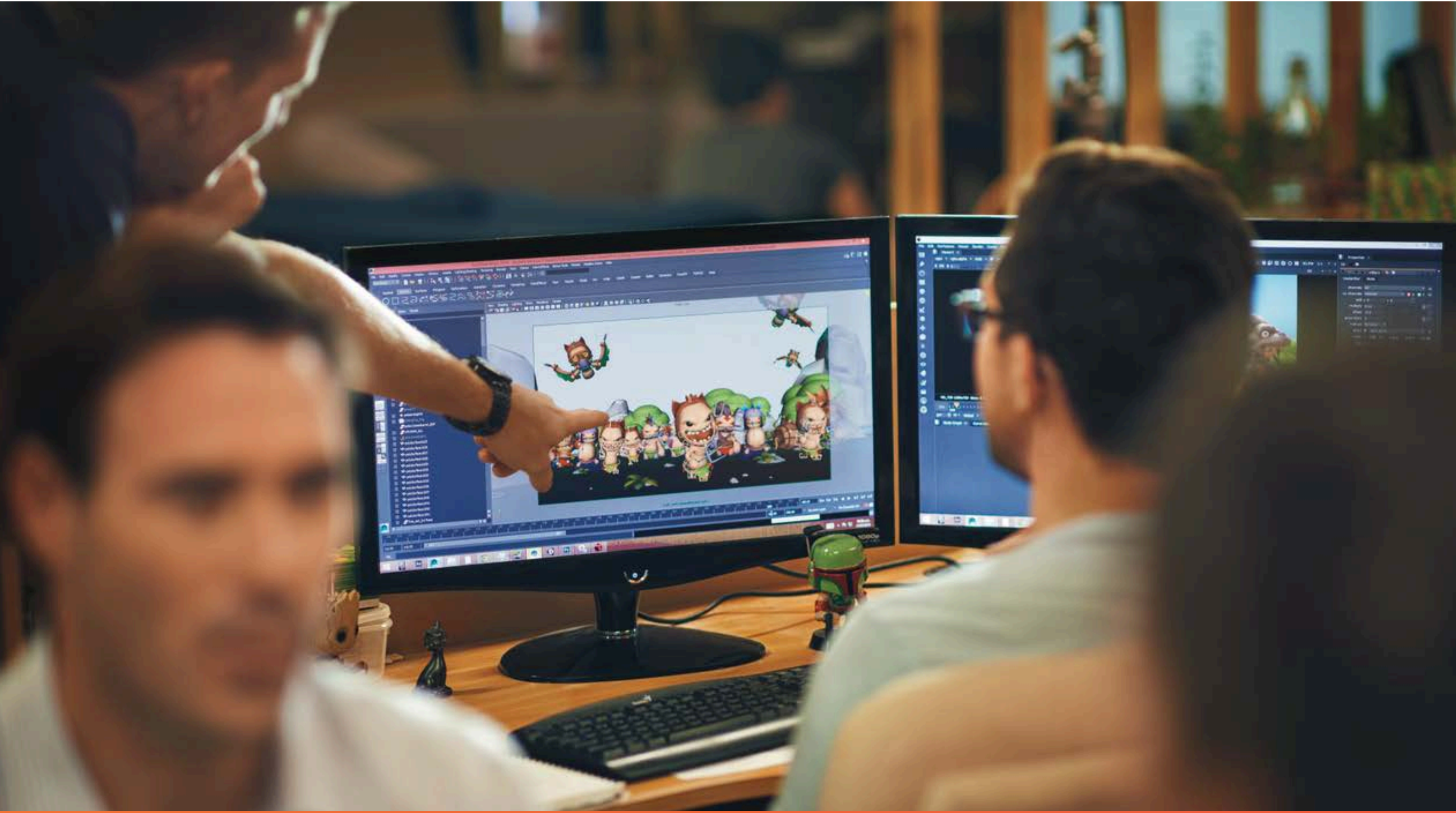

RESUMING NORMAL SERVICE?

Assessing future prospects for New Zealand-China services trade

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Commissioned by:

NEW ZEALAND

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New Zealand China Council
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FOREWORD

The rapid expansion of bilateral trade between New Zealand and China will be well known to readers of this report. But even at its height in 2016-19, trade in services tended to be overshadowed by New Zealand's export of primary products to China and import of manufactured goods. This despite the fact that at one point services accounted for 25 per cent of our exports to China by value.

The huge disruption to services exports and imports caused by COVID as travellers were blocked from travelling between New Zealand China to deliver and consume established services such as tourism and education, let alone emerging sectors requiring careful nurturing and development, has tilted our trade profile even more in favour of goods for the time being.

The ramifications of this disruption are serious. Apart from billions of dollars of lost export revenue and consequent economic hardship for many New Zealand businesses, trade in services often delivers a wide range of indirect economic and non-economic benefits as well. In the case of tourism and education, visits by family and friends, decisions about future investment, migration, research and business links, can all flow from the personal contact that comes with services consumption and delivery.

As the relationship between New Zealand and China continues to evolve in response to changing bilateral and regional circumstances, the more direct personal contact we can achieve in both directions the better.

I am confident that the situation will improve from its 2021-22 low point, as the world continues to emerge from the global pandemic. But quite when and how this will occur is less clear.

What is evident is that the resumption of services trade will require concerted efforts by our two governments, and by our service sectors themselves.

First and foremost it will require travel between New Zealand and China to become more free-flowing again, which will only be possible if travellers can cross borders conveniently and with prompt access to the right visas.

Regulation of services delivery must also be as liberalised and facilitative as possible. The 2022 upgrade to the New Zealand-China free trade agreement made some welcome progress in this area and I hope new opportunities will be fully explored by business. But as pointed out in this report, more will be needed if our service sectors are to navigate an increasingly complex digital environment: fewer rather than more restrictions are required.

New Zealand's established and emerging service exporters will also have to adapt to a new environment and changing consumer preferences and trends. The report suggests that we will see less Chinese tour groups and more independent travellers and family visits looking for different experiences, for example; and that Chinese students may be more inclined than previously o study partly or fully in China, online or in offshore New Zealand study centres.

Despite all the unknowns, the wide range of case studies in our report illustrates the importance of resuscitating this crucial part of our trade relationship.

I would like to thank Stephanie Honey for her thorough and informed research to produce this report, and our sponsors Ngāi Tahu Holdings, ANZ Bank, Christchurch International Airport and the North Asia Centre for Asia-Pacific Excellence for their support. I trust you will find "Resuming Normal Service?" a useful and interesting read.

John McKinnon
Chair, New Zealand China Council

EXECUTIVE SUMMARY

2022 marks fifty years of diplomatic relations between New Zealand and China. Trade and economic links are key pillars of this important and complex relationship, and those connections have grown significantly in the decade and half since the bilateral Free Trade Agreement (FTA) was signed. In fact, merchandise trade with China played a significant role in helping to pull the New Zealand economy through the turmoil of the first years of the COVID-19 pandemic.[1]

While soaring goods exports to China have created headlines, services trade has also grown steadily – at least, pre-pandemic. The lion's share of exports has come from two sectors, tourism and education, but transport has been a steady performer and there are niche exports in other sectors. The pandemic has had a severe impact, however. While China remains New Zealand's third-largest services export destination, disruption to the trading environment looks likely to continue at least in the short to medium term.

A key question now is whether the period ahead will bring a return to the earlier trend, or a reorientation towards new modes of delivery and potentially even new services. It is timely to reflect on how New Zealand might navigate these new opportunities and challenges. The New Zealand China Council (NZCC) has accordingly commissioned this report in order to:

- Examine New Zealand-China services trade;
- Investigate how this trade have been affected by the pandemic; and
- Explore the prospects for 'resuming normal service' in the period ahead.

Key Findings

Services deliver many benefits, not just export returns

- Services trade matters. The potential benefits go well beyond export returns (although these can be significant): services trade overcomes the 'tyranny of distance', offers the promise of greater inclusion and sustainability, plays a critical enabling role for goods trade, and supports productivity, innovation and economic growth overall.
- Some services sectors, notably tourism and education, also offer important intangible benefits such as greater cross-cultural awareness and diversity, and lasting personal connections between the two countries.

New Zealand exports a range of services to China, but tourism and education dominate

- In 2019, New Zealand exported NZD$3.4 billion of services to China (around 17 percent of exports), of which nearly 90 percent comprised tourism and education.[2] Other services exports that year included transport for passengers and freight, distribution and other trade-related services; financial services; government services and insurance, along with niche exports in personal, recreational and cultural services.
- The pandemic has had a major impact. Services exports slumped from $3.4 billion in Year Ending (YE) June 2019 to $1.1 billion in YE June 2022 – a contraction of 68 percent.[3]

[1] Sense Partners (2022), '*In Perspective: The New Zealand-China Trade and Business Relationship, 2022 Update'*, Report for New Zealand China Council

[2] All figures used in this paper are from Statistics New Zealand (including its New Zealand Trade Dashboard), unless otherwise specified. Depending on the specific example, figures are Year Ending (YE) June, or calendar year/YE December, as indicated. Figures throughout the paper are in New Zealand dollars unless otherwise specified.

[3] StatsNZ: Total services exports, December Years: 2019 $3.37b, 2021 $1.17b; June Years: 2019 $3.35b, 2022 $1.06b

Tourism and education have faced severe challenges through the pandemic...

- The pandemic caused a steep fall in both Chinese travellers and students, and consequently on the "travel services" category (primarily tourism and education).[4]
- Tourism has contracted by over $1.5 billion, and continues to struggle, falling 92 percent from $1.6 billion in 2019 to $119 million in YE June 2022.[5]
- The education sector has been somewhat less hard-hit, thanks to the continued presence of Chinese students in New Zealand and the ability of providers to pivot to online delivery. Exports fell 44 percent from $1.3 billion in 2019 to $720 million in YE June 2022.[6]

…and prospects are uncertain, with the rebound likely to be uneven

- The two sectors face different trajectories. Tourism may not recover significantly before 2024, and will likely involve reshaping to higher-value, more sustainable models.
- While the fall in education was less steep, the recovery may lag. Factors include the lingering effect of New Zealand's closed border on the 'pipeline' of students, perceptions around value-for-money, and difficulty for students in accessing visas and post-study work rights.
- "Blended" education models involving online delivery may be a promising future focus for the sector – but for this, much depends on China's evolving attitude to digital delivery.
- Also promising is expanded in-market provision, leveraging shifting attitudes in China towards "international education at home"; but this will continue to be subject to the regulatory complexities of operating in the Chinese market.

Other sectors have fared better – and worse

- Exports in other sectors are more modest, and have performed highly variably. Some exports have expanded through the pandemic (insurance and some business services), while others have fallen steeply, including financial and computer services, although this may be related as much to the regulatory environment as to the pandemic.
- Non-travel services exports are dominated by transport services. The pandemic has seen a significant decrease in New Zealand exports from this sector, and a significant increase in Chinese imports. New Zealand Government support for supply chain resilience has been critical through this period, not only to the sector itself but also to support goods exports.
- In other sectors, a range of impressive niche exporters have been able to innovate for greater resilience during the pandemic, but the operating environment remains highly challenging.
- Digital services (such as videogaming) and digitally-delivered services (including from more 'traditional' sectors) have significant promise, including to tap into China's large and vibrant consumer digital economy. However, there are considerable regulatory impediments and restrictions relating to data handling, personal information protection and digital content, not only for tech exporters but in fact for any New Zealand business operating online.

Services offer potential for greater inclusion for Māori businesses and women entrepreneurs

- The trade policy literature identifies the services sector as an important way for under-represented groups, including women entrepreneurs and Māori-led businesses, to circumvent structural impediments in trade.
- While the participation of such businesses in services exporting to China is difficult to measure, there are prominent niche examples in tourism and in creative sectors such as information, communications and technology services (ICT), digital trade and design, among others.

[4] StatsNZ: Travel services exports, Dec Years: 2019 $3.04b; 2021 $0.96; June Years: 2019 $2.99b; 2022 $0.85b
[5] StatsNZ: 'Other personal travel', Dec Years: 2019 $1.62b, 2021 $0.11b; June Years: $1.58b; 2022 $0.12b
[6] StatsNZ: 'Education-related travel', Dec Years: 2019 $1.29b, 2021 $0.84b; June Years: 2019 $1.28b, 2022 $0.72b

Imports are small, but steady

- Imports of services from China – including transport and travel, business services, ICT and others – have experienced slow but steady growth, although at a significantly lower level than New Zealand exports. By YE June 2022, imports had risen to an historic peak of $832 million, but this figure does not fully reflect the strength of China as a global services exporter.
- There is clearly room for expansion in Chinese services imports into New Zealand. Those imports can help to deliver some of the broader economic benefits described above, and also facilitate other kinds of trade, including tourism and goods trade.

The period ahead will be challenging…

- The period ahead is likely to continue to be challenging, with many downside risks.
- Most prominent among these risks are continuing COVID-related disruptions, impacting both travel (and hence tourism and education, as well as the people-to-people connectivity that supports other business sectors) and the delivery in-market of services involving personal proximity, such as recreational services.
- The Chinese economy is also forecast to slow significantly in the period ahead.[7] This may reduce demand for services that support business and investment activity, such as legal and financial services, as well as for consumer services in-market.

…but there are also likely to be opportunities

- Niche exporters are likely to continue to be able to find opportunities across a range of sectors, including those where the Upgraded FTA includes new commitments – although the prospects will be improved once travel, and deeper people-to-people connections, resume.
- The FTA has also opened up new opportunities for in-market delivery in some sectors, although this remains challenging for many businesses, requiring a significant investment of time and energy alongside the regulatory compliance it entails.
- The pandemic has seen a rise in digitally-delivered services to China, including online delivery of education, as well as digitally-delivered services in other sectors, such as business, personal and recreational services. At the same time, China's digital economy remains highly regulated and complex, particularly in relation to the handling of 'sensitive' data, in accessing some platforms, and in relation to digital content, entailing high compliance costs for business.
- Feedback from exporters has underscored that building formal and informal relationships, including through regular visits and broad and deep connections, are all critical. People-to-people contacts remain a key enabler of services trade: with China, relationships come first, business second.

Sustained efforts are needed to simplify the regulatory environment and deepen connections

- Services trade is notable for the range, complexity and obscurity of the regulatory barriers it involves, including with China. Regulations can limit whether and how exporters are able to enter and operate in the Chinese market, including relative to competitors.
- The New Zealand-China FTA, signed in 2008 and upgraded in 2022, is important not only for opening up market access opportunities and levelling the playing field for exporters, but also by enabling greater transparency and predictability in the regulatory environment that they face and in smoothing other kinds of barriers, for example around the recognition of professional qualifications or quality assurance for distance education.
- Continued engagement from the New Zealand Government can help to support greater regulatory coherence and confidence for exporters in the longer term.

[7] World Bank (2022), 'Reforms for Recovery: East Asia and Pacific Economic Update, October 2022

A quick note on services trade statistics

It is challenging to measure services trade accurately. The statistics used in this report are drawn primarily from Statistics New Zealand (StatsNZ), which uses the 'Balance of Payments' methodology, accounting for direct exports (via "Modes" 1, 2 and 4 – explained further in Section One of this report), but not including services that are delivered through a foreign affiliate such as a subsidiary or branch in China ("Mode 3").[8] *The latter may mean that the full value of New Zealand exports via wholly foreign-owned entities in China is not reflected in the trade statistics.*

It is also particularly difficult to measure the value of "digital trade"; current international methodologies are only able to measure a component of this, primarily via computer services and software exports, as well as the aggregated category of 'charges for the use of intellectual property', which also includes software licensing. Annex I gives a fuller discussion. Nevertheless, the statistics used in this report give a sense of the general trends, even if in some cases they may undervalue the trade.

Note also that two main data sets have been used: a StatsNZ discontinued data set which covers 2007 to 2020, and a more updated set covering 2015 to 2022. These two datasets do not always match exactly, but show the general trends over the period.

[8] The WTO has established an experimental database which includes Mode 3, the Trade in Services by Mode of Supply (TiSMoS). However, many TiSMoS Mode 3 figures are estimates and are not broken down by market. The database also only covers the period 2011 to 2017. The TiSMoS data for New Zealand shows that roughly half (54%) of New Zealand services exports over that period were via Mode 3, mainly in insurance and financial services; telecommunications, information and computer services; and trade-related services, especially distribution.

