

Australian Services Trade in the Global Economy

Excerpt: Tourism

Executive summary

The ongoing structural transformation towards a services economy, across all countries and at all levels of development, has immense potential to improve the well-being of Australians. Technology has reduced trade and transaction costs for both goods and services, thereby facilitating more complex and services-intensive production networks. Telecommunications, audio-visual and computer services constitute a digital network at the heart of the world trading system. Transportation, courier, logistics and distribution services form the backbone of global supply chains. Legal, accounting, insurance and banking services are essential enablers of trade and finance. Architectural, engineering, mining and constructions services are a fundamental foundation of physical infrastructure. Health, education and tourism services are at the heart of better lives.

Yet impediments to services trade remain pervasive, while trade and regulatory policy in these individual services sectors are often made with limited regard for economy-wide impacts. This report aims to provide a better understanding of Australia's services performance in the global economy, to inform trade and regulatory policy makers of the likely effects of unilateral or concerted reforms and to help prioritise policy action. Taken together, the main findings seek to contribute to a national strategy by which Australia can fully capitalize on the strength of its services sectors and exporters to ensure that services trade works for all Australians.

Main findings

Services are Australia's gateway to global markets

Australia's regional and global services trade and productivity performance is strong. Services exports, and services embedded in other exports such as food products, machinery and electronics, account for half of Australia's exported domestic value added. There is evidence, however, that Australian services suppliers face increasing competition. As such, a national services trade strategy can help sustain and strengthen Australia's comparative advantages.

Australia's services regulatory environment is a source of strength

Australians benefit from an open, efficient and generally pro-competitive regulatory environment that is favourable relative to many of its peers. Australia's domestic regulatory regime is more liberal than average in 21 of the 22 services sectors measured by OECD Services Trade Restrictiveness Indicators. There is scope for improvement in all sectors, however, and a targeted regulatory reform agenda can ensure that Australia's business environment remains a source of international competitiveness.

Global services sector growth is an opportunity for Australians

Technical progress, urbanisation and fast-growing markets are driving a rising share of services in consumption across the globe, and Australian exporters are well positioned to capitalize on these trends. Rapid change and dynamic demand factors, however, require adaptation and new approaches to maintain existing strongholds and gain ground in new and diversified markets, especially in strategic sectors such as education, travel and tourism services.

Ambitious services trade policy can transform bottlenecks into gateways

Services trade restrictions and regulatory heterogeneity impose costs on services and manufacturing sectors, with a disproportionate burden falling on small and medium sized enterprises (SMEs). Enhanced commercial opportunities for Australian exporters can be secured by concerted efforts to encourage behind-the-border regulatory reforms in key markets (through fora such as the G20 and APEC), coupled with an ambitious trade negotiating agenda to secure new market access and bind applied regulatory regimes.

Strategic national reforms can boost Australia's services trade competitiveness

Services generate more than two-thirds of global gross domestic product (GDP), attract over three-quarters of foreign direct investment (FDI) in advanced economies, employ the most workers, and create most new jobs globally. The OECD recommends that countries adopt a whole-of-government approach to co-ordinated services trade policy and regulatory reforms as a driver of inclusive economic growth and employment, and encourages Australia to seize this opportunity. Horizontal and sector-specific policy conclusions are presented in the final chapter of this report.

Whole-of-report policy conclusions

The analysis carried out in this report highlights the importance of services in the Australian economy. Evidence demonstrates the relative strength of Australia's services trade and productivity performance, and the opportunities arising from Australia's proximity to the world's most dynamic region. The report also highlights the challenges faced by Australian services exporting firms, including the risk of losing ground in stronghold sectors such as education and tourism. Furthermore, the empirical evidence included in the report highlights how services trade restrictions in foreign countries prevent Australia from exploiting its full export potential.

In this context, there is significant potential for services to sustain productivity and enhance the global competitiveness of Australian businesses. This section delineates key factors to be considered in response to the opportunities and challenges posed by a rising degree of globalisation and a growing tradability of services. On this basis, a strategic whole-of-government approach to the performance of Australian services in the global economy can help Australians fully capitalize on the strength of its services sectors and exporters to ensure that services trade works for all.

