

**ASX**

AUSTRALIAN STOCK EXCHANGE

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**Australia-China States Free Trade Agreement Scoping Study**

Thank you for the opportunity to make a submission as part of the scoping study examining a possible free trade agreement between Australia and China.

The Australian Stock Exchange (ASX) believes that improving Australia's trade and investment relationship with China offers significant potential economic benefits. It is clear that China will play an increasing role in the Asia-Pacific's economic landscape given its size, rapid growth and the economic changes flowing from its accession to the World Trade Organisation.

We would support pursuing the negotiation of a comprehensive agreement with China if it is in Australia's national interest. Such an agreement would complement free trade agreements Australia has already negotiated with New Zealand, Singapore, Thailand and the United States and will also supplement multilateral trade negotiations that Australia is party to.

The two-way trade relationship between China and Australia is already healthy. Reducing any barriers restraining Australian companies' exports to and investment in China should further enhance their ability to grow and provide shareholders with higher returns.

To date, the two-way flow of investment between the two countries has been more limited, although we would expect this aspect of the relationship to grow over time. The lack of convertibility of the Chinese Renminbi and exchange controls in place restrict investment flows at the moment. There are also restrictions on purchases by foreigners of shares in listed Chinese companies.

China has embarked on a program designed to improve the soundness of their financial institutions and the overall fundamentals of their financial system. While this process will take time to raise supervisory standards and investor protections to levels applying in more developed capital markets the Chinese authorities have shown a commitment to meeting these challenges.

China has adopted a policy of gradual financial market liberalisation to manage their transition from a more centrally managed capital market. Once the foundations of a robust financial system are in place, capital account liberalisation and opening up of financial markets to global financial institutions and capital would help Chinese markets grow and underpin future economic growth.

While much attention is given to the banking sector in China, as important over the longer term will be the growth of securities markets. A healthy and liquid securities market enables the efficient allocation of resources to productive uses and lowers the overall cost of capital for the private sector.

China has two major mainland securities exchanges but they remain relatively underdeveloped given the size of the Chinese economy. The Shanghai Stock Exchange and Shenzhen Stock Exchange both commenced operation in late 1990. By the end of 2003 their combined market capitalisation was around \$US513 billion, somewhat below that of total Australian market capitalisation of around \$US585 billion. When measured relative to GDP the relative size differential is pronounced, with Chinese market capitalisation being around 35 per cent of GDP while in Australia the figure is around 100 per cent.

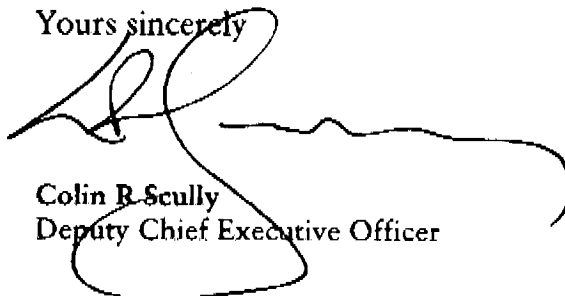
ASX has good relations with the Shanghai and Shenzhen exchanges, having been one of the first exchanges to sign Memoranda of Understanding (MOU) with them. These MOUs provide for general cooperation across a range of activities particularly in the area of staff secondments. To date these secondments have focussed on areas of listings, trading and market surveillance. ASX has also developed good working relations with the China Securities Regulatory Commission (CSRC), the principal regulatory body in China.

Through these relationships we hope to provide some assistance to the Chinese in their capacity building and establishment of markets of integrity.

As China reforms its domestic financial system and puts in place appropriate regulatory standards there may be scope for more closely linking our two capital markets. The ultimate objective would be to develop arrangements that would allow Chinese investors to invest in Australian listed companies and vice versa in a simple and cost-effective manner.

It is perhaps a little premature to try and identify potential barriers and possible solutions to greater access in the securities industry until China's domestic reforms are completed. However, any free trade agreement may be able to establish a framework for these issues to be addressed in the future.

Yours sincerely



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