Although Australia’s relations with Asia have been the subject of many recent books and articles, less has been written about economic relations. That is the subject of this book.

The selection of essays presented here reflects the author’s recent research interests. Almost half are about trade with Indonesia and that country’s economic problems. The remainder deal with past and future Australian trade with Japan and China and with some broader aspects of economic relations with southeast Asia. One essay explores the prospects for expanding trade relations between Asia and the countries of South America.

The collection of these essays into one volume is of special value to students of economics, and also brings to the general reader a wealth of valuable recent information on Australia and Asia not readily available elsewhere.

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AUSTRALIA AND ASIA
By the same author

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*The Australian Trading Banks*, 1957

*The Australian Economy: A Volume of Readings* (with W. M. Corden) 1963

*Taxation in Australia: Agenda for Reform* (with R. I. Downing et al.), 1964

*A Small Rich Industrial Country*, 1968

*The Australian Economy: A Second Volume of Readings* (with A. H. Boxer), 1972
Australia and Asia Economic Essays

H. W. ARNDT
To Tina
Preface

Much has been written about Australia's relations with Asia in recent years. The subject, for obvious reasons, is a constant theme in public discussion in Australia, although, for equally obvious reasons, it is peripheral to the concerns of people in the Asian countries. The only claim to novelty this book can make is that it deals with Australia's economic relations with her Asian neighbours—with just a little admixture of politics or at least political economy.

The selection of particular Asian countries is somewhat arbitrary and reflects the author's recent research interests. Thus almost half the book deals with Indonesia and Australia's relations with Indonesia. The other half examines the past and future of Australia's trade with Japan and China and some broader aspects of economic relations with the southeast Asian region. One chapter looks to the other side of the Pacific and may be thought to have demanded a different title for the book but will be found to have some common themes with the chapters on trade with Indonesia and Japan.

Some of the essays—even the one on Japan which was written only a few months ago—have required updating. This has been done by short postscripts written just before Christmas 1971. To make the essays easier to read, all footnotes except references for direct quotations and all statistical tables have been eliminated; interested readers may consult them in the original version to which reference is made on the first page of each chapter. A bibliographical note at the end of the book will, it is hoped, be useful to those who want to go into some of the topics more deeply.

Thanks are due to editors and publishers who have given permission to assemble these essays in book form and to the Australian National University Press for their helpful co-operation.

Canberra
December 1971

H.W.A.
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On the Fringe of Asia

Indonesian fishermen and Malayan trading vessels for centuries made landfalls on Australia's inhospitable northwestern coast. Chinese seafarers may have discovered Australia in the fifteenth century and turned away. By the accidents of history, Australia became a British colony. For a century and a half it developed as part of the British Empire and Commonwealth. Now that the tide of British power has receded from Asia, here Australia remains, one of two nations of European settlement and civilisation on the fringe of Asia, flourishing, affluent, confident, yet preoccupied with the task that history and geography have posed for its people, the task of coming to terms with Asia.

Until the fall of Singapore in 1942, Australians did not think much about Asia, not much more than did their cousins in London or Lancashire. On the only occasion in the nineteenth century when Australians feared invasion, it was the Russians, not any Asians, they thought were coming. Even the influx of Chinese into the goldfields in the 1860s did not initially cause much concern. It was the attempts of sugar planters to bring into the country indentured labour from the Pacific Islands that first gave rise to demands by organised labour for restrictions on non-white immigration, although in the following decades the 'White Australia' policy was undoubtedly linked in the minds of most Australians with vague fears of the 'yellow peril', of being ultimately overwhelmed by the 'teeming millions' to the north. Australians did not have to think much about Asia because almost all their connections—of kinship, of trade, of culture—were with Britain, because the British navy was strong and Asia was weak.

All this changed during World War II and has been changing further ever since. The initial dramatic impact on the Australian

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mind was made by the demonstration of Japan's military might at Singapore and the experiences of the bombing of Darwin, of submarines in Sydney Harbour, and of fighting the Japanese in New Guinea. Then came the overthrow of Dutch rule in the neighbouring East Indies in which the Australian Government, almost to its own surprise, parted company from its British and American allies in lending strong and sympathetic support to the young Republic of Indonesia, and this was followed in quick succession by the transformation of all the former Asian colonies into independent states and by the victory of communism in China.

After a century and more of comfortable remoteness from the main stages of world history, Australians have in the past twenty years found themselves on the edge of the area of greatest tension. Australian troops have fought in Korea, in Malaysia, in Vietnam. Developments in southeast Asia have been the continuous focus of most of Australia's foreign policy. The economic development of the countries of south and southeast Asia has, next to its responsibility for New Guinea, been the predominant concern of Australia's efforts in foreign aid, beginning with its initiative in the establishment of the Colombo Plan. The orientation of Australia's trade has shifted in a generation from close ties with the United Kingdom towards a much more diversified pattern in which Asian trade partners, and above all Japan, have come to play a major role.

All these developments have caused a profound change in the ways Australians think about their own country and its relations with the outside world. In the preceding half-century Australian nationalism had reflected little more than the restiveness of the growing child tied to mother's apron strings. Today most Australian thinking about their country's identity and future revolves around its relations with Asia. It would be idle to pretend that the average Australian man or woman knows much about Asia. The distances are still great, and the gulf between Australia's cultural heritage and way of life and those of its Asian neighbours too deep and wide for real understanding. But a good deal has happened and is being done to narrow the gulf. Australian schoolchildren learn about Asian countries and their history in their lessons. Some study Asian languages at schools and universities. Newspapers devote to Asia much of their foreign news coverage.
Australians have had the opportunity to meet thousands of Asian students studying at Australian universities and colleges. More Australians every year visit Asian countries as tourists or businessmen. One factor that has perhaps helped in all this has been the large post-war immigration to Australia from the European continent. Not that these European migrants have come with more interest in or knowledge of Asia than the British; on the contrary. But the leavening of Australian society with so many ‘foreigners’ has broken down some of the former British insularity and made Australians more understanding of ‘otherness’.

**Political Relations**

How do Australians now see their relations with Asia? In the short run it is convenient to separate political and economic aspects, although in the more distant future both merge on the larger canvas of hopes and apprehensions.

Australian opinion on political relations with Asia has been shaped in the past twenty years by divergent attitudes to the Cold War, the defence alliance with the United States, the role of communist China, and the Vietnam war, and by interpretations of political developments in Indonesia, Malaysia and other countries of the whole region stretching from Pakistan to Korea.

Throughout this period Australia has had conservative governments which, supported by a majority of public opinion, have in general endorsed American foreign policy—in the cold war confrontations with the Soviet Union, on China, in Korea and Vietnam. A major consideration has undoubtedly been the belief that Australia can no longer look to Britain but must look to the United States for help in her own defence. But there has also been broad agreement with American official thinking about the issues at stake, the need to contain communism both in the interests of the Western powers, including the United States and Australia, and in the interests of Asian countries under threat of internal subversion and external attack. Even official Australian policy has not always seen eye to eye with American. But where there may have been a disposition to question the wisdom of American attitudes, as on the issue of recognition of communist China, there has been reluctance to voice open criticism.

Australian public opinion, however, like public opinion in all the Western democratic countries, has been far from unanimous.
In the Labor Party, in the trade unions, and among intellectuals, there has been a strong current, stemming from the radical and socialist tradition, which has tended to be anti-capitalist and therefore anti-American if not pro-communist on all the major issues. This current has at various times been reinforced by the sort of resentments which American power and bigness have aroused around the world, by pacifist or more vaguely internationalist condemnation of ‘power politics’ and all that goes with it, and among intellectuals by a sympathy with Asian anti-colonialism in which feelings of guilt for past wrongs done by the white race play an important if not always conscious role. In the last few years, this opposition to official Australian foreign policy has been sharpened and widened by the Vietnam war, drawing support from young and older opponents of conscription at home and from the upsurge of dissent in the United States. Even on the issue with the widest appeal, withdrawal of Australian forces from Vietnam, the opposition is still a minority of public opinion, but it is vocal and attracts many of the younger generation.

On the problem of the Indo-China war, the Australian Government and its supporters have broadly accepted the Johnson-Nixon policy. They are reconciled to the need for American disengagement but hope that it will proceed sufficiently gradually to allow the Saigon Government to hold its own against North Vietnam, and that on this basis the war may be brought to a formal or informal end. They endorse the ‘Nixon doctrine’, which enjoins the non-communist countries of southeast Asia to co-operate in their own joint defence, able to count on American military help in future only against intervention by a major power, and they intend that Australia shall play an active part in such co-operation. In doing so, they are only partly concerned with ‘forward defence’ of Australia, the notion that it is better to hold a line against communist aggression on the Asian mainland than on Australia’s own shores. There is also a strong sense of solidarity with the countries of southeast Asia whose peoples, they believe, have no wish to come under communist rule.

Those opposed to the government’s policy include, besides the tiny but active communist groups, many who believe that communism provides the only solution to the social and economic problems of the countries of south and southeast Asia, and others who take the view that military intervention by white Western
countries in Asia does more harm than good, however well in­
tentioned. All these would argue with more or less conviction
that Australia's defence interests are in any case not sufficiently
involved and would opt for a defence policy confined to defence
of the Australian continent. Discounting any danger from what
they would call the 'bogy' of communism, even to southeast Asia,
let alone to Australia, they would claim that what threat there is
can best be countered by economic development and institutional
reform and would confine Australian intervention in southeast
Asia to aid in this sphere.

In the background to the debate on Vietnam and other south­
east Asian issues loom uncertainties and fears about the role of
communist China which Australia shares with most of the rest
of the world. No one in Australia, at least among the moderately
well-informed, lives 'in fear of China' in any short-run sense. If
there is such fear, it is fear of Chinese support of communist
subversion in south and southeast Asia, possible Chinese take­
over attempts in Korea, Taiwan, and Hong Kong, and the risk of
a third world war arising from great power involvement in local
disputes. It is with these risks in mind that some Australians have
been tempted to welcome a Soviet Russian presence in the south­
east Asian region, not without provoking widespread disagreement
from others.

Finally, thought is increasingly being given to Japan's future
political role in the region. Few believe that Japan's low political
posture of the past two decades will for much longer survive the
phenomenal growth of her economy and the extension of her
economic interests into southeast Asia. But there is confidence
that for some years ahead at least a more active Japanese part
in the politics of the region will help rather than harm Australia's
own interests and concerns.

**Economic Relations**

Economically, Asia presents to Australia today two very different
faces: that of Japan, an industrial giant still growing at an un­
paralleled rate, Australia's largest market and increasingly im­
portant supplier of goods and capital; and that of the under­
developed countries of south and southeast Asia.

Japan displaced Britain in the mid 1960s as Australia's main
export market. In addition to her still growing demand for Aus­
Australia's wool and foodstuffs, Japan has found in Australia a large and convenient source of minerals, especially iron ore, bauxite or alumina, coal and nickel, needed in ever growing volume by her industries. In return, she is finding in Australia a smaller but also growing market for her manufactures. Australia is counting her blessings, happy to promote the booming trade partnership, welcoming the help of Japanese, as much as American, British, and European, capital and know-how in the exploitation of her mineral resources and her industrial development. Not a few Australians are unhappy about what they see as a trend towards excessive foreign ownership of Australian industry and excessive haste in selling off the newly discovered mineral wealth in unprocessed form. But these protests are not specifically directed against Japan. Nor is there as yet much fear of excessive economic dependence on Japan.

With most of her other Asian neighbours, Australia's economic relations are those between a small, rich, industrialised but primary exporting country and less developed countries struggling with immense economic and social problems. While her trade with some of the smaller and more prosperous countries of the region, such as Malaysia, Singapore, Hong Kong, and Taiwan, has been expanding, the pattern of her trade with most of the larger ones, such as India, Pakistan and Indonesia, is still competitive rather than complementary. The singular exception is communist China which for several years has bought large quantities of Australian wheat; but this is a market which, while welcome, is regarded as highly uncertain, liable to disappear overnight if and when China can meet her own food needs.