General key findings

- It is important to continue to promote regulatory reforms and the reduction of services trade restrictions in the applied regimes of priority markets abroad by, inter alia, advocating the potential of services reforms to drive inclusive economic growth and employment, ensuring the effective implementation of the APEC Services Competitiveness Roadmap and encouraging national and collective actions consistent with the G20 Strategy for Global Trade Growth.
- In addition to existing FTAs, it would be beneficial to continue pursuing bilateral, plurilateral, regional and multilateral trade agreements with ambitious market access, national treatment and domestic regulation provisions for services. Besides maximising the economic benefits accruing to Australians, this would also lock applied regimes and thereby secure a predictable and rules-based environment for services trade and investment. OECD empirical analysis confirms that the legal bindings found in services trade agreements tend to have a positive effect on services trade by reducing uncertainty.
- Continued investment in an efficient and effective visa system is desirable. The envisaged streamlining of the current visa system would be beneficial to international visitors, international students, and domestic as well as foreign businesses.
- Consideration could be given to the relationship between the Temporary Skill Shortage (TSS) visa and the cost of recruiting highly qualified foreign workers, and the ability of some international students to apply for jobs on the list of skilled occupations (with concomitant implications for the education sector).
- Australia ensures that data can flow freely across borders, while respecting privacy and security considerations. It is important to continue facilitating an environment

that enables digital trade, through free trade agreements, harmonisation of standards and implementation of trade facilitation measures.

- Despite efforts to improve coordination of government initiatives promoting export capability, innovation and growth, there is still some work to do to increase transparency and to improve the dialogue between the different level of government agencies and transparency. Firms find it difficult to navigate through the different programmes available to them. Also, there is a lack of co-operation between businesses and other actors, such as universities or research institutes. Hence, as recommended in the OECD *Economic Surveys: Australia 2017*, there is a need to develop a more integrated, “whole-of-government” approach to science, research and innovation and consolidate innovation support programmes. This approach could help to reduce the number of support schemes for innovative SMEs and exporters, facilitating the management and efficiency of the different schemes, allowing for more generous programmes while keeping total expenditure constant.
- A review of the R&D Tax Incentive, a program supporting business innovation, found that smaller firms face compliance costs of up to 23% of the of the program benefits. The Government continued efforts, through the recently announced reforms of the R&D TI, to improve the integrity of the program, continue assist smaller companies and refocus support for larger companies undertaking higher intensity R&D, are commendable. However, in line with other recommendations (Ferris et al., 2016), it would be desirable to improve also the administration of the R&D TI program by reducing compliance costs. This would increase companies accessibility and ensure a more inclusive participation.
- Application processes for government support schemes, such as the Export Market Development Grant (EMDG) are often time consuming and unnecessarily burdensome. Many firms turn to professional consultants for these processes. Application and reporting could be simplified so that firms could reap the full amount of the incentives available.
- The paucity of official statistical trade data, including the lack of Foreign Affiliate Trade Statistics (FATS), complicates the understanding of Australia’s strength and weaknesses in services. Improving the statistical base would allow for a more robust analysis of services trade and investment. While efforts in this direction are underway, the timely implementation of an annual survey to collect on a regular basis information on inwards, but also outwards, foreign affiliate sales and a harmonisation of the disaggregation level for the collection of trade statistics and business statistics are essential for an accurate investigation of the benefits of FTAs.

Tourism

- More coordination among the Federal Government, individual states and territories and industry associations would be desirable in creating more effective marketing strategies to better sell Australia attractiveness as a tourism destination.
- A streamlining of the visa application procedures could enhance the competitiveness of the sector. Moreover, in line with the objectives of the Tourism 2020 national strategy, there is a need for developing skilled tourism workforce and for further investment in private and public tourism-related infrastructure and facilities (particularly in regional areas), including accommodation, local attractions and transport (airports, roads, ports).

Insights into strategic sectors: The Growth Potential of the Australian Tourism Sector

Tourism is a vital part of the Australian economy. In the year to June 2017, Australia welcomed 8.5 million international visitors, up by 9% from previous year, who spent a record AUD 41 billion in the same year, 7% up from June 2016.¹ The strong growth in international tourism is moving Australia towards the lower bound of its *Tourism 2020* growth target for overnight visitor expenditure. Despite all the growth potential outlined in the national strategy for tourism, Australia still faces considerable challenges.

Promoting Australia's image overseas and marketing Australia as an international destination are critical for increasing the number of international visitors, particularly in a very competitive environment. Australia might benefit from recent geopolitical developments, including concerns around safety, increased levels of protectionism, and greater economic and political uncertainty, but cannot afford to be complacent. Much can still be done to increase the visibility of the country, secure major international events and entice international tourists to visit Australia. A coordinated response from the Commonwealth and individual states and territories, as well as from industry associations, is necessary to create interesting and effective marketing strategies to publicise Australia attractiveness as a great tourism destination.