REPORT

Section One: The 'why' and 'what' of services trade

Hearing the phrase "trade with China" likely evokes an image of ships carrying containers of milk powder or beef, rather than Chinese students or tourists coming to New Zealand to study or enjoy the sights. Similarly, streaming a New Zealand videogame on a Chinese platform, or serving as an engineering consultant on a Chinese project, may not be immediately recognisable as "exporting" – but these are examples of services trade in action. Services trade delivers many tangible and intangible benefits, as the box below explains.

Services trade matters

Trade in services is less familiar to many people than goods trade: it may not look much like "trade", and can involve complex and opaque regulatory requirements which do not closely resemble traditional tariff barriers. This 'image problem' can mean that services trade gets less attention than it deserves – but in fact services not only contribute to export returns – at their high point, accounting for one-third of New Zealand's total exports – but also play a critical enabling role in goods trade, and support productivity, innovation and economic growth:

- Services exporters can more easily have global reach and scale than goods exporters – helping to overcome the 'tyranny of distance' that has shaped much of New Zealand's trade history. Services exporting offers a more accessible way for small firms, women and Indigenous businesses to enter global markets.
- Services exports mostly have a much lower environmental footprint than goods trade (although less so for exports of tourism and in-person education).
- In addition to being exported directly, services can be "embedded" (that is, bundled with goods, such as after-sales service with an electrical appliance), or "embodied" in goods (as inputs such as R&D, design, software, finance or logistics). Embodied services have been estimated to make up 57 percent of the value of New Zealand goods exports; for food and beverage and wood products (major New Zealand exports to China), services inputs are estimated at nearly one-third of export value.[9]
- Services trade can generate a range of broader economic and intangible benefits. As Section Four shows, services exports such as tourism and education can deepen cross-cultural awareness as well as generating jobs, including in regional New Zealand, greater productivity and lifelong personal connections.
- For *all* New Zealand businesses, access to competitive local and imported services enable them to use tools such as cloud computing and professional services for greater efficiency, integrity and value-adding.
- The "tradable sector", which includes services such as wholesale trade, professional and technical services, information, computer and technology (ICT) and financial services, is more productive and employs more people than the non-tradable sector, thereby boosting New Zealand's economic performance overall.[10]

In short – services trade matters!

Trade rules for services

Services trade takes place when a supplier in one country sells a service to a buyer in another. This is sometimes called "weightless trade": as the saying goes, a service is something you can buy and sell, but cannot drop on your foot – like education, a videogame or engineering advice. The way that the service gets to the customer, called the "mode", forms the basis for the rules:

- In Mode 1 ("cross-border trade"), the *service* moves; this captures any service that is delivered digitally, and also includes transport. For example, a New Zealand architect emails building designs to a client in China, or a product is transported by air or sea to China.

[9] Rajanayagam, S. (2016), '*The "servicification" of trade*', New Zealand Productivity Commission Research Note 2016/4

[10] "Tradable sector" services can be exported directly, contribute to goods exports or are exposed to international competition. From Bailey, P. and Ford, D. (2018), '*MFAT Working Paper: Estimates of New Zealand's tradable and non-tradable sectors using Input-Output tables*'. For the contribution of imported services to services-sector productivity, see New Zealand Productivity Commission (2014), *Boosting Productivity in the Services Sector*, May 2014.

- In Mode 2 ("consumption abroad"), the *consumer* moves. For example, Chinese students or tourists come to New Zealand to study or visit.
- In Mode 3 ("commercial presence"), the *services supplier* moves, by setting up a foreign affiliate. For example, a New Zealand tech company sets up a branch or subsidiary in China.
- In Mode 4 ("presence of natural persons"), a *representative of the services supplier* moves. For example, a New Zealand engineer goes to China to advise on a project, then returns.

In trade agreements such as the New Zealand-China FTA, trading partners make detailed market access commitments by mode, and across selected services sectors or sub-sectors. Unlike goods trade, services trade does not involve tariffs. Instead, governments use regulations and administrative measures to control whether services suppliers are able to operate; what they are able to sell; how they are treated; and other conditions such as whether professional qualifications are recognised. These barriers can be hard for exporters to identify, and can make it challenging to know exactly which rules may apply. Often, local legal or other professional advice is required.

The digital transformation of services trade: The rise of Mode 1

Even before the COVID-19 pandemic, rapid digitalisation had transformed services trade. New services, products, data-driven solutions and services 'global value chains' have emerged.[11] Services which once could only be delivered in-person can increasingly be supplied remotely, at scale and with greater value-adding, through the internet – the case study on Magic Memories is an example of this.

The share of "digitally-deliverable" services, including from more traditional sectors such as financial services, research and development, professional services and even recreational services, is expanding rapidly.[12] This shift may have helped to mitigate the impacts of the pandemic as exporters have been able to pivot from in-person delivery (for example, onsite education in New Zealand via Mode 2) to 'remote' or distant forms (delivery of the same content online – Mode 1 – or through a joint institution in-market, Mode 3). Looking at the statistics, education has contracted less than expected, and digitally-deliverable services such as insurance and business services have increased.

In other cases, although businesses may have been able to shift to Mode 1, continuing travel restrictions have constrained the important contribution of person-to-person contacts in building foundational trade relationships. The case study on Wētā Workshop illustrates this challenge. Notwithstanding the importance of digital connectivity, the extent to which new business relationships and opportunities can be fostered in future will continue to depend on the ability to move between the two markets.

Section Two: The New Zealand-China FTA

The rules for New Zealand-China services trade are set out in the New Zealand China Free Trade Agreement (FTA), which was signed in 2008 and upgraded in 2022. The FTA has opened up market opportunities in a range of sectors (albeit somewhat modestly in many cases), and helped to streamline the requirements that New Zealand exporters need to meet in the market, as well as creating a more level playing field for exporters relative to both Chinese and other foreign competitors. Overall, however, one of the FTA's most important benefits is to provide exporters with

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[11] WTO (2019), *World Trade Report 2019*, pages 14-15

[12] OECD, WTO and IMF (2020), *Handbook on Measuring Digital Trade*, pages 13-14. The services that can be digitally delivered or "ICT-enabled" include insurance and pension services, financial services, charges for the use of intellectual property, research and development, professional and management consulting services, architecture, engineering, scientific and other technical services, 'other business services', audio-visual and related services, health services, education services and heritage and recreation services.

greater transparency and predictability about the regulatory environment in which they will be operating. Annex II has more detail.

For the two biggest sectors – education and tourism – the 2008 FTA came at a time when exports were already performing well: at that time, China was New Zealand's fifth-largest source of tourists and single largest education market.[13] It was anticipated that the FTA would help to grow those sectors thanks to the new market access commitments, the development of direct air links and the introduction of a Working Holiday Scheme. Indeed, as the next section illustrates, these sectors have been a notable success story, at least pre-pandemic.

Of note, on education, the FTA included an undertaking by China to keep the names of key New Zealand education institutions on the Chinese Ministry of Education 'Study Abroad' website, thereby boosting the confidence of Chinese students in choosing a New Zealand provider. The FTA also included a commitment from both sides to initiate joint work on quality assurance criteria for qualifications which included a distance delivery component.

The 2022 Upgrade builds on the original 2008 commitments, and helps to bring the opportunities for New Zealand exporters onto par with the more recent commitments that China has made to other trading partners in their respective FTAs. The Upgrade includes:

- New market access commitments in 22 sectors, including environmental services, a range of services relating to airport operations and air services and sound recording distribution;
- Improvements in existing commitments in 17 sectors, including real estate services, translation and interpretation services, non-academic training in English language, cooking and handicrafts, and a handful of others.

These new commitments are by and large incremental. In many cases, for example, they provide for New Zealand exporters to establish wholly foreign-owned entities in the market rather than being obliged to participate in a joint venture. This may be a promising model for New Zealand exporters in future, although it may still continue to involve considerable compliance costs in the Chinese market.

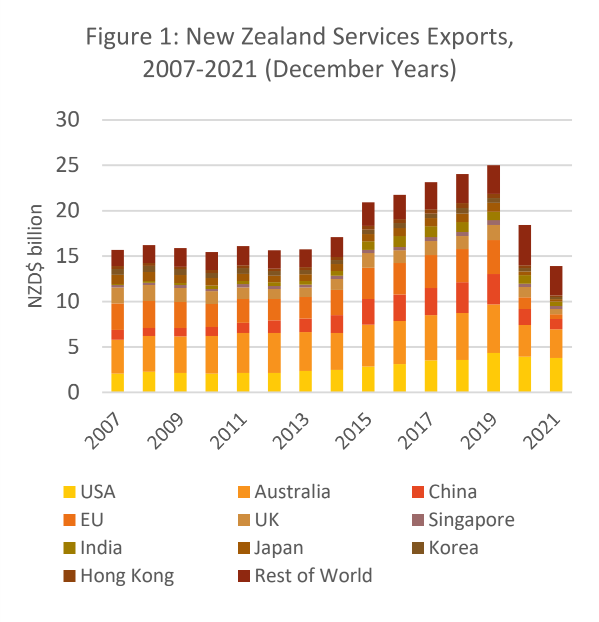
The Upgrade also updates the New Zealand visa allocation for Chinese providers of "iconic Chinese occupations" to deliver services in New Zealand, including Chinese tour guides and tourism specialists, Mandarin teaching aides and others. While beneficial for Chinese exporters, these commitments will also help New Zealand businesses to employ qualified staff to support the revitalisation of Mode 2 services exports in the education and tourism sectors.

Section Three: New Zealand services trade

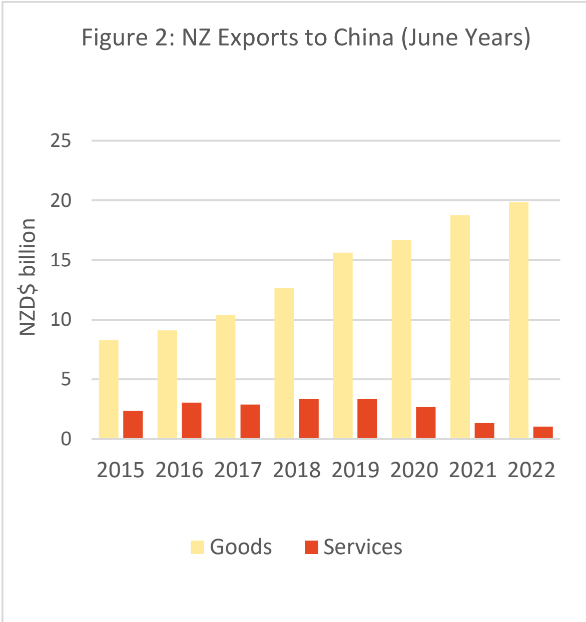
China has been among the top five New Zealand services markets since the FTA was signed, and the third-largest export market since 2018, as Figure 1 shows. Services exports were worth $3.4 billion pre-pandemic, and accounted for over one-quarter of all New Zealand exports to China at one stage (in 2016).[14]

[13] New Zealand-China FTA National Interest Analysis, page 10

[14] StatsNZ figures: June Years: 2016, 25.1% of exports to China ($3.05 billion); 2022, $3.35 billion (5% of exports). Growth in NZ services exports to the world averaged 4.3% per annum between 2008 and 2018, higher than world growth (4.1%) and NZ goods export growth (2.7%). Ministry of Business, Innovation & Employment (2022), '*New Zealand's Export Advantage: Composition and Performance of New Zealand's comparative advantages from 1995-2018*', RSBED Insights Paper 22/01.



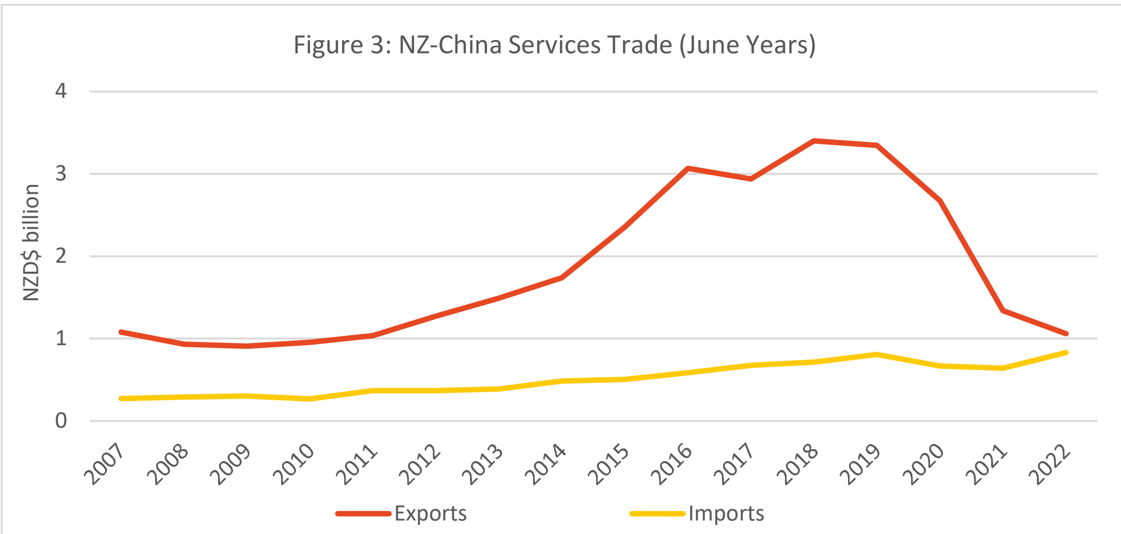
Source: StatsNZ data, December Years



Source: StatsNZ data, June Years

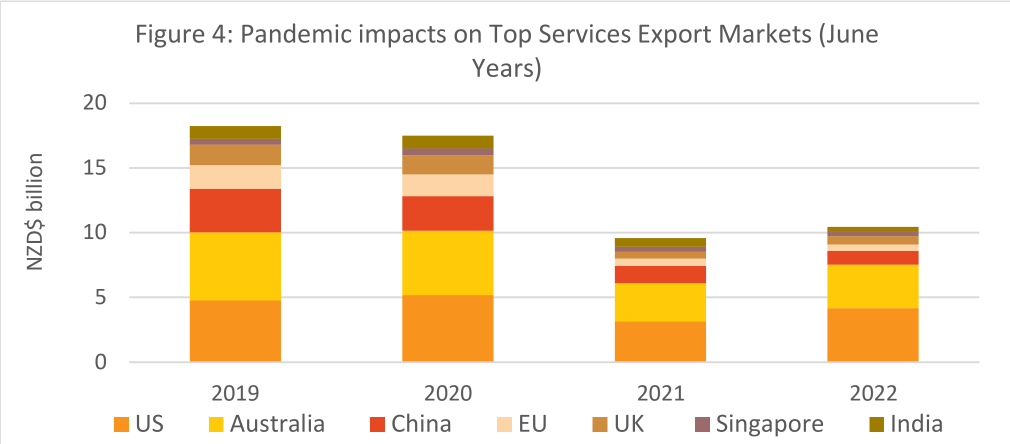
Exports to China were part of a strong performance overall from the New Zealand services sector in the decade leading up to the pandemic. However, even at their peak, the share of services exports to China was worth somewhat less than the share of services exports in total exports to the world (around 25 percent, compared to 31 percent), and by 2019 this figure had dropped to only 17 percent of exports. This declining export share is largely due to even more significant relative increases in the value of New Zealand goods exports to China over the period, as Figure 2 illustrates.

Figure 3 shows the growth of services exports and imports since the FTA was signed. For exports, after an initially slow start, there was strong growth from 2011, largely driven by tourism, peaking in 2018 at just over $3.4 billion. The pandemic led to a sharp contraction in exports: between YE June 2019 and YE June 2022, services exports fell by 68 percent to $1.1 billion, a mere 5 percent of New Zealand's $21 billion in exports that year.



Source: StatsNZ data, June Years

This steep decline likely reflects the dominance of Mode 2 services in China trade, and the impacts of COVID-19 on person-to-person delivery. By contrast, New Zealand services exports to world markets declined by only 48 percent, from $27 billion to $14 billion between 2019 and 2022. As Figure 4 shows, the services export recovery has been somewhat stronger in, the United States and Australia, likely reflecting the lower share of Mode 2 exports to those markets.

