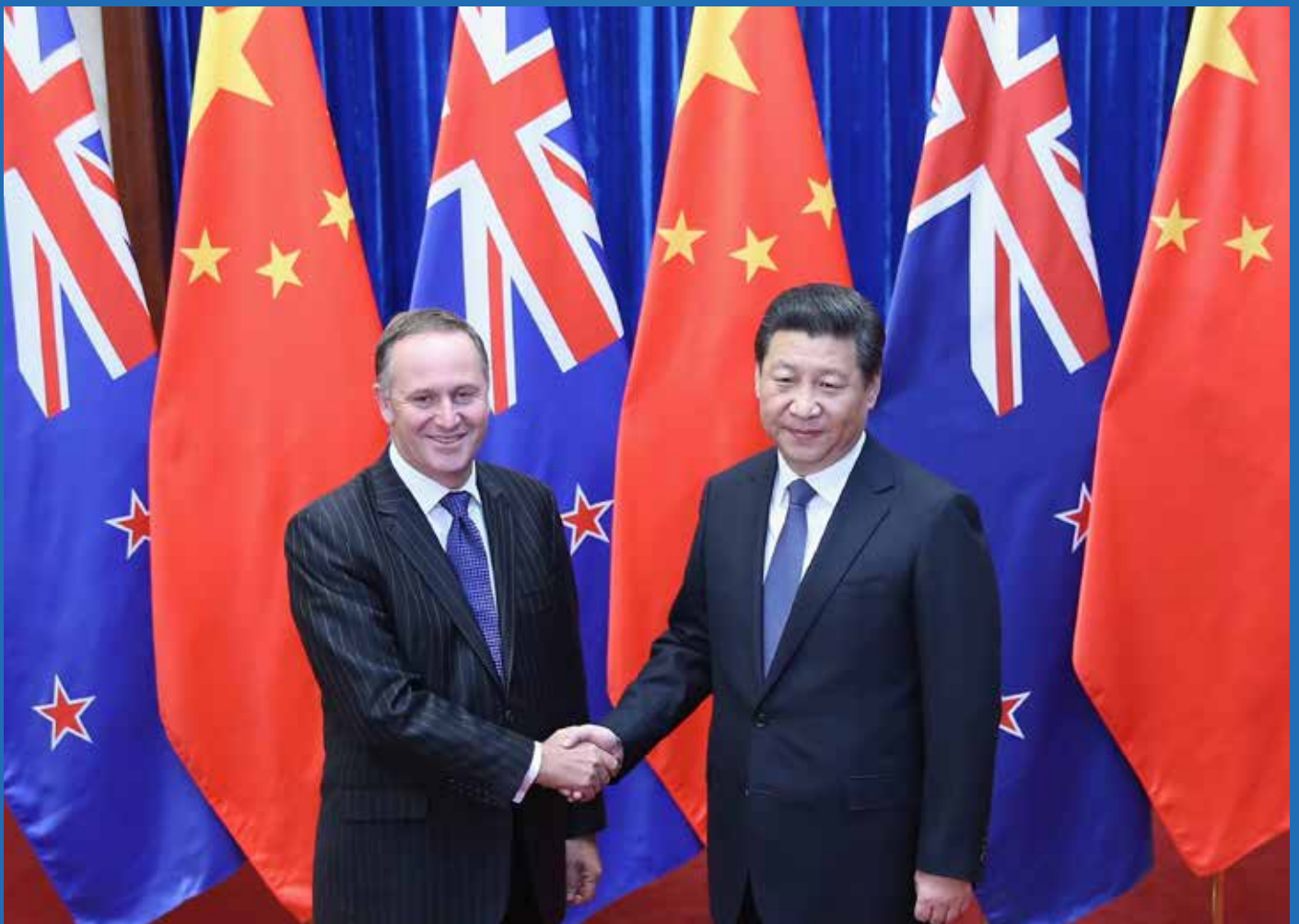


# NEW ZEALAND'S CHINA POLICY

Building a Comprehensive Strategic Partnership

July 2015



**FRONT COVER IMAGE:**

Chinese President Xi Jinping shakes hands with New Zealand's Prime Minister John Key at the Great Hall of the People in Beijing, March 19 2014.

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Published by the  
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ISBN 978-0-9942825-1-4

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## ACKNOWLEDGEMENTS

The New Zealand Contemporary China Research Centre would like to thank Professor the Honourable Bob Carr, Director of the Australia-China Relations Institute, for commissioning the project and Dr John Larkindale as the primary author of this policy brief. Our acknowledgements also go to Mr Tony Browne, Dr Andrew Butcher, Professor James Laurenceson, Dr Jim Rolfe and Dr Jason Young for their contributions and comments.

## EXECUTIVE SUMMARY

New Zealand has been building a comprehensive strategic partnership with China. Strong political relations are a platform for growing trade and economic links, positive people-to-people exchanges and cooperation with China in regional forums. New Zealand's strategy toward China has been consistent and bipartisan. The relationship has never become a topic for partisan political division, though elements of China's growing presence in New Zealand and aspects of the economic links are increasingly attracting debate, and sometimes controversy. China looms large in New Zealanders' awareness of international influences on their wellbeing. New Zealand is proud of being the first OECD country to secure a free trade agreement (FTA) with China in 2008. That agreement marked a significant spurt in New Zealand's economic relationship and has changed New Zealanders' perceptions of where their economic future now lies. Today, China has become New Zealand's first or second export market and an important source of investment, immigrants, students and tourists.

New Zealand had few links with China from pre-colonial times and there was comparatively little of significant substance in the relationship until the agreement to enter into formal diplomatic relations in December 1972. That new diplomatic relationship grew from a narrow political base, with trade links a lesser driver, although it was recognised then that a sound political relationship would influence how trade and economic links might ultimately develop. It was also understood from the outset that New Zealand's interest in China would rate relatively higher than China's in New Zealand. From the mid-1980s, New Zealand has worked to build a concerted whole-of-government strategic approach to guide the relationship. Successive incoming governments have adopted the same broad policies. They have understood the asymmetry of the relationship and the need for New Zealand to be proactive to provide China with a value proposition.

New Zealand's relationship with China stands out in that China is the only one of New Zealand's major political and economic partners with which it does not share an entrenched liberal democratic tradition or

*It was also understood from the outset that New Zealand's interest in China would rate relatively higher than China's in New Zealand. From the mid-1980s, New Zealand has worked to build a concerted whole-of-government strategic approach to guide the relationship.*

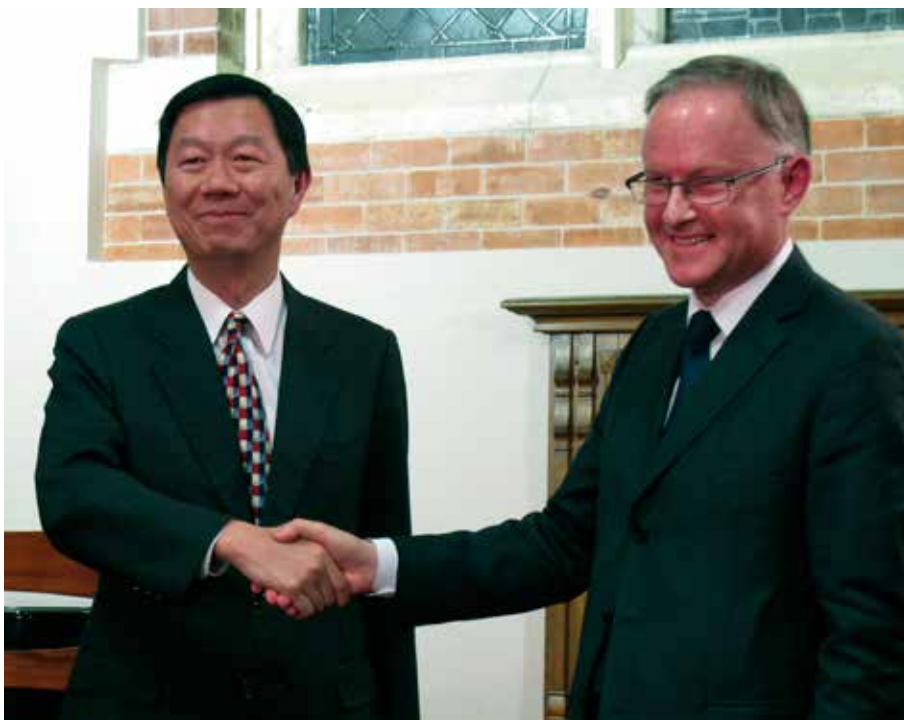
defence and security links. New Zealand has intrigued China. As a Western country that does not fall easily into Chinese assumptions about Western attitudes and policies, China has found room to explore opportunities in the relationship that are not easily replicated with others. Its leaders have almost all made early visits to New Zealand. It has responded positively to the long-held policy in New Zealand that it was in New Zealand's interests for China to become an active participant in as many relevant international and regional institutions as possible. New Zealand has openly embraced a 'no surprises' relationship, raising 'difficult' topics away from public scrutiny and bringing the relationship with China into the enunciation of what an independent foreign policy means in practice.

In 1997 New Zealand became the first Western country to conclude a bilateral agreement on China's accession to the World Trade Organization (WTO), the first of several 'firsts', all of which have emanated from calculations about the relative weight to be given to assessments of national interest as against the comfort of 'like-minded' positions. New Zealand's ability to respond quickly and to act independently gave it the leverage to conclude an agreement with China that was more favourable than would otherwise have been the case. Three more 'firsts' followed: recognition of China as a market economy, the first developed country to enter into negotiations for an FTA and the first to sign a high-quality, comprehensive and balanced FTA with China. Chinese leaders have taken to endorsing the relationship in very positive terms – 'the best it has ever been', a 'model for a relationship between a developed and a developing country' and so on. The importance of the relationship to China was recognised by President Xi Jinping who, with Prime Minister John Key in November 2014, characterised it as a 'comprehensive strategic partnership'.

While New Zealand and China do not see the world the same way, the relationship has been managed so that only rarely do their interests around the world rub against each other. New Zealand's economic wellbeing is reliant upon a benign global and regional security environment. New Zealand views on the South China Sea, on the Air Defence Identification Zone (ADIZ) issue and the East China Sea have seen clear differences from China's, but equally have not bound

it to positions that China has considered inimical to its interests. In the South Pacific, of strong and immediate interest to New Zealand, China's presence is seen as being in line with its expanded presence elsewhere and broadly commensurate with its growing political and economic weight.

China's increasing military capabilities do not impact directly on New Zealand, but are nevertheless an important component of the regional security environment. These capabilities are understandable, and New Zealand works actively with China to encourage it to act constructively on international and regional security issues.



Taipei Economic and Cultural Office Representative Elliott Charng, left, and New Zealand's Director of the Commerce and Industry Office Stephen Payton sign a free trade agreement Wellington, New Zealand, July 10 2013

AP Photo

The flexibility and hard diplomatic graft that saw New Zealand become the first OECD country to sign an FTA with China continued beyond 2008 with New Zealand concluding FTAs (using flexible nomenclature) with both Hong Kong and Taiwan – the only OECD country to do so.

New Zealand's exports to China have grown from less than three percent of total exports in 2000 to around 20 percent in 2014. Yet as a share of China's total imports there has been scarcely any change over the past 40 years. Similarly, New Zealand's relative importance as



a destination for China's exports is largely unchanged. New Zealand remains heavily dependent on the primary sector for its exports and although it is not unduly exposed to overdependence on China, the fact that so many other of its major trading partners count China as their most important (or close to it) partner does suggest an indirect vulnerability to economic developments in China.

Chinese investment in New Zealand has become somewhat controversial, particularly in respect of farmland. New Zealand's non-discriminatory overseas investment regime has seen Chinese investment grow steadily to reach little more than five percent of all overseas investment. New Zealand's legislation does not treat State Owned Enterprises (SOEs) differently from other potential overseas investors. The Overseas Investment Office (OIO) screens investments in 'sensitive land' and all those above NZ\$100 million. Overseas investment in residential property, when not triggered by the overseas investment regulations, is subject to the same regulations as investment by New Zealanders. The Shanghai Pengxin purchase of New Zealand farmland was challenged twice in court. The High Court overturned the approval given by ministers on the basis of advice received from the OIO, citing the legal provision that the benefit to New Zealand from overseas investment must be 'substantive and identifiable'. In so doing, the court ruled that the comparison should not be between the current state of the asset and what might be done by a new overseas owner to improve that asset, but rather that the test should be whether the benefit from an overseas owner would outstrip that which a domestic owner might be expected to achieve. As a major source of capital for capital-poor New Zealand, the trend of increasing Chinese investment is likely to continue. New Zealand investment in China is unduly low given the strength of the overall trade and economic relationship but this is not unique to New Zealand's China relationship.

Chinese students in New Zealand remain an important component of the international education business. Numbers are markedly less than in the damaging boom and bust environment of the early 2000s but are picking up steadily. Overall, however, New Zealand is still attracting relatively fewer students than other English-speaking destinations. By contrast, the number of Chinese visitors coming to

New Zealand has increased significantly with China now being second only to Australia as the largest source of tourists.

Socially, China and Chinese have become an increasingly prominent part of life in New Zealand. The presence of a growing Chinese community is part of a much wider picture of rapid social change, with over 25 percent of the population now being born outside New Zealand. But New Zealanders have found it harder to make the adjustments required for a society whose future is inextricably tied to its links with Asia, and with China in particular. The teaching of Chinese language in New Zealand remains seriously underdeveloped.

In sum, starting with a narrow political base in 1972, New Zealand has managed to build a comprehensive strategic partnership with China based on consistent, pragmatic and proactive policies.

## THE HISTORICAL CONTEXT

New Zealand's relationship with China has developed since the establishment of the People's Republic of China (PRC) and, in particular, since the agreement to enter into formal diplomatic relations in December 1972. The initial focus was very much on developing political relations, with trade links a lesser driver, although it was recognised that a sound political relationship would influence how trade and economic links might ultimately develop. It was also understood from the outset that New Zealand's interest in China would rate relatively higher than China's in New Zealand and that this factor would necessarily determine how New Zealand sought to manage the relationship. By the mid-1980s New Zealand had concluded that its relationship with China needed to be built on the premise that China's modernisation programme would largely succeed and that it was in New Zealand's interest that it do so. This led to the introduction of a whole-of-government coordinated strategic approach to guide the developing relationship, an approach that has largely been followed to this day.

A focus on China is nothing new for New Zealand. In pre-colonial times China was for a while New Zealand's largest export destination, mainly through the importance of Guangzhou as a market for sealskins. That market duly collapsed and the pattern of New Zealand's engagement with China in the 19th and early part of the 20th centuries largely paralleled that of the other English-speaking countries of the Pacific (Australia, Canada and the United States): some trade, but not much; some immigration during the respective gold rushes, but not too much and highly controlled; and a large measure of concern driven by racial prejudice about an ill-understood culture and people resulting in punitive legislative measures (the poll tax in particular) to ensure that numbers resident in New Zealand could be kept under tight control.

In the first part of the 20th century there were some desultory attempts by the New Zealand Government to explore the potential of trade links with China but these came to little and little attention was given to events in China. One notable exception, however, was

the relatively strong New Zealand missionary presence in China prior to World War II. Their work focused not only on the evangelical but also on social reform, seeking to improve the lives of those in the communities where they lived. Importantly, this required fund-raising back home, and their newsletters and information material had an impact on a changing view of New Zealanders towards China and the Chinese. In particular, following the Japanese incursions into China in the 1930s, public sentiment in New Zealand became more favourable towards the Chinese.

At an official level, attitudes were changing too. The advent of the Labour Government in 1935 led to New Zealand adopting a more assertive role in foreign policy with a particular emphasis on the League of Nations. Japan's actions in China were seen as a challenge to the principles of the League and in 1937 and 1938 New Zealand was prepared to advocate in support of China's position much more strongly than Britain and the other Dominions.<sup>1</sup> An interesting echo of this is that one of the reasons advanced by the then Chinese Government in late 1945 for its proposal (which was not followed up) that the two countries should exchange diplomatic representatives was that it regarded New Zealand as the most progressive of the 'British nations'.<sup>2</sup>

Following the establishment of the People's Republic of China in October 1949, the question of New Zealand recognising the new Government needed to be addressed. A number of considerations had to be weighed up but by December 1949 the balance of the argument was shifting towards recognition.<sup>3</sup> However, the new National Government that came to power following the general election that year required time to formulate its position, and external events (in particular the Korean War and the UN's declaration that China was an aggressor) changed the calculus and recognition was withheld. Over the next two decades opinion on the subject in official circles was not monolithic but circumstances were never judged to be such as to support recognition.

<sup>1</sup> C J Elder and M F Green, 'New Zealand and China 1792-1972', a paper presented to the *21st Otago Foreign Policy School*, 1986, pp. 28-29.

<sup>2</sup> *Ibid.*, p. 31.

<sup>3</sup> *Ibid.*, p. 48.

That had to await the advent of Norman Kirk's Labour Government in December 1972. Following the admission of the PRC to the United Nations in 1971, the previous National administration had been seeking a way of accommodating the two imperatives (as it saw them) of accepting the irrevocable move by most of the international community away from Taipei towards Beijing while also not reneging on its previous support for Taiwan. The incoming Labour Government quickly accepted that these two goals were irreconcilable and one day after Australia's move to recognise Beijing announced its own switch to the PRC. The key clauses in the brief communiqué announcing the establishment of diplomatic relations were:

The Chinese Government reaffirms that Taiwan is an inalienable part of the territory of the People's Republic of China and that Taiwan is a province of the People's Republic of China. The New Zealand Government acknowledges this position of the Chinese Government.

