries increased to 20 percent, 13 percent higher than the previous survey.

The competitive landscape has evolved significantly during the past three years. The survey respondents revealed that other foreign companies still constitute their strongest competition. Significantly, private Chinese companies have largely replaced state-owned enterprises (SOEs) as key competitors of our respondents.

Pandemic restrictions on peoples' movement and ongoing tensions in Sino-Australian relations with trade restrictions are perceived as top challenges.

Surveyed organisations report rising costs, including payroll, tax, licenses, and regulatory compliance, as concerns. But unlike the 2018 survey, concerns about intellectual property (IP), cyber and data-security have either abated or crowded out by more pressing concerns.

When asked about the impact of climate change on their China business, one third of respondents believe their companies will benefit from new opportunities to sell products, services, and solutions.

Economic and Policy Outlook

Economic growth in China continues to appeal to the Australian organisations. Perceived threats to growth are therefore carefully considered. The top three perceived risks come as no surprise. Two are clearly contemporary (COVID-19 impact and geopolitical instability), while the third, a decrease in domestic demand in China, has been ongoing from past surveys, although it is now amplified by the recent strict "dynamic COVID-19" policy, lockdowns, and the possibility of a global recession.

The business outlook is optimistic about long-term growth opportunities and increasing profitability with China's consumption shifting to higher quality products and services. However, respondents are pessimistic about costs and regulatory intervention.

Key opportunities in the China market are now focused on expanding into new cities and regions, building on "Brand Australia's" reputation for safe and high-quality products and services and a perception of future greater market access.

Business Performance

When it comes to the bottom line, the survey indicates on average a decrease in profitability for the two years just past. The forecast for 2022 suggests a turnaround in profitability with a modest increase. In absolute terms – and despite the significant decrease – profitability was still positive or break-even for 82 percent of the respondents. That result corroborates the reluctance of the respondents to reduce their presence in China.

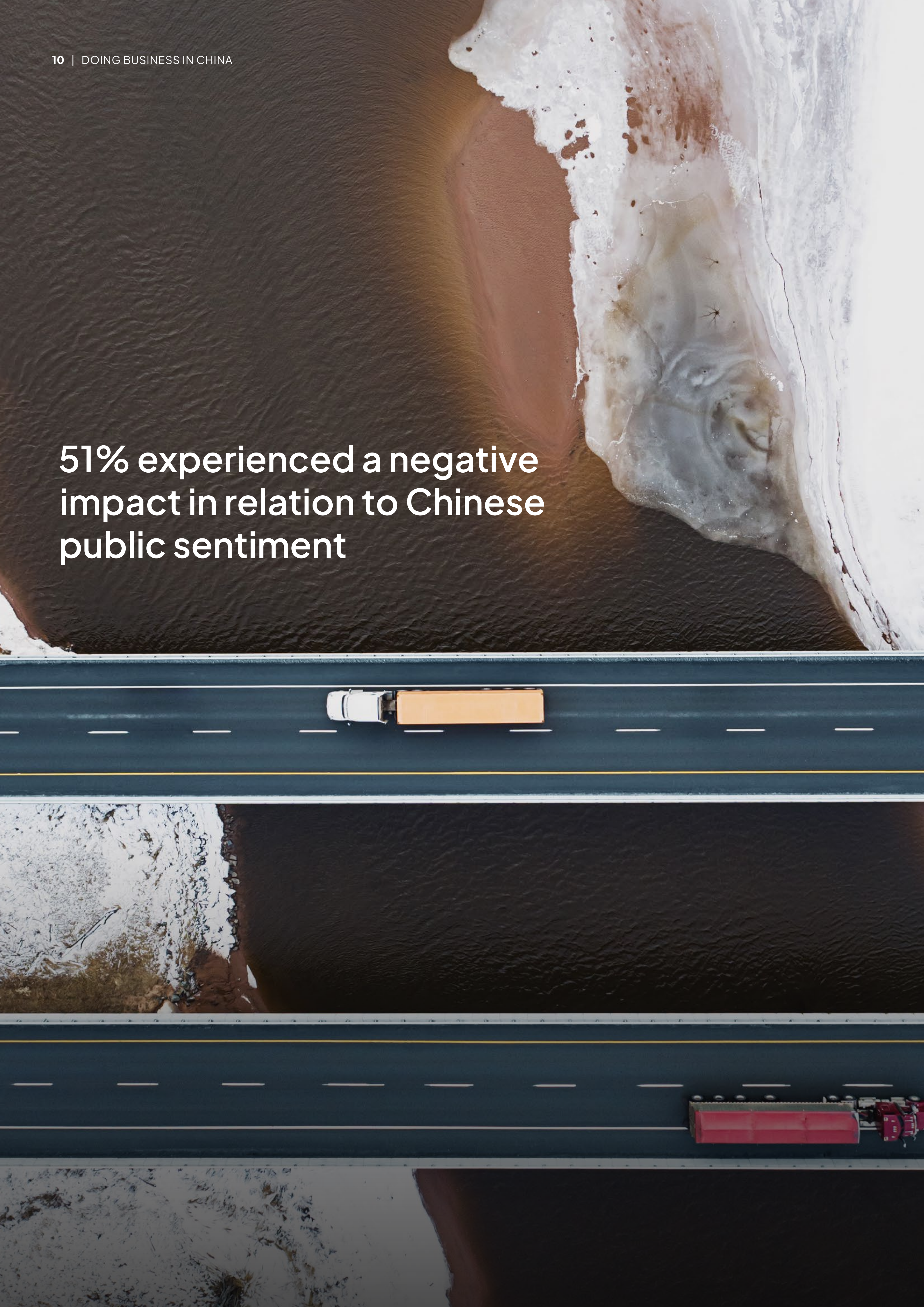
Treaties and International Agreements

The 2022 survey is much less positive than earlier surveys about the impact of the China-Australia Free Trade Agreement (ChAFTA). Only 20 percent saw benefits from the FTA, a drop from 66 percent in 2018. Two thirds had "no opinion" or considered ChAFTA had "no effect" on their business.

The multilateral Regional Comprehensive Economic Partnership (RCEP) and the Progressive Agreement for the Trans-Pacific Partnership (CPTPP) are more recent trade agreements and perhaps unexpectedly, both are considered slightly more beneficial to business than ChAFTA. However, both also have higher figures for no impact, or no opinion.

With global trade under a COVID-19 pall, it is still too early to judge the two pluri-lateral trade agreements and the potential for ChAFTA to be reinvigorated. Nonetheless, 36 percent of Australian exports are still going to China.

51% experienced a negative impact in relation to Chinese public sentiment



Key findings

Bilateral relations and geopolitical risk in numbers

53%

believed Australian media reporting on the bilateral relationship had a negative impact on their business. 4% believed Australian reporting had a positive impact. For Chinese media reporting, 54% felt negative effects and 2% felt positive effects.

47%

noted Australian public sentiment negatively impacted their business, while none of the respondents recorded a positive impact. 51% experienced a negative impact in relation to Chinese public sentiment, while 2% reported a positive impact.[1]

70%

of respondents reported dissatisfaction with the Australian government's management of the Australia-China relationship[1].

44%

reported a reduction in sales as a direct result of the deterioration in Australia-China relations.

68%

of respondents believed that the ongoing US/China trade disputes have negatively impacted their business, while 6% believed that they have had a positive impact.

Other key findings of the 2022 survey

53%

of respondents had their primary strategy geared towards production and sourcing in China for sales in China or third countries other than Australia. In 2018 that figure was 26%.

57%

of respondents spent all their time in China, while 27% spent no time in China, in the past two pandemic years.

75%

of respondents had been operating in China for over a decade.

57%

of respondents believed that China's climate change policy targets will create opportunities for their organisation's China business.

75%

of respondents' China business did not report a loss in 2020 (in fact, 47% were profitable), and this increased to 82% who did not report a loss in 2021 (and 53% were profitable).

1. Responses to this question were provided by respondents in the second quarter of 2022 and accordingly the responses are in respect to the Liberal/National Coalition Government prior to the Federal election in May 2022.

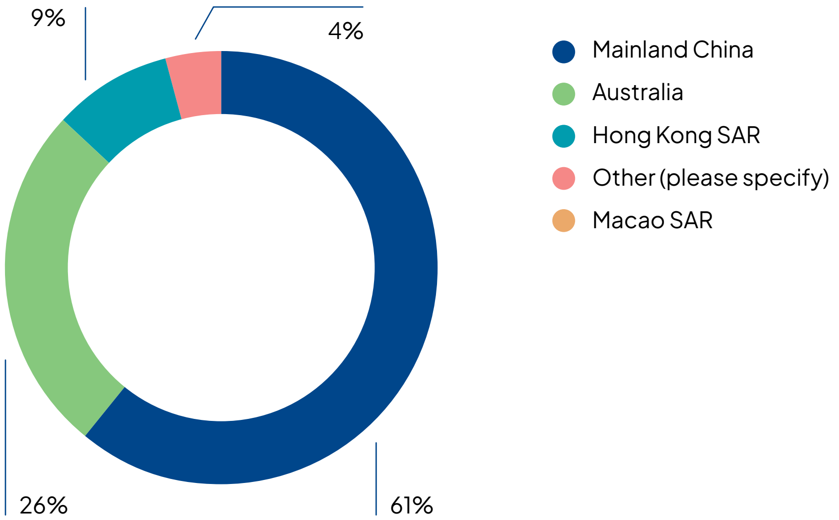
About the 2022 Survey

The survey for *Doing Business in China* was conducted with the membership of the China-Australia Chamber of Commerce (AustCham China), the Australia China Business Council, the Australian Chamber of Commerce in Hong Kong, the Australian Chamber of Commerce in Shanghai, AustCham China West China Chapter and AustCham China South China Chapter, during April and May of 2022. All responses were received prior to the Australian Federal election.

For the third edition of the Doing Business in China report, executives from 160 Australian companies that are operating in or doing business with China have provided valuable source data to inform Australian policy makers, business sector leaders and the media community. The 160 respondents were from Australian companies and/or members of AustCham China, AustCham HK, AustCham Shanghai and ACBC. Fifty seven per cent of respondents held an ABN at the time the survey was conducted.

Figure 01

Where are you filling out this survey?

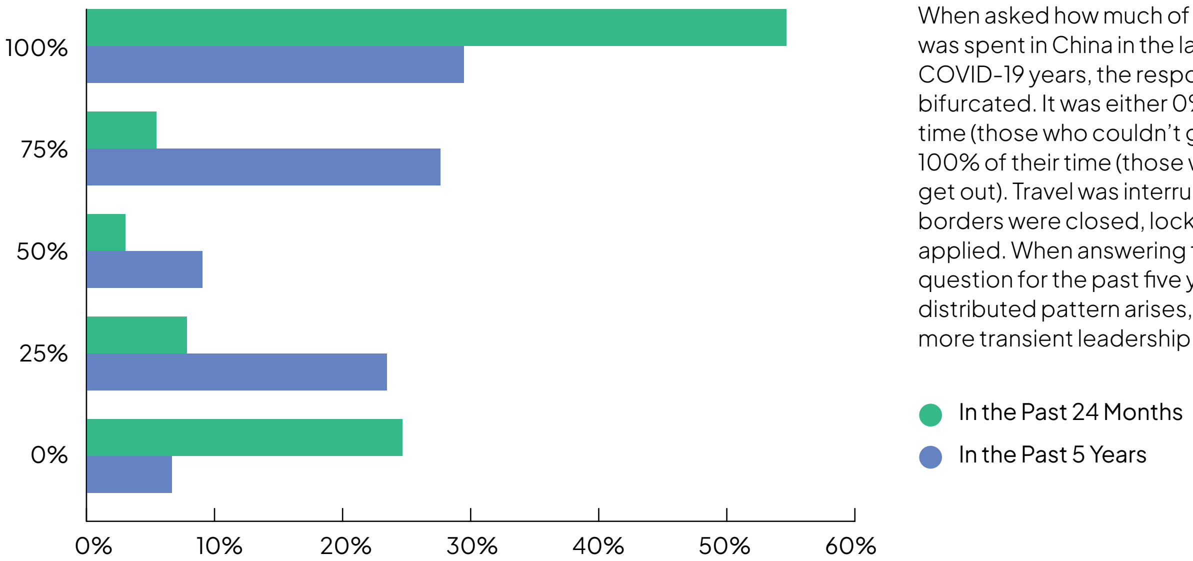


The 2018 and 2017 surveys had 165 and 100 respondents respectively, largely operating in China, contributing their views and opinions. Many of the new respondents are not permanently located in China but are actively trading with Chinese suppliers, distributors, and customers.

The views and detailed findings of the report are worthy of close attention. These are not journalists, academics, advisors, or bureaucrats. Rather, they are Australian business people, leading Australian organisations, large, medium, and small, across most sectors of the economy and investment structures in rapidly changing Chinese markets. It is worth noting that China is the destination for 36 percent of Australia's exports, eclipsing by far its other trading partners.

Figure 02

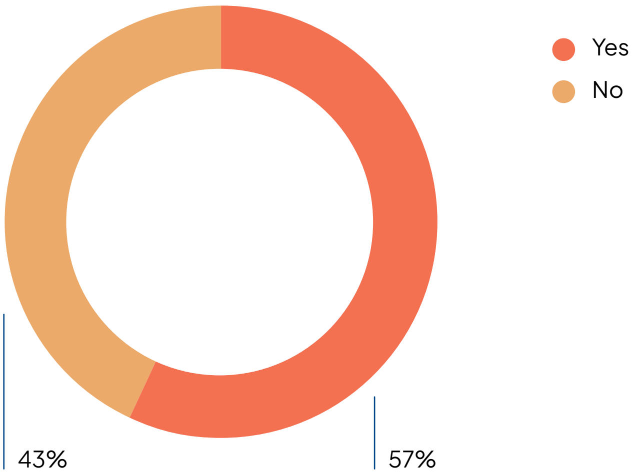
What percentage of time have you been in China – in the past 24 months/in the past 5 years?



When asked how much of their time was spent in China in the last two COVID-19 years, the responses bifurcated. It was either 0% of their time (those who couldn't get in) or 100% of their time (those who couldn't get out). Travel was interrupted, borders were closed, lockdowns applied. When answering the same question for the past five years, a more distributed pattern arises, suggesting a more transient leadership pre-COVID.

Figure 03

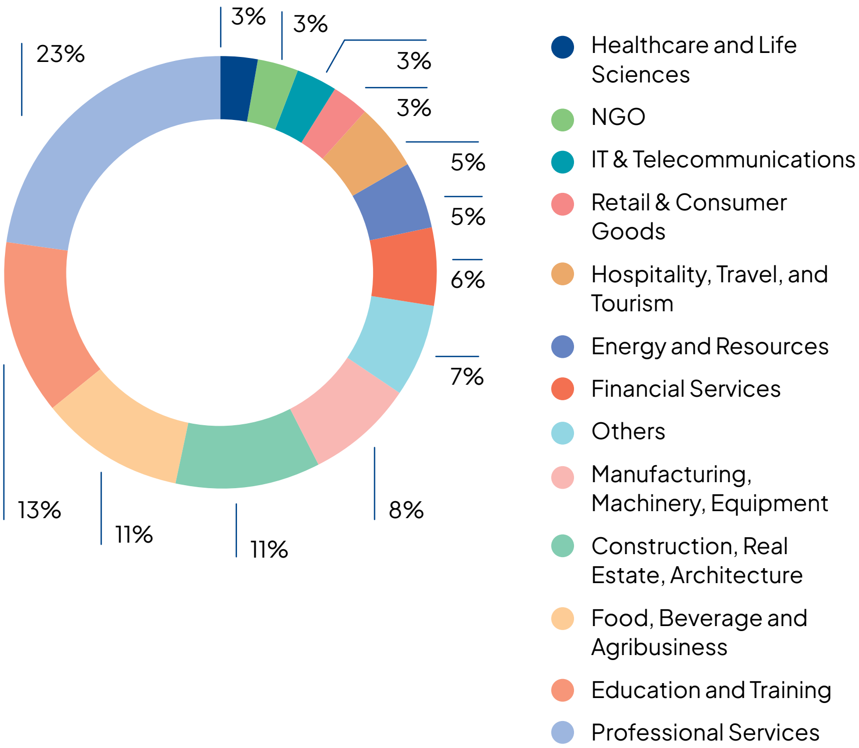
Does your organisation hold an Australian Business Number (ABN)?



57% of the survey respondents are registered in Australia with an Australian Business Number (ABN), a decrease compared to the 2018 cohort where 80% held an ABN. Those surveyed without an ABN would be registered in China (or in third countries).

Figure 04

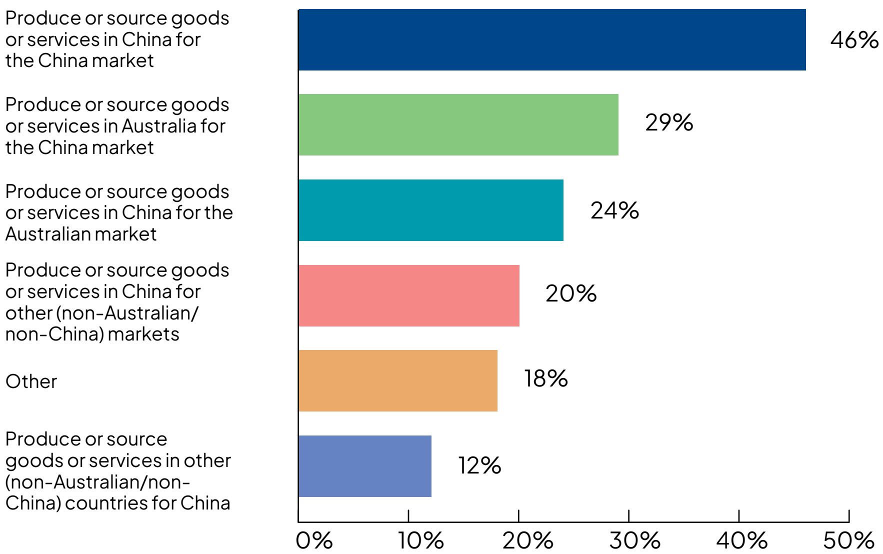
Which best describes the main industry you work in?



The DBIC survey was conceived as a longitudinal study of the experiences of Australian organisations. The three annual surveys provide a snapshot in time, but also allow for intertemporal comparisons. While there has been some attrition (replaced with new entrants), most organisations that featured in the 2017/18 surveys have 'survived' and participated again. The mix of industry/sector representation has therefore remained almost identical in the three DBIC surveys. The responding organisations cover a broad range of industries/sectors, dominated by service providers (professional and financial) followed by education, food and agribusiness producers, and construction. Manufacturing companies remain under-represented – as do health, retail and IT – sectors where Australian business is at a (comparative) disadvantage to China.

Figure 05

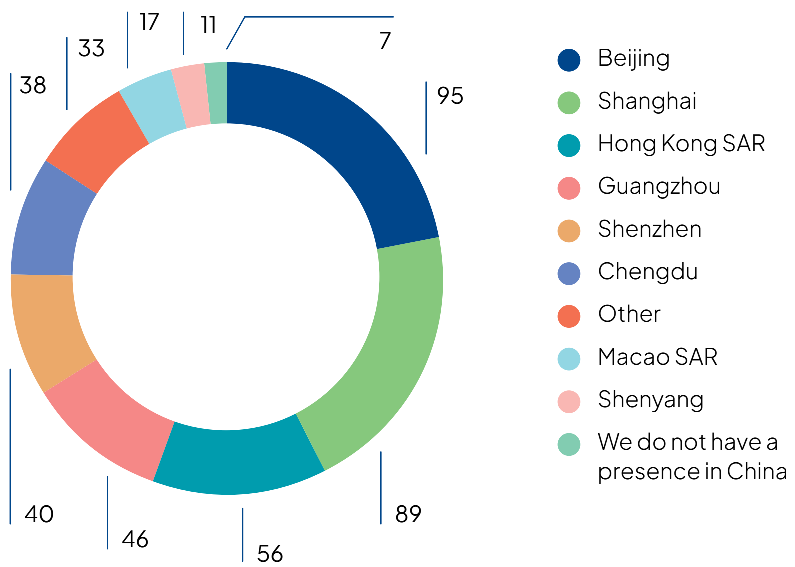
What is your organisation's primary strategy in China?



46% of respondents' strategy was to produce or source goods or services in China for the Chinese market while 29% of respondents produce or source goods or services in Australia for the China market. 24% of respondents produce or source goods or services in China for the Australian market. These strategic choices reveal a considerable increase in goods and services produced or sourced in China for the Chinese market since the previous surveys (from 19% in 2018 to 46% in 2022). It is suggested that lower cost of offshore production in the presence of unsaturated market demand, maintains its strategic appeal. At the same time, the increase in products or services sourced and produced in China for the Chinese market shows the growing importance that Australian companies attribute to the Chinese market.

