CANADA-AUSTRALIA COMMERCE: ENHANCING THE RELATIONSHIP

A REPORT FOR THE CANADIAN COUNCIL OF CHIEF EXECUTIVES

This study explores the potential to expand commercial relations between Canada and Australia in terms of trade, investment and other areas of economic partnership. Due to policy advances in other relationships, Canada and Australia no longer offer each other the best terms on offer to other partners; providing each other genuine most favoured nation status in a number of areas would provide a significant boost to bilateral commerce. A bolder vision is also possible. Australia and Canada can leverage the similarities in their economies, their societies and their governance system, as well as the high degree of confidence earned by years of close and sustained inter-agency cooperation, to create a virtually seamless economic space for the movement of goods, services, capital and labour bilaterally in the context of a broader trans-Pacific trade agreement.

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Canada-Australia Commerce: Enhancing the Relationship

EXECUTIVE SUMMARY

Canada and Australia are highly similar economies in terms of size, wealth, governance systems, most observable socio-economic characteristics, resource endowments and specialization in international trade. To the extent that countries trade because they are different, this works as a disincentive to deepening trade relations. Yet there are important sources of gains that flow from these very attributes: the similarities of consumer preferences come with complementarities in opposite seasonality, the similarity of export engagement comes with complementarity in time zones, the similar output structures come with similar needs for specialized inputs and producer services, and the overall degree of socio-economic similarity lowers the risks associated with bilateral liberalization.

The commercial relationship is stronger than often thought

Cross-border merchandise trade is well balanced at about US$ 1.8 billion in each direction in 2011 (measured using each country's import data), but represents for each country only a modest share of its global trade.

Services trade is more important in this bilateral relationship than it is in either country's global trade. While the scale is modest—Canada's 2010 exports to Australia were about $US 800 million, while Australia's exports to Canada were about $US 527 million—the services share of bilateral goods and services trade is close to double that in Canada's and Australia's global goods and services trade.

Investment is by far the most important feature of bilateral commerce. Both Canada and Australia have global direct investment (FDI) stocks that are larger than annual global exports of goods and services. For Canada, in 2010, the stock of investment was 1.55 times the size of global exports of goods and services; for Australia, the comparable ratio was 1.31. However, in the bilateral relationship, these ratios are about an order of magnitude larger: for Canada the ratio of direct investment in Australia to its exports of goods and services to Australia in 2010 was 8.7; for Australia the comparable figure was 13.1.

While foreign affiliate sales data are not available on a bilateral basis, applying the global average of a $1.67 in foreign affiliate sales for $1.00 in FDI, foreign affiliate sales in 2010 may be estimated at US$ 36 billion for Australian firms in Canada and US$ 25 billion for Canadian firms in Australia. Seen this way, the relationship suddenly looks neither small—US$ 65 billion in two-way trade plus foreign affiliate sales—nor lagging in growth.

The number of Canadian firms exporting to Australia, as recorded in Canada's Exporter Registry, grew from 2,161 in 2003 to 2,977 in 2008, before falling off to 2,780 as the global economic crisis unfolded in 2009. The number of Australian firms exporting to Canada was reported by Austrade to have been about 2,000 in 2008, or about 2/3 as large a number. The investment figures suggest that many firms have also established a commercial presence. Accordingly, there is an expanding base of business with an interest in the policy environment. The establishment of the business Leadership Forum in 2010 is no surprise in light of these findings; governments need to take note.

At the policy level, this bilateral relationship has not received as much attention in recent years as have others. Given their expanding web of free trade agreements, Australia and Canada now provide each other less than "most favoured nation" treatment in many areas. There is some evidence that this matters: for example, the introduction and survival rates of Canadian products in the Australian market following the AUSFTA fell off sharply.

Examining the range of bilateral instruments affecting the commercial relationship, the present study suggests that there is considerable potential for policy to further boost the strength of this relationship.

Trade in goods

Both countries have several thousand tariff lines in place against each other of 5% or higher. Tariff elimination alone could boost bilateral goods trade by about US$520 million, or by about one-sixth. Given the modern "made in the world" paradigm for goods production, restrictive rules of origin for tariff preferences would largely defeat the purpose of tariff elimination, especially for relatively low tariffs. Accordingly, for the above-mentioned potential gains in trade from tariff elimination to be actually realized, an accommodating approach to rules of origin would be required. Some additional boost to trade would be provided even for goods that are presently not subject to tariffs from the various facilitative measures that typically accompany tariff elimination.

The assessments of market potential by the official trade promotion agencies also suggest there is room for further development of trade in various sectors of particular interest, including (in terms of Canada's export interests) agricultural products; food and beverages; fish and seafood products; agricultural technology and equipment; forest products; metals, minerals and related equipment, and consumer products (including apparel and fashion); and (in terms of Australia's export interests), environmental goods, mining and oil & gas technology, and wine.

In the non-agricultural sector, non-tariff barriers appear to be low. Both Australia and Canada are active in aligning standards internationally and have MRAs in some conformity assessment areas. Since both countries appear to be at the leading edge of efforts to reduce barriers in this area, significant scope for further enhancement of the commercial relationship on a bilateral basis does not likely exist.

In the agricultural sector, however, Canada's supply-management system, particularly in the dairy sector, and Australia's quarantine regime, which it maintains to protect its unique ecology from risk of entry of non-indigenous pests and plant and animal diseases, pose very high barriers. Australia's export interests in dairy could be accommodated by Canada without disrupting its overall supply management system by extending an increased quota to Australia. Given the opposite seasonality, the quota arrangement could be structured on a seasonal basis so as to reduce inventory costs in Canada. Whether it is possible for Australia to accommodate Canada's export interests in areas such as beef, pork and salmon, where would-be Canadian exporters have been thwarted in the past, is difficult to assess. Australia has brought its risk assessment for agricultural commodity imports into apparent conformity with SPS rules; since these rules allow Australia to set very high standards, it would be inconsistent for Australia to relax these on a bilateral basis. That being said, inter-governmental cooperation appears to have led to the identification of less trade-restrictive ways to handle Australia's legitimate biosecurity concerns in a number of areas. A similar process adopted in the Australia-Canada relationship could also potentially facilitate market entry for Canadian agricultural products into Australia's market while meeting Australian prudential concerns.

Services trade

Applying commonly used techniques, the analysis suggests that bilateral trade could be increased by US$343 million or by over 50%. Given the difficulty of tying trade impacts to specific regulatory measures, this result is subject to greater uncertainty than the estimates for goods trade and must be treated with appropriate caution.

One specific area where cross-border services trade can be improved is through a modernized air services agreement that provides the best possible travel opportunities for business, tourism and personal reasons. An agreement with a high level of ambition in terms of the "freedoms" of competition covered would also have the potential to increase competition and efficiency in both the Australian and Canadian air services markets.

Moreover, some degree of services trade expansion may be expected from service trade related to expanded goods trade, progress on mutual recognition of qualifications, and improved access to government services procurement opportunities.

Investment

Generally there are minimal hurdles for Australian and Canadian companies seeking to invest in each other's economies and thus limited scope to enhance the relationship in this area.

One notable imbalance concerns the threshold for review of inward investment. Australia applies a higher threshold for New Zealand and US investors than for Canadian investors. When Canada implements its commitment to raise the threshold for review of inward investment, Canada will be applying a threshold to Australian investors comparable to that which Australia applies to New Zealand and US investors. Accordingly, a bilateral investment agreement that achieves MFN treatment for Canadian investors in the Australian market has some potential to facilitate bilateral investment.

Further, modernization of the bilateral tax treaty to bring it fully up-to-date and, to the extent appropriate, aligned with the updated model OECD code, was identified as a useful facilitating measure.

Labour Mobility

Given the importance of investment to bilateral Australia-Canada commerce, facilitating the movement of personnel between corporate offices is clearly an important way to reduce deadweight procedural costs. Both Australia and Canada have uncapped employer-sponsored temporary foreign worker programs, primarily to meet general domestic labour market needs. While only a small percentage of temporary foreign workers are transferees within multinational firms, the close connection between temporary movement of personnel and immigration attracts the panoply of regulation associated with permanent migration.

Canada's terms for intra-company transfers are less onerous than its general rules: no labour market opinion is required and the length of stay is also longer—5 years for technical ("specialized knowledge") staff and 7 years for senior executives or managerial staff, although the initial work permit is issued for only 1 year and renewal of a permit requires a stay outside of Canada. Australia also waives a labour market test but the permitted length of stay is 4 years, the same as for temporary workers brought in for domestic labour market requirements. Reciprocation by Australia of Canada's terms would represent a benefit for Canadian firms operating in Australia at no risk to Australia.

Mutual recognition of qualifications between professions in Canada and Australia is an area which business has identified as important in facilitating bilateral commerce. In this regard, a recent assessment by stakeholders from Australia and Canada noted a "skewed reciprocity", with Australia facilitating immediate access to practice for Canadian-qualified professionals in a number of fields, while Canada has been less forthcoming. A review of the system for rrecognition by Canadian jurisdictions of qualifications acquired in Australia thus appears to be a way to further improve the bilateral relationship.

In a similar vein, Canada fully acceding to the APEC Business Travel Card program, in which Australia already is a full participant, would facilitate business development travel for both Canadian and Australian business travelers.

Finally, the conditions imposed on youth travelers vary considerably in stringency. Matching the best terms provided by either would be a way to provide a gentle long-term boost to Canada-Australia relations.

Government Procurement

In the revised WTO Government Procurement Agreement, Canada extends to other GPA members the same commitments it has made in respect of provincial and territorial commitments under the Canada-United States Government Procurement Agreement as well as under the NAFTA procurement measures in respect of federal crown corporations. Since Australia is not a party to the GPA, it gets less than MFN treatment.

Australia's rules generally prohibit discrimination against potential suppliers due to their degree of foreign affiliation or ownership, location or size; however, the specific measures to ensure non-discrimination against SMEs are limited to Australian and New Zealand firms. Accordingly, in this respect Australia provides less than MFN treatment to Canada.

Government procurement has been identified as a priority sector in Australia-Canada trade; there is a basis for improvement of the bilateral commercial relationship by full MFN extension of government procurement policies on a bilateral basis.

Competition Policy/Trade Remedies

The relationship between the Australian and Canadian competition authorities is very well developed. Indeed, the strength of this relationship makes it feasible to contemplate another step in the direction of creating a seamless operating environment, namely replacing antidumping with competition policy measures in the bilateral relationship. Antidumping investigations in respect of Australia-Canada bilateral trade are rare (only eight investigations were initiated over the last two decades, seven by Australia and one by Canada, resulting in duties being applied in four cases, only one of which is still in effect). Accordingly, the main impact of such a step would be to reduce uncertainty about market access.

Small and medium-sized enterprises

Finally, given the expansion in the number of firms engaged in cross-border trade in the Australia-Canada bilateral relationship, it can be straightforwardly concluded that the vast majority of new entrants are small or medium-sized enterprises. The facilitation of bilateral market access thus represents a very significant boost to potential growth for individual small and medium-sized exporters, particularly those serving niche markets where the similarity of tastes between Australia and Canada will work in their favour. Accordingly, concerted efforts by governments to remove barriers to bilateral commerce in this relationship should be seen as benefitting primarily small and medium-sized enterprises.

Summary

Working within the established institutional framework for the bilateral relationship, a number of areas can be identified where policy adjustments could enhance the relationship:

1. Eliminate tariffs on bilateral trade, accommodating Australia's dairy interests through an expanded quota, and applying non-restrictive rules of origin. This would boost two-way trade in goods by about one-sixth and would likely leverage associated gains in services sectors even without explicit measures in the latter sector.
2. Update the bilateral air services agreement with a high level of ambition in terms of the "freedoms" of competition covered.
3. Enter into a bilateral investment agreement that achieves MFN treatment for Canadian and Australian investors in terms of the level of investment subject to policy review.

4. Conclude the negotiations to modernize the bilateral tax treaty to bring it fully up-to-date and, to the extent appropriate, aligned with the updated model OECD code.
5. Enter into a labour mobility agreement that offers each other the best terms currently on offer by either on a bilateral basis for intra-company transfers and youth working holiday programs.
6. Enter into a government procurement agreement that provides each party MFN treatment.
7. Enter into a competition policy agreement that suspends the operation of antidumping law in the bilateral relationship.

In addition, Canada could potentially boost the relationship with unilateral action in a couple of areas:

8. Review the process for recognition of qualifications acquired in Australia by Canadian jurisdictions to remedy the apparent "skewed" nature of reciprocity in this area.
9. Expedite its full participation in the APEC Business Travel Card program.

A Bolder Vision

The above-listed measures would provide a tangible, albeit modest, boost to the bilateral relationship. It is however possible to think more ambitiously about this relationship.

Canada and Australia represent a special case. The similarity in size and wealth of the economies, as well as in socio-economic characteristics and governance systems, can serve as a natural replacement for many of the controls that nations put in place at their borders to prevent exploitation of large *differences* in these regards—of different levels of wages, of social security benefits, and of regulatory safeguards. Meanwhile, distance serves to minimize incentives to exploit marginal differences in these regards. The many similarities between Canada and Australia, both in current circumstances and in historical evolution, have made them a staple for comparative studies; thus, there is both depth and breadth of mutual understanding of each other's economy and society. Finally, inter-governmental cooperation is well with developed with inter-agency contact being routine; in consular affairs, both countries already extend services to each other's citizens in many third countries.

The basic framework for deepening economic relations involves putting in place the "four freedoms" of free circulation of goods, services, capital and labour. The relevant thought experiment is thus as follows: are there low-cost, informal measures that Canada and Australia could contemplate that would move the relationship in this direction, extracting the major part of the benefits, without incurring the governance costs associated with establishing formal frameworks?

- For goods trade, this might be accomplished through the following:
  - Tariff elimination.
  - A very relaxed approach to rules of origin, e.g., allowing goods to qualify for mutual preferential access simply on the basis that they can legitimately claim, under the respective domestic laws, to be "Made in Australia" or "Made in Canada".
  - A negative list approach to standards, under which areas where standards involve genuine differences (e.g., quarantine products) remain subject to controls but it is left to the market to determine which products put on the market in one country can find markets in the other.
  - Customs cooperation between Canada and Australia to put in a place a low-cost, risk-based approach to the Authorized Economic Operator system that is being implemented in the context of the World Customs Organization.
  - Suspension of antidumping in bilateral trade.

- For services trade, the most important element for freedom of movement of services—the right of establishment—is already effectively in place. Cross-border business services that can be provided on a contract basis over the Internet were never subject to regulation and hence are also effectively open. Effectively free circulation could be approached by implementing the measures discussed above, namely:
  - Effective reciprocity by Canada to Australia's ready acceptance of Canadian qualifications.
  - National treatment in government procurement for services.
  - A blue skies agreement with the maximum "freedoms".
- For investment, free circulation is effectively in place for most intents and purposes. A bilateral investment agreement that achieves MFN treatment for Canadian and Australian investors in terms of the level of investment subject to policy review, as recommended above, would round out the package.
- For labour, Canada and Australia , safe in the knowledge that people are not moving because of massive wage or social security differentials, could waive the detailed controls on labour movement and replace them with the "good hospitality" policy that both countries normally apply to each other's citizens in all other matters.
  - To make this truly effective, Canada's internal inter-provincial and Australia's internal inter-state agreements on recognition of qualifications could be extended to each other's sub-national jurisdictions through the familiar processes that both countries have put in place for internal market purposes.
  - For companies doing business bilaterally, the removal of all red tape for business visits or for intra-company transfers of staff would provide a seamless operating environment.
  - For both labour markets, job-mismatch unemployment could be reduced.
  - For young travellers working to supplement their resources, the experience of each other's country would come without procedural costs.

Many of the rules and controls that apply to bilateral commerce might never have occurred to governments to put in place were these the only two countries to which the rules would apply. By the same token, informal arrangements, based on a handshake with a likeminded partner, might facilitate bilateral commerce. Arguably Canada and Australia are better placed than perhaps any other two economies to try such an experiment. While the gains from improved resource allocation that this would allow would be moderated by the scale of bilateral trade and investment, they would by the same token come without adjustment shocks.

Canada has announced its intention to enter into the Trans-Pacific Partnership negotiations; if realized, this entry would provide the opportunity and framework to explore low-cost and informal ways to deepen the bilateral economic relationship to mutual benefit.

Contents

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Responsibility for the analysis of course rests with the author.

1. INTRODUCTION

Countries trade, it was long thought, because they are different. Canada and Australia are, however, *similar*; in fact, Australia's merchandise trade structure in terms of the balance of trade by commodity resembles Canada's more closely than that of any country in the world. Moreover, bilateral commerce faces the "tyranny of distance"[1] imposed by the Pacific Ocean. From Canada's perspective, Australia is the most distant market in the world.[2] From Australia's perspective, Canada is only one of many distant markets, ranking 80th in the list.[3]

Notwithstanding these apparent *disincentives* to bilateral commerce, Australia and Canada have long been important economic partners. There are good reasons for this. With modern trade logistics, transport costs are far from prohibitive. Meanwhile, for many services, telecommunications advances have genuinely meant the "death of distance". Moreover, the similarities in wealth, socio-economic characteristics, and resource endowments also work to boost trade. With similarity of consumer preferences comes complementarity in opposite seasonality; with similarity of exports comes complementarity in time zones in serving global markets; and with similarity of domestic economic structures come investment possibilities, similar needs for specialized producer services, and opportunities for supply chain participation. And the strong contribution of resources to both economies results in similar responses to commodity price shocks, dampening bilateral exchange rate fluctuations.

However, there is a perception that bilateral commerce has lagged in recent years. This may reflect the pull of other major markets for Australian and Canadian business. But it may also reflect a lack of policy attention as both countries have pursued trading opportunities elsewhere. This study examines this perception and finds that the bilateral commercial relationship is stronger than often thought. At the same time, it identifies a number of areas where Canada and Australia could boost bilateral commerce simply by providing each other conditions already offered to others—i.e., genuine most favoured nation status—or by reciprocating the best treatment offered by either. However, working within conventional frameworks, the gains from such moves would be modest in global perspective.

A bolder vision is also possible. Australia and Canada can take advantage of the similarities in their economies (both in scale and structure), in their societies, and in their governance systems, as well as the high degree of confidence earned by years of close and sustained inter-agency cooperation, to engage in policy entrepreneurship that might entail excessive risks in other bilateral relationships. Towards this end, this study suggests a "thought experiment" concerning the possibility of creating a virtually seamless economic space for the movement of goods, services, capital and labour that would improve resource allocation within both economies without the disruptions that fuller market integration might entail in other bilateral pairings. Canada's announced intention to enter into the Trans-Pacific Partnership (TPP) negotiations, if realized, would provide the opportunity and the framework for such an initiative. In this regard, this study argues that the Australia-Canada commercial relationship is a special case that may reward special attention.

This study is organized as follows. Section 2 describes the current state of bilateral commerce; Section 3 briefly the institutional background. Section 4 evaluates the scope to expand bilateral commerce in goods trade (Section 4.1), services trade (Section 4.2), investment (Section 4.3), labour mobility (Section 4.4), government procurement (Section 4.5) and competition policy (Section 4.6). Section 5 considers the scope for a bolder initiative to create a virtually seamless economic space. Appendix 1 summarizes the results of model simulations for trade in goods and services. Appendix 2 summarizes the results of the analysis of the impact of the Australia-United States on new trade flows ("extensive margin"). Appendix 3 reports the results of the online survey of Canadian business interests in the Australian market.

2. CANADA-AUSTRALIA COMMERCE IN PERSPECTIVE[4]

2.1. COMPARING THE ECONOMIES

Canada and Australia are roughly similar in size and very similar in per capita incomes. In 2011, Canada's population was 53 percent larger, while per capita income evaluated on a purchasing power parity (PPP) basis was about the same (see Table 1).[5] Accordingly, on a PPP basis, Canada's economy is about 50% larger than Australia's. However, the strong valuation of the Australian dollar in 2011 narrowed the size of the gap measured at market exchange rates, with Canada's 2011 GDP of US$ 1,737 billion being only about 20% larger than Australia's comparable figure of US$ 1,448 billion.

Table 1: Size of the Australian and Canadian Economies in 2011

	Australia	Canada
Population (thousands)	22,504	35,083
Per capita gross national income (current USD at market exchange rates)	64,351	50,265
Per capita income at purchasing power parity (USD)	40,816	39,982
Gross domestic product (current USD billions at market exchange rates)	1,448	1,737

Source: International Monetary Fund, World Economic Outlook Database, April, 2012.

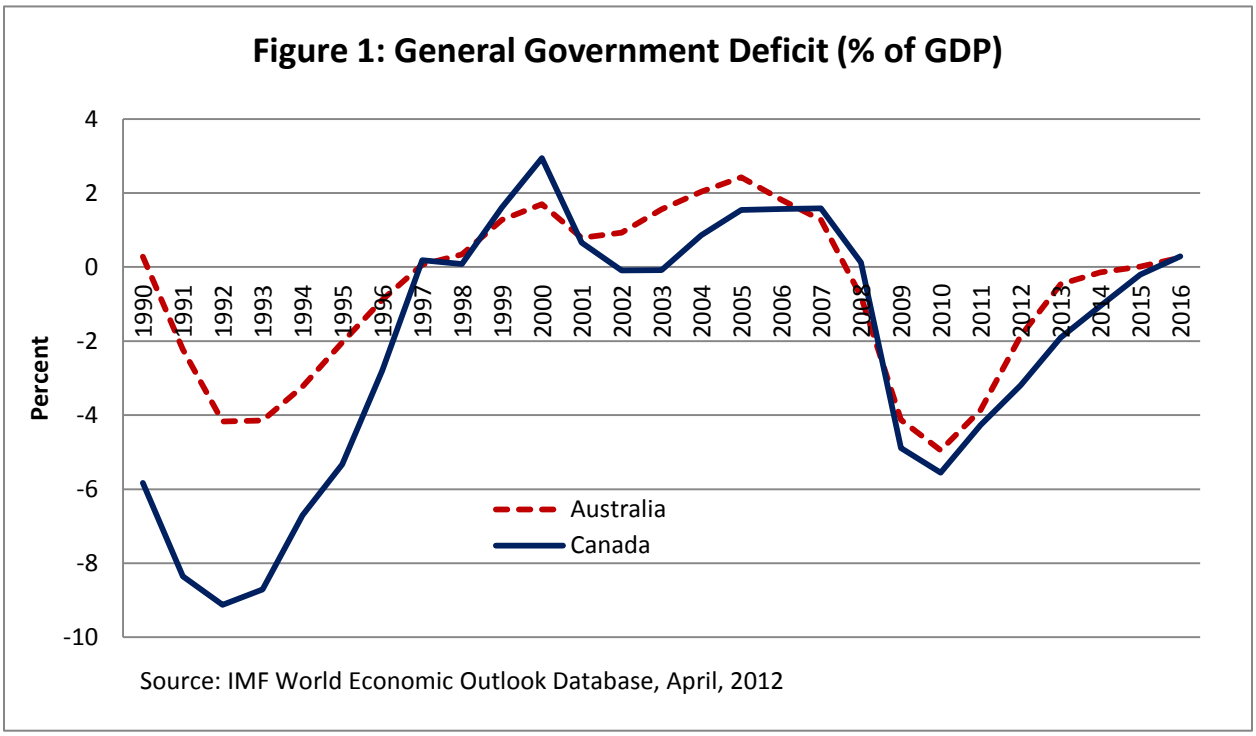
Macroeconomic performance tends to be generally similar. Canada has had marginally lower inflation but Australia had stronger employment and productivity growth (Table 2). The IMF projects a continuation of this relative performance in growth and inflation for the two economies over the medium term.

