

Australia's Approach toward APEC and Japan's Response

By Okamoto Jiro

When Bob Hawke, former prime minister of Australia, visited South Korea in January 1989, he proposed the creation of an intergovernmental forum within the Asia-Pacific region to discuss economic cooperation, a proposal which culminated in the establishment of APEC.

During the period from January to December 1989, when the inaugural ministerial meeting of APEC took place in Canberra, the Australian government, in particular the Department of Foreign Affairs and Trade, worked tirelessly to promote the idea and persuade would-be members to join the new organization, not an easy task as some ASEAN countries were concerned that the new organization might threaten ASEAN's existence.

The Australian government dispatched the foreign minister and several high-level department officials to members of ASEAN to assure them: that APEC, if established, would be a forum consisting of countries with different social and political systems and levels of economic development; that APEC would not devalue the meaning of any regional organization already in existence in the area; and that any APEC decision would be made on a consensus basis. It was not by accident that the principles of APEC activities confirmed at the first ministerial meeting included each of these accords.

It is clear that Australia was the motor force behind the creation of APEC. It also seems that, after its establishment, Australia has been trying to lead the process as much as it can. In April 1992, Prime Minister Paul Keating revealed his idea of establishing a leaders' meeting within the APEC framework. Although the other members were not at first particularly interested, an unofficial leaders' meeting took place about one and half years later in Seattle, thanks to an initiative from U.S. President Bill Clinton.

This year, Australia has again been



Canberra, the capital of Australia, where the first APEC meeting was held in 1989.

active in promoting the Bogor Declaration of November 1994 which set target dates for completing trade and investment liberalization in the region. Foreign Minister Gareth Evans visited Malaysia in February to discuss the matter with Prime Minister Mahathir, and Keating visited Japan, the host nation of this year's ministerial and leaders' meeting, in May to exchange opinions. In this short article, I would like to analyze, briefly, the reasons behind Australia's approach to APEC trade and investment liberalization. Following that, I will discuss how Japan can and should respond to Australia's approach from a multilateral and a regional perspective.

Why Australia needs liberalization

To understand why the government is expecting positive results from trade and investment liberalization, Australia's history regarding protection-

ism and the drastic policy changes which have been implemented since the 1980s need to be reviewed.

From Federation in 1901 until the 1970s, the Australian government enacted policies which protected domestic industries. The exceptions were the mining and agriculture sectors which were internationally competitive from an early stage.

Before Federation, Australia was divided into six autonomous dominions. To create a nation state in a short period of time, the federal government needed a set of policies and goals which most citizens could agree with, and "protection of normal citizens' lives" became its objective. Several principal policies were implemented to realize this goal, including sustenance and improvement of individual income levels by restrictive immigration policies; protection of domestic industries through tariffs and quantitative restrictions on imports; and, arbitration of industrial disputes and wages.

The tendency toward protectionism went further when World War I broke out. Imports of manufactured goods from the United Kingdom, the biggest trading partner by far at the time, were reduced significantly and the government promoted "import substitution." By the mid-1920s, Australia had one of the highest levels of tariffs on manufactured goods. Under this protective umbrella, domestic industries such as textiles, cloth, footwear, food processing, electrical appliances and steel developed and increased production. The costs of protection, of course, were financed by the competitive mining and agriculture sectors.

The Australian manufacturing industry has always relied on foreign capital: manufacturers, denied access to the Australian market by protectionist measures, invested in Australia to gain access to the domestic market. The resulting manufacturing industry tended to produce goods solely for the domestic market, resulting in few incentives for R&D and expansion into foreign markets. This economic structure remained unchanged until the 1980s.

Domestic opinion against protectionism grew after World War II, especially among academics. However, it was not until the late 1960s that the first moves to reduce tariffs were made. In 1967 the Tariff Board, established in 1921 and a useful instrument in aiding governmental decisions on the level of protection afforded each manufacturing sector, voluntarily reviewed every tariff placed on manufactured goods to identify excessively protected goods and industries and advised tariff reductions. However, the beneficiaries of this traditional protection practice, such as industries, trade unions and some parts of the government bureaucracy, were simply not ready to accept this recommendation.

