

***China's Future Diplomacy  
Research and Public Symposium***

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***Chinese approaches to negotiation  
Implications of contemporary practices for the  
future***

***An "outside" perspective***

***(Speaking Notes only)***


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## ***Introduction***

I do not claim any expert knowledge of contemporary Chinese diplomacy. Nor, specifically, of contemporary Chinese negotiating methods or styles. I offer merely a few observations, and insights, from my perspective as Executive Director of the Australian Services Roundtable. The Australian Services Roundtable is the peak industry body in Australia for the services sector. My remarks today reflect my ongoing experience as a practitioner, at industry level, of what is commonly called, these days “economic diplomacy” and more specifically in my own case, ‘trade diplomacy’. The thought that an industry representative can be involved in ‘trade diplomacy’ might strike some of you as somewhat unusual, the thought is that it is no longer only governments that conduct diplomacy. But this is actually central to my thesis so I want to emphasise it from the outset.

What I mean, for the purposes of this paper, by ‘economic diplomacy’ is simply the conduct of international economic relations.

 *the process of influencing the policy making of other Governments or influencing the regulatory decision-making of international institutions with respect to international economic issues (such as trade in goods and services, investment, financial flows, information technology flows, labour movements).*

 *Obviously there are many different aspects to the practice of economic diplomacy and negotiation is only one; for any negotiation to be successful, however, negotiating activities and negotiating skills need to be coupled with a variety of other activities and skills, including preparatory research and analysis, policy formulation, decision-making, internal bureaucratic coordination and domestic and international stakeholder consultation and advocacy.*

I wanted, for the purposes of this paper, to consider two contemporary case studies; one case study in ‘trade diplomacy’, namely the case of the trade

negotiations currently underway for a China/Australia Free Trade Agreement currently and, more briefly, one case study in what might more properly be labeled as ‘commercial diplomacy’, namely the case of the commercial price negotiations just completed between steel mills in China and Japan and Australian iron ore suppliers, RioTinto and BHP Billiton. Unfortunately, these latter negotiations have proved relatively impenetrable for commercial –in confidence reasons. So although I will draw wherever possible in my final paper from anecdotal evidence in relation to these commercial negotiations, my focus today is on the Free Trade Agreement (FTA) negotiations.

Both China and Australia are currently negotiating FTAs with a number of bilateral partners. China is negotiating for example with the Gulf Cooperation Council and with ASEAN and Chile – these latter two are both ‘works in progress’ which have delivered early harvests but have not yet covered all relevant issues. China has clear potential interests in negotiating FTA or FTA –type agreements with a large number of other strategic trading partners. My paper focuses only on the single particular example of the FTA negotiations with Australia, and necessarily as an ‘outsider’ not only with respect to China but with respect to both parties to these negotiations. The fact that as an industry representative I know anything at all about these negotiations is proof of one very important aspect of contemporary trade negotiations ie they are necessarily very much more open and transparent to domestic stakeholders than in the past. This is an important point and one to which I will return. I should note that my research included personal interviews to obtain the views on this matter of some of Australia’s own key FTA negotiators.

**What is required to negotiate an FTA effectively – and are contemporary Chinese negotiating styles and methods likely to be working effectively in support of China’s FTA objectives?**

Although most FTA negotiations seem largely politically motivated, they are in fact serious commercial negotiations affecting the entire economy and subject to binding WTO disciplines (and to non-binding APEC guiding principles.). WTO disciplines require that the FTA partners move to zero tariffs on trade in goods over a period of no more than 10 years and that the FTA cover, for trade in goods, ‘substantially all trade’ in ‘substantially all sectors’. For trade in services, the rules require coverage of substantially all services sub-sectors and all modes of supply ie all means of delivering

services. I need to explain quickly that one common means of delivering a services overseas involves opening up an office in that overseas market – this is a form of investment – so the FTA is obliged to cover certain aspects also of investment regimes. So FTA partners have to get as close as possible to removing all tariffs on all goods and to facilitating bilateral trade and investment in most services industries. That is what an FTA is. So it obviously is going to affect the entire domestic economy.

So an FTA negotiation is obviously going to require a great deal of **preparation** to properly identify all of a country's negotiating interests and priorities. Long before official government 'diplomats' sit down to negotiate, a great deal of prior domestic homework has to be undertaken – and other kinds of negotiations have to take place.

**This, it seems, is one area where China still has some way to go in learning how to make its internal practices more effective.**

First, to obtain domestic political support, most FTAs can not be undertaken without intensive economic research, including economic modelling work, to identify the potential economic costs and benefits as well as the political and strategic impacts. On this front, China seems well equipped. This preliminary research provides key information to the process of identifying one's own national interests and formulating, eventually, a formal negotiating mandate.

Second, a process of intensive internal bureaucratic consultation and coordination needs to take place to ensure that all domestic interests are taken into account and an 'all-of-government-approach' is achieved. After the WTO accession process, MOFCOM now seems to be highly skilled in this arena.