Table 2: Main Economic Indicators

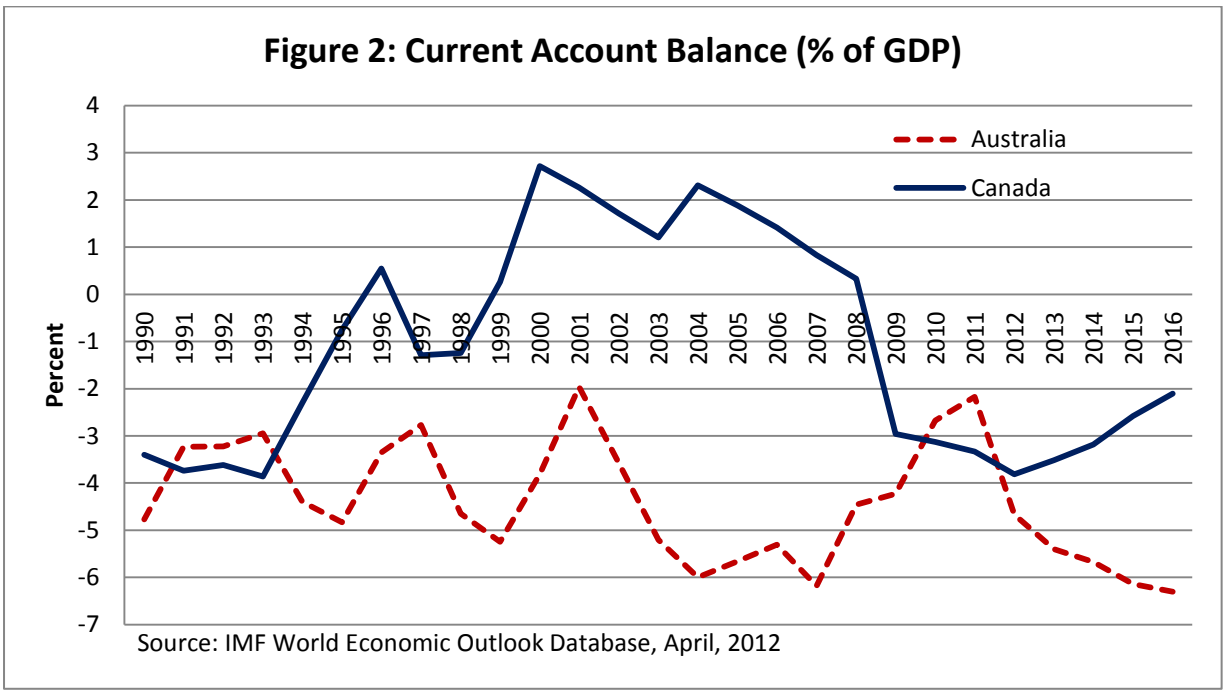
	1991-2000	2001-2010	Forecast: 2011-2016
Average Annual Real Growth in GDP			
Australia	3.48%	3.07%	3.25%
Canada	2.92%	1.87%	2.33%
Inflation (consumer prices)			
Australia	2.21%	3.00%	2.81%
Canada	1.99%	2.02%	2.03%
Employment			
Australia	1.35%	2.27%	n/a
Canada	1.22%	1.45%	n/a
Aggregate Productivity			
Australia	2.09%	0.78%	n/a
Canada	1.68%	0.42%	n/a

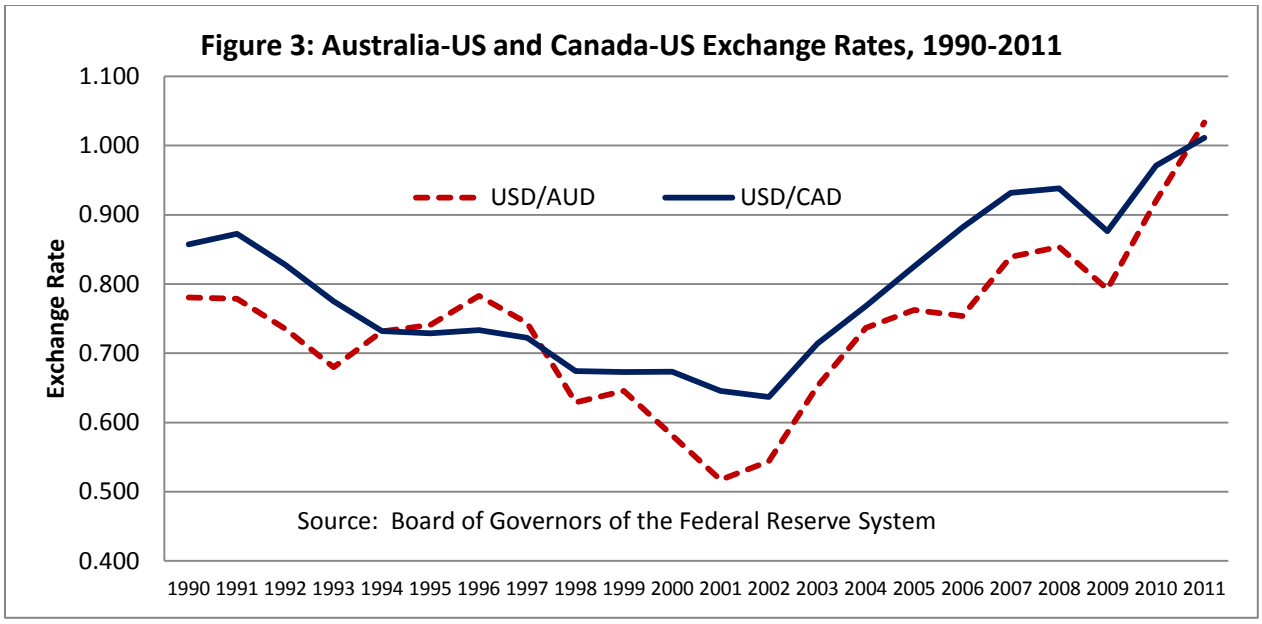
Source: International Monetary Fund, World Economic Outlook Database, April, 2012

Fiscal performance has also followed similar paths in the two economies: both countries dug themselves out of deep holes in the early 1990s (although Canada's was much deeper) and enjoyed a strong run of fiscal surpluses from the late 1990s until the onset of the Great Recession of 2008-2009. The extent of fiscal deterioration and the projected recovery path are also highly similar (Figure 1).

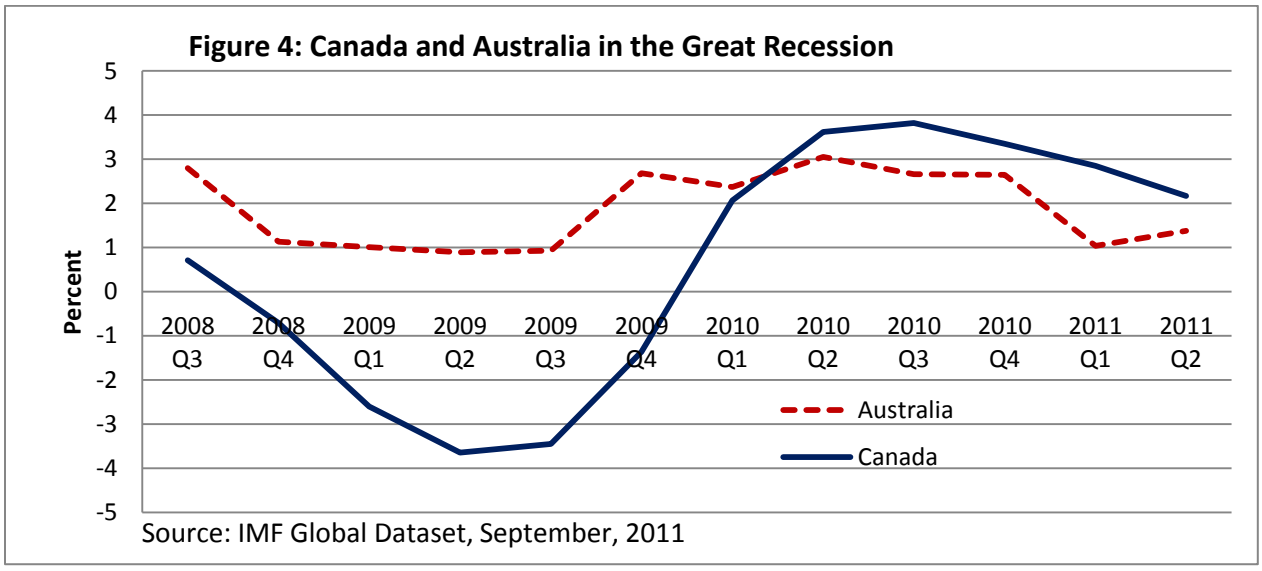


Despite the similarity of fiscal performance and a similar exposure to commodity price shocks, performance on the current account has differed: Canada's current account balance expressed as a share of GDP followed its fiscal pattern while Australia's stayed in deficit throughout the past two decades (Figure 2). This occurred despite highly similar exchange rate trends (Figure 3).



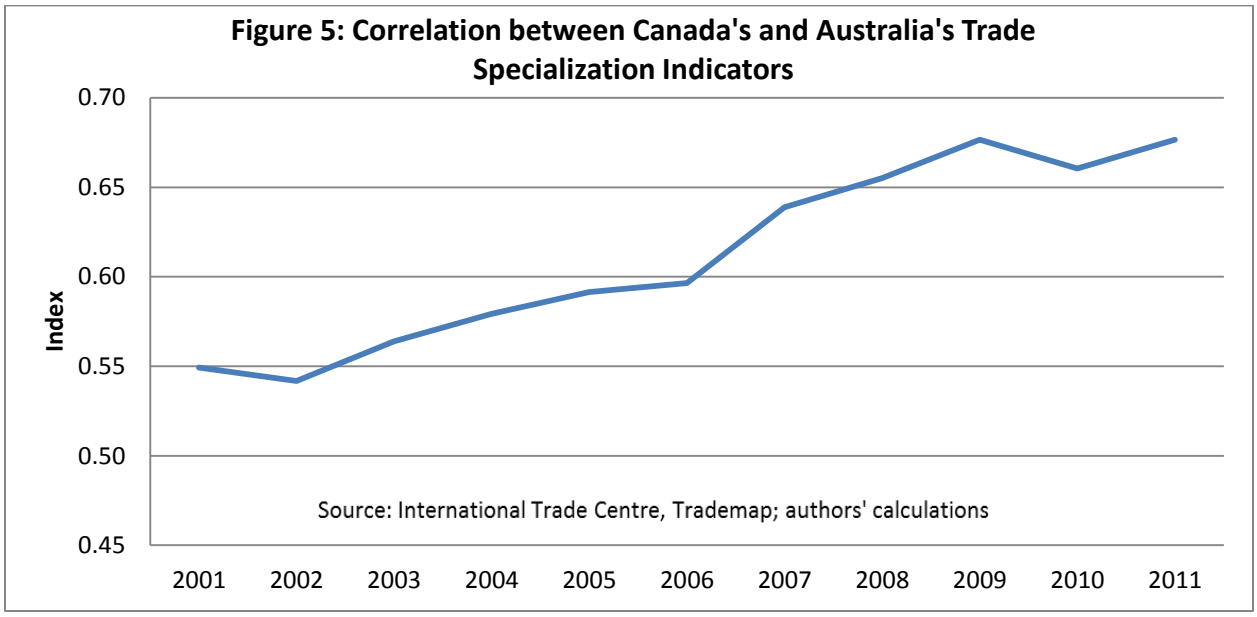


Both economies weathered the global crisis of 2008-2009 well. Neither economy experienced a financial crisis, despite the fact that both had witnessed significant run-ups in housing prices in the mid-2000s boom. Canada with its deep exposure to the United States, which was the epicentre of the crisis, experienced a large contraction in output but rebounded strongly as the global economy stabilized (Figure 4). Australia escaped even a technical recession; this is generally credited to the shift of its trade and investment linkages towards Asia, and in particular towards China, which has become the largest foreign investor in Australia (UNCTAD, 2011).



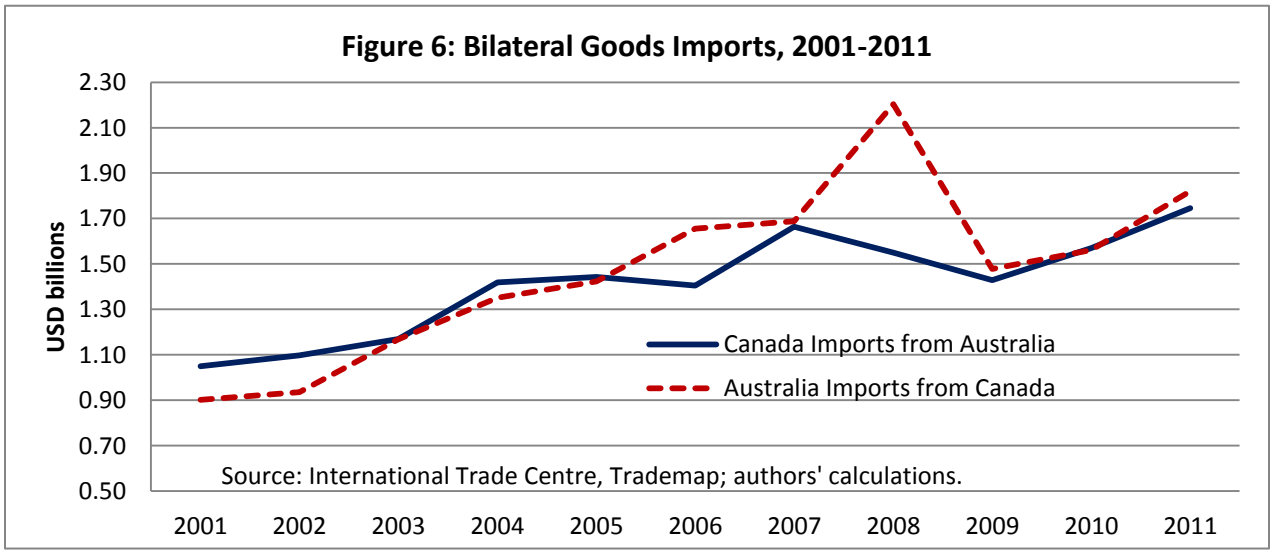
In terms of industrial structure and trade, the Canadian and Australian economies are again highly similar. This similarity is best brought out by the correlation coefficient between the trade specialization indicator (TSI) for Canada and Australia. The TSI, for good *i*, is given by the following expression: $TSI_i = (X_i-M_i)/(X_i+M_i)$. The TSI reveals the pattern of net trade by product or product group (values run from -1 if a country only imports a product to +1 if it only exports the good; 0 indicates balanced trade). The evolution of this indicator over time reveals changes in a country's comparative advantage. If the Canadian and Australian patterns of net trade by product are similar,

the correlation coefficient will be positive; the closer to the value "1", the closer the similarity of the pattern of revealed comparative advantage between the two economies. As shown in Figure 5, the Canadian and Australian economies have a highly similar pattern of net exports by product—and the pattern has been getting more similar over time.

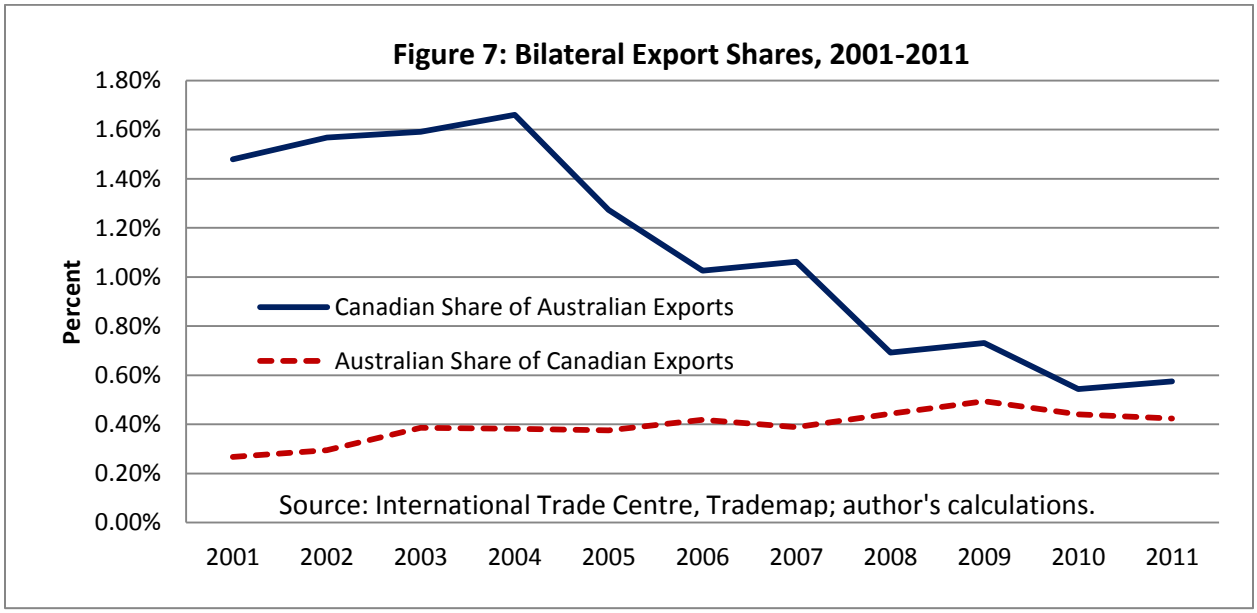


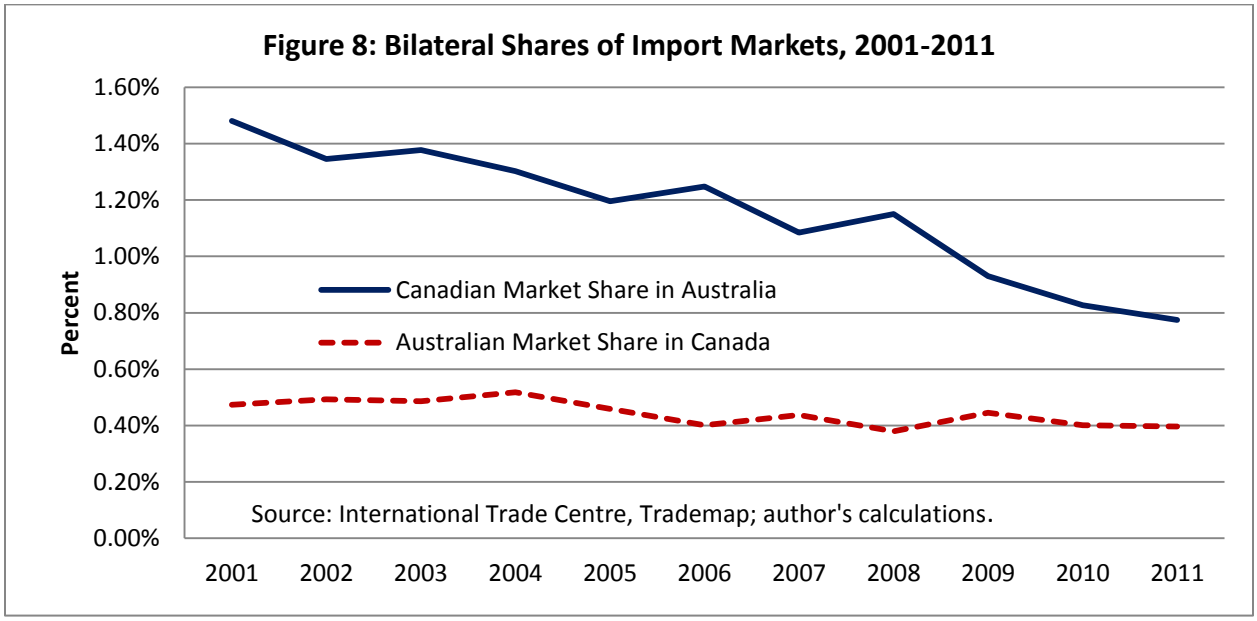
2.2. THE CANADA-AUSTRALIA COMMERCIAL RELATIONSHIP IN PERSPECTIVE

Goods trade appears to be well balanced. Using import data on both sides to measure the trade flows, each country reported imports from each other valued at close to US$ 1.8 billion in 2011. Indeed, measured this way, the bilateral trade relationship has been almost perfectly balanced over the past 10 years (Figure 6): over this 11-year period, each country imported, in round figures, a cumulative US$ 16 billion from each other.



In terms of relative importance in bilateral goods trade, however, the trends were divergent. From Australia's perspective, the more rapid growth of two-way trade with Asia resulted in Canada slipping both in terms of the share of its exports that went to Canada and the share of its imports sourced from Canada. From Canada's perspective, Australia edged up in importance as a destination market for its exports and slipped only marginally as a source of imports.

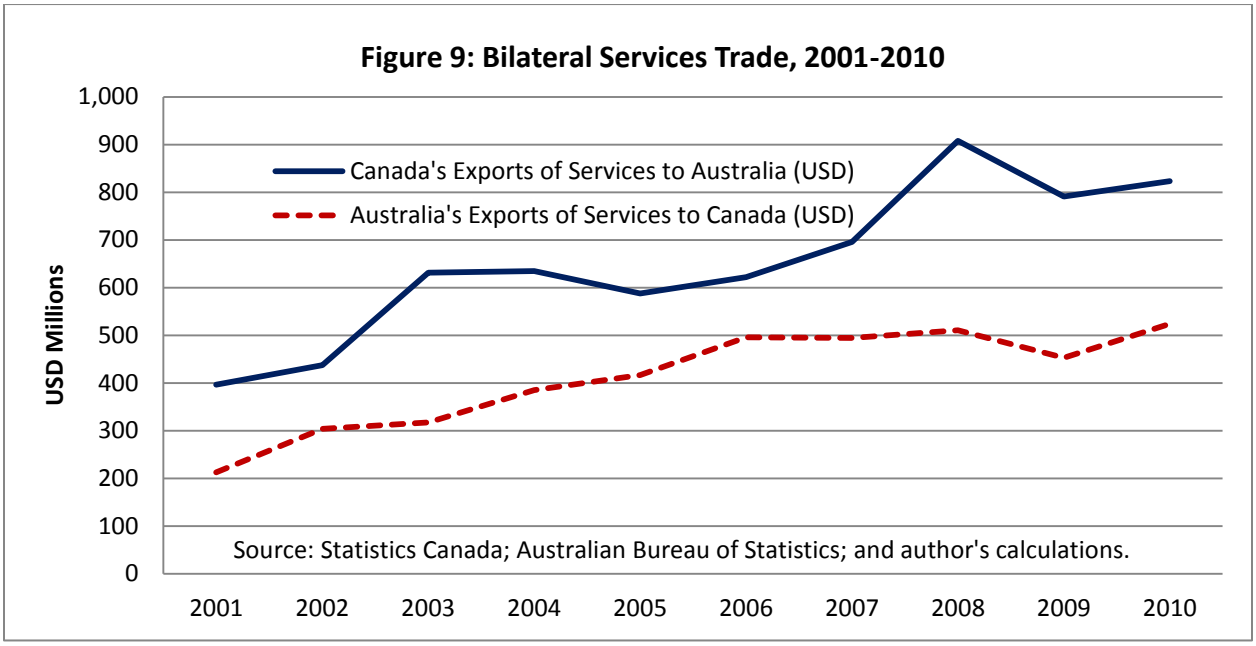




Canada was the 20th-ranked market for Australian goods exports in 2011 (counting the European Union as a single market). This represents a slide from 17th largest in 2006. The US$ 1.54 billion in exports in 2011 (measured by Australian export data) accounted for a little over half a percent of Australian sales abroad, down by almost half from a decade earlier. Meanwhile Australia ranked 11th on the list of world markets for Canadian merchandise exports (again counting the European Union as one market). This represents a slide from 8th place as recently as

2006. The US$ 1.9 billion in sales (measured by Canadian export data) accounted for a little less than half a percent of Canadian sales abroad in 2011.

In services, two-way trade is small but growing solidly: Canada's 2010 exports to Australia were about $US800 million, while Australia's exports to Canada were about $US527 million (Figure 9).