Australia has tried to assist the less developed countries of Asia by providing training facilities, experts, project and food aid, and trade preferences. The amounts have until recently been small, little more than gestures of goodwill, partly because of the rapidly growing demands made on the Australian taxpayer by the need to develop New Guinea for independence. In the past few years, Australian aid to Indonesia has assumed more substantial proportions, because of all Asian countries Indonesia, as Australia's nearest, largest, and poorest neighbour, is the one whose success in coping with its problems is thought to affect Australia's own future most closely and whose chances of doing so under its
present government seem better than under any of its predecessors or likely alternatives. The scheme under which Australia has uni-laterally granted tariff preferences on imports of manufactures from the less developed countries, including those of Asia, is still exceedingly modest, limited by fears of exposing some of the more vulnerable of Australia's own manufacturing industries to Asian competition. But that Australia, which only twenty years ago discriminated against Asian countries, now discriminates in their favour is a notable sign of changing attitudes.

Another way in which Australian economic involvement in Asia is increasing is through investment by Australian companies in industrial and other development in countries of southeast Asia. The process is at its very beginnings, because only in the past decade have Australian manufacturers looked seriously for export markets and because until recently government policy tended to discourage direct investment abroad for rather misguided balance of payments reasons. While such private investment is unlikely for some time to make a significant contribution to the economic development of the recipient countries, it constitutes another opportunity for Australians and Asians to get to know, and involved with, one another.

Finally, Australia has in the past ten years quietly liberalised her restrictions on immigration from Asia. Those admitted each year still number only a few thousand, mostly people with professional qualifications or other skills needed in Australia. The government has proceeded quietly so as not to arouse apprehensions and prejudices which still lie dormant among many ordinary Australians. But there is a good deal of public pressure, especially from the younger generation who resent race discrimination on principle, and liberalisation is likely to go further. There is no significant disagreement with the official view that the criterion of immigration policy must be 'assimilability'. Australia does not want to saddle herself with problems of race conflict which, as the experience of most of her Asian neighbour countries demonstrates quite as much as that of white countries like the United States, are the almost inescapable consequence of large minorities of a different race. Differences of opinion relate only to the numbers of Asian immigrants who could be admitted without giving rise to such problems.
The Longer-Term Future

So much for the present and immediate future of Australian attitudes towards and relations with Asia, and it might be sensible not to attempt to look further ahead. The more distant future is so uncertain that it may be pointless to speculate. But Australians cannot help wondering what the future holds for their children and grandchildren. No doubt that future will lie somewhere between the doom for white Australia which geopoliticians at the other end of the globe are so prone to predict and the maintenance of something very much like the status quo which suggests itself so readily to the complacency of a lucky people. Just where in between will be determined very largely by events in Asia and to some degree by Australian responses to these events.

Let me begin with an optimistic scenario, the sort of developments most Australians would like to see. The Vietnam war comes to an end within a year or two, with the border between north and south re-established along the 17th parallel, each side free, as in Germany and Korea, to reconstruct and develop in its own way. The neutrality of Laos and Cambodia is restored, guaranteed by an agreement among the great powers not to intervene and by an agreement among the countries of the southeast Asian region to come to one another's assistance against external aggression. The United States withdraws its forces from southeast Asia but remains ready to project the non-communist countries of east and southeast Asia against attack from China. China after Mao abandons permanent revolution and settles down to peaceful development of her socialist society. The countries of south and southeast Asia, with the help of capital and technology from the West, from Japan and from the communist bloc, make steady progress with economic development and social reform, co-operating with one another on a regional basis within a multilateral world trading system and maintaining broadly democratic political processes and open societies. Australia, increasingly involved in regional economic and defence arrangements, co-operates with them through trade and aid, giving their industrial products increasing access to her domestic market and contributing increasingly to their economic progress through technical assistance, capital aid, and private investment.

It is all too good to be true. So immense are the economic and social problems of India, Pakistan, Indonesia, and even of some
of the smaller countries like the Philippines, so great are the difficulties of reconciling the requirements for economic progress and social reform with the forces of traditionalism and vested interest in countries subject to inexorable population pressure and desperately short of the technical, administrative, and managerial skills needed for development, that it is excessively optimistic to expect even moderately steady and peaceful advance everywhere. There will be setbacks, class and race conflict, and national animosities between neighbours. Wherever governments prove unable to meet the need for food and jobs and to alleviate gross inequality and social injustice, social unrest is liable to grow into subversion and revolt and to invite foreign intervention—from the communist countries to help the 'popular forces' and from anti-communist countries to assist the 'legitimate governments'.

It does not, alas, require much imagination to foresee other possible troubles in Australia's Asian neighbourhood. If American ability and will to play a continuing role in Asia should be further undermined by domestic problems and dissent, Indo-China may after all fall under Hanoi control. It may then not be long before Thailand, Malaysia, and the Philippines come under pressure of communist subversion and before China feels strong enough to take over Taiwan or Hong Kong, and North Korea to attack South Korea. Even if Pakistan and India manage to remain at peace with each other, there is some risk to the national unity of either, with unpredictable international implications. Nearer home, if the Suharto régime should prove unequal to its task, Indonesia may once again descend into political turmoil. Even Japan may not indefinitely enjoy domestic political stability and confine her external expansion to the economic sphere, as in the past twenty years.

It is difficult to see even in the most dire of these eventualities a direct threat to Australia in the foreseeable future. There are those, in Australia and more confidently and smugly in more remote parts of the world, who predict that in the long run the contrast between population pressure in Asia and Australia's 'empty continent' must prove irresistible, that China or Indonesia or Japan will sooner or later intrude into Australia by infiltration, economic pressure, or military force. One wonders whether population pressures work this way in the world of today, or tomorrow. However, this is a nightmare that has certainly played some part
as a motive behind Australia's deliberate policy to increase her population by assisted immigration, behind her defence alliance with the United States, and behind her desire to see communism contained on the Asian mainland. Not one or all of these safeguards, nor any others, may in the end prevail, but this is looking too far and too gloomily ahead.

Meanwhile Australia can do no better than to pursue her domestic economic and social development, sharing her opportunities with as many newcomers, including newcomers from Asia, as she can absorb; to give what help she can, through economic and technical assistance and more liberal trade policies, to her Asian neighbours; to co-operate in whatever regional defence arrangements the southeast Asian countries may be able to agree upon and invite her to take part in; and to promote better mutual understanding between Australians and Asians through greater emphasis on Asian languages and culture in Australian education, through freer movement of people in both directions, and through whatever other ways may be found of bridging the gulf of mutual suspicion, indifference or ignorance.

Postcript

This essay was written for a special issue of Quadrant on the occasion of the 28th International Congress of Orientalists held at Canberra in January 1971. It was intended to tell foreign orientalists something about Australia's relations with and attitudes towards Asia.

Much has happened in Australia's part of the world since then. The withdrawal of Australian and American troops from Vietnam has become an accomplished, or nearly accomplished, fact. China has been admitted to the United Nations and Taiwan expelled. A rapprochement between the United States and China is on the way. India and Pakistan have been at war and a new Asian state, Bangla Desh, has arisen. The international monetary system and economy have passed through a period of severe disarray, initiated by President Nixon's economic measures of 15 August 1971, which has cast a shadow on the economic prospects for Japan and indirectly for Australia.

Yet, except for the occasional word here and there, I would not wish to change what I wrote eighteen months ago. I have not changed my mind on Vietnam where the American decision to
help defend South Vietnam from a communist takeover has been justified by the substantial achievement of its objective there, though its consequences at home have been in many ways calamitous, and I still believe the Australian decision to lend moral and token military support to the Americans was sound at the time. I welcome the long overdue admission of China to the United Nations, but regret that, partly because it was so long delayed, it has been made so completely on Peking's terms, including the expulsion of Taiwan, a country larger in population than Australia and no less entitled to national independence. The rapprochement between the United States and China is also to be welcomed by Australia, provided the United States is willing and able to negotiate from a position of strength. For in important respects, a triangular balance among the super powers will make for a safer world than the situation in the past when the Soviet Union could press demands, secure in the knowledge that the other two would not get together. The fourteen-day war between India and Pakistan was perhaps the lesser evil than the indefinite continuation of the burden of ten million refugees on India's strained economy, but its outcome creates problems, both in a politically and economically weak Bangla Desh and in a humiliated Pakistan, which may trouble the sub-continent for a long time to come.

But none of these developments fundamentally changes the political or economic issues that confront Australia in her relations with Asia. Politically, what happens in southeast Asia will continue to be more important for Australia than events on the Indian sub-continent, and in southeast Asia her interests will continue to be in the stability of the region, including the protection of its member countries from subversion and external aggression by their joint efforts and, in the last resort, by help from without. Economically, Australia's future remains bound up primarily with the economic prosperity and growth of Japan, compared with which China will for long remain of quite minor importance. But the economic development of Indonesia and the other countries of southeast Asia will present to her both opportunities and obligations.
INDONESIA
More than five years have passed since the abortive coup of 1 October 1965 which heralded the end of Sukarno's régime in Indonesia and ushered in the 'New Order' under the leadership of General Suharto. Much has changed in these five years, mostly for the better. Much, too much, has remained unchanged.

The Legacy of Sukarno

To appreciate how much has been accomplished one has to recall the condition of the Indonesian economy when the new régime took over. A decade of ever increasing economic mismanagement had brought a degree of economic breakdown with few parallels in modern history.

The country was literally bankrupt, unable to meet payments due on foreign debts incurred largely for military and other non-productive purposes, the precise magnitude of which was unknown but which were estimated at some $US2·5 billion. Export earnings had fallen to a level where they were barely sufficient to finance half the country's minimum import requirements, excluding debt service.

Inflation, which had been chronic since the early days of the Republic, had got completely out of control. Money supply had doubled in 1965 and again in the first quarter of 1966. Prices were rising at 30 to 50 per cent per month. Unrestrained resort to the printing press to finance government expenditure reflected a far-reaching dissolution of orderly processes of government. The president, ministers, government departments, the armed forces, regional authorities had come to spend for their own purposes what money they could lay their hands on, without any effective budget control.

Inflation and corruption, which had eroded the collection of

taxes, had also undermined the complex and constantly changing system of government controls of Sukarno's 'socialist' economy. Corruption—inevitable when even senior officials' salaries had declined in purchasing power to some $2 a month, apart from the weekly rice ration—had made Indonesia, in the words of a local wit, 'the most laissez faire socialist economy in the world'. Black markets, smuggling and other forms of evasion had reduced government economic controls to the status of a costly nuisance.

In most sectors of the economy production was on the decline. Production of rice, the staple food, and of other foodstuffs, while not reduced absolutely, had failed to keep up with population growth, so that by 1966 some 10 per cent of the country's food needs had to be imported. Production of the main export crop, smallholder rubber, had also been maintained (in volume though not in quality). But output of most of the estate crops had declined following the government takeover after 1957, disastrously so in the case of the sugar industry which ceased to be able to export at all. Official export earnings were further reduced by extensive smuggling. Shortage of foreign exchange for raw materials and spare parts had reduced output in most manufacturing industries to 10 to 20 per cent of capacity. After years of neglect of roads, ports, public utilities, irrigation works and every other form of capital equipment, transport and communications were operating so inefficiently as to hamper all other forms of economic activity. In fact, for a decade or more, Indonesia had been living on her capital, maintaining consumption by running down physical capital at home and borrowing abroad.

In the circumstances one might wonder how the majority of Indonesians survived. But they did. In fact, in 1965, living conditions for the masses of the Indonesian people were probably not very much worse, and in some respects better, than twenty or forty years earlier. The majority, making a living as peasants in near-subsistence conditions, were only marginally affected by the inflation and were used, from time immemorial, to the other evils of bad government. The urban masses were protected from starvation and acute shortages of essentials by imports the country was less and less able to pay for, and from open mass unemployment by an ever growing government payroll, civil and military, which was the main factor behind the inflation. It was not popular revolt against intolerable living conditions which made continua-
tion of this rake's progress impossible, but the increasing inability of the régime to cope with mounting economic disorganisation, its attempts to escape from these problems by slogan-mongering and foreign adventures, and the sharpening of domestic political conflict which resulted from both. And it was precisely this that the communists sought to exploit in the abortive coup.

**A Poor 'Rich' Country**

How could things have come to such a pass? The answer is to be found in the geography and history of the Dutch East Indies and the Indonesian Republic and can here only be sketched in a few strokes.