Figure 06

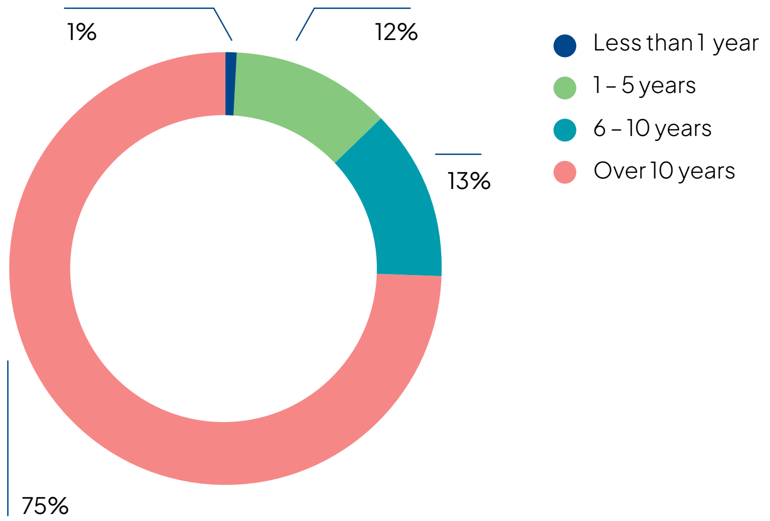
Where does your organisation have a presence in China?



Along with their primary strategy in China (focusing on low-cost production and market demand), the respondents also made strategic location choices. Beijing and Shanghai are often complementary "first tier" choices in building a presence in Mainland China. Hong Kong SAR, Guangzhou, Shenzhen, and Chengdu are "second tier" choices with Shenzhen and Chengdu becoming business hubs for hi-tech and resources business opportunities, respectively.

Figure 07

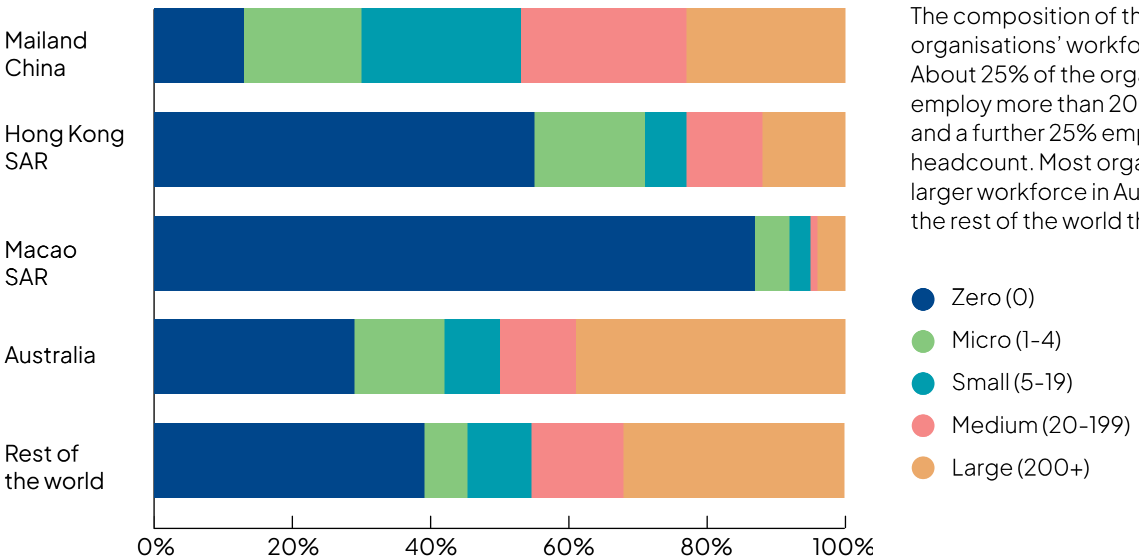
How long has your organisation been operating in China?



The survey sample has further matured since 2018. 75% of survey respondents have now been operating in China for over a decade. A further 13% has operated in China between 6 and 10 years. Newcomers (that is, arrivals in the last year) dropped from 7% of the sample to just one single new entrant in the past year.

Figure 08

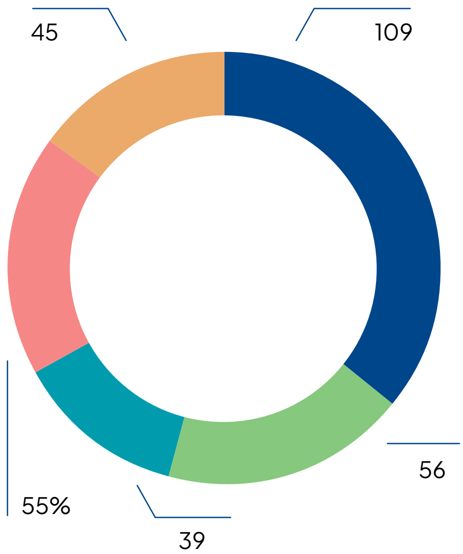
How many employees work for your organisation in the following countries/regions?



The composition of the surveyed organisations' workforce is a mixture. About 25% of the organisations employ more than 200 headcount and a further 25% employing 20–199 headcount. Most organisations have a larger workforce in Australia and/or in the rest of the world than in China.

Figure 09

Is your organisation a member of the following associations?



- AustCham China (including West China and South China chapters)
- AustCham Shanghai
- AustCham Hong Kong
- Australia China Business Council
- Other China business related association (specify)

Biased by invitation and selection into the survey sample, the majority of respondents are members of the various associations representing Australian businesses in China – most respondents through the regional chapters of AustCham, aligned with their (multiple) geographic operations.

The investment environment[2]

Almost five years since the initial survey on Doing Business in China, the investment environment has become significantly more challenging. Despite increasing complexity, China continues to offer ample opportunities for Australian organisations, with 58 percent of respondents still identifying China as a top three priority for global investment.

Following a precipitous decline from 6.7 percent in 2018 to 2.2 percent in 2020, China's economic growth rate rebounded spectacularly to 8.1 percent in 2021. While the 2022 growth rate is still unknown, in the first three quarters of 2022 China's GDP grew by 3 percent[3] on account of the spring lockdowns across China, but especially in Beijing and Shanghai. Nonetheless, China's growth rate and outlook remains the envy of most of the developed and emerging economies across the world.

In response to China's economic growth spurt in 2021, two-way trade in goods and services between Australia and China was again at record levels. China's resilient and strong market proves its value once more as our respondents show growing optimism for total investment in 2022, compared to 2020 and 2021.

For the future, an interesting scenario arises from the survey. Respondents showed divided notions to how their organisations will develop in China during 2022 compared to the rest of the world. But, when asked about China's inbound investment environment, a majority sees it deteriorating. Despite this, the respondents decided to increase investments in China. This is consistent with surveys by the American, European, British, German and other chambers of commerce in China, driven by its long term growth potential and to ameliorate any future international moves towards decoupling of economies.

2. Source: "Statistical Communique of the People's Republic of China on the 2021 National Economic and Social Development," National Bureau of Statistics of China, Feb 28,2021.

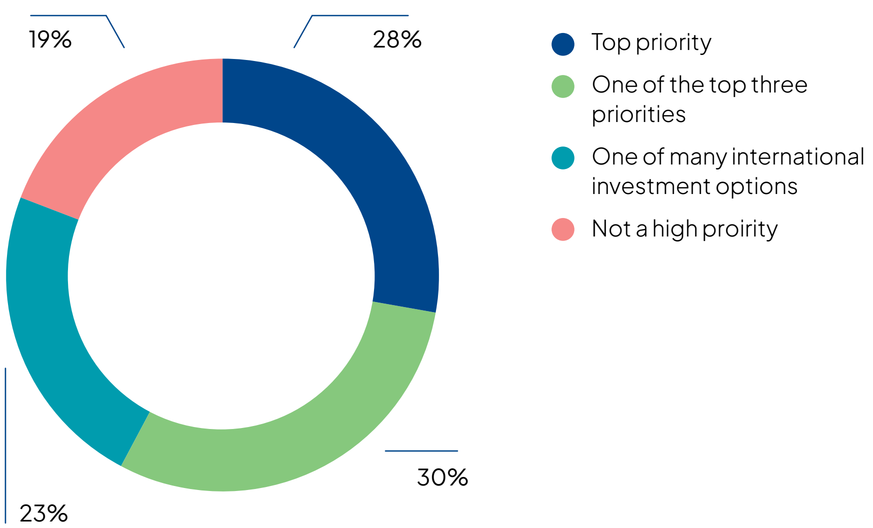
3. Source: http://www.stats.gov.cn/english./PressRelease/202210/t20221025_1889685.html

"Use senior business leaders with good relations with China to establish backdoor communications."

[anonymous respondent]

Figure 10

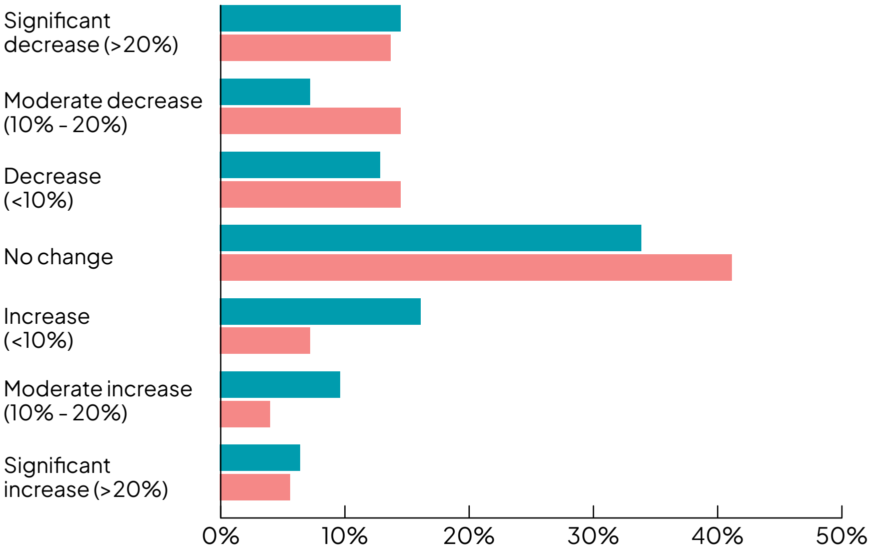
How does China rank in your organisation's global investment plans over the next three years?



When asked about the importance of China as a top three priority in their investment plans, 58% (from 81% in 2018) indicate that it is in their top three priorities, with 28% (45% in 2018) stating China as their top priority. A reassessment of importance, although still a very strong China focus. These results are consistent with US businesses, where 60% identifies China as a top three priority in their investment plans, with 22% stating China as their top priority.

Figure 11

How will your organisation's total investment in its China business change in 2021 and 2022, relative to 2019

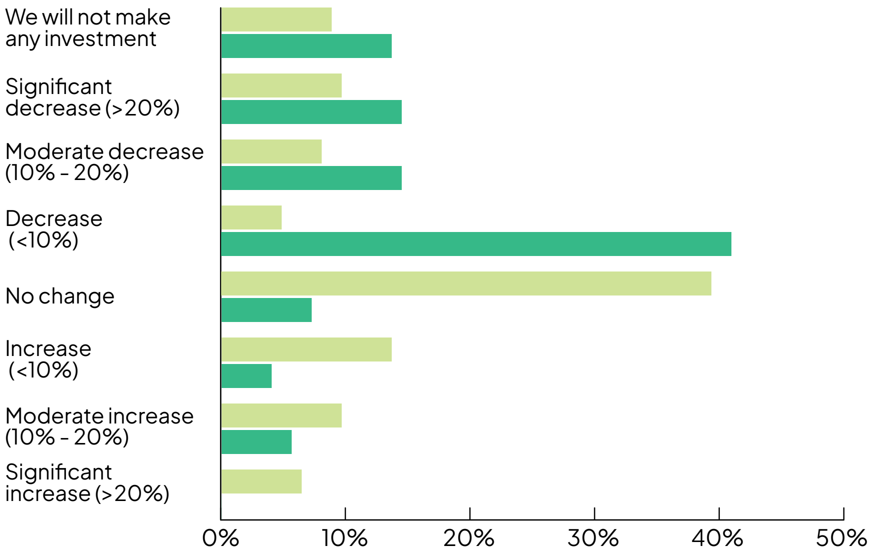


Consistent with indicating that China is still a top investment destination, when asked about total investment in 2020 and 2021, relative to 2019, the predominant answer is "no change", with a partial revival in 2022.

- In the Year Ending 31 Dec. 2022
- In the Year Ended 31 Dec. 2021

Figure 12

How will your organisation's total investment in its China business change in 2021 and 2022, relative to 2020?

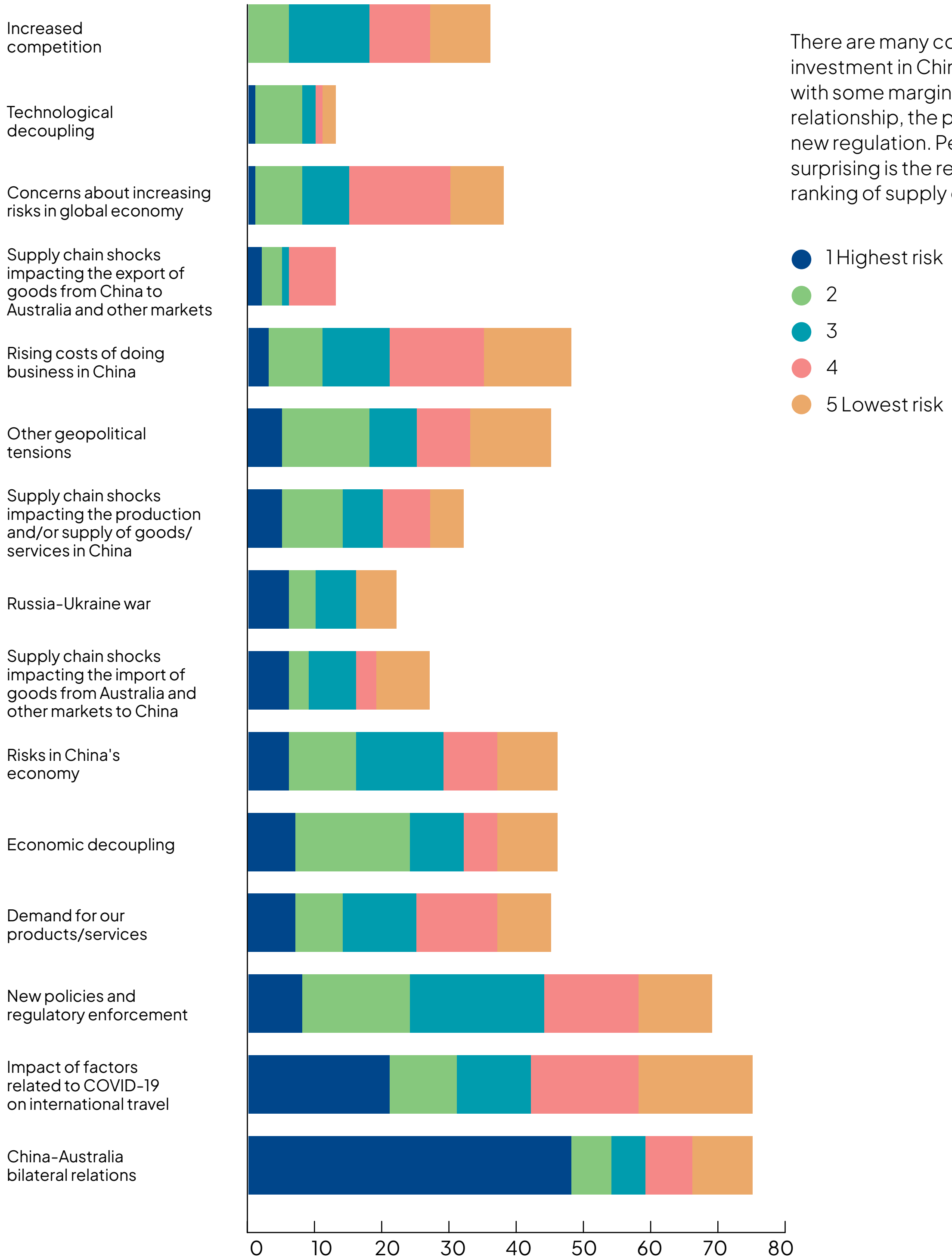


And when compared to 2020, we can see that there was a sharp decrease in total investment in 2021, with a growing optimism occurring in 2022.

- In the Year Ending 31 Dec. 2022
- In the Year Ended 31 Dec. 2021

Figure 13

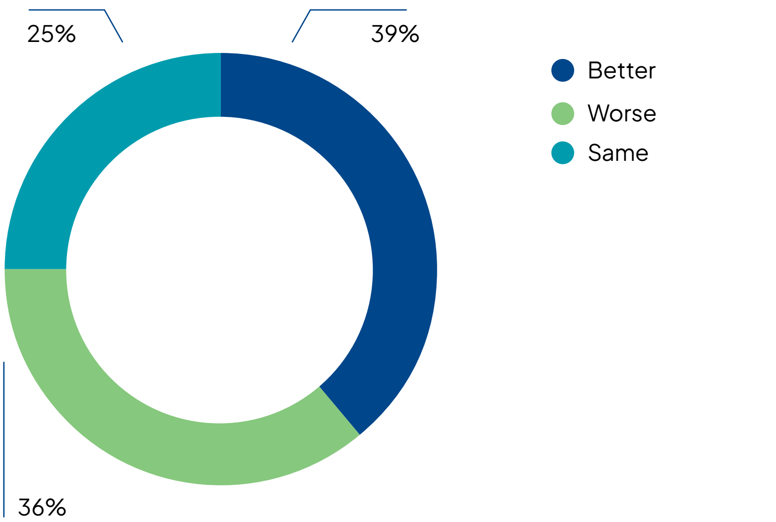
Rank the top 5 risks impacting your organisation's decision to make future investments in China?



There are many concerns that limit investment in China. The top 3 risks – with some margin – are the geopolitical relationship, the pandemic, and new regulation. Perhaps somewhat surprising is the relatively low risk ranking of supply chain shocks.

Figure 14

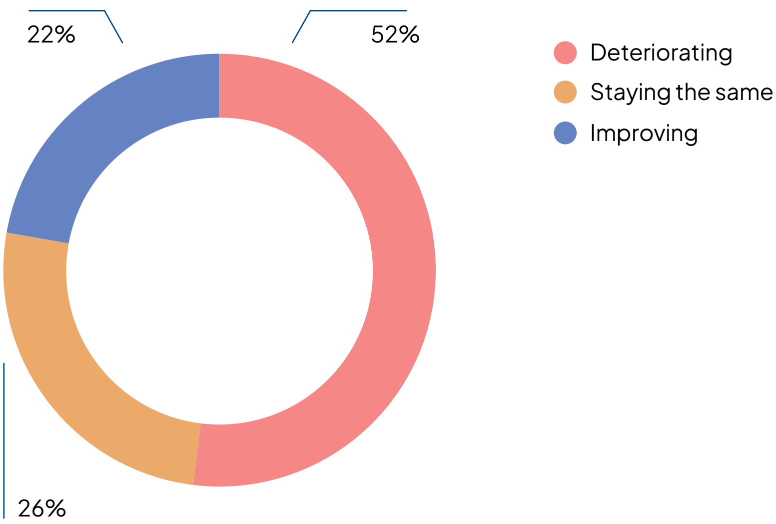
How do you think your industry in China will develop in 2022 compared to other markets in the rest of the world?



Uncertainty reigned in the assessment of the current environment. 39% believe that business will rebound (faster and stronger) in China, but there is an equal expectation (36%) that things may turn out worse.

Figure 15

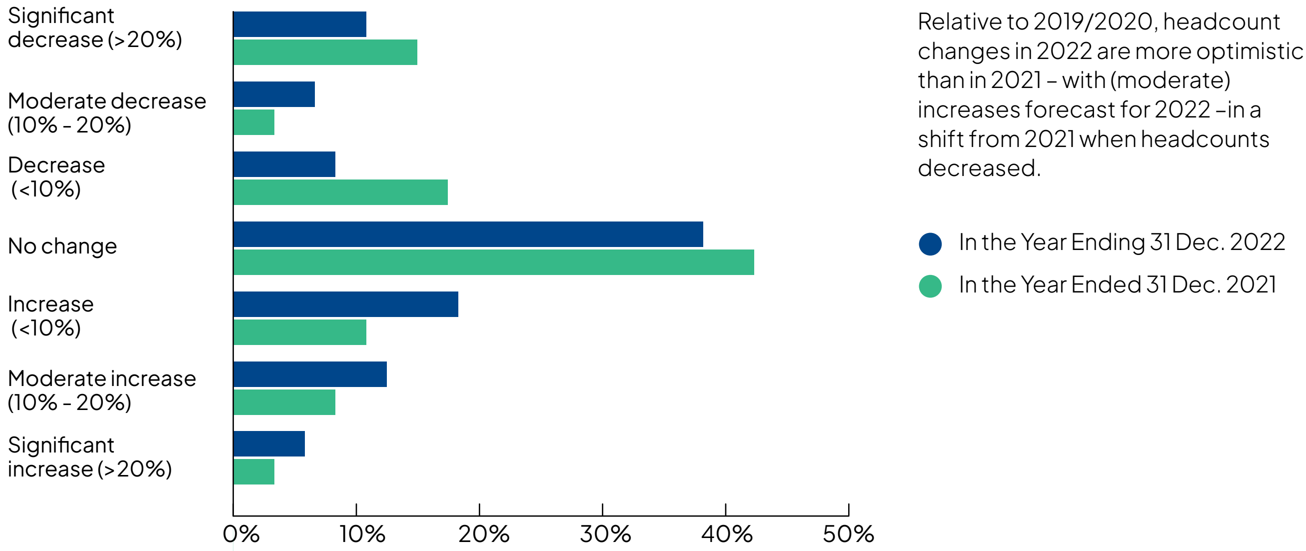
How do you feel about China's inbound investment environment?



