

Japanese story: Australia and Japan after the crisis.

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Australia in the past three decades has undertaken an amazing economic transformation. We've transformed ourselves from an inward looking protectionist poorly performing economy to one of the most open, dynamic and best performing economies in the OECD (or as my American commentator friends on CNBC Asia say, we've gone from 'down under' to down wonder'. There's no better illustration of this than in the midst of the Lehman Brothers crisis, when we saw the biggest collapse in trade volumes since the Great Depression of the 1930s, and yet Australian export volumes remained in positive territory. To coin a famous phrase of Australian political history, Australian exporters were the 'true believers' who kept the faith when times were tough. Another illustration of this is in the labour market, where Australia now has one of the lowest unemployment rates in the industrialised world, compared to the 1970s and 1980s when our jobless rate was typically twice that of the USA. Now the positions are reversed with the US's unemployment rate twice that of ours and Australian exporters can again take some credit for this, as they hung onto their workers when times were tough (a term known as 'labour hoarding' in the economist's jargon), and adjusted hours, whilst elsewhere in the USA, UK and Europe they laid workers off.

What's the reason for the Australian miracle? Historically we can point to the great reforms of the 1980s and 1990s implemented with great courage by Bob Hawke and Paul Keating. The floating of the Australian dollar, the reduction of tariffs, the introduction of superannuation and the social wage were all part of the reasons for the success we experience today. We can also point to the fiscal reforms of the 2000s and the stimulus package formulated quickly and bravely in response to the global financial crisis (GFC) that drew the praise of re-known international economists such as the Nobel laureate Joe Stiglitz. We can also point to the stimulus package of China (we've benefitted more from 'bamboo shoots' in Australia than 'green shoots') and the rest of Asia for our success. Now over 70 per cent of Australian trade is with the Asia Pacific, and the likes of China, India, ASEAN and the emerging markets are helping drive demand for Australian exports and lifting our growth and employment rates not to mention our record terms of trade (the price of exports we receive relative to the price we pay for our imports). With the rise of Asia in the 21st century, it's no wonder we've shaken off the mindset that the famous Australian economic historian Geoffrey Blainey dubbed 'The Tyranny of Distance' in how we explain our relationship with the world, and have replaced it with 'The Power of Proximity'. In other words, Australia, 'The lucky country' has made its own luck, and finds itself in the right place at the right time in relation to Asia's rise. But it wasn't inevitable. If we hadn't put our own house in order and embraced openness we would not have been in this fortunate position now. And the continued economic growth and urbanisation of China and India and the emerging markets, generates strong demand for all sorts of Australian exports from coal, iron ore, LNG to expertise in construction, architecture, finance, education and

agribusiness services. So the lucky country will ride this boom and enhance it for some time to come. We don't know whether it is, again in Blainey's words, 'The rush that never ended' but it is a long term structural shift in the global economy that is centred on Asia with Australia being a key beneficiary *and a contributor* (along with a few other key emerging players like Brazil.)

But when you get lucky, you don't do it by yourself. Before the great reforms of the 1980s took place, Australia has one very important friend. That friend was Japan. In 1957, just 12 years after the devastation of World War Two, Japan and Australia signed an economic co-operation agreement. This enabled Australia to forge a beach head in Asia, as Japan's rapid industrialisation in the late 1950s, 1960s and 1970s, drove demand for our commodity exports. There would be no Australian success in China, India and ASEAN today without Japan. Indeed there would be no Asian century and the world, the region (and Australia) would be obviously poorer for it. Amazingly, after the 1957 agreement was forged, it only took Japan a decade to take over from the UK as our key export destination, a position they held for over 40 years, and just recently been surpassed by China. This occurred right at the time that Geoffrey Blainey wrote his famous 'Tyranny of Distance' treatise. Furthermore, once Japan industrialised, and our trading relationship matured, Japan began to play an important role as a foreign investor in Australia and in the rest of Asia, a role that has remained important to this day, along with the rise of new sources of foreign direct investment (FDI) in Asia from ASEAN, China and India.

I think it's important that we remember the past and the role that Japan has played in enhancing Australia's economic prosperity, when we look to the present and the devastation that the Tsunami and the earthquake has played on our friends in Japan. As well as the obvious human tragedy, the economic impact has been devastating, in terms of trade and industrial production and there's further uncertainty with respect to the nuclear industry's impact. The impact has been felt here in Australia too. In the recent survey of exporters carried out in the DHL Export Barometer, the Japanese Earthquake and Tsunami had had a major economic impact on export confidence together with the Christchurch earthquake and natural disaster back home particularly in Queensland. Most of the impact has been felt by the tourism industry (with 27 per cent of tourism operators affected) along with large falls in revenue and demand elsewhere. As a result, Japan is at the foot of the DHL Export Barometer table when it comes to export confidence.

So the reconstruction job will be big for Japan, but we can remember that it has been through this before. On the smaller scale, it had the Kobe earthquake in 1995 with its associated economic stimulus, but if we got further back to the 1940s, we know that Japan has renewed itself before in its history. Of course, it had a lot of international support; the famous US Economist Martin Bronfenbrenner travelled around Japan after the devastation of the War and the bombing of Hiroshima and Nagasaki, (in his famous paper *An Airport Economist in the Ryukyus*) and helped get aid out to the millions of affected citizens. But bit by bit, Japan rebuilt itself into being a global economic powerhouse within a couple of decades. This gives some reasons for cautious optimism. After all, if Japan recovered in the 1940s as a poor country, then surely it will be able to recover in the 2010s as a rich one.