Indonesia is an archipelago of over 3,000 islands. The intrinsic difficulty of governing such a country is aggravated by great ethnic, religious, linguistic, and economic diversity among its peoples who were welded together into a single political entity only by the gradual extension of Dutch rule. To create 'Unity in Diversity', the motto of the Indonesian Republic, has been a major national objective, and the considerable extent to which it has been achieved in the past twenty years, not least by the spread of the national language through a national education system, was perhaps Sukarno's major achievement.

Sukarno's greatest disservice to his people was his refusal, especially in his latter years, to face the country's enormous economic problems, rationalised by soporific incantations about Indonesia's 'riches'. The notion that Indonesia is a 'rich' country has entered into foreign as well as domestic folklore. It rests on three facts, all in varying degrees deceptive: the fertility of Java's soil; the lush vegetation of the jungles of Sumatra and Kalimantan (Borneo); and the country's mineral resources.

Certainly, Java's volcanic soil is very fertile (though much of the island is mountainous) and 150 years ago, with a population of some five millions, it must have been prosperous by the standards of traditional peasant societies. Today Java has a population of nearly 80 millions, growing at well over 2 per cent a year, and population pressure on the land is steadily approaching a Malthusian situation, with widespread chronic malnutrition in much of east and central Java.

With the exception of a few areas, such as parts of North Sumatra, the so-called 'outer islands' lack Java's fertility: their
leached soils will grow jungle but (without costly investment in clearing and improvement) little else. Indonesia certainly possesses considerable mineral resources, especially the rich and productive oil industry, and with only 5 per cent of the area thoroughly surveyed more will no doubt be discovered. On the other hand, Indonesia lacks substantial high-grade deposits of the two minerals that have hitherto been basic to industrial development, iron and coal.

All this, however, is really rather beside the point. The natural resources which dazzle the layman are only part of the whole economic development potential. They are good to have, especially in such amplitude as in Australia, but one need only look at Japan's phenomenal economic development to recognise that what really counts is not natural resources but human and man-made capital, the enterprise and skills of the people and the stock of productive capital they gradually accumulate through saving. Of the two, the former is more fundamental. Germany and Russia, with their skills intact, needed only ten years to reconstruct their economies destroyed by war. Independent Indonesia, short of skills and know-how of almost every kind and with a cultural inheritance not always conducive to economic development, in fifteen years of mismanagement and neglect destroyed much of the capital created by the Dutch.

During their long rule over the East Indies, the Dutch developed what was in some respects a model colonial economy. They established plantations, built roads, railways, irrigation works, public utilities, towns and cities, and even developed some manufacturing, mainly cotton weaving. But it was the Dutch who did all this, with the help of some other Western capital. They governed the colony, administered its services, managed its larger businesses, factories and estates, filled its professions—over 200,000 of them. Small-scale business, trading in towns and in the rural areas, was largely in the hands of overseas Chinese. Indonesians, by and large, were not needed or wanted in jobs requiring higher skills and were neither educated nor trained for them. When Dutch rule came to an end, there were only a few handfuls of ‘natives’ with a completed tertiary education, with experience in administration, business, or professions.

To these basic explanations of Indonesia's underdevelopment must be added the consequences of almost a generation of war and
political turmoil. The economy had hardly recovered from the Great Depression of the 1930s when it was hit by the Dutch ‘scorched earth’ policy, Japanese occupation, and loss of export markets during World War II. It was almost five years after the declaration of independence in 1945 before the Dutch finally abandoned their attempts to restore colonial rule by force. During the 1950s there were years of promise of political stability and economic development. But even these were interspersed with rebellions, while bouts of inflation alternated with efforts at financial stabilisation. For some years, Sukarno sought to maintain a balance between the contending forces of the Army and the Communist Party. But as his troubles mounted, he drifted from ‘guided democracy’ to virtual dictatorship; from expulsion of all Dutch and other Europeans to foreign adventurism, the West Irian campaign and ‘Confrontation’ with Malaysia; and increasingly towards the communists at home and abroad.

Economic Stabilisation 1966-8

It took almost a year after the abortive left wing coup of 1 October 1965 (which was bungled by the communists and smashed by the army) before policies for stabilisation and rehabilitation of the Indonesian economy were evolved and began to be applied. For six months—during which the army rounded up communists and sympathisers, many hundreds being killed by the military and far more in ghastly unorganised massacres in towns and villages of Java and Bali—Sukarno remained president, though power was slipping from his hands, while the economy went from bad to worse. In March 1966, Sukarno was induced to transfer executive authority to a triumvirate consisting of General Suharto, the Sultan of Jogjakarta and Mr Adam Malik. In the following months, as the new régime slowly consolidated its political hold on the country, General Suharto emerged as its undisputed leader. He was appointed president in 1967.

From the outset, General Suharto, conscious that the military was ill-equipped for the job, insisted on leaving economic policy making to civilians, especially a group of Western trained economists of the University of Indonesia, under the leadership of Professor Widjojo. With the help of an International Monetary Fund mission, which had been sent to Djakarta primarily to sort out Indonesia’s foreign debt position, this group during 1966
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devised the economic strategy of the 'New Order', the first outlines of which were announced in a speech by the Sultan in April 1966. They became the members of a council of economic advisers to the president and were appointed to key ministerial posts. Reinforced in 1968 by the return to Indonesia of Dr Sumitro, dean of Indonesian economists and former Minister of Finance, they have been the effective economic policy makers ever since.

Convinced that there had to be an end to foreign adventures and government by slogans, that for some years at least the task of pulling the economy out of the morass had to have priority over everything else, the new leadership adopted a deliberately low key, pragmatic, non-ideological tone and approach. Economic recovery was presented as a long haul, in three stages—stabilisation, rehabilitation, development. A two-year stabilisation program was drawn up aimed at four short-term objectives: halting inflation, decontrol, a moratorium on foreign debts and new credits, and a new policy towards foreign investment.

The first essential in the fight against inflation was to restore some order in government finances. President Sukarno's extravagant 'special projects' were stopped and almost all development projects suspended. Efforts were made to restore treasury control over government expenditure. For the first time for some years, a budget was drawn up for 1967. By ruthless cuts in allocations, not least to the armed forces, the budget was to be balanced quarter by quarter, and senior army officers were put in charge of the responsible sections of the Ministry of Finance to see to this. Steps were taken to intensify tax collection and to reduce the huge financial drain through subsidies and losses of state enterprises. Fiscal measures were reinforced by severe restraints on bank credit and by raising bank interest rates closer to the rates of 15-20 per cent per month ruling in the unorganised market.

Decontrol seemed the only way out of the impasse created by ideological pressure for a socialist controlled economy which the cumbersome, inefficient, and corrupt bureaucracy was unable to administer effectively. Ostensibly designed to correct the inequities of the market and protect the 'suffering masses', direct controls had tended in practice to favour consumers (especially urban consumers) at the expense of producers (especially rural producers) and by aggravating the distortion of price relationships
due to inflation they tended to suspend all market incentives to efficient production.

Decontrol centred in the first instance on dismantling the complex system of foreign trade and exchange controls that had been built up over the years. From October 1966, exporters were free to sell their foreign exchange receipts in a free market, subject only to varying rates of export tax, and importers were freed from licensing controls. The gamut of multiple exchange rates was reduced to two, the BE (Export Bonus) rate for essential imports and the DP rate for less essential imports and capital transfers, and for some time both rates were allowed to find their own level. More slowly, since it required considerable political courage, steps were taken to bring the prices of subsidised consumer goods, especially petrol and public utility rates, more in line with costs of production.

During 1966, as one of its first tasks, the new government concluded 'rescheduling' agreements with Indonesia's foreign creditors under which debt service was deferred. These agreements were re-negotiated annually until 1969 when, with much difficulty, first the western and then the communist countries were persuaded to accept a long-term settlement of the 'Sukarno' debts. This involved repayment over thirty years beginning in 1970, with an optional grace period for part of the capital repayments and deferment of interest to the last fifteen years, 1985-99.

The political complexion of the new régime ruled out further help from the communist bloc. For urgently needed foreign aid, therefore, Indonesia had to turn to the western countries and Japan. In 1966, she received $US170 million of emergency aid credits. Early in 1967, the non-communist donor countries (including Australia) formed a consortium, known as the Inter-Governmental Group for Indonesia (IGGI). A formula was reached by which aid commitments were shared in equal parts between the United States, Japan, and the remaining donors, and in the following years total commitments rose from year to year to $600 million in 1970. Most of the aid was provided in donor country currency or food aid to support Indonesia's balance of payments, the rest in project aid.

Finally, both to confirm the new approach in foreign policy (already demonstrated by ending 'Confrontation' and rejoining
the United Nations) and as a first step towards a renewal of economic development, a foreign investment law was passed early in 1967. This offered financial incentives and assurances for direct investment of private foreign capital in Indonesia, whether alone or in joint ventures with Indonesian firms. Most of the Western enterprises placed under government supervision in 1963 and 1964 were returned to their former owners with the exception of the Dutch whose enterprises had been nationalised and for which compensation had been negotiated.

The stabilisation program succeeded beyond expectation in its primary object of slowing down and halting the raging inflation within two years. The rate of price increase was markedly reduced in 1967 and after a setback, due to a severe rice shortage late that year, the cost of living remained fairly stable from mid-1968 on. It rose by less than 10 per cent in 1969 and again in 1970, not much more than in many Western countries. A similar degree of stability was attained in foreign exchange rates. It was a remarkable achievement (there are few if any precedents for successful control of hyperinflation without destruction and replacement of the old currency) and almost certainly a necessary condition of any other improvement in the economic situation of Indonesia. But it was only a first step and its initial costs were high.

**Development Policies 1968-70**

The immediate effect of the drastic disinflationary measures, especially the credit squeeze and the halt to all public works expenditure, was inevitably to depress economic activity still further. The paralysis which spread through trade and industry was aggravated by a wave of persecution of the Chinese business community (motivated by a mixture of traditional xenophobia and resentment of alleged Peking support for the local communists). From mid-1967, as prices began to stabilise, the government took the first steps to revive business, by tariff protection for domestic industry and by allocating funds for public works, especially rehabilitation of roads and ports. Firm measures were also taken to stop the attacks and pressures on the Chinese. During 1968, the emphasis shifted increasingly from stabilisation towards efforts to stimulate business activity and resume economic development.

Credit restrictions were progressively relaxed. The state banking system, which had been debilitated by inflation and mismanage-
ment, was reorganised and enabled to resume its role in financing development. A program of high interest rates on fixed deposits was introduced to attract funds out of private hoards and central bank support was provided for medium and long-term investment. In 1968, for the first time since 1951, Indonesia achieved a balanced budget. Most of the increase in tax revenues came initially from the oil industry and from taxes on foreign trade. But to reduce the burden on the export industries the weight was shifted from export taxes to import duties, and efforts were made to make income tax more effective.

From 1968 onwards, modest surpluses in the current budget became available to finance public investment, but the bulk of finance for the development budget came from the counterpart funds of foreign aid. Another important source of finance during 1968 and 1969 was the very large increase in money supply that became possible without inflationary effects—and indeed necessary to sustain business activity—as public confidence in the currency returned and people became again willing to hold money balances, in notes or on bank deposits.

The main efforts of the government were directed at increasing rice production, repairing transport and communications, rehabilitating the estate and smallholder export industries, and encouraging investment in natural resource development and manufacturing. The Bimas (mass guidance) program for intensification of rice production through the use of high-yielding varieties, fertiliser, farm credit and extension services, which had been started in 1963, was greatly extended, for a time (not very successfully) through contracts with foreign supplying companies. During 1967 and 1968, most of the major national roads were repaired and considerable progress made in putting ports, railways, electricity supply, and telecommunications in working order.

Production of export crops was deliberately made more profitable, through more favourable exchange rates and lower export taxes (which also helped by reducing the incentive to smuggle), and steps were taken to promote more effective marketing and production of higher quality products. Machinery was set up under the new foreign investment law to negotiate contracts with foreign companies to undertake direct investment in mineral, forestry and fisheries development and in manufacturing and service industries. At the same time, the state oil enterprise negotiated production-
sharing contracts for new oil exploration and development, especially in offshore areas throughout the Java Sea. Domestic industry was assisted by improved supplies of raw materials, credit facilities, and tariff protection and by investment incentives under a domestic investment law.