When asked how respondents felt about China's investment environment, 52% see the environment deteriorating (up from 24% in 2018), and 22% see it improving. Despite the negative results, only a small number are taking action. Some are even expecting to increase their investment in China, which seems to imply that the problem is not the market (long-term) but the circumstances (short-term). The benefits of waiting must outweigh the costs of withdrawing from their China business.

Figure 16

How will your organisation's FTE headcount in its China business change in 2021 and 2022, relative to 2019?



Relative to 2019/2020, headcount changes in 2022 are more optimistic than in 2021 – with (moderate) increases forecast for 2022 –in a shift from 2021 when headcounts decreased.

Figure 17

How will your organisation's FTE headcount in its China business change in 2021 and 2022, relative to 2020?

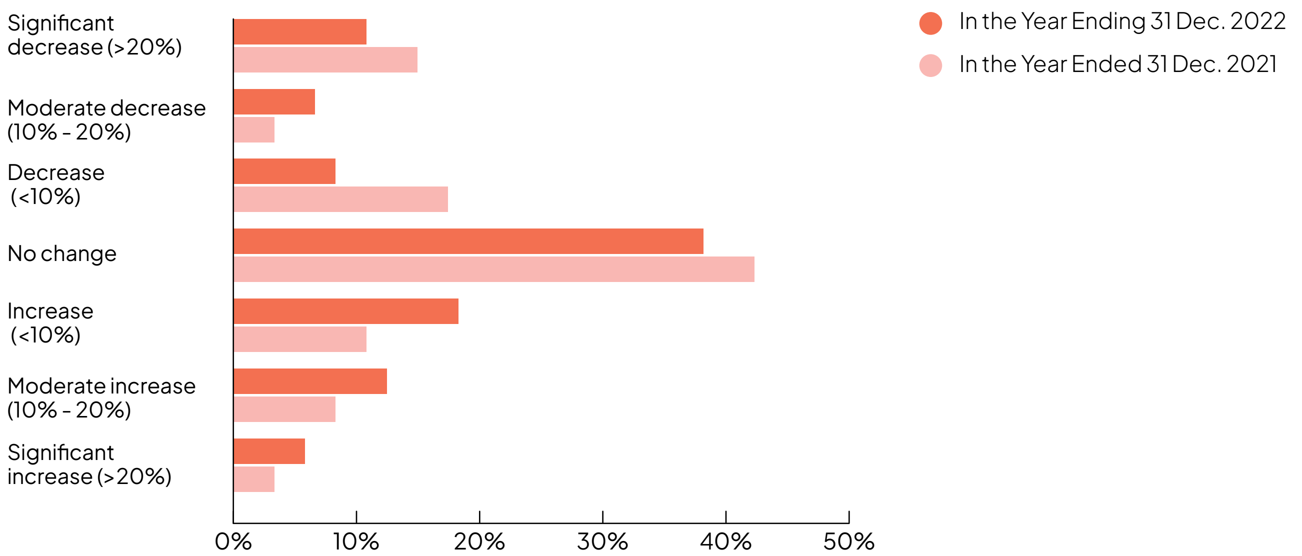
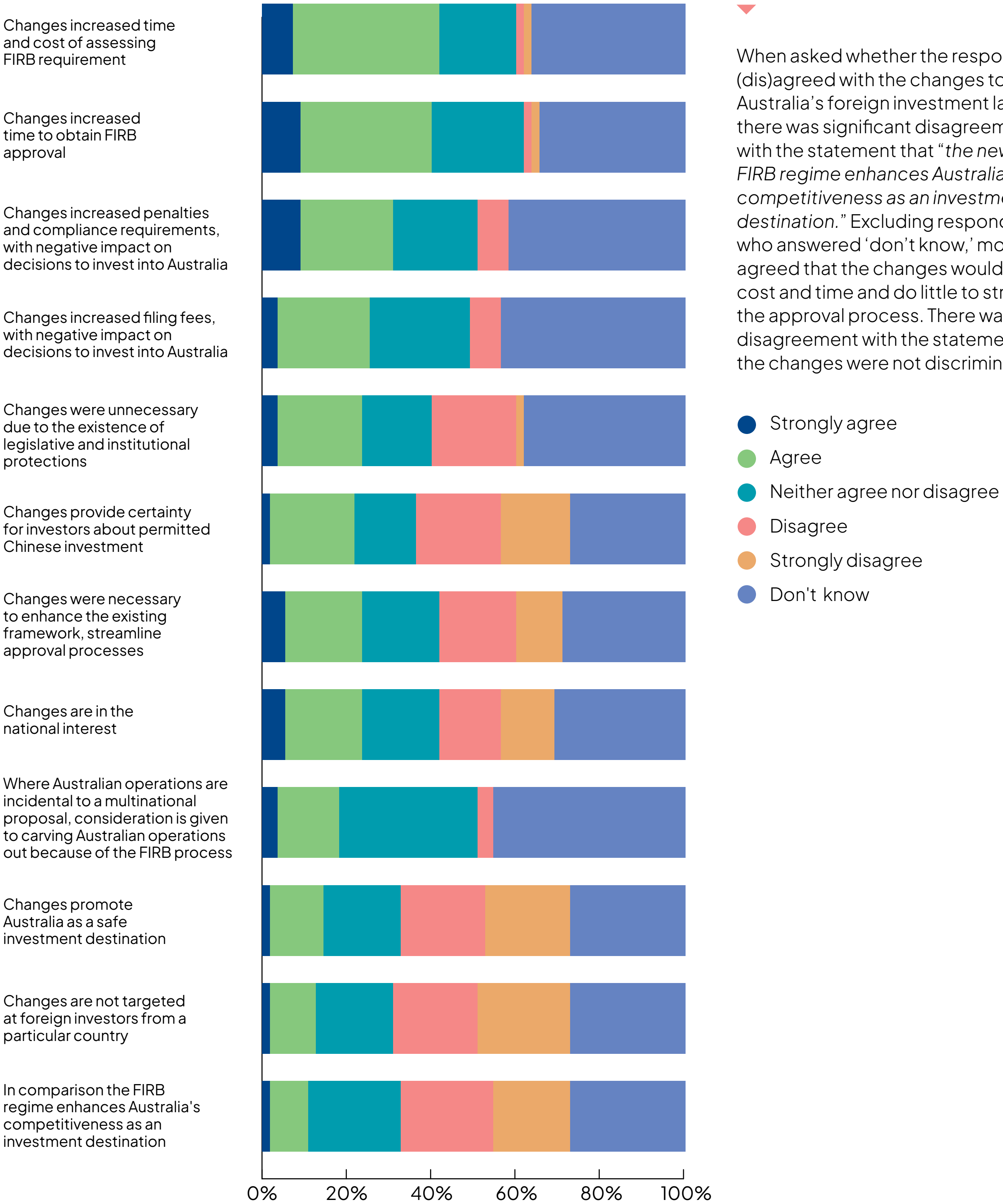


Figure 18

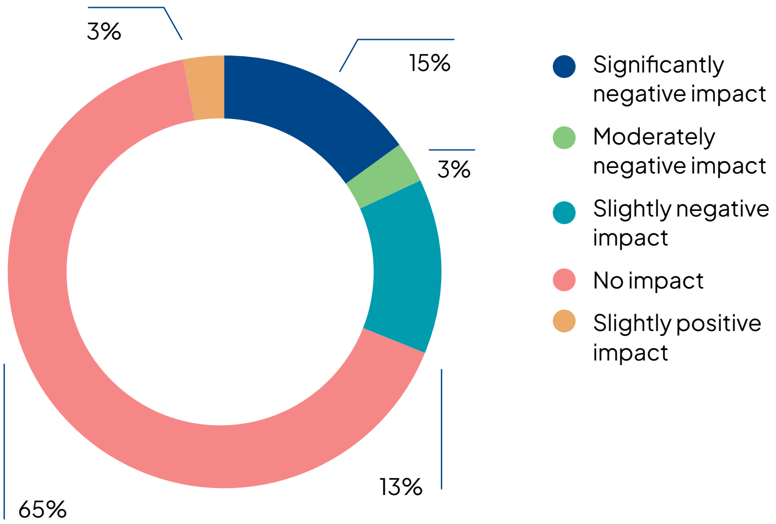
Consider whether you agree or disagree with the statements in relation to Australia's foreign investment laws (FIRB), which came into effect in 2021?



When asked whether the respondents (dis)agreed with the changes to Australia's foreign investment laws, there was significant disagreement with the statement that "*the new FIRB regime enhances Australia's competitiveness as an investment destination.*" Excluding respondents who answered 'don't know,' most agreed that the changes would impose cost and time and do little to streamline the approval process. There was also disagreement with the statement that the changes were not discriminatory.

Figure 19

How have the changes to Australia's Foreign Investment Review Board regime impacted your China outlook directly or indirectly?



65% of the respondents measure no impact on their China outlook due to the new FIRB. The remaining respondents are negatively disposed following the new foreign investment law.

China's business climate

Two and a half years into the global pandemic, China is making a strong economic recovery, albeit tempered by geopolitical tensions, ongoing risk of COVID-19 outbreaks, and a war in Ukraine. International macroeconomics have become dominated by a mix of rising inflation, increasing interest rates, cost of living challenges and risk of stagflation spreading globally.

The impact of these external events temper China's business climate. Conversely, China's inflation rate is under control at 2.5 percent, though concerns persist with hesitant consumer consumption, property markets under stress, while youth and graduate unemployment are nearing 20 percent. The country's zero COVID-19 policy and its consequent limitation for travel, both locally and international, is noted by respondents as a top challenge for their China business.

Despite the complexity, respondents rate the ease of doing business in China as improved compared to 2018. Moreover, respondents identify China's climate change commitments as opportunities for Australian organisations to engage with China.

With its 14th five-year plan from 2021 to 2025 firmly underway, China has embarked on a path of business environment improvement. And not just to facilitate domestic business but extending to foreign enterprises. Recent policies include tax reforms, removal of foreign ownership limits, and streamlined foreign investment laws. The plan also creates regional opportunities for foreign business, including improved access to free trade zones, Special Administrative Regions (SAR) and the Greater Bay Area.

China's ongoing transition to a services and domestic consumption-oriented and technology-infused economy brings additional opportunities for Australian businesses. In its pursuit of continued high economic growth for delivering prosperity, China is seeking to shift from volume-based growth to quality growth. That includes a focus on services, including within finance, healthcare, education, and science, IT/digital technology and the green economy. Areas where Australian businesses can meaningfully engage.

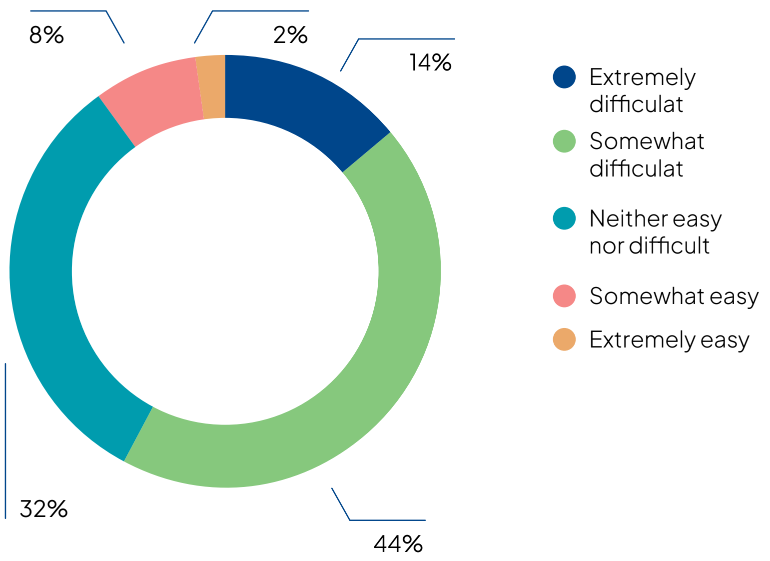
So, the settings are there, but nobody is under any illusion that doing business in China is easy. This survey teases out the challenges and pain points for new Australian entrants.

"China is keen to onshore technological development, particularly in industries that are critical to industrial growth."

[anonymous respondent]

Figure 20

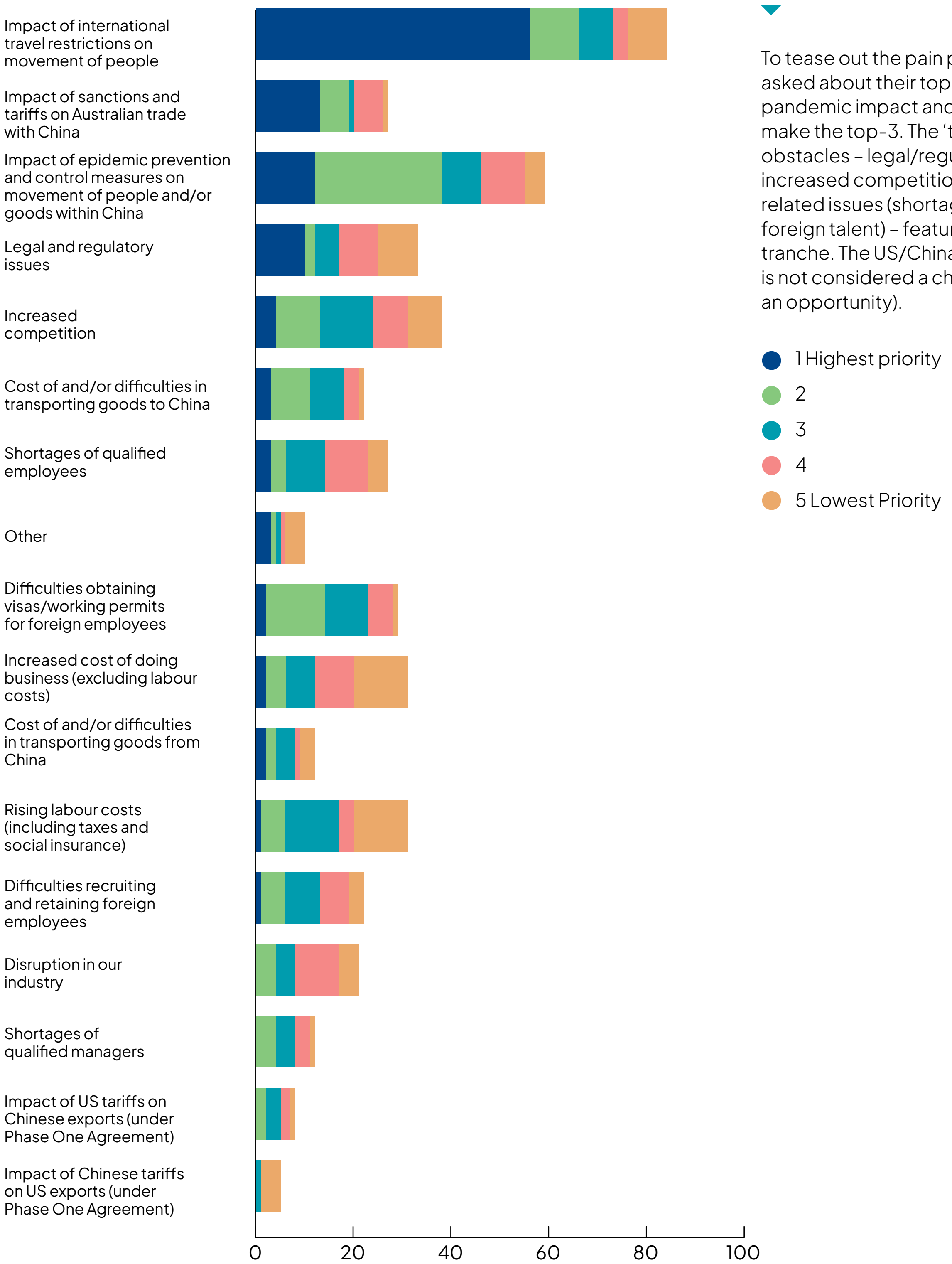
How would you rate the ease of doing business in China?



Is it getting easier doing business in China? All-in 58% of the respondents rank the degree of difficulty from somewhat to extremely. Interestingly, that number is down from 2018. We gather that with the 'maturing-operations-in-China' of the surveyed organisations, they have become more adept in navigating the difficulties. Still, only 10% of respondents find doing business in China (extremely or somewhat) easy.

Figure 21

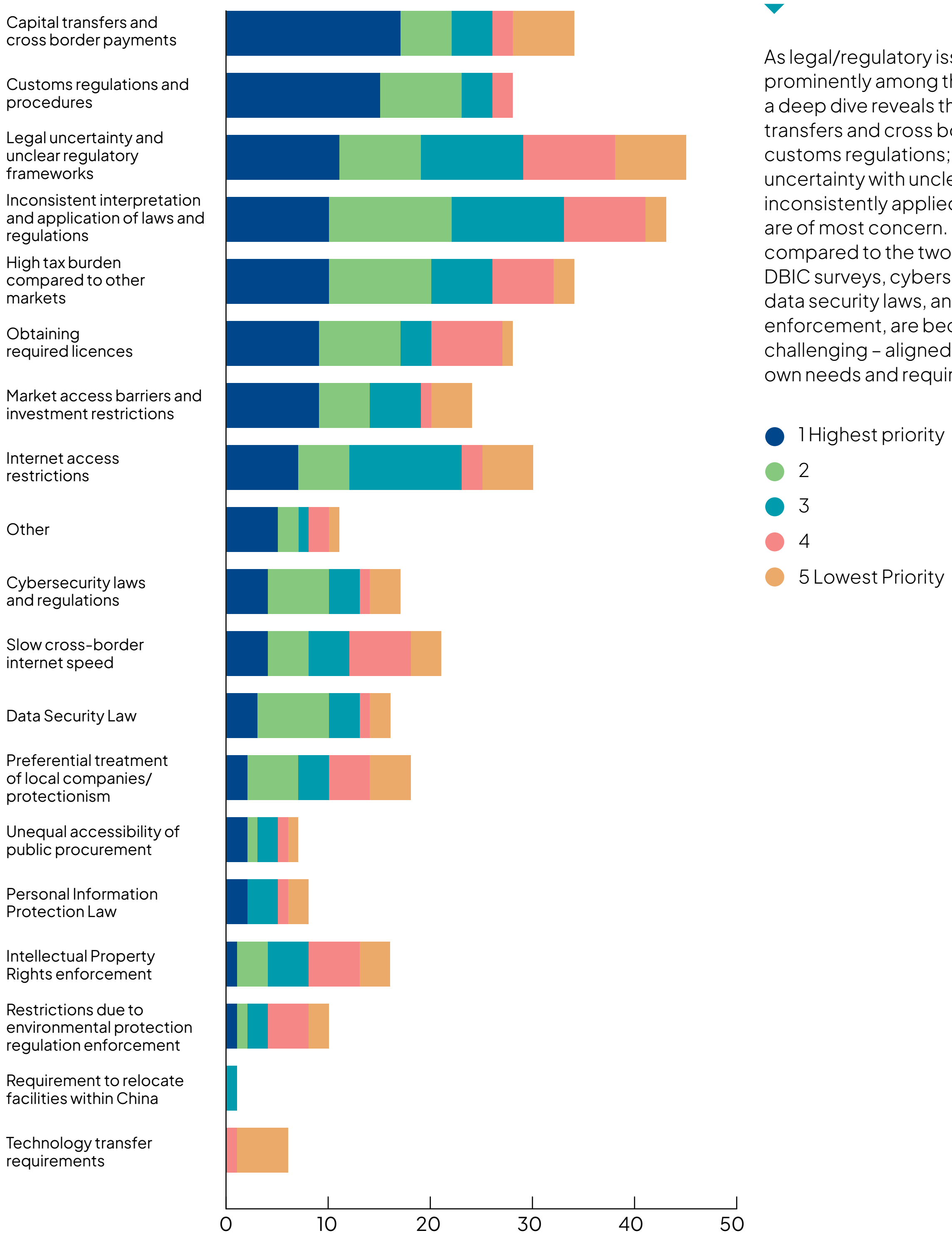
What are the top challenges facing your organisation's business in China?