Australia has made considerable progress in facilitating visa applications for certain nationalities, for instance implementing new and innovative tourist visa products, such as trials of lodgement in Simplified Chinese and a ten-year-validity Visitor Visa (subclass 600) for Chinese citizens to reduce red tape for frequent travellers. In addition, Australia has introduced a priority consideration service, whereby 'fast-tracked' Visitor Visa applications (including those lodged online) can be processed within 48 hours for an additional fee. Furthermore, as of July 2017, Chinese, Indian and United Arab Emirates nationals can lodge their application for the Visitor Visa online. Extending online lodgement to a wider range of nationalities is a significant enhancement in reducing part of the red tape involved in Visitor visa applications and might help to reduce processing time. Further embracing new technology and risk management settings would continue to ensure Australia maintains a sustainable growth of the tourism sector.

The national strategy *Tourism 2020* was introduced in 2011 with the objective of doubling overnight visitor expenditure by 2020. The plan identified the following key policy priorities: encourage high-quality tourism experiences, including Indigenous tourism; limit the tax, red-tape and other regulatory burdens the industry faces; undertake coordinated and

effective marketing campaigns; and work with industry to support the development of tourism infrastructure that can drive demand. Tangible targets of the national strategy include increasing accommodation by 6 000 – 20 000 new rooms by 2020, capacity increases of 40-50% in international aviation and of 23-30% in domestic aviation, and an additional 152 000 persons employed by 2020 to meet demand.

The Australian National Audit Office (ANAO) recently published a review of the *Tourism 2020* strategy to assess its implementation so far by Austrade and Tourism Australia. Monitoring and reporting of progress against the strategy targets, based on robust performance measures, concluded that there is sound evidence pointing to effective implementation. However, there is a gap in the assessment of the overall impact of the strategy in terms of net benefits to the Australian economy. Finally, the review also indicated that Australian Government funding allocated to the tourism sector is based on a transparent communication strategy, although there is still scope to improve on performance measurement at the operational level (ANAO, 2017).

The tourism industry and government have a major partnership role in promoting sustainable and more inclusive tourism growth. Achieving strong and sustained growth in international tourism depends on public confidence in Australia as a safe and secure tourism destination, and on well-managed and orderly visa programmes. The Government is embarking on a transformation of the existing visa system (Box 2.3), which will make it easier to understand and navigate, to the benefit not only international tourists but also international students and professional services providers making business visits to supply their services.

Tourists pay additional border charges, such as the Passenger Movement Charge (PMC) of AUD 60. This tax, included in the plane ticket price, is levied on all passengers departing Australia on international flights.² Australia has the third highest departure tax of all OECD members after the United Kingdom and Germany. The United Kingdom charges an Air Passenger Duty (APD) of GBP 75 (approximately AUD 127) on outbound flights in economy class, and GBP 150 (AUD 253) for all other classes. However, the APD offers lower rates of GBP 13 (AUD 22) for economy class and GBP 26 (AUD 45) for all other classes on flights of less than 2000 miles. The rate in Germany varies between EUR 7.47 (AUD 11.40) for European destinations and EUR 41.99 (AUD 64) for long-distance flights. As the PMC does not vary with distance, it is relatively more expensive than the tax levied in other countries for short-haul flights. For instance on the Trans-Tasman route, the International Air Transport Association (IATA) estimates it accounts for nearly 10% of an average return fare. The PMC was raised from AUD 55 to AUD 60 in 2016 and IATA estimated that the "reduction in aviation-related gross value-added (GVA), compared with a scenario where the passenger movement charge was abolished, could total AUD 375 million with 3800 fewer jobs supported" (IATA, 2016). The higher PMC not only affects international visitors but also Australian passengers, via higher fares, and Australian exporters by increasing transport costs and hence reducing competitiveness. Tourism and travel industry groups reacted to the 2016 increase by claiming that the tax might reduce demand from inbound passengers.

Industry associations are also calling for an expansion of air routes and agreements and the removal of aviation capacity restrictions. Aviation capacity is typically regulated by bilateral Air Service Agreements (ASAs), which set out the operation of scheduled international air services between two countries. Capacity, or access, entitlements, include the number of seats or flights that can be operated on established routes between the ASA partners. To date, the capacity of international airlines is restricted in Australian major

gateway airports like Brisbane, Melbourne, Perth and Sydney, and secondary airports in Melbourne and Sydney, but is unrestricted for other regional Australian airports. Industry associations and major airports claim that the lack of capacity within certain ASAs effectively restricts access to the Australian market for some international airlines, limiting competition between foreign and domestic airlines on a number of routes, involving for instance main Australian gateway airports and Hong Kong, China or Malaysia. Lack of competition drives up airfares, dampening demand for tourism, travel, and trade in general.³ Costs are affected by exchange rate fluctuations as well, which might contribute to influence the motivation to travel.