Most of these policies were incorporated in the first Five Year Development Plan which the president ordered to be prepared in the latter part of 1968. It came into operation on 1 April 1969. The Plan, known by its Indonesian acronym Repelita, was little more than a set of policy priorities and rough output targets, together with a public investment plan which counted heavily on foreign aid. It was deliberately kept flexible, to be revised each year in the light of the previous year's performance. But much was made of it as the symbol of the government's will to press on with economic development. A valiant and not unsuccessful effort was made to use Repelita as a slogan and catalyst of national effort, the nearest thing to an ideology and emotional mass appeal of a government anxious to do without either.

Successes and Failures—A Balance Sheet

Economic conditions in Indonesia have unquestionably improved very considerably in the past five years. Not only has inflation been brought under control, but after years of decline productive activity and real income are on the increase. Available estimates suggest that in the first year of the five year plan, 1969/70, GNP rose by close to 5 per cent, implying a rise of some 2 per cent in average real income per head, and that a still larger increase was achieved in the second year, 1970/1.

With the help of a good season, 1968 yielded a record rice harvest and, while the 1969 harvest was somewhat disappointing, 1970 promised to show a further step forward towards the goal of self-sufficiency by 1973. Export earnings, which had declined from $US880 million in 1960 to $US630 million in 1965, had recovered to over $US1,000 million in 1969 and were expected to exceed $US1,150 million in 1970. The major contribution was made by the oil industry, now an efficient state enterprise run by an army general. Output of crude oil rose by 60 per cent in three years, but other export industries also improved their performance, if rather unevenly, with an overall rise of 13 per cent in 1970. There has been a marked improvement in the condition of the
main roads, ports and other infrastructure, and a substantial re-vival in manufacturing and construction activity. With better hotel and transport facilities, the tourist industry is becoming a signif-icant earner of foreign exchange.

After initial hesitation, foreign companies have come forward in large numbers to take advantage of the new climate for investment in natural resource development and manufacturing industry. By May 1970, some 235 contracts had received government approval, involving a total planned investment of $US1.2 billion, mostly in mining and forestry but including more than 130 manufacturing projects. In addition, some 30 oil exploration con-tracts had been negotiated and a number of foreign banks had established branches in Djakarta. Actual inflow of private foreign capital was still modest, perhaps $US80 million in oil and another $US30 million in other industries, but the first results were showing in rapidly rising timber exports and there was every reason to expect substantial contributions to Indonesia's export earnings from oil and other minerals in the next few years. Domestic investment, by private and government enterprise, picked up during 1969, as did public investment under the development plan, aided by an increasing flow of project aid by international agencies, such as the IDA (a subsidiary of the World Bank) and the Asian Development Bank, and by individual donor governments.

Most important perhaps in the longer run, much has been done to create an institutional environment more favourable to business activity and economic development. Order has been brought into the central government's finances, with reasonably effective budget control over expenditure by government departments and agencies. Business has been freed from some at least of the former welter of direct controls, with their high cost in terms of time (spent at government offices) and money (for bribes). Most of the worst distortions between prices and costs have been removed, or at least alleviated, so that rice farmers, for instance, are now reason-ably assured of a price for their paddy which makes it worth their while to buy fertiliser, and smallholders have an incentive to produce more (and better quality) rubber and copra. Throughout the country, though probably more so in Djakarta than elsewhere, there is now a feeling that things are getting better, a measured optimism about the country's economic future.
So much for the credit side of the ledger. Unfortunately, there is much also to be entered on the debit side. The undoubted progress that has been made has been painfully slow in coming and has as yet done little to improve the lot of the ordinary people in the cities and villages of Indonesia. In some respects, indeed, standards of living and social welfare have deteriorated. And the long-term prospects for the Indonesian economy are far from rosy.

Every credit entry in the ledger needs to be qualified. Exports have risen but not enough to match the rising import needs of the growing population and expanding economy. Rice production has increased but not as yet sufficiently to reduce the country’s dependence on food imports. Foreign investment is beginning to make an important contribution by supplying managerial and technical know-how, as well as capital, but it is also beginning to arouse nationalist resentment, not least among domestic businessmen in fear of formidable competition.

While industrial production and employment have risen, the country’s oldest and largest manufacturing industry, cotton weaving, remains beset with almost insoluble problems of small-scale units and obsolete equipment. There are hardly yet the beginnings of the massive industrialisation that will be needed to provide jobs for millions of unemployed and underemployed and for the new entrants to the workforce. Rehabilitation of roads, harbours, irrigation and other public works has largely been confined to the more developed regions of Java and North Sumatra, with little impact on the less developed provinces whose regional governments are mostly hamstrung by lack of finance and capable administrators.

Despite effective decontrol in some sectors, especially foreign trade and exchange, bureaucratic red tape remains pervasive and stifling in most others. In the absence of alternative employment, it has proved impossible to reduce the huge civil and military establishment of government, and the itch to interfere on the part of civil and military officials, high and low, has tended to make a mockery of the proclaimed policy of greater reliance on market forces.

Meanwhile, not only has unemployment almost certainly increased with the virtual stop on civil service and military recruitment, but the very necessary all-out effort at economy in government expenditure has severely hit social welfare services, such
as education, health, and housing. It would be unfair to say that the government has neglected them. In some branches, with international aid and technical assistance, a good deal is being done to raise standards. But financial stringency has certainly prevented an expansion of services in step with the growing needs of a growing population.

The country's educational system is in dire straits. The Sukarno era's achievement was the creation of a national system of primary education which has brought literacy to the majority of Indonesian children. Considerable strides had also been made in building up secondary schools and teachers' training colleges, and state universities were established in every one of the country's twenty-eight provinces. But the university program, in particular, far outdistanced available teaching resources, buildings, and equipment. With few exceptions, standards at the grossly overcrowded universities were and remain low. As in most other developing countries, moreover, secondary and tertiary education was geared mainly to produce white-collar workers and neglected technical and vocational training. The inflation years depressed teachers' salaries, and the government economy measures of 1966-8 made it still more difficult for schools and universities to cope with ever-growing numbers of pupils and students. Increased funds have been made available in the past year. Plans are now in hand for a thorough overhaul of the whole educational system. But reform on a scale to match the country's needs, in quality rather than in numbers, and for qualified and skilled manpower, will be a long haul.

Whether the distribution of income has become more unequal is much more debatable. With all the talk about socialism and equality under the 'Old Order', its effective policies had done little to produce a more just society. With expanding business in the past five years, and a deliberate policy of providing market incentives to producers, some have no doubt become richer. But the inequality that has aroused most resentment—disproportionate to its significance for overall income distribution—has been the enrichment of powerful individuals through corruption. This, too, has been nothing new in Indonesia. But a number of factors have made corruption the chief talking point of critics of the government and the Achilles heel of the régime. Among them are the key role of a number of generals at the head of government
agencies, such as the state oil enterprise and the rice procurement agency, which gave them access to large funds, and the absence of other issues in a period of political doldrums. Early in 1970, press criticism of corruption and student demonstrations assumed such dimensions that the president appointed a commission of four elder statesmen to inquire into the problem. The commission's report was outspoken and led to a series of government measures to limit opportunities for corruption and deal more effectively with offenders.

The two most serious problems which darken the economic future of Indonesia are the balance of payments, with no end in sight to Indonesia's dependence on foreign aid, and a rate of population growth which is still accelerating towards 3 per cent a year. The Suharto Government has at last reversed the calamitous Sukarno policy of discouraging birth control and has thrown its weight behind an official program of family planning. But with all the foreign help that is being offered and with more efficient administration than is likely to be forthcoming, this program can, over the next decade, at best hold back the acceleration in the rate of growth of Indonesia's population. Nor is there any prospect, in the light of decades of frustrating experience, that transmigration—government-assisted movement of people from Java to the outer islands—can make any impact on the problem of overpopulation on Java.

The crucial problem is no longer food but employment. While a very great effort is still needed to increase food production, the new high-yielding varieties of rice offer a reasonable prospect of expanding food supply for the foreseeable future at least in step with population growth. But the need for new employment opportunities, both for the unskilled urban unemployed and rural underemployed and for the graduates of high schools and universities, is growing every year more desperate. Only a further acceleration of economic development, including large-scale industrialisation, offers any hope of coping with the problem.

'New Order' Politics

For the past five years, Indonesia has been under an army régime. The army won out in a ruthless power struggle with the Communist Party and it dealt ruthlessly with its vanquished opponents, many of whom were killed; many more remain in prison camps.
But in power General Suharto has been very much less ruthless than a communist leadership would have been (by 1965 there was no other alternative) and in many respects less autocratic, and much less erratic, than his predecessor, Sukarno.

Suharto has been ruthless neither in silencing his critics nor in cleaning up corruption nor in dismissing redundant or incompetent officials nor in mobilising the country's resources of labour and capital. Partly no doubt with an eye to Western opinion, but at least as much in deference to a deep ideological commitment of most of the Indonesian intellectual élite and articulate public opinion, the army leadership has leant over backwards to maintain the forms of parliamentary democracy and a considerable degree of freedom of expression. The Indonesian press is raucous in its criticism of the government, and the intellectual and political atmosphere in Indonesia has little of the odour of fear and suspicion characteristic of dictatorships.

For five years the Suharto Government has laboured to clean up the mess left behind by Sukarno and to set the country on the road to economic progress. The régime has given economic recovery priority over everything else. It has consciously adopted a low posture in international affairs and accepted dependence on foreign aid and foreign investment. It has put off institutional and social reform, and has tackled the enormous economic job pragmatically and gradually, resorting neither to Sukarno's appeal to ideology and mass emotion nor to the communist combination of ruthlessness and indoctrination. But in doing so the régime has rendered itself doubly vulnerable.

On the one hand, having staked everything on its economic performance, it must deliver the goods. While much has been accomplished in the five years, progress has been slow. To survive, the régime needs to achieve a momentum of economic growth sufficient not merely to secure a perceptible rise in per capita income, to find employment for the growing workforce and to reduce the country's dependence on foreign aid, but also to find a sufficient surplus in the coming years for the most urgent needs of social welfare.

On the other hand, having committed itself to democracy and the restoration of civilian rule, the régime cannot count much longer on the relative political calm of the last few years. General elections were held in July 1971. While the procedures laid down
virtually assured the army régime of majority control in parliament and congress, the elections are likely to mark the beginning of a new and livelier phase in domestic Indonesian politics, a phase in which the approach of the 'New Order' to Indonesia's immense economic problems will be put to an increasingly severe test.

Postscript
The most important event in Indonesia in 1971 was the general election. The Golkar (Functional Groups) organisation which the government had brought into being as its new political base achieved a far greater success at the polls than even its lavish endowment with funds and frequently questionable methods of vote gathering had led observers to expect. The outcome greatly strengthened the régime's confidence in public support and in its own ability, with at last a firm majority in parliament, to push ahead its legislative reform program. A cabinet reconstruction still further emphasised the role of the government's economist advisers who now fill five key ministerial posts. Indonesia's standing as a member of the community of nations was acknowledged by the election of Mr Adam Malik as president of the United Nations assembly.

On the economic front, slow progress has continued. The balance of payments remains a worrying problem, with exports performing rather less well than in the previous year while imports run ahead. But, for the present, adequate foreign aid seems assured, since Indonesia does not seem affected by the decision of Congress to cut back American foreign aid. The price level has remained stable, despite a 10 per cent devaluation of the rupiah, and domestic and foreign investment activity is creating new jobs, though even yet probably not enough to match the growth in the work force.

A second five year plan, to begin in 1974, is now being prepared. While the first gave priority to agriculture, and particularly to rice production, the second is expected to allocate more resources to industrial and regional development and to social capital.
Trade Relations

In 1935 a young Australian economist writing about Australia's trade with the Dutch East Indies said optimistically:

We have a picture of two countries whose trade relations are largely complementary, each providing goods the other needs and cannot conveniently produce itself.¹

Yet now, more than thirty years later, Australia and Indonesia, two large neighbouring trading nations, hardly trade with each other. Indonesia takes less than 0.5 per cent of Australian exports and, except for oil, supplies less than 0.5 per cent of Australian imports. Similarly, in Indonesia's total foreign trade, Australia accounts for little more than 1 per cent of total imports and probably for less than 1 per cent of non-oil exports. In fact, it is hardly an exaggeration to say that bilateral trade between the two countries would be balanced but almost insignificant, were it not for the considerable purchases by the Australian subsidiaries of international oil companies from their Indonesian sister organisations.