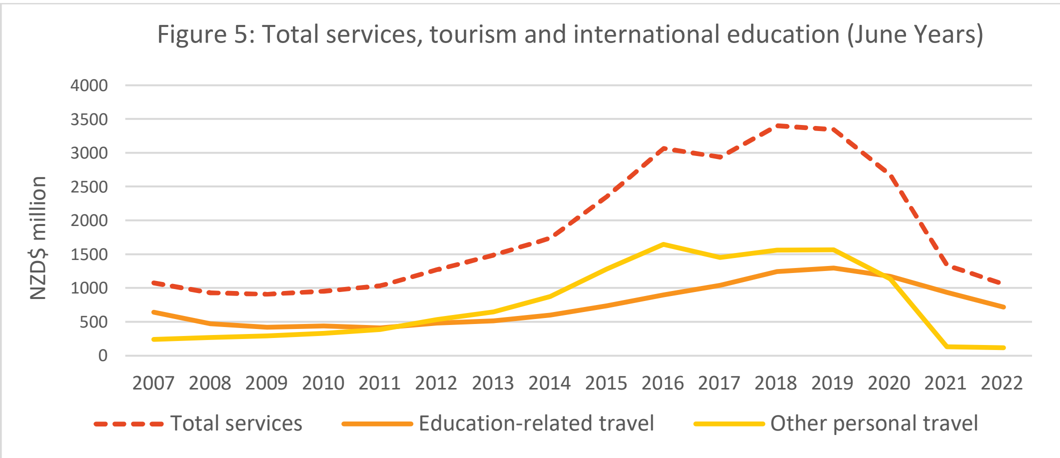


Source: StatsNZ data, June Years

On the import side, there was slow but steady growth pre-pandemic, although at a much lower level than exports: pre-pandemic, imports peaked at $804 million in 2019. Although there was a slight dip in imports in 2020 and 2021, they have subsequently risen to $832 million in YE June 2022 – coming close to balance with New Zealand services exports at $1.1 billion in that same period.

Section Four: "Travel services": International Education and Tourism

"Travel services" ranked as the fourth single largest pre-pandemic export category for New Zealand to China in 2019, behind dairy, meat and wood and accounted for 90 percent of all services exports. Travel services are primarily tourism ("other personal travel" in the trade statistics jargon) and international education ("education-related travel"), along with business and other types of travel. Growth in this sector averaged around 5 percent per annum in the decade from 2008 to 2018.[15]



Source: StatsNZ data

[15] Not surprisingly, travel services has been assessed as the sector of New Zealand's strongest revealed comparative advantage in services, with few other services sectors coming close Ministry of Business, Innovation & Employment (2022), '*New Zealand's Export Advantage: Composition and Performance of New Zealand's comparative advantages from 1995-2018*', RSBED Insights Paper 22/01.

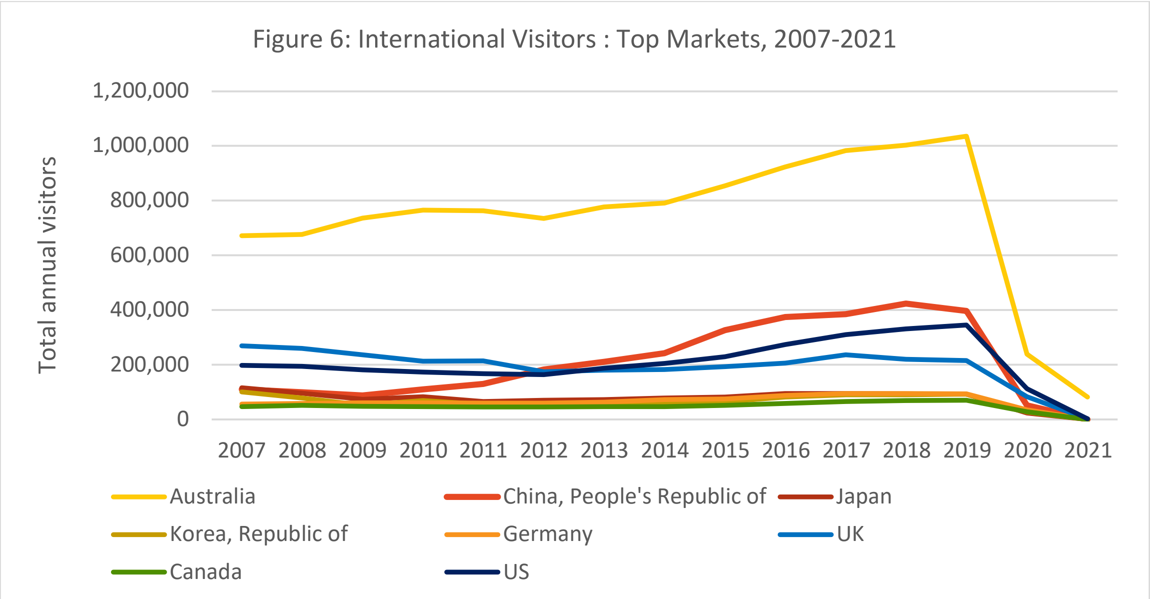
These sectors typically involve close person-to-person contact; unsurprisingly, COVID outbreaks and pandemic-generated border closures, quarantine and other disruptions caused a steep fall in Chinese visitors, students and business travellers to New Zealand. This had a severe impact on trade in this sector and as a consequence, on services exports overall to China, as Figure 5 shows.

Tourism

Tourism has been one of the most notable success stories of all New Zealand services exports to China. Exports grew rapidly from around 2011 to reach $1.6 billion in YE December 2019, making China New Zealand's second largest international visitor market that year, with 407,000 Chinese visitors – see Figure 6. Chinese tourists were also among the most valuable visitors in terms of spend (an average of over $4,600 per person) and duration (with one-third of visitors staying between eight and 14 days – note that the "holiday market" normally entails a shorter length of stay, while visits from friends and family tend to be longer).[16]

The sector's contribution to New Zealand goes beyond simply export dollars, however. Tourism has had a significant positive impact on regional economies, including through creating employment and boosting productivity and value-adding in industries supporting the core tourism sector, such as food and beverage, retail, arts and recreation, education services and others. Visitor spend also helps to fund 'social amenity', such as restaurants, recreational activities, events and road and air connectivity, in local communities. One report estimates that, where the core tourism output in 2018 was $12.3 billion, there was a $39.3 billion "Visitor Economy", comprised of supporting industry output at $19.4 billion, GST at $3.7 billion and $4 billion of imports sold directly to visitors.[17]

Beyond this, of course, tourism also helps to deepen mutual cultural understanding and foster people-to-people connections.



Source: StatsNZ data

16 Tourism New Zealand – market insights on China for 2019 (accessed in October 2022), https://www.tourismnewzealand.com/insights/markets-overview/

17 Tourism New Zealand, '*Te Ohanga Report*', November 2020, https://www.tourismnewzealand.com/assets/insights/industry-insights/tnz-te-ohanga-report-2.pdf

Pandemic impacts

The pandemic triggered a significant contraction in the sector, as shown in Figure 7. Exports fell by over $1.5 billion between YE December 2019 and 2021, to $114 million. In YE June 2022, there was a very slight recovery, to $119 million; the overall decline between YE June 2019 and June 2022 was 92 percent. While China still ranks as New Zealand's third largest market, tourism now accounts for only 11 percent of services exports to China, compared to 48 percent pre-pandemic.

Source: StatsNZ data

Case Study: Ngāi Tahu Tourism

Ngāi Tahu Tourism is part of Ngāi Tahu Holdings – one of the largest iwi-owned businesses in Aotearoa. Pre-pandemic, Ngāi Tahu Tourism offered a range of experiences to visitors from China and elsewhere, including the Agrodome, Shotover Jet, the Dark Sky Project, the Huka Falls, Franz Josef Glacier visits, the Hollyford Track and others. The Chinese market has been very significant, with some attractions – notably the Agrodome – attaining iconic status for Chinese tourists, and with strong Chinese interest in Māori cultural elements during visits. Even prior to the pandemic, however, demographic changes had been evident, with a shift from tour groups towards independent travellers, including high net-worth family groups interested in tailor-made travel experiences.

The pandemic effectively put Ngāi Tahu Tourism into "hibernation", severely reducing visitor returns and prompting the disestablishment of many positions in the business. It also gave Ngāi Tahu a good chance to reflect on the business and how to rebuild it sustainably post-COVID. In the short term, there are capacity constraints at the New Zealand end, with significant labour shortages across all tourism businesses and supporting industries.

In Ngāi Tahu's view, future growth seems likely to come from innovative new product offerings which add value to the visitor experience, for fewer, but higher-yield, customers. New Zealand is now an expensive destination for Chinese visitors compared to Asia or Europe; the earlier model – large numbers, low margins, short stays – may no longer be sustainable. However, the future looks pretty bright. Despite challenges such as pandemic travel restrictions and China's economic slowdown, a core cohort of Chinese tourists will still be keen to come to New Zealand. A gradual restoration of travel seems likely in the period ahead – but New Zealand also has a lot of work to do to be ready for the return of Chinese visitors.

Case study: China Travel Services

China Travel Services (NZ) Ltd was established in New Zealand in 2000, one of the overseas branches of the parent company based in Hong Kong. CEO Lisa Li, originally an international student before setting up China Travel Services in Auckland, recalled that challenges in those early days included a lack of direct flights and restrictions on visas, despite New Zealand being among the first countries to receive Approved Destination Status from the Chinese government in 1999.

2010 was a real turning point, with more direct air connectivity, more open visa policies, a concerted push from Tourism New Zealand and operators, and a new interest from Chinese visitors in longer stays and higher-quality visits. China Travel Services had been able to increase its coach tours from one itinerary in 2003, to seven in 2010. Chinese visitors were valued for their discerning approach, high average spend and year-round interest in visiting. By 2016, however, the capacity limits of good-quality New Zealand hotels and other infrastructure were becoming apparent, and Li had advocated for increased investment. Growth was strong, but numbers were lower than forecast. New Zealand was perceived as expensive – and sometimes of variable quality.

The pandemic had a severe impact, but has also given the sector a chance to re-evaluate existing models. China Travel Services has stayed connected through the period with Chinese consumers via social media – an important channel to reach the younger generation of travellers, and one on which New Zealand operators would need to focus increasingly in the future. Looking ahead, the picture was still optimistic, both for tourism out of China and also for the Chinese diaspora globally (another important potential target market, in Li's view). A key consideration would be how to maintain value for money: a long-haul destination like New Zealand was inherently an expensive proposition; prices could be high, as long as visitors were satisfied. Currently the sector was struggling with labour shortages and supply and quality constraints. There were also continuing challenges for visitors in accessing visas, particularly now that global immigration offices had been replaced with a slow and burdensome online process. These elements would all need to be addressed to see tourism return to its earlier trajectory.

Imports of tourism services (that is, New Zealanders going to visit China) have always been at a much lower level compared to exports, reaching a peak of $258 million in YE December 2018, but falling to $36 million in YE June 2022. Nevertheless, more than 100,000 New Zealanders are estimated to have visited China in 2019.[18]

Prospects

Pre-COVID, China accounted for around one-tenth of the world's tourism departures and was the world's largest source of tourists, but at present, China is effectively absent from world markets. It is widely expected that pandemic restrictions, including mandatory quarantine measures and inbound travel controls, will gradually start to be eased in 2023, but there is persistent uncertainty about the pace and timing of this. During the October 2022 National Day holiday, for example, domestic tourism revenues reached just 44 percent of their 2019 level, despite earlier upbeat forecasts, and COVID-linked disruptions continue to occur.[19] Recent commentary suggests that Chinese tourists may not return to New Zealand until 2024.[20]

Once Chinese citizens are able to travel more freely, the prospects are promising for a revival of tourism in the medium term, although whether this will rebound to earlier levels remains unclear. The Economist Intelligence Unit's *Tourism Outlook 2023*, for example, anticipates that Chinese tourist

[18] https://www.nzcta.co.nz/chinanow-profile/2057/china-nz-celebrate-successful-year-of-tourism/
[19] https://www.reuters.com/business/healthcare-pharmaceuticals/china-holiday-tourist-trips-fall-18-year-broad-covid-curbs-2022-10-08/
[20] https://www.1news.co.nz/2022/11/20/tourists-from-china-may-not-return-until-2024-nash/

numbers will only return to about one-third of pre-pandemic levels in 2023 at least.[21] China's aviation regulator has issued a five-year development plan with a focus on restoring international air travel over an even longer timeframe, by 2025.[22]

Key factors in Chinese consumer decision-making on future travel are the lifting of international border restrictions in China and the incidence of COVID-19 cases in the destination country, according to surveys.[23] Research also suggests that lockdowns have tended to lower consumer confidence, although this has rebounded after a period.[24]

Surveys of Chinese traveller sentiment undertaken throughout 2021 and in mid-2022 suggest that the desire to travel both domestically and abroad remains strong, despite the factors noted above. Among 'Active Considerers' (New Zealand's target demographic), 89 percent are keen to travel within six months of restrictions lifting, although in the short term, intentions are focused on domestic and short-haul travel. In terms of destinations of interest, 62 percent of Active Considerers are eager to travel to New Zealand within three months of it being possible.[25]

Whenever tourism resumes, both the New Zealand offering and Chinese demand seem likely to be reshaped, as the two case studies above illustrate. Chinese traveller preferences are shifting away from group travel and towards family holidays and independent travel, with an emphasis on quality and value for money.[26] There is likewise a focus at the New Zealand end on higher-value tourism as well as an increasing emphasis on environmental and economic sustainability.

Commentators also identify a shift towards more digitally-oriented consumer channels, such as using social media and influencers to connect with potential customers and promote New Zealand as a destination. New Zealand operators will need to be prepared to respond to this shift and engage online in the period ahead in order to boost the sector's recovery.[27]

International education

China is a very important destination for New Zealand international education, accounting for one-third of international student enrolments in 2020, and consistently ranking as New Zealand's top market in terms of export value. China is also a significant leader in terms of the number of fee-paying international students, as Figure 8 shows, peaking at 38,555 in 2017, dropping off slightly to 35,460 in 2019, and falling to 15,230 in 2021. For context, total international student numbers were 118,305 in 2017, 110,095 by 2019, and 37,620 in 2021 – meaning China accounted for 40 percent of the international student body in New Zealand in 2021.[28]

Despite China's importance to New Zealand, however, New Zealand has a small share of the very large total population of mobile Chinese tertiary students, accounting for only 1.8 percent of students in 2019. By contrast, Australia had a 14.7 percent share.

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[21] Economic Intelligence Unit (2022), *Tourism Outlook 2023 – Turbulence in the travel industry*.
[22] https://www.reuters.com/world/china/china-targets-over-270-civil-airports-by-2025-aviation-regulator-2022-01-07/
[23] Kantar (2022), 'Impact of the COVID-19 pandemic on intentions to travel among Chinese Active Considerers'.
[24] McKinsey & Company (2022), '*Outlook for China tourism in 2022: Trends to watch in uncertain times'*, 22 February 2022
[25] Kantar (2022), 'Impact of the COVID-19 pandemic on intentions to travel among Chinese Active Considerers', June 2022
[26] China Briefing from Dezan Shira & Associates, 'Tourism in China: 2022 Trends and Investment Opportunities', 9 August 2022, https://www.china-briefing.com/news/chinese-tourism-2022-trends-and-opportunities/
[27] Interview by Kea with Tourism New Zealand CEO, https://keanewzealand.com/tourism-nz-road-to-recovery/
[28] https://www.educationcounts.govt.nz/statistics/international-students-in-new-zealand

Figure 8: International Fee-Paying Students in NZ

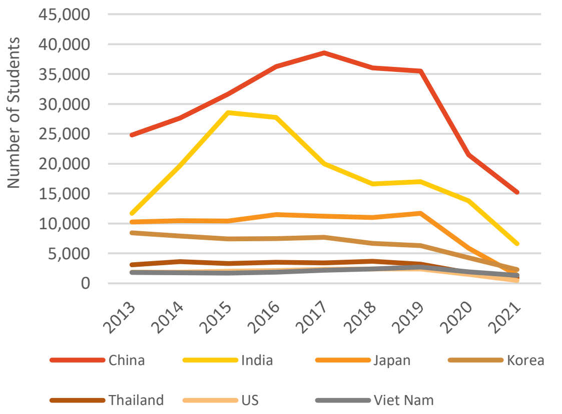
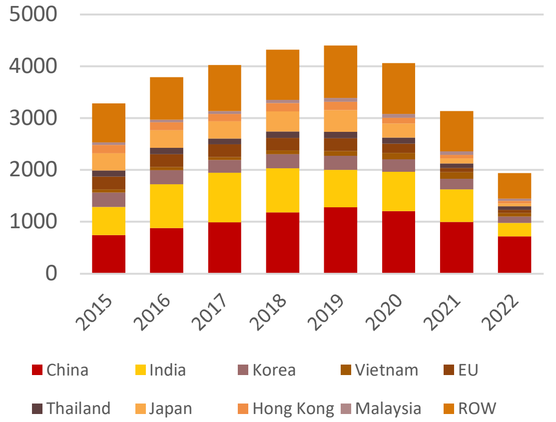


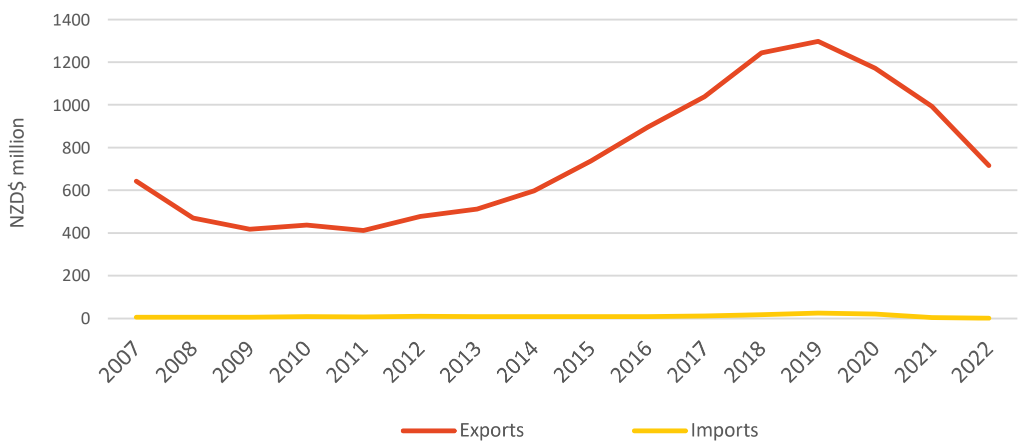
Figure 9: International education markets



Source: https://www.educationcounts.govt.nz/statistics/international-students-in-new-zealand

In terms of export returns, education-related travel to China peaked at $1.3 billion in YE June 2019 – roughly double the $643 million value of 2007 – but had already been growing strongly since 2011, as Figure 10 shows.