There is also an infrastructure shortfall. Private and public investment is needed to improve the breadth and quality of offering, for projects like new airports and road links. In 2016–17, aviation infrastructure projects were worth over AUD 10 billion. More than half the pipeline investment in aviation was accounted for by the Western Sydney Airport at Badgery's Creek, with the rest spread across other major aviation infrastructure projects including upgrading and expanding of existing airports.⁴ Increasing port capacity to accommodate more ships could also work to increase tourist demand. The estimated total output of the cruise industry in 2015-16 was AUD 2.9 billion, 10% up from the previous period.⁵ In just over twelve years, the number of cruises has doubled, as has the passenger capacity of visiting ships (ACA, 2016). Industry associations suggested that infrastructure investment, including accommodation, attractions and telecommunications, could create a more diversified and widespread offer, reaching beyond the most visited cities, so as to ensure a more equitable and sustainable future growth of the sector.

There have already been various policy responses under the *Tourism 2020* plan, including the establishment of a network of investment specialists around the world to assist prospective foreign investors. These specialists should help identify high-potential projects, connect international investors with Australian counterparts, and assist them through the investment approval process.⁶ Increasing investment in transport infrastructure like airports, roads, trains and cruise ship terminals, would address current growth constraints in the sector.

Availability of an adequately skilled workforce is another challenge to the growth potential of the tourism sector. A recent report suggests that skilled labour supply in the sector falls short by 38 000 positions based on 2014 ABS data, with rising vacancy rates (Deloitte, 2015b).⁷ It also indicates that there has been a large increase in the number of businesses signalling skills deficiencies. In addition, productivity growth in the tourism sector is at below average to average relative to that of other industries, according to a recent report by the Committee for Economic Development of Australia (CEDA, 2017). Over the last fifteen years, labour productivity (output per hour worked) has increased in the retail trade, accommodation and food and transport sector, but has lagged behind elsewhere in the tourism sector. The sector's slow productivity growth could be explained by rapid wage growth, but also by the changing composition of tourism workforce. Jobs in the sector have become more seasonal, with increasing staff turnover rates, and higher shares of part-time workers, which are less likely to be involved in skills training programs. The report suggests that the Government could assist by improving the quality of training opportunities and the management of temporary workers. The provision of training would ensure a future supply of skilled workers to undertake tourism jobs that respond to the effects of digital disruption. A simplification of the visa arrangements around foreign skilled workers would also boost efforts addressing the skills shortage in the tourism sector. It would also be important to build the right management skills among tourism operators

so they can tailor their services better to the rising demands of visitors from key tourism markets.

In summary, there is strong potential for increasing Australia's tourism market share, although some challenges still need to be addressed. From the perspective of a potential international tourist, the country's appeal could be enhanced with more effective tourist campaigns overseas, easier entry and more competitive air services competition. A more diversified intake of international visitors would reduce the dependence of Australian tourism on certain countries. There is also a need to better understand the commonalities and market synergies between tourism and international education.

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1. For more details, see the Tourism Australia, International Visitor Survey, available at: <http://www.tourism.australia.com/en>. According to the ABS Tourism Satellite Account statistics (cat. no. 5249.0), total consumption by non-residents on inbound trips amounted to nearly AUD 45 billion in 2016-17.
 2. According to IATA, the PMC is considered more of a departure tax than an airport charge, as its revenue is collected by the DIBP and does not directly contribute to passenger processing at airports.
 3. The Productivity Commission suggested tackling this lack of competition by providing unrestricted access to foreign airlines operating air transport services to and from Australian's major gateway airports through open sky or open capacity agreements (PC 2015c).
 4. More details can be found in the Tourism Investment Monitor 2017, from Tourism Research Australia, made available at <https://www.tra.gov.au/>.
 5. While this figure refers to all passengers, including domestic ones, expenditures by international passengers contributed to more than half.
 6. For additional information on current investment promotion initiatives in the tourism sector see: <http://www.tourisminvestment.com.au/en>.
 7. However, that the term "skilled" used by Deloitte (2015b) does not align to the definition of skilled for migration (visa) purposes, which is referenced to Skill Level 1 to 3 occupations in the Australian and New Zealand Standard Classification of Occupations (ANZSCO).