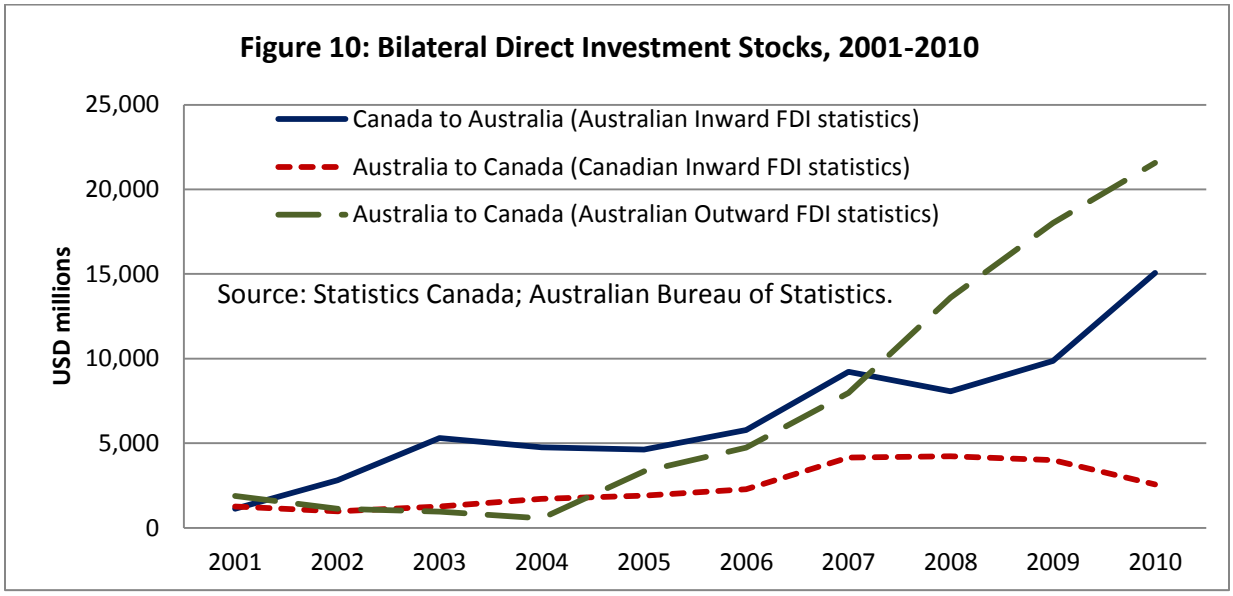


However, to put these figures into perspective, for both Canada and Australia, global services exports account for less than one-fifth of global exports of goods and services; by comparison, bilaterally, this share of services is on the order of one-third for both countries. Clearly, services travel more greater distance more easily than goods.

Cross-border trade statistics do not reflect goods and services delivered through a local commercial presence in the destination economy established with foreign direct investment. For some types of goods (e.g., bottled drinks) and for many services, sales by foreign affiliates consititute the most important mode of trade. Bilateral Canada-Australia foreign affiliate sales (FAS) data are not available. Some idea of the importance of foreign affiliate sales for commerce can, however, be gained from a look at the global figures. According to UNCTAD (2011) global foreign affiliate sales in all host economies amounted to US$ 32.96 trillion in 2010, 74% greater than global exports of goods and services which amounted to US$ 18.9 trillion in 2010 (WTO, 2011), and 67% greater than the stock of global FDI which amounted to about US$ 20 trillion in 2010 (UNCTAD, 2011).

As regards direct investment between Canada and Australia, an important caveat concerns measurement. Direct investment statistics at the bilateral level are notoriously weak and subject to potentially large discrepancies for a variety of reasons (UNCTAD, 2011; Box 1). In the case of Australian investment in Canada, the discrepancy is huge: Australia's figures for outward FDI to Canada indicate a level of about US$ 21.6 billion in 2010; Canada's estimate suggests a level of only about US$ 2.6 billion. Accordingly, these figures have to be treated very cautiously. A large discrepancy such as this most likely reflects the path that investment takes, due to considerations of corporate structure, "tax planning", or other reasons. For example, an Australian firm might choose to make a direct investment in Canada through its US subsidiary rather than directly from the Australian parent. In this case, from the perspective of Canadian inward FDI statistics, the apparent investment in Canada comes from the United States whereas the Australian parent may report the same flow as an investment in Canada. While statistical

agencies generally consider inward FDI statistics as being more robust than outward FDI statistics, in this case the apparent scale of Australian presence in the Canadian market gives some credence to the higher Australian figures.



One way to put these data into perspective is to compare the investment stocks with the annual flow of goods and services, bilaterally and globally. Both Canada and Australia have global direct investment stocks that are larger than annual global exports of goods and services. For Canada, in 2010, the stock of investment was 1.55 times the size of global exports of goods and services; for Australia, the comparable ratio was 1.31. However, in the bilateral relationship, these ratios are about an order of magnitude larger: for Canada the ratio in 2010 was 8.7; for Australia, an eye-opening 13.1. According to UNCTAD (2011; Table 1.5) the ratio of sales of foreign affiliates to the stock of FDI globally was about 1.67 in 2010. If we apply this global ratio to the bilateral investment stocks of Canadian and Australian companies, we arrive at figures of foreign affiliate sales in 2010 of US$ 36 billion for Australian firms in Canada and US$ 25 billion for Canadian firms in Australia. Seen this way, the relationship suddenly looks neither small, nor (taking into account the growth of bilateral investment) lagging.

Modern trade theory, which focuses on the behaviour of trading firms, argues that firms face a "proximity-concentration" trade-off: that is, they trade-off efficiency gains from concentrating production in their home base against efficiency gains from reducing shipping costs by establishing separate production facilities in more distant markets. Clearly, distance (and in all likelihood similarity as well) favour investment and sales through foreign affiliates very heavily over cross-border trade in Canada-Australia bilateral commerce.

To summarize, bilateral cross-border goods trade is remarkably well balanced and growing steadily, but at less than the pace of each country's global trade, implying a declining share in each other's overall trade picture. Services trade constitutes a greater share of overall trade bilaterally than globally, consistent with the expectation that distance is less important for services trade than for goods trade. Most importantly, FDI appears to be an order of magnitude greater in bilateral commerce than globally, consistent with expectations based on a proximity-concentration trade-off whereby more distant markets are accessed by commercial presence. Using the global ratios of foreign affiliate sales to FDI stocks, two-way goods and services trade between Canada and Australia, including foreign affiliate sales, may have been on the order of about US$ 65 billion in 2010, at least an order of magnitude greater than cross-border trade alone.

The number of Canadian firms exporting to Australia, as recorded in Canada's Exporter Registry, grew from 2,161 in 2003 to 2,977 in 2008, before falling off to 2,780 as the global economic crisis unfolded in 2009. The growth in Canada's exports to Australia in the 2000s thus was driven in part by a wave of entry of new Canadian exporters into the Australian market. The number of Australian firms exporting to Canada was reported by Austrade to have been about 2,000 in 2008, or about 2/3 as large a number.[6] The investment figures suggest that many firms have also established a commercial presence.

Accordingly, there is an expanding base of business with an interest in the policy environment. The establishment of the business Leadership forum in 2010 is no surprise in light of these findings; governments need to take note.

3. INSTITUTIONAL BACKGROUND

Throughout their history, Australia and Canada have had a close bilateral relationship across the full range of areas—political, social, and economic. In fact, Australia was the first economy to which Canada dispatched a trade commissioner.[7] Close ties have been fostered by common circumstances and concerns, like-minded views on many issues, and many shared historical experiences. Australia and Canada cooperate as confirmed multilateralists in promoting an open global trading system in the context of the World Trade Organization (WTO), as founding members of the Asia Pacific Economic Cooperation (APEC) forum, and in many other global and regional fora, including the United Nations organizations and the Commonwealth. Under consular sharing arrangements, Australians and Canadians can seek assistance from each other's diplomatic missions in some 40 countries. The commonalities of interests and issues and the similarities of institutional governance frameworks have also naturally led to discussions and consultation at the government, academic and business levels on virtually the full gamut of public policy issues. The Australia-Canada Economic Leadership Forum, the inaugural meeting of which took place 16-18 November 2010 in Sydney, is the most recent example.

Australia provides support for its export and investment interests in Canada from its High Commission in Ottawa and the offices of Austrade, its trade promotion agency, in Toronto and Vancouver. Canada supports its export and investment interests in Australia from the High Commission in Canberra and the Consulate General in Sydney. A general framework for bilateral cooperation was established with the Trade and Economic Cooperation Agreement (TECA) signed Nov 15, 1995, and the Canada-Australia Trade and Economic Cooperation Arrangement 2007.

Bilateral trade in goods is conducted for the most part under WTO rules. The Canada-Australia Trade Agreement (CANATA), established in 1960 and amended in 1973, offered preferential tariff rates on a limited range of products. The CANATA still provides some tariff preferences. However, the significance of these is minimal: according to the 2011 Trade Policy Review of Australia, most of the CANATA measures have been superseded by tariff reductions negotiated in the WTO (WTO, 2011b; p. 25).[8]

Australia has six FTAs currently in force (ASEAN, Chile, New Zealand, Singapore, Thailand, and the United States), plus nine more under negotiation.[9] According to the Australian Department of Foreign Affairs and Trade (DFAT), the countries covered by in-force FTAs account for 28 per cent of Australia's total trade. The generally low levels of Australian tariffs mean that the trade diversionary effects of these FTAs is fairly modest; indeed the Australian Productivity Commission (2010) found that utilization rates for Australia's FTAs were low, reflecting undoubtedly the costs of documenting supply chains to meet rules of origin.

Canada meanwhile has in-force agreements with 11 partners (Colombia, Peru, European Free Trade Association (EFTA), Costa Rica, Chile, Israel, and the United States and Mexico (North American Free Trade Agreement)).

Canada has 9 other negotiations at various stages of the process, some agreed and subject only to ratification, others still under negotiation)[10]. A similar consideration regarding trade diversion effects applies in respect of Australia's exports to Canada: low MFN tariffs tend to limit trade diversion, although some undoubtedly does take place.

Bilateral trade in services is conducted under the multilateral WTO General Agreement on Trade in Services (GATS), to which both Australia and Canada are signatories. Most of the effective impediments to services trade are however sector-specific measures in domestic regulatory systems, including immigration rules that cover labour mobility. Bilateral instruments dealing with these issues are described in more detail in the discussion of the potential to enhance services trade.

As regards ***investment***, UNCTAD lists three types of instruments: bilateral investment treaties (BITs), double taxation treaties (DTTs) and "other". Globally, there are at present thousands of such agreements in place. [11] Both Canada and Australia are active in signing such agreements: the UNCTAD data base lists 158 such agreements for Canada and 103 for Australia. Bilaterally, Australia and Canada have a double taxation agreement in force[12] but not a bilateral investment treaty (foreign investment promotion and protection agreement or FIPA in Canadian terminology; and investment promotion and protection agreement or IPPA in Australian terminology).

Typically, BITs address post-establishment issues including provisions for national treatment, MFN treatment, transparency, transfer of investors' funds, and expropriation and nationalization. In some cases, such as the NAFTA Chapter 11, the agreement provides for investor-state dispute settlement. BITs may also address pre-establishment issues and thus provide for some investment liberalization. Both Canada and Australia have included investor-state dispute settlement provisions in some of their respective bilateral trade agreements. Accordingly, there is less than most favourable treatment applied in the Canada-Australia relationship. However, based on the general assessment of the impacts of international investment agreements, the potential positive impact of entering into an IPPA/FIPA that includes investor-state dispute settlement, if any, is likely to be minimal.

As regards ***intellectual property***, Both Canada and Australia are members of the major multilateral body, the World Intellectual Property Organization (WIPO), and parties to the major multilateral agreements (WTO TRIPs Agreement, the UNESCO Convention on the Protection and Promotion of the Diversity of Cultural Expressions), and the plurilateral Anti-Counterfeiting Trade Agreement (signed in 2011). All of Australia's recent FTAs have included intellectual property chapters. For the most part, these simply reaffirm the commitments in the WTO TRIPS Agreement. The FTAs with Chile and the United States, however, go beyond the TRIPs agreement and, for example, extend the term of protection for copyright and related rights, to the life of the author plus 70 years. Canada generally does not include intellectual property chapters in its FTAs; the NAFTA and draft CETA agreements are the exceptions.

Electronic commerce ("e-commerce") is an immense emerging area for policy and thus for policy cooperation and coordination. Since e-commerce is inherently global in nature, the policy issues have generally been addressed in multilateral organizations. Moreover, as a mode of commerce, the issues that are raised cover virtually the gamut of issues encountered in direct commerce and at all levels—sub-national, national, regional and global. The Government of Australia and the Government of Canada have been active at all levels and importantly have issued a *Joint Statement on Global Electronic Commerce* to promote the development of electronic commerce in both countries by, *inter alia*: ensuring that existing legal and commercial frameworks apply to electronic transmissions and that new rules or changes to existing rules for business transactions take into account electronic commerce; building trust for users and consumers by addressing such issues as privacy, security, and consumer protection; and working towards a seamless global environment for electronic commerce. The action agenda covers bilateral

cooperation in regional and multilateral fora, including in APEC, the OECD, the WTO, the World Customs Organization (WCO), the World Intellectual Property Organization (WIPO), and the United Nations Commission on International Trade Law (UNCITRAL). As well, it covers bilateral consultation and cooperation on a range of issues, including taxation, electronic authentication (including recognition arrangements among certification services providers and the authentication certificates they issue), consumer protection, privacy, security of electronic platforms, dealing with illegal and harmful content (e.g., deceptive spam, spyware, malicious code, botnets, and other related network threats), and addressing global Internet governance issues.

Canada and Australia are both active in terms of use of ***science and technology agreements***. Australia has been the more active of the two countries in establishing formal state-to-state agreements in this field with some fifty-five S&T agreements in place. By comparison, Canada has only nine agreements in force, although S&T agreements are considered one of the main instruments under Canada's Global Commerce Strategy. S&T agreements are commonly used to provide a framework for collaborative research, fellowships/visiting scholar programs that generate longer-term ties between scientific communities, and in some cases providing funding for projects that are priorities for both governments. Such agreements typically feature regular joint meetings to provide strategic direction. Canada and Australia currently do not have an existing S&T Agreement. They have however recently explored possibilities for greater collaborative research[13] and there is much collaboration between individual Canadian and Australian educational institutions. Indeed, Canadian and Australian universities have established over 700 formal and informal agreements amongst themselves.[14] The promotion of S&T cooperation thus already features prominently in the bilateral programs of both Australia and Canada; the value-added of a formal agreement, absent funding for compelling specific projects, is not clear.

Finally, in ***education***, Canada and Australia have a long history on educational policy consultation and many students have taken advantage of formal international student exchange programs: in 2010, 45 Canadian institutions reported operating student exchange programs with 36 Australian institutions.

4. ENHANCING CANADA-AUSTRALIA COMMERCIAL RELATIONS

While Australia and Canada are highly open economies, both still maintain restrictive tariffs on bilateral trade in goods under a significant number of tariff lines and have in place a range of regulatory policies that tend to restrict bilateral trade in services. Moreover, in a number of areas policies are less favourable than applied to other partners. Barriers to direct investment are, for most potential investments, minimal. Mergers and acquisitions involving large companies may run into difficulties as happened with BHP Billiton's proposed takeover of Potash Corporation of Saskatchewan, but these are likely to be few and far between. Other regulations may, however raise the cost of doing business, dissuading at least some potential investors at the margin.

4.1. TRADE IN GOODS

Two-way cross-border goods trade was about US$3.6 billion in 2011, and very evenly balanced (going by each country's import statistics). However, this is a fairly modest amount given the size of the two economies and their openness to trade. Neither country is in the other's top ten list of export destinations. This section takes up the question of the extent to which these numbers can be increased through policy initiatives.

TARIFF ELIMINATION

Australia has 2,771 non-zero tariffs in place on Canadian goods, the large majority at a flat rate of 5%. Some 224 tariff lines feature rates of 10%, while only a handful are below 5% or above 10% (Figure 11). Those in the latter category include 5 tariff lines on varieties of cheese and 6 lines on used motor vehicles. According to the Australian tariff schedule for 2011, Australia provides preferences to Canada on 504 tariff lines, almost all of them in respect of MFN tariffs equal to 5% (the simple average of the tariff preferences is 4.8%). Canada has a greater number of quantitatively significant tariffs (Figure 12): close to 2,000 are in the 5.0 to 20% range and about 150 are higher still. Canada provides preferences to Australia on 383 tariff lines with an average preference value of 5.78% (based on International Trade Centre MacMap data).

Figure 11: Distribution of Australian Tariffs on Imports from Canada

Source: Australian Tariff Code, 2011

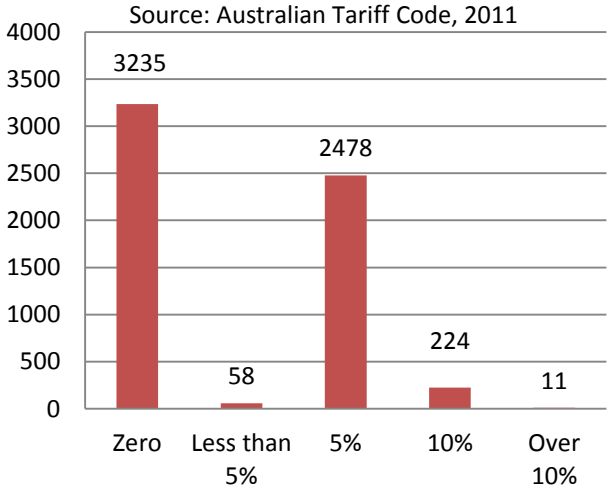
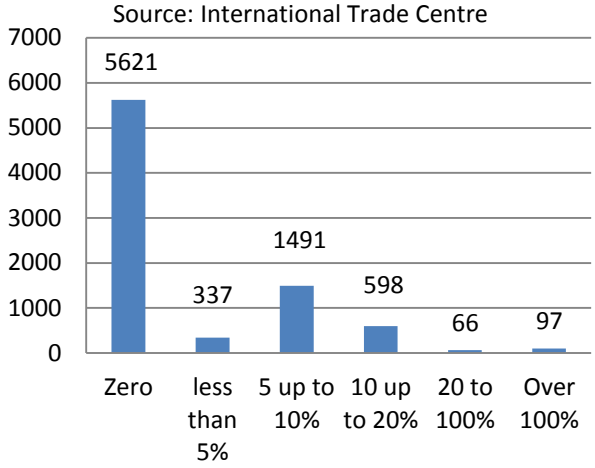


Figure 12: Distribution of Canadian Tariffs on Imports from Australia

Source: International Trade Centre



According to the simulations using the GTAP model reported in Annex 1, tariff elimination could expand two-way goods by US$ 520 million or 16%, and on a reasonably balanced basis. The major gains for Canada are identified as likely to be in manufactured products, largely in machinery and equipment; for Australia, the major gains are identified as likely to be in agricultural products, mainly in beef and dairy. Both countries make smaller gains across a range of other sectors.

However, this may not be the whole story. Typically, tariff elimination takes place in the context of a broader trade agreement that includes various other facilitating elements. Direct measures of these various other effects are generally not available. In this study, we look for evidence of gains in trade that could be identified with new firms entering into export markets or existing firms introducing new products, using the Australia-US FTA as a "natural experiment" for Canada and Australia. There is some circumstantial evidence that the AUSFTA increased both the introduction rate and survival rate of Australian products in the US market; however, the reverse was surprisingly true for US products in the Australian market. A second test considered tariff lines in which zero trade was observed from 2000 through the first year of the AUSFTA but trade was observed on a more or less sustained basis over the period 2008-2010. About 4% of both US exports to Australia and of US imports from Australia over the period 2008-2010 were in such categories. While most of this trade was in tariff lines in which there were no tariffs to eliminate, there is no compelling evidence for a strong "extensive margin" effect. Accordingly, there is no

basis for a claim that stronger effects than those indicated by the CGE analysis can be obtained through conventional bilateral measures.

A 16% expansion in two-way trade remains nonetheless a tangible, if modest, gain in the commercial relationship. Moreover, consideration of the evidence concerning the number of firms engaged in trade in the Canada-Australia relationship suggests that tariff elimination would likely bring several hundred new firms, mostly small and medium-sized enterprises, into bilateral trade activity. For these firms, the trade gains would be significant, most likely representing an important diversification of export markets, and possibly associated with the firm-level innovation and productivity gains that empirical evidence based on modern heterogeneous firm trade theory demonstrates. It is interesting to note that Austrade sees Canada as a "step-up" market that Australian exporters can enter in preparation for the larger US market. Australia could serve the same role for Canadian exporters looking to venture beyond North America and gain an Asia-Pacific exposure, and some Canadian firms do indeed look at the Australian market in that way.

While tariffs are a relatively minor inhibiting factor in bilateral trade, a number of firms indicated that tariff elimination would be a very important factor in helping them to expand business. Two firms identified tariffs on used machinery as the main reasons for abandoning previous attempts to enter the Australian market.

Overall, the simulations suggest there is a tidy gain to be made in goods trade from the elimination of tariff barriers, with likely some knock-on benefits in terms of prompting a new cohort of firms to enter into trans-Pacific trade.

NON-TARIFF MEASURES

Technical standards and reliability conformity assessment have both positive and negative effects on competition and international trade. On the one hand, such regulations can increase consumer acceptance of new products by addressing consumer safety concerns and increasing the transparency of product information. Moreover, assurance of specifications and quality of production inputs is vital for business supply chains. On the other hand, meeting certification requirements in each new market multiplies costs for exporting firms.

Both Australia and Canada are active internationally in agreeing internationally aligned standards, including multilaterally through the International Standards Organization (ISO) and regionally through the APEC Subcommittee on Standards and Conformance. Canada and Australia have two mutual recognition agreements (MRAs) concerning conformity assessment in place with each other, for telecommunications equipment (as part of the APEC MRA), and for medicine manufacture. This does not appear to be a policy area where the Canada-Australia relationship lags.

In goods trade, the main areas where non-tariff barriers impact on bilateral trade potential are agricultural support policies and sanitary and phytosanitary (SPS) measures.

On Canada's side, the major factor is the restriction on trade posed by supply managed agricultural sectors, in particular in the dairy sector. Australia and Canada both have dairy sectors of roughly comparable size (Australia has about 1.7 million head of dairy cows compared to Canada's approximately 1.0 million), although they appear to operate somewhat differently, with climatic conditions, land availability and cost factors obviously playing a significant role. The potential increase in Australian dairy exports to Canada estimated in the CGE analysis of about US$70 million could be accommodated with an expanded quota under Canada's supply management system with only a modest impact on Canada's sector, if phased in over a number of years. The seasonal differences (milk

production peaks in the spring and troughs in the autumn) would favour north-south trade in the traded components of milk (milk powder concentrates for commercial production) since transportation costs would be offset by reduction of inventory costs. The possibilities for trade in differentiated dairy products (cheeses, yogurts etc.) should be as good as for other differentiated food and beverage products such as wine. In short, given the scale similarities between Australia and Canada, bilateral trade liberalization in dairy is thinkable for Canada under modalities that do not involve wholesale reform of the supply management system.

On Australia's side, the most important factor is the quarantine regime that Australia maintains to protect its unique ecology from risk of entry of non-indigenous pests and plant and animal diseases. Australia tends to have low tariffs on agricultural products but very restrictive quarantine provisions, which translate into very high tariff equivalents. Under WTO rules, a country is permitted to set its own risk threshold; the only requirement is that it be based on a scientific risk assessment and applied consistently. Australia's quarantine provisions have impacted on Canada's exports in a number of areas, including beef products, fresh pork and unprocessed salmon. Australia has recently introduced new regimes for beef and pork and reached agreement with Canada on salmon. However, the conditions of access remain difficult to meet; Canada has suspended the process for gaining access to the Australian beef market and does not compete in Australia's fresh pork and salmon markets. Perhaps in recognition of the difficulty in moving in this area, Australia's quarantine system is not one of the top priority issues for Canada's agricultural market access listed in the 2010-2011 market access report by Agriculture and Agri-Foods Canada.[15] Nonetheless, as Australia has agreed to facilitation mechanisms regarding its biosecurity system in some of its FTAs[16], this is a step that could be taken in a Canada-Australia context and would respond to the interests of Canadian exporters who indicated that the SPS regime was an inhibiting factor.