To tease out the pain points, when asked about their top challenges, the pandemic impact and trade barriers make the top-3. The 'traditional' obstacles – legal/regulatory issues, increased competition, and employee related issues (shortage, labour cost, foreign talent) – feature in the next tranche. The US/China trade dispute is not considered a challenge (nor an opportunity).

Figure 22

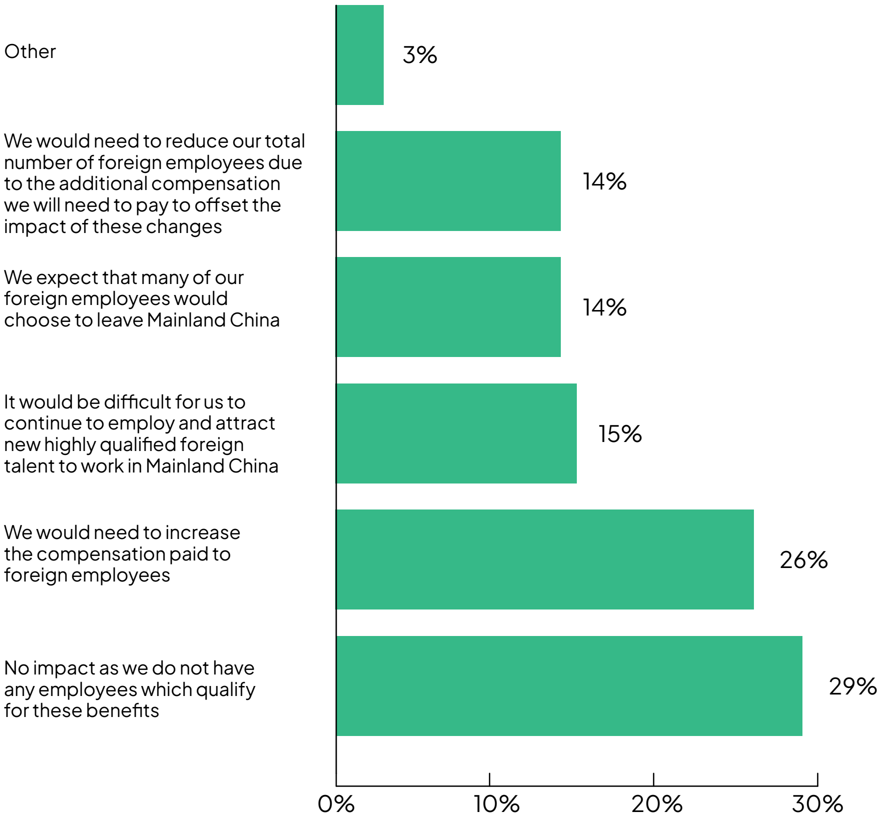
What are the top challenges for your China business relating to the operation and enforcement of laws and regulation in Mainland China?



As legal/regulatory issues feature prominently among those challenges, a deep dive reveals that: capital transfers and cross border payments; customs regulations; and legal uncertainty with unclear and inconsistently applied regulation; are of most concern. Interestingly, compared to the two earlier DBIC surveys, cybersecurity and data security laws, and IP rights enforcement, are becoming less challenging – aligned with China's own needs and requirements.

Figure 23

What would be the impact on your business in China of a removal of the preferential tax treatment on fringe benefits for expatriates working in China?



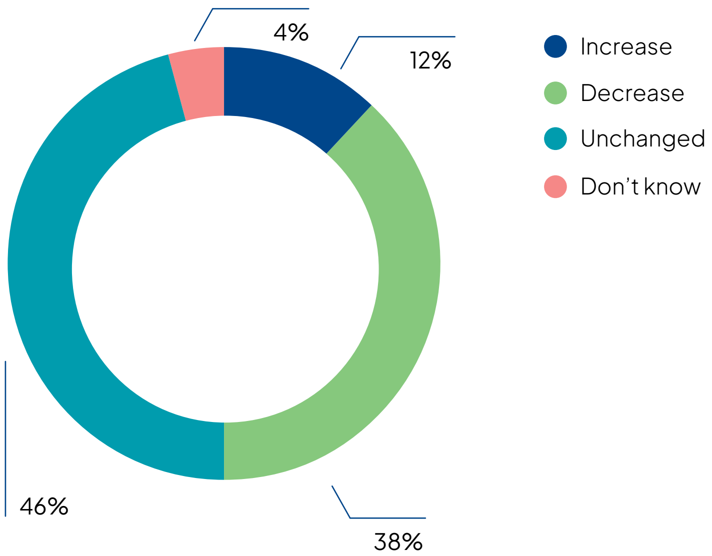
When asked about removal of the tax benefits for expatriates working in China, the respondents indicate that this may lead to a flight of foreign talent, or significantly increase labour costs to counter this *foreign flight*.

> "Regulations are increasingly transparent and IP enforcement is improving."

[anonymous respondent]

Figure 24

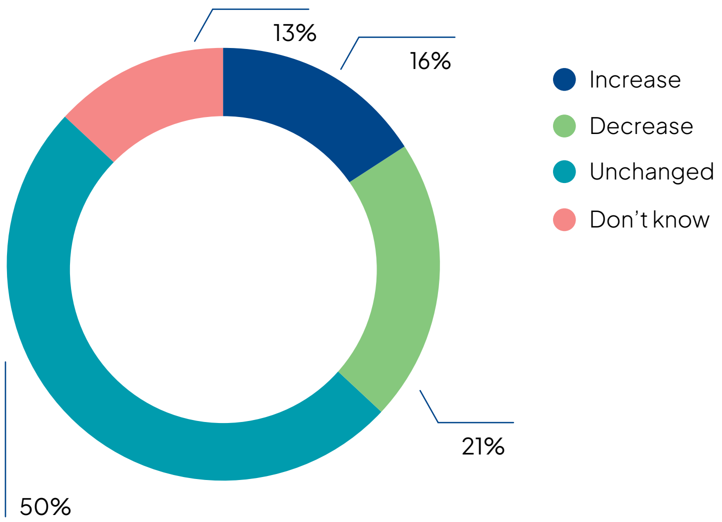
How has the number of employees in your organisation in Mainland China who are not Chinese citizens changed over the past 3 years?



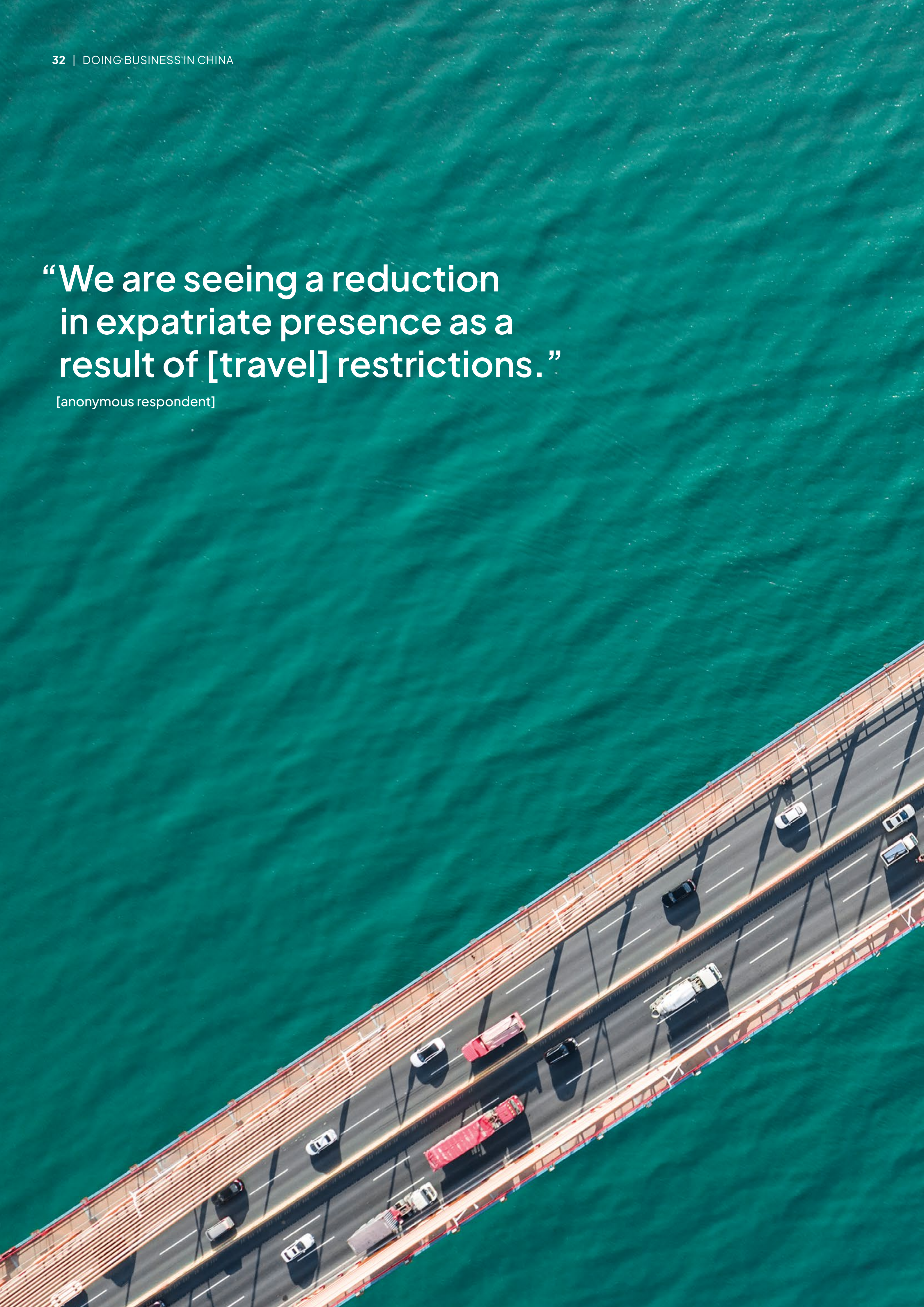
Some of this tax-induced foreign flight is included in the 38% of respondents who have seen a decrease in the number of their foreign employees. Other reasons – substantially more important – include the impact of the pandemic, China travel restrictions, and the tensions in geopolitical relations.

Figure 25

How will the number of employees in your organisation in Mainland China who are not Chinese citizens change over the next 3 years?



To verify whether the contraction in foreign employees will continue, the respondents were asked to look ahead. They now forecast a return to normal turnover over a three-year period and a much larger proportion that predicts no change.

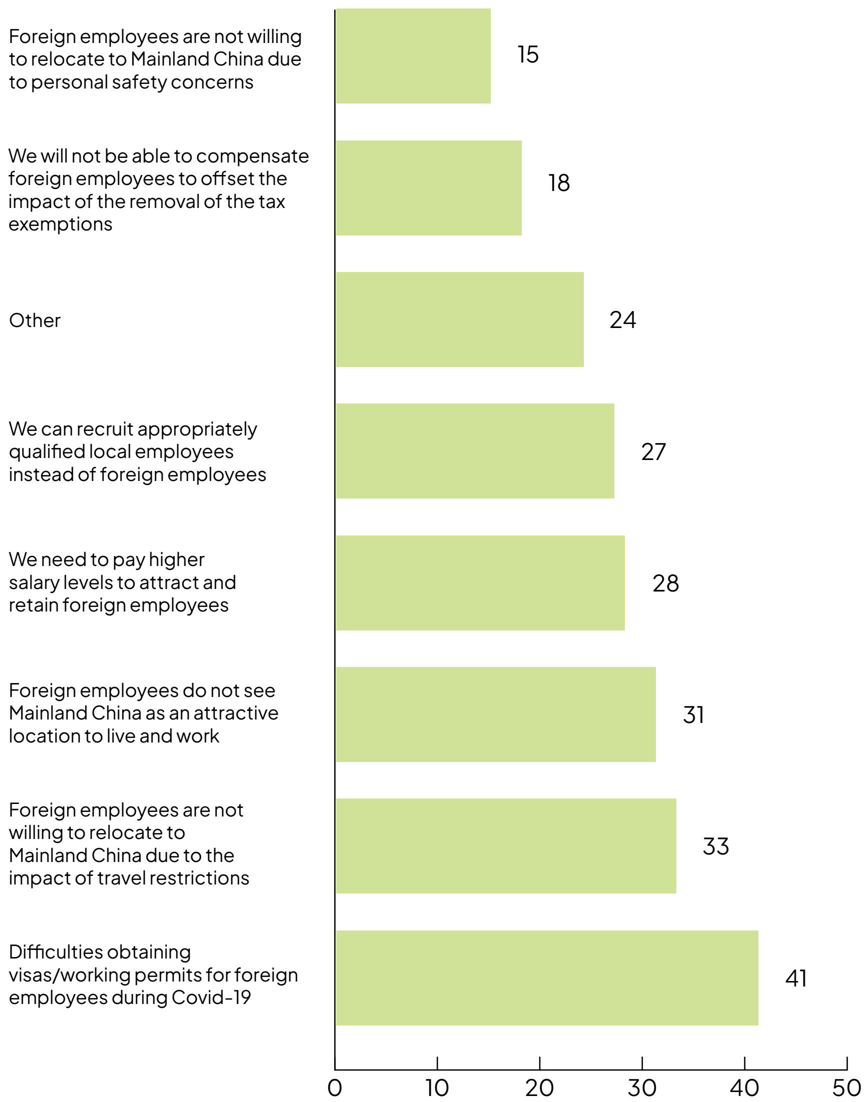


“We are seeing a reduction in expatriate presence as a result of [travel] restrictions.”

[anonymous respondent]

Figure 26

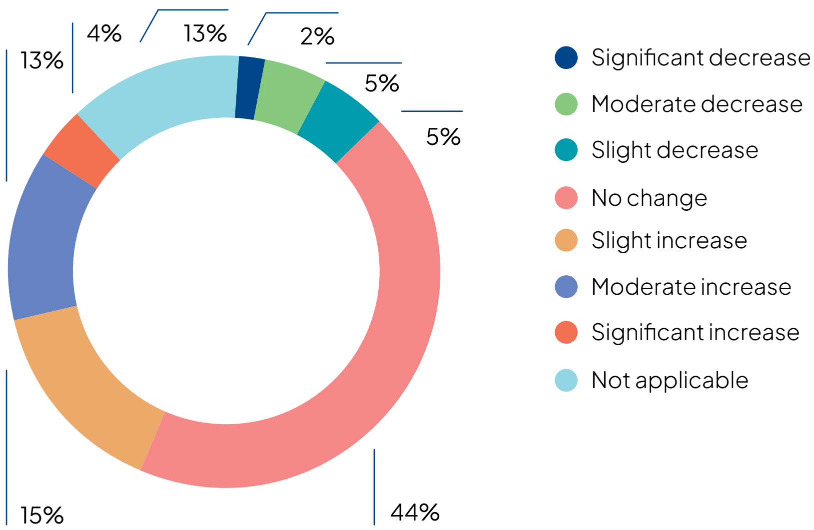
What are the reasons for the change in the number of employees in your organisation in Mainland China who are not Chinese citizens ("foreign employees")?



To better understand the reasons for the decrease in foreign employees, we asked for their specific reasons. The two most important reasons were indeed COVID-19 related. Third on the list is the perception of Mainland China as an unattractive location to live and work. Despite improving air quality, other dimensions to liveability also need addressing.

Figure 27

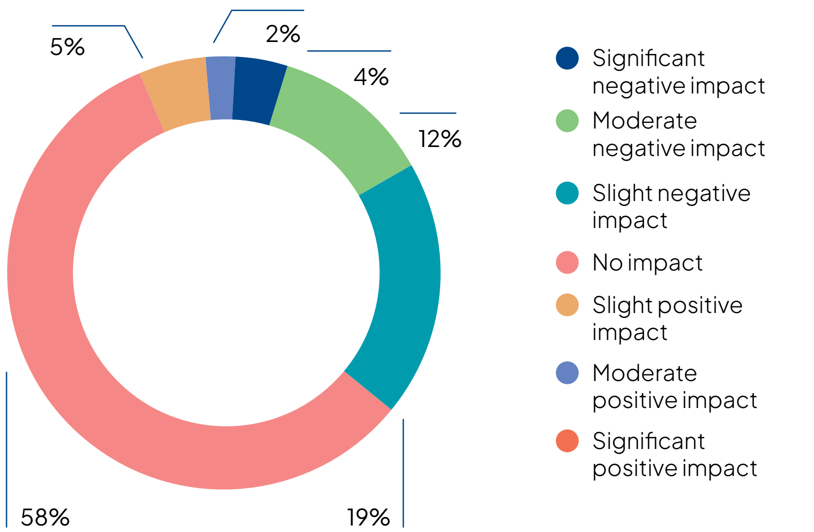
Have you noticed any change in the frequency and level of attention or engagement related to your firm from Chinese authorities, including industry-wide regulatory change in the last year?



A recurring question on China's business climate considers the impact of, and changes in public and regulatory scrutiny. While 44% observed no change, 32% (12%) are experiencing an increase (decrease) in attention. Those numbers were similar in the 2018 survey.

Figure 28

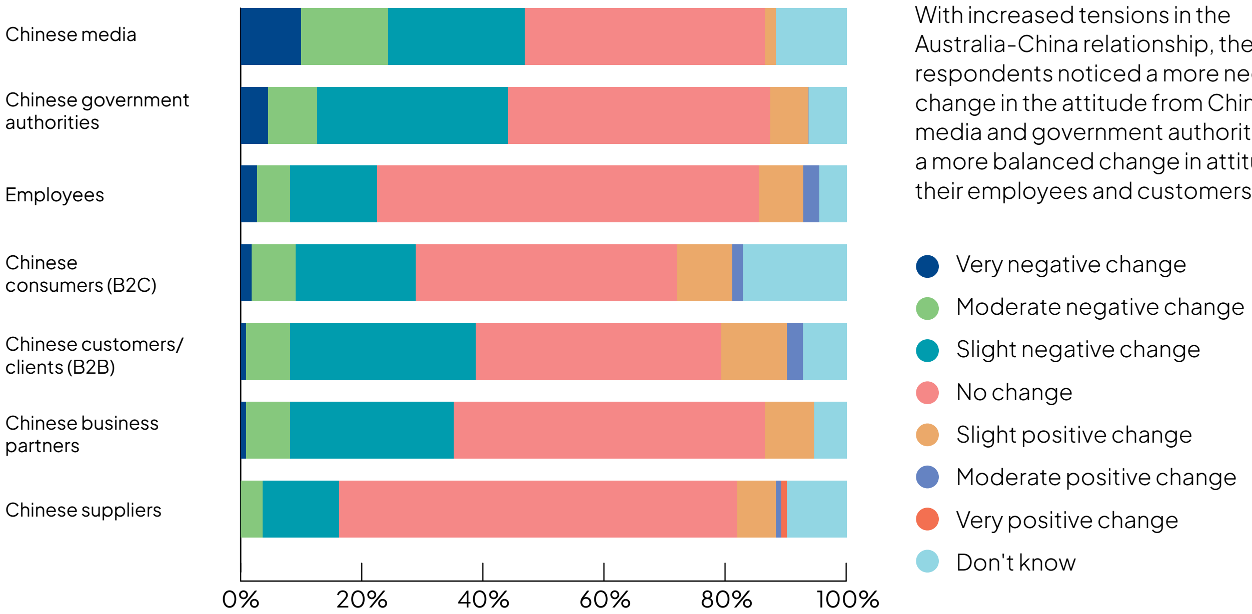
How have the changes (if any) impacted your business?



It is one thing to notice increased attention/scrutiny, another altogether in terms of its impact on doing business. On this occasion, 58% noticed no impact on their business operation. Of the remaining 42%, the impact has mostly been moderate to slight negative (31%). For comparison, in the 2018 survey the impact was perceived to be much more negative.

Figure 29

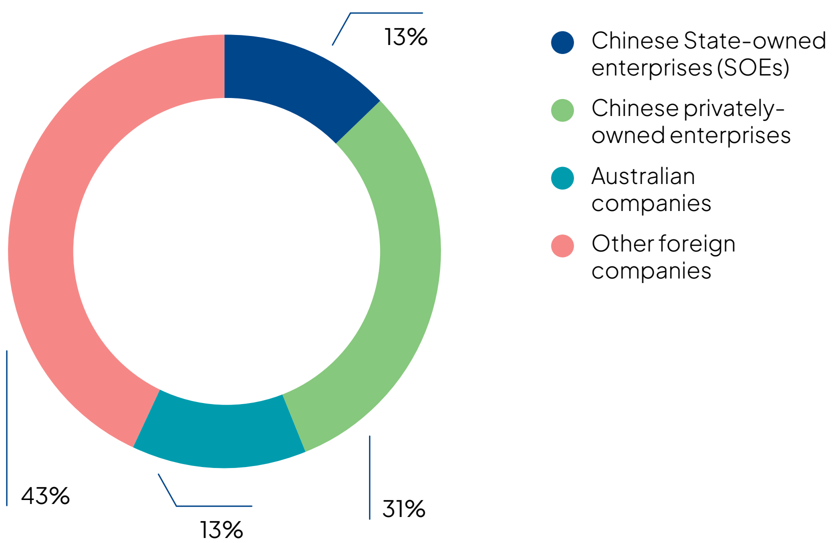
Have you noticed any change in the attitudes from the following stakeholders towards your organisation in the period since 1 January 2020?