*But* as already explained, an FTA negotiation may require an even deeper level of bureaucratic coordination than the WTO. Depending on how open the services sector already is or is not, for example, the FTA could require new commitments that go well beyond the WTO. Which typically means, for a developing country, that the number of Ministries and government agencies, and the number of provincial and local government entities that need to be consulted and involved is potentially much greater. New committees may need to be formed to allow this process to take place. Anecdotal evidence abounds which suggests that this is an FTA negotiating

reality which China has experienced severe infrastructural difficulties in grasping. The necessary consultative inter-Ministry processes simply don't always exist. Cross –Ministry dialogue in China is still relatively constrained and policy making still tends to take place in independent silos.

Third, an effective process is also required, of consultation with non-government stakeholders, including NGOs and of course, local industry representatives. This is a critical element in identifying a country's offensive and defensive commercial interests. Where defensive interests are identified, contingency plans may need to be drawn up to accommodate any potential domestic losers. This is a critical element in ensuring that any FTA deal will have a high degree of domestic public acceptance.

This stakeholder consultation process therefore involves, in addition, an important element of domestic advocacy. China has handled this aspect well in the case of the WTO. But may be neglecting to put in an equivalent effort into advocacy for its FTA negotiations.

Advocacy, which must begin at home with the local community, also needs to take place in the bilateral partner country, to ensure that once agreed, the FTA is to be acceptable domestically in both countries. Until the recent visit of Premier Wen to Australia, China seemed to have got away with largely leaving advocacy in Australia of the Australia/China FTA to the Australian Government to handle. This was largely the case in the lead up to commencement of the negotiations, when China sought, as a pre-condition for FTA negotiations, acceptance by Australia of China's status as a developing economy for anti-dumping purposes. And it still seems largely true, with Chinese Embassy public commentary focused more on delivering a message regarding China's sensitivities in for example agriculture, than on any advantages of an FTA for the Australian industry audience. This contrast markedly with the Australian Government's very very active FTA advocacy effort underway inside China. And it contrasts with other countries' FTA advocacy efforts inside Australia. But China can not take public support in Australia for an FTA with China for granted. Indeed, far from it. If China has indeed identified critical commercial interests for these negotiations (and it may actually be the case that it has not – and we will come to that possibility in a moment), then China needs, in my view, to devote more diplomatic effort to positive engagement with the wider Australian business community. If not, China risks having an incomplete

understanding of all of the factors driving its negotiating partner, including of course, important political factors.

The next step in the preparatory process is to allocate sufficient resources and form a dedicated negotiating team. On this front, MOFCOM seems to be doing well. Though appointment of the Lead negotiator took place only after the first official 'round' of negotiations in Sydney. And the negotiating team is stretched. Even though there is a separate Lead negotiator for China's FTA negotiations with New Zealand for example, much of the rest of the team is the same and some problems have arisen resourcing both negotiations more or less simultaneously.

Next you need a negotiating mandate. Well it wasn't clear for quite a while that the Chinese negotiators knew exactly what they wanted. Draft text on maybe as much as 75 percent of the proposed structure was tabled at the last negotiating round in Beijing in May. But all of it was drafted by Australia. To an 'outsider' that does not look even remotely 'prepared'. (Even the UAE, during the FTA negotiations with Australia, which have now ceased due to GCC constraints on the UAE, tabled its own draft versions of certain chapters.) China has taken oral positions on the structure of the FTA Agreement, (positions sometimes diametrically opposed to the Australian positions), but China seems to have difficulty committing quickly to written text. This is a great potential negotiating strength. It can also a great potential negotiating weakness. Because it limits China's ability to take the lead with the written word and thereby influence the internal structure of the Agreement. Unlike the United States, Australia does not have an FTA template. Which means China did have, but has now effectively lost, the opportunity to table text.

Let me come back, for a moment, to the positions which China reportedly has been expressing about the structure of the text. Chiefly I am referring to reports that China does not want certain Chapters. I will explain in my longer written paper (or during the discussion period, should time suffice) why these positions may not in fact be helpful to China in maximizing its own domestic economic gains from an FTA and why they demonstrate to an 'outsider' an apparent lack of understanding in China of what, from an OECD country's perspective, a modern FTA in a globalised world economy is all about. And to my mind, this may be further evidence, perhaps, of lack of real internal preparedness for these negotiations. It is also, in itself, of course, a negotiating tactic. But not one, in my view, though others may see

it differently, which is likely ultimately to work to China's advantage. Because it could limit significantly the opportunities available for China to optimize its economic benefits from a deal.

[ Box: The Tables of Contents of most recent FTAs involving OECD countries show that Services-related issues and 'WTO plus' issues dominate the FTA negotiating agenda. Interalia this is because most modelling work assessing the economic impact of any particular FTA shows, despite problems of measurement, that the potential domestic economic gains from liberalising services and investment are stronger than the gains from liberalising trade in goods. Neither Services issues nor WTO plus issues such as Investment or Competition Policy can realistically be avoided in any FTA negotiation with a developed economy. And in Australia's case, it is the Services sector where nearly all the gains from an FTA with China are likely to accrue.]