Figure 10: Trade in international education (June Years)



Source: StatsNZ data; figures show "education-related travel services"

Most of these "Mode 2" onshore education exports have been delivered through universities (41 percent of Chinese students in 2019), Institutes of Technology and Polytechnics, (now Te Pūkenga, 12 percent in 2019) and at private tertiary establishments (11 percent in 2019), with a growing cohort also present in schools.[29] It is worth noting that the relatively stronger performance of the university sector likely relates to the cultural importance attached to high-quality university education in China. This may have implications for the uptake of vocational education, despite new FTA opportunities (see 'Prospects' below).

In addition to this onshore delivery, New Zealand institutions have also developed a range of Mode 3 (or combined Mode 2 and Mode 3) offshore models, including institutional partnerships such as joint programmes, joint institutes, "articulation" or credit recognition and other models of exchanges or

[29] Education New Zealand (2022), '*Market Insights Dashboards*', https://intellilab.enz.govt.nz/

links between institutions, teachers and students. In many cases, students study for periods in both China and New Zealand, with the China component serving as a pipeline to onshore delivery. Offshore delivery may also include some "Mode 4" provision (where a New Zealand academic goes to China temporarily to teach or provide management services at a shared institution).

As is the case for tourism, the trade statistics alone do not tell the full story of the value of export education to New Zealand. There are important intangible cultural and social benefits for both sides that are generated by deeper awareness and mutual understanding of respective cultures, perspectives and views, as well as the development of business, investment, research and other partnerships. Chinese students, including at post-graduate and post-doctoral level, contribute to the diversity, depth and richness of the academic community: their academic publications help to support the international rankings and competitiveness of New Zealand universities, and their research in New Zealand and in partnership with Chinese academic collaborators feeds in to the New Zealand research and development ecosystem.

There are also broader economic benefits. "Education-related travel services" is a standard statistical category which includes the value of goods and services acquired by international students in New Zealand, including tuition costs and living expenses such as food and accommodation. However, this does not fully capture the "induced impacts" such as employment in the wider economy from student spending, domestic tourism and family visits. Using this framework, the economic value of Chinese students was assessed at $1.8 billion for 2019, compared with "education-related travel services" of only $1.3 billion.[30] China accounted for over one-third of the total $4.9 billion of the onshore economic value of international education in 2019, and Chinese students made the highest economic contribution per student of the international student body.[31]

Pandemic impacts

The international education sector has fared somewhat less badly than tourism through the pandemic, falling from $1.3 billion in YE June 2019 to $715 million in YE June 2022. China's first place in the international education rankings has been sustained, and in fact exports to China between June 2019 and June 2022 fell by proportionately less than New Zealand education exports to India and other top markets: China dropped by 44 percent, compared to a contraction of 63 percent for India.

The proportionately lower drop in education compared to tourism no doubt reflects the fact that international students come to New Zealand and stay for a period. Student enrolments from China decreased by 31 percent in the first year of the pandemic, but while new students were not able to come to New Zealand, a proportion of the Chinese student body remained in-country, meaning that "exporting" effectively continued.[32] By contrast, for tourism, the 'visitor tap' was turned off.

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[30] Education-related travel statistics from Statistics New Zealand. The "value" of international education is from Education New Zealand (2021), *2019 Economic Contribution and Enrolments Infographic*, January 2021, https://intellilab.enz.govt.nz/economic-impact/

[31] Market Economics Consulting (2019), *2018 Economic Valuation of International Education in New Zealand*, page 24.

[32] ENZ Market Insights Dashboard (2022).

Case Study: University of Waikato

The University of Waikato has a longstanding relationship with China. Having launched its first initiatives with Chinese partners as far back as 1997, and with significant new collaborations established in 2002 and 2015, the University of Waikato's current programmes with China include:

- A Joint Institute at Zhejiang University City College (ZUCC) in Hangzhou, offering three undergraduate programmes fully taught in China by ZUCC staff and 15 New Zealand University of Waikato academics, leading to a degree from both universities. Since 2017, it has had around 230 students each year with around 900 students recorded in 2022;
- A programme with Shanghai International Studies University (SISU), including three New Zealand staff, offering pathways to degrees at the University of Waikato; and
- An undergraduate programme at Hebei University of Science and Technology in Shijiazhuang for an engineering degree, which can be transferred for the final 1.5 years at the University of Waikato.

The University of Waikato is the first New Zealand university to be approved to teach and award three of its degrees fully onsite in China. Pre-pandemic, ZUCC students would come to New Zealand for short-term study abroad, but this has not been possible since 2020; pandemic restrictions have also affected the ability of students in New Zealand to return home for holidays. There has also been significant disruption to programmes in China, with restrictions on face-to-face delivery and gathering sizes on-site, and challenges for staff working in China, with rolling lockdowns and sporadic moves to online teaching. Given these impacts, the University of Waikato has been concerned about student pastoral care and staff welfare, including the challenges that come from studying at home. Accordingly, the University set up a 'China Learning Centre' at Hainan University in Haikou, catering to a cohort of up to 40 students per semester. Students who remain in China are able to live and study at this new campus, participating in online classes delivered by University of Waikato academics, with academic tutors physically present to provide both learning support and pastoral care.

Case Study: University of Auckland

At the start of the pandemic, the University of Auckland quickly pivoted to become New Zealand's largest online education services provider, losing only around 3 percent of its students between 2019 and 2021.

The University established five China Learning Centres throughout China, accommodating around 1,000 students per year; the first cohort is close to completing a full qualification using this learning centre model. These Centres sought to duplicate the normal "student experience", with students living in dormitories and collectively participating in classes online. This approach has been very successful, with the University of Auckland rated as one of the best performers in terms of enrolment, retention and student satisfaction compared to the study centre offering of its international competitors.

Looking to the future, the University of Auckland's Associate Director, Innovative Business Solutions, Jerry He, commented that international students could be grouped into three main categories: around 70 percent wanted to continue to study in New Zealand and make use of post-study work rights; another group wanted to study abroad but return home afterwards; and a third group wanted an international accreditation, but would prefer it "at home".

In He's view, digital delivery as well as different forms of articulation or joint programmes would both be integral to any future New Zealand strategy, offering advantages in terms of sustainability (by reducing air travel), innovation in programme design, creating a pipeline of onshore students, and meeting increasing Chinese interest in undertaking international education within China. The University of Auckland was actively expanding its articulation and joint programmes. Although China had traditionally been reluctant to approve online delivery, prospects for this continuing looked promising so far.

In terms of future success, a more coherent New Zealand Inc approach would be useful, He commented, focusing on welcoming and facilitating Chinese students and nurturing New Zealand's welcoming profile. Other models such as licensing the New Zealand 'brand' for delivery in-market could be considered, as had been successfully utilised by Australian and other competitors.

Case Study: ICL Education Group

ICL Education Group is a private international education provider. It offers a range of tertiary-level business, computing, English and Early Childhood Education programmes, including Master's degrees and graduate and other diplomas, delivered through three Auckland-based schools (ICL Graduate Business School, Auckland English Academy and Bridge International College). China is the source of over half of ICL's current students, although this share was around 30 percent pre-pandemic.

COVID-19 has had a significant impact, reducing the student body from 1,100 pre-pandemic to under 250 at the lowest point, with English language students falling sharply from 600 students to 80. As a provider of graduate-level programmes, ICL has been able to offer advanced degrees such as its Master of Management and Master of Business Informatics programmes to students who wanted to remain in New Zealand (or had not been able to return to China) but had completed their previous programmes. ICL had quickly pivoted to offering online delivery, like all institutions.

Being able to offer online study to offshore students has enabled it to continue to recruit in China, although it has had to adjust its Google-integrated 'Canvas' Learning Management System technology platform to accommodate Chinese digital restrictions. It currently offers "hybrid classrooms" for two of its Masters courses and three language courses. ICL Chairman Ewen Mackenzie-Bowie anticipates that some online students will want to come to New Zealand to complete their degrees when conditions permit, but also foresees that "blended learning" will be a key part of future models.

ICL is seeking to develop new programmes that will include a year studying online in China and then up to two years in-person in New Zealand, enabling students to access post-study work rights – although in ICL's experience, this was not of interest to all. Mackenzie-Bowie is optimistic about future prospects with China: the relationship is good, there is still strong interest from Chinese students, and innovative approaches have enabled business and relationship continuity despite the challenges of the pandemic.

Case Study: Whitecliffe College

Whitecliffe College is one of New Zealand's highest-ranked and awarded private sector research institutions, with Schools of Fine Arts, Design Innovation, Fashion and Sustainability, Information Technology and Creative Arts Therapies. Pre-pandemic, Whitecliffe had been seeking to grow its international student body, but this cohort was still small, meaning Whitecliffe had been less badly affected by pandemic disruptions than many others in the private sector. Early in the pandemic, in fact, it had started to see some growth in enrolments of international students who had completed their existing studies and wanted to remain in New Zealand. Whitecliffe's focus was increasingly on bachelor-level postgraduate qualifications such as master's degrees (which gave a longer period of post-study work rights) and on sectors such as digital technologies, IT, creative enterprises and innovation.

China is a key market in Whitecliffe's export education growth strategy. Whitecliffe has recently developed a joint programme for a Bachelor of Design and Digital Media with Jingchu University of Technology, entailing three years' study in China and two in New Zealand. Around 100 students have enrolled for 2023, and staff from both institutions will spend some time teaching in each country. This would not only enhance Whitecliffe's international presence, but also generate professional and research opportunities for staff. Whitecliffe had also developed a relationship with Shendong Women's University to look at cooperation opportunities, and is currently in discussions for a similar partnership with Qingdao Film Academy.

During the pandemic, Whitecliffe had pivoted to online delivery and this had worked well, but it was also investing in new product development at bachelor level and above, and exploring other models, including institutional partnerships and more immersive approaches along with blended digital and in-person learning. Success in China demanded both innovation and agility, including to navigate a challenging regulatory environment, but there were promising opportunities.

It is worth highlighting the different trends in student preferences that emerge in the case studies above: while some students continued to study at their existing institutions during the first part of the pandemic, others had completed courses and, rather than returning to China, chose to transfer to higher-level programmes or institutions in New Zealand. Other students continued with their existing studies but remotely from China, notably using 'study centres'; in other instances, institutions were even able to recruit new students in China for remote study in New Zealand courses.

Prospects

The continuation of the 'study centre' model is uncertain, and depends not only on the duration of current Chinese travel restrictions (and hence the absence of students in-person in New Zealand), but also on China's continued acceptance of digital delivery. China has previously had a restrictive approach to online delivery, but allowed considerable flexibility on this through the pandemic, unlocking the innovative models that are described in the case studies – albeit that providers still faced a range of restrictions, for example around accessing some platforms and apps, due to Chinese digital regulations. Some New Zealand institutions see promise in "blended" (partly online, partly in-person) or fully online models in the future, including to meet emerging Chinese demand for "international education at home".

The pivot to digital during the pandemic may also have created new opportunities for New Zealand 'edtech' (educational technology) exporters as part of the innovative models described above, or even integrated into China's domestic education provision.

As China continues to develop a stronger domestic education sector and there is greater confidence and interest in this offering from Chinese students, there may be new opportunities for New Zealand providers to supply international education in-market. On the other hand, there are also emerging restrictions, such as recent "double reduction" regulations which prevent education providers from offering academic courses to primary and middle school students on a for-profit basis.[33]

In any case, the pandemic is likely to have lingering impacts on New Zealand export education export competitiveness. Factors include Chinese perceptions of New Zealand as a safe and open destination, as well as current New Zealand and Chinese immigration and education policy settings. International surveys of agents and students suggest that New Zealand may now be seen as less welcoming than previously, likely as a result of the lengthy border closure and slow visa processes compared to competitors. While the majority of Chinese students have a positive student experience, the surveys also show that they rate the New Zealand experience lower than the average for international students. Awareness of New Zealand as a study destination also decreased from 2020 to 2021.[34]

A further critical element relates to the ability of students to access visas and post-study work rights, which was frequently identified as a major challenge in our interviews in rebuilding exports in a very crowded and competitive marketplace. New Zealand only restarted visa issuing in the third quarter of 2022, and there is a sizeable backlog.[35] Onshore student visa numbers dropped sharply at the start of 2020 and have fallen steadily since then; approved student visas from China have fallen by 67 percent year-on-year.[36] Some of those interviewed commented that re-establishing an immigration

[33] https://thechinaguys.com/china-double-reduction-policy-private-education-tutoring-crackdown/

[34] Navitas (2021), *Navitas Agent Perception Survey* – this survey tracks sentiments since early 2020. The quoted insights are from a survey of over 1,000 agents conducted in October 2021; and Education New Zealand (2022), '*Market Insights Dashboards*'.

[35] https://www.nzherald.co.nz/travel/backlog-of-36000-international-tourists-waiting-for-visitor-visas/TQ4APUWU6IKXM7HBQMBXT3HQ4U/

[36] Education New Zealand (2022), '*Market Insights Dashboards'*, https://intellilab.enz.govt.nz/

footprint in China could be helpful to support the recovery, as student feedback suggests that the online process can be burdensome, slow and frustrating.

By contrast, a number of New Zealand's major competitors, such as the United States, Canada, the United Kingdom and Australia, have been open for some time and are actively increasing post-study work rights. On the other hand, geopolitical tensions could also influence decisions about study destinations. Overall, it was hard to make firm predictions about the shape of the future market.

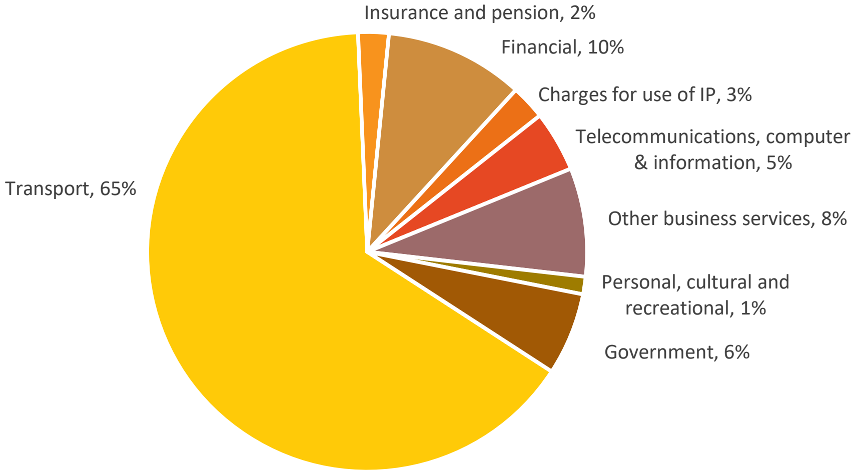
There may potentially be scope to grow the vocational education sector thanks to new commitments in the 2022 FTA Upgrade to enable in-market delivery of non-academic training in English, cooking and handicrafts, as well as further cooperation on the recognition of professional qualifications. This may enhance the ability of New Zealand education providers to deliver vocational education services in China, including serving as a pipeline to onshore provision. However, it seems that interest from New Zealand providers may be limited for now, reflecting both a mixed business case and low Chinese consumer demand.