The situation is further highlighted by contrasting Indonesia with Malaysia and India as Australian trade partners. Australia's trade with India has declined in the past twenty years while her trade with Malaysia has grown substantially. But trade with both these more distant countries has generally been five to ten times as large as (again excepting oil) with Indonesia.

Why is this so?

The contrast with India and Malaysia suggests one possible explanation. Australia and Indonesia, although neighbours, were parts of two different colonial empires. Government policies, business interests, and personal links had over a century geared their economies to those of the metropolitan countries and in

¹ First appeared as 'Trade Relations between Australia and Indonesia', in Economic Record, June 1968.
Australia's case to sister colonies, rather than to outsiders however close by. Many of these links survived the severing of political ties with independence. In other words, expansion of trade between Australia and Indonesia has had to overcome the obstacle of former membership of different politico-economic blocs.

There is no doubt something in this explanation. Its significance does not derive from legal barriers to trade. At the Australian end, Commonwealth tariff preferences have, with quite minor exceptions, ceased to confer any significant advantage on Commonwealth countries competing with Indonesia in the Australian market. Similarly, there is no suggestion that Indonesia has, in her import licensing and other commercial policies, discriminated in favour of the Netherlands. The explanation, such as it is, derives on both sides from other factors.

On Australia's side, historical associations among branches, customers, or suppliers of the same British firms, common banking, shipping, and other services, community of language, laws, and trading practices, all these have made the former British countries of south and southeast Asia easier for Australian firms to trade with than Indonesia. A few years ago, a former Australian Assistant Trade Commissioner contrasted 'the apparent lack of general interest of Australian exporters in Indonesia' with 'the many exporters who continually are wending their way to Singapore, Malaya, Hong Kong and other well known markets'.

Conversely, many threads still link Indonesia with Holland and through Dutch connections with Western Europe—threats of sentiment and language, of traditional business connections, of familiarity with brands, trade marks, weights and measures, customs and styles. Without any deliberate discrimination by Indonesia in her imports of manufactures, her traditional suppliers also enjoy an inevitable advantage over newcomers, through established consumer tastes in the case of consumption goods and through specifications for replacement and spare parts in the case of capital goods.

Nonetheless, any attempt to explain the lack of trade between Australia and Indonesia primarily in terms of their historical association as ex-colonies must remain unconvincing. There have been very large changes in the directions of trade of both countries since the early post-war years. Trade with the metropolitan country has declined dramatically in both cases. In Australia's
case, the shift in export trade has been towards Japan and other Asian countries and in import trade towards the United States, Japan, and Western Europe. In the case of Indonesia, the shift has also been towards Japan and was, at least until 1965, towards the communist countries.

Clearly, historical associations have not prevented major changes in the pattern of trade. But the changes that have occurred have not, so far, been such as to favour bilateral trade between Australia and Indonesia. The basic fact is that, contrary to first appearances, the Australian and Indonesian economies have not in the past been strongly complementary and their economic development since World War II has done little to alter this situation.

Australia's traditional exports are temperate zone foodstuffs, such as wheat and flour, meat, dairy products, and fruit; industrial raw materials, such as wool and non-ferrous metals, especially lead and zinc; and sugar. With two minor exceptions, none of these has ever figured significantly among Indonesia's imports, while one of them (sugar) used to be one of Indonesia's major export commodities. The exceptions are flour and dairy products. For both of these, the Dutch East Indies used to be a significant market. But the consumers were mainly the Dutch. Since independence, and more especially since the departure of the Dutch after 1957, Indonesian demand for Australian foodstuffs, with the partial exception of flour, has become a luxury consumption demand. As such, it has inevitably suffered from a low priority rating under import licensing or foreign exchange controls.

The position is more favourable in the other direction. In addition to oil, which in the past twenty years has been both Indonesia's most important single export and Australia's most important single import, Indonesia exports a number of tropical products which Australia imports in significant quantities, especially rubber, coffee, tea, tobacco, copra, and palm oil. But all of these together account for only a small and diminishing part of Australia's import bill.

Australia's seven main groups of export commodities (wool, wheat and flour, meat, dairy products, sugar, fruit, non-ferrous metals) which between them accounted for 68 per cent of Australia's export earnings in 1963-4 represented only 3 per cent of Indonesia's imports in the 1950s and less than 2 per cent in the
early 1960s. Indonesia's seven main export commodities other than oil (rubber, tea, coffee, tin, copra, palm oil, tobacco) which accounted for 85 per cent of non-oil exports (and 55 per cent of total exports) represented less than 3 per cent of Australian imports in 1963-4. (Oil, crude and refined, represented another 10 per cent.)

Looking at the same problem the other way, we find Australia's imports, apart from oil and tropical products, consisting almost wholly of manufactures which Indonesia cannot yet produce, let alone export; and Indonesia's imports consisting of textiles, rice, capital equipment and industrial materials, such as yarn, steel, fertiliser and cement, none of which has been a major Australian export in the past though some may be in the future.

Indonesia and Australia, in other words, have not in the past twenty years been 'natural' trade partners. Both have, in the main, exported primary products and imported manufactures. And while they have not generally been competitors in world trade, neither has the structure of their trade—with the major exception of oil—been complementary. The basic reason for lack of substantial bilateral trade is therefore the same as between Australia and India. Between Australia and India a modest volume of two-way trade has nonetheless been maintained mainly on the basis of two features not present in the Indonesian case—India's capacity to produce textiles for export and to consume substantial quantities of wheat. Indonesia has maintained a similar volume of trade only one way, on the basis of her oil industry.

Upon the obstacles to trade arising from historical dissociation and lack of structural complementarity of the two economies, special obstacles to trade were superimposed in the years of Indonesia's political and economic troubles after World War II, and especially in the latter years of the Sukarno régime—declining capacity to produce, chronic balance of payments difficulties, inadequate shipping, banking and other trading facilities, declining credit standing, deficient government administration and business management.

**Australian Exports to Indonesia**

Before the war, flour and butter accounted for three-quarters of Australia's exports to the Dutch East Indies. The rest consisted of other foodstuffs, mainly for European tastes, such as preserved
milk, biscuits, fresh fruit, wines, and trifling quantities of such items as coal, leather, soap, drugs. Australian exports to independent Indonesia have been even less broadly based. Through most of the 1950s they were sustained almost entirely by quite substantial sales of flour. When these fell away after 1957, the decline was partly compensated by increased exports of manufactures. But only part of this increase was genuine trade; much of the export of machinery, roadmaking equipment, vehicles, etc., shown in the trade returns represented Australian aid.

Australia's flour trade with the Indonesian islands goes back to 1908. It was pioneered by a Melbourne flour miller, V. Y. Kimpton, who in that year travelled through southeast Asia looking for export markets. In the inter-war years, sales were built up to over 100,000 tons a year. The flour trade became the mainstay of regular shipping services between Australia and Indonesia provided by the Dutch K.P.M. and the Australian Burns Philp lines.

When trade resumed with Indonesia after the war, Australian exports of flour quickly revived. They reached a peak in 1955-6 of nearly 180,000 tons, valued at $A11 million (f.o.b.) and accounting for over one-quarter of total Australian exports of flour. After 1957 the Indonesian market for Australian flour shrank and almost disappeared until 1967. It was given a big lift in September 1967 by large purchases with the use of Australian BE (Export Bonus) credit.

The departure of the Dutch from Indonesia probably played some part in the shrinkage of the market. But unlike some of the other foodstuffs traditionally bought from Australia, flour had a wider market among the Chinese population (chiefly for noodles) and among middle-class Indonesians (for bread and cake). Indeed, for some years, the Indonesian Government encouraged the consumption of flour as an alternative to rice. Flour ranked for a while as an essential commodity for exchange control purposes. The Indonesian authorities also co-operated in an Australian promotion effort in the form of a 'technical assistance' mission of Australian bakers to demonstrate baking in Indonesian cities. But foreign exchange difficulties gradually throttled the trade. Australia also complained about inroads into its Indonesian market for flour by American PL 480 (commodity aid) supplies and by subsidised sales by France and Italy.
In 1957 Australian government and trade representatives visited Indonesia to counter this competition and negotiations for a trade agreement were begun. The agreement, which was finally signed in December 1959, did in fact, as its main item, contain an undertaking by the Indonesian Government 'to work towards ensuring a greater predictability in the flour trade'. But the agreement did nothing to maintain the trade in the face of the growing shortage of foreign exchange.

The 1959 trade agreement (which was renewed without change in 1963 and again in 1966) had attached to it two lists of goods and commodities in which each partner declared itself to be interested in expanding exports to the other. The Australian list contained, apart from the traditional foodstuffs and non-ferrous metals, a range of manufactures, such as steel products, industrial chemicals and pharmaceuticals, building materials and builders' hardware, motor vehicles and parts, industrial and agricultural machinery, railway equipment, and radio, telecommunications and electronic equipment. Sporadically over the past ten years, Australia has made export sales to Indonesia in all these categories.

General Motors-Holden began in 1958 to deliver completely knocked-down Holden utilities to an Indonesian-owned assembly plant in Surabaja. Despite difficulties, especially in 1966, this trade has continued and promises to increase even if the ill-conceived notion of buying 150 Holden cars for Indonesia's MPs had to be abandoned under pressure of student protests. Australia's major steel companies, BHP and Lysaghts, have found in Indonesia a market for some steel products, BHP mainly reinforcing rods for ferro-concrete construction, Lysaghts mainly sheet steel (for roofing and as a raw material for canning plants). Australian Carbon Black, an Australian subsidiary of the American United Carbon, in 1963-5 developed sales of carbon black to the government-owned tyre company in Djakarta. Other examples of commercial exports of Australian industrial products to Indonesia are sales of stearic acid (used in rubber processing), agricultural materials (insecticides, fungicides), and recently also other chemicals (detergents, polythene, solvents) and some fertiliser. The official statistics also show exports of communications equipment, agricultural machinery, and roadmaking equipment. But these, like a considerable part of the exports of commercial
vehicles, have been gifts under Colombo Plan projects, aid rather than trade.

The main reason for Australia's failure to find a significant export market in Indonesia has certainly been that Australia's traditional exports have been raw materials and foodstuffs which Indonesia either has not needed at all or has given a low priority in the allocation of scarce foreign exchange, while the goods which Indonesia has needed most—manufactures, both consumer and capital goods, and such commodities as rice and cotton—Australia has in the past generally not been able to supply.

In recent years, this has begun to change. Australia has become an actual or potential exporter of a wide range of industrial products. But as a potential market for Australian manufactures Indonesia has well illustrated the difficulties which a newcomer faces in trying to sell manufactures abroad in competition with the established major industrial countries.

One has simply been lack of interest and experience in exports among Australian manufacturers. It was not until about 1960 that any considerable number of Australian manufacturing firms, under the stimulus of financial incentives and prodding provided by the government, began to take a serious interest in developing exports to southeast Asia. Until recently, no Australian manufacturing firms had their own agents or representatives in Indonesia. They sold through Australian trading firms, like H. C. Sleigh & Co., or sometimes through agents in Singapore. If, as was (and still is) frequently the case, they were subsidiaries of international companies, they could break into the Indonesian market only if they could persuade their parent companies to grant them export franchises or allocate to them the Indonesian market for some of the groups' products.

There is some reason to believe that Australian firms were more easily discouraged than their more experienced Dutch, German, or Japanese competitors by the almost incredible difficulties of trading with Indonesia in the latter years of the Sukarno era: constant changes in import licensing and exchange control regulations; time-consuming and costly dealings with officials; unreliable shipping, congested ports, losses through pilfering, declining efficiency, and growing demands for credit on the part of Indonesian exporters. The latter two problems became particularly serious
in the last phase, as the state trading corporations which had succeeded the former Dutch trading houses proved increasingly inadequate to their task and as domestic bank credit became virtually unobtainable or prohibitively expensive.