4.2. TRADE IN SERVICES

The strong growth in business services trade on a cross-border basis in the Internet age is strongly indicative of the potential for gains from trade due to improved matching of service providers' capabilities and business requirements. However, evaluating the trade potential from liberalization of services trade is complicated by a number of challenges. Unlike the case of merchandise trade, for which there exists a comprehensive and reasonably reliable data set describing the height of barriers to cross-border trade, such information does not exist for services trade. Services trade barriers take the form of regulations (e.g., requirements for service providers to meet particular qualifications or standards or to acquire licenses, as in the case of medical or legal practitioners), government procurement restrictions, the requirement for foreign providers to establish subsidiaries with minimum capital for prudential regulatory purposes as in the case of financial institutions, the presence of regulated monopolies in sectors with steep increasing returns or network externalities such as telecommunications which create difficulties for foreign suppliers to gain access to established networks, the granting of monopoly concessions on services on profitable market segments to finance the provision of service on a mandatory basis to other areas where such services would otherwise be lacking (thinly populated rural areas for mail, and less dense air and rail passenger routes), and others. Tariff equivalents for the impact of these highly heterogeneous restrictions on market access to international service providers do not exist. By the same token, it is not possible to directly link liberalization commitments to quantified increases in services trade.

SERVICES TRADE POTENTIAL

Estimates of the impact of services trade liberalization are generally based on inferences drawn from available indicators. Two methods predominate. First, gravity models of bilateral services trade flows are used to infer the relative height of services trade barriers in a particular market by comparing the intensity of services trade in that

relationship (given size of the economy, distance and other factors) to the intensity of bilateral service trade within, for example, the European Union which provides a baseline against which the intensity of services trade between other nations can be evaluated. Second, the margins realized by service providers in a particular market can be compared to margins in the most open market for which data are available (Hong Kong and Singapore are typically used as the benchmark for the most competitive and thus by inference open market).

Based on the latter approach, according to the simulations using the GTAP model reported in Annex 1, two-way bilateral trade could be increased by US$343 million or by over 50% on a well-balanced basis. Based on the available estimates of margins in various sectors, there is significant room for expansion of two-way trade in business services and air transportation, with more moderate gains in financial services and insurance, telecommunications and shipping. An important caveat to these estimates is that this approach does not tie the trade impacts to specific regulatory measures that are liberalized; the results accordingly are subject to greater uncertainty than the estimates for goods trade and must be treated with appropriate caution.

Even in the absence of liberalizing measures targeted at specific services, some degree of services trade expansion may be expected from a broader initiative encompassing a variety of measures to deepen commercial relations. For example, expanded goods trade, progress on recognition of qualifications (a factor identified by business interests as an impediment to business), improved access to government services procurement, improved air services (discussed in greater detail below) and possibly other measures can all work to generate more business and attract more competition to particular services areas, thus generating the trade activity and efficiency gains that theory predicts.

For example, the services provisions in the AUSFTA were for the most part those already made under the GATS; hence, a large impact would not be expected. However, given that the traditional services exporters have been losing market share to surging services imports from low-cost developing countries (e.g., US imports of services from India rose by a factor of more than seven between 2000 and 2010), it is interesting to observe that Australia's share of the US services market held up better than Canada's in the post-AUSFTA period, by an amount that would be equivalent to a 16.3% expansion in services exports. As regards, the US share in the Australian market, there is an apparent change in trend coincident with the AUSFTA from a declining trend to a flattish upward trend. Compared to alternative extrapolations of the pre-AUSFTA trend, Australia's services imports from the United States were about 20-25% greater in 2010 than they would have without the FTA. While no conclusions can be drawn from this level of analysis, there is some *prima facie* evidence for positive effects.

AIR SERVICES AGREEMENT

The 1988 *Agreement between the Government of Canada and the Government of Australia relating to Air Services,* as renewed by a memorandum of understanding in 2000, is less than state of the art.

From Canada's perspective, it is less liberalizing than more recent agreements under Canada's new international air policy, *Blue Sky*, introduced in 2006. To date, Canada has negotiated 28 new or updated agreements, including one with New Zealand.

Australia currently has air services agreements with 68 countries. The Australian Government is also seeking to move to a new generation of air services agreements with like-minded partners that go further than the traditional exchange of traffic rights to include open capacity, beyond and intermediate rights, safety, security, environment, competition and investment provisions.

Accordingly, this is one area where there is room to enhance the commercial relationship. Business has indicated that improved air connections would be valuable in facilitating doing business in a bilateral context.

4.3. INVESTMENT

Without a doubt, the strongest feature of the Australia-Canada commercial relationship is direct investment. While foreign affiliate sales information is not available, based on global estimates of the value of sales for a dollar of FDI, it is likely that this mode of trade is by far the most important for both goods and services.

Both Australia and Canada promote inward investment and maintain highly welcoming regimes for foreign firms seeking to establish a local presence. Australia and Canada rank 2nd and 3rd respectively in the World Bank's 2012 *Doing Business* rankings in terms of starting a business and 13th and 15th in terms of overall ease of doing business. Canada imposes few requirements on business start-ups. Companies that incorporate federally under the Canada Business Corporations Act (CBCA) must establish a registered office within Canada, and at least 25% of the directors must be resident Canadians. If the corporation has less than four directors, then at least one must be a resident Canadian. There are no minimum paid-in capital requirements. Australia's requirements are equally minimalist, if slightly different: a company must have an Australian business address and at least one Director and one secretary who are normally resident in Australia. There are no capital requirements.

As regards entry through a merger or acquisition, under both Australian and Canadian competition law, mergers and acquisitions that would work to reduce competition in the internal market are subject to review by competition authorities.

In addition to the general framework governing investment, both countries maintain some restrictions on foreign direct investment, including limitations on investments in a small number of sectors and a screening procedure for "large" investments in other sectors. In this regard, Australia and Canada fall into a small group of countries with such procedures, although, as shown by Bergevin and Schwanen (2011), the respective regimes are quite dissimilar in their details. For example, Australia discloses undertakings made by investors whereas Canada does not. Moreover, under Australia's system, the onus is on the government to show why the investment is not in the national interest whereas, under Canada's system, the onus is on the investor to demonstrate net benefits.[17] Interestingly, the OECD considers Canada's overall regime to be more restrictive than Australia's but Australia's review mechanism to be more restrictive than Canada's (Bergevin and Schwanen, 2011; Figure 3).

Sensitive sectors in Australia are as follows:[18]

- media (daily newspapers, television and radio, including internet sites that broadcast or represent these forms of media);
- telecommunications;
- transport (including airports, port facilities, rail infrastructure, international and domestic aviation and shipping services provided within, or to or from, Australia);
- the supply of training or human resources, or the manufacture or supply of military goods or equipment or technology, to the Australian Defence Force or other defence forces;
- the manufacture or supply of goods, equipment or technology able to be used for a military purpose;
- the development, manufacture or supply of, or the provision of services relating to, encryption and security technologies and communications systems;
- the extraction of (or the holding of rights to extract) uranium or plutonium or the operation of nuclear facilities.

Australia's Foreign Investment Review Board (FIRB) screens investments in non-sensitive sectors above thresholds that are indexed annually; for 2012, the thresholds are AUD 244 million for Australian businesses and AUD 53 million in non-heritage developed commercial real estate. For US and New Zealand investors, the threshold for non-sensitive businesses is AUD 1,062 million.[19]

Canada reviews acquisitions above certain thresholds. For cultural businesses, these thresholds are set at $5 million and $50 million for direct and indirect acquisitions respectively;[20] these thresholds apply to all investors. For WTO members, the general threshold for review is expected to be set at CAD 330 million for 2012. The 2008 report by the Red Wilson Panel called for a higher general threshold of CAD 1 billion based on enterprise value (Competition Policy Review Panel, 2008). Corresponding amendments to the *Investment Canada Act* were announced in 2009,[21] although implementation is pending the revision of related regulations. When implemented, these amendments will raise the review threshold for WTO investors from the 2012 threshold of $330 million based on book value of assets to $600 million based on "enterprise value", and subsequently over the course of a phase-in period to $1 billion.

As part of the 2009 reforms, the list of "sensitive sectors" subject to lower review thresholds in Canada was reduced to only the cultural industry with the 2009 Investment Canada Act revision. However, the same revision added a new review process for investments that could be "injurious" to national security; this new measure would allow a review of investments in the specific sectors dropped from the Act (uranium processing, financial services and transportation services), but also of investments in other sectors. Under the national security provision, the federal Cabinet is authorized to take any measures that it considers advisable to protect national security, including the outright prohibition of a foreign investment in Canada. Moreover, financial services and transportation services remain subject to sector-specific regulatory regimes. In substance, there appears to be effective equivalence between the restrictiveness of the Canadian and Australian review processes.

Generally speaking, outside of the cultural sphere, Canada's review requirements have only a small impact in terms of process and a negligible impact substantively. Only 11.5% of the 14,418 acquisitions notified under the Investment Canada Act from 1985 through year-end 2011 were subject to review. Of the 1,657 non-culture sector reviews, only one proposal was disallowed.[22] Since 1999, the Minister of Canadian Heritage has reviewed and approved 98 cultural investments, while disallowing three proposals.

These procedures did, however, come into play once in the bilateral relationship, in respect of the proposed takeover by Australia's BHP Billiton of Potash Corporation of Saskatchewan. On 3 November 2010, Canada's Minister of Industry indicated that he was "not satisfied" that the proposed transaction would be of net benefit to Canada. BHP Billiton did not submit any additional undertakings and withdrew its application for review. The withdrawal meant that there was no final decision to be made by the Minister.[23]

In summation, there are few barriers facing Australian and Canadian companies seeking to invest in each other's economies and thus limited scope to enhance the relationship in this area. Both countries review sensitive investments, but as made clear by the infrequency of Canada's refusals to allow reviewed investments, the amount of investment actually deterred may be minimal. Canada and Australia currently apply similar thresholds for review of large investments to each other. However, this will change when Canada implements the commitment to raise the threshold for review of inward investment to $1 billion. Since Australia applies a similarly high threshold for New Zealand and US investors, a bilateral investment agreement that achieves MFN treatment for Canadian investors would be a desirable objective.

BILATERAL TAX AGREEMENT

A tax treaty has the dual role of avoiding double taxation when a resident of Canada becomes a resident of a partner country or vice versa, and of preventing tax evasion. Canada and Australia signed the "Avoidance of Double Taxation Convention and the Prevention of Fiscal Evasion with Respect to Taxes on Incomes" in 1980. This was updated and amended by a Protocol in 2002. Following amendments to the OECD model bilateral tax code in 2008, Australia and Canada opened a consultation process for negotiations towards a modernized tax treaty in December 2009 but negotiations have not yet been completed. Modernizing the agreement was listed by business as a welcome facilitating factor for bilateral commerce.

4.4. LABOUR MOBILITY

Canada and Australia both recognize the importance for their national economies of drawing on qualified foreign workers. Current programs include short-stay visa programs for business professionals; uncapped employer-sponsored temporary foreign worker programs for longer-term stays, the recently revised Temporary Foreign Worker Program (TFWP) in Canada and the 457 Visa employer-sponsored program in Australia; [24] and programs for youth working holiday programs. As well, both countries have well developed and recently modernized national programs to facilitate recognition of skills and qualifications acquired abroad. Accordingly, both are well placed to address issues related to temporary movement of skilled workers and professionals.

SHORT-TERM BUSINESS ENTRY

Canada has a general provision for business visitors who engage in international business activities in Canada (e.g., marketing, purchasing, providing after-sales services, or providing or receiving training, etc.) without directly entering the Canadian labour market. The test for the latter criterion is based on the primary source of remuneration for the business activities being from outside Canada; and the principal place of business and actual place of accrual of profits being predominately outside Canada. Canada has made narrower commitments under the GATS in this area for persons operating in specified services sectors. Australia has similar short-stay business visa (S456 visa which permits applicants to stay of up to three months at a time for purposes such as pursuing investment opportunities and attending to business interests and negotiations), and has made similar GATS commitments.

A facilitating development in this area is the APEC Business Travel Card (ABTC). This well-established scheme, launched in 1999, provides qualified persons with a multiple-entry, working-visa-free right of entry for stays of two to three months (depending on the economy) for business development in an APEC economy that is a full member of the program. Pre-clearance by participating economies is required; this results in waiting times ranging up to 3 months to acquire the card.

Qualification criteria also vary—and quite significantly. To give a sense of the possibilities, Singapore's criteria are very simple and appear to be available to a wide range of persons[25]:

- bona fide business persons (i.e., those who represent an economically-active business entity);
- members of professional bodies (e.g. doctors, lawyers, artists); and
- public officers from Ministries, Government departments, economic agencies and statutory boards who need to travel in their official capacity.

Australia's criteria, as revised in November 2011, by comparison, are quite detailed and laden with process.[26] To be eligible, the applicant must:

- Demonstrate frequent travel for business purposes (defined as a minimum of 4 business trips during the previous 12-month period) to another APEC economy, with verification through checks of movement records.
- Be either a CEO, board member, regional/country head or owner/director of a business entity or director of an Australian peak business association; or an employee nominated by one of the above people in their business entity (except a board member); contract employees are excluded.
- Be employed by an Australian-based peak business body or a registered business entity, which must establish that is engaged in international trade or investment with APEC member economies, either by being on the Forbes Global 2000 business list or other specified qualifying list, or, pursuant to arrangements still being put in place, certified by an "approved body" (which will be a set of business associations decided in the course of consultations).

Canada joined the ABTC program as a transitional member in November 2010 for a 3-year term. As a transitional member, Canada does not issue the card to Canadian businesspersons and still requires a valid passport and work visa for business persons from other APEC economies to travel and work in Canada; the transitional membership essentially goes no further than to provide access to special immigration clearance lanes at designated airports, an added perk of the system.[27] Canadian business organizations which focus on the Asia Pacific have strongly recommended that Canada participate fully. It remains to be seen as to how freely available the ABTC will be made to Canadians when the full program is implemented.

Given the apparent popularity of the card, full entry by Canada into the ABTC program, on relatively non-restrictive terms, should reduce the red tape for persons travelling on bilateral business development.

LONGER-TERM TEMPORARY FOREIGN WORKER PROGRAMS

Multinational corporations account for a disproportionately large share of global commerce. Such corporations routinely station personnel abroad as part of general career advancement for the individuals concerned and/or bring in workers from abroad to meet corporate needs. Both the Canadian TFWP and Australian S457 visa programs have been used with increasing intensity over the years for this purpose.

In Canada, the major use of these programs is for domestic firms to bring in foreign workers with particular skills in short domestic supply—this includes skilled workers or other temporary workers such as seasonal workers or live-in caregivers. The standard term is 4 years. Moreover, a labour market opinion (LMO) is required to ensure that the jobs could not be filled by Canadians. Two general exceptions are of interest – inter-company transferees and young people who work to support themselves while travelling.

Australian S.457 (Temporary Business) visas have general features similar to Canada's TFWP program. They permit 4-year stays and are generally subject to a labour market test (LMT). Australia's use of this visa to meet domestic labour market needs increased steeply in the 2000s, similar to Canada's experience.

INTRA-COMPANY TRANSFEREES

A small percentage of temporary foreign workers are transferees within multinational firms. For example, Canada admitted 192,281 temporary workers in 2008, of whom only 10,200 or 5.3% were intra-company transferees. The

comparable figures for 2007 were 8,200 of 165,198 or just under 5.0%. This percentage has, however, been steadily growing over the years: in 2000, the total number of intra-corporate transferees was just 1,634.

The provisions for intra-company transferees (ICTs) are subject to Canada's GATS commitments, and in some cases to relevant provisions in some of Canada's FTAs. These provisions are more accommodating than the general provisions governing other classes of temporary workers.[28] No labour market opinion is required; this applies to foreign nationals from any country. The length of stay is also longer—5 years for technical ("specialized knowledge") staff and 7 years for senior executives or managerial staff, although the initial work permit is issued for only 1 year. There is additional flexibility for transferees who move back and forth between their parent company and the Canadian operation. The Guidelines give an example of a specialized knowledge worker who works for two years for the Canadian entity, then is transferred to an Australian branch of the same company for two years; this worker would be eligible for consideration under the intra-company transferee provisions as a specialized worker for another full five-year period. A recent ruling by Citizenship and Immigration Canada allows documented time spent outside Canada during the duration of the work permit to be recaptured to allow the ICT five or seven full years of physical presence in Canada. On completion of a 5- or 7-year term, a 12-month stay abroad permits re-application. In terms of application requirements, detailed evidence must be presented to establish the eligibility of the application for ICT treatment; moreover, the foreign national employee must be able to transfer back to the foreign company at the end of their assignment in Canada.

Australia's GATS commitments also waive the labour market test in the S457 visa for intra-company transfers of executives, managers and "specialists". The term however remains for four years, the same as for other categories in this visa class (although an extension to six years for applicants sponsored by qualified Australian-based employers has been recently announced). Statistics on the share of Australia's S457 inflows accounted for by intra-company transferees are not available. However, based on the data available for other OECD countries, the share is likely to be similar to Canada's.

Australia also has an interesting provision to facilitate temporary or permanent entry specifically for companies establishing a regional headquarters in Australia.

YOUTH LABOUR MOBILITY

Both Australia and Canada have programs to facilitate travel and cultural exchange by young people by providing for temporary work permits to supplement their financial resources while travelling.

Australia has two closely related mechanisms with slightly different features under the Working Holiday Maker Programme[29]: the *Australian Working Holiday Visa* and the *Australian Work and Holiday Visa*. Australia has reciprocal arrangements with 28 partner countries. The agreement with Canada falls into the former, less restrictive category.

The comparable Canadian program is the recently renamed *International Experience Canada*, under which Canada has reciprocal arrangements with 31 partner countries. *International Experience Canada* has separate programs for working holidays, young professionals and internships. The terms and conditions vary by country. Some allow participation up to age 29, some to 30, and others to 35; some programs are subject to per-country quotas while others are not; some require payment of fees while others do not; and some require the demonstration of a stipulated amount of funds in a bank account, although again the amount and conditions vary. Additional requirements cover such as issues as bona fides (e.g., no criminal record), and health insurance. Medical certification is required to work in particular fields.[30]

A Memorandum of Understanding to facilitate mutual use of the programs by young Australians and Canadians was signed by the governments of Australia and Canada in 2007.[31] There are numerous differences in conditions. For example, Australia requires that Canadian youth have "good health"; by contrast, Canada applies a more onerous requirement that Australian youth purchase comprehensive health insurance for the duration of their stay and purchase additional work insurance while in Canada. Canada extends the term of stay to Australian youth to 24 months on a "trial basis". Australia limits the stay of Canadian youth to 12 months, unless they undertake specified rural work in which case they can reapply.

QUALIFICATIONS RECOGNITION

Both Australia and Canada have federal structures in which sub-national levels of government (States/Territories and Provinces/Territories respectively) have jurisdiction over professional qualifications. Both countries have entered into agreements on internal mobility that provide for mutual recognition of qualifications internally across a broad spectrum of occupations.[32] Moreover, both countries have been active in facilitating the recognition of foreign credentials in order to meet increasingly sophisticated and varied domestic labour market requirements. While the main objective of these programs is to better integrate permanent immigrants into the domestic workforce, an issue that is not within the scope of the present study, progress in this regard also facilitates the recognition of qualifications of temporary foreign workers, an issue that is widely seen as increasing in importance.

In Australia, Australian Education International (AEI), through the National Office of Overseas Skills Recognition (AEI-NOOSR), is the official body providing information and advice on the comparability of overseas qualifications with Australian qualifications, using the Australian Qualifications Framework (AQF) [33], which provides for internal consistency in qualification recognition across Australian jurisdictions, as a benchmark. Meanwhile, in Canada, the Federal Government has established a Foreign Credential Recognition Program through which it works with provincial/territorial governments, licensing and regulatory bodies, sector councils, employers and other groups to improve the integration of internationally trained immigrants into the work force by accelerating the assessment and recognition of foreign credentials. [34]

Australia and Canada have entered into several mutual recognition agreements in respect of professional qualifications:

- Management accounting: CMA Canada and CPA Australia entered into an MRA in April 2008, establishing guidelines for qualified members to gain reciprocal membership. This agreement enhances mobility within the management accounting profession.[35]
- General accounting: CGA Canada and CPA Australia also entered into an MRA at the same time with a similar aim for the general accounting professionals.[36]
- Engineering services: Engineers Australia and Engineers Canada entered into an MRA in October 2007 for mutual recognition of Registered/Licensed Engineers.[37]

However, both countries have gone with further with other partners. Australia's internal agreement was extended to New Zealand in the Trans-Tasman Mutual Recognition Arrangement (TTMRA) which committed all jurisdictions to recognise each other's licensing and registration requirements for the sale of goods and provision of services.[38] The expectation is that the arrangement will eventually be extended to other economies, including South Pacific and APEC partners. The Australia-United States Free Trade Agreement (AUSFTA), which came into force in 2005, included broad commitments to enhance bilateral cooperation in particular areas. The Professional Services Working Group, established under the AUSFTA has focussed on accounting, engineering and legal services but is open to other groups. Future agreements under the AUSFTA may also have an impact on the movement of

registered persons working in occupations that also fall under the TTMRA. Notably, the Australian Law Council has recently entered into a Memorandum of Understanding (which is not an MRA and is limited to friendly exchange of information and contact) with the California Bar. This is one of 16 such Australian MOUs; Canada is not on the list.

One Canadian province, Québec, has also gone considerably further in reaching an MRA with France, *Entente en matière de reconnaissance mutuelle des qualifications professionnelles*, signed in October 2008, covering 25 professions and over 40 trades.[39]

As well, the British Columbia College of Applied Biology has entered into an MRA with the UK's Society of Biology which provides College members in the Registered Professional Biologist category the ability to become registered as a Chartered Biologist with the Society on the strength of their College registration and vice versa.[40]

Finally, the Australian and Canadian architectural associations are parties to the Canberra Accord, an agreement which recognizes the substantial equivalency of accreditation/validation systems in architectural education of the signatories (which also include the architectural associations of the United States, the British Commonwealth, China, Korea and Mexico). The recognition of "substantial equivalency" of systems; it does not address matters related to accreditation of individuals for professional registration or licensure.

POTENTIAL TO ENHANCE LABOUR MOBILITY

In the framework of their general provisions governing short-term business visitors and medium-term temporary movement of foreign workers under the intra-company transfer provision or youth working holiday programs, there is some scope for either government to facilitate labour mobility.

- Australia could match Canada's longer terms for intra-company transferees.
- Canada's full entry into the APEC Business Travel Card program would be a valuable facilitating measure for Canadian and Australian short-term business visitors.
- Both countries could update the MOU on youth mobility by matching the most favourable terms and conditions applied by the other.

As regards mutual recognition of qualifications between professions in Canada and Australia, at the *Australia-Canada Roundtable on Foreign Qualification Recognition* held in Melbourne in 2011, stakeholders from Australia and Canada assessed progress. [41] Regulatory bodies were seen as having played the lead role in new developments in areas such as engineering, medicine, dentistry, physiotherapy, and accounting. The Report concludes, however, "To date, a trend toward 'skewed reciprocity' has been defined, with Australia facilitating immediate access to practice for Canadian-qualified professionals in a number of fields. There is clear potential to establish mutual arrangements in the future given the number of Australians working temporarily in Canada, as well as Canadian students qualified in the Australian tertiary system." (Public Policy Forum, 2011; at 10). This expert view can only be endorsed. This is also an area which business has identified where bilateral commerce could be facilitated.