With increased tensions in the Australia-China relationship, the respondents noticed a more negative change in the attitude from Chinese media and government authorities, but a more balanced change in attitude by their employees and customers.

Figure 30

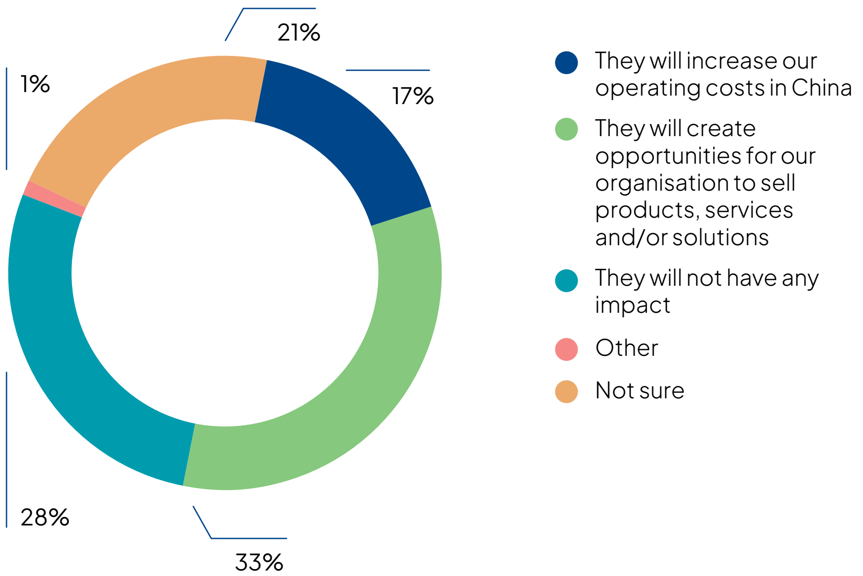
Who are your key competitors in China?



China's competitive environment is changing. Key competitors for the respondents are now either Chinese privately-owned enterprises or other foreign companies, a combined 74% of key competition. SOEs – reported as a major competitor in the 2017/18 surveys – are now deemed less important.

Figure 31

What impact(s) will the laws, regulations, policies, and actions that China implements to achieve its carbon peaking and carbon neutrality goals have on your organisation's China business?



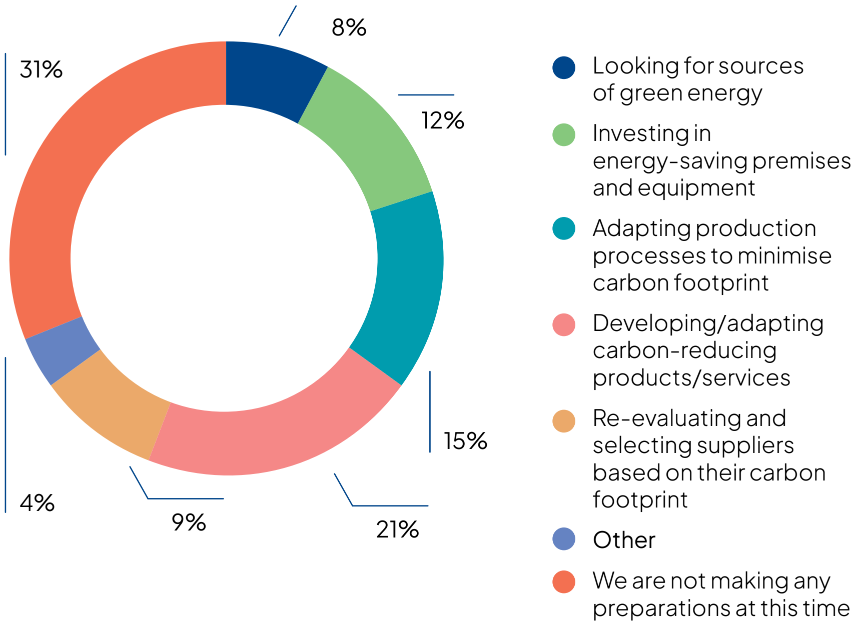
China's environmental policies seem to lay fertile ground for new business opportunities to engage with China. 33% of respondents believe that Chinese actions towards the 2030 peak in CO2 emissions and the 2060 goal of carbon neutrality will create opportunities for their organisation's China business. It is also noted that a smaller group of respondents (17%) anticipates increased costs for operating in China.

> "Seek areas of mutual interest… encourage climate-related low carbon cooperation."

[anonymous respondent]

Figure 32

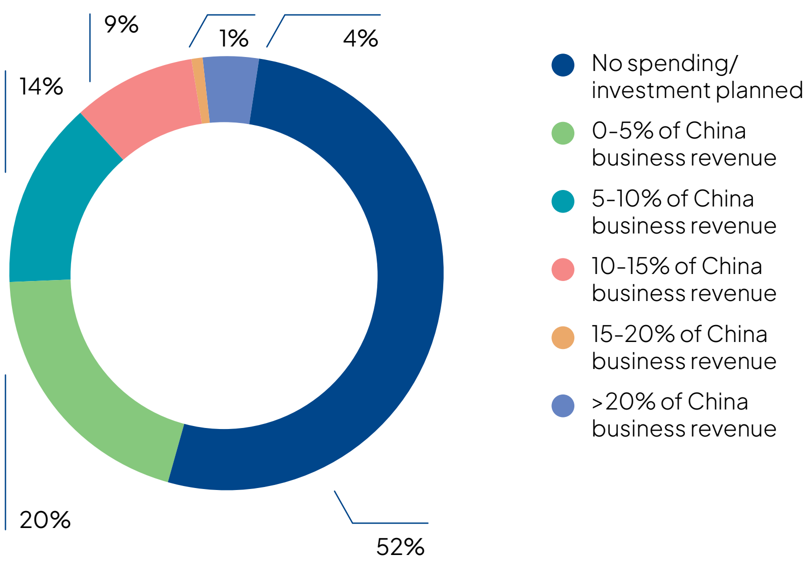
What actions is your organisation already taking or planning to take in respect of your China business in response to and/or expectation of these requirements?



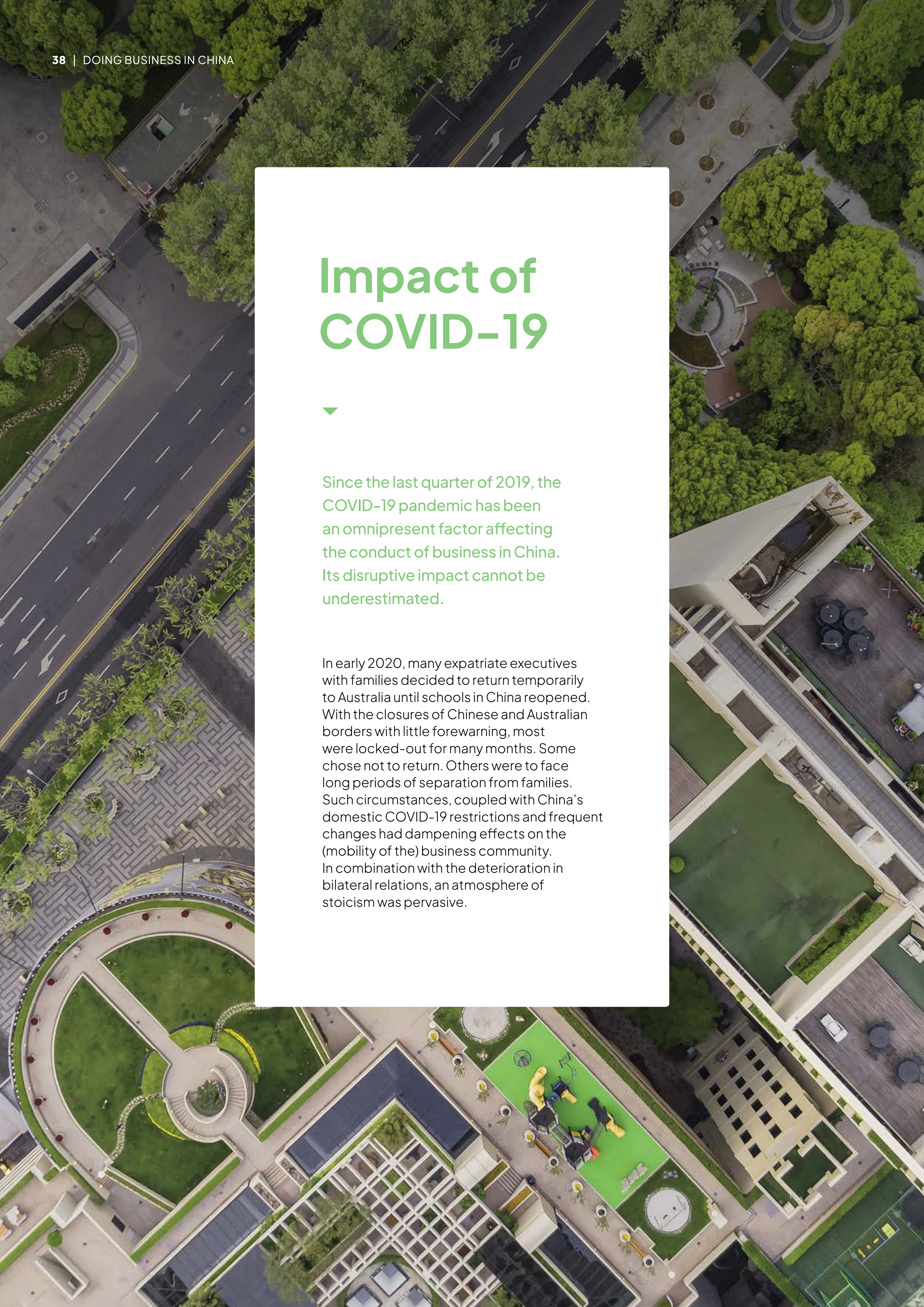
To reduce cost and comply with new environmental regulations and policies, 65% of the survey participants are already engaged in energy saving and carbon reduction processes, products and services. This speaks to how proactive the surveyed organisations are in fighting climate change.

Figure 33

On average, how much does your organisation plan to spend/invest on these actions in each year up until 2030?



20% invests very little (0–5% of China revenue) on climate change actions, followed by equal parts of 14% which invest 5–10% and more than 10% of business revenue. Still, 52% do not have any climate change investment planned. The economic and business uncertainty seems to be holding back more ambitious investment.



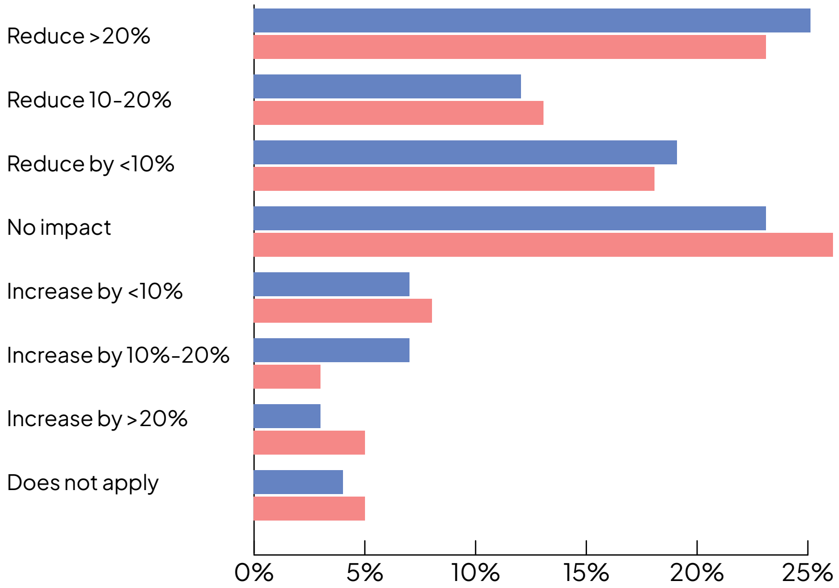
Impact of COVID-19

Since the last quarter of 2019, the COVID-19 pandemic has been an omnipresent factor affecting the conduct of business in China. Its disruptive impact cannot be underestimated.

In early 2020, many expatriate executives with families decided to return temporarily to Australia until schools in China reopened. With the closures of Chinese and Australian borders with little forewarning, most were locked-out for many months. Some chose not to return. Others were to face long periods of separation from families. Such circumstances, coupled with China's domestic COVID-19 restrictions and frequent changes had dampening effects on the (mobility of the) business community.
In combination with the deterioration in bilateral relations, an atmosphere of stoicism was pervasive.

Figure 34

What was the impact of COVID-19 on sales and profitability of your organisation's China business in 2021 compared to 2019?

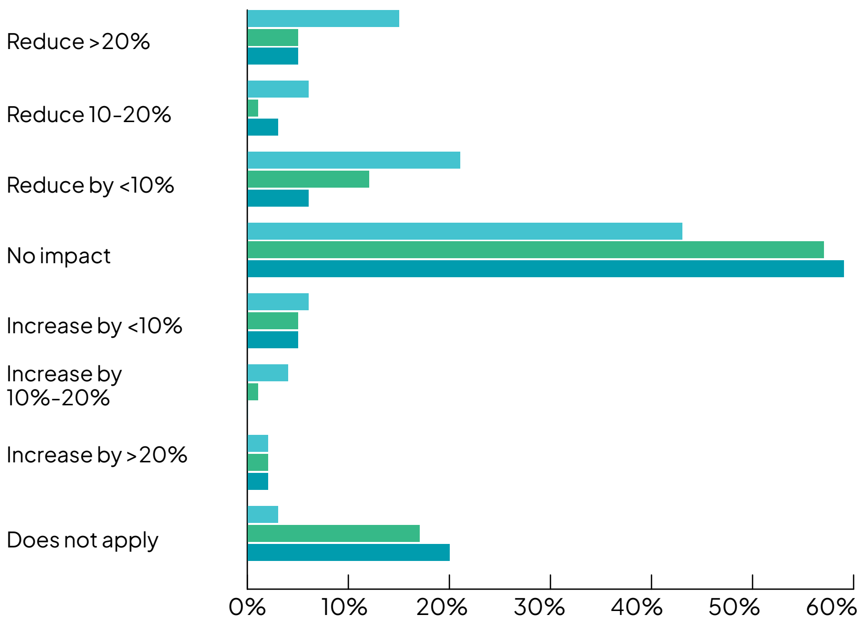


The impact of COVID-19 has been and continues to be significant on many dimensions of Doing Business in China. In relation to the financial outcomes, we asked about the COVID-19 impact. Both sales and profitability decreased significantly compared with 2019 levels. Three times as many respondents noted a decrease than respondents who noted an increase.

- Sales/Revenue
- Profitability

Figure 35

What was the impact of COVID-19 on FTE headcount (in China, Australia, and Rest of the World) of your organisation's China business in 2021 compared to 2019?

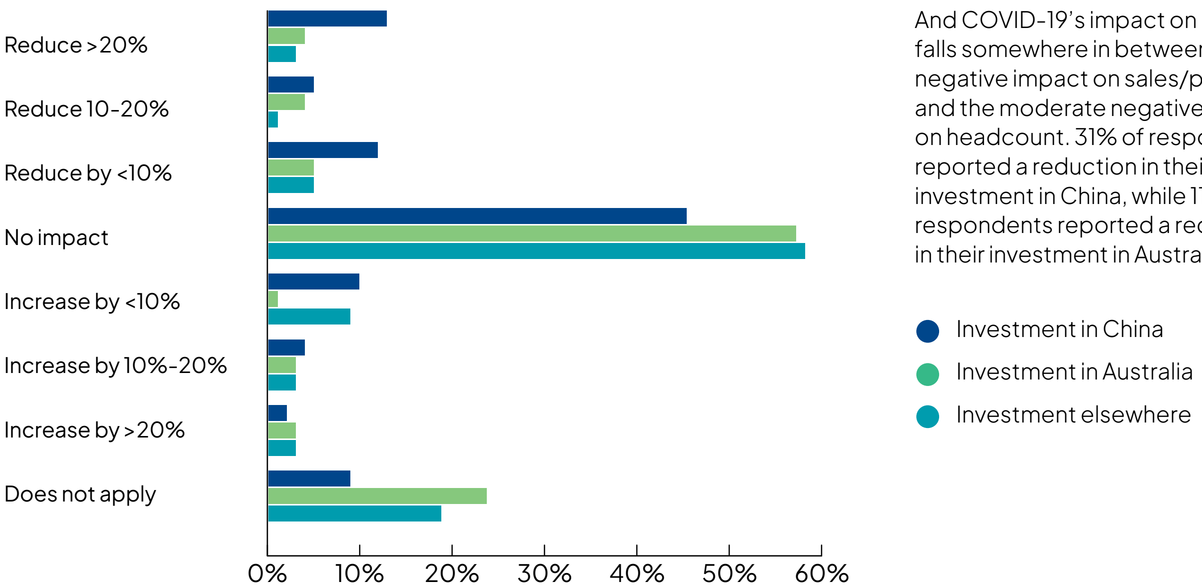


Headcount was also negatively impacted by COVID-19. But not nearly to the same extent as sales/ profitability. 36% of respondents reported a reduction in headcount in China. With very low Australian unemployment levels (and therefore limited interest to seek employment in China), the surveyed organisations adopted a strategy to minimise the risk of losing talent. The ability to effectively work-from-home maintained employee productivity for the surveyed organisations – even when this did not translate into sales.

- Full-Time Employment (FTE) Headcount in China
- FTE Headcount in Australia
- FTE Headcount elsewhere

Figure 36

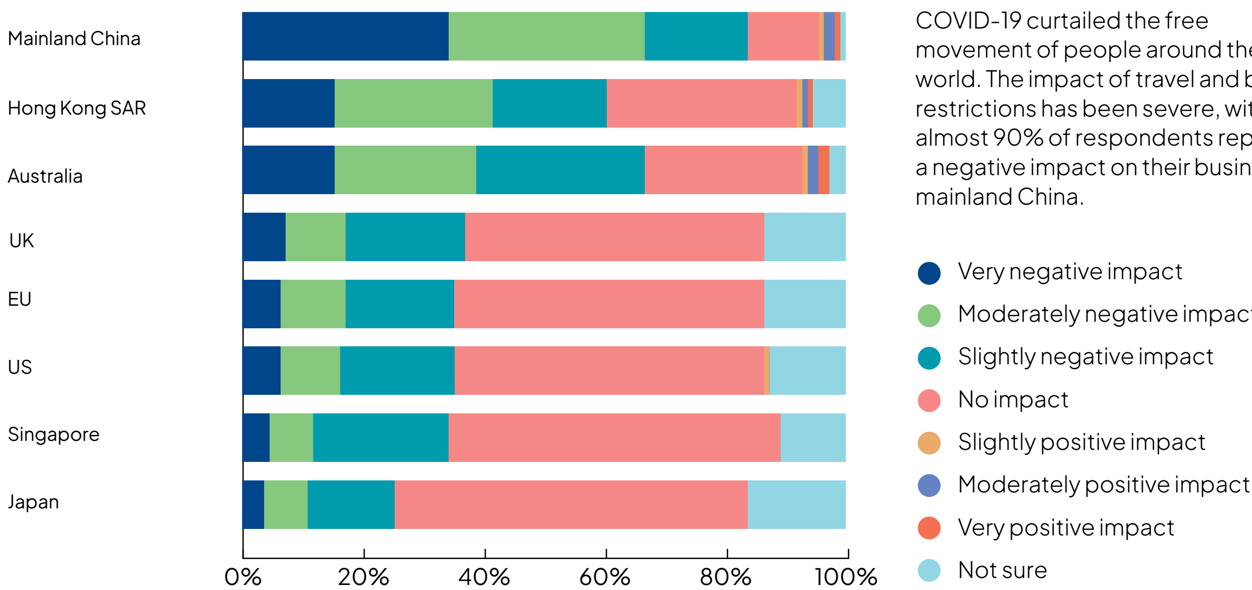
What was the impact of COVID-19 on investment (in China, Australia, and Rest of the World) of your organisation's China business in 2021 compared to 2019?



And COVID-19's impact on investment falls somewhere in between the high negative impact on sales/profitability and the moderate negative impact on headcount. 31% of respondents reported a reduction in their investment in China, while 11% of respondents reported a reduction in their investment in Australia.