Section Five: Other services export sectors

Figure 11 below shows the shares of "non-travel services" exports to China for YE June 2019 (that is, excluding tourism, international education and other types of travel) – for scale, the total value of these non-travel services in YE June 2019 was $313 million, while in the same year, travel services were worth $3.0 billion – ten times the value.

Transportation[37] dominates the non-travel category, accounting for 65 percent of non-travel exports, with the next two largest categories being *financial services* and "*other business services*". The latter includes some important services that support New Zealand goods trade, such as *distribution* and *technical services* (including engineering and architecture), as well as *professional services* (such as law or accounting) and *research and development*.

Figure 11: Shares of non-travel services, Year Ending June 2019



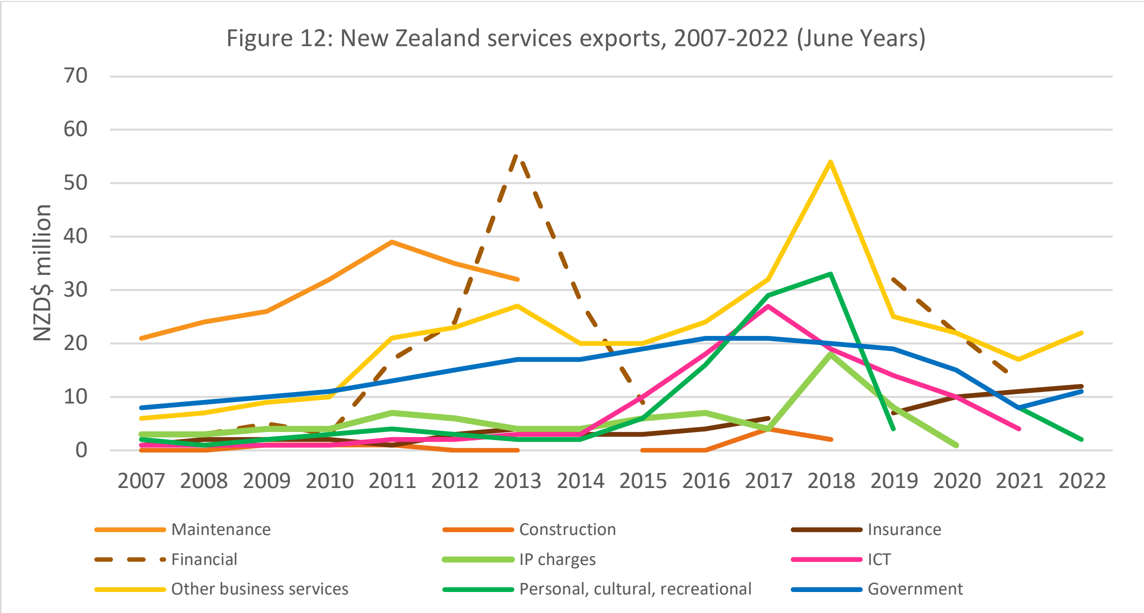
Source: StatsNZ data

Other important services exports to China over the last five years have been of a considerably smaller order of magnitude and highly variable performance, as Figure 12 illustrates. Sectors have included insurance and pension services; government services; personal, cultural and recreational services

[37] This category includes passenger transport, freight, other transport and auxiliary services, and postal and courier services.

(including film and television, heritage and cultural services, recreation, health services and education services); charges for the use of intellectual property (including licensing fees for franchises and trademarks, licences for the reproduction or distribution of computer software or audio-visual products, and other charges for the use of intellectual property); and 'Information, Communications and Technology' (ICT) (including sectors such as software and videogaming). There is limited data available for 'maintenance and repair services' and construction.

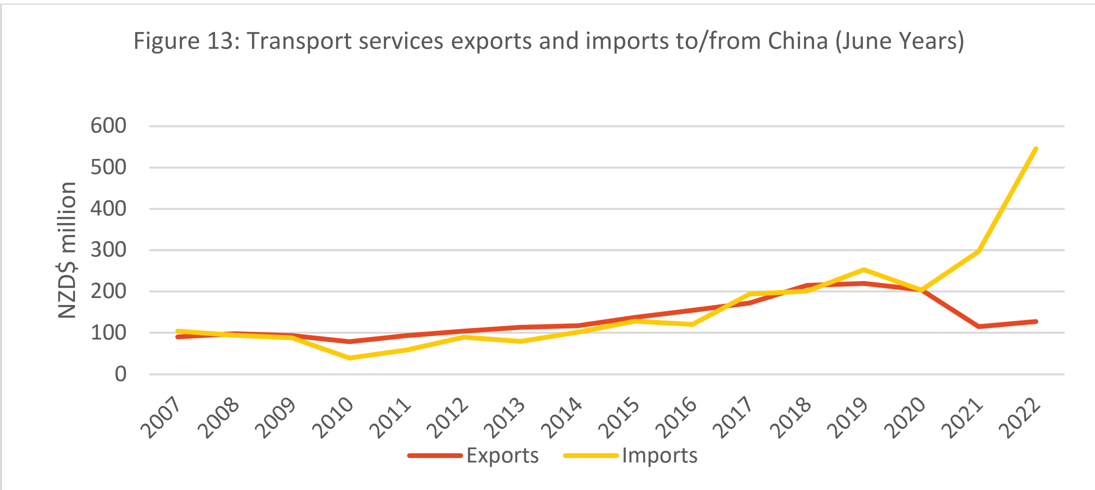
Selected sectors are discussed further below, including transport, ICT services and personal, cultural and recreational services. Additional material on financial services, insurance and pension services and 'Other Business Services' is in Annex III.



Source: StatsNZ data, 'Discontinued' BoP series and Trade Dashboard

Transport

New Zealand's exports of *transport services* to China includes a range of sub-sectors, including sea transport (primarily sea freight), air transport (passenger, freight and other) and postal and courier. It is not possible to give a detailed breakdown of the shares of each of these categories on the export side due to data gaps and data suppression. For imports, in 2022, 85 percent were from sea freight.



Source: StatsNZ data

Transport services is a significant category, representing around 12 percent of services exports to China in 2022 and 66 percent of imports. Both exports and imports were steady pre-pandemic, with exports gradually increasing from around $100 million to a peak of $221 in YE June 2019 and imports gradually increasing from a similar level to $256 million in YE June 2019. China was the second-highest export destination for transport pre-pandemic.

However, as Figure 13 shows, the pandemic has had a significant impact: by 2022, exports had dropped to $127 million, and imports had surged to $546 million – reflecting globally high prices as much as volume. This has some important implications for the headwinds that New Zealand goods exporters may continue to face, despite the record performance of primary sector exports.

The two case studies below illustrate different perspectives on transport services: an airline and an airport, both focused on facilitating people movement as well as airfreight, and both also closely engaged in downstream sectors such as tourism.

Case Study: Air New Zealand

Air New Zealand has a longstanding commitment to China, being the first carrier to launch non-stop direct flights in 2006, and running daily services between Shanghai and New Zealand prior to the pandemic. Air New Zealand's deep engagement with the Chinese market has been driven by a combination of significant visitor volumes, strong and growing business links, and increasing airfreight demand. Its relationship has represented a significant investment in what has been a challenging, complex and highly competitive operating environment.

Not surprisingly, those challenges became even more daunting with the onset of the pandemic. Severe and unpredictable travel disruptions, restrictions and border closures quickly threatened the continued viability of airline connectivity – and by extension, would have had a negative ripple effect on trade as well as the broader bilateral relationship.

Some 80 percent of airfreight normally takes place 'under the feet' of leisure and business travellers; a buoyant tourism economy means more efficient and competitive airfreight – and vice versa. Support from the New Zealand Government for airfreight capacity has been absolutely crucial through this period. Air New Zealand remained focused on connectivity through Shanghai but was able to diversify by providing additional cargo access into Guangzhou for exporters to Southern China as road connectivity out of Hong Kong proved challenging, and made good use of demand for cargo-only charters.

Looking to the period ahead, challenges look likely to remain the order of the day, thanks to continuing COVID uncertainties, including in respect of Chinese policy settings, airport operations and demand, as well as pandemic-induced capacity constraints at the New Zealand end.

Air New Zealand is keen to reengage and rebuild as soon as market conditions allow. There remains a strong demand for airfreight, including in response to the growth of e-commerce out of China and its "fast-fulfilment" needs; there would be benefits for the resilience of the operating model if New Zealand airfreight were also to diversified somewhat from a few key primary sector products. Connectivity among different ports and with road transport or multimodal models (for example, integrating sea freight) at the China end also remains challenging, with implications for New Zealand freight as well as passenger traffic.

The role of the New Zealand Government – to support airfreight capacity, but also to engage and build confidence with Chinese counterparts in relation to regulatory settings for air services – has been and will remain critical. The period ahead will be an important and demanding one for businesses, including Air New Zealand but also others in the freight, logistics and distribution sectors, as they seek to rebuild critical supply chain pathways and relationships in China.

Case Study: Christchurch International Airport

Christchurch International Airport (CIAL) identified China as a key market many years ago, and has actively sought to develop a vibrant, broad and deep engagement between China and South Island businesses and sectors.

An important first step was establishing a direct air connection between China and Christchurch. CIAL was able to achieve this through the development of a relationship with China Southern Airlines – an engagement that took considerable time, effort and energy over an extended period (not to mention creative advocacy for a market which initially ranked 190th in the list of destinations for the airline), which eventually resulted in the establishment of daily flights year-round.

This connectivity generated significant economic benefits, with the value of widebody aircraft flights estimated at an additional $150 million in visitor spend and $550 million in airfreight exports each year; and for the airline itself, enhanced profitability through a high-value route.

Other initiatives have included efforts to create a welcoming visitor experience (for example, with Chinese-language signage and 'ambassadors' at CIAL), the 'South' programme, which helps to build the China-readiness and connections of South Island businesses; and a relationship with the Alibaba Group, including making use of Alibaba travel services platform Fliggy to promote the market, and encouraging South Island businesses to accept Alipay in order to facilitate the Chinese visitor experience. A central theme has been 'flying in formation' – coordinating the broader business community in the effort to promote and innovate in the New Zealand tourism offering.

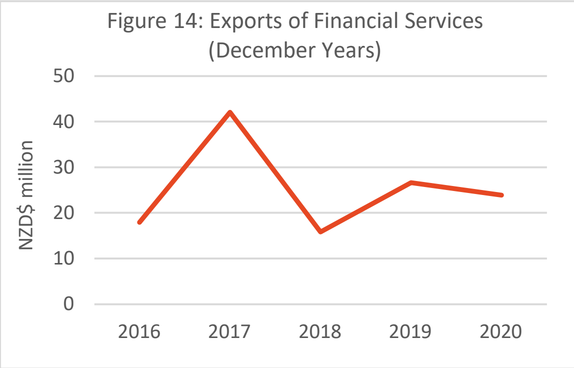
A key lesson in dealing with China, according to Justin Watson, Chief Aeronautical and Commercial Officer at CIAL, is the importance of relationships: "With China, it's relationships first, business second". Both formal and informal engagement is needed, informed by up-to-date knowledge about influential figures in the market. This meant that, with the advent of the pandemic, extra effort was required – both to reassure Chinese contacts about New Zealand's commitment to the relationship, and to keep the connections 'live' despite the severe curbs on connectivity.

Equally important has been the involvement of the New Zealand Government, agencies such as the Ministry of Foreign Affairs and Trade, Tourism New Zealand and New Zealand Trade and Enterprise, and local government (CIAL helped coordinate a visit to China by the Mayor of Christchurch, and a letter from South Island mayors, for example). This has helped to build confidence across all levels of the China ecosystem, deepen regulatory cooperation and lend credibility to business efforts.

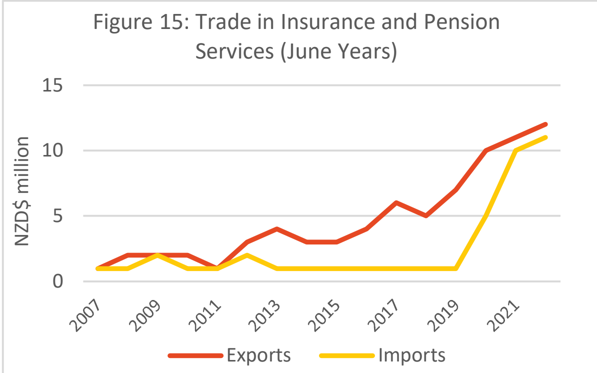
Looking ahead, CIAL is optimistic about the future. Clearly, a very significant rebuilding of relationships will be needed once China opens up again. Careful targeting of important market segments will likewise be needed, but this had already been integral to CIAL's approach, as a 'niche' operator when it came to China. Of significance, however, it seems unlikely that the market would return to the same size: it would possibly settle permanent at about half the pre-pandemic volume, reflecting both a Chinese economic slowdown and a swing in preferences towards domestic tourism rather than international. But there were still growth opportunities to be found, and the high-end leisure market was forecast to rebound the most of any tourism segment, leaving New Zealand well placed.

Financial Services

Recent trade in *financial services* is shown in Figure 14. Growth in financial services pre-pandemic was highly variable, but peaked at $42 million in 2017 and fell to $23 million in 2020. The data shows an export value of zero for 2021 and YE June 2022. China accounted for 1.8 percent of New Zealand's total exports of financial services in 2020. Data on financial services imports is only available in a discontinued data set, and is subject to extensive data suppression. However, it indicates that financial services imports reached $64 million in YE June 2018, but have declined since.



Source: StatsNZ data, December Years



Source: StatsNZ data, June Years

Insurance and Pension Services

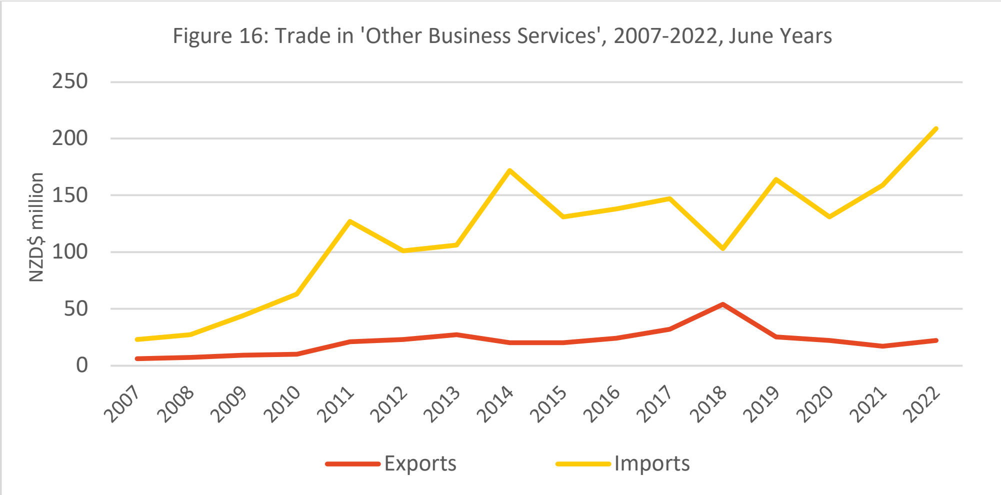
Figure 15 shows trade in *insurance and pension services*. This has been a sector of steady growth in both exports and imports – mainly reinsurance – and especially through the pandemic, albeit small in dollar terms and of a considerably lower order of magnitude than financial services in particular. In YE June 2022, New Zealand exported $13 million of reinsurance services to China (New Zealand's second-largest market for insurance exports), up from $3 million in 2019. China now accounts for 14 percent of New Zealand's total exports of insurance and pension services, up from 3 percent pre-pandemic. New Zealand also imported $11 million in reinsurance from China.