4.5. GOVERNMENT PROCUREMENT

Canada is one of 15 parties[42] to the plurilateral WTO Agreement on Government Procurement (GPA); Australia, however, is not a member. A complete revision to the GPA, which has been negotiated as part of the "built-in agenda" agreed in the Uruguay Round, is expected to be signed in 2012. This revision, *inter alia*, modernizes the

GPA to address new issues such as use of electronic commerce tools in procurement, provides additional flexibility in certain rules (e.g., shorter time-periods for procuring generally available commercially available goods and services), clarifies the special and differential measures for developing countries, expedites entry negotiations, revises the rules governing domestic review procedures for supplier challenges, and also extends the coverage of members' procurement commitments, mainly to include sub-national government and governmental bodies, services and other areas of public procurement.[43]

In the revised GPA, Canada extends to other GPA members the same commitments it has made in respect of provincial and territorial commitments under the Canada-United States Government Procurement Agreement as well as its NAFTA procurement commitments in respect of federal crown corporations. Canada does not, however, make commitments in respect of municipalities, school boards, academic institutions and hospitals.[44]

In addition to the GPA with the United States and the NAFTA provisions, Canada has included chapters on government procurement in its FTAs with Chile[45], Colombia, the European Free Trade Area (EFTA),[46] Panama (including the Panama Canal Authority), and Peru. Canada also has launched talks to modernize the FTA with Costa Rica and has established a consultations process to expand the Canada-Israel FTA; in both cases, Canada has signaled its intention to include a government procurement chapter.

Australia's Commonwealth Procurement Guidelines are generally based on the principle of "value for money" and stipulate that procurement methods must not discriminate against potential suppliers due to their degree of foreign affiliation or ownership, location or size. Specific measures to ensure non-discrimination against SMEs are, however, limited to Australian and New Zealand firms (with SMEs defined as companies with employment under 200).[47]

Australia has also agreed to government procurement provisions in several of its FTAs. The FTA with New Zealand appears to be the most comprehensive: New Zealand is for all intents and purposes treated as part of Australia for government procurement purposes and vice versa (Murphy, 2010). The agreements with Chile and the United States cover sub-national governmental bodies.[48]

Accordingly, government procurement is an area where Australia and Canada grant each other less than MFN treatment and where room exists to deepen bilateral commerce.

4.6. COMPETITION POLICY

The role of competition policy in facilitating international trade has long been recognized given the potential for private anti-competitive practices to undermine market access negotiated at the state level. The massive expansion of foreign direct investment has also made international cooperation on mergers increasingly important.

At the multilateral level, competition policy was included in the work program of the WTO for a brief period as one of the four "Singapore Issues", adopted at the 1996 WTO Ministerial in Singapore, was subsequently included as part of the Doha Development Agenda work program in 2001, and was dropped from the program pursuant to a 2004 decision of the WTO General Council. The issues addressed in the WTO work program included core principles in the application of competition laws (transparency, non-discrimination and procedural fairness), formal (so-called "hard-core") cartels, modalities for voluntary cooperation, and capacity building for developing countries. While no multilateral agreement emerged from this work, the initiative did serve to thoroughly air the issues, including by stimulating a significant body of literature (see e.g., Clarke and Evenett, 2003 and Drexl, 2004). While the WTO work program has ended, a second multilateral process launched in 2001, the International

Competition Network (ICN), continues to address global antitrust concerns through policy coordination.[49] The ICN, which counts Australian and Canadian competition authorities as members, held its tenth Annual Meeting of the ICN in The Hague, 18-20 May 2011 and maintains an extensive work program on competition issues which encompasses the international dimension.

At the regional level, APEC has adopted the *APEC Principles to Enhance Competition and Regulatory Reform* and maintains an ongoing work program on competition policy which is presently conducted within the Competition Policy and Law Group (CPLG) of the APEC Economic Committee. The CPLG meets annually; its most recent meeting was held in March 2011 in Washington DC.

The OECD also maintains a very active work program in the area of competition policy which covers the international dimension. For example, the agenda of the 2012 Global Forum on Competition to be held 16-17 February in Paris includes *Improving International Co-Operation in Cartel Investigations* (with written contributions from both Australia and Canada); the background note developed by the OECD Secretariat provides an up-to-date review of developments in respect of horizontal, vertical and export cartels, abuse of dominance and mergers (OECD, 2012).

Finally, many countries have entered into competition policy cooperation agreements, in some cases as chapters included in trade agreements. Such agreements typically cover issues such as: notification of cases by one party that concern important interests of the other party; exchange of information relating to the implementation of the competition rules; cooperation and coordination of antitrust actions; and comity undertakings pursuant to which the parties commit to take into account the important interests of the other party when they take measures to enforce competition rules ("traditional comity") and/or provisions to allow a party to invite the other party to address anti-competitive behaviour implemented on its territory which affects the important interests of the requesting party ("positive comity"). Australia and Canada routinely include competition chapters in their FTAs.

Finally, the Australian and Canadian competition authorities have also exchanged senior staff on a regular basis and developed informal agreements for the exchange of non-confidential information on competition and consumer protection issues (Cassidy, 2001). Accordingly, there is a well-established level of cooperation between the two countries.

The absence of a full-fledged international competition regime is generally argued as justifying certain departures from free trade allowed under GATT rules, most notably antidumping policies. Indeed, antidumping evolved historically as the international trade analogue of antitrust policies.[50] Exemplifying this conceptual parallel, antidumping has been replaced by competition laws within the EU's internal market, in the EFTA-Singapore and EFTA-Chile FTAs, in the Australia-New Zealand Closer Economic Cooperation Agreement and in the Canada-Chile Free Trade Agreement (Ahn, 2009; Table 8.3). A proposal to replace antidumping with competition law was also made by Canada, unsuccessfully, during the negotiations for the Canada-US Free Trade Agreement (Dutz 1998: 100).

However, in modern practice, antidumping is rarely applied in contexts in which predatory tactics are likely to be successful (for detailed analysis of EU practice in this regard see Bourgeois and Messerlin 1998; similar evaluations for the US and Canada respectively are provided by Shin 1998 and Hutton and Trebilcock 1990). Stiglitz (1997) concludes that antidumping is primarily used in lieu of safeguards to deal with import surges because its design makes it more attractive to both governments and industry than the safeguards instrument.

At the same time, antidumping has been found to have a "chilling" effect on trade (Vandenbussche and Zanardi, 2010). As well, the procedural requirements under antidumping law for complainants to demonstrate sufficient support for a petition to have standing can actually promote collusive, anti-competitive behaviour.[51]

In light of these considerations, and given the well-developed relationship between the Australian and Canadian competition authorities, the replacement of antidumping with competition policy measures in the bilateral relationship appears to be eminently feasible. Since antidumping investigations in respect of Australia-Canada bilateral trade are rare, the effect would be modest: only eight investigations were initiated in the last two decades, seven by Australia and one by Canada, resulting in duties being applied in four cases, one of which is still in effect[52]. However, this would be a step in direction of providing a seamless operating environment for bilateral business.

4.7. SUMMARY AND RECOMMENDATIONS

The Canada-Australia commercial relationship is solid and, in a global perspective, relatively friction-free. Two-way trade in goods and services, taking into account sales of foreign affiliates, is likely on the order of US$ 64 billion, well balanced, and growing briskly, particularly through affiliate sales driven by strong two-way investment flows. Available data show that the number of companies engaged in two-way trade has grown substantially. An indicator of growing business interest is the recent establishment of the Australia-Canada Economic Leadership Forum in 2010.

Working within the established institutional framework for the bilateral relationship, a number of areas can be identified where policy adjustments could enhance the relationship. For the most part, these can be considered "low-hanging fruit". These moves would enhance the relationship while entailing low negotiating and adjustment costs. On this basis, Canada and Australia should:

1. Eliminate tariffs on bilateral trade, accommodating Australia's dairy interests through an expanded quota.
2. Update the bilateral air services agreement with a high level of ambition in terms of the "freedoms" of competition covered.
3. Enter into a bilateral investment agreement that achieves MFN treatment for Canadian and Australian investors in terms of the level of investment subject to policy review.
4. Conclude the negotiations to modernize the bilateral tax treaty to bring it fully up-to-date and, to the extent appropriate, aligned with the updated model OECD code.
5. Enter into a labour mobility agreement that offers each other the best terms currently on offer by either on a bilateral basis for intra-company transfers and youth working holiday programs.
6. Enter into a government procurement agreement that provides each party MFN treatment.
7. Suspend the operation of antidumping law in the bilateral relationship, relying on competition law to address competition-distorting practices.

In addition, Canada should, unilaterally:

8. Review the process for recognition of qualifications acquired in Australia by Canadian jurisdictions to remedy the apparent "skewed" nature of reciprocity in this area.
9. Expedite its full participation in the APEC Business Travel Card program.

These measures would provide a tangible boost to the bilateral relationship. Realistically evaluated, however, they would not be in any sense "game changers" for either economy. Is it possible to think more ambitiously about this relationship? This question is taken up next.

5. A BOLDER VISION

Similarity and distance have their disadvantages in commercial relations, but also certain advantages.

In particular, similarity in size and wealth, as well as in socio-economic characteristics and governance systems, can serve as a natural replacement for many of the controls that nations put in place at their borders to prevent exploitation of major *differences* in these regards—of different levels of wages, of social security benefits, and of regulatory safeguards. Meanwhile, distance serves to minimize incentives to exploit marginal differences in border costs (e.g., by re-routing third party trade through the bilateral Canada-Australia channel).

The many similarities between Canada and Australia, both in current circumstances but also in historical evolution, have made them a staple for comparative studies.[53] Thus there is both a depth and breadth of mutual understanding of each other's economy and society. Inter-agency contact is routine between the Canadian and Australian governments. In consular affairs, both countries already extend services to each other's citizens in many third countries.

Is it possible to leverage these similarities, and if so how?

The framework for such a thought experiment is provided by the basic features of the deepest economic integration experiment involving modern industrialized economies in practice, namely the Eurozone, an arrangement which provides for the "four freedoms" of free circulation of goods, services, capital and labour.

The "how" is suggested by the approach taken by the Australian Customs and Border Protection Agency with regard to supply chain security: the Agency has signaled its interest in exploring low-cost risk-based while rejecting formal participation in the World Customs Organization Authorized Economic Operator program because the value proposition was not there for Australian business.

Accordingly, the thought experiment may be concretized as follows: are there low-cost, informal measures that Canada and Australia could contemplate that would move the relationship in the direction of the four freedoms and would allow realization of the major part of the benefits without incurring the governance costs associated with formal arrangements?

Canada has announced its intention to enter into the Trans-Pacific Partnership negotiations; if realized, this entry would provide the opportunity and framework. Some ideas are sketched out below to serve as the basis for a discussion. There are possibilities that Canada and Australia can contemplate on the basis of a handshake (i.e., a memorandum of understanding) that differences in scale and quality would make problematic with other partners.

5.1. EFFECTIVELY FREE CIRCULATION OF GOODS

Tariff elimination has the potential to expand bilateral Canada-Australia merchandise trade by about one-sixth on the basis of the analysis above. However, firms must document their supply chains to demonstrate that their products meet the rules of origin (ROOs) that allow access to the preferences. In some cases they must also obtain certification under local standards even after having met home market standards. Both procedural requirements represent fixed costs to market entry. Restrictive ROOs can to make tariff preferences worthless; minor differences in standards can act as prohibitive tariffs and cause firms to abandon markets.

Preferential ROOs are agreement- and product-specific; restrictiveness varies in both dimensions – i.e., across agreements and across products. There is no requirement for standard treatment, opening up the possibility for a

relaxed treatment in bilateral Canada-Australia trade. Even restrictive ROOs allow goods with considerable amounts of imported intermediate inputs to qualify for tariff preferences. Moreover, given modern-day use of value chains for input processing, it is quite conceivable that ROOs would allow access to tariff preferences for goods with less total domestic value than other goods that are disqualified, simply by virtue of the particular international processing path an input had taken en route to being incorporated in a product traded between Australia and Canada. Transportation distances and similarity of border and domestic production costs reduce the appeal of using Canada and Australia as production bases solely for purposes of circumvention of trade barriers against third parties, especially in a generally low MFN tariff environment. In short, it is questionable what value ROOs actually serve in the modern trading environment for Canada-Australia trade. Is it thinkable to allow goods to qualify for mutual preferential access simply on the basis that they can legitimately claim under the respective domestic laws to be "Made in Australia" or "Made in Canada"?

As regards standards, Canada and Australia both set high standards for goods to be placed on their own domestic markets and have both dealt with the issues faced in establishing internal markets in a federal framework. Moreover, markets play an important role. Firms purchasing production inputs must ascertain for themselves whether the goods in question meet their specifications. And commercial importers purchasing goods for consumer markets need to select goods that will meet retailers' acceptance. Accordingly, this appears to be a case where leaving the decision to the buyers might work just as well as imposing regulatory requirements for certification. Those goods subject to quarantine regulation or for which standards are markedly different can be specified, allowing others goods placed on the Australian market to be sold in Canada and vice versa. Given these considerations, is it thinkable to adopt a negative list approach to standards?

Finally, the evolution of customs procedures, in particular the development of the concept of "authorized economic operators", provides a basis for implementation of a relaxed regime. Canada fully participates in the World Customs Organization Authorized Economic Operator program to ensure security of supply chains for trading firms. Australia has conducted a pilot project and concluded the value proposition is not there for its firms; however, it has signaled its willingness to consider lower-cost approaches: "… we see further exploration on improving risk management through identification of low risk traders and transactions without the high costs of a formal AEO accreditation regime as a more immediate priority." (Australian Customs and Border Protection Service, 2009). What better partnership in which to consider exploring such an option than that between Australia and Canada?

The suspension of antidumping in bilateral trade would represent a complementary step; however, the anti-circumvention mechanisms in the national antidumping laws could still be kept to deal with cases where high or prohibitive tariffs on third parties create sufficient incentives.

5.2. EFFECTIVELY FREE MOVEMENT OF SERVICES

The most important elements for freedom of movement of services—the right of establishment—is already effectively in place. Cross-border business services such as might be provided on a contract basis over the Internet were never subject to regulation and hence are also effectively open. In this regard, as has been noted by a number of observers, the most important outcome of the Doha Round for cross-border services trade would have been to lock-in the existing liberal trading conditions. To go much further is difficult, as the European Union's experience has shown. The discrete measures identified in section 4 would simply round out the package: effective reciprocity by Canada to Australia's ready acceptance of Canadian qualifications, national treatment in government procurement and a blue skies agreement with the maximum "freedoms".

5.3. EFFECTIVELY FREE MOVEMENT OF CAPITAL

Free movement of capital is already effectively in place for almost all intents and purposes. The BHP Billiton-Potash event ("fiasco", in the words of a senior Canadian observer) was the unfortunate exception that proves the rule of no problems; the promised clarification of the guidelines for administration of the Investment Canada Act should make even more remote the possibility of another such incident. The recommendation made in section 4 above for MFN treatment by the Australian government for Canadian investments in terms of the review threshold, once the Canadian government raises its review threshold when the necessary regulations are in place, would be a minor boost. Other issues such as investor-state dispute settlement, which the Australian government has rejected for future trade agreements, and/or expanding intellectual property rights, an issue on which neither Australia nor Canada would have particular reasons to expend energy in the bilateral relationship, are neither here nor there in terms of impact.

5.4. EFFECTIVELY FREE MOVEMENT OF LABOUR

On labour mobility, Canada and Australia might well reflect on whether it would have ever occurred to either to put in place the wide range of rules and guidelines designed to restrict access to domestic labour markets, if the only movement of people for economic reasons observed was between these two states. In the likely event that the answer to this rhetorical question would be "no", both governments, safe in the knowledge that people are not moving because of massive wage or social security differentials, could waive the detailed controls on labour movement and replace them with the "good hospitality" policy that both countries normally apply to each other's citizens in all other matters. To make this truly effective, Canada's internal inter-provincial and Australia's internal inter-state agreements on recognition of qualifications could be extended to each other's sub-national jurisdictions through the familiar processes that both countries have put in place for internal market purposes.

For companies doing business bilaterally, the removal of all red tape for business visits or for intra-company transfers of staff would provide a seamless operating environment. For both labour markets, job-mismatch unemployment could be reduced. For young travellers working to supplement their resources, the experience of each other's country would come without procedural costs.

5.5. AN INFORMAL CLOSER ECONOMIC RELATIONSHIP

Consistency of treatment is a vital aspect of international rules for market access. It is central to the WTO principles of national treatment and most-favoured-nation, as well as to the requirement for scientific risk analysis for SPS rules and perhaps others. However, it is possible to distinguish between a meritorious consistency and a foolish consistency, as Ralph Waldo Emerson did in his often quoted observation on the subject.

Many aspects of Canada-Australia commercial relations are multilateral in nature. Here, there is no question concerning the importance of consistency of treatment. Many aspects are, however, intensely bilateral. In these areas, one may define a foolish consistency as being to apply rules devised for other relationships that raise costs for bilateral Australia-Canada commerce without any attendant benefits. One can think of these as rules that would never have occurred to governments to put in place were these the only two countries to which the rules would apply.

Can informal arrangements based on a handshake with a likeminded partner facilitate bilateral commerce? Arguably Canada and Australia are better placed than perhaps any other two economies to try such an experiment.

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[1] So referred to by Cooper, Higgott and Nossal (1993; ix).

[2] Australia is the furthest market from Canada going by distance between capitals. It is second-furthest taking into account the regional distribution of economic activity within each country. These distance evaluations are based on data from the Centre d'Etudes Prospectives et d'Informations Internationales (CEPII) distance database. Indonesia and Mauritius rank as the furthest markets from Canada under alternative measures of distance.

[3] The large number is somewhat deceptive; European markets are further from Australia than is Canada as are North African and Caribbean markets; however, the differences in distance are often quite small.

[4] This section is drawn with little change from Ciuriak (2012).

[5] All values in this study are expressed in US dollars, as a neutral currency. Since the Canadian and Australian dollars have been close to parity with the US dollar at market values in recent years, the equivalent values expressed in the latter currencies would be little different.

[6] See, Austrade media release, "Austrade outlines strategies for export success in Canada," Monday, 5 May 2008; http://www.austrade.gov.au/Austrade-outlines-strategies-for-export-success-in-Canada/default.aspx

[7] John Short Larke, was dispatched to Australia in 1895 with instructions: "to collect information both on the general trading requirements in Australia and specific trade opportunities" and "to promote trade between Canada and Australia in every possible way". In addition to successful efforts promoting the expansion of trade, Larke was instrumental in the laying of the Pacific cable to improve communications between the two countries. See Canadian High Commission (2009) *Canada in Australia.*

[8] According to the Australian tariff schedule for 2011, Australia provides preferences to Canada on 504 tariff lines, almost all of them in respect of MFN tariffs equal to 5% (the simple average of the tariff preferences is 4.8%). The Canadian trade policy review does not report on the CANATA preferences accorded Australia.

[9] China, Gulf Cooperation Council (GCC), India, Japan, Korea, Malaysia and Indonesia (which are also part of the ASEAN group), Pacific islands (PACER), and the Trans-Pacific Partnership Agreement (TPP; the current group includes Brunei, Chile, Malaysia, New Zealand, Peru, Singapore, the United States and Vietnam).

[10] Honduras, Panama, Jordan, the Caribbean Community (CARICOM), the European Union, India, Morocco, and the Ukraine. Canada also has initiatives under way to modernize the FTAs with Costa Rica and Israel; and has held exploratory discussions regarding an FTA with Turkey. Several other Canadian negotiations have stalled and appear to be moribund: Andean Community, Central America Four, Dominican Republic, Korea, Singapore, and the Free Trade Area of the Americas (FTAA).

[11] The UNCTAD data base on international investment agreements (IIAs) lists 14,710 IIAs from one side of such agreements, implying 7,355 on a bilateral basis. Of these, 2,820 are BITs, 2,972 are DTTs, and 1,565 fall into the "other" category.

[12] Canada and Australia signed the "Avoidance of Double Taxation Convention and the Prevention of Fiscal Evasion with Respect to Taxes on Incomes" in 1980. This was updated and amended by a Protocol in 2002. Following amendments to the OECD model bilateral tax code in 2008, Australia and Canada opened a consultation process for negotiations towards a modernized tax treaty in December 2009 but negotiations have not yet been completed.

[13] See "Australian-Canadian Scholarships & Funding," and "Canadian Funding Opportunities For Collaborative Research Between Canada And Australia," High Commission of Canada, Canberra Australia. Papers prepared for the Australia-Canada Universities Meeting on International Collaboration at the Association of International Education Administrators Conference, San Francisco, 21 February 2011. Available online at Australian High Commission, Partnerships and Scholarships http://www.canada.embassy.gov.au/otwa/educationpartnerships.html.

[14] Ibid.

[15] Agriculture and Agri-Food Market Access Report 2010–2011. Re-opening – Maintaining – Expanding Markets

[16] For example, the AUSFTA established a Committee on Sanitary and Phytosanitary Matters with provision for annual meetings and as well mandated the establishment of a Standing Technical Working Group to resolve specific bilateral animal and plant health matters with a view to facilitating trade and to consult on new measures that might affect trade.

[17] See Bergevin and Schwanen (2011; Table 1) for a detailed comparison.

[18] Source: Foreign Investment Review Board. Definitions. http://www.firb.gov.au/content/definitions.asp.

[19] Source: Foreign Investment Review Board. Monetary Thresholds. http://www.firb.gov.au/content/monetary_thresholds/monetary_thresholds.asp

[20] These lower thresholds also applied to several other industries

[21] Bill C-10, An Act to implement certain provisions of the budget tabled in Parliament on January 27, 2009 and related fiscal measures, 2d Sess., 40th Parl., 2009 (assented to 12 March 2009).

[22] See Fasken Martineau bulletin "Investment Canada's First Disallowance – Perfect Storm or a Change in Wind Direction?" http://www.fasken.com/en/antitrust_competition_and_marketing_bulletin_may2008/. The target in this takeover was MacDonald Dettwiler's space business which raised issues in respect of control of the Canadian firm's Radarsat 2, a Canadian government-financed remote sensing satellite that allows observation of Canada's Arctic.

[23] The incident prompted some debate in Canada's House of Commons. As reported by Fasken Martineau (2011), "… the House of Commons Standing Committee on Industry, Science and Technology (the "Industry Committee") undertook to review the Investment Canada Act in light of the concerns raised by the review of the BHP bid for

Potash Corp. Matters discussed at the Industry Committee included, among other things, whether transparency in the Minister's decision-making process should be enhanced; whether some or all of the undertakings given to the Government by an investor should be publicly disclosed; and, the efficacy of the "net benefit to Canada" standard and related enforcement. The election curtailed the Industry Committee's review of the Act and it remains to be seen whether the reconstituted Industry Committee will continue a review of the Act." The new Industry Committee has not yet, however, grasped this thorny issue.

[24] As regards Canada's TFWP, effective April 1, 2011, new disciplines were added to ensure the genuineness assessment of a job offer under the program. Employers can be deemed ineligible if, during the two years preceding a labour market opinion application, it is found that they have not provided wages, working conditions or an occupation to a temporary worker that were substantially the same as those in the job offer, and for which a reasonable justification has not been provided. If an employer is found to have failed the latter assessment, access to the TFWP may be denied for two years. Further, a maximum cumulative duration of four years of work for most temporary foreign workers is now imposed, followed by a period of four years in which the worker would not be eligible to work in Canada. For information and conditions of access to Canada's TFWP see: http://www.hrsdc.gc.ca/eng/workplaceskills/foreign_workers/index.shtml. For information and conditions of access to Australia's 457 Visa for employer-sponsored extended entry by skilled workers see http://www.immi.gov.au/skilled/skilled-workers/sbs/.

[25] See, Singapore Immigration and Checkpoints Authority, APEC Business Travel Card, http://www.ica.gov.sg/page.aspx?pageid=148

[26] Australian Government, Department of Immigration and Citizenship, APEC Business Travel Card Eligibility, http://www.immi.gov.au/skilled/business/apec/eligibility.htm#a

[27] Until the ABTC program is fully in place in Canada, Canadian citizens who conduct regular business in the APEC region can apply for membership in the NEXUS or CANPASS Air programs which provide expedited border clearance procedures for low-risk, pre-approved member travelers. See Canada Border Services Agency website, at http://www.cbsa-asfc.gc.ca/media/facts-faits/064-eng.html.