The New Zealand Government recognizes the Government of the People's Republic of China as the sole legal government of China.<sup>4</sup>

With this formulation, New Zealand clearly accepted that there was only 'One China'. Embassies in the two countries were set up the following year.

Although New Zealand had never sought to ban travel to the PRC and had to some extent even encouraged the seeking out of trade opportunities, China in the 1970s was largely unknown to most New Zealanders. The reverse was also the case. However, some in China's senior leadership knew something about New Zealand and had a generally positive view. This was in part because the Communist Party of New Zealand (CPNZ) was, alongside its Albanian counterpart, the only fraternal party that sided with China during the Sino-Soviet split. Indeed, the then Secretary-General of the CPNZ, Vic Wilcox,

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<sup>4</sup> 'Joint Communiqué on the Establishment of Diplomatic Relations Between the People's Republic of China and New Zealand (21 Dec. 1972)' available at *The Embassy of the People's Republic of China in New Zealand*, Oct. 27 2003, [www.chinaembassy.org/nz/eng/zxgxs/t39440.htm](http://www.chinaembassy.org/nz/eng/zxgxs/t39440.htm) accessed May 14 2015.

was routinely received in Beijing as if he were a head of state and his writings were given worldwide distribution by the Chinese.

Chinese views of Wilcox were clearly demonstrated at the time of the Honourable Joe Walding's pioneering ministerial visit to China in March 1973 which was reported in the People's Daily on page three on the same day that a visit to Beijing by Wilcox was given front page treatment.<sup>5</sup>

The activities of Rewi Alley also contributed significantly to a positive view of New Zealanders. Alley had come to China in the late 1920s and had committed himself to social and community service, establishing an effective industrial cooperative during the war years and setting up the Shandan School in Gansu. He was a supporter of China's progressive political movements and had the support of the Chinese leadership, Premier Zhou Enlai in particular.

In 1972, bilateral trade between New Zealand and China totalled only \$1.7 million, and there were no air links between our two countries. To a New Zealander in 1972, China would have seemed an unknown, mysterious country of close to a billion people. And it's hard to believe New Zealand figured highly in the minds of most Chinese (Rt. Hon. John Key, 2012).<sup>6</sup>

New Zealand's primary purpose in establishing diplomatic relations with China was, on the one hand, a reflection of the reality that China had an enduring and effective government and was in full control of the country and, on the other, an understanding that it was important for New Zealand's security and economic interests to be able to have a relationship that could carry substantive dialogue on issues of interest to either or both parties. As New Zealand's interests broadened – the more so after the UK entered the then-European Economic Community – it became increasingly evident that New Zealand would have to engage internationally more widely and more deeply than hitherto. This was recognised by the Kirk Government,

<sup>5</sup> Kerry Taylor, 'Story: Wilcox, Victor' *Dictionary of New Zealand Biography*, Volume 5, 2000, cited in Te Ara: the Encyclopedia of New Zealand, [www.teara.govt.nz/en/biographies/5w30/wilcox-victor-george](http://www.teara.govt.nz/en/biographies/5w30/wilcox-victor-george), accessed May 14 2015.

<sup>6</sup> Rt Hon. John Key, 'Opening Address to the China Symposium' *New Zealand Government*, September 5 2012, <http://www.scoop.co.nz/stories/PA1209/S00054/john-key-opening-address-to-china-symposium.htm>

*The bilateral relationship would, in practice, in large part be driven by China's priorities and willingness to invest time and effort into the relationship. New Zealand's role had to be to provide a reason, a value proposition for China to do just that.*

and given practical effect in 1973 by the opening of the Embassy in Beijing, by re-opening the Embassy in Moscow that had been closed in 1950 and by establishing an Embassy in Vienna primarily for the purpose of developing trade and economic links with the countries of Eastern Europe (first Hungary and Romania and, a little later, Czechoslovakia and Poland).

While trade was a primary driver for the post in Vienna, this was not the case in Beijing. New Zealand's trade with China was very small, as was China's share of world trade and of the global economy. The focus in the 1970s was very much on political relations. China evidently valued the independent approach to foreign policy the Kirk Government was carving out, particularly against the background of the China/USSR split. As the relationship developed, New Zealand assessed that China saw some advantage to having a small, Western, well-respected country as an interlocutor on issues of regional and global interest. New Zealand saw similar benefit from such a dialogue but also had specific issues of its own to raise, China's approach to Southeast Asia and to nuclear testing in particular.

New Zealand understood from the outset that as a very small country, New Zealand's potential interest in China would always likely rate relatively higher than China's interest in New Zealand. New Zealand would always have to work harder to prove relevance and to register on China's radar screen. It helped that China's approach, both in principle and in practice, was to treat all countries seemingly as equals and with similar respect. New Zealand, a country with very limited geopolitical heft, was used to adopting a similar approach to its international relations and not to try to seek to put pressure on its diplomatic partners. The corollary was that it was understood that while New Zealand could seek to influence the pace and direction of the bilateral relationship, it would, in practice, in large part be driven by China's priorities and willingness to invest time and effort into the relationship. New Zealand's role had to be to provide a reason, a value proposition for China to do just that.

In turn, this led to an understanding that the bilateral relationship would have to be developed in a broad manner and not focus on only a small number of areas. While bilateral trade did not loom

particularly large at that time, the nature of the Chinese economy made it self-evident that the state of the political relationship would have an influence on the direction of trade and economic links. The rehabilitation of Deng Xiaoping in late 1977 and the decisions taken at the Third Plenum of the Eleventh Central Committee of the Chinese Communist Party committing China to the 'Four Modernisations' marked a far-reaching break point in China's development trajectory. The consequent changes did not occur overnight and it was far from clear at the outset just how enduring and far-reaching these new policies might be. It was not until 1984 and 1985 that China's reforms really began to gain visible traction in terms of its engagement with the international community.

Like most countries, New Zealand carefully monitored developments and by the mid-1980s had come to the view that China was deeply committed to opening up to the world and to achieving long-term sustainable substantial economic growth. Careful analysis showed that China's success would be in New Zealand's interests.<sup>7</sup> While 180 degree u-turns in Chinese policy had come about in the past, New Zealand concluded that there was no benefit in developing its bilateral relationship with China on the premise that China's ambitious modernisation programme would fail: the approach should be based on the likelihood of future success and New Zealand should invest in the relationship accordingly.

One of the practical consequences of this decision was the establishment in 1985 and 1986 of a whole-of-government coordinated strategic approach towards building New Zealand's relationship with China. The China Coordinated Programme had as its key objective ensuring that scientific and technical cooperation and academic, cultural and other contacts, as well as political exchanges, all contributed to enhancing the overall bilateral relationship. While this approach was in accordance with the holistic approach to the bilateral relationship that New Zealand had adopted since the establishment of diplomatic relations with Beijing, it was also clearly understood that such an approach would support the New Zealand private sector in its nascent efforts to open up the Chinese market.

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<sup>7</sup> Discussions with the New Zealand Ministry of Foreign Affairs and Trade.



## POLITICS ABOVE ALL ELSE

### EARLY DAYS

From a New Zealand perspective, its relationship with China is unique, not in the sense that New Zealand has a 'special relationship' with Beijing (as has on occasion been claimed) but because China is the only one of New Zealand's major political and economic partners with which it does not share an entrenched liberal democratic tradition and defence and security links, whether formal or informal. China is also very different in geographical size and population and there is little by way of shared history or people-to-people contact. Lastly, the pace of change over the past quarter-century in the relationship is unprecedented.

In 1976 Robert Muldoon (second from right) visited China, the first official visit by a New Zealand Prime Minister, here meeting Chinese leader Mao Zedong (third from left)

Archives New Zealand -  
Te Rua Mahara o te  
Kāwanatanga



*China is the only one of New Zealand's major political and economic partners with which it does not share an entrenched liberal democratic tradition and defence and security links, whether formal or informal.*

Despite the third Labour Government having recognised China soon after coming to office in December 1972, events were such that neither Norman Kirk nor Bill Rowling, who became Prime Minister following Kirk's death in August 1974, were able to visit China. Robert Muldoon was the first New Zealand leader to visit China, in April 1976. Muldoon was staunchly anti-Soviet and this was very likely a significant factor in the warm welcome he received in Beijing against the background of the Sino-Soviet split. In fact, Muldoon was the last Western leader to meet Mao Zedong before his death later that year. A significant consequence of the changes that took place in the two years or so following Mao's death was that the Chinese senior leadership began to travel abroad, a practice that had fallen into desuetude for some decades. New Zealand provided a low-key environment for Chinese

leaders to be exposed to the West after the long years in which China had largely been closed off to the outside world.

New Zealand was a relatively early beneficiary of this change. Premier Zhao Ziyang and General Secretary Hu Yaobang visited New Zealand in April 1983 and April 1985 respectively, in both cases their first visit to a developed country (both leaders also visited Australia). New Zealand's location in the Asia-Pacific region was likely one factor underlying these early first visits, but other elements would have been the meeting of minds on the risks posed by the Soviet Union Muldoon had achieved during his second visit to China in September 1980.

Zhao's visit also provided the opportunity to roll out one of New Zealand's enduring themes underpinning its view of China in the world, namely its support for China becoming a member of as many relevant international and regional institutions as possible. New Zealand not only considered that the institutions themselves would gain strength through the participation of all significant countries but also that New Zealand and the wider international community would benefit from China being brought into the key structures of global political and economic governance. This view continues to have contemporary relevance as seen by New Zealand's decision to become the first Western country to apply for membership of the new Chinese-promoted Asian Infrastructural Investment Bank (AIIB).

As an indication of the positive way in which New Zealand was seen by the Chinese leadership, David Lange, visiting China in early 1984 as Leader of the Opposition, was able to meet an unusually high number of senior figures, taking the opportunity to underline the importance that he and the Labour Party placed on the independent approach to foreign policy espoused by Kirk in the early 1970s. A further insight into how China viewed New Zealand came about in early April 1985. Unusually, Hu Yaobang agreed to be interviewed by a New Zealand journalist immediately before his visit to New Zealand. In the course of the interview, Hu made a number of comments strongly suggesting that China supported New Zealand in its anti-nuclear stance, comments that were interesting not least because of China's own nuclear status. It became apparent subsequently that Hu had been more specific in enunciating his support than was China's purported

public position at that time, and senior officials sought to reframe Hu's remarks accordingly.<sup>8</sup>

Hu Yaobang, Beijing, 1984.

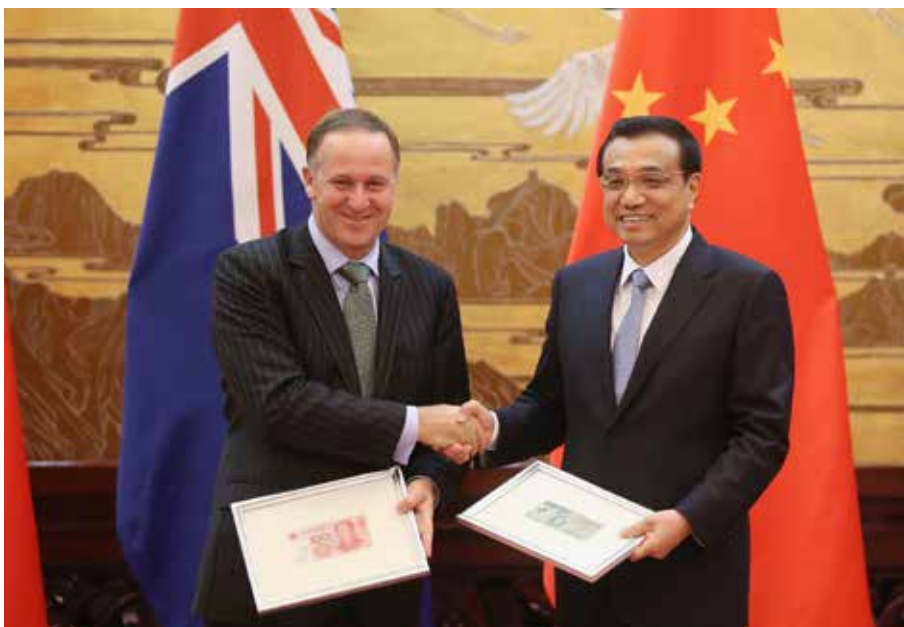
AFP photo



Against this background, one of the spin-offs from Hu's visit was Chinese support for the South Pacific Nuclear Weapon Free Zone, which led to China subsequently becoming the first nuclear weapons state to sign the protocols to the treaty setting up the zone, an action that the Western nuclear weapons states declined to undertake for quite a number of years. By the mid-1980s, China's engagement with the outside world had increased rapidly and was beginning to grow exponentially. Any suggestion that New Zealand might have some kind of advantaged position vis-à-vis other countries was rapidly being submerged under the sheer weight of resources that others were able to apply to the relationship. In 1986 the Foreign Affairs and Defence Committee of the House of Representatives undertook a review of New Zealand's relations with China. Taking more than six months, this was perhaps the most comprehensive review ever undertaken by the Committee. While the overall findings of the

<sup>8</sup> Discussions with former diplomat of the New Zealand Ministry of Foreign Affairs and Trade.

Committee were not unduly revealing, it did make the point that New Zealand could not continue to rely on what had been achieved to date and that increased resources needed to be devoted to the relationship if New Zealand were not to fall off China's radar. Perhaps most significantly, one of those who testified to the Committee was the then Chinese Ambassador, Zhang Longhai, perhaps the first time in modern Chinese history that a Chinese representative participated in a formal parliamentary enquiry in a Western country.



New Zealand Prime Minister John Key and Chinese Premier Li Keqiang exchange Chinese yuan and New Zealand dollar banknotes during an announcement ceremony at the Great Hall of People Beijing, March 18 2014

AP Photo

High-level visits continued to ramp up in the second half of the 1980s, with, over time, most of China's most senior leaders visiting New Zealand, and with appropriate reciprocal visits to China. Foreign Ministry consultations began in 1987, providing another channel through which the two countries could better understand each other's policies and positions. In particular, these talks provided the opportunity for New Zealand to take up with China in private its concerns about issues such as human rights and the rule of law. Senior New Zealand leaders visiting China also took the opportunity in their private talks with Chinese counterparts to raise such concerns. From the outset, New Zealand took the view that raising 'difficult' topics in public was unlikely to be productive; the Chinese would have little option but to push back, making any forward progress the more difficult. In a similar vein, the Dalai Lama did not meet formally with

*New Zealand could not continue to rely on what had been achieved to date and that increased resources needed to be devoted to the relationship if New Zealand were not to fall off China's radar.*

the New Zealand Prime Minister or ministers during his visits to New Zealand in 2009 and 2013.<sup>9</sup>

By the end of the 1980s the broad parameters for New Zealand's political engagement with China had fallen into place. The Tiananmen Square crackdown in June 1989 led to some holding back of official contacts but within two years the relationship began to normalise; the reality was that China had become an increasingly important player in the Asia-Pacific region so far as New Zealand was concerned and that it was not in New Zealand's interests that it be isolated. New Zealand remained of the view that the more China was integrated into the region the better it would be for all parties.

### THE PACE QUICKENS

If the 1980s was the decade in which China emerged to take up a full role in international discourse and trade, the years that followed were ones which consolidated that progress and allowed China to develop and change at an exponentially increasing rate. The platform for the bilateral relationship that had been laid down by New Zealand provided a solid basis for a small country on which to build further connections as opportunities presented themselves. New Zealand took a number of these opportunities.

In 1997 there was internal pressure on Chinese negotiators to show progress on China's bid to join the WTO<sup>10</sup> and as a consequence a proposal was made to New Zealand that was aimed at getting it to conclude its bilateral negotiations. The offer was clearly in New Zealand's interests; the only reason not to sign was that it cut across a widely agreed Western position to maintain solidarity to put more pressure on China. The New Zealand Government made a considered decision that national benefit from advancing the relationship with China outweighed considerations of like-minded consensus in Geneva. New Zealand became the first Western country a mere two

<sup>9</sup> Prime Minister Helen Clark had an informal conversation with the Dalai Lama at Brisbane Airport in 2007 when their schedules overlapped.

<sup>10</sup> Chris Elder (Ed.), *Forty Years On; New Zealand-China Relations Then, Now and in the Years to Come*, Victoria University of Wellington Press, Wellington, 2013, p. 25.

weeks later to conclude a bilateral agreement on China's accession to the WTO.<sup>11</sup>

This demonstrated to the Chinese that New Zealand was able to take an independent stance and act in the New Zealand interest and that it could respond quickly when required. It suggested to Beijing that New Zealand could on occasion be a good partner if it were looking to make progress on some seemingly intractable issue. Agreement with New Zealand, as a Western country, albeit a small one, could be precedent setting, thus assisting China. For New Zealand, being offered the opportunity to be the first to conclude an agreement with China could give it leverage it would be highly unlikely to have in any other circumstances and thus to achieve a better outcome. Further, New Zealand's small size could allow it to act more quickly than others and thus seize opportunities that might open up unexpectedly in China as a consequence of internal political drivers.

The second 'first' came seven years later. In early 2003, in advance of a visit to New Zealand by President Hu Jintao, New Zealand officials were looking for economic outcomes from the visit. As part of its broad policy of promoting trade liberalisation through the negotiation of FTAs, work had been done on the possible modalities of an FTA negotiation with Taiwan. The Chinese Ambassador in Wellington encouraged New Zealand officials to explore whether China itself might be a possible partner.