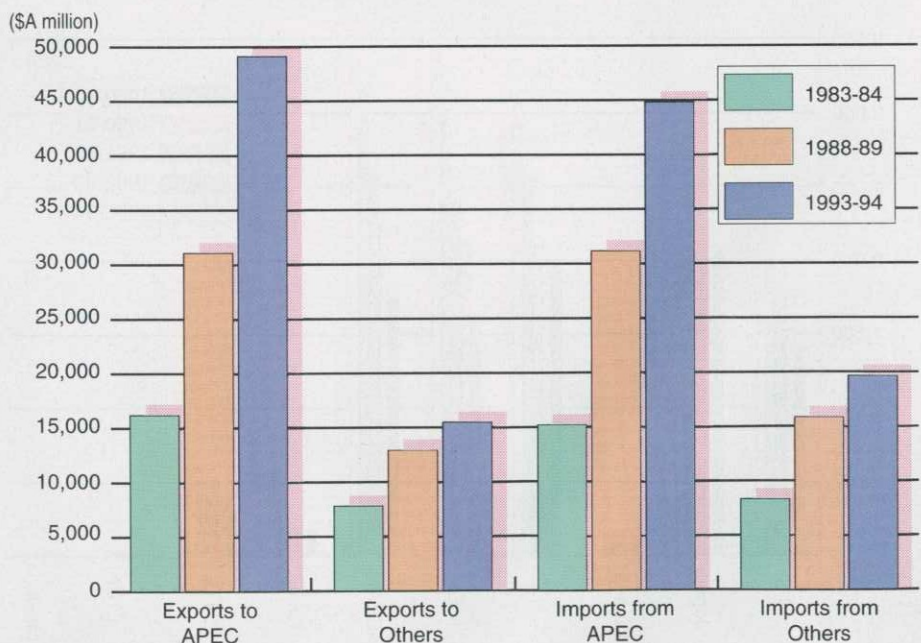
The Whitlam Labor government, elected in 1973, reorganized the Tariff Board into the Industries Assistance Commission, with the new role of advising the government on how resources should be distributed efficiently to benefit both producers and consumers. During the commodity "boom" period

of the early 1970s, Australia's current account recorded a substantial surplus and by 1974 the Australian currency had appreciated 18% against the U.S. dollar. The government reduced tariff rates across the board by 25% in July 1974, and devalued the currency by 12% to ease growing inflationary pressure. On the domestic front, the government abolished the wage indexation system and repressed investment and consumption through high interest rates. Thus, the first substantive move to reduce protection of the manufacturing industry arose as a means to counter inflation.

However, following the first oil crisis in the mid-1970s, Australia's main trading partners—the United States, Japan and the EC—experienced an economic recession and Australia's export earnings were considerably reduced. That led Australia into a recession in which it remained for the rest of the 1970s. The move to reduce protection by lowering tariffs ended, at least for a while, due to strong opposition from traditional interest groups.

Following a brief recovery period in the early 1980s, Australia's terms of trade deteriorated and its economy was once again in recession. This time the Hawke Government, elected in 1983, realized that Australia could no longer sustain its traditional economic structure of financing protectionism with earnings from mining and agricultural exports. Drastic liberalization and privatization reforms began. First, the government opted for monetary reform. In 1983, it floated the currency exchange rate, deregulated interest rates and allowed the entry of foreign banks into the domestic market. As a result, the Australian dollar depreciated 24% during the period from 1980 to 1988. The government expected that the depreciation of the dollar would lead industries to gain price competitiveness and exports would increase. The increased export earnings would improve the current account deficit and reduce foreign debt. However, this did not happen immediately. The current account deficit hit 4.5% of the GDP in 1986.

Figure 1: Australia's Merchandise Trade



Source: *The APEC Region Trade and Investment: Australian Supplement*, Department of Foreign Affairs and Trade, November 1994

The next step was to make domestic manufacturing industries efficient and competitive in the world market. The federal and state governments promoted investment in selected industries, such as mineral resource processing, communications, computers, biotechnology, and energy development. Plans for privatization of industries which were formerly dominated by state enterprises, such as aviation (domestic and international), banking and telecommunications, were announced. Furthermore, in 1989, the government announced a concrete schedule of reducing tariffs. According to the schedule, all tariff rates, except on automobiles, automobile parts, textiles, clothing and footwear (TCF), are to be reduced to 5% by 1996; for TCF, tariff rates are to be lowered to 25% by 2000; for automobile and auto parts, to 15% by 2000; and, the average nominal rate of assistance will be lowered to 3% and the average real rate of assistance to 5%

by the same year.

The economic reforms begun in the 1980s were the first and most significant redirection of economic policies for the Australian economy since Federation. It is not hard to imagine that changing policies that were kept almost untouched for more than 70 years is a very difficult task. However, ongoing reform has been a long-pending question and it seems that the government will not retreat this time.

