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HD **Industry Insight Industry comment by Peter McGregor Managing Director, Industrials, Food , Beverage and Agriculture Commonwealth Bank**

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The signing of the **China** Australia Free Trade Agreement in November, and also the announcement that Australia would operate as a settlement hub for renminbi (RMB) trading, demonstrate how enmeshed the economic relationship between the two countries is becoming.

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When it comes to trade relations between the two countries, the attraction is mutual. Australia is the second highest and second most attractive destination for **Chinese** investment, worth almost $70.1 **billion** in 2013.

The deep links created by these investment levels provide a strong growth platform for businesses in both countries, and the FTA will only help to further bolster those relationships.

While the FTA has potentially a very significant impact on many sectors, the opportunities for Australian agribusiness are enormous. Indeed even before the FTA, the global macro-cycle was already advantageous.

Consider this. **China** has 19 per cent of the world's population but less than 10 per cent of the world's arable land. That, combined with growing wealth and the huge increase in the **Chinese** middle class, is driving changing consumption patterns in ways favourable to our local producers.

Michael Workman, Director Economics, Commonwealth Bank, commented, "**China** is our biggest trading partner and it is also the one with the most significant growth potential. Over the next 10 to 15 years, middle income households in **China** are set to double or even triple in size, assuming the economy keeps moving along the track it has followed for last five to 10 years."

That is good news for Australian food producers, given middle income households in **China** tend to consume a lot more of the types of products they develop. Those products tend to be protein based around grains, **dairy** products and of course seafood.

In fact, the FTA with **China** is the third of its kind in recent times, following similar agreements with Japan and South Korea. Those three markets account for 60 per cent of Australia's exports, and together they will drive demand for Australia's food beverage and agriculture exports.

There was another significant announcement in November, with broad implications for bilateral trade between Australia and **China**, and that was the establishment of Sydney as an RMB settlement hub with Commonwealth Bank acting as a foundation member of the Australia RMB working **group** that helped facilitate the initiative.

The settlement hub will greatly increase cross border RMB denominated capital flows, increase RMB liquidity in Australia and help with product innovation in relation to the **Chinese** currency. RMB continues to grow in importance when it comes to global trade says Sangeeta Venkatesan, Global Foreign Exchange Chief Operating Officer at the Commonwealth Bank.

"The ability to trade in RMB more efficiently has big implications for Australian **business**.

"Now that we have the settlement hub we can think of more innovative ways to use the RMB as a product and also provides more direct access to the market in **China**. In fact, we have recently launched RMB dealing on our electronic portal, Commbiz Markets. This enables clients to **buy** and sell the currency electronically, providing a more efficient and seamless settlement process," says Ms Venkatesan.

"By using RMB for cross border trade, companies can negotiate better pricing arrangements with suppliers or trade partners in **China**. They can also access a wider array of suppliers or counter parties in **China**, since many companies there can't receive funds in $US or $A and must rely on the RMB."

For Australian food, beverage and agriculture exporters these two announcements mean better market access and more effective and efficient tools for trade, further strengthening the trade relationship with **China**.

As trade links become more embedded over time, companies need to appreciate the opportunities and risks, and understand what they can do to mitigate them.

The first thing to realise is that while the FTA and RMB settlement hub are substantial advancements in trade relations, they alone will not guarantee success. For starters, tariffs will not all come off immediately. For many products, tariffs will gradually be removed over the next four to nine years, so those expecting an immediate uptick in trade volumes may be disappointed.

Instead, production capacity needs to build up gradually and consistently over the next four to five years as the export market opens up.

Simply increasing capacity in the hope of acquiring additional markets offshore is the wrong approach in such a highly competitive environment. Moreover, establishing relationships in the region and finding the right partners and customers is paramount when developing and implementing an export strategy.

There are also other elements for exporters to consider, not least of all the competitive landscape.

Companies looking to break into this highly competitive market need to consider how they are going to dislodge incumbents. They need to understand their own unique selling proposition and also that of their competitors.

In addition, there are other fundamental perils to be aware of, such as cross-border and counter-party risk.

As Adnan Ghani, Executive Director Global Head of Trade Products, Commonwealth Bank, notes: "Companies want to get paid at the end of the day and they may fear that while they can export the goods, there may be some challenges in getting the money out in dollars."

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