Figure 37

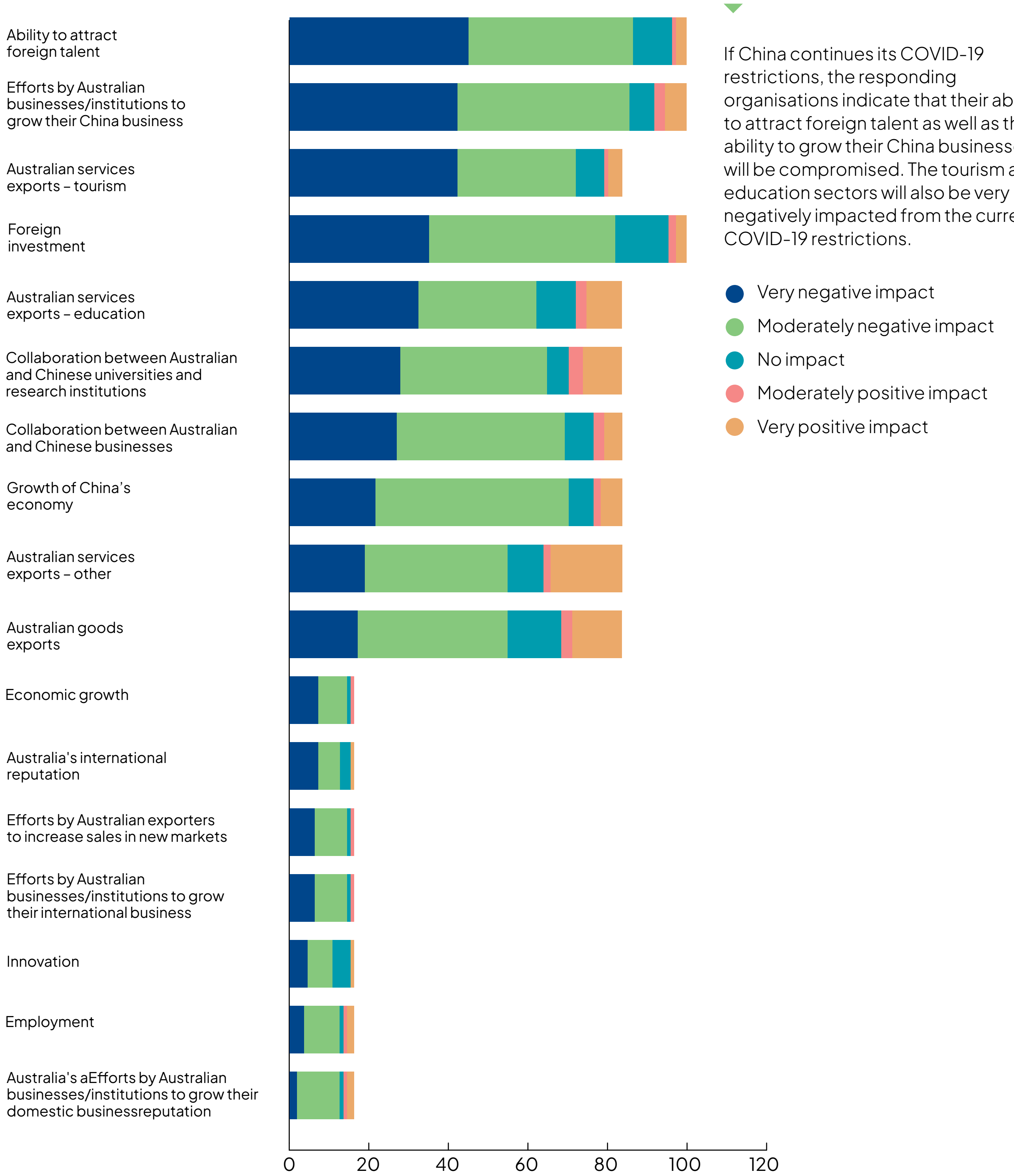
What is the impact of travel and border restrictions in the following countries and regions on your organisation's China business?



COVID-19 curtailed the free movement of people around the world. The impact of travel and border restrictions has been severe, with almost 90% of respondents reporting a negative impact on their business in mainland China.

Figure 38

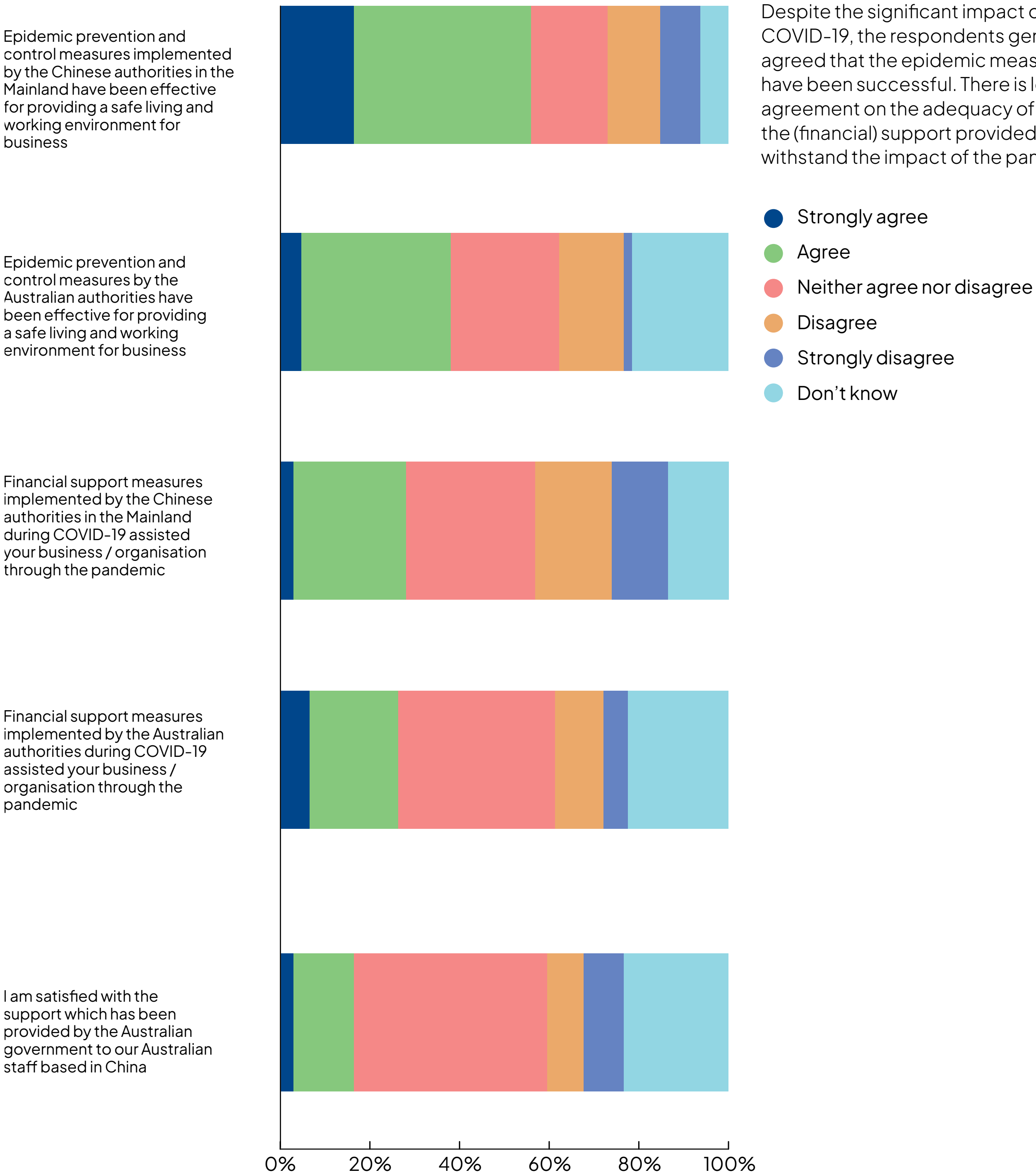
If China continues the current COVID-19 restrictions while the rest of the world is opening, how would this impact the following activities/outcomes in China?



If China continues its COVID-19 restrictions, the responding organisations indicate that their ability to attract foreign talent as well as their ability to grow their China businesses will be compromised. The tourism and education sectors will also be very negatively impacted from the current COVID-19 restrictions.

Figure 39

Do you agree or disagree with the following statements?



Despite the significant impact of COVID-19, the respondents generally agreed that the epidemic measures have been successful. There is less agreement on the adequacy of the (financial) support provided to withstand the impact of the pandemic.

Economic and policy outlook in China

The latest figures from the National Bureau of Statistics of China show economic growth in China for the first three quarters of 2022 at 3%. The OECD interim report forecasts growth for 2023 at 4.7%.

At the time of the survey, the Chinese growth rate for 2022 was forecast at 5.8%. While vulnerable to global uncertainties, China's economic outlook is still positive.

Our survey respondents state that the Chinese economy remains strong and presents opportunities for Australian companies. Based on their survey responses, the focus is shifting to expanding into new cities and regions within China, building upon the safe and high-quality perception of the "Australia brand".

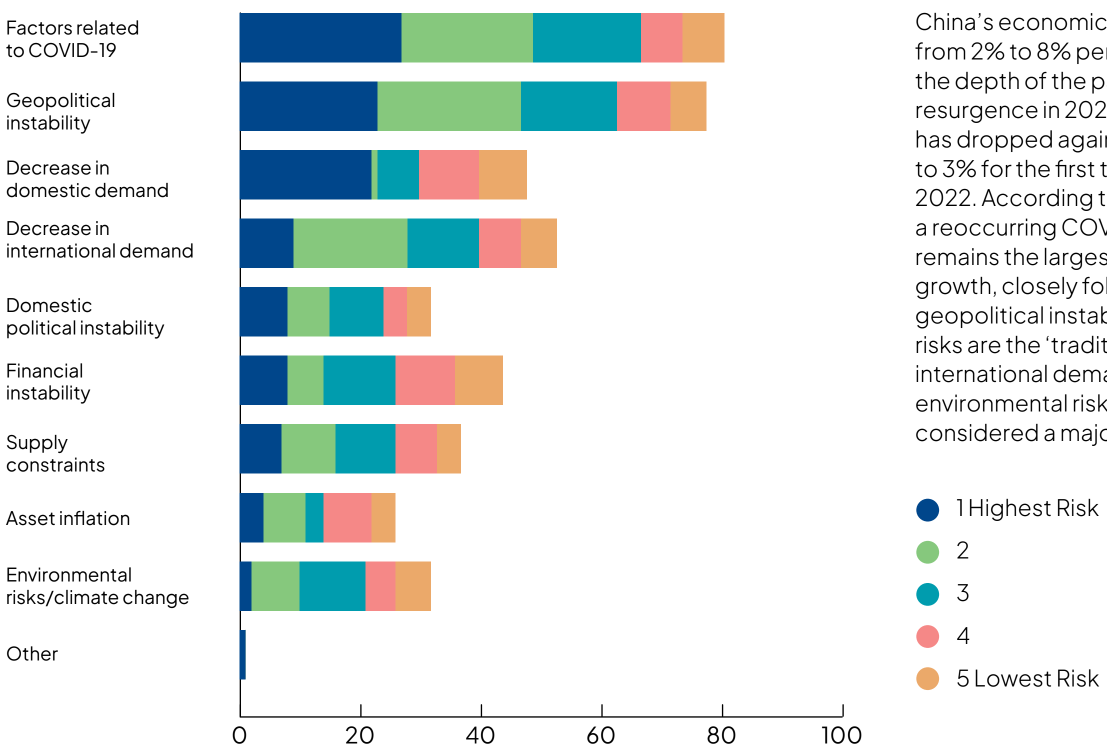
Surveyed Australian organisations perceive key risks to China growth as well as the opportunities to share in, and benefit from that economic development. For companies and organisations operating in China, policy uncertainty remains a major concern. Such challenges would be significantly alleviated if bilateral relations were stabilised, improving the outlook overall. Due to the deterioration in Australia/China government-to-government relations, businesses have opted for discrete engagement to maintain business-to-business links.

“The fundamentals of China’s economy are strong. The tech space may attract stable inbound investment.”

[anonymous respondent]

Figure 40

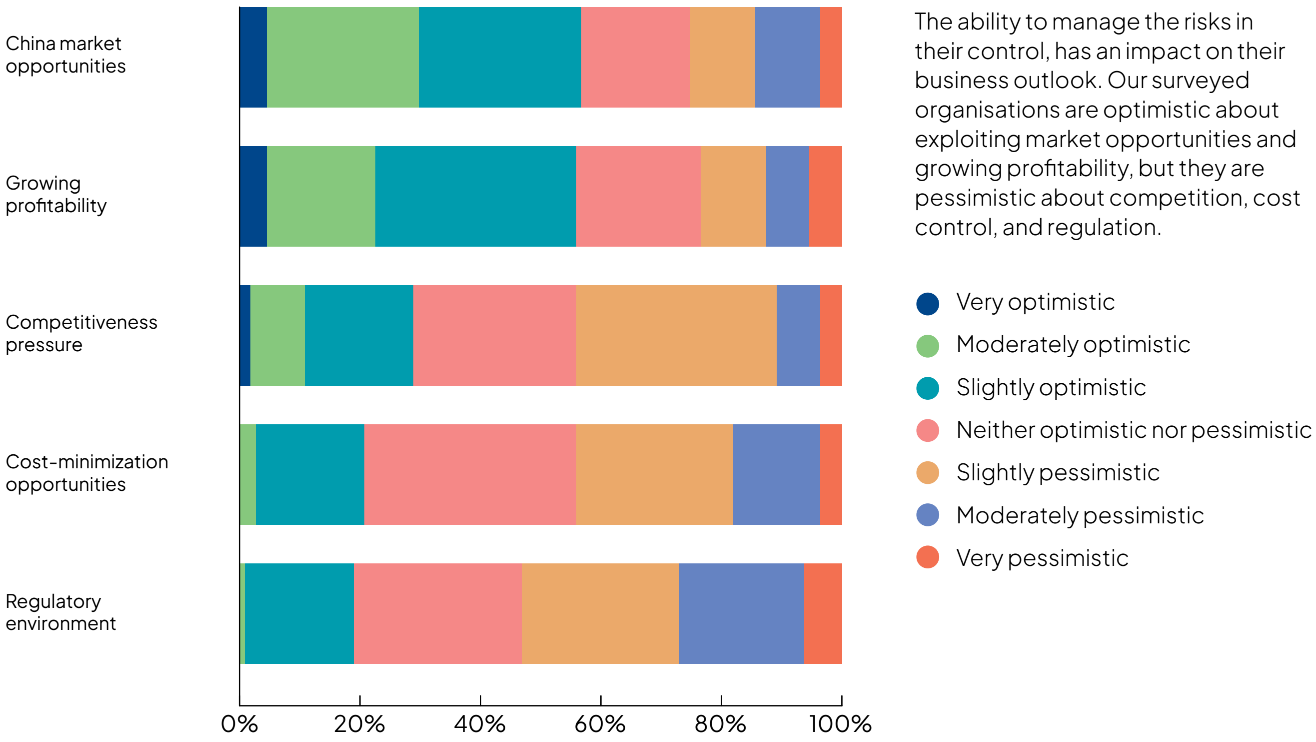
What do you view as potential risks to China’s economic growth? (1 = highest risk)



China’s economic growth has swung from 2% to 8% per annum, from the depth of the pandemic to the resurgence in 2021, although growth has dropped again subsequently to 3% for the first three quarters of 2022. According to the respondents, a reoccurring COVID-19 outbreak remains the largest threat to sustained growth, closely followed by unresolved geopolitical instability. Next highest risks are the ‘traditional’ domestic and international demand risk. Poignantly, environmental risk is (again) not considered a major risk.

Figure 41

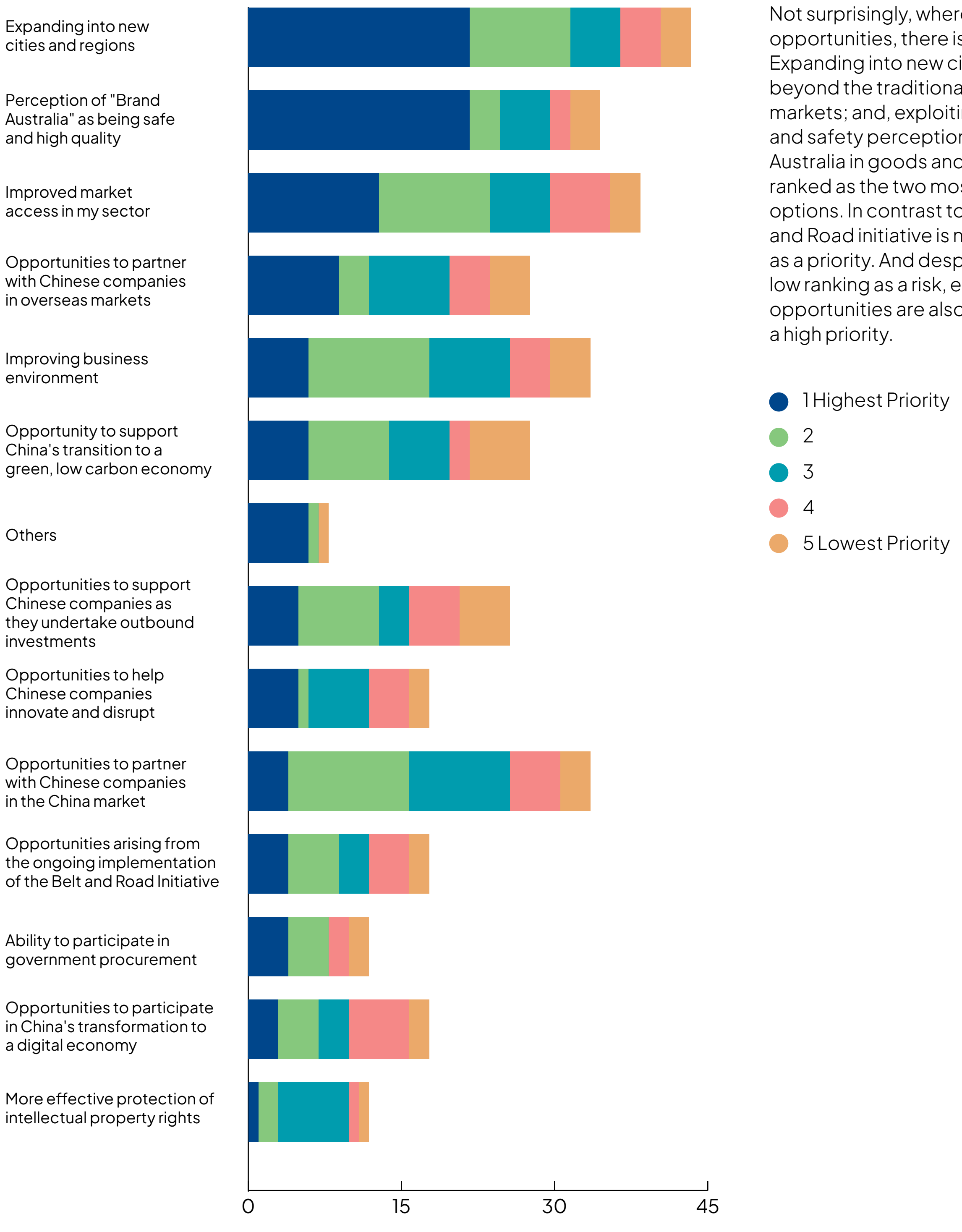
How would you describe your business outlook in China in each of the following aspects over the next two years?



The ability to manage the risks in their control, has an impact on their business outlook. Our surveyed organisations are optimistic about exploiting market opportunities and growing profitability, but they are pessimistic about competition, cost control, and regulation.

Figure 42

Which of the following are the key opportunities in China that your organisation is focusing on? (1 = highest priority)



Not surprisingly, where there are opportunities, there is optimism. Expanding into new cities/regions beyond the traditional Chinese markets; and, exploiting the quality and safety perception of brand Australia in goods and services, are ranked as the two most promising options. In contrast to 2018, the Belt and Road initiative is no longer seen as a priority. And despite its surprisingly low ranking as a risk, environmental opportunities are also identified as a high priority.

Bilateral relations and geopolitical risk

To many respondents, the last three years have demonstrated that fortunes of business are not just threatened by poor business decision-making, but are equally at the mercy of external risks. The 2018 survey identified a range of threats to Australian businesses arising from the then looming US-China trade war. Since then, Australia's bilateral political relations with China have worsened considerably.