Australian manufacturers have frequently claimed to be handicapped in international competition with competitors from the major industrial countries because of the latter’s superior ability to offer liberal supplier’s credit and to secure markets for capital goods through direct investment. It is doubtful whether this has been relevant to Indonesia in recent years where private foreign long-term capital has been unwelcome. Nor is there any reason to believe, as is sometimes suggested, that Australian exports to Indonesia have been hampered by inadequate export credit insurance facilities. Government aid to Indonesia, on the other hand, has been an important influence in securing access to the Indonesian market for the products of the donor countries. This applied to virtually all the project aid granted by Western and communist countries before 1965 and again conspicuously to the balance of payments aid granted in the form of tied BE credits by the creditor countries of the ‘Tokyo Club’ in 1967. Although half the first tranche of the Australian BE credit was used to buy once again Australian flour, the other half led to orders for a wide range of Australian manufactures which, in the opinion of the firms concerned, they could not have secured in any other way and which, by making their brands known in Indonesia, were expected to establish them in the market and bring in their train commercial orders. Whether the cost of such aid to the taxpayer can be justified on one ground or the other, to the private exporter it is in any case welcome as costless sales promotion.

**Indonesian Non-Oil Exports to Australia**

If the special case of oil is left on one side, Indonesia’s export trade with Australia presents much the same picture as Australia’s with Indonesia: a small volume of trade recovering for some years after World War II but declining after 1957 and throughout dominated by one commodity, in this case tea.

Apart from oil, Australia has never yet been more than a minor market for a few of Indonesia’s staple export commodities. Before the war, Australia obtained from the Dutch East Indies about two-thirds of her tea imports, one-third or more of her coffee, one-fifth
of her rubber, almost all her kapok, and a little tobacco together with small quantities of such other tropical products as spices, sisal, gums and resins, bamboo and rattan. But for none of these export commodities was Australia a major market, her largest share in total Dutch East Indies exports being about 20 per cent in the case of tea.

In broad outline, the position remained the same in the post-war years. Tea only partially recovered the ground lost during the war and slipped back after 1957. But with most other commodities doing even less well, tea dominated the scene more than ever. In the last five years, it has accounted for almost three-quarters of the total trade.

Historically, the most important reason for Australia's relative insignificance as an Indonesian market is undoubtedly the orientation of each of the two colonial economies towards its metropolitan market, together with other countries of Western Europe in the case of Indonesia and other parts of the British Empire in the case of Australia. Generally speaking, it would not have occurred to Dutch exporting firms to look actively for markets in Australia or to Australian importing firms to search actively for supplies from the East Indies. After Ottawa, Commonwealth tariff preferences tended to strengthen this pattern but there is no reason to believe that they have ever constituted a significant obstacle to Indonesian exports to Australia.

Three sets of circumstances have combined to prevent any lasting improvement in this historical pattern. One was the complete cessation of trade for almost a decade of war and post-war political upheaval. During those years, Australia switched to alternative sources of supply. Some Indonesian exports, especially tea, tobacco, and rubber never regained the ground thus lost.

The second was a series of shifts in Australian demand, due to changes in taste and technology, all adverse to Indonesian export commodities. There has been a shift from tea to coffee in Australian drinking habits with the increase in the proportion of people with continental habits and the invention of instant coffee. Since the pre-war years imports of coffee have increased sevenfold in volume while imports of tea have risen by only about 30 per cent. For various reasons—the lower quality of Indonesian robusta coffee, export quotas under the international coffee agreement and Australian preference for Papua and New Guinea—
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Indonesia has so far derived little benefit from the expansion of Australian coffee imports.

Technological changes have also tended to depress the Australian market for kapok (increasingly replaced by the inner spring mattress), for resins for paint manufacture and for sisal for ropes and fibroplaster (both increasingly replaced by synthetics). Australia has also ceased buying rubber and rattan (for wicker furniture) direct from Indonesia. But both the rubber imported from Singapore and the processed rattan imported from Hong Kong are believed to originate largely in Indonesia. To this extent, Australia is a more important export market for Indonesia than the statistics suggest.

The only new exports for which Indonesia developed a market in Australia in the 1950s to offset those adverse trends were molasses, palm oil, and timber. But shipments of molasses ceased after 1961 and of palm oil after 1963. Timber exports have so far been very small.

The third set of factors which undoubtedly played some part in the stagnation of Indonesian exports to Australia, though just how much it is in the nature of the case impossible to say, has been the decline in Indonesia's capacity to export. With the exception of copra, none of Indonesia's major (non-oil) export commodities ever regained its pre-war level of production or export after the war. Total exports of most of them fell steadily and calamitously in volume and price for most of the 1960s.

There is no way of telling how far Australian imports from Indonesia have been held down by supply difficulties. A larger capacity to produce or export would have made little difference in the case of commodities like rubber where Australian demand could at best have been affected through a lower world price. Nor would a larger output have helped Indonesia, where technological changes were making her products obsolete, as with kapok and sisal, or where exports were restricted by international agreement, as in the case of coffee. But where Indonesia directly competed with other countries in the Australian market inability to maintain supplies, or to supply more or more reliably, was probably often decisive. This clearly was the reason why the promising export trade in molasses and palm oil came to an end. Increasing failure on the part of Indonesian exporters during the early 1960s to maintain regular and prompt deliveries of tea are believed to
have been an important factor in inducing Australian import firms to turn to Ceylon and other alternative suppliers.

Shipping
One aspect of trade between Australia and Indonesia that deserves a few paragraphs of comment is shipping. Proximity reflected in lower transport costs, is, after all, the most obvious reason for expecting close trade relations between neighbouring countries.

In this as in most other respects, conditions deteriorated in the post-war years. During the 1930s, shipping facilities between Australia and the Dutch East Indies were described as 'fairly satisfactory'. Two shipping lines, the Dutch K.P.M. and the Australian Burns Philp, each provided regular monthly services both ways. The K.P.M. called at all major Indonesian ports and from them provided efficient facilities for transhipment to inter-island shipping. Freight space was generally adequate, but freights were high, mainly because the volume of dry-good cargo on the south-bound voyage was too small.

In the 1950s, after the exclusion of Dutch ships from Indonesian ports, shipping services between Australia and Indonesia were provided for some years by members of the Australia-Malaya shipping conference—mainly British lines—operating as the Australia-Indonesia conference. Declining volume of cargo offering, increasing delays and losses in Indonesian ports, and finally 'Confrontation', put an end to the service early in 1964. For some months the Blue Funnel Line put on a six-weekly service but abandoned the attempt under pressure from the Indonesian Government. From then until early 1967, the Indonesian government line, Djakarta Lloyd, provided the only liner service to Australia, but even this gave rise to increasing complaints. The Australia-Indonesia shipping conference continued a nominal existence but did not operate.

Since 1967 there has been a considerable improvement in shipping services. In addition to a regular monthly Djakarta Lloyd service, the Austasia Line (a subsidiary of the British Blue Star Line) began a monthly service from Australia to Djakarta in January 1967 and the Pakistan National Line has provided services to several Indonesian ports if sufficient cargo is offered. The Blue Funnel Line, too, has been willing to pick up cargo to Indonesia when available. Large consignments such as shiploads
of flour are usually carried in charter ships, mainly Hong Kong registered tramps. In the reverse direction, Djakarta Lloyd retains a monopoly enforced until last year by an Indonesian government regulation requiring Indonesian exporters to ship by the national line.

Complaints that trade between Australia and Indonesia was being hampered by inadequate shipping services have become less common. Except during the short period of heavy Indonesian imports financed by Australian BE credit, shipping space on the Australia-Djakarta run has generally been more than adequate for the cargo offering. With the improvement in Indonesian port conditions, transit delays have also been reduced. Freight rates are rather high and while in general high freight rates have been the least of the shipping worries of those engaged in Australian-Indonesian trade in recent years, they may have some importance in relation to Australian manufactures. For most of these no special conference rates have yet been negotiated and they therefore attract the high 'general cargo' rates. In fact, as in the case of exports to Singapore, Australian manufacturers are believed to have no advantage in lower transport costs over British or continental European competitors in the Indonesian market, the advantage of the much shorter distance being offset by higher freight charges per ton-mile. But whereas in the case of the Australia-Singapore trade the volume of trade is sufficient to justify modernisation of ships and handling methods which would bring down freight rates, this is not at present the case in trade between Australia and Indonesia.

This is the crux of the problem. By far the most important reason why trade between the two countries does not enjoy the benefit of reliable and cheap shipping services is that there is not enough of it. The fact that Australia's main import from Indonesia, oil, is carried in tankers while large-volume dry cargo such as flour is liable to be shipped in chartered tramps further reduces the flow of cargo offering for liner services. On the other hand, trade between the two countries has an advantage in that Indonesian ports lie on the main shipping route from Australia to Singapore; a relatively small flow of cargo is sufficient to attract shipping provided it is reasonably regular. For this reason, Australian-Indonesian trade has probably more to gain from an improvement in the present indifferent service on the Australia-
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Singapore route than by any other practicable improvement in shipping facilities. In both directions, there may be scope for ‘developmental’ freight rate reductions on new or potential exports. Outside competition such as that offered by the Pakistan National Line is likely to benefit shippers. On the other hand, flag discrimination regulations, such as those in force until recently in favour of Djakarta Lloyd, probably hamper rather than help trade, even in the long run. With some reservations, it is safe to assume that, between Australia and Indonesia at least, shipping will readily follow trade.

Oil

Paradoxically, most accounts of Australian-Indonesian trade never mention, or dismiss in a sentence, the largest and in some ways most important component, Australia’s imports of Indonesian oil. The explanation is no doubt that those imports have for the most part taken the form of internal transactions among the Australian and Indonesian subsidiaries of the major international oil companies. In Indonesia especially—and since discussion of trade policy always concentrates on exports it is in relation to Indonesian trade that one would be more likely to find the oil trade with Australia discussed—the oil industry has tended to be treated as set apart from the rest of the economy, an enclave of the foreign oil companies or an imperium of the army. The fact that the foreign exchange proceeds from oil exports have only partially, if at all, accrued to the national government has reinforced this tendency.

Yet trade in oil has in magnitude quite overshadowed trade in other products between the two countries. Australian imports of oil have in most of the past twenty years been ten times as large as all other imports from Indonesia put together, and also about ten times Australia’s exports to Indonesia. During most of this period, Indonesia has been the source of about one-quarter of Australian oil imports and Australia has, as it happens, also been the market for one-quarter of Indonesia’s oil exports. During the 1950s when oil accounted, on average, for 11 per cent of Australia’s total import bill, nearly 4 per cent represented oil imports from Indonesia.

The oil trade between the two countries goes back to the first years of the present century. Oil had been produced in the Dutch
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East Indies from about 1890. In 1901 a Shell subsidiary was set up in Australia to import and distribute Indonesian kerosene; and before 1914 Shell had begun to import Indonesian motor spirits. In the decade before World War I, Australia imported about one-half of its modest petrol requirements and about 10 per cent of its kerosene and other mineral oils from the Dutch East Indies. All the rest, except for some lubricating oil of Russian origin, came at that time from the United States.

Until Australia began to build her own refinery industry in the 1950s imports consisted almost wholly of refined products. Throughout the inter-war years, the refineries in the Dutch East Indies supplied about one-half. The other half continued to come mainly from the American west coast until the Persian Gulf began to make significant contributions in the mid-1930s. The Japanese occupation cut off all supplies from the East Indies in 1942, compelling Australia to rely almost wholly on Middle East oil for the next seven years. Since 1949 when the Indonesian refineries resumed production, they have supplied about one-quarter of Australia's imports of refined products. With the shift to local refining in Australia during the 1950s, the proportion of oil imported in the form of refined products has of course greatly declined. But Indonesia has in turn become a major supplier of crude oil for Australian refineries. While Indonesia's share in Australia's reduced imports of refined products diminished greatly in the years 1960-6, her share in the Australian market for crude oil was well maintained and even increased a little.

In general terms, the Indonesian-Australian oil trade of the past sixty years has been a simple case of natural complementarity: Indonesia as a major oil producer has been the nearest source of supply for Australia as a major net importer. In detail, the pattern of trade has been determined from time to time by the interaction of a variety of technical and economic factors.