China, for its part, was signalling that recognition of Market Economy Status, to overturn provisions relating to dumping and trade remedies in China's WTO Accession Protocol, would be high on President Hu's goals for the visit. New Zealand officials negotiated a joint statement by Prime Minister Clark and President Hu under which China undertook to open negotiations on a Trade and Economic Cooperation Framework (TECF) with New Zealand. New Zealand, in that context, agreed to consider the Market Economy question. The TECF negotiations in Beijing in early 2004 agreed that New Zealand would move straight to the head of China's line to begin an FTA negotiation in return for recognition of Market Economy Status. The

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<sup>11</sup> Part of the agreement was subject to "satisfactory terms being agreed" on wool and this actually took three more years before being concluded.



decision to accept the deal was approved by the New Zealand Cabinet and acceptance was conveyed to Beijing within a week of the offer being made. For New Zealand, a practical consideration was that if it were not first in that line it would have little chance of again attracting China's attention. The benefits that were assessed as resulting from a China FTA made the decision to break with Western consensus on not accepting China as a market economy an easy one for New Zealand ministers to take. After a short feasibility study formal FTA negotiations began the same year.

This then led to the next two 'firsts', namely the formal commencement of FTA negotiations and the completion in 2008 of those negotiations resulting in New Zealand being the first OECD country to sign a high-quality, comprehensive and balanced FTA with China. A fifth 'first' is perhaps New Zealand's application to join the AIIB. China has made it clear that it would value identifying further 'firsts'.



**New Zealand Prime Minister Helen Clark delivers a speech at the celebration party for the FTA agreement between New Zealand and China in Beijing on April 7, 2008.**

Source: AFP PHOTO - MINORU IWASAKI

### TABLE 1: NEGOTIATING THE NEW ZEALAND-CHINA FTA

The New Zealand-China FTA is a treaty between New Zealand and China that liberalises and facilitates trade in goods and services, improves the business environment and promotes cooperation between the two countries in a broad range of economic areas.

Negotiations on the New Zealand-China FTA began in 2004 and continued for 15 rounds over three years. Negotiations entered their final stages after Premier Wen Jiabao's 2006 visit to New Zealand where agreement was reached on including dairy in the FTA. New Zealand Minister of Trade the Honourable Phil Goff and Chinese Minister of Commerce Chen Deming signed the FTA in Beijing on the April 7 2008. It entered into force on the October 1 2008.

The New Zealand-China FTA was China's first FTA with an OECD nation and one that set an important precedent for trade liberalisation in the Asia-Pacific. China is one of New Zealand's top trade partners. Two-way bilateral trade with China has more than doubled since 2008. New Zealand exports to China have grown by a factor of four.



**TABLE 2: NEW ZEALAND AND THE AIIB**

The Asian Infrastructure Investment Bank (AIIB) is a Chinese-led proposal for a bank to provide loans to Asian countries to develop infrastructure in the region. New Zealand publically signalled its interest in joining the bank at least as early as November 2014 when Prime Minister John Key said New Zealand wanted to participate in the newly launched bank and work with China to contribute to the region's infrastructure development.<sup>12</sup> New Zealand became the 24th founding member of the AIIB at the beginning of January 2015,<sup>13</sup> by far the earliest Western country to do so.

Former New Zealand Prime Minister, the Honourable Jenny Shipley, argued in March 2015 that 'New Zealand believes that there is a place for another development bank and decided to be one of the prospective founding members early so not only can we engage in this conversation but we can influence the governance framework.' Shipley argued that although New Zealand might be small, it has chosen to be in the conversation and through participation, support the development of rules-based systems for clarity, transparency, good governance and good leadership. By March 2015 New Zealand had already seconded people into the work party for setting up the governance systems in the bank.<sup>14</sup>

Within New Zealand there has been support in Government for participating in the AIIB. For example, Treasury Secretary Gabriel Makhoul argued New Zealand's involvement was a good move for the country because it would help to channel much needed investment into Asia and the Pacific: 'Being willing to take a lead shows openness and a continuing commitment to partnership with other countries in the region. Steps like this deepen our international connections, and help, among other things, to build resilience into our relationships.'<sup>15</sup>

<sup>12</sup> Fu Peng, 'New Zealand PM eye greater trade potentials with China', *Xinhuanet*, Nov. 12 2014, [http://news.xinhuanet.com/english/china/2014-11/12/c\\_133784344.htm](http://news.xinhuanet.com/english/china/2014-11/12/c_133784344.htm), accessed July 21 2015.

<sup>13</sup> 'New Zealand becomes 24th founding member of AIIB', *China Daily*, Jan 5 2015, [http://www.chinadaily.com.cn/business/2015-01/05/content\\_19239019.htm](http://www.chinadaily.com.cn/business/2015-01/05/content_19239019.htm), accessed July 21 2015.

<sup>14</sup> NZ hopes to influence new China bank, says former PM', *BBC News*, March 30 2015, <http://www.bbc.com/news/business-32110576>, accessed July 21 2015.

<sup>15</sup> Jason Walls, 'Support for China's new world bank increases' *National Business Review*, April 1 2015, <http://www.nbr.co.nz/article/support-china-new-world-bank-increases-jw-p-170855>, accessed July 21 2015.

New Zealand's political relationship with China is based largely on pragmatic decisions taken so both parties gain from what is seemingly an inherent asymmetric relationship between a major power and a small, isolated country half a hemisphere away. It is also significant that New Zealand has sought consistently to take a strategic approach to the development of its relationship with China. There is a strong line of continuity of approach from the early days of the China Coordinated Programme to the whole-of-government China Strategy launched in February 2012.<sup>16</sup>

**TABLE 3: THE NZ INC CHINA STRATEGY**

Five Strategic Goals
1. Retain and build a strong and resilient political relationship with China
2. Double two-way goods trade with China to \$20 billion by 2015
3. Grow services trade with China (education by 20 percent, tourism by at least 60 percent and other services trade) by 2015
4. Increase bilateral investment to levels that reflect the growing commercial relationships with China
5. Grow high quality science and technology collaborations with China to generate commercial opportunities

Source: 'Opening Doors to China' (2012) Ministry of Foreign Affairs and Trade

As Trade Minister Tim Groser stated in July 2014, '[T]here is no difference between 'foreign policy' and 'trade policy' for New Zealand. Get it right, and they complement each other. Get one of them wrong, and it is like waving the wrong flag at a bull...'.<sup>17</sup> The NZ Inc China Strategy continues the longstanding theme of seeking to maximise the benefits to New Zealand from having a coordinated approach across as many sectors as possible. As part of the implementation of the NZ Inc China Strategy the New Zealand China Council was established in 2012, inter alia 'to connect New Zealanders from business, the public sector, academia, sciences and the wider community who engage with China'.<sup>18</sup>

*[T]here is no difference between 'foreign policy' and 'trade policy' for New Zealand. Get it right, and they complement each other.*

Trade Minister Tim Groser

<sup>16</sup> 'Opening Doors to China: NZ Inc Strategy', *New Zealand Ministry of Foreign Affairs and Trade*, 2012, [www.mfat.govt.nz/NZ-Inc/6-Opening-doors-to-China/3-NZ-Inc-China-strategy/index.php](http://www.mfat.govt.nz/NZ-Inc/6-Opening-doors-to-China/3-NZ-Inc-China-strategy/index.php), accessed June 2 2015.

<sup>17</sup> Tim Groser, 'Address to China at the Crossroads: What the Third Plenum Means for China, New Zealand and the World', Victoria University of Wellington, July 2 2014.

<sup>18</sup> 'What We Do' *The New Zealand China Council*, 2015, <http://www.nzchinacouncil.com/#!the-council/c3z7>

New Zealand Trade Minister  
Tim Groser at a press conference  
at the Trans-Pacific  
Partnership meeting  
Sydney, October 27 2014

AP Photo



The strategy is about getting greater efficiency and effectiveness across all government agencies that work in, and with, China. And it's about developing more targeted and cohesive services to help successful businesses develop and grow in China. We want to be transparent about our bilateral interests, and get on with advancing them (Rt. Hon. John Key, 2012).<sup>19</sup>

Sound relationships need two-way buy-in. The fundamental political value proposition that New Zealand has for China is that it has for more than 30 years followed a consistent and bipartisan approach to the bilateral relationship; that it has demonstrated independent thought and action (its non-alliance relationship with the United States is relevant); that it is a well-respected, responsible and resourceful member of the international community; that it consistently fulfils the obligations that it takes on and is a trustworthy partner; and that it undertakes its engagement with China in an appropriately respectful member, in particular not seeking to air differences in public.

<sup>19</sup> Rt Hon. John Key, 'Opening Address to the China Symposium' *New Zealand Government*, September 5 2012, <http://www.scoop.co.nz/stories/PA1209/S00054/john-key-opening-address-to-china-symposium.htm>

As a reflection of the growing significance of the relationship to New Zealand, in March 2014 the New Zealand Government announced the establishment of seven new positions in the Ministry of Foreign Affairs and Trade to further political and economic relationships with China, the addition of a Beijing-based Public Affairs Manager and Advisor and nine new positions in the Ministry of Primary Industries as well as the building of a new Chancery in Beijing.

This relationship has never been stronger. We have great confidence that the coming years will see trade between us increase at a very fast pace ... To support what we see as the ever increasing importance of the China market and its growth potential, we intend to invest heavily in resourcing the region appropriately (Rt. Hon. John Key).<sup>20</sup>



**Chinese President Xi Jinping and New Zealand Prime Minister John Key address mayors from local councils at the launch of the New Zealand-China Mayoral Forum Auckland, November 21 2014**

AP Photo

During President Xi Jinping's visit to New Zealand in November 2014, the strength and depth of the bilateral relationship was recognised by President Xi and Prime Minister John Key by designating it as a 'comprehensive strategic partnership'.

<sup>20</sup> Rt. Hon. John Key, Prime Minister of New Zealand, 'China and NZ set ambitious new trade goals', New Zealand Government (March 19 2014) available at <http://www.beehive.govt.nz/release/china-and-nz-set-ambitious-new-trade-goals>.

#### TABLE 4: NEW ZEALAND-CHINA COMPREHENSIVE STRATEGIC PARTNERSHIP

On November 20 2014, President Xi visited Wellington where he signed a comprehensive strategic partnership with the New Zealand Government.<sup>21</sup> This reaffirmed the importance of the establishment of diplomatic relations in 2004, the 'four firsts' and pointed to the 'deepening of mutual trust and understanding, and the expansion of practical cooperation and exchanges'.

The partnership agreement stated 'the New Zealand-China relationship shows that countries with different political systems, history and cultural traditions and at different stages of development can constructively cooperate together.' This new framework stressed the importance of high-level meetings, of a relationship based on mutual respect and the significance of trade in the post-FTA environment.

It listed a number of areas of the relationship to develop further including agricultural cooperation; television and film coproduction; people exchanges; tourism and education; science and technology cooperation (especially food safety); defence engagement; regional and international cooperation; cooperation on crime; protection of human rights; communication and coordination on major international and regional affairs (APEC, FTAAP, RCEP, ASEAN Regional Forum, ADMM+); and working constructively together in the Pacific region.

*Only very rarely do China and New Zealand's interests around the world rub directly against each other.*

#### THIRD-COUNTRY RELATIONS

New Zealand and China do not see the world the same way. A myriad of factors, including history, geographic location, physical size, economic weight and social and governmental structures, contribute to these differences. Nevertheless, only very rarely do China and New Zealand's interests around the world rub directly against each other. New Zealand's economic wellbeing is directly linked with global and regional security and the consequences that flow from the maintenance of such security. New Zealand's position on issues such

<sup>21</sup> New Zealand Government, 'Establishment of NZ-China Strategic Partnership', Scoop, November 20 2014, <http://business.scoop.co.nz/2014/11/21/establishment-of-nz-china-strategic-partnership/>

as the East China Sea and South China Sea is to urge all parties, China included, to be transparent in their activities and to use the available channels to seek negotiated and peaceful solutions to the differences that exist.



**Chinese ocean surveillance, fishery patrol ships and a Japan Coast Guard patrol ship sailing about 27 km west of the group of disputed islands known as Senkaku in Japan and Diaoyu in China in the East China Sea; the aircraft is a Cessna CJ2 Citation chartered by Japanese media covering the clash 18 September 2012**

Kyodo News / Reuters / Picture Media

As an area close to New Zealand, and one in which New Zealand has longstanding close economic and political relations, the South Pacific was seen by some, both in New Zealand and elsewhere, as one where China's increased presence and more active role could be deemed unhelpful. However, New Zealand's assessment is that there is no evidence that this increased effort is out of kilter with the way in which China has expanded its activities elsewhere around the globe over the past decade or so. This effort is entirely in accordance with what a major rising power might be expected to pursue, with it being given a priority and focus commensurate with the overall relatively minor importance of the interests involved. A concern, however, is that even small scale (by Chinese standards) interventions in the South Pacific can have unexpectedly significant impact because of the small size of most Pacific Island societies and economies.<sup>22</sup> Second order effects could impact New Zealand and its interests.

In particular, there is the impact of China's aid to the Pacific. This has ramped up significantly over the past decade and is broadly

<sup>22</sup> Internal document prepared for the Department of Prime Minister and Cabinet, September 2013.

welcomed by the Pacific Island countries as it is by New Zealand; increasing the quantum of assistance available to these countries which have significant needs is a positive. Chinese aid is provided with fewer conditions than the longer established donors in the region, though often by way of soft loans rather than grants. New Zealand has encouraged China to align itself with global best practice in delivering its development assistance, with a particular emphasis on encouraging greater cooperation with other donors.<sup>23</sup> The tripartite aid agreement with China to invest NZ\$60 million to jointly improve water quality in Rarotonga (Cook Islands) is an example of this.<sup>24</sup>

### GOING FORWARD

Is the current relationship sustainable? If taken in isolation it probably is. But inter-state relations do not take place in a vacuum. Hitherto, for all of New Zealand's post-European settlement history, its major trading partners have shared similar political systems, cultures and values. New Zealand's major economic partners have also been its major security partners and guarantors. With China, it's different. For the first time New Zealand's largest or second-largest trading partner (it depends on whether goods alone or goods and services are taken into account) is not a security partner and is a country with very different values and traditions.

More broadly in the Asia-Pacific region, the sometimes-uneasy relations among the key players suggest that New Zealand may at some stage have to navigate a complex path between its traditional ties with Australia (especially) and the United States and its newer relationship with China. That remains an underlying tension for New Zealand policy makers but not one that there is any sense that it needs to be resolved in the present regional and international environment.

<sup>23</sup> See: 'China and the Pacific: The View from Oceania' National University of Samoa, Apia, Samoa, February 25-27 2015, *New Zealand Contemporary China Research Centre*, <http://www.victoria.ac.nz/chinaresearchcentre>

<sup>24</sup> 'New Zealand and China collaborate on world first in development' *New Zealand Aid Programme*, 2012, <https://www.aid.govt.nz>





## DEFENCE AND SECURITY

New Zealand's security context is one in which the military threat to New Zealand is limited at worst. The armed forces are used primarily to support New Zealand's international interests in a stable and secure world in which world affairs are conducted according to generally agreed rules and norms and where good relations with all states are sought as a matter of policy.

**TABLE 5: NEW ZEALAND'S SECURITY INTERESTS**

**New Zealand's core security interests are:**

- > a safe and secure New Zealand, including its border and approaches
- > a rules-based international order which respects national sovereignty
- > a network of strong international linkages
- > a sound global economy underpinned by open trade routes.

**Pursuit of these interests can also be described in terms of specific tasks that New Zealand's defence and security agencies are expected to undertake. These include:**

- > to defend New Zealand's sovereignty
- > to discharge our obligations as an ally of Australia
- > to contribute to and, where necessary, lead peace and security operations in the South Pacific
- > to make a credible contribution in support of peace and security in the Asia-Pacific region
- > to protect New Zealand's wider interests by contributing to international peace and security, and the international rule of law
- > to contribute to whole-of-government efforts at home and abroad in resource protection, disaster relief and humanitarian assistance
- > to participate in whole-of-government efforts to monitor the international strategic environment
- > to be prepared to respond to sudden shifts and other disjunctions in the strategic environment.

Source: New Zealand Government, Defence White Paper (2010)<sup>25</sup>

<sup>25</sup> New Zealand Government, 'Defence White Paper 2010', *Ministry of Defence*, November 2010, p. 9 and p. 37.

In operationalising these central tenets, New Zealand's geographical location is a key factor: New Zealand is distant from the world's major powers and conflict areas; as an island nation it has no land borders; it is allied to Australia; and there are no significant inter-state disputes or tensions anywhere near its own neighbourhood. New Zealand has historically very close defence ties with Australia, the United Kingdom, Canada and the United States dating from the end of World War II, close ties with Malaysia and Singapore through the quasi-alliance Five Power Defence Arrangements and is developing closer military relationships with a range of states, including China.

### NEW ZEALAND'S MILITARY RESPONSES TO CHINA

New Zealand's overarching defence priorities, especially in terms of developing a rules-based international order and a network of strong international linkages, are the basis of its engagement with China. China is not seen as a physical threat to New Zealand's territory, although the consequences of a regional dispute or conflict involving China would be of direct concern. In terms of dealing with an ever stronger and often more assertive China, the intent for more than 25 years has been to engage and be inclusive in dealings with China.

*China is not seen as a physical threat to New Zealand's territory, although the consequences of a regional dispute or conflict involving China would be of direct concern.*

New Zealand's security relationships with China have ebbed and flowed according to the wider relationship. New Zealand had little contact during the so-called 'Century of Humiliation' of the 19th and early 20th centuries during which China was unable to assert itself against Western powers and Japan. As noted earlier, by the late 1930s New Zealand was supporting China against Japanese aggression and then contributed through the Council of Organisations for Relief Service Overseas (CORSO) and other relief agencies to its post-war reconstruction.