The continued success of the policies to adjust Australia's domestic economic structure depend, in part, on the maintenance of the global free trading system. Australia's domestic market is still too small to sustain the high standard of living which was already achieved, even if the domestic manufacturing industry gained competitiveness in the near future and substituted imports as planned. It is vital for Australia that the newly competitive goods and services,

in addition to its traditional exports, are guaranteed free trade across borders. However, the prospect of maintaining a free trade system appeared to decline during the 1980s. The Uruguay Round was deadlocked, the United States and Canada, then Mexico, formed a free trade area and the EC created a single market and became the EU. The moves to form potentially protectionist regional free trade areas naturally drew Australia to involve itself actively in the effort of maintaining free trade. Two of its most significant activities have been the development of APEC and the Cairns Group of agricultural free traders.

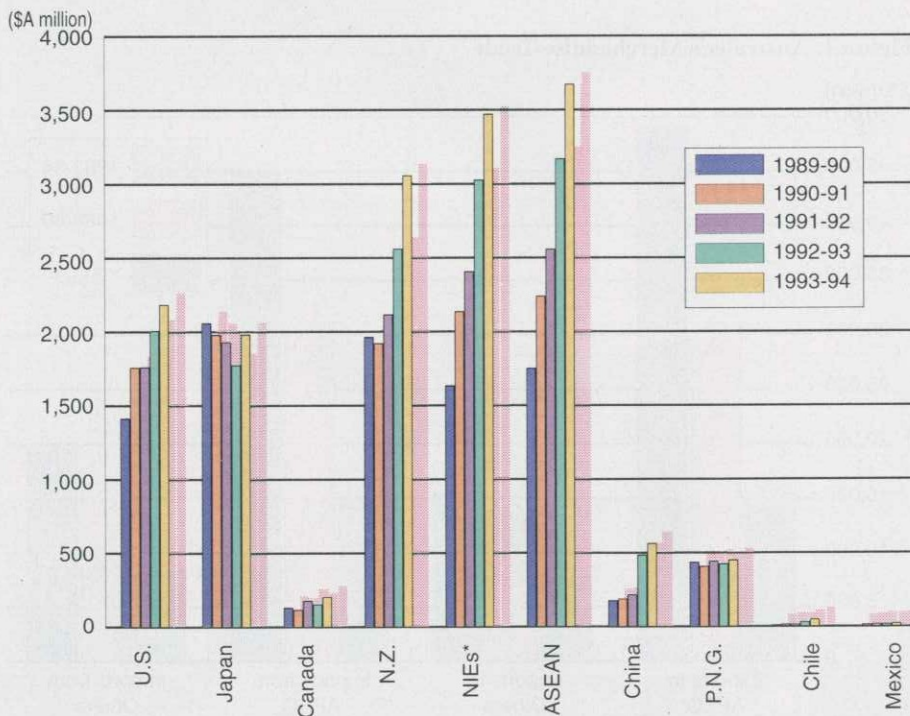
A shift in emphasis

Australia's basic stance on international trade now is to respect the GATT/WTO principles of multilateral free trade and most-favored nation (MFN) treatment. It also proposed the creation of APEC and promoted this process as a way to reinforce the Uruguay Round which was going nowhere at the time. APEC was also seen as a way to counter protectionist tendencies in North America and Europe.

For Australia, there were two primary reasons why it had to be APEC that promoted freer trade and investment. First, Australia, even if it wanted, had no chance of joining NAFTA or the EU. Second, Asian economies became increasingly important as trade partners. Until the 1960s, Australia's main trading partner had been the United Kingdom, followed by the United States and other European countries. However, Japan emerged as the largest export destination in the latter half of the 1960s and has remained so ever since. Following Japan's track, Hong Kong, South Korea, Singapore and Taiwan started their rapid industrialization and economic growth, absorbing imports from Australia. More recently, the ASEAN countries have followed a similar path.

Figure 1 shows the trend of merchandise trade in the last decade. In 1983-84, exports to APEC nations already amounted to 67.5% of the total exports, and imports held 64.6% of the total.