Until close to World War II, the dominant fact was that the Indonesian oil refineries were the only large refineries in the eastern hemisphere and that their owners were among the largest distributors of petroleum products in Australia. While the Caltex group, H. C. Sleigh, and (just before the war) the new Australian Ampol company imported mainly from the United States, the Royal Dutch-Shell group obtained its supplies for the Australian
The development of Australia's own refinery industry during the 1950s has reduced imports of refined products to a few categories such as power kerosene for tractors and aviation petrol for planes still using propeller engines. A declining market has not warranted the creation of domestic refining capacity. A fair proportion of those still come from Indonesia. But much of the larger part even in value terms of Australian oil imports in the past decade has consisted of crude oil. Here the relative shares of the main oil producing areas in the Australian market have to a considerable extent been determined by historical accident.

Some of the largest Australian refineries have been built by groups such as British Petroleum (the former Anglo-Iranian) which have no interests in Indonesia or groups such as Shell and Stanvac which have had their own refineries in Indonesia and whose Indonesian crude oil production has not in recent years been sufficient to yield a significant surplus for export. Their Australian refineries have been designed to use Middle East crudes (and in the case of Shell also its own crude from North Borneo). Caltex, on the other hand, designed its Kurnell (Sydney) refinery for crude oil from its productive Minas field in Central Sumatra. Minas crude bought from Caltex (Indonesia) is also used in its Brisbane refinery by Ampol (which used to buy its refined products from Caltex in Australia) and in small amounts by the Mobil-Esso (former Stanvac) group in its refinery at Altona, Melbourne. Under processing contracts, the Caltex (AOR) refinery at Kurnell also refines Minas crude for Esso and H. C. Sleigh. In the last few years, all the refining companies have been required by law to use a small quota of Australian crude oil from the Moonie field.

How much crude oil Indonesia sells to Australia depends, therefore, in the short run, almost exclusively on the turnover of the three distributing companies in Australia which use Minas crude, Caltex, Ampol, and H. C. Sleigh. Quality differences between the various kinds of crude oil are such that a refinery designed for one cannot, without considerable expense, be adapted to another. (Thus, Middle East crude requires special desulphurising equipment, Indonesian crude special wax extraction...
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plant.) Nor is there much scope for blending of both kinds. Price plays little if any part. Under the system of basic-point pricing evolved by the international oil companies, the landed price in Australia of crude oil from whatever source is calculated, allowing only for differences in quality, on the basis of the posted price at the Persian Gulf plus average freight costs from there. In principle, therefore, the Australian refining company derives no benefit in price from its greater proximity to and lower transport costs from Indonesia. The 'geographic advantage' accrues wholly to the Indonesian supplying company. In practice, this broad principle has been subject to two qualifications. On the one hand there has been more than a suspicion that at various times the prices charged by the international parent companies to their Australian subsidiaries have been inflated so as to minimise tax liability in Australia. In recent years, pressure by the Australian taxation authorities is believed to have substantially eliminated this practice. On the other hand, the prices actually paid for crude oil have, especially in the conditions of world excess supply since 1961, frequently been reduced well below posted prices by discounts. But these qualifications do not affect the conclusion that price has not significantly influenced the choice of imports of crude oil by Australian refining companies, and therefore the volume of imports from Indonesia.

Available information suggests that there has never been any direct business contact between the Australian importing and the Indonesian exporting oil companies, even where they were subsidiaries of the same international companies. The Australian subsidiaries, such as Shell, Caltex, Mobil, and Esso would typically place their orders with their parent companies, while independent Australian companies such as Ampol or Sleigh would deal either with the Australian subsidiary or the overseas parent organisation. This, one gathers, remains as true of present purchases of crude oil as it was earlier (and still is to some extent) in relation to imports of refined products. Payment is made in New York or London, the foreign exchange proceeds of the Indonesian exports to Australia being presumably credited to the Indonesian company in its intra-company accounts with its American or Dutch-British parent company.

At the Indonesian end these foreign exchange proceeds have never played quite the same role as other foreign exchange earned
by Indonesian exports. In the first place, Indonesia’s oil exports have always had a considerably higher ‘foreign exchange content’ than her other major exports. For some years for which estimates are available, the oil industry’s net earnings in foreign exchange, after deducting foreign exchange costs of imported materials and equipment, and of dividends remitted to foreign parent companies, were only 20 to 40 per cent of gross receipts. Secondly, it is generally believed that, at least until 1967, even the Indonesian Government’s share in the profits of the oil industry never reached the central government, whether as a contribution to its foreign exchange reserves or to its budget. They appear to have been retained by the Ministry for Oil Affairs for its own requirements or that of the government oil undertakings and after 1965 also for the needs of the armed forces. This of course does not mean that the foreign exchange earned was altogether lost to Indonesia. But some of the foreign exchange expenditures financed under such a régime would hardly have survived an assessment of national priorities.

**Future Prospects**

Our survey of the past history and present condition of trade between Australia and Indonesia is not encouraging. Except in the rather special case of oil, the two large neighbouring economies have not hitherto found much scope for bilateral trade. The main reason has been that, hitherto, the structure of their foreign trade has not been markedly complementary. Australia’s main exports have not been among Indonesia’s main imports, and vice versa. This basic lack of complementarity was aggravated in the earlier colonial history of the two countries by the tendency for their trade to be oriented to the metropolitan country and in recent years by the general economic deterioration in Indonesia.

What of the future?

By a peculiar irony there is every reason to expect the next decade to witness the virtual disappearance of what has hitherto, as we have seen, been by far the largest part of bilateral trade between the two countries, the trade in oil. The recent oil discoveries in Australia make it very likely that by 1975 Australia will be self-sufficient in crude oil. Of course, Australia will probably continue to import some crude oil, just as she has continued not insignificant imports of refined products in recent years. But
one can only assume that Australia's importance as an export market for the Indonesian oil industry will greatly decline.

On the other hand, it is doubtful whether this need cause much concern in Indonesia. Not because of any misguided notions that oil exports do not matter to the Indonesian economy—the integration of the oil industry into the national economy is one of the tasks of rehabilitation of Indonesia from the ravages of the Sukarno era—but because Indonesia should have little difficulty in finding foreign markets for all the oil she can produce and spare from her rapidly growing domestic demand. Japan, in particular, but also other countries in south and east Asia are likely to be net importers of oil on an increasing scale for any foreseeable future.

The prospects for Indonesia's other traditional exports in the Australian market look little better. Most of them, as we saw, face adverse changes in taste or technology. Some others carry the additional handicap of preferential treatment for a direct competitor in the Australian market, Papua New Guinea. This applies especially to the prospects for increased sales of Indonesian coffee in Australia. Efforts are also under way to expand production of tea in New Guinea, but here Indonesia suffers from no disadvantage in quality; sales in Australia could, it is believed, be considerably increased if Indonesia could assure regular and prompt delivery.

Do any new export industries hold out better promise? In the long run, Indonesia, like other large and over-populated developing countries, must industrialise and will no doubt develop manufacturing industries which can compete in export markets. But Indonesia's industrial development is so much behind that of India and most other countries of south and east Asia that there is no prospect of this in the next few years. Nor can the handicraft industries of Indonesia be expected to earn much foreign exchange, even with the help of their recent exemption from all Australian tariffs: the market is too small and marketing costs too high.

The three new export industries which are generally believed to offer the best prospects for Indonesia in the next 5 to 10 years are minerals, timber, and tourism. Australia may be a customer for at least one or two minerals, such as tin and perhaps sulphur, and could certainly become a major buyer of timber and tourist
services. But all three industries must first be developed. The capital and enterprise needed are not available in Indonesia. At least in the case of minerals and timber, they are most likely to be provided by countries like Japan which wish to assure themselves of raw material supplies. It is doubtful whether such direct investment for import supplies will for some time yet attract much Australian capital. Tourism which, besides reasonable political stability, needs only air and hotel services has the best chance of becoming a major foreign exchange earner from Australia.

The need to develop new export industries applies as much to Australian exports to Indonesia as to Indonesian exports to Australia. Flour is a possible exception. During the food crisis of September 1967, it was Australian flour rather than Australian manufactures that attracted the bulk of demand for Australian Credit BE. Even if Indonesia became self-sufficient in rice, she will have a continuing demand for wheat and wheat flour which Australia is well placed to supply. But if the present effort at rehabilitation of the Indonesian economy is successful and leads on to a reasonable rate of economic development, Indonesia's import requirements will be overwhelmingly for industrial products, raw materials, and capital equipment. Not least important among these will be the inputs needed to expand agricultural production, fertiliser, chemicals like insecticides, and agricultural machinery; and equipment for basic industries, such as road and rail transport, communications, shipping, ports, power, and irrigation. Australia's manufacturing industries should be capable of supplying many of these needs.

How effectively Australia will in fact be able to compete with the major industrial countries is another question. In markets in the developing countries, Australian manufacturers labour not merely under the handicaps of all newcomers, such as lack of experience, contacts, established brand names, and traditional business connections, and a relatively small domestic market as a base for exports, but also under the handicap, diminishing but still significant, of restrictions on export franchises imposed by overseas parent companies, and above all under the difficulties which flow from the developing countries' chronic shortage of foreign exchange. Inevitably these countries give preference to suppliers prepared to sell on private or government credit. At the present time, and for many years to come, this applies to Indo-
nesia more than to most. To a considerable extent, those countries can sell to Indonesia which are prepared to give government aid or undertake direct private investment.

The dilemmas arising from the relationship between aid and trade are not peculiar to Australia. Exports financed by grants or unrepayable loans may yield profits to private exporters but are hardly an economic proposition to the exporting country. But aid-financed exports may open markets to commercial exports. In any case, aid may be desirable on grounds quite unconnected with export promotion. In relation to Indonesia, the fact that there are widely thought to be particularly strong non-economic arguments for aid in Australia's own enlightened self-interest may give Australian trade a slight advantage in these respects.

In direct private investment, on the other hand, Australia starts well behind scratch. It is only in the last few years that Australian industrial firms have taken any interest in extending operations to other countries and that government policy has looked on such overseas investment by Australian companies with a more kindly eye. In Indonesia there is still only one modest example of direct investment by an Australian manufacturing firm, though one or two others may be in the offing. Yet the market for imported capital equipment and materials in Indonesian industries will for some years to come consist very largely of the demand created by direct investment of overseas capital, and the orders will largely go to the investors.

Finally, it need hardly be stressed that Australia's prospects for export trade with Indonesia depend upon Indonesia's economic and political future. They will prosper if Indonesia prospers and maintains an open trading system. They will stagnate if Indonesia fails to rise from her present economic nadir or if another turn of the political wheel leads her once again to subordinate her trade to political and ideological considerations.

Postscript
This essay, written early in 1968, is several shades more pessimistic in tone than one would write it now. The Indonesian economy has performed better than even sympathetic observers dared hope four years ago. With the improvement in economic conditions in Indonesia, the interest of Australian firms in Indonesia, both as traders and as investors, has quickened, and trade
between the two countries has, with one exception that was predictable in 1968, grown quite rapidly.

Australian exports to Indonesia have tripled in value in the past four years, from $A14 million in 1967/68 to $A39 million in 1970/71. They included in the latter year a wide range of manufactures, such as motor vehicles and parts ($A7 million), machinery ($A5 million), iron and steel ($A2.4 million), chemicals ($A2.5 million), building materials ($A1.2 million) and many others. Moreover, the proportion of exports that is aid financed has declined. BE aid increased only a little, from $A4.8 million in 1967/68 to $A5.2 million in 1970/71. Allowing for commodity aid and the export component of project aid, commercial exports appear to have risen from about $A9 million to $A26 million. As Australian products are becoming more widely known in Indonesia, a significant commercial market is developing.