But with the advent of the PRC in 1949 and that country's attempts to export the Communist revolution, the New Zealand approach followed its traditional allies. Thus, in 1950, concerns were being voiced about Communist success in China, Communist insurrection in Malaya and Communist aggression against South Korea, although New Zealand set these concerns very much in the context of regional security in the Pacific rather than of any potential direct impact on New Zealand

territory itself.<sup>26</sup> Other than during the Korean War, the focus of New Zealand's concerns as expressed in successive Defence Reviews was very much on the threat of 'Communist aggression' and the export of revolution to Southeast Asia as part of a worldwide drive by the Communist bloc to achieve global domination rather than on China as an expansionist or aggressive power *per se*.<sup>27</sup>

From the 1970s, as China opened to the world, the tone of commentary in successive Reviews grew cautiously more positive as the way China was playing down support for revolutionary movements and the increasing role China was playing in the region were noted. In 1972 the 'diplomatic vigour and new flexibility of China' were noted and in 1978, the 'decrease in support for revolutionary movements in Southeast Asia' was highlighted.<sup>28</sup>

In 1987 in a sign of warming relations, HMNZ Ships *Canterbury* and *Southland* visited Shanghai, the first ever New Zealand naval visit to China. By 1997, as China was beginning to develop closer links with the region, the Government noted that:

... the principal new element in the region's strategic equation is the rapid rise in the economic importance of the People's Republic of China. China's return to the region is impressive and welcome, but it will require an adjustment in the existing structure of regional relationships ... Working out the relationships among China, Japan and the United States will, more than anything else, determine the levels of confidence in the region.<sup>29</sup>

And that cautious optimism was continued in subsequent Defence policy documents. China's ability to challenge militarily was 'limited' and although China was seeking to 'enlarge its own room for

<sup>26</sup> New Zealand Government, 'Statement on Defence 1950', *Ministry of Defence*, Paper H-4, 1950, p. 2.

<sup>27</sup> See for example, New Zealand Government 'Review of Defence Policy', *Department of External Affairs*, Publication No. 181, p. 4, and 'Review of Defence Policy 1961', Paper A19, Wellington: Government Printer, p. 4.

<sup>28</sup> New Zealand Government, 'Review of Defence Policy 1972: New Zealand's Defence Policy Perspectives', paper A5, Wellington: Government Printer, 1972, p.8 and '1978 Defence Review', p. 13.

<sup>29</sup> New Zealand Government, 'The Shape of New Zealand's Defence: A White Paper', Wellington: *Ministry of Defence*, 1997, p. 14.

manoeuvre' internationally, it had to focus on its internal issues, which were probably a more pressing issue at the time.<sup>30</sup>



**An MH60 Seahawk on the flight deck of HMNZS Canterbury.**

AP Photo

By 2010 the tone of Defence rhetoric was both more optimistic and more cautious:

China both benefits from and contributes to regional stability and prosperity, but there will be a natural tendency for it to define and pursue its interest in a more forthright way on the back of growing wealth and power. The pace of China's military modernisation and force projection programme, and the response this could prompt from neighbouring states, may test the relationships of the major regional powers.<sup>31</sup>

China's increasing military weight is recognised in the 2014 *Defence Assessment*:

<sup>30</sup> Strategic Assessment 2001', Wellington, *External Assessments Bureau*, 2001, p. 4.

<sup>31</sup> New Zealand Government, 'Defence White Paper 2010', Wellington: *Ministry of Defence*, November 2010, p. 30.

Chinese military power will continue to increase in relative and absolute terms. Much of its spending is focused on developing capabilities that expand China's ability to conduct military operations in areas outside its own territory, including a larger more capable submarine fleet, advanced combat aircraft, aircraft carriers, ballistic and cruise missile programmes, and cyber capabilities.<sup>32</sup>

This narrative of official responses to China demonstrates that New Zealand has overall been descriptive rather than prescriptive in its discussions of China and China's activities. New Zealand generally has chosen not to comment directly on China or its activities. In part that might be a standard New Zealand disinclination to use megaphone diplomacy to comment on other countries; in part it could be that China's activities have been interesting but not of direct concern.

Alongside the trend of more positive rhetoric has been a corresponding trend of ever-increasing military links with the Chinese People's Liberation Army (PLA). High-level defence discussions began in 1996 with the visit to New Zealand by the PLA Deputy Chief of General Staff who met senior ministers, military personnel and civilian officials. That visit had been able to be arranged because New Zealand's Secretary of Defence took the opportunity a year earlier to engage a senior PLA General in transit through Auckland to emphasise New Zealand's interest in developing our defence relationship 'in modest useful ways'.<sup>33</sup> Since 1996 visits in both directions by senior ministers and officials have been an almost annual event.

Defence attachés were established in each country from 1998 and the senior official visits have been mirrored by working level and technical visits and defence educational exchanges. Warship visits have been a feature since 1987 and have occurred almost annually since 1998. Bilateral military exercises began in 2007 with Chinese and New Zealand participation in a maritime search and rescue exercise. In 2013, New Zealand took the opportunity through its hosting of Exercise *Phoenix Spirit*, a humanitarian assistance and disaster relief

<sup>32</sup> 'Defence Assessment 2014', p. 38.

<sup>33</sup> Justin Fris, 'Neither Staunch Friends nor Confirmed Foes: New Zealand's Defence Diplomacy in Asia', Unpublished MA thesis, *Victoria University of Wellington*, June 2013, p. 63.

(HADR) planning exercise that had previously involved Australia, China and New Zealand, to also bring in the United States, in order to help build positive defence engagement between China and the US.<sup>34</sup> Exercises of this nature are an annual event and may be expanded.

## TO THE FUTURE

For New Zealand, there are two main implications. First, it's very much in New Zealand's interest to encourage China to act constructively on international and, especially, regional defence and security issues. A key aspect of this is to encourage as much transparency as possible by Beijing. Concrete engagement by China in the development of the regional (and international) security architecture will result in enhanced Chinese 'ownership' of the outcomes and is to be encouraged. Further, the greater the level of operational and tactical cooperation that can be achieved among defence forces, especially by junior and mid-level officers, the greater the ensuing level of trust and understanding.

New Zealand, albeit with only a limited defence capability, is contributing to this suite of activities. Thus, for example, as a result of dialogue on peacekeeping activities, China has used New Zealand's armed forces' rules of engagement as the basis for formulating those of the PLA.

Second, New Zealand is looking to increase direct defence coordination with China. Apart from the ongoing exchanges involving their respective staff colleges and occasional ship visits that provide the opportunity for reciprocal familiarisation activities, New Zealand is keen to enhance defence cooperation with China in the South Pacific. This is primarily centred on HADR, given the recurring needs of the region in coping with natural disasters, in order to bring together the Chinese military's vast experience of responding to such events in China and New Zealand's familiarity with the South Pacific. Looking to the future however, there could be a sound basis to work cooperatively with China in providing engineering and medical assistance to Pacific

*Concrete engagement by China in the development of the regional (and international) security architecture will result in enhanced Chinese 'ownership' of the outcomes and is to be encouraged.*

<sup>34</sup> Paul Sinclair, 'New Zealand Expands Defence Ties with China', *Centre for Strategic Studies, Victoria University of Wellington*, July 24 2014.

Island countries in the same way as New Zealand has worked previously with the United States.

The most important component of the defence and security relationship between New Zealand and China in the last 20 years has been the way in which each country has been prepared to move steadily but with no preconceived ends other than to develop the relationship. A central component has been the recognition by New Zealand that the process had to move at a speed China was comfortable with. Underlying this has been the intent by New Zealand that China recognise New Zealand as a consistent and long-term partner which can be trusted and with which any diplomatic or technical missteps could be accepted without rancour or adverse publicity.





## ECONOMIC AND TRADE RELATIONS

### A LARGER SHARE OF GLOBAL TRADE

*The fulcrum of global economic development was already shifting to the Asia-Pacific region even prior to China's emergence as a major power.*

China's emergence from an isolated state scarcely involved in the global economy into the world's second largest economy has had unparalleled global impact, not least on New Zealand. Never before have so many people been brought out of poverty so quickly, but also never before have so many people been brought so quickly into upper middle income status.<sup>35</sup> Per capita gross domestic product (GDP) in China increased almost five-fold from US\$949 (at current values) in 2000, to US\$4,433 in 2010, and then by a further 50 percent to US\$6,807 by 2013.<sup>36</sup>

In a relatively short time, therefore, not only have global economic power and influence balances changed significantly, but also the number of potential consumers wanting to and being able to partake of a very different kind of life than their parents and grandparents has multiplied significantly. The fulcrum of global economic development was already shifting to the Asia-Pacific region even prior to China's emergence as a major power but with China also in the mix the combined effect for New Zealand is potentially profound: for the first time in its post-settlement history is the world's economic growth centre in its part of the world.<sup>37</sup> The 'tyranny of distance'<sup>38</sup> which seemingly has had a significant impact on weakening New Zealand's economic performance, might be loosening its grip.

The economic impact on New Zealand of China's growth and the consequent deepening and thickening of links between the two countries can be demonstrated in a number of areas including trade in goods, the number of Chinese students studying in New Zealand, visitor numbers and investment flows. The deepening of economic relations post-FTA has raised a number of important questions

<sup>35</sup> 'Data' World Bank, [www.data.worldbank.org](http://www.data.worldbank.org), accessed 25 May 2015.

<sup>36</sup> Ibid.

<sup>37</sup> More or less; in fact, a map drawn with a hemisphere centred on Wellington reveals that Beijing is in the other hemisphere.

<sup>38</sup> 'An International Perspective on the New Zealand Productivity Paradox', *New Zealand Productivity Commission*, April 2014.

concerning New Zealand's economic future and position in the global supply and value chains in the Asia-Pacific.

## FREE TRADE AGREEMENTS

Both positive and negative forces have pushed New Zealand to develop a viable strategy of regional integration since the 1980s. Closer Economic Relations (CER) with Australia showed how creating a common market provided new opportunities for the New Zealand economy. However, analysts also recognised the need for a defensive stance to counter trade diversion effects from being left out of the major trade blocs, the European Common Market and the North American Free Trade Agreement (NAFTA). These external events, coupled with domestic reform and liberalisation, led to a revision of New Zealand trade policy and the development of a four-track trade strategy (unilateral, multilateral, regional and bilateral).<sup>39</sup> The strategy affirmed the executive's commitment to trade liberalisation and turned New Zealand from a protected and largely isolated economy in the South Pacific to a promoter of regional integration and open regionalism in the Asia-Pacific.

New Zealand has put much effort into achieving agreements at the regional level. This includes being a founding member economy of Asia-Pacific Economic Cooperation (APEC, 1989) and supporting the APEC Business Advisory Council promotion of a comprehensive FTA for APEC members, the proposed Free Trade Area of the Asia-Pacific (FTAAP), the Pacific Four (P4), the Regional Comprehensive Economic Partnership (RCEP) and the Trans-Pacific Partnership (TPP). Arguably, however, bilateral trade agreements have been the dominant track for New Zealand trade policy even if the naturally preferable track for a small nation like New Zealand is multilateral. As the New Zealand Minister of Trade, Tim Groser, has pointed out, in light of the stalling of multilateral momentum, New Zealand will continue to put efforts into bilateral negotiations.<sup>40</sup> The New Zealand-

*Both positive and negative forces have pushed New Zealand to develop a viable strategy of regional integration since the 1980s.*

<sup>39</sup> Ministry of Foreign Affairs and Trade. *New Zealand Trade Policy – Implementation and Directions: A Multi-Track Approach*, New Zealand Ministry of Foreign Affairs and Trade, Wellington, 1993.

<sup>40</sup> Tim Groser, 'Speech to the Opening of Synlait new dairy factory', *New Zealand Government*, 2011, <http://www.beehive.govt.nz/speech/opening-synlait-new-dairy-factory>

China FTA represents the outcome of New Zealand's broader strategy of reducing barriers to trade in the Asia-Pacific.

**TABLE 6: NEW ZEALAND PRINCIPLES FOR JOINING ECONOMIC AGREEMENTS**

<b>First</b>	<b>Having an open mind on New Zealand joining – by itself or with others – formal trading arrangements <i>provided they are not inherently exclusive.</i></b>
<b>Second</b>	GATT (WTO) is the most important trade policy agenda for New Zealand and the world economy and results there will shape other options.
<b>Third</b>	New Zealand must be realistic. It cannot threaten but can negotiate and build coalitions with other countries in the region that are prepared to join in opening up their markets.
<b>Fourth</b>	It makes sense to continue to work together with Australia as even though there are major differences, it is to our mutual advantage to present a united front.
<b>Fifth</b>	Any economic arrangement would have to make economic sense to New Zealand, involve genuinely complementary and compatible economic systems, which means that agricultural trade liberalisation has to be involved.
<b>Sixth</b>	Any arrangement has to be GATT-compatible, comprehensive in coverage and could not raise existing barriers to other countries.
<b>Seventh</b>	Any agreement must be 'Pacific friendly', namely, it should be judged on whether or not a particular set of arrangements add practical momentum to bringing countries in the region closer together.

Source: Bolger (1992:6-7).<sup>41</sup>

The New Zealand-China FTA, the first comprehensive FTA between China and an OECD country, entered into force on October 1 2008. It liberalises and facilitates trade between the two countries across all areas of trading interest to New Zealand. Most of its provisions have come fully into force, although tariffs relating to a small number of items have yet to phase down to the agreed end-point (zero in almost all cases) between 2016 and 2019.

For New Zealand, the case for seeking to negotiate a comprehensive agreement with China was compelling; it provided an opportunity for

<sup>41</sup> Rt. Hon. Jim Bolger, 'Regional Trade Policy: the Seven Pillars of Wisdom', *Newsletter / Institute of Policy Studies*, no. 33, 1992, pp. 5-7.

New Zealand to gain competitive advantage in seeking to develop a comprehensive economic relationship with a rapidly growing major economic power.

**TABLE 7: NEW ZEALAND-CHINA FTA (2008)**

<b>Liberalised trade in goods</b>	The removal over time of tariffs on 96 percent of traded goods.
<b>Rules to govern trade</b>	Rules to determine which goods qualify for tariff cuts (the 'Rules of Origin') as well as rules to counter unfair trade or unexpected surges in imported goods from the other country.
<b>Liberalised trade in services</b>	China expands its commitments in services including in education and environmental services.
<b>Movement of people</b>	Provisions to facilitate the travel of business people to China and to provide access to skilled workers from China in certain occupations where long term skills shortages exist.
<b>Facilitation for investment</b>	Enhanced protections for investments established in China, as well as a provision to ensure that New Zealand investors remain competitive with investors from other countries. Access to binding third-party arbitration procedures if either government breaches the investment provisions.
<b>Measures to improve the business environment</b>	Measures relating to customs procedures and cooperation, sanitary and phytosanitary measures, technical barriers to trade and intellectual property, designed to reduce barriers to doing business between New Zealand and China. A framework for cooperation to enhance the benefits of the FTA.
<b>Conformity Assessment of Electrical and Electronic Equipment</b>	A Mutual Recognition Agreement on Electrical and Electronic Equipment (EEEMRA), to facilitate conformity assessments of a large proportion of electrical and electronic products traded between New Zealand and China.
<b>Dispute Settlement</b>	Robust dispute settlement mechanisms and protections to preserve both countries' domestic regulatory and policy-making flexibility.
<b>Environment and Labour</b>	A binding Environment Cooperation Agreement and a binding Memorandum of Understanding on Labour Cooperation. These Agreements enhance communication and cooperation on these issues and help towards the objectives of raising working standards and improving environmental protection in both countries.

Source: MFAT (2008) New Zealand-China Free Trade Agreement. Wellington: Ministry of Foreign Affairs and Trade, pp. 8-9.

New Zealand dairy exports have been subject to a mid-term review and special safeguard mechanisms. These mechanisms have

*For New Zealand, the case for seeking to negotiate a comprehensive agreement with China was compelling.*

meant that when triggered, China can apply an additional tariff on liquid milk, butter, cheese and milk powders up to its WTO and most favoured nation (MFN) tariff rate (10-15 percent). The only exclusion preventing the FTA from applying in time to 100 percent of New Zealand exports is in processed wood and paper products where it was agreed that China's MFN commitment to Canada in its WTO accession negotiations, would result in potentially greater harm than benefit to New Zealand exporters.<sup>42</sup>

**TABLE 8: NEW ZEALAND-CHINA FTA: MAIN FEATURES**

<b>Goods</b>	Tariffs on 35 percent of trade eliminated on Entry into Force 2008; remaining tariffs phased down to zero over 12 years (2019) with some (dairy) safeguards remaining; tariffs on sheep and beef meat, kiwifruit, sheepskins reduce to zero by 2016; 2.5 percent of current trade (wool over quota and some processed wood and paper products) not subject to tariff elimination.
<b>Dairy</b>	All tariffs eliminated by 2019, but safeguards will apply for up to a further five years.
<b>Meat</b>	All tariffs eliminated by 2016; no safeguards.
<b>Investment</b>	Provisions included to protect investment, including investor-state dispute settlement; MFN clause included.
<b>Services</b>	WTO-plus commitments in a wide range of sectors including education, environmental services, construction, computer services and transport; MFN clause applying to some specific service sectors (the above excluding education, and engineering services).
<b>Education</b>	Listing on China's Ministry of Education web-site of major New Zealand tertiary education institutions and a small number of private training establishments; agreement to work jointly on quality assurance criteria for qualifications that include distance delivery; establishment of a Joint Working Group on mutual recognition of vocational qualifications.