'Other Business Services'

The category "*Other Business Services*" includes a wide range of services, which can be grouped under three main sub-categories, including *technical, trade-related and other business services* (this includes architectural, engineering, scientific and other technical services, as well as waste treatment and de-pollution, agricultural and mining services, operating leasing services and trade-related services such as distribution, a key enabler of goods trade via e-commerce platforms); *professional and management consulting services* (which includes sectors such as legal, accounting, management consulting, public relations, advertising and market research); and *research and development*.

As Figure 16 shows, New Zealand exports have been fairly static since the FTA was signed, with a small peak of $54 million in YE June 2018, followed by a gradual decline. Exports in YE June 2022 were $22 million. Imports have been consistently higher, ranging from $100 million to over $150 million since 2010, and increasing steeply through the pandemic period to peak at $209 million, representing one-quarter of services imports from China.

The dominant export sub-category has been *technical, trade-related and other business services not elsewhere indicated* ("n.e.i."), with modest levels of *professional services* and very small exports of *research and development*. Within the first category, trade-related services, especially distribution, dominate, along with a residual '*other business services'* category which includes translation services; in professional services, legal services make up the biggest share by far. Overall exports in the "*Other Business Services*" categories declined during the pandemic, but imports have increased. This may reflect the growth in Chinese exports of distribution services, for example through increased and evolving e-commerce activity and integration with other types of services, including e-payments.[38]



Source: StatsNZ data, June Years

Case Study: Magic Lamp

A number of businesses have been able to leverage high-quality New Zealand primary sector products to develop innovative and interlinked niche services offerings related to trade. Magic Lamp, which operates in the cross-border e-commerce (CBEC) space, is a good example of this kind of creative thinking. Chinese CBEC channels have expanded rapidly in recent years, with the market estimated to be worth 14.6 trillion yuan (about USD$2.25 trillion) in 2021.[39] China's regulatory settings support this growth, including through trade-facilitating rules on registration, testing and labelling.

Magic Lamp showcases high-quality New Zealand consumer brands (mainly premium food and health products including infant formula, honey and others) on major Chinese e-commerce platforms such as Tmall, JD.com and Little Red Book. It also provides a range of support services to New Zealand brand owners including logistics, shipping and Customs clearance for CBEC sales.

Since 2015, Magic Lamp's business model has evolved considerably: initially based on the "*Daigou*" channel, it shifted to e-commerce platform sales supplied out of New Zealand warehouses and even established brick-and-mortar stores in New Zealand to support CBEC sales. It also expanded to include products from Australia and a number of other countries. Magic Lamp was the e-commerce category award winner in the 2017 HSBC New Zealand China Business Awards, and in 2018 won Best Startup from the Tencent Incubator Shenzhen Office.

The pandemic caused significant disruption to the existing business model, due to persistent challenges with airfreight availability and tourism contraction that led to the closure of a number of its retail stores – even as demand surged in China. Magic Lamp has pivoted to focus on livestreaming, utilising key platforms including Douyin, Kuaishou and WeChat Video, and providing services to brands to support content creation. It has also shifted to supplying customers out of bonded warehouses in China, with inventory sent via sea freight, and focuses on wholesale business-to-business customers in China, rather than Daigou channels. Founder Ray Pengyu Deng believes that even more innovations are possible in future services trade, including the potential to package products in China for discerning Chinese customers, licensing New Zealand intellectual property and brands to do so.

[38] Mark Tanner, 'When Douyin Reached Critical Mass for Ecommerce in China', 2 November 2022, blog for China Skinny, https://chinaskinny.com/blog/douyin-ecommerce-china
[39] http://english.www.gov.cn/news/topnews/202204/26/content_WS62675588c6d02e5335329edd.html

'Telecommunications, computer and information' services

It is challenging to measure the value of digital services exports, including digitally-delivered exports of a range of more traditional services, such as finance or business services. (Annex I has a fuller discussion of this issue.)

While it is accordingly difficult to gauge the overall level of "digital services trade" with China, there have been some clear trends in trade with China of *telecommunications, computer and information* (ICT) services, including computer services, software and other related services.[40] Also relevant are 'charges on the use of intellectual property', which includes software licensing; while the data is not available to disaggregate the headline category to this level, it is worth noting that this category peaked in 2017, as did ICT and the sub-sector of computer software.

New Zealand exports to China of ICT services peaked at NZD$27 million in YE June 2017, but fell to $14 million in 2019, and to only $4 million in 2021. (Figures for 2022 are not available.) By contrast, as Figure 18 shows, New Zealand exports of ICT services to world markets were worth $1.6 billion in YE June 2021, having risen steadily through the pandemic. Exports to China accounted for a mere 0.3 percent.[41]

Figure 17: New Zealand trade in ICT services with China

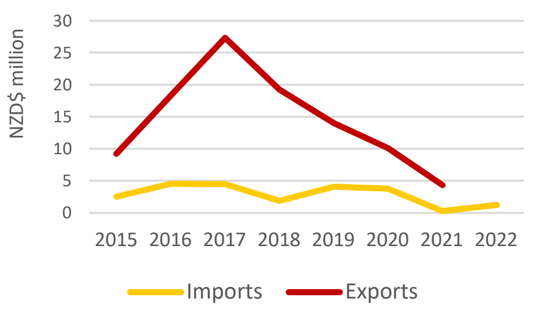
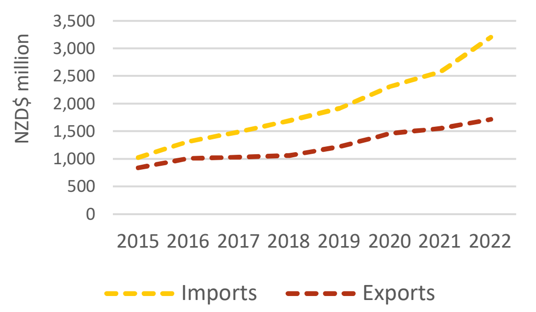


Figure 18: New Zealand trade in ICT services with the world



Source: StatsNZ data

Breaking down the category further, New Zealand exports of computer software (which includes videogames) to world markets were worth $1.1 billion in 2022, up from $0.6 billion in 2019. By contrast, exports of software to China peaked at $3 million in June 2017, and fell to a mere $0.5 million in 2019.

Chinese consumers are highly digitally-oriented and significant consumers of all kinds of "digital trade", including digitally-delivered services and interactive media (including videogames), along with physical goods ordered via e-commerce platforms such as Alibaba or JD.com. China's digital economy is booming (second only in size to that of the United States) and potentially offers an important and vibrant market for New Zealand digital services exports. The trade statistics for computer services and software are accordingly somewhat surprising.

However, China's digital regulatory environment is complex, opaque and often restrictive. In particular, there are strict rules on where data is processed and stored, including for cloud computing services, and how personal data or other "important" or "sensitive" categories of data must be managed. China has recently enacted two key legislative pieces of its comprehensive cybersecurity and data governance framework – the *Data Security Law and the Personal Information Protection*

[40] "Computer services: includes hardware and software-related services and data processing; "computer software" includes software, software development services and related licences, both downloaded and delivered via other channels, and other computer-related services.

[41] December Year figures are: $26.3 million in 2016, $23.6 million in 2017, $16.4 million in 2018, $10.7 million in 2019, $7.8 million in 2020 and $1.7 million in 2021.

Law, both of which build, and work in concert with, the *Cybersecurity Law* enacted in 2017.[42] These restrictions can affect not only cloud computing services and 'tech' companies but in fact any business that utilises data that relates to China and Chinese citizens in Mode 1 exports, for example. This necessitates businesses taking significant care in the handling of personal data, and entails additional costs in terms of setting up local data storage in order to comply with Chinese regulatory requirements for important, sensitive or personal data.[43]

Case study: RocketWerkz

Source: RocketWerkz; images from 'Icarus'

RocketWerkz founded by Dean Hall in Dunedin and now also with a studio in Auckland, is the developer of the ambitious and highly successful sci-fi survival game Icarus, which topped the global PC gaming sales charts on its launch weekend in August 2021. RocketWerkz is part of New Zealand's booming videogaming industry – a sector which has continued to see strong growth in both jobs and earnings in New Zealand despite the pandemic. New Zealand gaming revenues increased from $203 million in 2019, to $271 million in 2020 and $276 million in 2021, of which 97% is estimated to come from exports.

New Zealand games are sold around the world, with 13% of New Zealand game development studios reporting that they earn a significant portion of their income from China.[44] The global gaming market is worth $250 billion annually, and growing rapidly.

RocketWerkz has a strategic partnership with the gaming arm of Chinese tech giant Tencent – the largest gaming investor in the world. Tencent invested in RocketWerkz in 2016 and provided a second round of funding in 2019, taking Tencent's share to 47%. Chief Operating Officer Stephen Knightly describes the relationship with Tencent as "going global via China": it has helped to create a pathway to other markets around the world for RocketWerkz. The capital injection has supported scaling, including the expansion of the studio to Auckland, and product development, responding to a common challenge faced by the New Zealand tech sector in accessing venture capital. Just as importantly, the partnership with Tencent has enabled RocketWerkz to leverage Tencent's networks, market intelligence and expertise globally, including around preparing to launch into new markets, to build its business outside of China.

Tencent has a similar outlook to RocketWerkz in seeking to take a long-term view to the development of relationships, teams, talent and projects. It is an active investor in the Asia-Pacific gaming sector, and not only serves customers in China but is also engaging in more diversified markets globally. Tencent has also recently invested in other New Zealand studios including Grinding Gear Games and Digital Confectioners.

[42] MFAT (2022), 'China's Data Governance Framework takes shape: Implications for New Zealand businesses', https://www.mfat.govt.nz/en/trade/mfat-market-reports/market-reports-asia/chinas-data-governance-framework-takes-shape-implications-for-new-zealand-businesses/

[43] www.mfat.govt.nz/en/trade/mfat-market-reports/market-reports-asia/chinas-data-goveranance-framework-takes-shape-implications-for-new-zealand-businesses/

[44] New Zealand Game Developers' Association, '*NZ Interactive Games 2021 Survey Results*', 9 December 2021. https://nzgda.com/news/survey2021/; https://www.china-briefing.com/news/china-resumes-license-approval-whats-next-for-its-gaming-industry

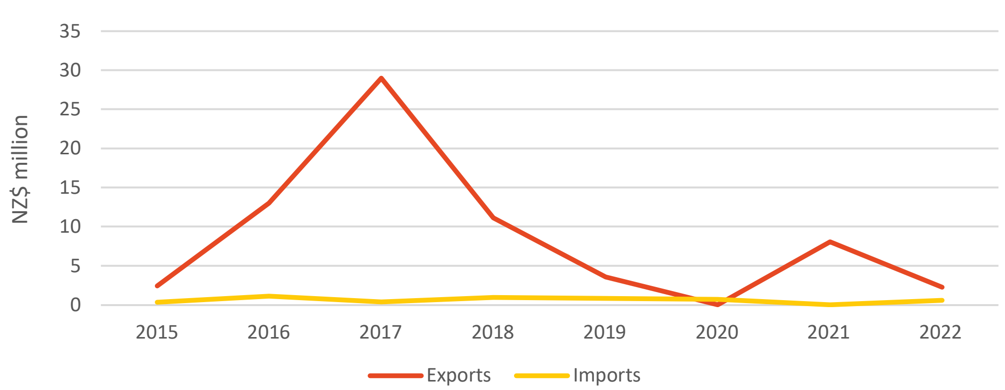
The videogaming market – the largest media sector in the world, with over 660 million consumers – is also a challenging environment. The market has had high growth although this is now slowing. In line with a general regulatory tightening in digital policies (and close regulation of a range of media including films, games and internet content), China imposes restrictions on the number of videogaming licences it issues each year. In 2021 it put in place a complete ban on new licences, although this restriction is now gradually being relaxed with a small number of approvals being granted for domestic games in 2022.[45] This has impacted the ability of New Zealand gaming studios to supply Chinese customers directly.

There is also increasing tension and fragmentation of digital regulatory approaches and technology standards, especially between China and the United States; this may also make for a more contentious business environment for New Zealand digital services exporters.[46] In short, the digital economy, while offering enormous promise as an innovative, weightless and sustainable export sector, also requires very careful navigation. It may be that many New Zealand exporters have decided that China is largely in the 'too hard basket' for now.

Personal, cultural and recreational services

The *personal, cultural and recreational* category of services includes a wide range of sub-sectors, including audio-visual services such as film and television, and other personal, cultural and recreational services. There is a lack of disaggregated data by sub-sector, but overall exports and imports were low for much of the period up to 2015 (although recall that this does not include Mode 3 exports). Exports peaked at $29 million in YE June 2017, as shown in Figure 19. However, as the case studies below show, while export returns may be low in aggregate, there are some impressive niche exporters who have been able to innovate in their offerings in response to the pandemic. The operating environment will continue to be highly disrupted in the medium term, but there is also likely be pent-up demand for many of these services when circumstances permit. New opportunities may also emerge for New Zealand exporters – for example, in response to policy support from the Chinese government for outdoor sports.[47]

Figure 19: Trade in personal, cultural and recreational services, 2015-2022 (June Years)



Source: StatsNZ data

[45] https://www.china-briefing.com/news/china-resumes-license-approval-whats-next-for-its-gaming-industry
[46] See for example, Dan Ciuriak (2022), '*Unfree flow with no trust: the implications of geoeconomics and geopolitics for data and digital trade*', Centre for International Governance Innovation, https://www.cigionline.org/articles/unfree-flow-with-no-trust-the-implications-of-geoeconomics-and-geopolitics-for-data-and-digital-trade/
[47] Mark Tanner, 'The Great Outdoors Opportunity for Brands in China', Blog on China Skinny, 16 November 2022, https://chinaskinny.com/blog/china-outdoors-opportunities

Case study: Les Mills China

Les Mills International is a global New Zealand business, providing its "life-changing fitness experiences" to customers for over 50 years. It established a wholly foreign-owned enterprise in China in 2014. Pre-pandemic, the company had been performing well, building on an increasing interest from Chinese consumers in fitness, and a low level of penetration into the Chinese "fitness population". In China, this constituted around 70 million people, or a penetration rate of about 5 percent, compared to typical penetration in the United States or United Kingdom of up to 20 percent. Les Mills at present is working with over 2,000 clubs in China, licensing its programmes for use by nearly 10,000 instructors.

However, as was the case for other retail businesses, fitness clubs were among the first to close at the start of the pandemic, and have been among the last to reopen, facing challenges including consumers' risk perceptions of working out in gyms. This daunting environment provided an opportunity for Les Mills to pivot towards the digital sphere. Initiatives have included an online training and certification programme for instructors; licensing of digital content for recorded and streamed online classes; bundled sales of equipment for use at home with streamed classes; and other more innovative projects including most recently, releasing virtual reality 'Body Combat' classes with Pico (a VR company of Bytedance, which also owns TikTok).

Although in-person fitness will remain popular, Les Mills sees online content as having huge potential in the highly digitally-oriented Chinese consumer market, offering scope to provide tailored products for travelling, schools, corporate settings and at-home exercisers, for example.

As a provider of digital content, Les Mills has had to navigate the complexities of Chinese digital regulations, including data privacy and other requirements. It wanted its system to be interoperable with its New Zealand-based parent, but also needed to ensure that it was both user-friendly for locals and complied with Chinese regulatory obligations. That has meant some back-office effort has gone into its digital systems, including setting up data warehousing in China. This had worked well to date.

Case study: Vista Group

Vista Group International designs and develops cinema management software for the global cinema exhibitor industry, straddling both the ICT sector and the screen industry: although it is a software company, in effect it relies on box office to survive. Pre-pandemic, China was the world's second-largest film market after the United States. Vista Group China, a joint venture of Vista with a Chinese partner, has been very successful in the thriving Chinese cinema sector despite a highly complex and restrictive regulatory environment.[48] Vista was able to secure one of a very few licences that are issued to enable the cinema ticketing business in 2009, and has worked with local cinema chains to build the business significantly since 2014.

With the advent of the pandemic, however, movie theatres were shut down for over seven months, and film and television production halted. Even once cinemas were allowed to reopen, consumer confidence had been severely dented and the current 'cinema experience' is highly restricted (for example, eating and drinking are not allowed). Film producers have continued to delay the release of new films. Box office returns are currently estimated at less than one-third of 2019 levels.

The future of the sector is uncertain while the Zero COVID policy remains in force. Vista Group China has sought to develop new products to help sustain the business, including new units focusing on in-cinema advertising, an online shopping mall offered to cinema loyalty members, livestreaming and NFT products.