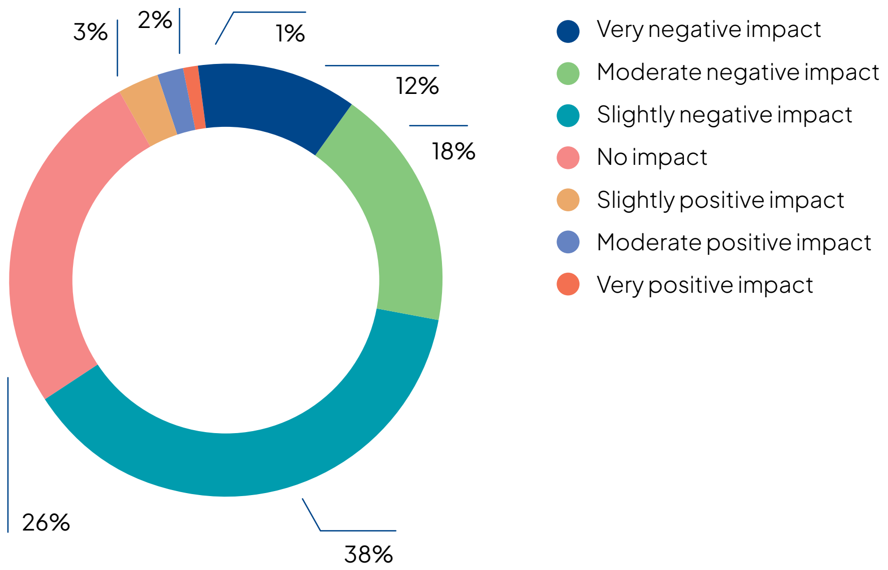
These political tensions have no doubt had an impact on businesses operating in the China-Australia market. But has this impact affected sentiment, business performance and business, all, or none?

Respondents reported that the effects of deteriorating bilateral relations have been either negative or neutral at best. Regardless, no significant action was taken by the responding organisations in response to the worsening conditions. This is not surprising, given that those organisations individually or collectively believed they were not equipped to divert the trajectory of political trends either in Australia or China. The most significant outcome of these challenging times was the shift by a large number of surveyed organisations towards accelerating localisation of their value chains in China and to expand sales into third countries other than Australia. As a result, the majority of respondents indicated that sales, costs, headcount and investment in China had not experienced significant detrimental impacts due to the hostile geopolitical climate. Nonetheless, 15 percent of organisations did report a marked decline in sales, and 10 percent reported an increase in costs.

Overall, the business-to-business situation remained resilient despite the political climate, except for sectors facing large tariff hikes such as wine and beef or those dependent on open borders, which included education and tourism.

Figure 43

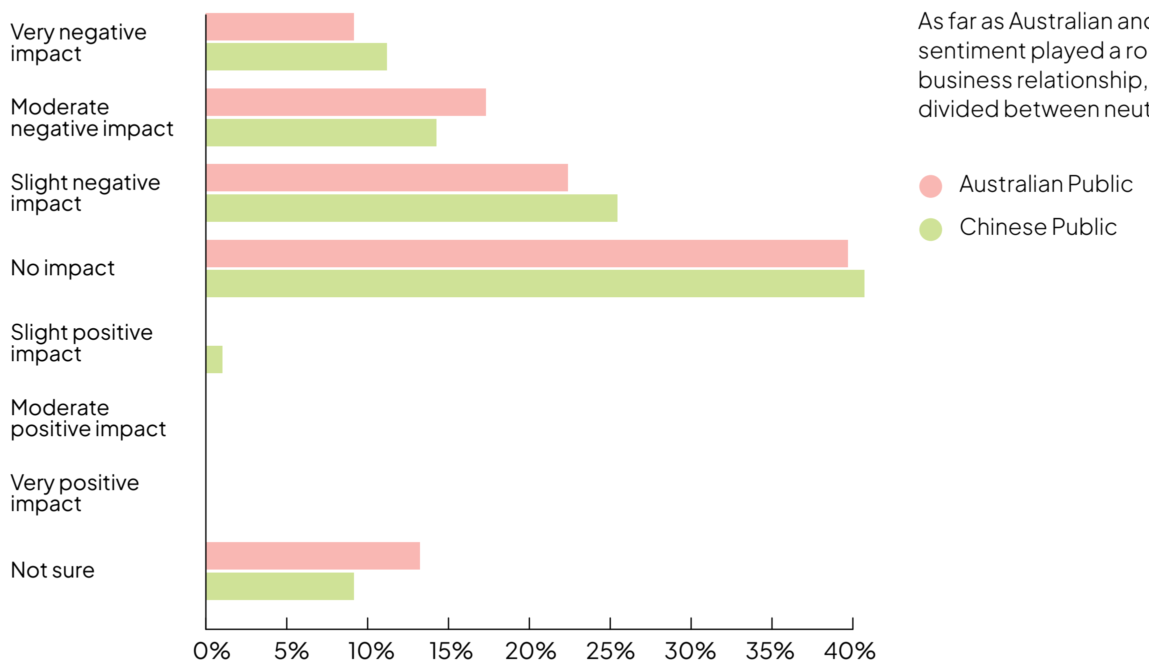
To what degree have the ongoing US/China trade tensions resulted in collateral effects on your organisation's China business?



The deterioration in the Australia/China relationship was preceded by the US/China trade tensions in 2018. When asked how the US trade war with China spilled over into their China business, 68% of our respondents noted a negative impact. Only 6% noted a positive impact. As a major trading partner of China, Australia did not benefit from the US/China trade disruption.

Figure 44

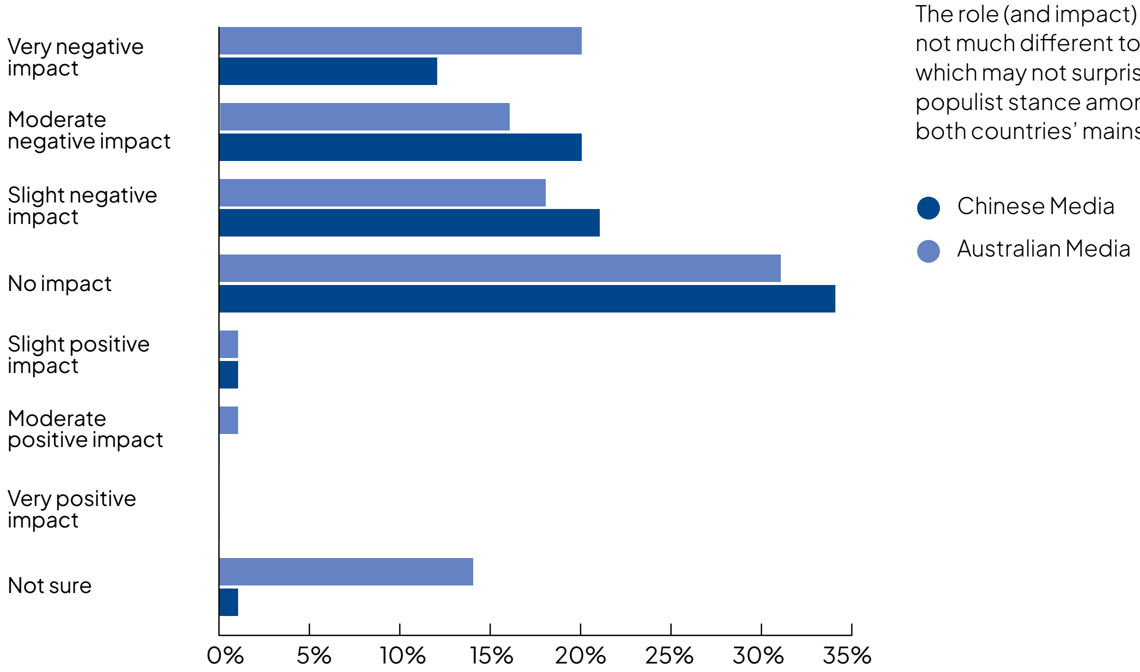
To what extent have shifts in Australian and Chinese public sentiment impacted your organisation's China business?



As far as Australian and Chinese public sentiment played a role in altering the business relationship, the impact is divided between neutral and negative.

Figure 45

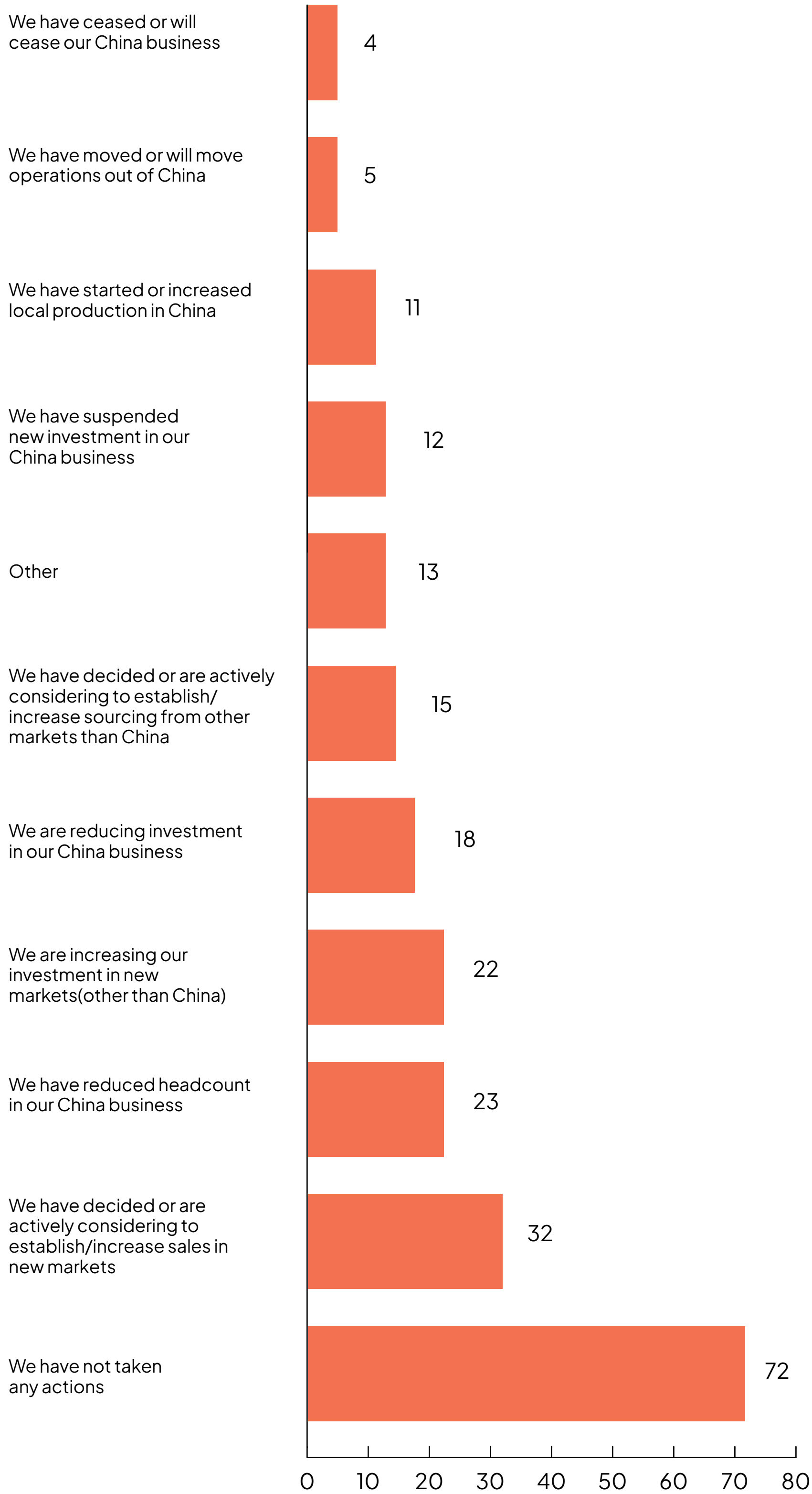
Describe the impact of Australian and Chinese media reporting on the bilateral relationship on your organisation's China business during the past 24 months?



The role (and impact) of the media is not much different to public sentiment, which may not surprise given the populist stance among elements of both countries' mainstream media.

Figure 46

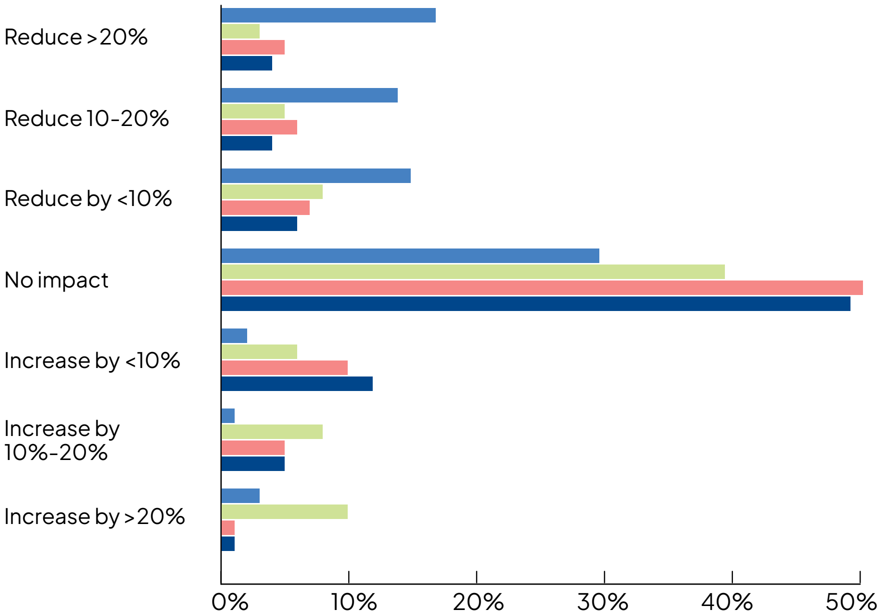
What actions has your organisation taken or decided to take as a result of the impacts?



While the impacts seem severe and comprehensive, it is surprising to note that 45% of the respondents decided not to take action. They might have been unable to change course, they might anticipate a turnaround in the relationship, or the cost of action was simply too high. Of those that did take action, China evasion (considering new markets) or China contraction (reducing headcount) were the preferred course of action.

Figure 47

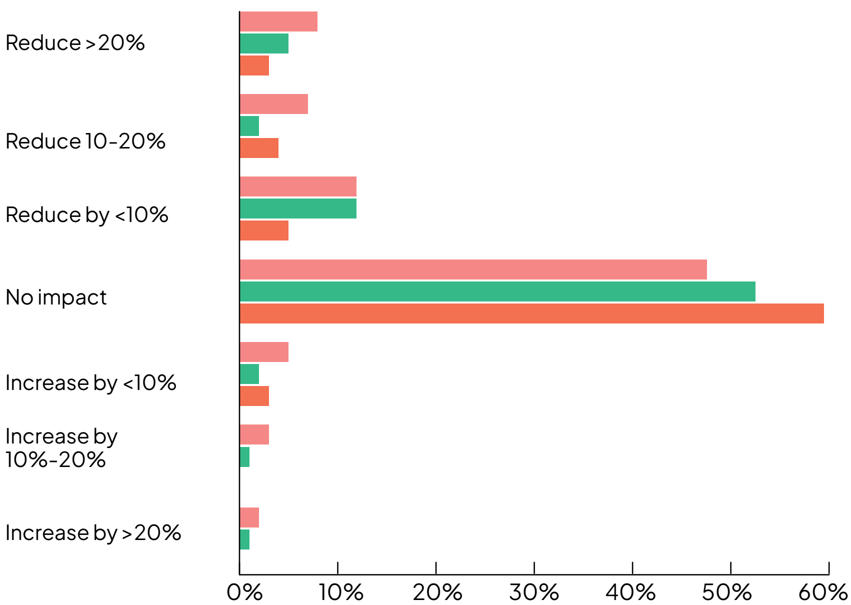
What has been the impact of the deterioration in Australia-China relations on sales and costs in your organisation since 2019?



Consistent with the prevailing absence of action is the response of no impact on sales and costs. Between 30–50% did not experience a change in (cost of) sales, payroll, or other costs. 15% of organisations did experience a marked decline in sales while 10% experienced an increase in cost (of sales). Payroll costs impact has been moderated by a decrease in headcount.

Figure 48

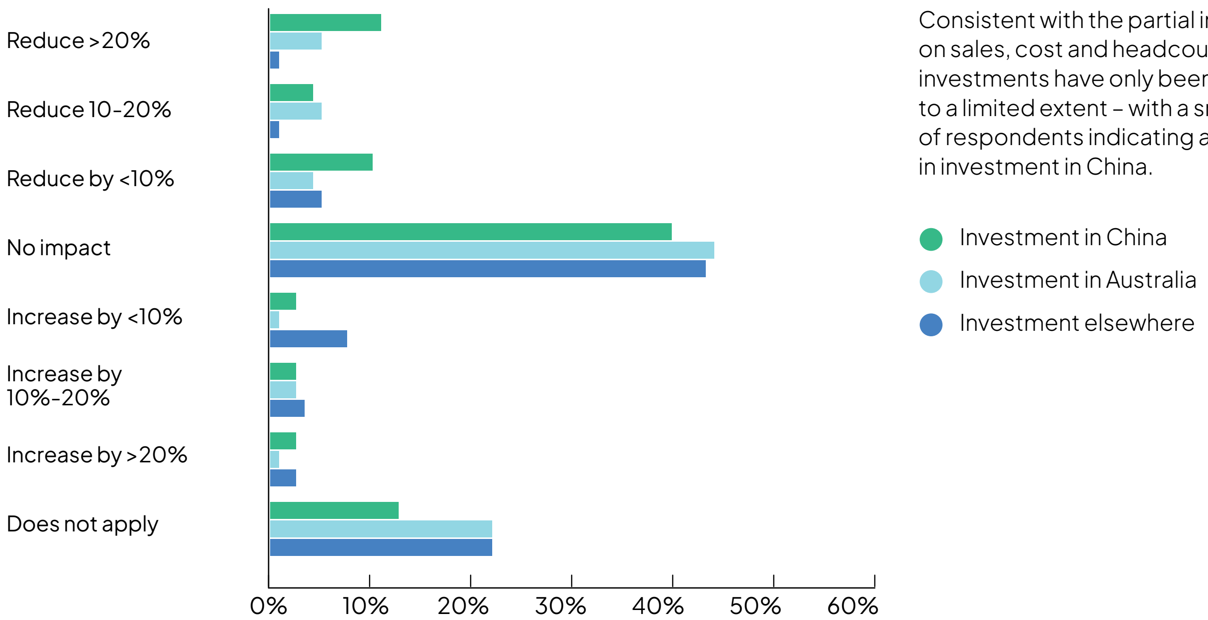
What has been the impact of the deterioration in Australia-China relations on the jobs (headcount) in your organisation since 2019



Similar to the impact on sales/costs, 50% of the respondents note no impact on headcount since 2019. Of those that were impacted, 5–10% indicated a reduction in China headcount, while 2–5% indicated an increase in China headcount.

Figure 49

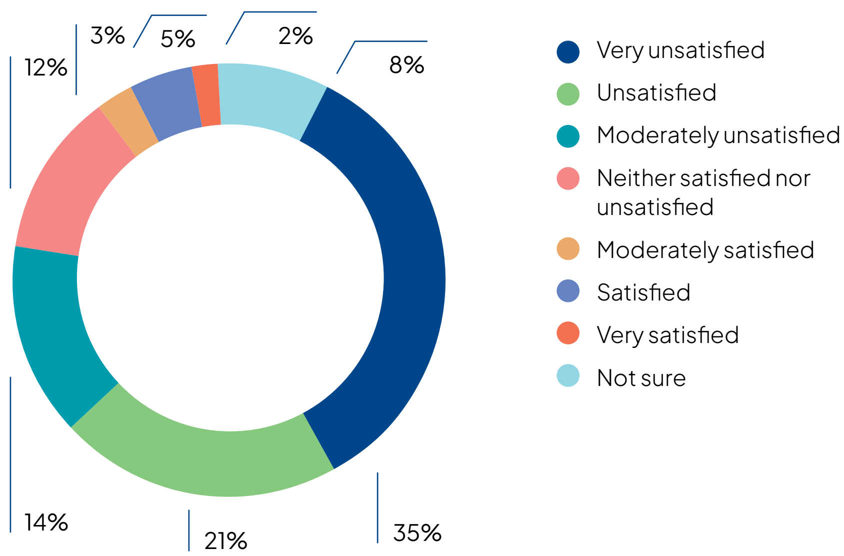
What has been the impact of the deterioration in Australia- China relations on investments in your organisation since 2019?



Consistent with the partial impact on sales, cost and headcount, investments have only been affected to a limited extent – with a small group of respondents indicating a reduction in investment in China.

Figure 50

Describe your level of satisfaction with the Australian government's management of the bilateral relationship over the past 24 months?[4]



Given the negative impact on business of a worsening bilateral geopolitical relation, 70% of the surveyed business leaders are not satisfied with the handling of the relationship.