Source: Ministry of Foreign Affairs and Trade (MFAT) Wellington compiled from <http://www.chinafta.govt.nz/>

The coming into force of the FTA soon had an impact on trade, particularly on New Zealand's exports to China (see below). An initial target set by the two countries' leaders of achieving two-way trade of

<sup>42</sup> 'New Zealand-China Free Trade Agreement: National Interest Analysis', *Ministry of Foreign Affairs and Trade*, no date, <http://www.chinafta.govt.nz/1-The-agreement/3-Publications/National-interest-analysis.pdf>

NZ\$20 billion by 2015 was reached by mid-2014.<sup>43</sup> During President Xi Jinping's visit to New Zealand in November 2014, he and Prime Minister Key agreed to explore an upgrade to the FTA. This decision recognised the strong growth of bilateral trade and investment between the two countries as well as the fact that both countries have since 2008 concluded FTAs with other countries (the China-Australia FTA is particularly relevant). The joint investigation as to whether the FTA should be upgraded reflects the wish of both governments to ensure that the agreement remains up to date and relevant to the current bilateral trade, investment and wider business environment.<sup>44</sup>

New Zealand has also concluded an FTA with Hong Kong, with the agreement coming into force on January 1 2011. This agreement is in many ways aligned with the New Zealand-China FTA, particularly in relation to phasing in tariff reductions. The agreement locked in for New Zealand existing access arrangements and provided an 'early harvest' of Hong Kong's commitments made in the WTO Doha Round.<sup>45</sup> Negotiations on this FTA had begun a number of years earlier, but conclusion had to await the completion of negotiations between New Zealand and China.

In addition, negotiation of a broad trade and economic agreement with Taiwan, the Agreement between New Zealand and the Separate Customs Territory of Taiwan, Penghu, Kinmen, and Matsu on Economic Cooperation (ANZTEC),<sup>46</sup> was concluded in July 2013 and the agreement entered into force on December 1 2013. The agreement reduces tariffs for New Zealand goods entering Taiwan so that 98.7 percent of all exports will be duty-free four years after entry into force, with further reductions for the remaining products according to a

<sup>43</sup> John Key, 'Trade target with China surpassed early' *New Zealand Government*, June 27 2014 [www.beehive.govt.nz/release/trade-target-china-surpassed-early](http://www.beehive.govt.nz/release/trade-target-china-surpassed-early), accessed June 2 2015.

<sup>44</sup> 'Upgrade of the New Zealand-China Free Trade Agreement', *ChinaFTA.govt.nz*, April 20 2015, [www.chinafta.govt.nz/4-Events-and-press/index.php#upgradesubmissions](http://www.chinafta.govt.nz/4-Events-and-press/index.php#upgradesubmissions), accessed May 26 2015.

<sup>45</sup> 'New Zealand-Hong Kong, China Closer Economic Partnership; National Interest Analysis', *Ministry of Foreign Affairs and Trade*, no date <http://www.mfat.govt.nz/Trade-and-Economic-Relations/2-Trade-Relationships-and-Agreements/Hong-Kong/index.php>

<sup>46</sup> Agreement between New Zealand and the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu on Economic Cooperation.

slower timetable. ANZTEC is a comprehensive agreement covering investment, air services, film co-production and other sectors.<sup>47</sup>

New Zealand's exports to Taiwan increased by nearly 15 percent in the first 12 months after ANZTEC came into force, while there was little change in the value of Taiwan's exports to New Zealand.<sup>48</sup>

Taiwan is one of New Zealand's 'Top 10' trading partners and, as such, there was sound economic logic backing the conclusion of an FTA between the two territories. However, because of New Zealand's firm adherence to the 'One China' policy, negotiating such an agreement was not straightforward. Three elements combined to make this outcome eventually possible. First, Taiwan's entry into the WTO in January 2002 established a specific nomenclature for Taiwan as a 'customs territory', thus clearly differentiating it from a political entity. Second, one consequence of the signing of the Cross-Strait Economic Cooperation Framework Agreement (ECFA) between Beijing and Taipei was that it signalled that the PRC was indeed willing to see Taiwan enter into bilateral and regional economic cooperation arrangements. Third, a good relationship between New Zealand and China was an important factor.<sup>49</sup> The full extent of New Zealand officials' parallel engagement with Beijing while negotiating with Taipei is not publicly disclosed. But the 'no surprises' principle guiding the relationship with Beijing was certainly relevant. New Zealand took the view that by ensuring that what it was seeking to achieve with Taiwan was clearly understood in Beijing, it was making no concessions to China (nor giving it any right of veto over New Zealand's sovereign decisions). The fact that the New Zealand-China FTA was already in place was important. It is unlikely that China would have viewed with anything short of major displeasure any country negotiating with Taiwan before reaching a similar agreement with the PRC.

<sup>47</sup> 'Agreement between New Zealand And the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu on Economic Cooperation' *New Zealand Commerce and Industry Office*, (no date) available at [www.nzcio.com/webfm\\_send/93](http://www.nzcio.com/webfm_send/93), accessed 29 May 2015.

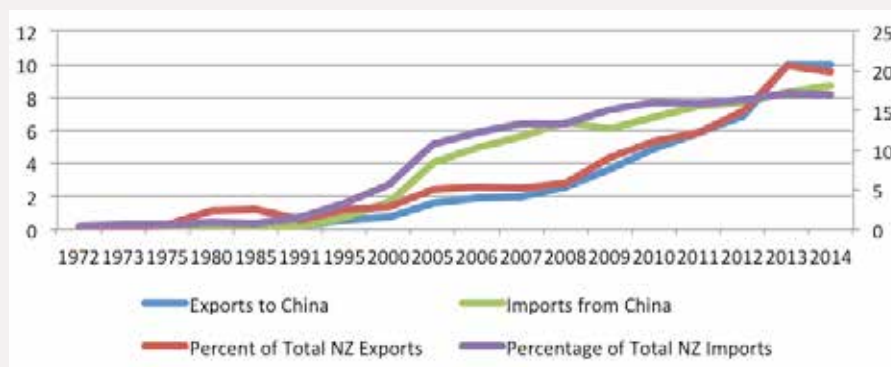
<sup>48</sup> 'Global New Zealand, International Trade, Investment and Travel Profile' *Statistics New Zealand*, 2015.

<sup>49</sup> Jason Young, 'Space for Taiwan in regional economic integration: Cooperation and partnership with New Zealand and Singapore', *Political Science*, 2014, Vol 66(1) pp. 3-22.

## MERCHANDISE TRADE

Merchandise trade figures show very clearly how China's economic growth has affected New Zealand's overseas trade outcomes. In 1972/73, at the time New Zealand recognised the PRC, New Zealand's exports to China amounted to just under NZ\$6 million, or around 0.3 percent of New Zealand's total exports.<sup>50</sup> Ten years later, in 1982/83 the comparable figures were NZ\$177 million and 2.3 percent. A further decade later, exports to China had reached NZ\$368 million, but had levelled off proportionally, amounting to only 1.9 percent of total exports. By 2003, however, New Zealand's exports to China amounted to NZ\$1,376 million, or 4.8 percent of the total. After a further 10 years, during which time the New Zealand-China FTA came into effect, exports amounted to NZ\$9,965 million, this being 20.7 percent of all exports. Figure 1 illustrates the change in China's relative importance to New Zealand as a trading partner over the past 40 years.

**FIGURE 1: NEW ZEALAND-CHINA EXPORTS AND IMPORTS (1972-2014)**



Source: Statistics New Zealand; June years until 2000; calendar years thereafter, Units: Billion (1,000 million) NZD.

China's growing importance to New Zealand as an export destination is self-evident but the reverse is not the case; New Zealand's share of China's imports (measured in US\$) has remained relatively constant around a minuscule 0.3 percent and New Zealand's share of China's exports has similarly remained at around a 0.2 percent level.<sup>51</sup>

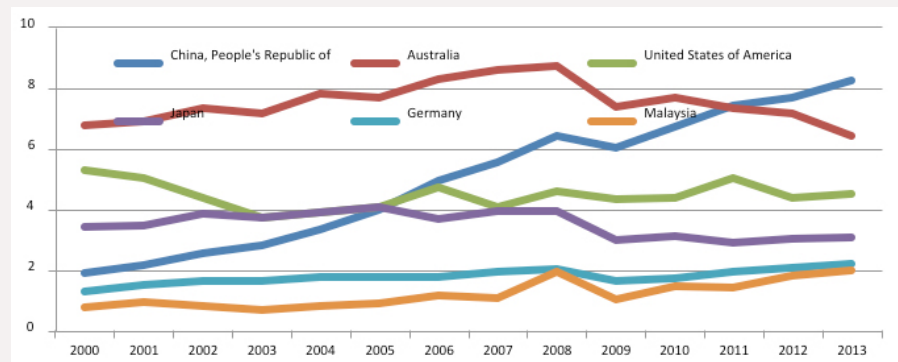
<sup>50</sup> Trade figures taken from New Zealand Official Yearbooks 1972-2000, thereafter from *Statistics New Zealand*, [www.stats.govt.nz](http://www.stats.govt.nz)

<sup>51</sup> 'Annual Data, Trade, 2014', *National Bureau of Statistics of the People's Republic of China*, [www.stats.gov.cn/english/statisticaldata](http://www.stats.gov.cn/english/statisticaldata)



Hence, despite the massive leap in the dollar value of New Zealand's exports and imports from China, the growth in bilateral trade has done no better than match China's overall foreign trade performance over the past 40 years. Following the rapid increase in trade following the New Zealand-China FTA, China and New Zealand have set a new target for 2020 of NZ\$30 billion in two-way trade; achieving this ambitious objective will be important if New Zealand is to achieve the target set by Government of growing total exports to reach 40 percent of GDP.

**FIGURE 2: TOP SIX SOURCES OF NEW ZEALAND MERCHANDISE IMPORTS (2000-13)**



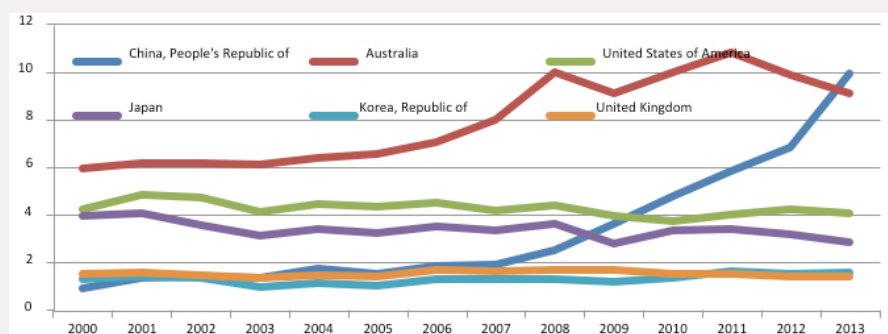
Source: Statistics New Zealand (2014); Units: Billion (1,000 million) NZD.

*Despite the massive leap in the dollar value of New Zealand's exports and imports from China, the growth in bilateral trade has done no better than match China's overall foreign trade performance over the past 40 years.*

With New Zealand's exports to China now hovering around 20 percent of total exports, it is relevant to explore whether or not New Zealand is becoming too dependent on one market. Taking the figures for April 2015<sup>52</sup> as a non-atypical example of the overall direction of trade, New Zealand's major export markets in that month took respectively the following market shares: China 18.0 percent, Australia 15.6 percent, US 11.7 percent, EU 11.7 percent, Japan 7.1 percent. Thus New Zealand's top five export destinations took, collectively, 64.1 percent of total exports. By comparison, in the 1990s and early 2000s, New Zealand's top four trading partners (then Australia, the EU, the United States and Japan) routinely provided the destinations for around 60-65 percent of New Zealand's exports.<sup>53</sup>

<sup>52</sup> 'Overseas Merchandise Trade' *New Zealand Statistics*, 2015, [www.stats.govt.nz/browse\\_for\\_stats/industry\\_sectors/imports\\_and\\_exports/OverseasMerchandiseTrade\\_HOTPApr15.aspx](http://www.stats.govt.nz/browse_for_stats/industry_sectors/imports_and_exports/OverseasMerchandiseTrade_HOTPApr15.aspx), accessed 26 May 2015.

<sup>53</sup> 1991: Australia 19%, EU 17.5%, US 13%, Japan 16%; 2000: Australia 21%, EU 16%, US 14%; Japan 13%; 2005: Australia 20%, EU 16%, US 15%, Japan, 11%. Source: New Zealand Official Yearbooks 1992, 2001, 2006.

**FIGURE 3: TOP SIX DESTINATIONS FOR NEW ZEALAND MERCHANDISE EXPORTS (2000-13)**

Source: Statistics New Zealand (2014); Units: Billion (1,000 million) NZD.

Arguably, therefore, New Zealand's overall vulnerability has decreased somewhat over the past couple of decades with the same proportion of exports now destined for five, rather than four, markets. Moreover, New Zealand has over the past three decades diversified both partners and products traded with partners outside the top five, thus also reducing reliance on too few markets (a very different situation from New Zealand's earlier dependency on the UK which in 1970 still took nearly 40 percent of its exports).

Another form of market vulnerability is having too large a proportion of trade relying on a limited number of products. In 2014, dairy products comprised some 43 percent of total exports to China, timber and wooden products 17 percent, meat 11 percent, and wool four percent - a total of around 75 percent.

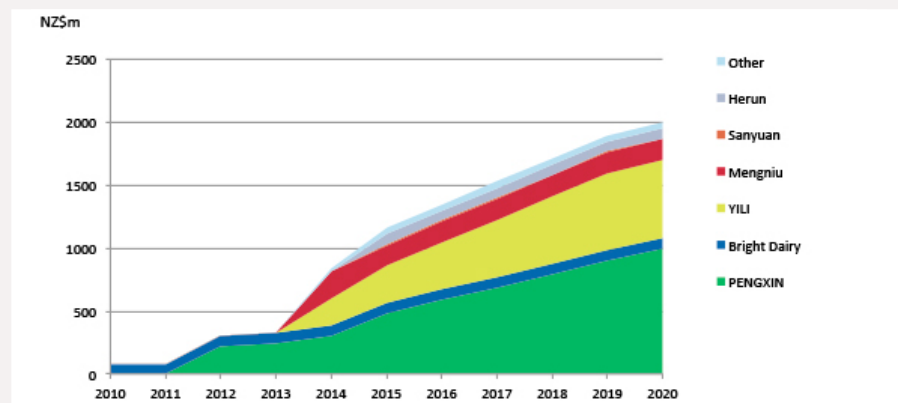
**TABLE 9: PRINCIPAL NEW ZEALAND EXPORTS TO CHINA (2014)**

Product	Value (NZ\$m)	Percentage of Total Trade
Milk powder	3,645	36.5
Logs	1,581	15.8
Sheep meat	807	8.1
Wool	407	4.1
Butter and dairy spreads	348	3.5
Frozen beef meat	233	2.3
Cheese	171	1.7
Sawn timber etc.	128	1.3

Source: Global New Zealand, International Trade, Investment, and Travel Profile, year ending December (2014), Department of Statistics.

This suggests an over-reliance on a few (primary) products and the consequences can be seen with the fall in export receipts experienced in the first part of 2015 relative to the previous year as a result (largely) of the significant fall in global dairy prices (some 34 percent between March 2014 and March 2015.)<sup>54</sup> The remainder of the trade is spread over a wide range of products but at this time there is little evidence that they can pick up the slack resulting from a fall in global commodity prices. A more positive analysis might, however, note that New Zealand's 'soft' commodities are likely to command a more stable market in volume terms over the medium to long-term than other countries' 'hard' commodity exports, given that in part at least they are linked more weakly to the overall pace of economic growth.

**FIGURE 4: CHINESE DAIRY INVESTMENTS IN NEW ZEALAND – ACTUAL AND ANNOUNCED TO 2020 (ACQUISITION PRICE BASIS)**



Source: NZTE China FDI/ODI database. Pengxin's forecast is based on company's announced plan to acquire \$1bn in farms by 2020, subject to OIO consent.

Second order effects too may impact New Zealand. As many of New Zealand's other trading partners also have external economic relations tightly linked to China, any diminution of economic growth and demand in China will also be felt by these partners and in turn impact their trade with New Zealand. A case in point is Australia with its trade, commodities trade in particular, bringing in lower returns. It is illustrative to note that New Zealand's exports to Australia were down 16 percent in April 2015 compared to the same month

<sup>54</sup> 'Results from last trading event', *Global Dairy Trade*, 2015, [www.globaldairytrade.info/en/product-results/](http://www.globaldairytrade.info/en/product-results/), accessed 26 May 2015.

the previous year, and quarterly exports to April 2015 were down 14 percent compared to the same three months in 2014.

## TRADE IN SERVICES

Trade in services is another component of New Zealand's trading relationship with China. This too has been growing in recent years but far more slowly than merchandise trade. Services exports to China have risen from NZ\$936 million in 2006 to NZ\$1,410 million in 2013 (June years),<sup>55</sup> representing, respectively, 6.3 percent and 8.8 percent of New Zealand's total value of export of services. Imports of services from China are smaller, NZ\$234 million (1.9 percent) in 2006 rising to NZ\$383 million (2.6 percent) in 2013. The value of New Zealand's services exports is likely to increase significantly in future years as the number of Chinese visitors to New Zealand increases.