[28] See FW 1 Temporary Foreign Worker Guidelines, section 5.31. The criteria under Canada's GATS commitments are essentially the same as the general criteria; immigration officers are instructed to process applications from GATS Members under the general criteria rather than the more specific GATS criteria for transparency and consistency. The FTA provisions are generally similar to those in the GATS.

[29] The "Work and Holiday" program has caps on the number of visas granted annually and additional eligibility requirements.

[30] A medical exam is required if the applicant wishes to work in child care, teaching, or health care or has recently resided in specified countries.

[31] See Memorandum of Understanding between the Government of Canada and the Government of Australia Concerning Youth Mobility, signed in Canberra, 10 September 2007. The MOU came into force on 1 January 2008.

[32] In Australia, *the Intergovernmental Agreement on Mutual Recognition*, entered into in 1992 by the Commonwealth and the States and Territories, provides that people who work in a registered occupation in one jurisdiction can freely enter an equivalent occupation in other jurisdictions. The MRA covers all occupations that require an individual to have some form of legal registration to practice that occupation. The MRA does not affect any laws or regulations concerning the way in which the occupation is conducted, only the eligibility of the person to legally practice that occupation. In Canada, Chapter 7 of the *Agreement on Internal Trade* (AIT), which entered into force 1 January 1995, has a similar purpose. By 2001, agreements had been reached in respect of most of the 51 professions subject to regulation in more than one Canadian jurisdiction. As well, the Red Seal program provides similar recognition of qualifications in the trades (e.g., machinists or millwrights). In 2009, all governments approved amendments to Chapter 7 of the Agreement to achieve full labour mobility for workers in regulated professions and regulated trades. Importantly, recognition of foreign qualifications in one Canadian jurisdiction requires that other Canadian jurisdictions accept that licensing decision. Thus, internationally-trained individuals who obtain certification in one province or territory cannot be treated any differently for certification purposes than a domestically-trained worker. See Forum of Labour Ministers (2009).

[33] The Australian Qualifications Framework, first established in 1995, was modernized in 2011. See Australian Qualifications Council (2011).

[34] See Human Resources and Skills Development Canada. 2011. *Skills for the 21st Century*, Backgrounder, Foreign Credential Recognition Program; http://www.hrsdc.gc.ca/eng/workplaceskills/credential_recognition/transf/backgrounder_fcr.pdf

[35] See: http://www.cpaaustralia.com.au/cps/rde/xchg/cpa-site/hs.xsl/careers-work-mutual-agreement-cma-canada.html

[36] See CGA Press Release, "Alliance Extends CGA-Canada's Global Reach," at http://www.cga-canada.org/en-ca/MediaCentre/MediaReleases/2008/Pages/ca_mdr_2008-04-08.aspx

[37] See, Engineers Canada, International Mobility, at http://engineerscanada.ca/e/files/MRA_engineers_australia.pdf

[38] Prior to the Trans-Tasman agreement, labour mobility was governed by the Australia-New Zealand Closer Economic Relations Trade Agreement (CER). The CER did not originally address the movement of people but the 1998 Trade in Services Protocol which amended the CER encouraged the two states to try and avoid licensing and certification requirement impediments to trade.

[39] Gouvernement du Québec, Entente France-Québec sur la reconnaissance mutuelle des qualifications professionnelles, http://www.immigration-quebec.gouv.qc.ca/fr/biq/paris/entente-france-quebec/

[40] British Columbia College of Applied Biology, *Mutual Recognition Agreement with Society of Biology,* https://www.cab-bc.org/mutual-recognition-agreement-society-biology

[41] See Public Policy Forum (2011).

[42] The European Union covers all 27 EU Member States and thus the GPA covers 42 WTO Members.

[43] The value of the new commitments in market access terms has been provisionally estimated by the WTO Secretariat as in the range of $80-100 billion annually, rising to $450 billion with the accession of the 8 parties currently negotiating access (which includes China).

[44] See "Canada Welcomes WTO Government Procurement Deal," posted December 19, 2011 by the Minister of International Trade and Minister for the Asia-Pacific Gateway, Ed Fast.

[45] The original FTA did not include a chapter on government procurement; however, this was built into the agreement in 2006 (Dymond, 2007), along with a financial services chapter.

[46] The procurement chapter in the EFTA simply follows the WTO GPA; since all EFTA members are parties to the WTO GPA, the value added is essentially nil.

[47] See Commonwealth Procurement Guidelines - December 2008; footnote 7.

[48] The Australia-Thailand FTA also commits Australia to participation in a working group on government procurement issues.

[49] See Bode and Budzinski (2005) for a discussion of the comparative advantages of the WTO and ICN processes.

[50] For example, the first AD law, which was introduced in Canada in 1904, was motivated by concerns over predation (see Finger 1992 for an account). New Zealand which followed Canada in adopting antidumping legislation in 1905, targeted selective price cutting by US-based International Harvester which threatened to create a monopoly on agricultural equipment in the New Zealand market (Ciuriak 2005). Similarly, the US Antidumping Act of 1916 was an extension of its antitrust law (Finger 1992). Viner (1923) provided the first formal articulation of antidumping as the international analogue to domestic competition policy. However, the close parallels between antidumping and competition policy quickly lapsed; As Finger (1992: 129) notes: "The 1921 act completes the shift of criteria. Any mention of antitrust criteria – conspiracy, combination, or restraint of competition – is gone. Antitrust's injury-to-competition standard has been replaced by a diversion-of-business standard."

[51] Blonigen and Prusa (2003) point to the high rate of withdrawal of petitions (about 25% were withdrawn over the period 1980-1998) as possible evidence of collusion in a US context. Zanardi (2004) provides indirect evidence that cases where petitions are withdrawn tend to involve industries where coordination costs are lower, adding suspicion to the possibility that antidumping law has abetted cartelization. Messerlin (1990) provides circumstantial evidence for this effect in EU practice: comparing EU antidumping and parallel cartel investigations over the period 1980-1987 found that one-fourth of the cases involved the same products and firms. Blonigen and Prusa (2003) survey the literature in this area.

[52] Source: Bown (2010).

[53] See, for example, Greasley and Oxley (1998) on economic policy; Walsh (2008) and Newbold and Bell (2001) on migration policy; Kealey and Patmore (1996) on labour studies; Svensson et al. (2009) on corporate behaviour; Ward (1993) on political science; and a wide-ranging set of other issues.

ANNEX A: CGE MODEL ASSESSMENT OF TRADE POTENTIAL

The main tool used for the analysis of policies that liberalize or facilitate trade on an economy-wide basis is a computable general equilibrium (CGE) model. A CGE model integrates data on bilateral trade flows, trade protection and domestic support together with national input-output tables that describe inter-sectoral sales and purchases of intermediate goods and services within each economy. This allows the model to generate estimates of the impact of simultaneous removal of trade barriers across a wide range of trade flows and to calculate the consequent impact on the level of national economic output (gross domestic product), employment and economic welfare.

The light that a CGE simulation can shed on trade potential is limited by an inherent feature: it evaluates the impact of a given reduction in a trade barrier (either a tariff or the tariff-equivalent reduction of another type of trade barrier) in respect of flows that already exist. In this sense, it evaluates trade gains at what is termed the "intensive margin"—an expansion or intensification of trade flows that are already happening. However, it cannot provide information on the impact of liberalizing measures on trade flows that do not yet exist—which is termed the "extensive margin". To be sure, aggregation of trade flows across tariff lines addresses this to some extent in that expansion of broadly defined sectors will include both the expansion of existing flows within that sector and the initiation of new trade in products that were previously not traded. However, if much of the response of trade in a sector comes from non-tariff factors, the use of elasticities that are plausible for existing flows results in underestimation of the total response; use of higher elasticities on the other hand is difficult to defend.

Furthermore, CGE simulations cannot adequately take into account potential initiatives in areas such as, for example, the temporary entry of business or professional personnel, or reduction of costs of travel through improved air services. Given the complementarities between goods and services trade, measures that facilitate or liberalize investment may induce a response in terms of trade in goods and services that analysis of these areas in isolation would not reveal.

As well, when governments signal interest in a bilateral relationship, there is some evidence that this can have a galvanizing effect on business behaviour. Such a reaction on the part of business can be readily understood through modern trade theory which focuses on the behaviour of firms in international commerce. Firms face sunk costs of introducing their products into foreign markets (so-called "beachhead costs") in terms of obtaining market intelligence, identifying foreign partners, dealing with foreign regulatory requirements, setting up distribution and after-sales service networks and so forth. Potential export market entrants also face uncertainty about success in foreign markets. They have less knowledge than established firms about these markets and the local partners or agents they must engage (information asymmetries). Because of these sunk costs and uncertainties, not all firms that could engage in trade and foreign investment actually take that step and, of those that do, many enter fewer markets than they might optimally serve. By the same token, political commitment and facilitative measures by government can provide extra inducement to business to commit the resources to take advantage of the new market opportunities. On this basis, the estimated increase in bilateral merchandise trade in a CGE simulation which is based on the height of formal trade barriers but does not take these behavioral factors into account is likely to underestimate the result. Accordingly, the results reported in this section should be considered as partial, even though they are labeled "general".

A few further preliminary observations are in order about the interpretation of modelling results.

First, the results of CGE simulations are best understood as estimates of the *potential* economic impacts a policy change, not as *forecasts* of likely results. Simulations compare the structure of an economy at a given point in the

past, as it was and as it would have been if the simulated policy change had been made some time earlier, with all economic adjustments completed. Given that, exchange rates, technology, global institutional arrangements etc. are inherently held constant (they are exactly what they were) and only the change due to the policy experiment is evaluated. The implicit assumption is, of course, that this potential remains if measures were put in place sometime in the future.

Second, CGE simulations provide no information about the adjustment path or the length of time it takes for all adjustments to take place.

Third, the present study assesses the potential for expansion of Australia-Canada bilateral commerce without reference to any specific negotiating context.

MODELLING SERVICES TRADE LIBERALIZATION

A number of challenges must be confronted in modelling services trade liberalization. First, the General Agreement on Trade in Services (GATS) classifies trade in services into four modes of supply:

1. Cross-border supply: a service is supplied from a supplier's country of residence to a consumer's country of residence.
2. Consumption abroad: a service is supplied through the movement of a consumer to a supplier's country of residence.
3. Commercial presence: a service is supplied through the movement of a commercial organization to a consumer's country of residence.
4. Presence of natural person: a service is supplied through the movement of a natural person to a consumer's country of residence.

Barriers to trade in services can be present in each of the four modes of supply. In this case, commerce can be expected to follow the path of least resistance. In the face of barriers to cross-border sales, firms may seek to establish local affiliates. While this is true for goods as well, given the nature of services[1], the establishment of foreign subsidiaries to export services tends to be more prevalent than for goods. However, the possibility of strong complementarities also exists. The establishment of a subsidiary may lead to the import of headquarters services and also on occasion the movement of service providers from the headquarter country on a consulting basis or the reverse movement of personnel to the headquarter country for training. Accordingly, the extent of cannibalization of activity through foreign affiliates by cross-border mode trade is not clear.

[1] Services are typically distinguished from goods in the sense that they are intangible, non-storable and require joint production (i.e., consumers and producers need to be in the same location at the point of consumption). See for example, Kneller et al. (2010). Services are often embodied in the provider who must move to provide the service in different places (e.g., performing arts). They are typically customized with consequential measurement issues related to breaking down value into quantity and price, taking into account quality of different providers, and so forth—although this is true of some goods as well. At the same time, the distinction between goods and services is far from clear-cut: a table shipped across a border is trade in goods whereas the carpenter going to the destination country to build it there is providing a traded carpentry service (see Copeland 2003 for a general discussion of trade in goods as trade in factor services). In durable goods, the consumption is not of the good itself but of the services that it provides. Moreover, the boundary between products and services has become increasingly blurred, as products are "servicized" and services are "productized" (Sako et al., 2006).

The greater issue encountered with evaluating the potential for services trade expansion is the measurement of barriers to services trade. Unlike merchandise trade, for which there exists a comprehensive and reasonably reliable data set describing the height of border barriers, a comprehensive database on the barriers to cross-border services trade does not exist.[2] Moreover, even if such a database existed, estimates for the liberalizing effect of specific negotiated changes to domestic regulations are not available.

Services trade barriers take various forms:

- Regulations, such as requirements for service providers to meet particular qualifications or standards or to acquire licenses, as in the case of medical or legal practitioners;
- government procurement restrictions,
- the requirement for foreign providers to establish subsidiaries with minimum capital for prudential regulatory purposes as in the case of financial institutions;
- regulated monopolies in sectors with steep increasing returns or network externalities such as telecommunications which create difficulties for foreign suppliers to gain access to established networks; and
- the granting of monopoly concessions on services on profitable market segments to finance the provision of service on a mandatory basis to other areas where such services would otherwise be lacking (thinly populated rural areas for mail, and less dense air and rail passenger routes).

Tariff equivalents for the impact of these highly heterogeneous restrictions on market access to international service providers do not exist. Services trade liberalization is therefore usually modeled based on inferences drawn from available indicators. Two methods predominate. First, bilateral services trade barriers can be inferred from gravity-model based estimates of potential versus actual services trade. For example, the intensity of services trade within the European Union provides a baseline against which the intensity of services trade between other nations can be evaluated. Second, the margins realized by service providers in a particular market can be compared to margins in the most open market for which data are available. Hong Kong and Singapore are the two benchmark countries typically chosen.[3] The present study adopts the second approach, based on estimates of margins from Francois, Hoekman and Woerz (2007).

MODEL SPECIFICATIONS AND ASSUMPTIONS

The results of CGE model simulations can be heavily influenced by the model structure, parameter estimates, the level of aggregation of the data, and the assumptions made as to how to run the simulations.

The standard GTAP model is used for the present simulations in conjunction with the 8.0 data set.[4] This level of disaggregation is important to reduce aggregation bias in estimating trade impacts, which is the primary aim in this

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2 For a detailed review of the issues facing the quantification of services trade barriers and estimating the impact of services trade liberalization, with specific reference to the Canadian context, see Copeland (2003); Chen and Schembri (2003); and Chen (2003).

3 See, for example, Francois, Hoekman and Woerz (2007). Both approaches are open to the criticism that they infer the height of barriers from residuals, whereas residuals are in fact a measure of ignorance.

4 The standard model is designated 6.2 in the GTAP documentation and the 8.0 data set which draws on 2004 and 2007 data to construct the base year. For simplicity we refer to the standard model run on the 2004/2007 base year data set as GTAP 8.0.

study of commercial potential.[5] The simulations were conducted on a fully disaggregated sectoral basis (57 sectors, of which 43 are merchandise).

For convenience, the simulations were conducted with the global economy aggregated into 9 regions: Australia and Canada; their major regional partners—respectively New Zealand, and the United States and Mexico; plus China, Japan, the EU27, and the rest of the world (ROW).

The main technical features of the GTAP model are as follows:

- On the production side, each sector has a representative firm which produces goods using land, labour (skilled and unskilled), capital and intermediate goods and services. The model employs a nested framework to address substitutability of the factors of production. Land, labour and capital substitute for one another in a value-added aggregate in the first nest, and composite intermediate inputs substitute for value-added at the next nest. Labour and capital are assumed to be fully employed, mobile across all uses within a country but immobile internationally.
- On the demand side, each region has a representative household whose expenditure is governed by an aggregate utility function. This aggregate utility function is of a Cobb-Douglas form allocating expenditures across private consumption, government spending, and savings. Private household demand is represented by a Constant Difference of Elasticities (CDE) functional form, which has the virtue of capturing the non-homothetic nature of private household demands (i.e., demand structure changes with increased income, reflecting the fact that consumption of particular types of goods such as luxury goods increases more with higher income than does consumption of other goods such as staple food products).
- Bilateral international trade flows are modeled based on the Armington hypothesis that goods and services are differentiated by region of origin and are imperfect substitutes. The standard GTAP parameter set was used; the key Armington parameters (the elasticities of substitution between products according to country of origin) have recently been updated based on new econometric research. These elasticities are on average lower than those used in some other models such as the World Bank's Linkage model; the estimated trade and welfare impacts reported here are thus relatively conservative.[6]

For each simulation, decisions are required as to which variables are to be fixed at predetermined values (i.e., exogenous) and which are to be solved by the model (i.e., endogenous). Alternative choices represent alternative "closures" of the model. It is important to note that closure choices influence the results significantly.

Under the GTAP default microeconomic closure, factor endowments (i.e., labour, skilled and unskilled, capital and land) are fixed; factor prices (i.e., wages and return to capital and land) adjust to restore full employment of the

[5] The GTAP family of models also includes a dynamic model which takes into account the impact of policy shocks on capital accumulation, and a version with imperfect competition in industrial goods which takes into account the impact on firm mark-ups. Given that Australia-Canada trade is small relative to the size of each economy, such effects would be small and can safely be disregarded.

[6] The comparative static version of the Linkage model produced income gains for industrialized countries under multilateral trade liberalization that were one third larger using the Linkage trade elasticities versus the GTAP 6.0 set. See van der Mensbrugghe (2006); at p. 71.

factors of production in the post-shock equilibrium.[7] Under alternative microeconomic closures that are sometimes used, the return to capital or to labour can be fixed and the supply of capital and/or labour then adjusts to restore equilibrium.[8] These alternative closure rules assume that the supply of labour and/or capital is either perfectly elastic or perfectly inelastic. The reality is somewhere in between. The GTAP model can be simulated to approximate intermediate values of the elasticity of supply of capital and/or labour. The modeller's assumptions for these parameters, based on empirical evidence drawn from outside the model, then determine how the response of the model to a given policy shock. Depending on the assumptions about supply-side elasticities established in the chosen closure, the impacts of a policy shock on an economy are felt to differing extents on prices or quantities. Following Ciuriak and Chen (2008), five alternative closures are constructed:

1. labour and capital supply fixed (the standard or default closure);
2. labour supply flexible, capital supply fixed;
3. labour supply fixed, capital supply flexible;
4. both labour and capital supply flexible; and
5. a central or preferred scenario, which reflects judgments as to the most appropriate assumptions for Australia and Canada, coupled with the default closure for all other countries or regions.

With regard to the long-run supply of labour, the economic literature supports the use of a positive but low supply elasticity. On the basis of recent empirical evidence, the labour market closure for Australia and Canada is based on fixing the elasticity of labour supply at approximately one.[9]

With regard to the long-run supply of capital, given that both Australia and Canada are highly open economies and provide virtually untrammelled access to capital inflows, the most plausible assumption for capital supply is that it is highly elastic; this corresponds closely to the steady state closure rule for capital.

The second aspect of closure is macroeconomic closure. Two approaches are available here: the standard approach with the GTAP model, which is used in the present simulations, is to allow the current account to adjust to the trade shock, with passive accommodation by international investment flows. In this case, the change in the current account implies a change in domestic investment. In the GTAP model, the change in investment is reflected in the profile of final demand, which in turn affects the profile of production and trade. However, the change in investment does not feed through into the productive capacity of industries/regions. The alternative macroeconomic closure is to fix the

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7 This is sometimes described as reflecting a medium-term time horizon in which labour supply is relatively "sticky." However, such a characterization is potentially misleading as CGE model simulations do not include an explicit time dimension.

8 The closure rule in which the rate of return to capital is fixed is sometimes described as reflecting longer-run "steady-state" growth conditions. For an example of the implications of fixing the return to capital and allowing investment to adjust, see Gilbert (2004). Gilbert reports net economic welfare gains for Korea that are 2.7 times larger, and for the U.S. that are 2.4 times larger, with this closure compared to standard closure. For an example of the use of the labour market closure rule under which the wage rate is fixed, see Francois and Baughman (2004).

9 For a discussion of the elasticity of supply of labour, see Ham and Reilly (2006).This study finds statistically significant inter-temporal labour supply elasticities of 0.9 with the Panel Study of Income Dynamics (PSID) data set and 1.0 with the Consumer Expenditure Survey (CES) data set. In terms of simulating GTAP, this assumption is implemented by an iterative approach to identify interventions into the model that result in approximately an equal percentage response for labour supply and wages.

current account, implicitly assuming no international capital mobility; this is a much less realistic assumption for both Australia and Canada and this option is accordingly not used.[10]

There are several issues concerning the underlying database for the GTAP simulations. The base year for the GTAP 8.0 data is 2007. The base year for the input-output tables in the GTAP 8.0 data base, however, varies from country to country. For Australia, the reference year is the financial year ending in June 1997 and for Canada it is calendar year 2003[11]—in other words, the internal linkages in the Australian and Canadian economies are as they were in the respective historical periods. Given the rapidity of economic change in recent years in terms of international sourcing and the increased use of global value chains this is something of a drawback; however, the implications of updated input-output coefficients are generally considered to be minor.

As regards the protection data, for Australia, these are obtained from Market Access Map (MAcMap), which was produced and is maintained collaboratively by the Paris-based Centre d'Etudes Prospectives et d'Informations Internationales (CEPII) and the International Trade Centre (ITC) in Geneva. The tariff data are compiled at the Harmonized Tariff System 6-digit level and include the *ad valorem* equivalent of specific tariffs and the tariff equivalent of tariff rate quotas (TRQs). For Canada, the protection data were updated for the present study to take account of the unilateral elimination of tariffs on 1,541 industrial inputs in the federal government's 2010 Budget.

Reflecting the institutional issues in agriculture discussed above, Canada's dairy sector is liberalized but Australia's is not, in order to reflect the constraint on Canada's dairy sector exports imposed by Canada's commitments to reduce subsidized exports. As regards beef, as there are no beef exports from Canada to Australia in the base data, no interventions are made to reflect potential gains if Canada in the future obtained clearance to export beef under Australia's Quarantine regulations.

SIMULATION RESULTS

This section describes the impact of eliminating barriers to Canada-Australia bilateral merchandise trade and of reducing the barriers to bilateral services trade to a level of openness commensurate with the most open services-importing economies in the world. The simulations involve full elimination of trade protection as captured in the GTAP database, updated as described above, for all industrial and agricultural sectors, and liberalization of cross-border services trade.

[10] See Gilbert (2004) for a comparison of the impact of using alternative macroeconomic closures in the context of modeling the U.S.-Korea FTA. The fixed current account simulations substantially reduce the economic welfare gains for Korea (to 3/5 the level of the simulation with flexible current account) and marginally (by 5%) for the United States.

[11] See Terry Maidment and Owen Gabbitas on the construction of the Australian input-output module for GTAP at https://www.gtap.agecon.purdue.edu/resources/download/4195.pdf ; and Richard A. Cameron and Shenjie Chen on the construction of the Canadian input-output module at https://www.gtap.agecon.purdue.edu/resources/download/4192.pdf.

TRADE IMPACTS: AUSTRALIA'S IMPORTS FROM CANADA

Table A1 sets out the changes in Australia's imports from Canada due to elimination of Australian tariffs on goods and liberalization of services. The impacts reported are based on the central scenario for closure. [12]

Table A1: Changes in Australia's Imports of goods and services from Canada

	Base Level (2007 US$ millions)	Change (level)	Change (percent)
Primary sectors & food products (GTAP 1-25)	353	8	2.2%
Other manufactured products (GTAP 26-42)	1,194	283	23.7%
Total Goods	1,547	291	18.8%
Total Services	372	162	43.5%
Total Goods and Services	1,919	453	23.6%

Source: Author's calculations based on GTAP simulations; central scenario closure.

Based on the 2007 level and sectoral composition of Australia's merchandise imports from Canada, tariff elimination would induce an increase of US$291 million or 18.8% in total goods imports from Canada. The gain in services imports is much larger percentage-wise at 43.5%. For total goods and services imports, the increase amounts to US$453 million or 23.6%.[13]

The top ten sectors in terms of increases in imports in value terms of Australian imports from Canada set out in Table A2. By far the largest gains are in the machinery and equipment sector.