[48] China Briefing from Dezan Shira & Associates (2022), 'Leading trends in China's Services Sector after COVID disruption', https://www.china-briefing.com/news/leading-trends-in-chinas-services-sector-after-covid-disruption/

Case study: Wētā Workshop, Pūkeko Pictures

Richard Taylor is the co-founder of the world-renowned Wētā Workshop and co-owner of television production company Pūkeko Pictures, both alongside his wife Tania Rodger. He has spent more than 20 years involved with China, forging a close, deep and mutually respectful relationship across local and central government, with business partners and manufacturing collaborators, with educational institutions including the Beijing Film Academy, and in the creative industries spanning sculpture, film and attractions.

Among other projects, Wētā Workshop has provided creative design and/or manufacturing services for two hugely successful Chinese movies, *The Wandering Earth* and *The Great Wall*, and designed the Botanical Museum of Traditional Chinese Medicine in Guangdong province, including designing the actual museum building, inspired by the image of a lotus petal alighting on water. Wētā's most recent project has been the design of a fully interactive, fantastical art installation in a giant atrium in the new Haikou International Duty Free Shopping Complex on Hainan Island, themed "the forest at the edge of the sky". As for Pūkeko Pictures, it developed the highly successful *Kiddets* children's programme in partnership with Chinese company Shambala – the first ever television co-production between a Chinese company and a foreign partner, and one which went on to inspire a children's themed play experience in Wuhan.

Reflecting on his more than two decades-long experiences in China, sparked by a childhood fascination with a book of sculptures by a Chinese artist, and involving many visits through China's varied regions, Richard noted that relationships were the bedrock of all business success there. The pandemic had made establishing and maintaining the "connective tissue" of those crucial relationships extremely difficult. The Haikou project, for example, had all been conducted via videoconference, with the myriad challenges that entailed. Building new business opportunities and achieving success in China demanded regular personal, and in-person, engagement: "You just can't do China over Zoom". Connection and respect had to come first – but, even though it could be a challenging environment, magic could be created.

Case study: Magic Memories

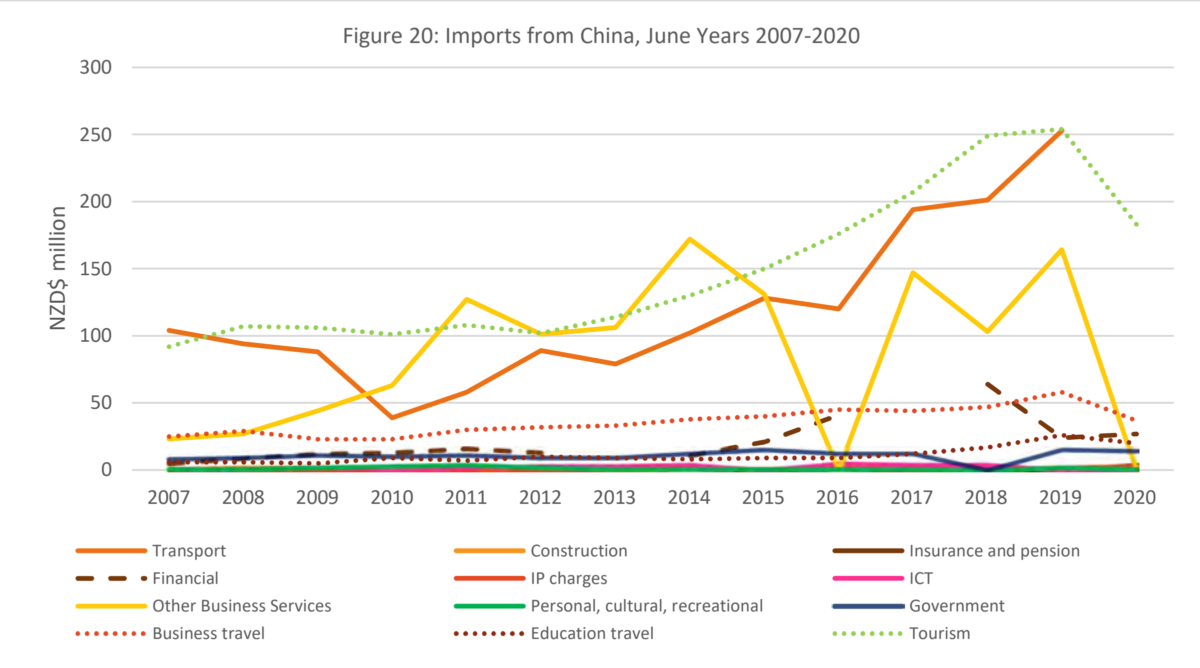
Magic Memories is a brand engagement platform partnering with more than 200 branded experiences worldwide, offering content experiences based on photographs, videos and selfies taken at attractions. In 2021, despite the challenges of the pandemic, the company expanded into China, working closely with longstanding partner Merlin Entertainments which was already operating successful attractions in the market. Magic Memories' personalised content experiences have added a new digital storytelling element to the overall customer experience and created new revenue channels. Magic Memories continues to evolve its customer-facing automated kiosks with large digital displays. This innovation responded not only to the constraints of the pandemic but also the strong digital orientation of Chinese consumers. A visitor can use their unique QR code token to access their own cloud-based 'photo album' directly from their mobile phone via a WeChat integration. What was once a traditional printed photograph has now become a multimedia product experience that guests can self-activate. Content is direct-to-mobile and able to be instantly shared on social media, including via the most common local platforms. Establishing the business in China during the pandemic was very challenging. Magic Memories set up a wholly foreign-owned legal entity and was scrupulous about compliance with local regulations, drawing on professional advice as well as strong support from New Zealand Trade and Enterprise and its business partner network. This included cloning and re-building its own digital platform in China to ensure its cloud-based system was consistent with Chinese data regulations and integrated with WeChat.

Visitation volume at attractions is significantly down, in effect putting Magic Memories' China business into something of a holding pattern for now. Executive director John Wikstrom is certain that pent-up demand will see a revival of the "industry of fun" at some point through so-called revenge travel, but it was far from clear when that would happen while the Zero COVID policy remained in place. In the meantime, Magic Memories is working tirelessly on continuing to evolve their brand engagement platform and value-add transformation in other markets.

Section Six: Imports of services from China

Figure 20 shows the trends in imports since the FTA was signed through to 2020. Over that period, China's own services sector has grown rapidly. While services represented 43 percent of China's GDP in 2009, by 2019, this had expanded to 54 percent of GDP, accounting for nearly 60 percent of China's total growth.[49] China is a substantial global exporter of services, contributing nearly 6 percent of global services exports, notably in transport, goods-related services, travel, 'other business services', ICT services and construction.[50] In 2021, according to Chinese Ministry of Commerce figures, China's services trade expanded by 16 percent year-on-year, with exports up 31 percent year-on-year, including strong growth in transport services and knowledge-intensive services exports.[51]

However, as Figure 21 shows, this performance is not strongly reflected in the trade relationship with New Zealand: imports from China are at a significantly lower level than New Zealand exports, rising to a peak of $832 million by YE June 2022 – significantly below the New Zealand services export peak of $3.4 billion in 2019. There is clearly significant unrealised potential for Chinese exports of services to New Zealand, including those that can support enhanced efficiency and productivity of New Zealand businesses and New Zealand goods trade such as 'other business services', financial services, transport and ICT services, as well as infrastructure services such as construction.



Source: StatsNZ data

As Figure 21 shows, immediately prior to the pandemic, transport and travel dominated imports from China, reflecting both goods trade as well as the education, tourism and business travel flows between the two markets. The services that support the broader trade and business relationship (including trade-related services, professional services such as legal services, and government services) were also notable. However there were few imports from other sectors.

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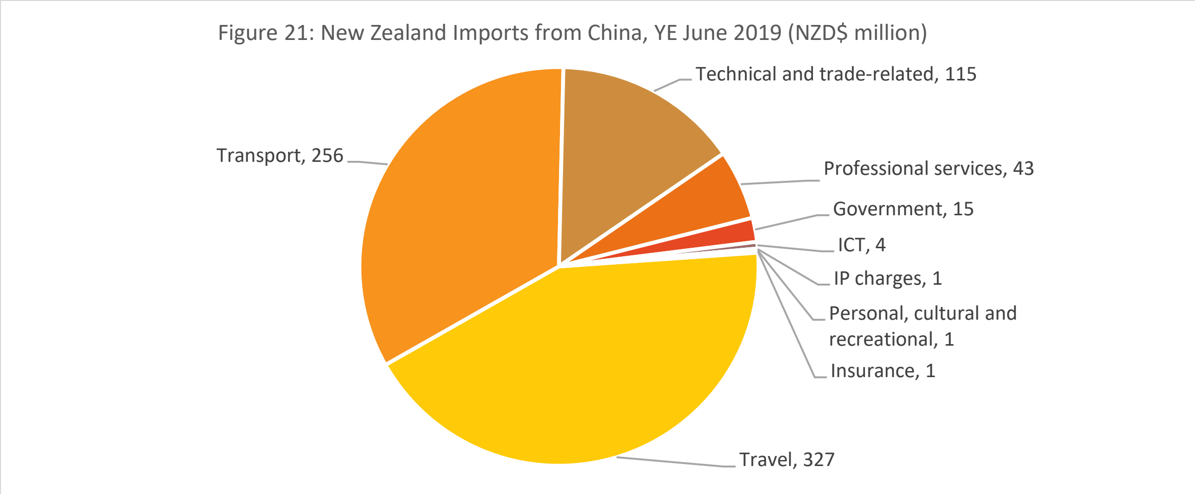
[49] China Briefing from Dezan Shira & Associates (2022), 'Leading trends in China's Services Sector after COVID disruption', https://www.china-briefing.com/news/leading-trends-in-chinas-services-sector-after-covid-disruption/

[50] WTO (2022), *World Trade Profiles 2021*, page 81, https://www.wto.org/english/res_e/booksp_e/trade_profiles21_e.pdf

[51] CGTN, 'China's service trade up 16.1 percent in 2021', https://news.cgtn.com/news/2022-01-31/China-s-service-trade-up-16-1-percent-in-2021-17giC6fwZuo/index.html



Source: StatsNZ data

Section Seven: Services trade and Inclusion

Services trade is often identified in trade policy literature as providing important trade opportunities for disadvantaged groups or those with unrealised economic potential, including women and Indigenous businesses. The nature of services trade – particularly digitally-delivered services – can enable faster and lower-cost reach and scale in global markets. Critically, services trade can also help such exporters circumvent some existing cultural biases and structural impediments, for example around financing or access to information and technical skills, that they otherwise typically face.

The participation of Māori enterprises and women entrepreneurs in services trade with China is difficult to measure due to gaps in sourcing and disaggregating the data. However, there are some strong performers in key tourism and education sectors. A report from New Zealand Māori Tourism identified 537 Māori tourism businesses, including 300 involved in accommodation and food sector, 141 in the arts and recreation sector, and 96 in other tourism industries, including transport services, motor and equipment rental and travel agency.[52] A recent report commissioned by Te Puni Kōkiri, '*Te Matapaeroa*', finds that almost 40 percent of Māori-owned businesses have women owners.[53] The case study on Ngāi Tahu Tourism is an example of a highly successful iwi-led model.

There are also some notable Māori- and women-led niche exporters, including in audio-visual services, design and videogaming, as well as other digitally-delivered services. However there is little detailed data available on the engagement of these businesses with the China market.

Section Eight: Future prospects and navigating uncertain times

The period ahead is likely to be challenging for New Zealand exporters, with many potential downside risks alongside new opportunities, pointing to the need for businesses to keep a close watch on the evolving picture and prioritise agility in their operating models. New Zealand government agencies can also continue to play a valuable role in raising awareness among businesses of the regulatory and business environment in China and deepening cooperation with Chinese counterparts, building on the strong foundation of the upgraded FTA.

[52] New Zealand Māori Tourism Annual Report 2020,

[53] Te Puni Kōkiri (2022), *'Te Matapaeroa 2020'*, https://www.tpk.govt.nz/en/o-matou-mohiotanga/maori-enterprise/te-matapaeroa-2020

In particular, COVID-19 disruptions are likely to continue, at least in the short- to medium term. Inevitably, this will continue to affect both transport and travel, and accordingly New Zealand's two largest services export sectors, tourism and education, as well as New Zealand providers of transport services and potentially also indirect impacts on goods trade.

As the paper discusses, there is currently an important window to consider how best to position New Zealand tourism and education exports to respond to evolving consumer preferences and perceptions once travel resumes more strongly, as well as seeking to maximise the 'enabling environment' created by policy settings in both New Zealand and China. It would seem wise not to assume that the future environment and appetite for these services will look the same as it did in 2019, for the range of reasons discussed in the report.

Equally important will be the dynamism of the passenger transport sector, with air connectivity (capacity, frequency, routing and cost) all having an impact on the uptake of Mode 2 services as well as airfreight for goods exports, as the Air New Zealand case study discusses. More broadly, it is clear that strengthening people-to-people links, including resuming business travel, will continue to be a key enabler of the services trade relationship, even when innovative technologies can achieve substantial connectivity. As a number of exporters commented in our interviews, with China, the relationship comes first, and business, second.

Besides tourism and education, China's continuing Zero COVID policy may also have a dampening effect on the consumption of other services involving person-to-person proximity in-market, such as personal, recreational and other services. As the case studies on Magic Memories, Vista Group China and Les Mills show, businesses have been able to respond to the current disruptions with creative thinking about innovations in the way that they deliver services, and the types of services that they offer, but it is clear that the environment will remain highly challenging. That said, there may continue to be niche opportunities, including to respond to pent-up demand for such services.

As much as the restrictions themselves, the continued uncertainty around pandemic impacts and responses seems likely to affect business planning and investment. This may compound the impact of the expected slowdown in the Chinese economy. The 2022 forecast is for GDP growth of only 2.8 percent, rebounding somewhat to 4.5 percent in 2023, a sharp deceleration from the 8.1 percent growth of 2021.[54] This may reduce demand for the backbone services that support broader business and investment activity, such as legal and financial services, as well as some high-end consumer services.

China remains focused on a 'dual circulation' economic policy, placing more emphasis on the domestic market and internal circulation while remaining open to the outside world. There is also growing confidence and patriotic pride in China's domestic services, including, for example, its own high-quality education. The latter may ultimately be reflected in consumer choices about preferring to study at home, rather than offshore – but may equally create new opportunities for New Zealand exporters to provide more education services in-market, including through partnership models.

In that regard, the Upgraded FTA commitments enabling delivery of services in China through local commercial presence – either in partnership with Chinese businesses, or through wholly foreign-owned entities – should help to provide a good foundation for growing trade flows. Anecdotally, exporters see partnerships, joint ventures and other cooperative models as an important way to leverage the regulatory expertise and networks of local partners to achieve greater success.

[54] World Bank (2022), 'Reforms for Recovery: East Asia and Pacific Economic Update, October 2022

The opening up of new services market access opportunities and improvements to existing commitments under the bilateral FTA may also create niche opportunities for New Zealand exporters across a range of sectors, spanning from translation services to environmental services, to sound recording to air transport services.

These commitments may also bolster existing trade. For example, airport operations and specialty air services can help to support tourism, education and airfreight goods exports; new commitments on sound recording distribution services can help to grow existing creative economy exports including from the screen and recording industries; improved commitments on non-academic education may provide opportunities for the vocational sector to broaden its in-market offering. The ability to provide 'bundled' (embedded and embodied) services with goods exports may also represent a hidden growth opportunity for New Zealand technical and knowledge-intensive services suppliers.

The pandemic has shown that digital delivery of services offers important opportunities for exporters, including for innovative new approaches to existing trade, for example for online delivery of education. However, it is by no means certain that China's current flexibility in permitting online delivery will continue – advocacy from the sector and the government for continuing flexibility in accepting digital delivery may be helpful.

For all businesses, China's complex and often restrictive digital economy regulations will require careful approaches to designing business models, including in relation to the use of some platforms and apps, and also close attention to the handling of data. Increasing use of digital delivery will also increase the need for careful protection of intellectual property in online settings. For the longer term, China's application to join the Digital Economy Partnership Agreement, which includes a more liberal approach to data regulation as well as creating a cooperative platform for the development of more agile and responsive digital regulation in other areas, may offer a path to a more business-friendly and predictable regulatory environment for digital trade.