Current total services trade between China and New Zealand thus amounts to around NZ\$1.8 billion annually. To put this into perspective, total services trade between Australia and New Zealand in the year ending June 2013 was around NZ\$9.4 billion. The fact that New Zealand's trade in services with Australia is so much greater than that with China is no surprise given the high degree of economic integration between the two former countries and the amount of two-way investment. What is significant, however, is that whereas China emerged as New Zealand's largest merchandise trade partner in 2013, taking goods and services together as representing a more complete picture of New Zealand's external trade performance, Australia remains New Zealand's largest trading partner by a margin of around NZ\$5 billion (25 percent) over China.

## INVESTMENT FLOWS

New Zealand operates a non-discriminatory overseas investment regime, the major details of which are summarised in the table below. This ensures Chinese investment in New Zealand is treated in the same way as investment from other parts of the world (Australia is a special case).

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<sup>55</sup> *New Zealand Statistics*, 2015, [www.stats.govt.nz](http://www.stats.govt.nz)

**TABLE 10: OVERSEAS INVESTMENT IN NEW ZEALAND**

The Overseas Investment Office assesses applications from overseas investors seeking to invest in sensitive New Zealand assets – being ‘sensitive’ land, high value businesses (worth more than \$100 million) and fishing quota. People who are not New Zealand citizens or who do not ordinarily reside in New Zealand must apply for consent to invest in these assets. That requirement also applies to overseas owned or controlled companies, other incorporated or unincorporated bodies, such as partnerships or joint ventures, and trusts, as well as associates of overseas investors (who may be New Zealanders).

The regime applies both when the acquisition is made either directly or through the acquisition of securities where the ‘overseas person’ acquires 25 percent or more of the securities. To obtain a ‘sensitive land’ approval, the ‘overseas person’ must satisfy certain ‘good investor’ criteria and establish that the investment will or is likely to benefit New Zealand. Benefits are assessed against economic, environmental, social and cultural factors unless the applicant intends to reside in New Zealand indefinitely. Most major sensitive land applications are decided by two Ministers after receiving recommendations from the Overseas Investment Office. All other decisions are made by the OIO under delegated authority.

Sources: Land Information New Zealand and Bellgully<sup>56</sup>

Dairy cattle are milked on a farm, near Reporoa, south of Auckland, New Zealand

AP Photo



<sup>56</sup> ‘Overseas Investment’ *Land Information New Zealand, New Zealand Government*, no date, [www.linz.govt.nz/regulatory/overseas-investment](http://www.linz.govt.nz/regulatory/overseas-investment), accessed June 10 2015; James Gibson et. al. ‘Investment into New Zealand and the Overseas Investment Regime’ *Bellgully*, June 2011, <http://www.bellgully.co.nz/resources/resource.02843.asp>, accessed July 21 2015.

Notwithstanding the universality of New Zealand's legislation, Chinese investment in New Zealand in recent years has in select cases been controversial. In part this was triggered by Shanghai Pengxin's purchase of a holding of 16 farms then in receivership, eventually finalised in late 2012. As part of the purchase an agreement was made that the farms would be managed in partnership with the New Zealand state-owned enterprise (SOE) Landcorp and that \$15.7 million would be invested in the run-down properties over the next several years. The arguments advanced against the purchase were several-fold and not all rested on legal argument: New Zealand should not sell farmland to overseas interests, the more so since China does not permit overseas investors to buy land in China; fears that over time the Chinese owners would seek to bring the properties into vertical ownership and through transfer-pricing or other means reduce the financial return to New Zealand; fears that China's Government might control entities such as Shanghai Pengxin and would be prepared to run the operations on a non-commercial basis thus engendering unfair competition; and that New Zealand was 'selling out its heritage' for short-term gain by facilitating profits moving offshore.

These elements come together when an investment involves a 'strategic asset'. Thus, for example, both Australia and the US have restricted Chinese investments in some areas, most notably the Australian Federal Government banned Huawei from having any involvement in the National Broadband Network because of security concerns.<sup>57</sup> By contrast New Zealand has no definition of 'strategic asset', recognising that it would be a complex task, not least because public opinion is likely to take a fairly broad view against overseas ownership of many asset classes involving infrastructure, land, and resources extraction. New Zealand's legislation does not treat SOEs differently from other potential overseas investors.

*Notwithstanding the universality of New Zealand's legislation, Chinese investment in New Zealand in recent years has in select cases been controversial.*

<sup>57</sup> 'Government maintains NBN ban on Chinese telco Huawei after security briefings' ABC (October 30 2013) available at <http://www.abc.net.au/news/2013-10-29/government-maintains-nbn-ban-on-chinese-telco-huawei-after-secu/5051622>.

The Shanghai Pengxin purchase was challenged twice in court. The High Court overturned the approval given by Ministers on the basis of advice received from the OIO, citing the legal provision that the benefit to New Zealand from overseas investment must be 'substantive and identifiable'. In so doing, the court ruled that the comparison should not be between the current state of the asset and what might be done by a new overseas owner to improve that asset, but rather that the test should be whether the benefit from an overseas owner would outstrip that which a domestic owner might be expected to achieve. Effectively, therefore the court imposed a relative rather than an absolute test as to benefit. In the event, following a revised recommendation from the OIO, ministers subsequently again approved the purchase that was upheld by the Court of Appeal. Nevertheless, the court's interpretation of the 'benefit' clause has not been overturned.

Underlying the concern about Shanghai Pengxin was a general feeling of unease that China, the new investment kid on the block, was beginning to turn its attention to New Zealand. While similar sentiments greeted Japan when it first began investing in New Zealand some decades ago, it is also the case that there is something of a stronger sentiment in New Zealand today opposed to foreign ownership of New Zealand assets, particularly rural properties.

Pressures on the Auckland housing market have put more focus on foreign investors who have bought properties in the city, often – anecdotally at least – for investment purposes or for capital gain rather than as occupied residences. Such investment has been promoted offshore by New Zealand real estate companies having identified a commercial opportunity. There are, however, no reliable statistics to quantify how significant these investments are in adding to the real housing pressures that exist. Another factor is that with New Zealand currently enjoying very high net in-migration, including from China and other Asian countries, purchases of property by new New Zealand residents are being misinterpreted as being made by offshore purchasers. Overseas investment in residential property, when not triggered by the overseas investment regulations as above, is subject to the same regulations as investment by New Zealanders.



From October 1 2015 capital gains will be taxed on residential properties bought and sold within two years<sup>58</sup> and all non-resident buyers and sellers will be required to provide a tax identification number from their home country along with identification such as a passport.<sup>59</sup>

Taking a broader view New Zealand remains today, as it ever was, a net importer of capital and China today has one of the largest global pools of capital available to invest. With the FTA providing a sound framework for investment, it is not unexpected that Chinese enterprises are showing increasing interest in investing in New Zealand (as indeed they are doing elsewhere around the world).

In so doing they need to satisfy the same overseas investment criteria as any other overseas investor. Our constraint on growth is not the size of the opportunity. It is our ability to access capital, knowledge, and people, and we get to decide this in part through policy (Rt. Hon Bill English, 2012).<sup>60</sup>

It is not straightforward to calculate the total value of Chinese overseas direct investment (ODI) in New Zealand, since it is estimated that some 70 percent of total Chinese ODI goes to Hong Kong, the Cayman Islands and British Virgin Islands, from where it is invested into other countries.<sup>61</sup> Best estimates, however, suggest that China is now New Zealand's fourth largest source of foreign direct investment (FDI) stock, amounting to around 5.4 percent of the total (NZ\$5.3 billion). Hong Kong is the immediate source of most Chinese FDI, but the ultimate source is predominantly from the PRC.<sup>62</sup>

*Chinese FDI into New Zealand is relatively diversified, with the largest sector being infrastructure/utilities, followed by primary industry and food.*

<sup>58</sup> This excludes the family home, death estates or properties sold as part of a relationship property settlement; note that capital gains are already taxed on investments in properties where the investment was intended for capital gain.

<sup>59</sup> 'Govt to tighten tax on capital gains', Radio New Zealand News (May 17 2015), available at <http://www.radionz.co.nz/news/political/273847/govt-to-tighten-tax-on-capital-gains>.

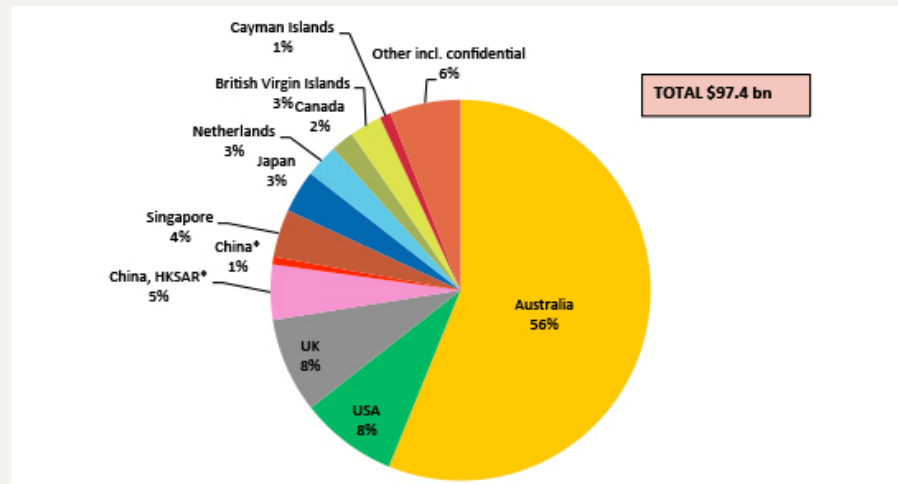
<sup>60</sup> Rt. Hon Bill English, 'Speech to the New Zealand Contemporary China Research Centre' *New Zealand Government*, August 13 2012, <http://www.beehive.govt.nz/speech/speech-new-zealand-contemporary-china-research-centre>

<sup>61</sup> Data from internal discussions with *New Zealand Trade and Enterprise*.

<sup>62</sup> Ibid.



**FIGURE 5: FDI STOCK IN NEW ZEALAND 2014 - IMMEDIATE INVESTOR BASIS**



Source: Statistics New Zealand international investment position. Immediate investor basis for March year 2014. \*China and HKSAR data is for December 2014 year, pending December year data for others countries

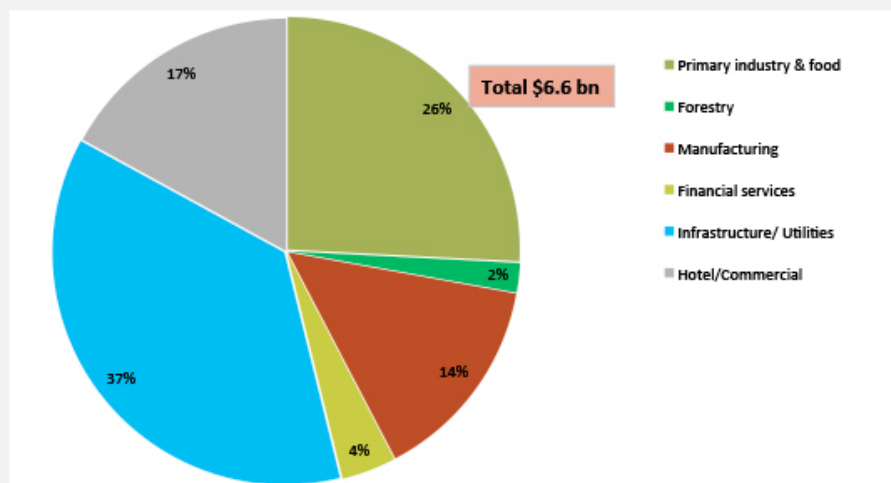
Overall, China's investments in New Zealand have risen strongly since 2011 from around a 1.5 percent share of the total to the current level. On current trends, China's share of New Zealand's FDI stock could more than double to reach 13 percent of the total by 2020. Chinese FDI into New Zealand is relatively diversified, with the largest sector being infrastructure/utilities, followed by primary industry and food. Other significant sectors are manufacturing and hotel/commercial.<sup>63</sup> As the Shanghai Pengxin case demonstrated, there is sensitivity in New Zealand around rural land sales in general and overseas investment in the dairy sector in particular. Nevertheless, actual and announced Chinese dairy investments in New Zealand are such that they are likely to reach \$2 billion by 2020, with investments being made by a number of different Chinese investors.<sup>64</sup>

Investment flows in the other direction, from New Zealand to China, remain low, with New Zealand's investment stock in China at the end of 2014 standing at NZ\$1.48 billion (0.8 percent of total external investment), ranking China 12th as an investment destination. Another three percent is invested in or through Hong Kong.

<sup>63</sup> Ibid.

<sup>64</sup> Ibid.

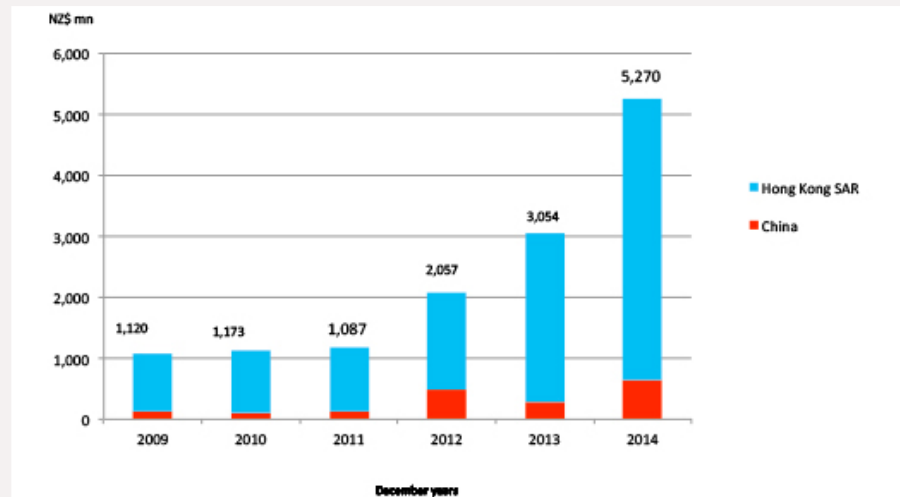
**FIGURE 6: CHINESE FDI IN NEW ZEALAND - BY SECTOR (MAY 2015 ACTUAL & ANNOUNCED) - ULTIMATE INVESTOR BASIS**



Total committed and announced FDI from China including HKSAR was \$6.6 billion to May 2015. Source NZTE China FDI/ODI database.

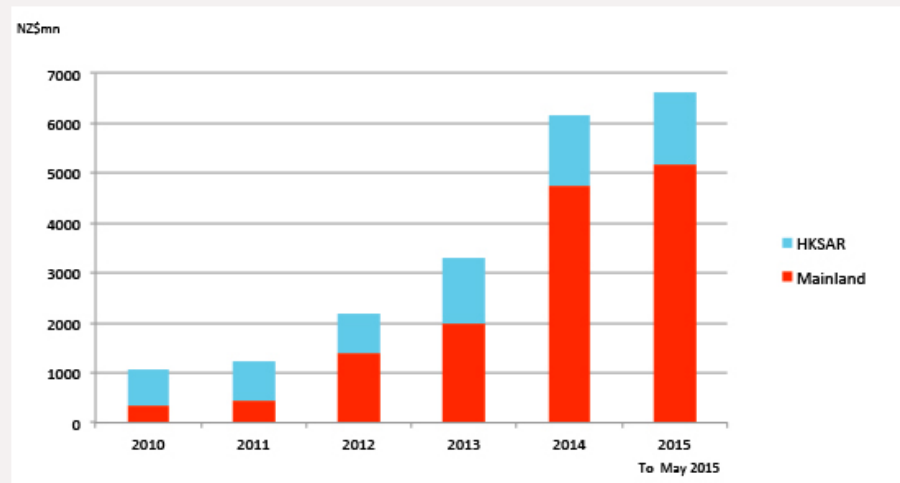
While this is almost a threefold increase on 2009, ODI committed in 2014 was less than five years earlier. A number of New Zealand companies have invested in China in past years, but outcomes in many cases were such that decisions were taken to back out of the investments made. In general, investment flows in both directions are not commensurate with the trade flows or with the general state of the overall bilateral relationship. The potential economic benefits stemming from enhanced investment in both directions are therefore yet to be realised.

**FIGURE 7: STOCK OF DIRECT INVESTMENT FROM CHINA - IMMEDIATE INVESTOR BASIS**



Based on immediate investor basis, ie the jurisdiction of registration of the investing entity, not the ultimate investor. HK 2014 is to end of Sept quarter as Dec quarter is confidential. Source: Statistics New Zealand.

**FIGURE 8: CHINESE FDI IN NEW ZEALAND BY ULTIMATE INVESTOR (ACTUAL AND ANNOUNCED)**



Source: NZTE China FDI/ODI database

## CHINESE STUDENTS IN NEW ZEALAND

From the latter part of the 1990s, New Zealand, like other developed countries particularly in the English-speaking world, attracted increasing numbers of Chinese students to its educational institutions. Initially, Chinese students focused heavily on English language learning opportunities with the consequence that a significant number of for-profit private training establishments opened up in response to the emerging market opportunity. Too many schools providing an inadequate learning experience while not providing sufficient pastoral care and support led inevitably to failures in the business model with a consequent negative fallout on New Zealand's reputation as a destination for China's students.