So how prepared is China for the next critical step in the negotiating process; the exchange of market access offers. The next negotiating session, In September in Beijing, will see the first exchange of offers on Goods – agriculture and manufactures. Reportedly China is indeed ready for this next step. Partly because China's trade negotiators understand the WTO extremely well and in the realm of Goods trade, things are relatively familiar in the FTA context. Indeed, informal official reports of the negotiations to date suggest that the Chinese negotiators close understanding of the WTO is actually problematic from the perspective of Australia's negotiators because it is unduly constraining China's negotiating style in the FTA. There is a sense that China has learned the WTO model over the ten year accession process and that China is now a bit stuck on that model which is seen as 'safe'. This rigidity is reportedly limiting significantly the Chinese negotiator's ability to see things 'outside the WTO box' which may mean that China might ultimately gain less than it could from the negotiation.

This is major problem when we leave the realm of Goods and Goods-related issues (such as customs, rules of origin, sanitary and phyto-sanitary measures etc) and consider all the newer issues on the international trade agenda, such as Services, Investment, Competition Policy, Intellectual Property, E-Commerce etc. Reports from the negotiations suggest that China is, to be blunt, badly under prepared in these areas – or at least wishes to appear so. And this is likely to be equally true when it comes to

negotiating matters such as Enforcement of Implementation (eg at local and provincial level) and consequent Dispute Settlement.

With respect to Services, the negotiations are literally, from the perspective of the Australian Services Roundtable, facing serious difficulties. Despite signalling that China has identified a few offensive services interests of its own, China has not yet demonstrated any readiness to actually engage. This is a systemic issue, and has nothing whatsoever to do with individual negotiators. And it is significant because unless things improve, there is no doubt that this would be reason enough for Australian industry to call for a freeze to the negotiations on Goods until Services catches up.

It's a delicate point, but right now, one could argue I suppose that China appears to have the upper hand, in that, despite the obvious major problems with Services, the negotiations on Goods have not been frozen. But Australian services industries are very alert to the situation and will not sit back and be passive if their interests are not addressed.

Which leads me to another potential weakness in China's overall position. There is, for example, no counterpart business organization in China for the services sector. There is no counterpart body which can engage patiently with Australian services industry to help reduce the potential level of frustration and misunderstanding. To engage effectively in international economic diplomacy, China needs, in my view, to foster greater industry to industry interaction. Industry is, these days, an important actor in economic diplomacy. And China needs more of its own actors out there.

I have made it clear that I see a number of significant limitations in China's preparedness for international negotiation. What happens, then when China actually gets to the negotiating table itself.

China is of course renowned historically for its international negotiating skills and its negotiating successes. And China is clearly able to learn and adapt as it goes. The question, for the case study I have chosen, is specifically whether the internal political and infrastructural impetus can be provided quickly enough to achieve what is really required for a successful, mutually advantageous FTA outcome with Australia.

Australia is providing to MOFCOM, through Ausaid, a simultaneous 12 month long programme of teaching FTA negotiating skills. This programme

has its critics! As if Australia has anything to teach China on the negotiating front! On the other hand, given the FTA negotiating evidence to date, perhaps we have? Personally, I suspect that this technical assistance is in fact very useful to China and hopefully will assist China to assert a stronger leadership role in best practice FTA negotiation in the region.

At the end of the day, effective FTA negotiation is all about pursuit of ones own national interests while understanding what is motivating your partner. China is the world's fastest growing and potentially largest economy. Australia is a medium player. What does a bilateral partner like Australia want from China. Obviously Australian industry wants access to the huge, rapidly growing Chinese consumer market. Today it's a sign of a successful business if you export to the US. But everyone knows that you'll be out of business altogether tomorrow if youre not starting to think about exporting to China. As the Vice Chancellor Ian Chub said yesterday evening in his opening remarks, Australia's interest lies in seeing China grow richer, increasing Chinese demand for everything, including Australian goods and services.

### **Implications for the Future**

Some of the previous speakers have explained how China's foreign policy goals have shifted in recent years. Other speakers have shown how China has become much more active internationally and much more creative in its international activity. The question I asked is whether China has sufficient new diplomatic resources to devote to these activities and appropriate new diplomatic techniques.

My case study suggests that China still has a lot of work to do to ensure that its negotiating styles and methods remain adequately adapted, in a fast globalizing world economy, to ensure it can achieve its objectives in bilateral economic diplomacy. In particular, there is some evidence to suggest that contemporary bureaucratic consultation and coordination practices inside China are not yet sufficiently sophisticated to do full justice in the international arena to Chinas various new international negotiating objectives. China needs to move more rapidly to adopt more modern, more inclusive approaches to 'all-of-government' economic diplomacy, engaging in a more consultative fashion with a wider range of domestic stakeholders.

In trade policy, over a period of ten years to WTO accession, China has learned the WTO multilateral model and learned it well. If China now wishes to engage truly successfully in bilateral trade diplomacy, its time to take inspiration and bring some new creative energy to bear.