Table A2: Changes in Australia's Imports of goods from Canada: top sectors in value gains

Sector	Base Level (2007 US$ millions)	Change (level)	Change (percent)
Machinery & equipment	440.8	145.0	32.9%
Transport equipment	137.3	25.1	18.3%
Motor vehicles & parts	66.8	21.1	31.5%
Wood products	60.2	17.7	29.4%
Electronic equipment	117.5	15.4	13.1%
Metal products	36.0	11.9	33.2%
Chemical products	131.8	11.9	9.0%
Textiles	15.9	7.5	47.4%
Other manufacturing products	18.7	6.4	34.3%
Food products	50.4	6.4	12.7%

Source: Author's calculations based on GTAP simulations; central scenario closure.

Table A3 sets out the model results for the services sectors that could plausibly be expected to be affected by Australia's liberalization. The biggest gains are in business services and air transportation. The estimates of service

[12] Note: the bilateral trade figures are not significantly influenced by the choice of closure. Accordingly, we report only the results for the central scenario for closure. As shown below, the main impact of alternative closures is on the extent of trade diversion experienced by third countries.

[13] Given the decline in trade during the 2008-09 global downturn, the levels of trade in 2011 are similar to those realized in 2007; accordingly, the value gains estimated above would be comparable against the current level of trade. As well, since the Australian and Canadian exchange rates are in reasonable proximity to parity with the US dollar, the order of magnitude of the estimated impacts would be about the same expressed in either currency; for simplicity, we report the figures in 2007 USD as per the data generated by GTAP.

sector gains are crude, a reflection of the limited empirical evidence for the extent to which liberalizing measures improve market access and the lack of evidence on which to base sector-specific elasticities of substitution.

Table A3: Changes in Australia's Imports of services from Canada: top sectors in value gains

Sector	Base Level (2007 US$ millions)	Change (level)	Change (percent)
Other business services	86.6	47.6	55.0%
Air transportation	34.8	47.0	135.3%
Telecommunications	66.1	34.3	51.8%
Other financial services	12.4	17.2	53.3%
Insurance	32.2	8.6	135.5%

Source: Author's calculations based on GTAP simulations; central scenario closure.

TRADE IMPACTS: CANADA'S IMPORTS FROM AUSTRALIA

Table A4 sets out the changes in Canada's imports from Australia as a result of tariff elimination on bilateral trade in industrial and agricultural products. Based on the 2007 level and sectoral composition of Canada's merchandise imports from Australia, tariff elimination would induce an increase of US$229 million or 13.5% in total goods imports from Canada while services liberalization would induce a stronger percentage increase in services imports of 61.4% although a somewhat smaller level gain of US$181 million given the smaller base. For total goods and services imports, the implication is an increase in imports of US$410 million or 20.6%.

Table A4: Changes in Canada's imports of Goods and Services from Australia

	Base Level (2007 US$ millions)	Change (level)	Change (%)
Primary sectors & food products (GTAP 1-25)	289	169	58.6%
Other manufactured products (GTAP 26-42)	1,405	60	4.2%
Total Goods	1,694	229	13.5%
Total Services	295	181	61.4%
Total Goods and Services	1,989	410	20.6%

Source: Author's calculations based on GTAP simulations; central scenario closure.

The top ten sectors in terms of increases in imports in value terms of Australian imports from Canada set out in Table A5. By far the largest gains are in agricultural products, led by beef and dairy products. Textiles and apparels imports increase by a moderate amount in absolute terms but quite substantially in percentage terms.

Table A5: Changes in Canada's Imports of Goods from Australia: Top Sectors in Value Gains

Sector	Base Level (2007 US$ millions)	Change (level)	Change (percent)
Bovine meat	76.4	92.1	120.6%
Dairy products	12.2	69.0	565.2%
Chemical products	396.8	18.8	4.7%
Machinery & equipment	225.4	9.5	4.2%
Food products	22.9	7.0	30.6%
Transport equipment	12.3	6.8	54.8%
Apparel	4.8	6.3	132.8%
Textiles	6.0	5.3	88.2%
Metal products	12.0	3.1	25.8%
Beverages & tobacco	304.4	2.9	0.9%

Source: Author's calculations based on GTAP simulations; central scenario closure.

Table A6 sets out the results for the services sectors affected by Canada's liberalization. The biggest gains are in air transport followed by business services. As noted earlier, however, the sectoral breakdown of the service sector gains is crude, a reflection of the limited empirical evidence for the extent to which liberalizing measures improve market access and the lack of evidence on which to base differentiated elasticities of substitution in the sectors under consideration.

Table A6: Changes in Canada's Imports of Services from Australia: Top Sectors in Value Gains

Sector	Base Level (2007 US$ millions)	Change (level)	Change (percent)
Air transportation	50.1	72.6	144.9%
Other business services	34.7	48.6	140.0%
Telecommunications	18.0	25.0	138.7%
Insurance	14.0	19.6	139.6%
Other financial services	7.2	10.1	140.1%
Shipping	3.5	5.1	147.6%

Source: Author's calculations based on GTAP simulations; central scenario closure.

TRADE CREATION, DIVERSION AND DEFLECTION

Liberalization on a preferential basis leads to both trade creation and trade diversion (imports) or deflection (exports). The relative sizes of these effects are shown in Tables A7 and A8, respectively.

As can be seen in Table A7, the closure choice impacts significantly on the extent of trade diversion in import markets. The extent of trade diversion is greatest under the more restrictive closures, in which either or both capital and labour supply are fixed and the gains from trade in the factor markets take the form of increases in wages and returns to capital, as the case may be. The amount of trade diversion is least when both labour and capital supply are fully flexible and gains from trade in factor markets are for the most part reflected in increases in output.

Table A7: Impact of Bilateral Liberalization on Imports: Trade Creation and Diversion

	Labour & capital fixed (i)	Capital flexible. Labour fixed (iii)	Labour flexible, capital fixed (ii)	Labour & capital flexible (iv)	Central Scenario (v)
Change in Australian imports					
Canada	449	449	450	457	453
ROW	-215	-218	-153	17	-97
Total	234	231	297	473	356
Change in Canadian imports					
Australia	405	406	405	414	410
ROW	-142	-135	-36	294	65
Total	263	271	369	709	475

Source: Author's calculations based on GTAP simulations.

Table A8 below provides a similar comparison of the trade creation and trade deflection effects on the export side. As can be seen, the expansion of productive capacity under the least restrictive closure (iv) is sufficient to support not only the expansion of bilateral trade but also additional exports to third parties for both Australia and Canada. Conversely, under the most restrictive closure rule with fixed supply of labour and capital, the expansion of

bilateral trade requires a reduction in Australian and Canadian exports to third parties due to supply side constraints.

Table A8: Impact of Bilateral Liberalization on Exports: Trade Creation and Deflection

	Labour & capital fixed (i)	Capital flexible. Labour fixed (iii)	Labour flexible, capital fixed (ii)	Labour & capital flexible (iv)	Central Scenario (v)
Change in Australian exports					
Canada	394	395	395	403	399
ROW	-231	-192	-234	47	-69
Total	164	203	161	450	330
Change in Canadian exports					
Australia	436	436	437	444	440
ROW	-218	-154	-199	295	56
Total	218	282	238	739	496

Source: Author's calculations based on GTAP simulations.

The empirical literature does not offer a consensus opinion on the extent of trade diversion/deflection caused by preferential liberalization. The "conventional wisdom" has been that trade creation dominates trade diversion. Direct attempts to measure whether preferential trade agreements reduce the amount of trade with third parties using gravity models have generally failed to show significant negative effects, although different studies have reached opposite conclusions on this point. The central scenario, which has only modest amounts of trade diversion and deflection, is thus not out of line with the empirical literature.

IMPACT ON GDP

Table A9 compares the changes in GDP for Australia, Canada and their major trading partners, under the alternative closure assumptions, that are associated with the extent of trade created under these various scenarios. Whereas the trade impacts generated by the model are relatively stable across the scenarios (with the bilateral trade impacts showing almost no sensitivity), the estimated GDP gains vary greatly depending on the assumptions concerning the supply response of the economy to the incentives created by liberalized trade

Table A9: Changes in GDP (USD millions/percent)

	Labour & capital fixed		Capital flexible, labour fixed		Labour flexible, capital fixed		Capital and labour flexible		Preferred scenario	
Canada	343	0.024%	387	0.027%	746	0.052%	2,114	0.148%	1,195	0.084%
Australia	504	0.061%	535	0.065%	817	0.100%	2,035	0.248%	1,309	0.159%
USA	-378	-0.003%	-321	-0.002%	-308	-0.002%	296	0.002%	-26	0.000%
Mexico	2	0.000%	3	0.000%	3	0.000%	10	0.001%	6	0.001%
Japan	-70	-0.002%	-53	-0.001%	-84	-0.002%	9	0.000%	-21	0.000%
EU27	-275	-0.002%	-226	-0.001%	-298	-0.002%	13	0.000%	-102	-0.001%
China	-47	-0.001%	-39	-0.001%	-44	-0.001%	29	0.001%	-5	0.000%
NZ	-19	-0.014%	-19	-0.014%	-17	-0.013%	-10	-0.008%	-15	-0.011%
ROW	-2	-0.001%	-95	-0.001%	-102	-0.001%	133	0.001%	16	0.000%
Total	-51	-0.001%	126	0.000%	670	0.001%	4,669	0.008%	2,358	0.004%

Source: Author's calculations based on GTAP simulations.

For Canada, the simulations suggest an increase in the value of GDP of between 0.024% in the standard closure scenario (labour and capital supply both fixed) to 0.148% in scenario (vi) where both capital and labour supply are flexible. In the central scenario (labour supply elasticity = 1, capital supply flexible), the GDP gain for Canada is 0.084%. For Australia, the GDP gains are somewhat greater, ranging from 0.061% in the most restrictive scenario to 0.248% in the least restrictive, with an increase of 0.159% in the central scenario.

For most third parties, bilateral liberalization between Australia and Canada has a negative impact on GDP under the restrictive standard closure (i). However, the size of the negative impacts diminish as the constraints on the production capacity in both Canada and Australia are relaxed under less restrictive closure rules (ii)-(iii) and (v), and turn into positive gains for many regions under the least restrictive scenario (iv). Under the central scenario, the GDP impacts on third parties are, for the most part, negative but negligible; and global GDP impacts are overall modestly positive, dominated by the gains experienced by Canada and Australia. This latter outcome is consistent with the positive association between trade liberalization and global growth.

IMPACT ON HOUSEHOLD ECONOMIC WELFARE

The economic benefits or costs of a policy change are conventionally measured by equivalent variation. This is the amount of money that would make the household sector as well off in the pre-policy shock scenario as in the policy shock scenario. Table A10 reports the economic welfare impacts by region.

Table A10: Household Economic Welfare Impacts (USD millions)

	Labour & capital fixed	Capital flexible, labour fixed	Labour flexible, capital fixed	Capital and labour flexible	Central scenario
			Australia		
Allocative efficiency	16	37	125	627	341
Endowments	0	55	224	1,342	718
Services Efficiency	59	59	59	59	59
Terms of Trade	58	49	61	-7	20
Total	138	203	472	2,018	1,139
			Canada		
Allocative efficiency	8	32	206	895	436
Endowments	0	64	259	1,381	681
Services Efficiency	65	65	65	65	65
Terms of Trade	53	37	49	-68	-12
Total	127	199	580	2,272	1,171
			World		
Allocative efficiency	6	53	309	1,501	759
Endowments	0	118	482	2,722	1,400
Services Efficiency	124	124	124	125	124
Terms of Trade	0	0	0	0	0
Total	130	295	915	4,348	2,283

Source: Author's calculations based on GTAP simulations. Note: reported effects do not add exactly to the total as the GTAP welfare calculation also includes a term that reflects the price differentials between saving and investment.

As in the case of the GDP impacts, the estimated economic welfare gains vary considerably across the alternative closure scenarios. The simulations suggest that Australian households would derive an economic welfare benefit of between US$138 million and US$2.0 billion, with our central scenario estimate at US$1.14 billion. For Canada, the results range from US$127 to US$2.3 billion, with our central scenario estimate at US$1.17 billion. Most other regions would incur minor losses due to trade diversion except under the least restrictive scenario. For the global economy as a whole, however, the gains in Australia and Canada outweigh the effects elsewhere and economic welfare improves.

With regard to the sources of gains/losses, this is influenced heavily by the closure assumption. If capital and labour are fixed, as they are in scenario (i), increased demand largely results in increases in wages and in returns to capital. These higher factor costs are passed on in the form of higher prices which are reflected in the model's accounting as terms of trade gains. In scenarios in which higher factor prices induce greater labour and capital supply, the gains attributed to terms of trade decline while the gains attributed to increases in allocative efficiency and endowments increase. Under the least restrictive scenario (iv), the endowment effect overwhelms all other gains.

ANNEX B: THE AUSTRALIA-US FTA: INFERENCES FOR CANADA-AUSTRALIA

The Australia-US Free Trade Agreement (AUSFTA), which came into force 1 January 2005, provides something of a "natural experiment" to shed light on the potential for trade gains from Australia-Canada liberalization. The United States is not quite as similar an economy to Australia as is Canada, nor as distant; moreover, it is more than an order of magnitude larger. That being said, the US pattern of trade specialization is reasonably similar to Australia's[14] and its general socio-economic and cultural features are also quite similar.

THE AUSTRALIA-US FTA AND RELATED MEASURES: BACKGROUND

The AUSFTA[15] eliminated most Australian tariffs immediately, resulting in about 97 per cent of tariff lines being duty free. The remaining non-zero tariff lines (clothing and textiles) were subject to a 10-year phase-out. The trade-weighted tariff fell from 2.6% pre-FTA to 0.1% by 2008. US agricultural market access was incompletely liberalized: tariffs on two-thirds of line items were eliminated immediately, with some further reductions phased in over 18 years. The tariff quota for beef was expanded and the out-of-quota tariff is slated to be phased out from its current level of 26.4 per cent between years 9 and 18 of the agreement. The dairy tariff quotas were also expanded but in this case out-of-quota tariffs are to be retained. There were no changes in market access for sugar. The trade-weighted tariff fell from 2.1% pre-FTA to 0.1% by 2008. Rules of origin, however, are comparatively restrictive.[16]

As regards services trade, the obligations under the AUSFTA are generally in line with undertakings under the WTO General Agreement on Trade in Services (GATS), although in some cases they are WTO-plus. The main provisions require MFN and national treatment and disallow local presence requirements. The agreement includes a framework for developing MRAs, including through the establishment of a Working Group on Professional Services. Most importantly, unlike the GATS commitments, the FTA commitments in respect of non-conforming measures are based on a negative list approach; hence the FTA had potentially a greater liberalizing impact than the GATS.

As regards specific provisions, the financial services and telecommunications chapters contain nothing novel. The main sectoral exceptions negotiated were in respect of Australia's local content requirements in audiovisual and broadcasting media (Australia retained its requirement that 55% of prime time programming, and 80% of prime-time advertising, be local in content on grounds of preserving Australian culture); and in respect of US restrictions on cabotage (the United States retained the Jones Act restrictions on shipping services).

Accordingly, the impetus to services trade from the FTA must be considered to come primarily from the reduction in uncertainty about future market access provided by the negative list approach to restrictions, the complementarities associated with goods trade, or the indirect effects of other facilitating aspects of the agreement or non-FTA initiatives, such as the US E3 visa which was created in connection with the AUSFTA especially for Australian temporary entrants.

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14 The simple correlation coefficient between the Australian and US trade specialization indicators at the HS02 level of trade in 2010 was 0.37.

15 The summary of the AUSFTA provisions is drawn from the Productivity Commission (2010).

16 The 16% of tariff lines with positive tariffs apply a double test of tariff classification change and a specified processing test to determine origin. See Productivity Commission (2010); at 79.

The E3 visa program is of interest because in many ways the conditions attached are less onerous than those applying to other US visa categories.[17] Professional qualifications for the visa are quite flexible: any Australian with a bachelor's degree or its equivalent in the area concerned is eligible. The access is, however, subject to an annual quota of 10,500. The United States-based employer of an E3 applicant must also fulfill certain obligations, including obtaining a Labor Condition Application (LCA) from the Department of Labor. The employer must also submit a job letter that establishes that the applicant will be engaged in qualifying work in a specialty occupation and be paid the actual or prevailing wage for that occupation. Further, if the job requires a license or registration, this must be obtained by the applicant. However, unlike most other temporary visas, employers need not submit a petition to the Department of Homeland Security. A change of employer requires a new E-3 visa application; however, this can be done while the applicant is inside the United States. New applications do not count against the annual quota. Of potentially great significance to potential applicants, the spouses of E3 visa holders may work in the United States, including in jobs that do not qualify as "specialty occupations" (however, the program indicates that spouses "may" apply to the Department of Homeland Security for an employment authorization document, which an employer could use to verify the spouse's employment eligibility).

Notwithstanding these relaxed conditions, the program's annual quota of 10,500 per year has not been approached since its inception, even though extensions of an E-3 visa are not counted against the annual quota.

Table B1. Usage by Australian Professionals of the US E3 Visa

		2005	2006	2007	2008	2009	2010
E3	Australian specialty occupation professional	4	1,918	2,572	2,961	2,191	2,175
E3D	Spouse or child of Australian specialty occupation professional	3	1,053	1,368	1,568	1,421	1,582
E3R	Returning Australian specialty occupation professional	0	0	6	114	561	782

Source: US Department of State. Nonimmigrant Visas Issued by Classification, various years.

As regards investment, the AUSFTA provides for MFN and national treatment, assures a minimum standard of treatment in accordance with customary international law, and raises Australia's screening thresholds for foreign investment from the United States to about 5 times the level applying to investors from other countries. The AUSFTA does not provide for investor-state dispute settlement.

FIRM-LEVEL IMPACTS OF FTAS – THE EXTENSIVE MARGIN

The focus of attention in the modern trade literature is the firm. Gains from trade are seen as coming mainly from the reallocation of market share from low-productivity to high-productivity firms due to the change in the population composition of firms as low-productivity firms exit and higher-productivity firms expand their production in order to serve export markets (see Redding, 2011 for a recent review of this literature). As well, firms entering export markets tend to grow substantially faster than non-exporters. The combination of higher initial productivity and faster growth after entry into exporting suggests that trade liberalization enhances aggregate productivity growth as well as its level by reallocating market share across firms (Bernard, Jensen, Redding and Schott, 2007). The mechanisms that drive this stronger performance are generally familiar from the previous trade literature: access to scale economies and a tendency to adopt process technology suited to larger markets (e.g.,

[17] See, "E-3 Visa Frequently Asked Questions," at http://www.visabureau.com/america/e3-visa-faqs.aspx#WHMFAQone.

Lileeva and Van Biesebroeck, 2010); greater absorption of foreign technology (e.g., Bas and Strauss-Kahn, 2010); the effects of competitive pressure (e.g., Holmes and Schmitz, 2010); and the relaxing of financial constraints (e.g., see Egger and Kesina, 2010, and Manova, Wei and Zhang, 2011, for evidence for Chinese firms; and Silva and Carreira, 2011, for evidence for Portuguese firms).

Importantly, for liberalization to generate such effects, either new firms must enter export markets or existing exporters must introduce new products. The Australian Productivity Commission recently concluded that Australia's FTAs were generally under-utilized by business. The reasons for this were potentially many.

- The main factors that influence decisions to trade or invest abroad are not directly influenced by BRTAs.
- Improvements in market access for agricultural goods remain largely unrealisable without concomitant reforms to quarantine requirements in partner countries.
- Businesses intent on supplying services to foreign countries typically already "work around" many formal barriers.
- Even where the mutual recognition of qualifications or testing procedures are agreed in a BRTA, additional requirements hamper the use of these measures.

Accordingly, it is an interesting question as to what effects the AUSFTA had in terms of new product and firm entry into bilateral trade. For goods, one source of evidence on such effects is the activity across tariff lines. The analysis here is constrained to the period 2002-2006 because of HS code reclassifications in 2002 and 2007 which compromises comparison of longer time series.

THE AUSFTA AS A NATURAL EXPERIEMENT

Table B2 shows the data for Australian products in US import markets. As can be seen, there is a high degree of "churn" in traded goods, with a large number of products being introduced each year and a large number dropping out. On trend, advanced economies tend to experience a trend decline in the number of exported products due to increased specialization (Imbs and Wacziarg, 2003). The Australian export presence in the US market followed this pattern in the mid-2000s (see the base year downward trend across successive cohorts) but the trend is interrupted by a sharp uptick in the 2006 cohort. As well, the survival rates in 2006 improved noticeably compared to previous years. This experience is consistent with the FTA enhancing the introduction of Australian products into US markets and their survival prospects.

Table B2: Introduction and Survival Rates: US Imports from Australia, 2003-2006

	Base year	Base year +1	Base Year +2	Base year + 3	Base year + 4
2002 cohort	4724	3394	2827	2511	2295
2003 cohort	4710	3388	2845	2545	
2004 cohort	4677	3361	2875		
2005 cohort	4652	3443			
2006 cohort	4755				
			Survival Rates		
2002 cohort		71.85%	83.29%	88.82%	91.40%
2003 cohort		71.93%	83.97%	89.46%	
2004 cohort		71.86%	85.54%		
2005 cohort		74.01%			

Source: World Trade Atlas; calculations by the author.

Table B3 provides the comparable data for Australian imports into Canada; as can be seen, survival rates increased for all cohorts in 2006 but not by as much as they increased in the US market. As well, the pace of new tariff line entry in 2006 was slower into the Canadian market than into the US market.

Table B3: Introduction and Survival Rates: Canadian Imports from Australia, 2003-2006

	Base Year	Base Year +1	Base Year +2	Base Year +3	Base Year +4
2002 cohort	3695	2494	2028	1754	1588
2003 cohort	3724	2538	2058	1808	
2004 cohort	3777	2587	2124		
2005 cohort	3763	2619			
2006 cohort	3830				
			Survival Rates		
2002 cohort		67.50%	81.32%	86.49%	90.54%
2003 cohort		68.15%	81.09%	87.85%	
2004 cohort		68.49%	82.10%		
2005 cohort		69.60%			

Source: World Trade Atlas; calculations by the author.

However, the performance of US products in Australian markets was quite the opposite (Table B4). The number of traded products fell off sharply in 2006, intensifying the preceding downward trend rather than reversing it. Moreover, the survival rates for each cohort worsened in 2006.

Table B4: Introduction & Survival Rates: Australian imports from the US 2003-2006

	Base year	Base year +1	Base Year +2	Base year + 3	Base year + 4
2002 cohort	6306	5799	5545	5372	5101
2003 cohort	6223	5781	5547	5216	
2004 cohort	6193	5780	5349		
2005 cohort	6144	5519			
2006 cohort	5822				
			Survival Rates		
2002 cohort		91.96%	95.62%	96.88%	94.96%
2003 cohort		92.90%	95.95%	94.03%	
2004 cohort		93.33%	92.54%		
2005 cohort		89.83%			

Source: World Trade Atlas; calculations by the author.

However, US product introductions and survival in the Canadian market also dropped sharply in 2006 (Table B5), and on across a much larger set of tariff lines, suggesting a common third factor was at place (e.g., the boom in the US market may have diverted potential exports to meet domestic demand).

Table B5: Introduction & Survival Rates: Canadian imports from the US 2003-2006

	Base Year	Base Year +1	Base Year +2	Base Year +3	Base Year +4
2002 cohort	17919	17367	17055	16812	16124
2003 cohort	17851	17399	17094	16360	
2004 cohort	17826	17376	16567		
2005 cohort	18281	17296			
2006 cohort	17858				
			Survival Rates		
2002 cohort		96.92%	98.20%	98.58%	95.91%
2003 cohort		97.47%	98.25%	95.71%	
2004 cohort		97.48%	95.34%		
2005 cohort		94.61%			

Source: World Trade Atlas; calculations by the author.

Perhaps the most compelling evidence for an effect of the AUSFTA on trade patterns is in terms of trade diversion. Table B6 shows the introduction and survival rates of Canadian products in the Australian market over the 2002-2006 period. As can be seen, there is a steep reduction in the number of tariff lines traded in 2006 and survival rates for all cohorts plummeted in 2006 as well.