The lesson drawn from this unhappy experience was that a laissez-faire approach to a sector such as education carried with it undue reputational risk and that a more regulated framework was required. It was also a demonstration that the Chinese Government was taking increased interest in the wellbeing of its citizens abroad and that it was prepared to take action to protect their interests. New Zealand accordingly moved as quickly as possible to strengthen its regulatory framework around private educational institutions and engaged actively with the Chinese authorities to have New Zealand reinstated as a favoured study destination. New Zealand was able to regain the necessary trust in its systems both by strengthening the compulsory Code of Practice for the Pastoral Care of International Students and by reinforcing fee protection schemes for private educational providers, and Chinese students continued to come to New Zealand.

Chinese student numbers in New Zealand peaked in the 2002-04 period at around 40,000 per annum<sup>65</sup> with numbers now stabilising at around the 23-24,000 mark.<sup>66</sup> Proportionally, the numbers declined from more than half of all international students in New Zealand in 2006 to just less than 27 percent in 2012. Chinese students remain, however, the largest single group of overseas students.

<sup>65</sup> Paul Merwood, 'International Students: Studying and Staying in New Zealand', Ministry of Business, Innovation and Employment, 2007, <http://www.dol.govt.nz/publication-view.asp?ID=235>

<sup>66</sup> 'International Student Enrolments in New Zealand 2006-2012', *Education Counts*, Ministry of Education, May 2013, <https://www.educationcounts.govt.nz/statistics/international-education/international-students-in-new-zealand>

They are enrolled in every kind of New Zealand educational institution ranging from primary school to university, although the numbers at primary and secondary school level are fewer than those at higher levels.

The precise economic contribution of Chinese students in New Zealand is difficult to ascertain. In 2012, overseas students are estimated to have provided total economic value-add of \$2.6 billion to the New Zealand economy.<sup>67</sup> Proportionally, therefore, Chinese students can be assumed to have provided around \$700 million of this total. While the proportion of Chinese students in New Zealand has declined, they continue to make a significant contribution to international education earnings.

Is New Zealand attracting a good proportionate share of China's students studying abroad? Raw figures suggest perhaps not. In 2012, of the 694,400 Chinese students studying abroad at tertiary level, only around 11,300 or 1.6 percent were studying in New Zealand.<sup>68</sup> By contrast, more than 85,000 were studying in Australia. There are a number of factors working against New Zealand increasing numbers: New Zealand's tertiary institutions are ranked lower than a number of Australian counterparts; Australia is closer to China and there are more cities with direct air connections to China; the cost of study in New Zealand has risen proportionally because of the stronger New Zealand dollar – but there should be scope for lifting student numbers and, thus, earnings from the educational sector.

China is investing significantly in its own tertiary educational institutions and over time it can be expected that an increasing number of students, undergraduates in particular, will stay at home for their education. Thus it is likely that New Zealand will be competing even more with other countries to attract its share of a relatively diminishing market. This suggests that tertiary education institutions themselves will have to ensure that they will be able to market themselves through demonstrable excellence in teaching

<sup>67</sup> 'New Zealand Schools – Trends in International Enrolments to 2013', *Education Counts*, Ministry of Education, July 2014, <https://www.educationcounts.govt.nz/publications/series/2531>

<sup>68</sup> 'International Student Flows', *UNESCO*, 2014, [www.uis.unesco.org/Pages/international-student-flow-viz.aspx](http://www.uis.unesco.org/Pages/international-student-flow-viz.aspx), accessed May 28 2015.

and research and that New Zealand will have to maintain – or better, enhance – its reputation as a place where, in addition to receiving a quality education, students can live and enjoy a safe environment and welcoming society.

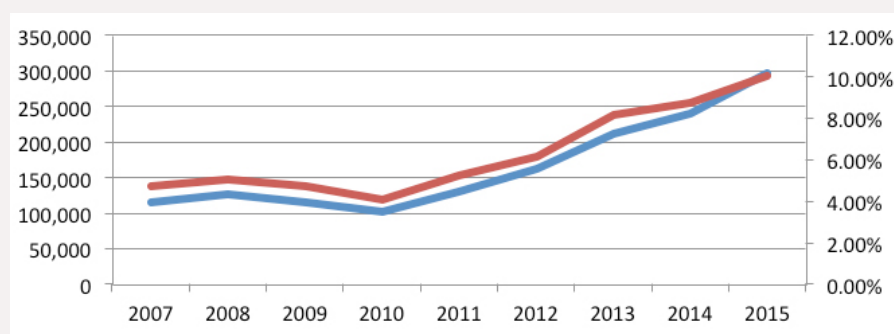
## TOURISM

China has no longstanding tradition of its citizens travelling abroad so the entire concept of 'Chinese tourism' is a new construct. The number of Chinese travelling to other countries is growing rapidly, reaching 107 million in the year ending November 2014.<sup>69</sup> Eighty-five percent of these travel within Asia, the majority of going to Hong Kong and Macau. Overall New Zealand ranks 19th in China's list of most preferred destinations (Australia ranks 15th with a little fewer than twice New Zealand's numbers according to Chinese figures).

As part of the growing trend for Chinese to travel abroad, Chinese visitor numbers to New Zealand have grown as shown in the figure below.<sup>70</sup>

*The economic return to New Zealand from Chinese visitors is likely to continue to increase, provided that the needs of visitors continues to be met.*

**FIGURE 9: CHINESE VISITORS TO NEW ZEALAND  
(2007-15, YEAR TO MARCH)**



Source: International Visitor Arrivals to New Zealand, Department of Statistics, March 2011 and March 2015.

The numbers continue to increase, with the 300,000 mark being exceeded on an annual basis for the first time in the year to April 2015,<sup>71</sup>

<sup>69</sup> 'China Outbound Tourism in 2014' *Travel China Guide*, no date, [www.travelchinaguide.com/tourism/2014statistics/outbound.htm](http://www.travelchinaguide.com/tourism/2014statistics/outbound.htm), accessed May 28 2015.

<sup>70</sup> 'International Visitor Arrivals to New Zealand', *Statistics New Zealand*, March 2011 and March 2015, <http://www.stats.govt.nz>

<sup>71</sup> 'Tourism New Zealand Corporate Website', *Tourism New Zealand*, no date, [www.tourismnewzealand.com](http://www.tourismnewzealand.com) accessed May 28 2015.

a growth rate of 26 percent year-on-year. China is now New Zealand's second largest source of tourists (after Australia, which remains far and away the largest). Over the 2007-15 period, the median length of stay of Chinese visitors to New Zealand has increased from around 3.5 days to 6.0 days (the overall median length of stay for visitors to New Zealand is 9.0 days).<sup>72</sup>

Following the enforcement of China's ban on 'shopping' tours in October 2013, there has been a change in the visitor mix from China. Although most Chinese visitors still come in organised tour groups (around 58 percent), there has been a nearly 70 percent increase in independent travellers touring New Zealand in camper vans and the like. Along with this change in the kind of tourists visiting New Zealand has come a significant increase in the number of 'stay days' per visitor. These changes suggest that the economic return to New Zealand from Chinese visitors is likely to continue to increase, provided that the needs of visitors continues to be met. In terms of the demographics of Chinese visitors, the majority fall into older age groups.

*New Zealand's strategy has been to promote New Zealand as a high-value destination to attract visitors who are high spenders and potential return customers rather than pursue an approach of increasing numbers at all costs.*

There is no indication that China's newfound interest in overseas travel is likely to abate in the near future; indeed, there are forecasts that numbers will double and spending triple by 2020.<sup>73</sup> While this prospect is welcome for New Zealand from an overall economic perspective, it also holds significant challenges. In particular, is the investment available to ensure that the visitor experience Chinese tourists will be seeking will be in place when required? Does New Zealand have in place the right marketing channels to ensure that an appropriate share of the growing numbers of Chinese travelling overseas will look to New Zealand? Or, conversely, are there risks of being swamped with demand?

The last point is an important one. Is there a risk of demand from China not only outstripping New Zealand's tourist infrastructure, but also as a consequence of ever-increasing numbers resulting in a diminution of the New Zealand experience? Already, around 10 percent of all international tourists globally are Chinese and in total

<sup>72</sup> Ibid.

<sup>73</sup> 'Asia's Independent Voice', *CLSA Website*, no date, <https://www.clsa.com/the-independent-view.php>, accessed 28 May 2015.

they are the largest spenders while travelling (some 50 percent more than Americans travelling abroad). Yet only around five percent of Chinese have passports.<sup>74</sup> Some impacts are already being felt: accommodation in many New Zealand centres, for example, was fully taken up this year when Chinese New Year coincided with the Cricket World Cup.

New Zealand's strategy has been to promote New Zealand as a high-value destination to attract visitors who are high spenders and potential return customers rather than pursue an approach of increasing numbers at all costs. The trends noted above suggest that this approach is bearing fruit, but risks and challenges remain.

### LESSONS FROM THE NEW ZEALAND-CHINA FTA

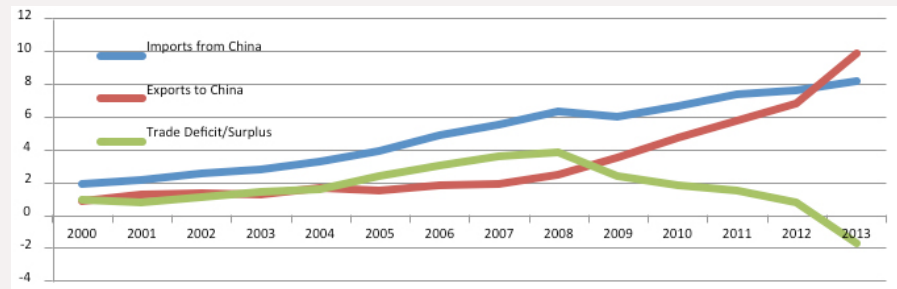
The New Zealand-China FTA has been followed by significant growth in New Zealand exports to China, particularly but not exclusively, rapid growth in dairy and timber exports as well as deepening economic relations in services (education and tourism), economic cooperation and investment. New Zealand has turned a trade deficit with China into a trade surplus in the post-FTA years when many traditional export markets have remained flat. Research shows New Zealand's trading relationship with China has provided welfare gains for both exporters and New Zealand consumers.

Urbanisation and growing household incomes, combined with problems in China's own dairy sector, have resulted in a significant increase in global demand for our primary export products and the continuing industrialisation of China's economy has resulted in significant downward pressure on the prices of many of our imported goods. The resulting increase in our terms of trade has meant a significant increase in New Zealanders' purchasing power.<sup>75</sup>

<sup>74</sup> 'Coming to a beach near you', *The Economist*, April 19 2014, <http://www.economist.com/news/international/21601028-how-growing-chinese-middle-class-changing-global-tourism-industry-coming>

<sup>75</sup> Ross Kendall, 'Economic Linkages Between New Zealand and China' *Reserve Bank of New Zealand Analytical Note Series AN2014/06*, October 2014, [http://www.rbnz.govt.nz/research\\_and\\_publications/analytical\\_notes/2014/an2014\\_06.pdf](http://www.rbnz.govt.nz/research_and_publications/analytical_notes/2014/an2014_06.pdf)



**FIGURE 10: NEW ZEALAND-CHINA IMPORTS, EXPORTS AND TRADE SURPLUS/DEFICIT (2000-13)**

Source: Statistics New Zealand (2014); Units: Billion (1,000 million) NZD.

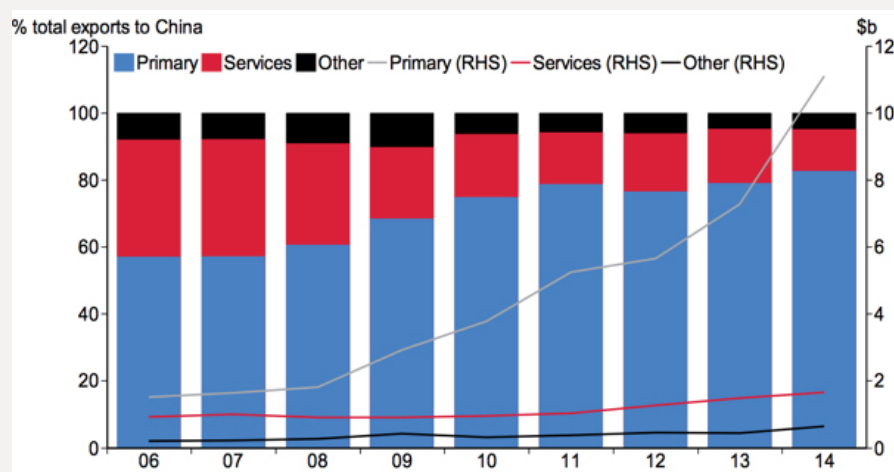
*While major growth of New Zealand commodity exports to China has been very positive for the New Zealand economy, growth in value-added exports and services has been far less impressive.*

Some business leaders have argued the FTA has not delivered comprehensive market access for New Zealand firms as significant non-tariff and behind the border barriers remain. These include issues with rules of origin, compliance with domestic regulations such as newly introduced food safety regulations and problems understanding Chinese consumer behaviour.<sup>76</sup>

While major growth of New Zealand commodity exports to China has been very positive for the New Zealand economy, growth in value-added exports and services has been far less impressive. The FTA has done less than hoped to facilitate New Zealand firms' integration into global value and supply chains and for New Zealand businesses to capture more of the wealth created in the supply chain.

<sup>76</sup> For example: 'Fonterra dairy recall shakes China consumer confidence' *Financial Times*, August 4 2013, <http://www.ft.com/intl/cms/s/0/c6b1585e-fcef-11e2-955a-00144feabdc0.html#axzz3cWEJN10r>

**FIGURE 11: COMPOSITION OF NEW ZEALAND EXPORTS TO CHINA (2006-14)**



Source: Kendall (2014:7).<sup>77</sup>

**TABLE 11: TOP FIVE EXPORT CLASSIFICATIONS BETWEEN NEW ZEALAND AND CHINA (2008 & 2013)**

	Chinese Exports to New Zealand		New Zealand Exports to China	
	2008	2013	2008	2013
Machinery & electrical machinery	2.3	3.1	Dairy produce	0.52 4.6
Apparel and clothing	0.9	1.0	Wood	0.34 1.9
Furniture	0.3	0.5	Meat	0.096 0.88
Iron or steel	0.3	0.3	Wool	0.19 0.40
Toys	0.14	0.27	Seafood	0.13 0.39
<b>TOTAL</b>	<b>6.4</b>	<b>8.3</b>	<b>TOTAL</b>	<b>2.5 9.96</b>

Source: Statistics New Zealand (2014); Units: Billion (1,000 million) NZD.

The key to New Zealand's economic future is moving up the value chain. However the lion's share of growth in New Zealand exports to China has been in low value commodity products, namely milk powder and logs. An argument is made that instead of using the FTA as an opportunity for upgrading New Zealand exports, the FTA has encouraged intensification of commodity exporting industries and the 'downgrading' of the New Zealand economy. The FTA has provided significant opportunities for New Zealand companies to

<sup>77</sup> Ross Kendall, 'Economic Linkages Between New Zealand and China'.

provide intermediate goods in global supply and value chains through partnerships and trade with Chinese companies but '[u]nless New Zealand producers take steps to upgrade their GVCs they may become little more than a Chinese cost centre'.<sup>78</sup> As the Treasury pointed out in March 2014:

[Our] position as the 'small partner' in the trade relationship may limit our exporters' ability to move up the value chain in later years. Indeed, while Chinese demand looks set to provide a stable base for future exports, such trade may increasingly be on their terms as buyers rather than our terms as sellers. This underlines the importance of exporters being ready to adapt to market conditions and to continue to look for opportunities to add value.<sup>79</sup>

Some critics argue that the FTA has allowed Chinese firms to vertically integrate their businesses and supply chains at the expense of New Zealand firms as Chinese firms make moves to get further down the supply chain. For example New Zealand's biggest company Fonterra has been losing farmer shareholders in response to a low dairy forecast payout in 2015, as rivals like Yili and Yashili offer better deals to supply their newly established processing facilities.<sup>80</sup> As discussed earlier, New Zealand investment in China is comparatively low. Moreover, some companies operating in the Chinese market have experienced regulatory challenges such as delays in approvals that have significantly impacted their operations and bottom line.

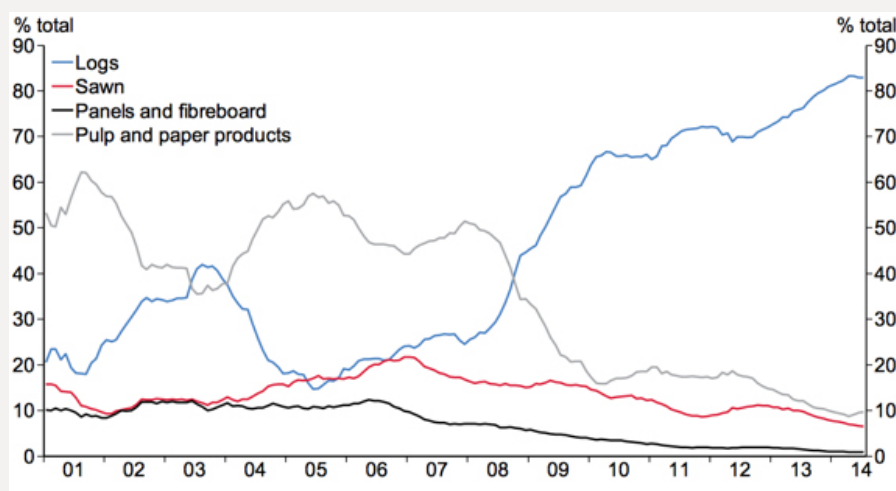
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<sup>78</sup> Christina Stringer. 'Christina Stringer says there is an urgent need for New Zealand companies to upgrade their GVCs to avoid becoming little more than Chinese cost centres' *Interest.co.nz*, September 23 2014, <http://www.interest.co.nz/business/72103/christina-stringer-says-there-urgent-need-new-zealand-companies-upgrade-their-gvcs>

<sup>79</sup> 'Special Topic: Should we worry about New Zealand's trade concentration?' *Monthly Economic Indicators March 2014*, The Treasury, 2014, <http://www.treasury.govt.nz/economy/mei/mar14/03.htm>

<sup>80</sup> 'Farmers sign up with Chinese milk processors' *Radio New Zealand News*, June 9 2015, <http://www.radionz.co.nz/news/rural/275738/farmers-leave-fonterra-for-rivals>

FIGURE 12: COMPOSITION OF FORESTRY EXPORTS TO CHINA



Source: Kendall (2014:10).