And what of the future? How will the Japan- Australia economic relationship fare as Japan rebuilds?

On the 50th the anniversary, I wrote of the 7'F's of the future of the relationship. It might be timely to revisit them in light of recent global events.

The first is free trade agreements (FTAs). In general the FTA with Japan receives little attention compared to other bilateral pacts. That's because of the maturity of the bilateral relationship. But a lot of focus is now on the intra-regional institutions such as APEC and the Trans Pacific partnership (TPP). This makes sense because of the nature of intra-regional trade and the important role that Japanese companies play regionally as a source of FDI and as a major facilitator of intra-regional trade. After all, as pointed out by the Asian Development Bank (ADB), 46 per cent of intraregional exports in emerging Asia and 75 per cent of intraregional imports were parts and components. Not surprisingly then whilst, Australian small and medium sized enterprises (SMEs) are mainly exporting to China and ASEAN rather than Japan, they are looking to set up strategic alliance and global supply chains set up by Japanese transnationals. Significantly, Japanese multinational companies themselves are a major player in Australia's trade and investment flows to the rest of East Asia. As the Australian National University's seasonal Japan analyst Peter Drysdale has pointed out: "the bilateral trade numbers underestimated the importance to Australia of Japanese trading companies, the role of Japanese global supply chains and the rise Japanese foreign direct investment (FDI) throughout the region. Japan's investment 'foot print' in Asia plays a huge role. For example, over the past eight years, exports to Asia from Japanese firms based in Australia rose from six fold \$ 1 billion to \$ 6 billion with major players like Kirin, Impex, Asahi and Nippon Paper doing much of the heavy lifting. Japan has not only provided momentum across the region as an investor and innovator but has also been generous in terms of aid as well."

The second is freeing up services. Japan had some acceleration of this reform when Prime Minister Koizumi reformed parts of the Japanese service sector. This will continue as the per capita of Asian economies continues to rise, and there is more collaboration across the region in terms of opening up services. Australia, in particular, has much to gain from these developments, given our strengths in professional services. For example, Blake Dawson has just become the first Australian law firm, to open an office in Japan, Bovis Lend Lease, is offering green building technology contracts to major multi-nationals and Japanese firms and Toll Holdings is expanding its client base in Japan following the acquisition of Osaka-based Footwork Express.

The third is freeters, young people with less permanent attachment to the Japanese labour market than the traditional 'salary men' of yesteryear. This is creating opportunities for Australia in terms of the development of human capital. According to Austrade Osaka's Chris Rees, Japan is looking to develop a more global literate workforce amongst its younger generations and Australia's strong international student component has helped to raise the cross-cultural skills of Australian graduates. Rees points to a number of Australian education institutions such as the University of New South Wales (UNSW) and the University of Southern Queensland (USQ) who have been help re-tool Japanese workforces to adjust to a more globally orientated business environment.

The fourth is football. We've had a great relationship with Japan economically coupled with numerous artistic and cultural exchanges but we haven't quite made it in terms of sport. There's no Ashes contest or Bledisloe Cup so maybe soccer (football) might be a good avenue to build a tradition. The Australian A-league is partly modelled on Japan's J-League, Australian Clubs and players often play in Japan and the entry of the Socceroos in the Asian Cup and gaining entry to the World Cup via Asia might just be the start of something. Of course, in 2006, our first World Cup finals in **32 years**, we played Japan (Just don't mention the score!). This could be built into something very special – a very friendly but vigorous rivalry!

The fifth is feminisation. Something has to be said about Japan's unique demographics. As well as the ageing population, Japan is becoming more female. This is occurring in the economy (more women shareholders, entrepreneurs and consumers), in politics and in society as a whole. This is changing the nature of Australia's services with Japan. For example in the key sector of tourism, short, intense tour bus holidays are being replaced by longer, more health conscious, reflective activities from Japan's new class of retirees. This is helping grow opportunities for health and well-being, education and creative based activities instead of the just the old golf and karaoke routine of the salary-men of long ago. There is also significant female ownership in investments including currencies ('carry trade') that impact Australia. The economic and political influence of Japanese women in future years will be an important trend to understand globally and in terms of the bilateral relationship with Australia.

And the final 'f' is a family anecdote. I first visited Japan in 1969, and had my first taste of Japanese generosity when I was 4 years old. My father was taking a sabbatical at Keio University in Tokyo and the whole family got to enjoy the experience. A Japanese family moved out of their own house so we – a family of six (!) – could live in comfort in Japan during our stay. Japan then had few foreign visitors and it was before Japanese travelled much outside their country but their generosity to our family was remarkable. I can remember most of all travelling on the bullet train (the *Shinkansen*) to the Osaka Expo site – nothing could make a four year old boy more excited than a fast train! I later visited the Aichi Expo in Nagoya as an adult which was a different experience. Just last month my parents returned to Japan for the first time in over 40 years. They again stayed with the same generous family in Tokyo and they gave them photos of us all as little children that they had saved for the return visit (no matter how long it took)! So my family has received over forty years of generous friendship from Japan, and my country has received over 50 years of economic friendship, so now after a terrible 2011, let's hope we can help repay some of that friendship with Japan, economically and culturally in the years to come.

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