Lastly, the importance of regulation as an enabler of (or barrier to) trade in services means that cooperation and confidence-building on domestic regulatory measures will remain a critical means to grow services trade and to shore up the resilience of existing exports, building on the foundation laid by the original and now upgraded FTA. Those we interviewed warmly welcomed the strong support from government agencies, including the Ministry of Foreign Affairs and Trade, New Zealand Trade and Enterprise, Education New Zealand and Tourism New Zealand. There is likely to be a continuing role for agencies and regulators to deepen confidence and mutual understanding with Chinese counterparts and work to create a more business-friendly regulatory environment where possible – including, for example, pressing ahead to implement the FTA undertaking for both sides to work together on quality assurance for international education.

ANNEX I: SERVICES TRADE RULES AND TRADE BARRIERS

Trade rules for services are commonly set out in trade agreements, such as the New Zealand-China FTA, or in countries' World Trade Organization commitments ("Schedules"). Trading partners make detailed market access commitments by 'mode of supply'. There are four modes, as summarised at pp.6-7 above.

These commitments by mode are made across the different services sectors (for example, education) or sub-sectors (for example, higher education). FTAs often deal with Mode 4 separately (in a chapter on Movement of Natural Persons), and sometimes also include separate chapters on financial services and electronic commerce.

These commitments are not always a good fit with business models, however. For example, a business may set up a local presence (Mode 3), but may also want to send in specialist staff temporarily (Mode 4). Or, while most of the services may be delivered through provision in the exporting country (Mode 2), the exporter may also want to include an online component delivered in the consumer's home market (Mode 1). FTA rules may not always include enabling rules across all of these modes, meaning that there is a mismatch with business operations.

Governments use regulations and administrative measures to govern services trade, rather than the tariffs that are typical of goods trade. These regulations can be highly restrictive, for example either prohibiting trade or investment, or imposing stringent conditions on exporters, including in relation to the types of services that can be supplied, how they can be supplied, geographically restricting where services can be supplied, or even the clients to which they can be supplied. There may be limitations in relation to entering the market, and how services exporters are treated relative to local firms.

Table 1: Modes of Supply and Trade Barriers

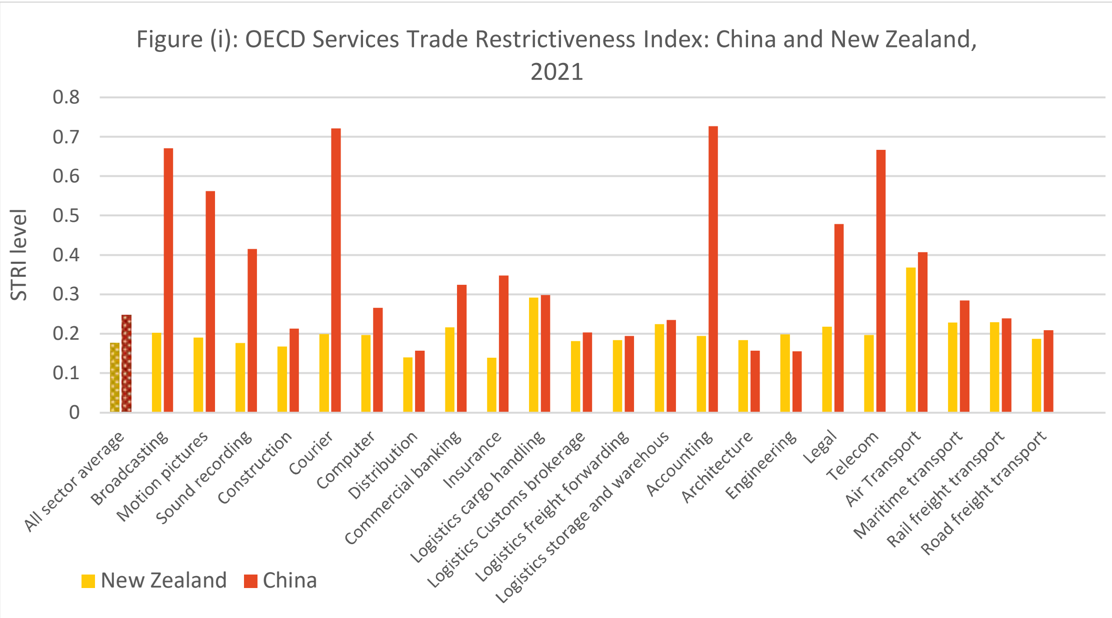
Mode	Typical trade barrier	Example
Mode 1 Cross-border supply	May include a requirement to establish a commercial presence in-market May include restrictions on digital delivery	Only mail order retailing services are permitted No online education delivery is permitted
Mode 2 Consumption abroad	Typically few barriers/restrictions	Mode 2 brokerage services are not permitted
Mode 3 Commercial presence	Typically many barriers, including requirements around corporate structures (e.g. only joint ventures are permitted), foreign equity limits, nationality requirements for staff or managers, and restrictions on the type or number of services that can be offered	Foreign law firms can only provide legal services in 19 specific cities; can only provide consultancy on the foreign jurisdiction's laws; representatives must have practiced for at least two years outside China. Only joint ventures are permitted for construction services
Mode 4 Presence of natural persons	There may be challenges in securing visas. Discriminatory licensing or lack of mutual recognition of qualifications may also be significant impediments	Visa processes may be slow or expensive, or may include labour market testing or economic needs testing

These restrictions can be accompanied by other measures that further limit the ability of exporters to supply services in the market, for example through narrow licensing requirements or a lack of recognition of professional qualifications. In addition, regulations are often focused on the domestic business environment in the importing market, rather than being specifically aimed at trade, which can make it difficult for exporters to identify the specific requirements that affect their businesses.

Globally, trade costs for services are still almost double the trade costs for goods, although they are dropping thanks to the combined impact of digitalisation, services trade reform and infrastructure improvements.[55] The OECD Services Trade Restrictiveness Index (STRI) measures how restrictive the regulatory environment is for services trade across a range of countries. As Figure (i) shows, China has an STRI value of 0.247 (in a range of zero to one, with one being the most restrictive). This is higher than the OECD average of around 0.2, and notably higher than New Zealand's STRI of 0.177.[56]

Some sectors are even higher than this average, including broadcasting, motion picture services and sound recording; courier services; banking and insurance; accounting and some legal services; some telecommunications and computer services, and air transport. Trade and investment in these sectors are prohibited or subject to stringent entry conditions; there are also economy-wide regulations including labour market tests for intra-corporate transferees (Mode 4) and for other services suppliers, explicit preferences for local suppliers in public procurement, and hurdles on digital trade (see below).

The sector with the highest scores relative to the average STRI across all countries include courier services, telecommunications and accounting. A number of these sectors involve key strategic or enabling services that support broader business and trade activities, and overarch the entire economy. In short, without an FTA, exporters would face potentially significant barriers in many key sectors in the Chinese market.



Source: OECD, Services Trade Restrictiveness Index, https://stats.oecd.org/Index.aspx?DataSetCode=STRI

China recorded significant decreases in its STRI between 2014 and 2021 as a result of progressive liberalisation of regulations governing foreign direct investment in particular.[57] A number of the new commitments in the upgraded New Zealand-China FTA reflect this liberalisation trend. For example,

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[55] WTO (2019), *World Trade Report 2019: The future of services trade*, https://www.wto.org/english/res_e/booksp_e/00_wtr19_e.pdf; and OECD (2022), '*OECD Services Trade Restrictiveness Index: Policy Trends up to 2022*', February 2022,

[56] OECD, *Services Trade Restrictiveness Index*, https://stats.oecd.org/Index.aspx?DataSetCode=STRI, accessed 20 November 2022. The STRI database covers the 38 OECD countries, plus Brazil, China, India, Indonesia, Kazakhstan, Malaysia, Peru, Russia, Singapore, South Africa and Viet Nam.

[57] OECD (2022), 'OECD Services Trade Restrictiveness Index; China – 2021', https://www.oecd.org/trade/topics/services-trade/documents/oecd-stri-country-note-chn.pdf

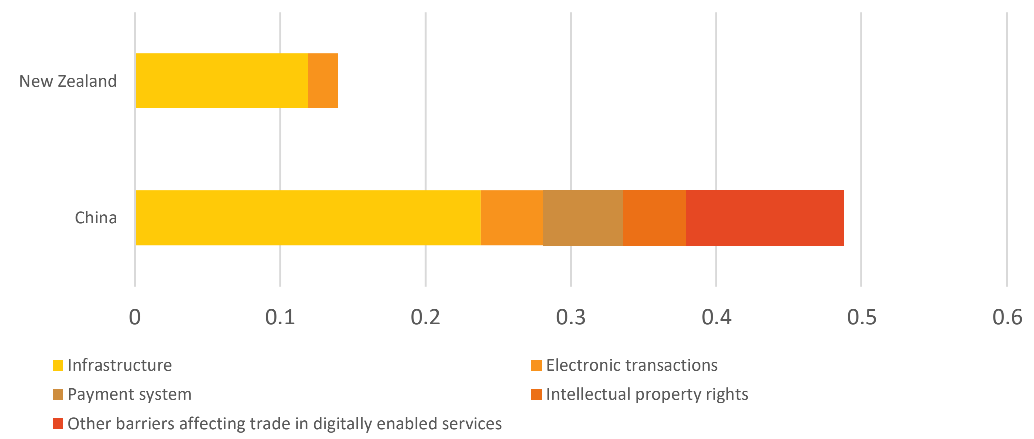
whereas previously New Zealand firms were typically required establish a local presence in the market in order to deliver services, or to establish a joint venture (with strict equity limits) with a local Chinese partner in order to deliver Mode 3 services, under the FTA Upgrade, in many sectors exporters can now establish a presence in the market through a wholly foreign-owned entity (see the next Annex).

Digital economy regulation

In the last few years, China has introduced a range of new laws, regulations and administrative measures relating to the digital economy, including the *Data Security Law*, the *Personal Information Protection Law,* and the *Cybersecurity Law*. These three laws establish a framework for rules for managing and storing different kinds of data, including for foreign entities operating in China (with much of the detail still to be determined in implementing rules, regulations and other measures still to be developed). These regulations may affect any New Zealand companies that handle data relating to China and Chinese citizens, including Mode 1 exports, requiring exporters to put in place specific procedures relating to the processing, storage or conditions around the flow of data out of China.[58]

The position of China in the OECD's Digital Services Trade Restrictiveness Index reflects these policy developments: China's DSTRI is 0.488, where New Zealand's DSTRI is 0.14; the average across all 44 countries in the Index is likewise around 0.14.[59] As Figure (ii) shows, China's regulatory environment is particularly restrictive in relation to infrastructure and connectivity (essential to engaging in digital trade), payment systems, and also the category of 'other barriers affecting trade in digitally enabled services', which covers elements such as mandatory technology transfers, limitations on downloading and streaming, restrictions on online advertising, commercial presence requirements and others.

Figure (ii): OECD Digital STRI for China and New Zealand, 2021



Source: OECD, Digital Services Trade Restrictiveness Index, https://stats.oecd.org/Index.aspx?DataSetCode=STRI_DIGITAL

Measuring "digital services trade"

[58] MFAT (2022), 'China's Data Governance Framework takes shape: Implications for New Zealand businesses', https://www.mfat.govt.nz/en/trade/mfat-market-reports/market-reports-asia/chinas-data-governance-framework-takes-shape-implications-for-new-zealand-businesses/
[59] OECD (2019), '*The OECD Digital Services Trade Restrictiveness Index*', OECD Trade Policy Papers, No. 221, https://www.oecd-ilibrary.org/trade/the-oecd-digital-services-trade-restrictiveness-index_16ed2d78-en; and https://qdd.oecd.org/subject.aspx?Subject=STRI_DIGITAL

There is no single agreed international definition of "digital trade", although there has been valuable work on this by international institutions in recent years.[60] Some services are explicitly related to the digital economy, such as computer services and software development, and 'charges on the use of intellectual property', which includes software licensing. Many services can now be digitally delivered, including those from more traditional sectors such as financial services, professional services and even education. Moreover, a range of more innovative, high-value digital services do not always fit neatly within existing services trade categories, such as those provided by digital intermediation platforms such as e-commerce sites and sharing platforms (for example, Alibaba and Tencent).[61]

[60] The Organisation for Economic Cooperation and Development (OECD), World Trade Organization (WTO) and International Monetary Fund (IMF) have developed a *Handbook on Measuring Digital Trade*, which defines digital trade as "all trade that is digitally ordered and/or digitally delivered".

[61] OECD, WTO and IMF (2020), *Handbook on Measuring Digital Trade*, pages 13-14. The services that can be digitally delivered or "ICT-enabled" include insurance and pension services, financial services, charges for the use of intellectual property, research and development, professional and management consulting services, architecture, engineering, scientific and other technical services, 'other business services', audiovisual and related services, health services, education services and heritage and recreation services.

ANNEX II: SUMMARY OF NEW ZEALAND-CHINA FTA SERVICES OUTCOMES

The New Zealand-China Free Trade Agreement (FTA) that was signed in 2008, and the Upgrade that was signed in 2022, established some important frameworks for enhanced services trade. Below is a summary of outcomes. (Note that this is intended for general information only, not for business use; does not constitute legal or business advice; and reference back to the legal text of the agreement is strongly advised.)

China's 2008 FTA commitments went further than those it had made in the WTO in respect of:

- Computer and related services – including software implementation services, data processing services, and input preparation services;
- Services related to management consulting;
- Education – a binding commitment to keep names of key New Zealand educational institutions on the China Ministry of Education 'Study Abroad' website, and a commitment to initiate joint work on quality assurance criteria for qualifications which include a distance delivery component; [62]
- Environmental services – an improved Mode 3 commitment on environmental services permitting wholly foreign-owned enterprises;
- Sporting and other recreational services;
- Air transport services: aircraft repair and maintenance services, and air travel computer reservation services; and
- Road transport services – freight transportation by road in trucks or cars; maintenance and repair of motor vehicles; storage and warehousing services; and freight forwarding agency services.

The above are subject to specific reservations or exemptions listed in China's schedule. In effect, New Zealand services suppliers were able to access the Chinese market without quotas and operate on the same footing as domestic Chinese services suppliers.

For its part, New Zealand committed to provide market access and national treatment in services sectors where FTA commitments went beyond New Zealand's WTO commitments. Commitments on the temporary entry of Chinese business visitors went beyond New Zealand's WTO commitments. New Zealand also committed to temporary employment entry of specific skilled workers.

The FTA also includes a reciprocal 'Most Favoured Nation' (MFN) provision. This means that any better treatment relating to services that China extends to third countries must also be extended to New Zealand (and vice versa). China's MFN obligations to New Zealand cover construction; environmental services; services incidental to agriculture and forestry (China entered a reservation against its commitment to this sector to the effect that it applies only to agreements that China concludes with OECD countries); engineering services; integrated engineering services; computer and related services, and tourism services.

The FTA also enables each side to preserve important areas of "policy space". In both cases, there are areas of sensitivity in particular sectors, modes or other aspects of services delivery, which each side has been able to exclude from FTA coverage. In addition the FTA includes 'general exceptions' to ensure that the Agreement does not impair the ability of either side to regulate for legitimate public

[62] The institutions include the eight New Zealand universities, the (then) Institutes of Technology and Polytechnics, Te Wananga o Aotearoa, Te Whare Wananga o Awanuiarangi, Te Wananga o Raukawa, and six degree-conferring private training establishments.

policy reasons. The FTA also includes the specific provision found in all New Zealand trade agreements which preserves the preeminence of the Treaty of Waitangi.

The 2022 Upgrade to the 2008 FTA builds on those original commitments to add in:

- New market access commitments in 22 sectors, including market access commitments in environmental services (nature and landscape protection and other environmental protection services), airport operation services, selling and marketing of air transport services, speciality air services, ground-handling services, and sound recording distribution services.
- Improvements in the existing 2008 commitments for 17 sectors including expanded access for real estate services, translation and interpretation services, "other" education services (non-academic training in English language, cooking and handicrafts), advertising, sport and recreation services and a number of other areas. In many cases, these improvements include the ability to operate wholly foreign-owned entities in China to deliver Mode 3 services in-market.
- The provisions on recognition of professional qualifications have been updated to recognise the work that has been done since the existing FTA was concluded and to recognise the need for further cooperation in this area between New Zealand and Chinese relevant authorities.
- MFN applies in relation to a range of new services, including private education and architecture.

New Zealand and China also agreed in the 2022 Upgrade to start negotiation on a new services framework within the next two years, which would provide scope for further opening up of the market through the use of a 'negative list' approach. Under such an approach, the Parties commit to providing market access except in areas where restrictions are listed. This will make it more straightforward for exporters to determine whether commitments apply to their area of business in China's market.

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