For 2015, New Zealand exports were \$4.2 billion, \$240 million or 5.5 percent lower than in April 2014. This drop is led by a \$237 million or a 66 percent drop in exports of whole milk powder to China.<sup>81</sup>

New Zealand's trade with China has also met challenges such as trade interruptions brought on by failure to adapt quickly enough to changed regulatory processes and uncharacteristic safety recalls. The 2008 melamine crisis that brought down Sanlu, a Chinese dairy company in which Fonterra held a 43 percent stake, was followed in January 2013 by residue of the fertilizer DCD being said to be detected in Fonterra milk. In August 2013 Fonterra whey protein concentrate tested positive for a bacteria that causes botulism, and its products were recalled in several countries. Further testing revealed it was a false positive. In February 2014 the Ministry of Primary Industries charged Fonterra for breaching food safety laws in its handling of the whey batch in question, and failure to 'escalate' the initial findings early. As the Minister of Trade, Tim Groser notes, while these issues should never have happened:

*The New Zealand-China FTA is one of New Zealand's major trade success stories. The growth in trade with China propelled by the FTA, has transformed the profile of New Zealand's global export business*

<sup>81</sup> 'Dairy weighs on trade balance' *New Zealand Herald*, May 27 2015, [http://m.nzherald.co.nz/business/news/article.cfm?c\\_id=3&objectid=11455100](http://m.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11455100)

Tins of Fonterra's Anlene milk powder in a Shanghai supermarket  
August 2013  
AP Photo



The evidence of the fact that we've moved on beyond that is the fact that normal trade is moving forwards, we've seen sales increase in China right across the board and we're well ahead of a year ago ... at the end of the day when you're dealing with adults in whatever culture you're dealing with - people understand that people make mistakes, it's how you deal with them that is the test of what they think of you after the event.<sup>82</sup>

The New Zealand-China FTA is one of New Zealand's major trade success stories. The growth in trade with China propelled by the FTA, has transformed the profile of New Zealand's global export business, even if not all of that growth can be credited to the agreement. The FTA has not, however, been a universal panacea for New Zealand traders' challenges in China. Nor was it ever expected to be. Questions now being asked about the detailed impact of the agreement need to be reflected on by both government and business. Barriers behind the border in China remain posing a challenge to the full realisation of the FTA's potential. But questions about the FTA's impact also need to look at what is happening behind New Zealand's borders too.

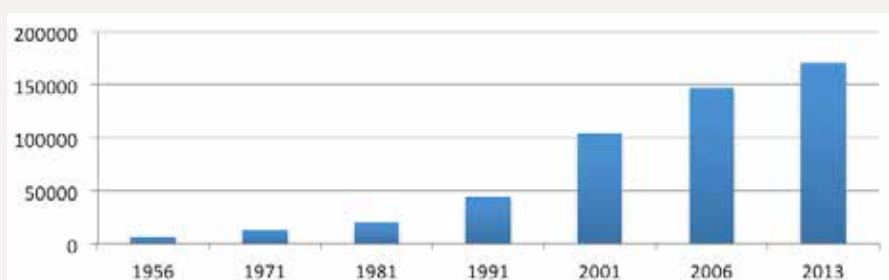
<sup>82</sup> Tim Groser, 'Chinese dairy consumers 'moving on'', *Radio New Zealand*, April 11 2014, <http://www.radionz.co.nz/news/rural/241363/chinese-dairy-consumers-'moving-on'>

## PEOPLE

### IMMIGRATION

The first Chinese immigrants came to New Zealand about a century and a half ago. The numbers of Chinese resident in New Zealand fluctuated around the 4,500-5,000 mark over the last 25 years of the 19th century, and then gradually declined to little more than half of that number until the mid-1930s, reflecting deaths of the first generation of immigrants, onward and return migration and legislative barriers and social discrimination that deterred Chinese migration to New Zealand. The 1936 census recorded 2,943 residents in New Zealand identified as Chinese. By the time of the first post WWII census in 1945, numbers had increased by around 2,000.<sup>83</sup> The numbers then increased steadily as shown in the figure below:

**FIGURE 13: CHINESE RESIDENTS IN NEW ZEALAND**



Source: New Zealand Statistics Census Data

In 2013 one in every four New Zealand residents was born overseas (compared to one in five in 2001 and one in seven in 1961). This is higher in Auckland where 39 percent are overseas-born.<sup>84</sup> The proportions of those of Chinese ethnicity born in New Zealand compared to those born overseas have changed markedly. In 1991, for example, approximately one third of the total Chinese population was New Zealand-born;<sup>85</sup> this had decreased somewhat to 26.6 percent in 2015.<sup>86</sup>

<sup>83</sup> 'New Zealand Official Yearbook 1990' Statistics New Zealand, 1991.

<sup>84</sup> 'Our Futures: Te Pae Tawhiti, The 2013 Census and New Zealand's changing population', *The Royal Society of New Zealand*, 2014, p. 6, <http://www.royalsociety.org.nz/expert-advice/papers/yr2014/our-futures/>

<sup>85</sup> '2001 Census: Asian people (2001) – Reference Report' *Statistics New Zealand*, no date, <http://www.stats.govt.nz/Census/2001-census-data/2001-census-asian-people/highlights.aspx>

<sup>86</sup> '2013 Census ethnic group profiles: Chinese' *Statistics New Zealand*, no date, [http://www.stats.govt.nz/Census/2013-census/profile-and-summary-reports/ethnic-profiles.aspx?request\\_value=24737&parent\\_id=24726&tabname=#24737](http://www.stats.govt.nz/Census/2013-census/profile-and-summary-reports/ethnic-profiles.aspx?request_value=24737&parent_id=24726&tabname=#24737)

*The general trend in the number of long-term arrivals (i.e. 12 months or longer) in New Zealand from China is a steady increase*

This change reflects large-scale migration from Asia, especially China, in the period from 1986, as discussed below.

Between March 1986 and March 2006, New Zealand's resident population that had been born in countries in Asia increased almost sevenfold, from 32,685 to 248,364. The Chinese component of the Asia-born population increased even more – by more than 800 percent during the 20 years. The population that identified with Asian ethnicities (including New Zealand-born) increased by 550 percent.<sup>87</sup>

As is the case in other migrant settlement countries, 'permanent residence' migrants in New Zealand are not always permanent. Immigration New Zealand data suggests that about 28 percent of all permanent residence migrants arriving between 1998 and 2011 had left New Zealand for six months or more by the end of 2011. Among Asian migrants this number varied between countries of origin, with China as high as 40 percent. Many of the 'out-migrants' from China had come in the 'investor' category, with much lower rates among those who had originally arrived on work or student visas.<sup>88</sup>

The general trend in the number of long-term arrivals (that is, 12 months or longer) in New Zealand from China is a steady increase, with 7,894 arrivals in the year to April 2013, 8,636 in 2014 and 10,126 in 2015.<sup>89</sup> Long-term departures have been stable for the past several years at around 2,500 per annum. The majority of migrants settle in the Auckland area – where almost a quarter of New Zealand's total Asian population live<sup>90</sup> with significant concentrations in some parts of the city resulting in a 'Sinification'<sup>91</sup> of some areas, with some suburbs recording at least 50 percent (and up to 80 percent) of its residents as Chinese.<sup>92</sup> On the whole, this appears not to have resulted in significant concern by the wider community. It has also not gone unnoticed in China, with one Chinese visitor, for example,

<sup>87</sup> Bedford and Ho, 'Asians in New Zealand: Implications of a Changing Demography', *Asia New Zealand Foundation*, 2008, p. 11.

<sup>88</sup> Friesen, 'Asian Auckland: The multiple meanings of diversity', *Asia New Zealand Foundation*, 2015, p. 12.

<sup>89</sup> 'International Travel and Migration', *Statistics New Zealand*, April 2015, [www.stats.govt.nz](http://www.stats.govt.nz)

<sup>90</sup> 'Our Futures: Te Pae Tawhiti, The 2013 Census and New Zealand's changing population', p. 6.

<sup>91</sup> Professor Paul Spoonley, address to *Institute of Public Administration New Zealand*, July 2013.

<sup>92</sup> Friesen, 'Asian Auckland'.

noting ‘we face a degree of racism in the West, but New Zealanders are unique in their warmth and openness towards Chinese people’.<sup>93</sup>

The Asia New Zealand Foundation’s annual social attitudes survey in 2014 showed that 80 percent of New Zealanders see Asia as important to New Zealand’s future with 84 percent saying it was important that New Zealand develop cultural and economic ties with Asia, and 91 percent viewing export market opportunities and tourism as beneficial to New Zealand.<sup>94</sup> New Zealanders’ attitudes were more mixed toward investment (64 percent positive) and immigration (53 percent positive). In both cases this reflected high media attention and was directed toward China and Chinese people. Previous surveys have, however, revealed New Zealanders have more positive attitudes toward Asia (and China) than either Australia or Canada.<sup>95</sup>

A small but increasing percentage (10.3 percent) of Chinese in New Zealand have multiple ethnicities. This is particularly true for Chinese under 15 years of age, of whom almost 30 percent have more than one ethnicity.<sup>96</sup> This indicates an increased level of integration that bodes well for maintaining a socially cohesive society. Combined with the quarter of the Chinese population New Zealand-born, this suggests a growing diversity in the type and experience of Chinese in New Zealand.<sup>97</sup>

## CHINESE LANGUAGE IN NEW ZEALAND

The teaching of Chinese in New Zealand schools is relatively recent, with the numbers of students learning Chinese increasing quite significantly in recent years. Chinese is now the fourth most widely studied foreign language (overtaking German), though nearly five times as many students learn French at secondary school. Most of this growth in Chinese language has been at primary level.

<sup>93</sup> *The Listener*, May 16 2015, p. 12.

<sup>94</sup> ‘New Zealanders’ perceptions of Asia and Asian peoples – 2014 Annual Survey’, *Asia New Zealand Foundation*, 2015.

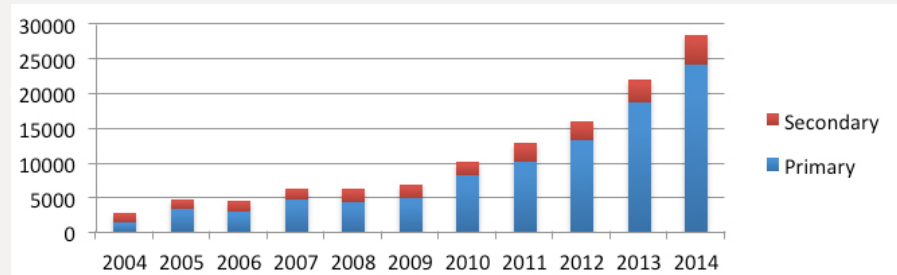
<sup>95</sup> ‘New Zealanders’ perceptions of Asia and Asian peoples – 2014 Annual Survey’, *Asia New Zealand Foundation*, 2015, p. 25.

<sup>96</sup> ‘2013 Census ethnic group profiles: Chinese’, *Statistics New Zealand*, no date, [http://www.stats.govt.nz/Census/2013-census/profile-and-summary-reports/ethnic-profiles.aspx?request\\_value=24737&tabname=Age,sex,andethnicities](http://www.stats.govt.nz/Census/2013-census/profile-and-summary-reports/ethnic-profiles.aspx?request_value=24737&tabname=Age,sex,andethnicities)

<sup>97</sup> See Friesen, ‘Asian Auckland’ for discussion about the diversity of the Asian populations in Auckland.



**FIGURE 14: STUDENTS STUDYING CHINESE LANGUAGE IN NEW ZEALAND SCHOOLS**



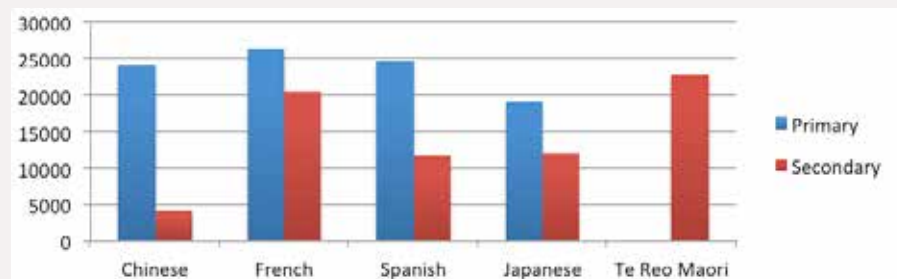
Source: Education Counts<sup>98</sup>

*The proportion of students learning Chinese is disproportionate to the importance of China as a global power and trade and economic partner of New Zealand.*

These numbers have continued to increase, with those learning Chinese at primary level increasing to around 24,000 in 2014. However, only just over 60 secondary schools offer the language. As the New Zealand China Council has pointed out, the proportion of students learning Chinese is disproportionate to the importance of China as a global power and trade and economic partner of New Zealand.<sup>99</sup>

A recent survey by the Asia New Zealand Foundation showed that 83 percent of New Zealanders thought that New Zealand school children should learn a language other than English with 49 percent saying that that language should be Chinese.<sup>100</sup>

**FIGURE 15: SECOND LANGUAGE LEARNING IN NEW ZEALAND PRIMARY AND SECONDARY SCHOOLS (2014)**



Source: Education Counts<sup>101</sup>

<sup>98</sup> 'Subject Enrolment', *Education Counts*, New Zealand Government, 2015, <https://www.educationcounts.gov.nz/statistics/schooling/student-numbers/subject-enrolment>

<sup>99</sup> 'A Crisis of Complacency? Chinese language learning in New Zealand', *New Zealand China Council*, April 29 2015, <http://www.nzchinacouncil.com/#1A-Crisis-of-Complacency-Chinese-language-learning-in-New-Zealand/cykj/555a84860cf23d0164a50440>

<sup>100</sup> 'New Zealanders' perceptions of Asia and Asian peoples', *Asia New Zealand Foundation*, 2015, <http://asianz.org.nz/reports/wp-content/uploads/2015/02/ANZF1046-Perceptions-of-Asia-Report2.pdf>

<sup>101</sup> 'Subject Enrolment', *Education Counts*, New Zealand Government, 2015, <https://www.educationcounts.gov.nz/statistics/schooling/student-numbers/subject-enrolment>

## PEOPLE-TO-PEOPLE

While it may be true as Lord Palmerston once said that ‘nations have no permanent friends and allies, they only have permanent interests’, the same cannot necessarily be said of individuals. Indeed individuals such as Rewi Alley and others who went to China in the first part of the 20th century played a meaningful role in helping lay the foundation for today’s bilateral relationship. So it is today. While the focus of this paper has largely been on the New Zealand end of the relationship, if it is to flourish exchanges and contacts need to be in both directions. New Zealand will always struggle to command even minimal attention in China. But it’s important that engagement takes place in both directions.

New Zealand needs to encourage more New Zealand students to take up the opportunities available to study in China and other channels bringing together New Zealanders and Chinese need to be promoted. The Prime Ministers’ Scholarships to Asia are successful in this; the majority of New Zealand students use their scholarships to study in China. The Asia New Zealand Foundation has several programmes which give New Zealand educators, journalists, business people and academics exposure to China, its people and its thinking. The Asia New Zealand Foundation, along with the China Council also raise New Zealanders’ awareness of China through high-profile research and media interviews. New Zealand has 31 sister city relationships with China and these cover a range of levels of activity and usefulness. They provide a way of bringing people into contact with each other and laying the foundation for at least a modest constituency for New Zealand in China. Perhaps even more importantly, sister city links provide a channel for establishing direct links with areas of China that are outside central control.

*New Zealand's future is increasingly bound with China's continued growth and prosperity.*

## CONCLUSION

New Zealand's future is increasingly bound with China's continued growth and prosperity. Perhaps not inextricably, but certainly the way that China tracks over the next decade and beyond will have a profound impact on whether New Zealand prospers as a nation. Most public and political commentary in New Zealand focusses on the state of the economic relationship. It is hard to overstate its importance for New Zealand's prosperity. But what underpins and sustains that relationship is much more than the ability to continue to produce commodities and services that can be sold to Chinese customers or the willingness and ability to provide opportunities for Chinese business to become more involved in New Zealand's growth. New Zealand governments have generally been strong in understanding and espousing the need for a broad-based, politically-founded relationship with China, without which all aspects of New Zealand's aspirations to maintain and grow ties with that country remain fragile. New Zealand has been consistent, flexible, imaginative, sometimes opportunistic but generally realistic about the way it has gone about building what is now by some distance its most important relationship in Asia and one of its most important anywhere. China for its part gives every indication that it still sees value in dealing with New Zealand as a serious partner.

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The New Zealand Contemporary China Research Centre aims to be a global leader in knowledge acquisition and knowledge sharing on political, economic and social life of contemporary China among tertiary institutions, the business sector and the policy community for the benefit of New Zealand.

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