Figure 2: Australia's Manufacturing Exports to APEC Economies



*Hong Kong, South Korea, and Taiwan

Source: *The APEC Region Trade and Investment: Australian Supplement*, Department of Foreign Affairs and Trade, November 1994

These figures increased to 76% for exports and 69.5% for imports in 10 years. Both Australia's exports and imports to/from APEC tripled in the same period. Moreover, Australia enjoys a trade surplus with most of APEC, except the United States. In 1993-94, Australia recorded a trade surplus with Japan, New Zealand, NIEs and ASEAN of \$A11,308 million, more than offsetting the trade deficit of \$A9,170 million with the United States. The importance of the APEC economies for Australia is the same for services trade. In 1992-93, Australia's exports of services reached 66% of total exports; imports reached 52% of total imports.

More importantly for the Australian government, the domestic manufacturing industry increased in competitiveness. Figure 2 shows Australia's manufacturing exports to APEC economies for the last five years. The figure indicates the importance of the United States, Japan, New Zealand, the NIEs and ASEAN as export destinations. However, it seems that the United States and Japan have stagnated in comparison to the growing markets of New Zealand, the NIEs and ASEAN. Though the United States and Japan remain important markets, exports to New Zealand, the NIEs and ASEAN grew 56%, 113% and 110% respectively during the last five years. China looks like another promising destination for Australia's manufactured exports if its "open policy" is maintained. In 1993-94, the value of exports to China was just over \$A500 million, but its growth rate in the last several years has been significant.

In summary, the economic transactions of Australia with the Asia-Pacific region, especially with the Northeast and Southeast Asian economies, has grown dramatically since the 1960s. To underpin ongoing domestic economic reform and resulting export growth, Australia needs to promote and help maintain free trade and investment. Though the countries in the region, with the exception of NAFTA, have been liberalizing their economies unilaterally and voluntarily, APEC can promote the

region-wide goal of trade and investment liberalization. At the moment, the Australia-New Zealand Closer Economic Relations Agreement (CER) is the only comprehensive free trade agreement that Australia has made. It is obvious that the CER alone does not fulfill Australia's needs. Thus, the recent tendency for APEC to become more than a communications forum—the creation of the "unofficial" but annual leaders' meetings and the Bogor Declaration which set target years for regional trade and investment liberalization—is very welcome to the Australian government.

Furthermore, APEC is a convenient vehicle to tie members together. As mentioned earlier, Australia's main economic transaction partners are located on both sides of the Pacific. Australia cannot afford to have North America and Northeast and Southeast Asia divided as economic blocs. APEC provides a great opportunity to promote economic liberalization and unite members into one region at the same time.

Communication and cooperation needed

How can and should Japan respond to the Australian approach towards APEC? To jump to the conclusion, Japan can cooperate with Australia in the APEC process because they have similar interests in the region. North America and Northeast and Southeast Asia are very important trade and investment partners for both countries. Japan would also be significantly disadvantaged if the APEC economies were divided into an eastern and western rim of the Pacific.

For Japan, as one of the biggest economic powers in the world, it is not only a matter of economic interest but also political and strategic interest. Collision between Asia and the United States over economic matters might lead to political and/or cultural disputes, and that is the worst scenario for Japan. Japan should make clear that it acts according to GATT/WTO principles, and lead the APEC process by example, such as meaningful trade and investment liberalization and facilitation.

Then, it can avoid the question: "which side is it on?" Japan can expect support on this matter from Australia whose actions have been consistent with GATT/WTO principles. Australia's sensible reaction to the recent trade dispute between Japan and the United States on automobile and auto parts was encouraging to Japan in this sense.

However, there is one concern regarding Australia's approach towards APEC. Recently it appears that Australia is opting for stricter methods to realize APEC liberalization. Like the United States, the Australian government has pushed for detailed commitments on trade liberalization. Trade Minister McMullan has also expressed his view that, to promote the APEC liberalization process, Australia might prefer reciprocal application of regional liberalization for outsiders to the MFN treatment. These views stand in sharp contrast to the developing economies in Asia which insist on a more flexible approach to trade and investment liberalization.

I have a rather optimistic view of APEC liberalization. All members are enmeshed in the global and regional economy, and they all know that multilateral free trade is the best way to realize their full potential. In addition, the target year to complete APEC liberalization is 2020, which should be enough time for them given their rapid economic development and the voluntary and unilateral liberalization moves they have already made.

APEC liberalization will be completed in time without forcing developing economies to do it right away. If a main, if not the main, objective for Japan and Australia is to keep the APEC framework itself and the liberalization process going, they should closely communicate and cooperate. Constant liberalization efforts from both countries will encourage each other's government and industries. Moreover, it will make other members confident of the APEC liberalization process. ■

Okamoto Jiro is a researcher of the Economic Cooperation Department at the Institute of Developing Economics (IDE).