Table B6: Introduction & Survival Rates: Australian imports from Canada, 2003-2006

	Base Year	Base Year +1	Base Year +2	Base Year +3	Base Year +4
2002 cohort	2847	2234	2008	1859	1645
2003 cohort	2875	2326	2067	1776	
2004 cohort	2997	2393	1959		
2005 cohort	3000	2183			
2006 cohort	2597				
			Survival Rates		
2002 cohort		78.47%	89.88%	92.58%	88.49%
2003 cohort		80.90%	88.87%	85.92%	
2004 cohort		79.85%	81.86%		
2005 cohort		72.77%			

Source: World Trade Atlas; calculations by the author.

Notably, there was no comparable trade deflection effect on Australian exports to Canada: there was no evident change in trends in terms net product introductions or survival rates (Table B7).

Table B7: Introduction & Survival Rates: Australian imports from Canada, 2003-2006

	Base Year	Base Year +1	Base Year +2	Base Year +3	Base Year +4
2002 cohort	3695	2494	2028	1754	1588
2003 cohort	3724	2538	2058	1808	
2004 cohort	3777	2587	2124		
2005 cohort	3763	2619			
2006 cohort	3830				
			Survival Rates		
2002 cohort		67.50%	81.32%	86.49%	90.54%
2003 cohort		68.15%	81.09%	87.85%	
2004 cohort		68.49%	82.10%		
2005 cohort		69.60%			

Source: World Trade Atlas; calculations by the author.

The impact of the FTA on trade flows can also be evaluated by considering the value of flows in tariff lines that were not traded pre-FTA but were post-FTA. There is no established way to measure this and causality cannot be concluded with assurance. Nonetheless it is of interest to examine the behaviour of trade at the extensive margin following the FTA. For this purpose, the analysis below considers tariff lines in which zero trade was recorded over the period 2000-2005 but for which trade was recorded in 2008-2010. This approach takes into account the fact that trade at the extensive margin typically takes some time to build up. The extensive margin flows can be further broken down into sustained extensive imports, which included trade flows that were recorded in each year over the period 2008-2010, and intermittent extensive imports as flows that were recorded in some of those years but not consistently. Further, they can be broken down into flows for which there was a tariff reduction and those for which there was not. Table 20 presents the results of this analysis for the US imports from Australia and Table 21 for US exports to Australia.[18]

Table 20: US Imports from Australia post-FTA: Extensive Margin

Sustained Extensive Imports (USD millions)	813
Intermittent Extensive Imports (USD millions)	292
Total Extensive Imports (USD millions)	1,106
Sustained Extensive Imports as % of Total Imports	2.99%
Intermittent Extensive Imports as % of Total Imports	1.08%
Total Extensive Imports as % of Total Imports	4.07%
Sustained Extensive Imports with Tariff Reduction as % of Total Imports	0.16%
Intermittent Extensive Imports with Tariff Reduction as % of Total Imports	0.33%
Total Extensive Imports with Tariff Reduction as % of Total Imports	0.49%

Source: World Trade Atlas; calculations by the author.

[18] US data are used for flows in both directions because this allows use of data for the whole 2000-2010 period. A detailed US data set is available with consistent concordances for the HS code revisions in 2002 and 2007.

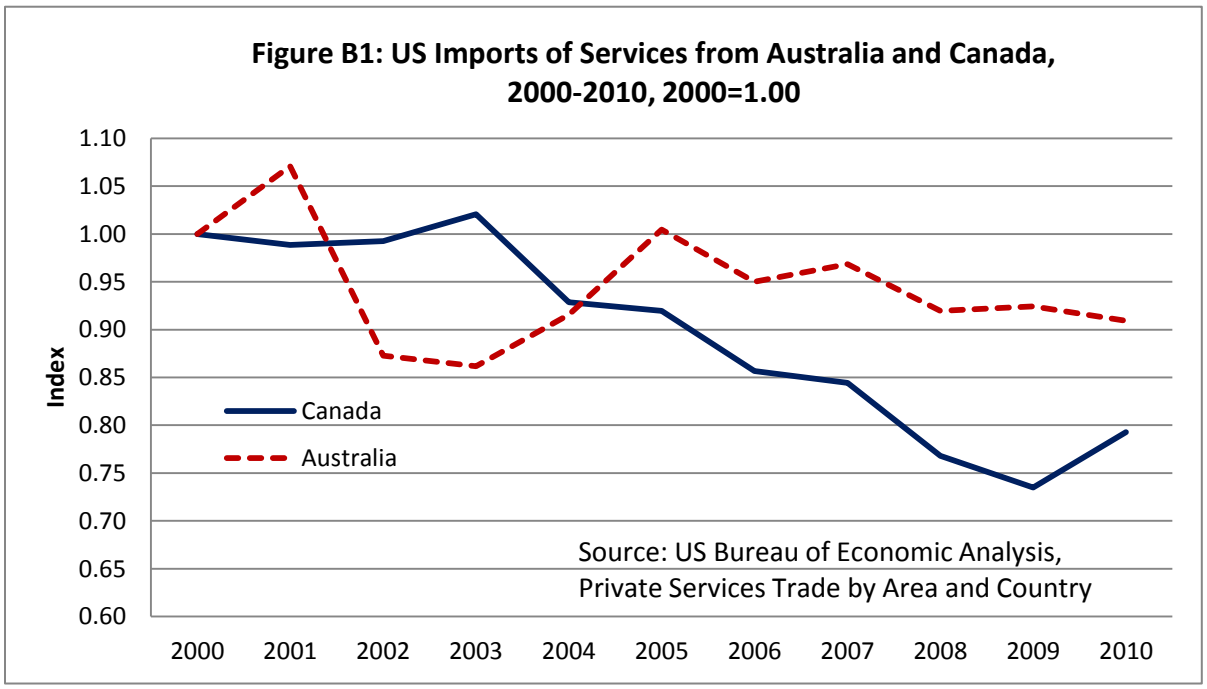
Table 21: United States Exports to Australia post-FTA: Extensive Margin

Sustained Extensive Exports (USD millions)	2,590
Intermittent Extensive Exports (USD millions)	575
Total Extensive Exports (USD millions)	3,165
Sustained Extensive Exports as % of Total Exports	4.07%
Intermittent Extensive Exports as % of Total Exports	0.09%
Total Extensive Exports as % of Total Exports	4.16%
Sustained Extensive Exports with Tariff Reduction as % of Total Exports	0.16%
Intermittent Extensive Exports with Tariff Reduction as % of Total Exports	0.004%
Total Extensive Exports with Tariff Reduction as % of Total Exports	0.16%

Source: World Trade Atlas; calculations by the author.

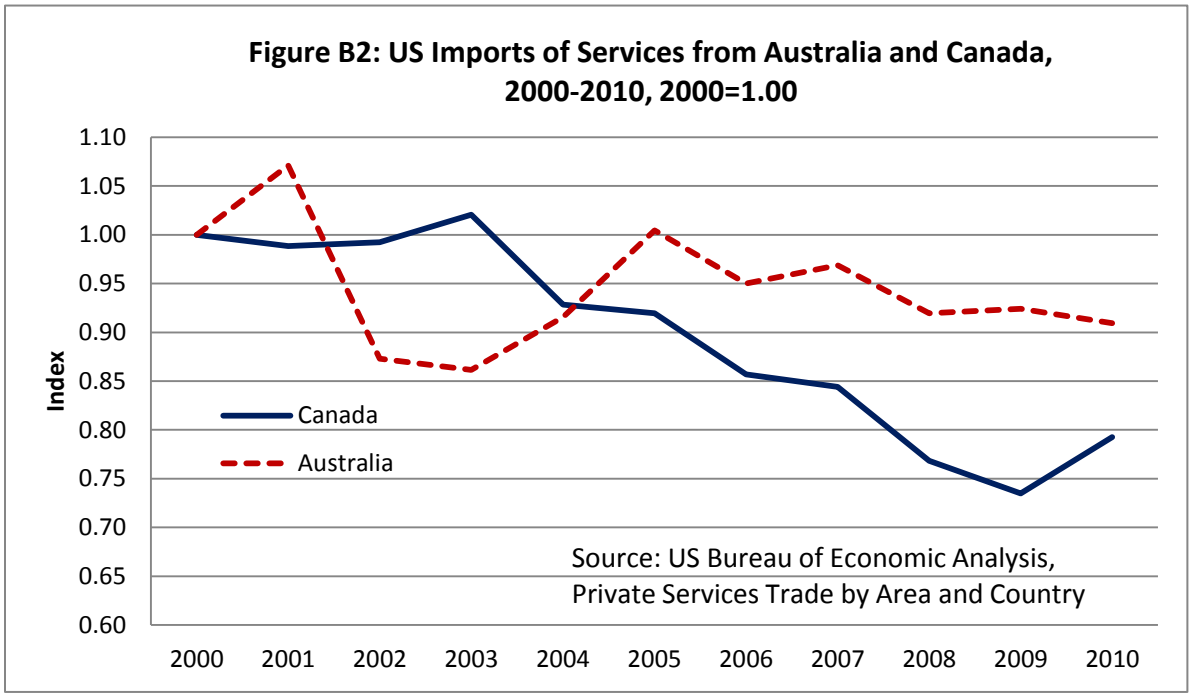
As can be seen, the gains in trade at the extensive margin, measured as above, are not inconsistent with a deepening of the Australia-US commercial relationship in the post-AUSFTA period in terms of trade in goods for which tariff reductions were not made. However, the effects are not large and not all of these gains could necessarily be attributed to the various facilitative elements that were put in place as a result of the AUSFTA and associated measures such as the E3 Visa category created by the US for Australian professionals.

As regards services trade, US imports of services from Australia were rebounding from a cyclical downturn in the early 2000s when the AUSFTA came into force. Since the services provisions in the AUSFTA were for the most part those already made under the GATS, a large impact would not be expected. Indeed, there is no clear point of inflection in terms of pre- and post-FTA trends to be seen in the absolute level of imports (Figure B1).



The Australian share of US imports also picked up in the immediate post-FTA period, but apparently as a continuation of the cyclical rebound; after 2006, a declining trend set in, consistent with the expectation that traditional services exporters to the United States would be losing market share to surging services imports from

low-cost developing countries (e.g., US imports of services from India rose by a factor of more than seven between 2000 and 2010). However, although Australia's share did decline, it held up better than Canada's (Figure B2).



As can be seen, the margin by which Australia held market share in the 2005-2010 period compared to Canada amounted to a gain of US$785 million or 16.3%; these figures may be compared to the CGE estimated gains of Australia in the Canadian market of US$181 million or 61.4%.

Turning to US performance in the Australian market before and after the AUSFTA (Figure B3), in absolute terms, the overall expansion of services imports by Australia from the United States amounted to 55% over the period 2004-2008 before the slowdown in imports associated with the global recession of 2009. When the US share of services is considered (Figure B4). there is no apparent surge that could be attributed to the AUSFTA; however, there is an apparent point of inflection where the US share shifts from a declining trend to a flattish upward trend. Compared to a simple trend extrapolation, Australia's services imports from the United States were about 25% greater in 2010 than they would have without the FTA. If services imports from low-cost countries that rapidly expanded their share of the Australian market are excluded, the apparent reversal of trend in the US share coincident with the FTA is much more striking (Figure B5); the implied gain in this case is still about 25%. A more conservative estimate would be to assume that the main gains were in the first several years following the entry into force of the FTA and that post-2007, the actual observed trend would have been replicated. On this latter basis, the gain would still be about 20%. Of course many other factors (e.g., exchange rates) remain to be taken into account. As well, general equilibrium effects are usually thought to take longer (e.g., a decade) to be fully reflected in the data; accordingly, the half decade of data from the US-Australia FTA may not perhaps tell the full story. However, realistically, this time frame should account for the major part.

Overall, notwithstanding the limited degree of services liberalization in the AUSFTA, there is some evidence for a positive impact on two-way trade that could be attributed to the various measures put in place to enhance the bilateral commercial relationship.

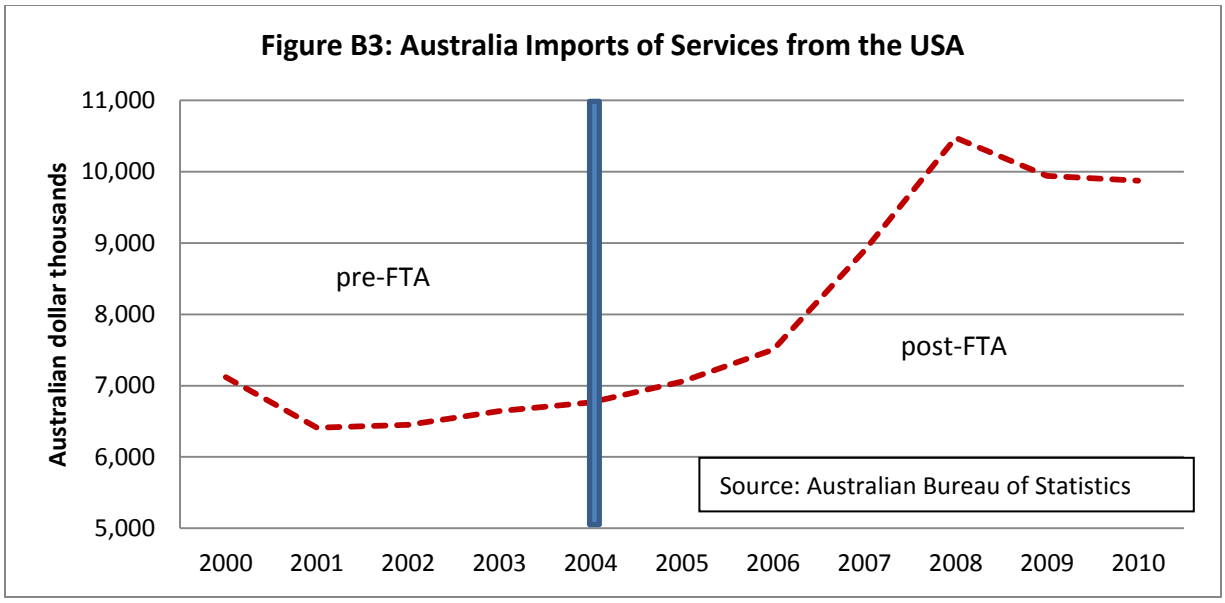


Figure B3: Australia Imports of Services from the USA
Australian dollar thousands
11,000
10,000
9,000
8,000
7,000
6,000
5,000
pre-FTA
post-FTA
Source: Australian Bureau of Statistics
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010

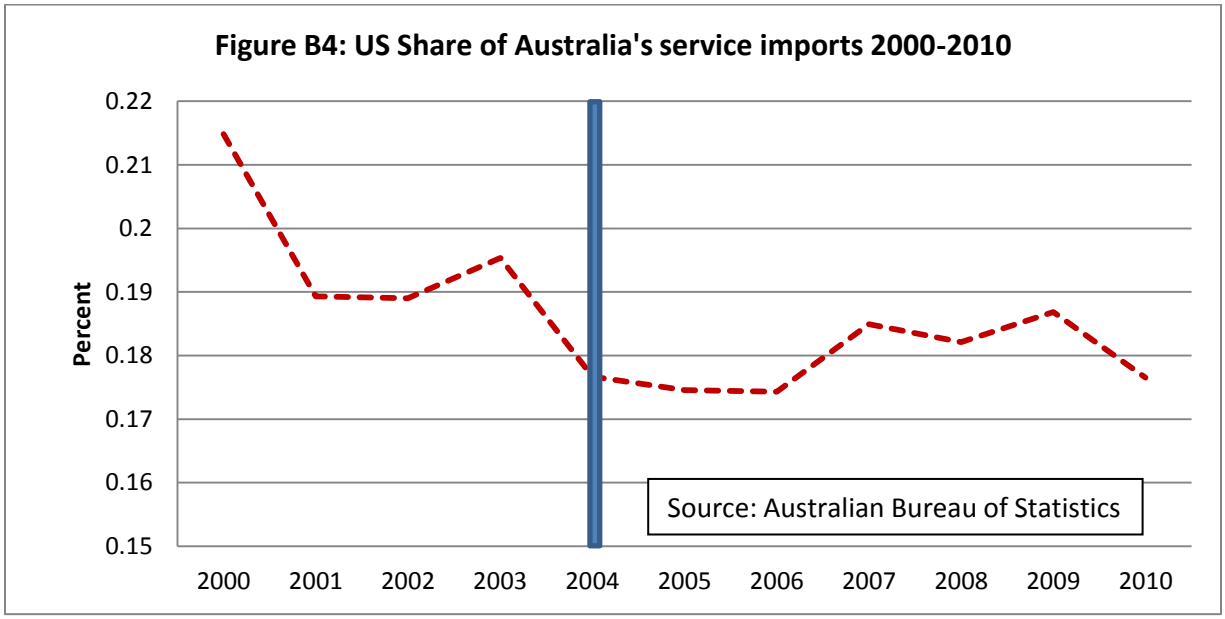


Figure B4: US Share of Australia's service imports 2000-2010
Percent
0.22
0.21
0.2
0.19
0.18
0.17
0.16
0.15
Source: Australian Bureau of Statistics
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010

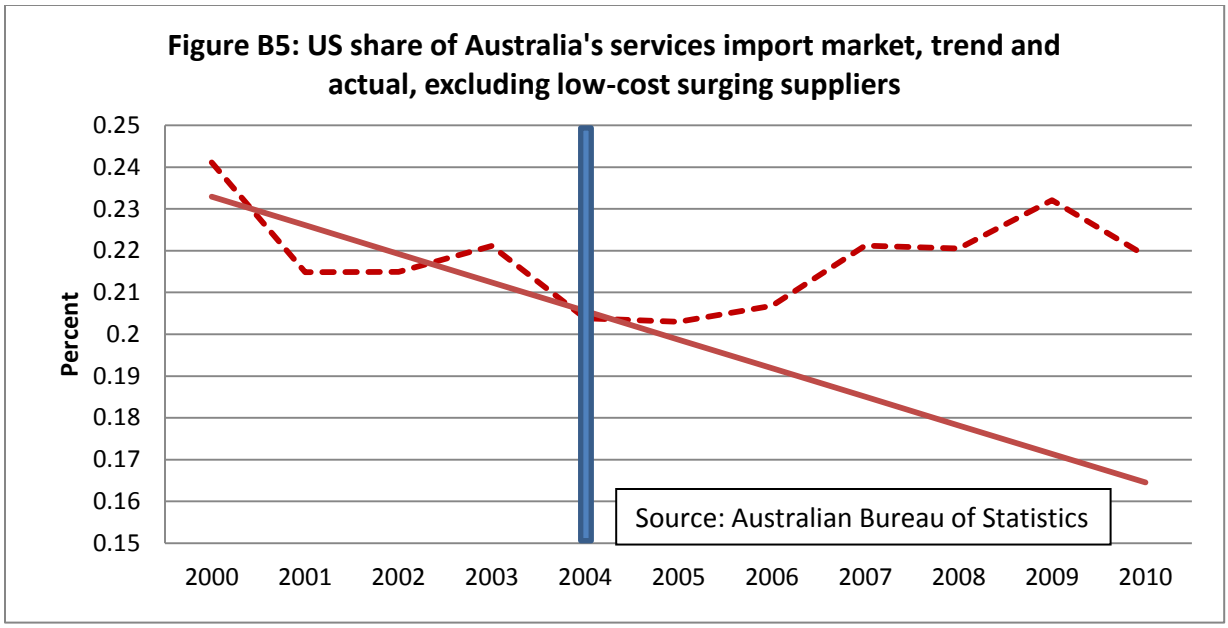


Figure B5: US share of Australia's services import market, trend and actual, excluding low-cost surging suppliers
Percent
0.25
0.24
0.23
0.22
0.21
0.2
0.19
0.18
0.17
0.16
0.15
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
Source: Australian Bureau of Statistics

ANNEX C: SUMMARY OF SURVEY OF BUSINESS INTEREST

The *Survey of Canadian Business Interest in Australia* was launched on November 9, 2011 in order to capture Canadian business interests and challenges in the Australian market. The survey is comprised of nine questions that relate to a firm's interests and profile; a list of the survey questions is provided at the end of this summary.

The number of responses received was low, in all only ten. Based on feedback from some firms, this may reflect the difficulty that firms found in relating their business experience to the policy-oriented questions. While the total number of responses received is too few to provide statistically significant inferences, there remains some value in the raw data. A description of them is provided below.

Responses were received from the agricultural/fishery, manufacturing, financial services and "other business services" sectors. These firms ranged in size from less than twenty employees to five hundred of more. Five of the firms are headquartered in Ontario, three in British Columbia, and one each in Saskatchewan and Alberta. All of these firms are active in other markets, including the US, NAFTA, Europe, East Asia, and other markets through direct investment and exports; three firms drew on supply chain inputs from other markets.

In regards to the Australian market, six of the respondents currently have a representative office in Australia. Responding firms export goods and services, licence production of their goods to an Australian company, purchase services from an Australian company, or have a subsidiary or joint venture in Australia. The only form of business relationship not represented was a Canadian firm obtaining a license for intellectual property produced in Australia.

For one-third of firms, Australia is viewed as a single market in their global business strategy; however four firms view Australia as part of the Southeast Asian market and one respondent positioned Australia as a location from which to manage business in Southeast Asia.

Against this diversified background, responding firms identified the following factors as hindering their ability to serve the Australian market.

- Eight firms identified the elimination of tariffs and the modernization of the bilateral tax agreement as being extremely or very important to expanding their business in Australia.
- Seven firms identified lower air fares and more convenient connections for business travel between Australia and Canada as being important obstacles to conducting business with Australia.
- Six firms identified investment barriers and cost of shipping as important impediments.
- Five firms identified mutual recognition of product standards and facilitation of termporary entry by business personnel as important factors.
- Four firms identified mutual recognition of qualifications of professional staff
- The one firm in the agricultural sector identified facilitation in quarantine management systems (SPS) as important.
- Other factors identified include burdensome import/export regulation and tariffs on used machinery as the reasons for abandoning previous attempts to enter the Australian market.

A Survey of Canadian Business Interest in Australia (Survey Questions)

1. Does your firm have an active business interest in Australia?
2. How does Australia fit into your firm's global business strategy?
3. Which of the following would be important in helping your firm to expand its business with Australia or create interest in entering the Australian market?
    a. Elimination of tariffs on Canada-Australia trade
    b. Lower cost and more convenient shipping alternative
    c. Removal of impediments to direct investment (e.g. screening test, requirement to show net benefit, restriction on use of foreign personnel)
    d. Facilitation in quarantine management (SPS)
    e. Facilitation of temporary entry of business persons
    f. Mutual recognition of qualifications of professional staff
    g. Lower air fares and more convenient connections for business travel between Australia and Canada
    h. Mutual recognition of standards for introducing new products
    i. Modernization of the bilateral tax agreements
4. If your firm had business interest in Australia in the past but abandoned them, which of the following factors were instrumental
    a. Increased competition from Asian emerging markets such as China
    b. Loss of customers to US rivals as a result of the Australia-US free trade agreement
    c. Loss of customers to other rivals as a result of Australia's free trade agreements with other countries
    d. Australian regulations raised costs of participation in the Australian market
    e. Exchange rate shifts undermined profitability of doing business with Australia
    f. Transportation cost increases raised the cost of doing business with Australia
    g. Other
5. If your firm has ever been frustrated in attempting to export to or invest in Australia, or in trying to establish supply chain relations with Australian suppliers, please describe the problems that you encountered
6. Is your firm engaged in other international markets?
    a. United States
    b. NAFTA
    c. Europe
    d. East Asia
    e. Other
7. What is the principal sector in which your firm is active?
    a. Agriculture or Fishery
    b. Forestry
    c. Oil and Gas
    d. Mining
    e. Manufacturing
    f. Financial Services
    g. Other

8. How many employees does your firm employ?
    a. Less than 20
    b. 20 to 99
    c. 100 to 499
    d. 500 or more
9. In which province is your firm headquartered?