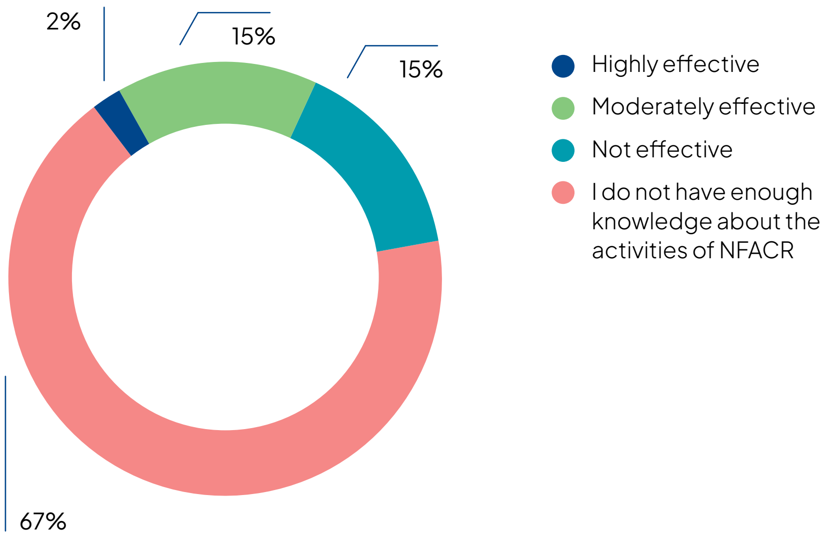
4. Responses to this question were provided by respondents in the second quarter of 2022 and accordingly the responses are in respect to the Liberal/National Coalition Government prior to the Federal election in May 2022.

> “Keep in mind for most things, we need China much more than China needs Australia.”

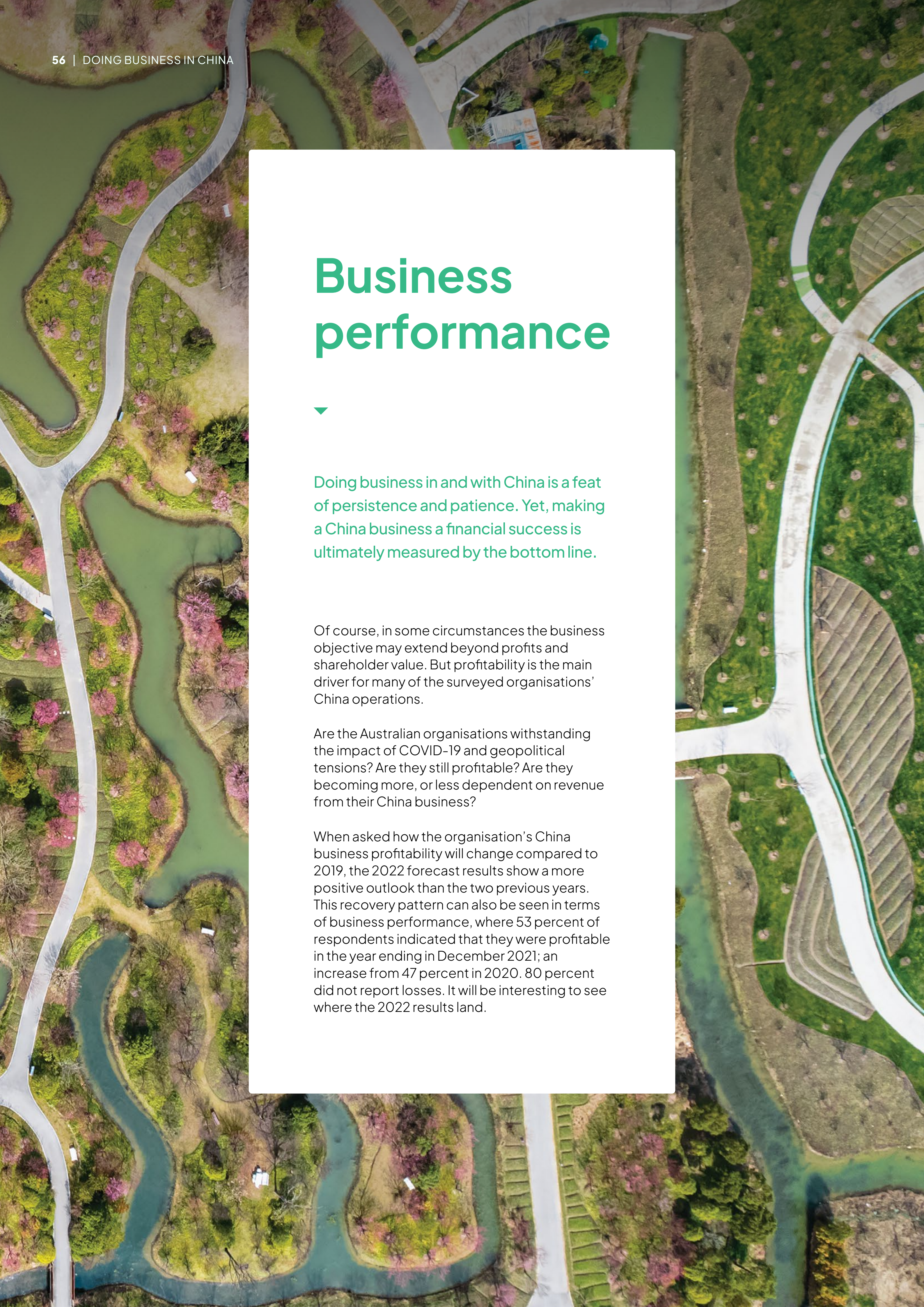
[anonymous respondent]

Figure 51

How effective has the National Foundation for Australia-China Relations (NFACR) been in achieving its objective of "*creating a national platform that engages government, business and communities to support and find ways to engage constructively with China*"?



As a related entity of the Australian government (and its Department of Foreign Affairs and Trade), the National Foundation for Australia-China Relations (NFACR) was established in 2020 to constructively assist Australian organisations engaged in business with China. The surveyed organisations' responses suggested that, as at early 2022, there was still some work to be done to enhance knowledge about the NFACR's activities.



Business performance

Doing business in and with China is a feat of persistence and patience. Yet, making a China business a financial success is ultimately measured by the bottom line.

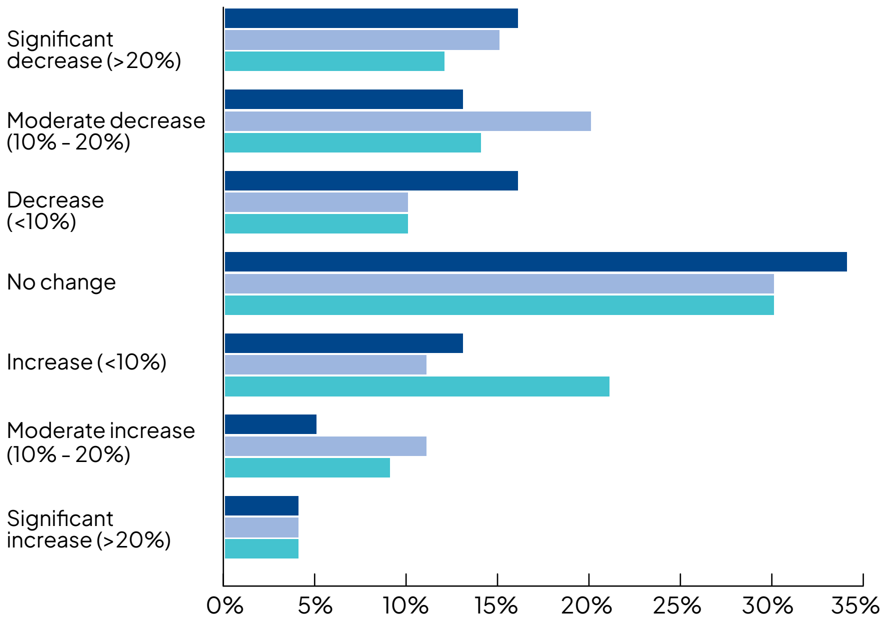
Of course, in some circumstances the business objective may extend beyond profits and shareholder value. But profitability is the main driver for many of the surveyed organisations' China operations.

Are the Australian organisations withstanding the impact of COVID-19 and geopolitical tensions? Are they still profitable? Are they becoming more, or less dependent on revenue from their China business?

When asked how the organisation's China business profitability will change compared to 2019, the 2022 forecast results show a more positive outlook than the two previous years. This recovery pattern can also be seen in terms of business performance, where 53 percent of respondents indicated that they were profitable in the year ending in December 2021; an increase from 47 percent in 2020. 80 percent did not report losses. It will be interesting to see where the 2022 results land.

Figure 52

How did/will the profitability of your organisation's China business change in the following years relative to 2019?

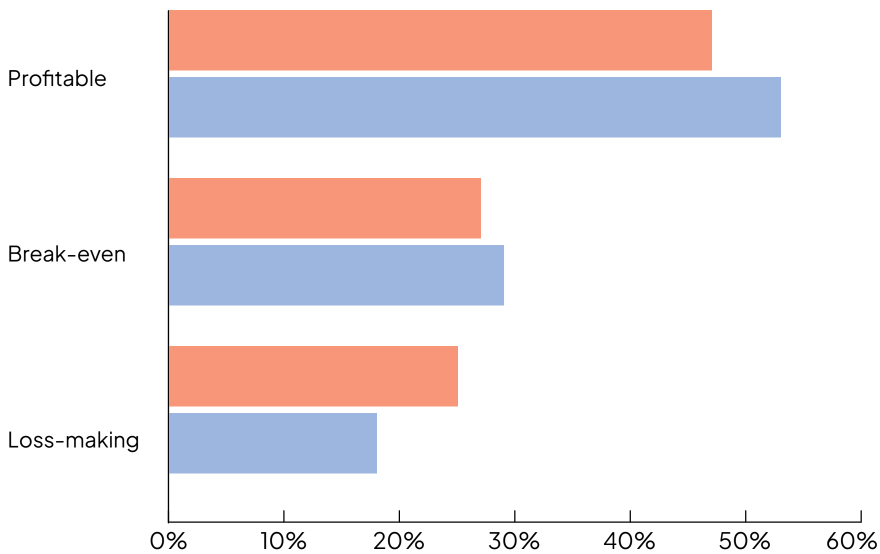


The surveyed organisations continue to deal with the financial impact of the COVID-19 impact. Compared to pre-COVID, the 2020, 2021 and forecast 2022 profitability has decreased on average in each of those years – with a slightly more positive outlook for 2022.

- In the Year Ended 31 Dec. 2020
- In the Year Ended 31 Dec. 2021
- In the Year Ending 31 Dec. 2022 (based on forecast)

Figure 53

What was the financial performance of your organisation's China business in the following years?



25% (18%) of organisations made a loss in 2020 (2021). It is, of course, noteworthy that 47% (53%) of organisations was in fact profitable in 2020 (2021), despite difficult circumstances and their impact on the bottomline.

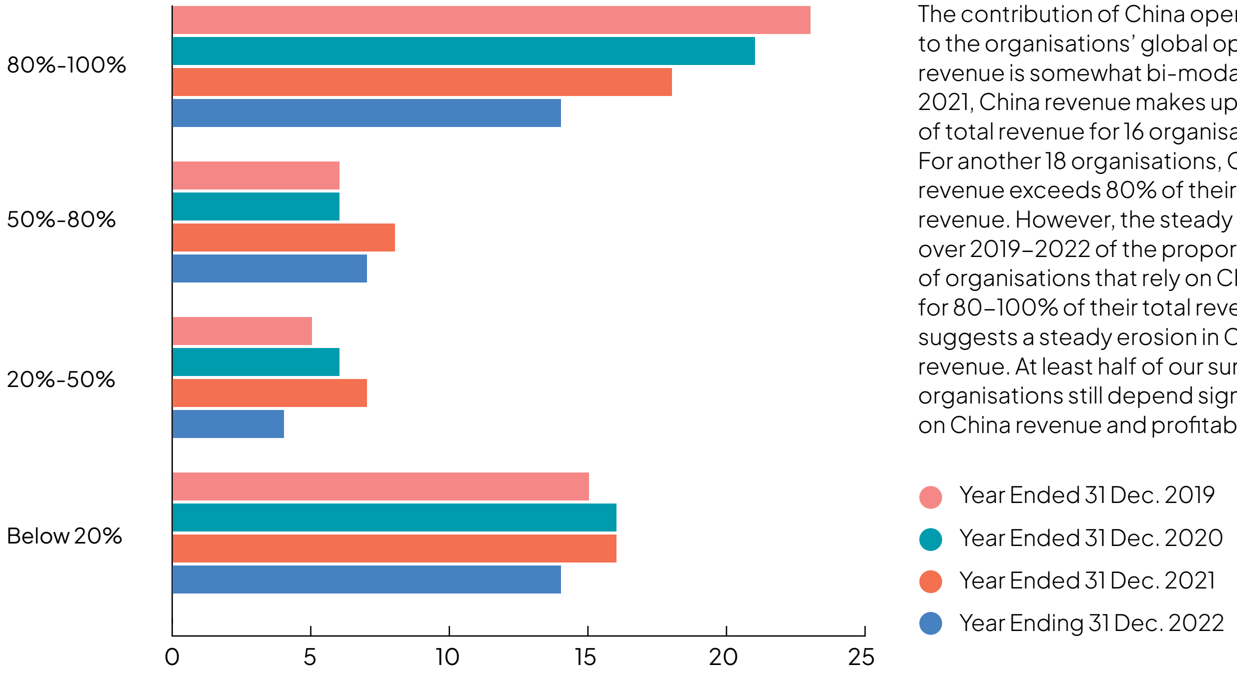
- In the Year Ended 31 Dec. 2020
- In the Year Ended 31 Dec. 2021

"At least half of our surveyed organisations still depend significantly on China revenue and profitability"

[anonymous respondent]

Figure 54

How much did/will the revenue from your organisation's China business represent as a percentage of your organisation's total worldwide revenue in each of the following financial years?



The contribution of China operations to the organisations' global operations revenue is somewhat bi-modal. In 2021, China revenue makes up to 20% of total revenue for 16 organisations. For another 18 organisations, China revenue exceeds 80% of their total revenue. However, the steady decline over 2019–2022 of the proportion of organisations that rely on China for 80–100% of their total revenue suggests a steady erosion in China revenue. At least half of our surveyed organisations still depend significantly on China revenue and profitability.

Impact of treaties and international agreements

What a difference a pandemic makes to free trade. With closed borders, global trade in goods and services became victims, prompted by the astonishing spread of COVID-19.

Of course, the US/China trade disputes had already done much damage, with the US rejecting the Trans-Pacific Partnership and imposing tariffs on imports from China. Add to that the damage caused by Brexit to free trade agreements.

The 2018 and 2017 DBIC surveys focused on the benefits from the China/Australia Free Trade Agreement (ChAFTA) and anticipated further progress in bilateral free trade negotiations between Australia and China. ChAFTA came into effect in December 2015, and the first two surveys revealed a positive impact on business in or with China while expressing hopes for further trade liberalisation.

Respondents in 2022 were asked whether they were still optimistic about the impact of three free trade deals: ChAFTA, the Regional Comprehensive Economic Partnership (RCEP) and the Comprehensive and Progressive Agreement for the Trans-Pacific Partnership (CPTPP). The 2022 survey indicates that ChAFTA now has significantly less relevance for many Australian businesses. The RCEP and CPTPP are recent agreements and only a minority of organisations have decided whether they will be beneficial or not. The majority of respondents have yet to make up their mind.

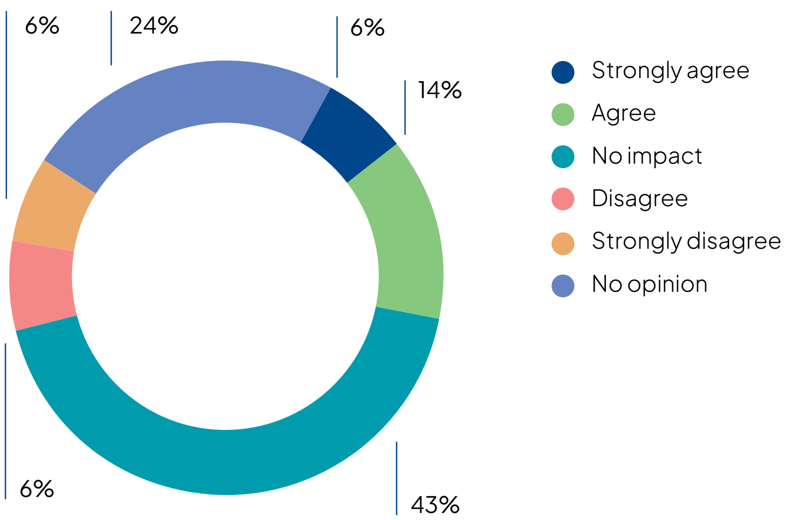
With the change in Australia's government, stabilisation of the Australia-China relationship would provide greater opportunities for revitalised trade with China. The next instalment of this survey will reveal whether that opportunity has been taken up.

"New tariffs and non-tariff barriers have offset any benefits of ChAFTA."

[anonymous respondent]

Figure 55

Over the past 24 months, the China Australia Free Trade Agreement (ChAFTA) has been beneficial to my organisation's China business



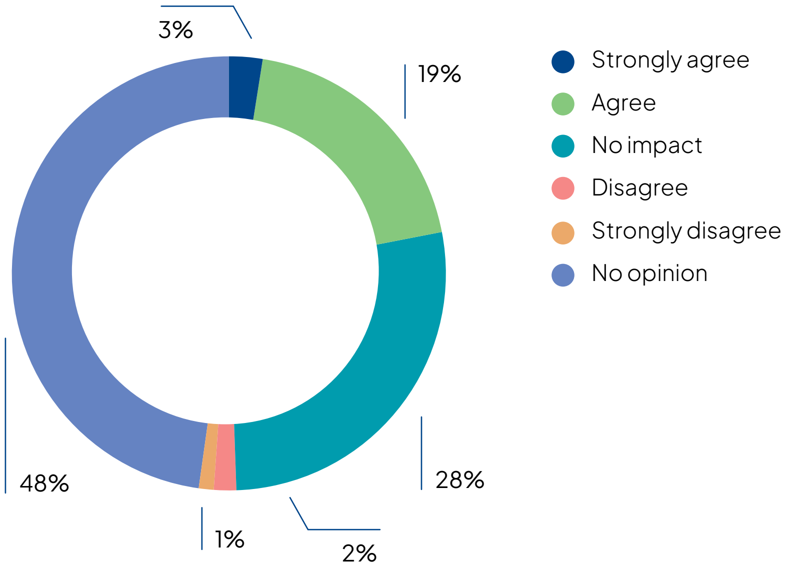
The worsening bilateral relationship with China has undone the optimism expressed in the 2018 survey towards the benefits of ChAFTA. The earlier surveys revealed over 50% of respondents claiming a positive impact. Now, after 7 years of operation, ChAFTA has lost some of its lustre. Only 20% can still see the benefits, with the balance either seeing no impact or not expressing an opinion

> “Any agreement to work cooperatively must be a plus.”

[anonymous respondent]

Figure 56

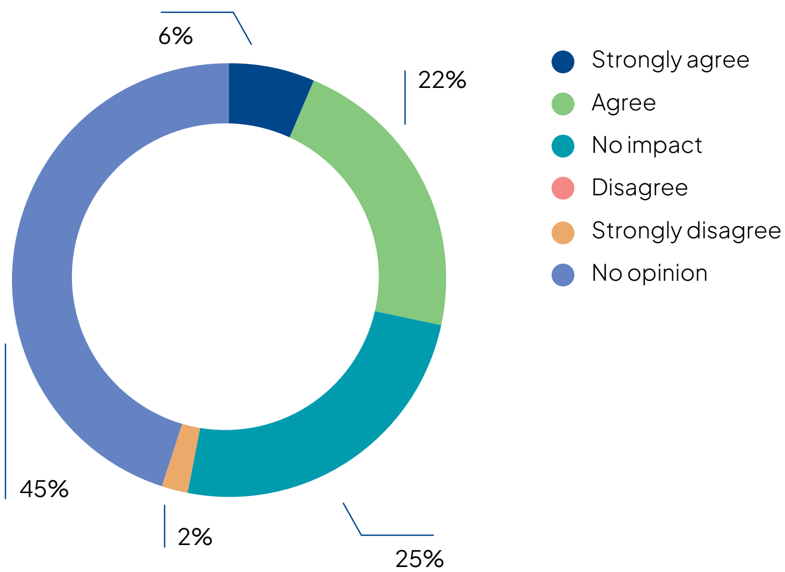
The Regional Comprehensive Economic Partnership (RCEP) will be beneficial to my organisation's China business



Negotiated in November 2020, the Regional Comprehensive Economic Partnership (RCEP) is a multilateral free trade agreement between 15 Asia-Pacific nations, including Australia and China. RCEP came into effect from January 2022. A similar picture arises, with 22% anticipating benefits, but 76% expecting no impact of having no opinion.

Figure 57

China joining the Comprehensive and Progressive Agreement for the Trans-Pacific Partnership (CPTPP) would be beneficial to my organisation's China business



The Comprehensive and Progressive Agreement for the Trans-Pacific Partnership (CPTPP) is the reincarnation of the Trans-Pacific Partnership (TPP), after the US unilaterally abandoned the TPP. The CPTPP is a multilateral free trade agreement between 11 Trans-Pacific nations, which entered into force on 30 December 2018 for Australia. As China is not a signatory to the CPTPP, any assessment of its benefits – and more specifically the admission of China – is purely speculative. Again, 70% of respondents expects no impact or has no opinion, although 28% expresses the sentiment that it can only get better.

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