Australian imports from Indonesia (other than oil) have grown less rapidly, from $A3 million to $A7 million, and more than two-thirds are accounted for by one commodity, tea. At the same time, with the development of Australia's own crude oil production, oil imports from Indonesia have fallen off sharply, from $A52 million in 1967/68 to $A16 million in 1970/71. The fall has not been as drastic as seemed likely in 1968 when optimistic forecasts suggested that Australia would be self-sufficient in crude oil by 1975. Unless exploration proves a good deal more successful than it has been in the past few years, this now seems unlikely, and for some time yet oil imports will remain by far the largest single item in trade between the two countries. But for the reasons explained in the essay, this is not as useful to Indonesia as would be a more substantial expansion of her Australian market for other products.

The investment picture is a good deal more exciting than it was in 1968. There are now over thirty Australian companies operating in Indonesia, in various branches of manufacturing, mining exploration, and service industries, and many more are actively interested in investing there. The formation, late in 1971, of an Australian-Indonesian Business Cooperation Committee to which some 100 Australian firms are affiliated and which is expected to be followed shortly by a corresponding Indonesian-Australian Committee in Djakarta reflects a new mood in business relations between the two countries.
When all this is said, however, the basic facts presented in the essay remain. Indonesia's share in Australia's exports remains less than 1 per cent and in imports, even including oil, only just over 1 per cent. Australia's share in Indonesian foreign trade is about 2 per cent in both directions. Virtually the whole of the notable increase in Indonesian exports in the past four years has consisted of primary products, raw materials, and foodstuffs, for which the major industrial countries, and especially Japan, have been the natural markets. And Indonesia's requirements for capital goods and other manufactures are met in the main by the same major industrial countries which are also the chief suppliers of aid and direct investment capital. In 1970, Australia's contribution to IGGI aid to Indonesia amounted to only 2½ per cent of the total, and the share of Australian investment projects in total intended investment under approved foreign investment projects was under 1 per cent.
Australian Aid

Indonesia is now the largest recipient of Australian foreign aid, accounting for well over one-third of all Australian bilateral aid (excluding net expenditure in Papua New Guinea). Indonesia's pre-eminence in Australia's current foreign aid effort reflects the political importance attached to Indonesia in Australian official thinking and accords with the sentiment of the Australian public which, as widespread voluntary aid activities show, has today more goodwill towards Indonesia than towards any other Asian country. Even the keen interest of many Australian business firms in the potentialities of investment in Indonesia, while undoubtedly motivated and circumscribed by business considerations, owes a good deal to this sentiment.

Yet the story of Australian aid to Indonesia since the early days of the Republic is rather a sorry tale, of a trickle of projects and technical assistance and recently of more substantial commodity aid and balance of payments support, pushed along by a handful of Australian officials in the face of heartbreaking frustrations arising from conditions in both countries: in Indonesia, the practical obstacles due to administrative inefficiency and all the other factors limiting the country's capacity to make effective use of aid; in Australia, the low priority accorded to foreign aid relative to competing claims on resources, vis-à-vis Indonesia, aggravated during the decade 1955-65 by strained diplomatic relations between the two countries, an administrative establishment for foreign aid policy formulation and implementation grossly inadequate even to the modest role assigned to foreign aid and, last but not least, the pushes from a Department of Trade interested only in export promotion and the pulls from a Treasury jealous of the taxpayer's money and sceptical about the value of foreign aid in general and aid to Indonesia in particular.

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In this essay I propose to give a brief account of the history of Australian foreign aid to Indonesia, outlining the main phases of policy and indicating some of the difficulties encountered. I shall not deal with Australian assistance to Indonesia's trade which I discussed in the preceding essay. But in the latter part of the essay I shall describe recent developments in Australian private investment in Indonesia; for, although hardly 'aid', such investment is at present keenly sought by Indonesia and could make a useful if marginal contribution to Indonesian economic development, particularly if official aid and private investment were more closely related than they have been in the past.

Colombo Plan Aid, 1953-65

Until the last few years, all direct Australian official economic aid to Indonesia has been under the auspices of the Colombo Plan. The Colombo Plan came into existence in 1950 on Australian initiative. Until then, American foreign aid had been largely directed towards Europe, under UNRRA and the Marshall Plan, and Australia herself had given aid mainly to the United Kingdom. But in 1949 President Truman had proclaimed Point Four and Australia was anxious to see aid being used to promote economic development and political stability in her Asian neighbourhood. The Colombo Plan began as a British Commonwealth scheme, but soon non-Commonwealth countries joined it, both as donors and as recipients, including the young Indonesian Republic in 1953.

Australia had played a prominent and sympathetic role at the birth of the Republic and in this spirit readily included Indonesia in her modest Colombo Plan program of capital aid and technical assistance. By June 1953 arrangements had been made to supply $A0.5 million worth of tractors and trucks for agricultural development and the first tractors had been shipped to Indonesia. In the following financial year the cumulative allocation for Indonesia was raised to $A2.5 million which was to include 100 diesel buses to improve public transport in Djakarta, $A0.7 million worth of broadcasting and telecommunications equipment, trucks and cranes for harbour development and 310 engines for fishing vessels to be built in Indonesia. The first Indonesian Colombo Plan students were brought to Australian universities and colleges. By June 1955, the allocation for Indonesia stood at $A3.4 million.
The promise of this spirited start was not borne out by developments in the following years. Many logistic difficulties were encountered, both in Australia and in Indonesia. By June 1956, the cumulative allocation for Indonesia had been scaled down to \$A2.8 million, and of this only about half had been spent in two and a half years. The delivery of the 100 buses for Djakarta was not completed until 1957 and that of other equipment could be described in the official report to the Colombo Plan only as ‘well under way’. At the same time, aid to Indonesia came to be overshadowed by increasing concern in Australia about the drift in Indonesia’s domestic political and economic affairs and by increasingly strained diplomatic relations between the two countries. From 1955 onwards, as communist influence in domestic Indonesian politics increased and as parliamentary democracy was superseded by Guided Democracy, leading to the campaign for West Irian, the Sumatran rebellion, the expulsion of the Dutch and later ‘Confrontation’ against Malaysia and expropriation of other foreign enterprises, the Australian Government endeavoured anxiously to avoid a break in relations between the two countries, despite its unsympathetic attitude on West Irian and its actual military involvement in ‘Confrontation’. Even in the worst years before 1965, aid was deliberately continued as evidence of this endeavour, a policy strongly urged by successive Australian Ambassadors in Djakarta. But the political atmosphere reinforced practical difficulties which kept down the flow of aid to a minimal and fairly constant level.

Australian Colombo Plan aid to Indonesia fluctuated from 1952/53 until 1964/65 around \$1 million a year, surpassing \$A1.5 million in some years and falling to little more than \$A0.5 million in others. The ups and downs in aid expenditure do not reflect at all closely those in the warmth of relations between the two countries, being determined much more by the rate at which projects could be brought to the point of actual delivery of equipment or despatch of experts. As a percentage of total Australian Colombo Plan aid, Indonesia’s share fluctuated around 10 per cent, and as a percentage of total Australian bilateral aid (excluding New Guinea) it fell markedly below this figure only in 1964/5 when the total was swollen by food aid to India. But in total Australian international aid, including multilateral aid and
net expenditure in New Guinea, Indonesia’s share in only two years up to 1964/5 rose above 3 per cent.

By June 1957, delivery of most of the equipment offered in 1953 and 1954, including the first 100 buses, had been substantially completed; some Australian experts and equipment had been sent to Indonesia under a scheme of technical assistance to vocational training centres, including a printing trades school; and, with the arrival in Australia of another 100 undergraduates in 1956/57 the number of training awards to Indonesians had risen to about 500. In the following year, technical assistance was extended to the Indonesian Civil Aviation Academy and to a food technology laboratory run by the Ministry of Agriculture. In 1959, Australia agreed to manufacture another 100 buses for Djakarta; these were delivered, together with requisite spare parts, in 1961 (followed by yet another consignment of 50 buses in 1962).

While the various smaller technical assistance projects continued, Australia, just before ‘Confrontation’, undertook two major projects of combined capital aid and technical assistance. In 1960, following (so the story goes) a golf course conversation between the Australian Ambassador and Dr Subandrio, Australia embarked on a road and bridge building project in Nusatenggara (begun on Indonesian Timor but subsequently diverted to the islands of Flores and Sumba); and in 1961 on a project of linking some of Indonesia’s main civil airports by an Aeronautical Fixed Telecommunications Network (AFTN). These two projects, whose estimated cost rose gradually to $A1.5 million for the road project and nearly $A3 million for the AFTN project, accounted for the bulk of Australian capital aid to Indonesia in the following years. Both projects were finally completed in 1968.

At the height of ‘Confrontation’, there were reports in the Indonesian press that the Indonesian Government had decided not to apply for further Colombo Plan aid from the United Kingdom and Australia and was considering recalling students from Australia. This did not happen, but in 1964 Indonesia, for different reasons, decided to discontinue nominating undergraduates for overseas study. Another major Australian project on which much preparatory work was done, a substantial strengthening of the Faculty of Agriculture at Brawidjaja University, Malang, had to be abandoned in 1965.
When the abortive coup of 1 October 1965 heralded the end of the Sukarno era, Australia had spent in all some $A13 million in capital aid and technical assistance to Indonesia over twelve years. During the same period, Indonesia had absorbed in capital aid, both civil and military, technical assistance, and private investment from other foreign countries a total gross amount estimated at not less than $US3,000 million.

What contribution had Australian aid made? For some years, Djakarta had a much better bus service, though by 1965 a large proportion of the fleet was unusable, run down through bad handling and insufficient maintenance, the diminishing number of buses kept on the roads through cannibalisation of the rest for spare parts. The AFTN project made a useful and lasting, if modest, contribution to Indonesia's civil airline operations. The Nusatenggara road project appears, in retrospect, to have been of much more doubtful worth; the choice of two sparsely populated and economically backward islands, however close to Australia, had little to commend it, and on last report little is left now of the roads, except the fine strong bridges built by the Australians—and one even of these has been rendered still more useless by a change in the river course. The experts and equipment provided by Australia to Indonesian vocational training institutions constituted a sensible form of aid at the time; if its impact was imperceptible, the main reason was that there was not enough of it. The policy of bringing so many Indonesian students to Australia, especially for undergraduate courses, has come in for much more questioning, in both countries. No doubt most of the students enjoyed it and learned something. But many had great difficulty in coping with Australian courses (a problem, incidentally, which would have been little less had the emphasis been on postgraduate training of students with no more qualifications than first degrees from Indonesian universities) and many of those who succeeded academically had great difficulty in finding jobs back home that made use of their training, if indeed they were lucky enough to get jobs at all.

It is arguable that the huge volume of external aid that Sukarno was able to secure from the United States and the Soviet Union prolonged his misrule of Indonesia, with implications for the whole concept of international aid that I will not pursue here. Australia's aid was much too small to have made a mark on the
wider canvas of Indonesian politics. If it had any political effects they were, as intended, to maintain through those difficult years a gesture of neighbourliness and this, in an uncertain world, made sense.

**Aid to the Suharto Government**

The Australian Government, supported by the great majority of the Australian public, made no secret of its relief and delight at the turn of events in Indonesia which followed the October 1965 coup attempt. There was relief at the sudden end to 'Confrontation' and to the drift of Indonesia towards communism, and there was delight at the increasing evidence from 1966 onwards that Indonesia had at last again a government that addressed itself pragmatically to the country's appalling economic problems. As the full measure of the legacy of Sukarno was gradually revealed, a wave of public sympathy and emotional desire to help found expression in the Australian press and in government pronouncements, although it is only fair to add that there was also horror over the 1965-6 massacres in Java and Bali, and initially at least concern over the emergence of what looked like a military dictatorship and much scepticism about the capacity and determination of the new régime to deal effectively with the huge task confronting it.

Since Australia's aid to Indonesia, as all her aid to less developed countries, had consisted wholly of grants, she was not one of the creditor countries which met first in Tokyo and then at the 'Paris Club' to negotiate with Indonesia over her default on her enormous external debts. But Australia sent official observers to the first Tokyo meeting and became an active member of the Inter-Governmental Group for Indonesia (IGGI) consortium which was formed in 1967 by the Western creditor countries and Japan to find and co-ordinate large-scale emergency aid. At the regular meetings of the IGGI in the Netherlands in the past three years, the Australian representatives have, together with the Dutch, lent the most sympathetic support to the Indonesian delegations in their quest for sufficient aid to support first stabilisation and since 1968 rehabilitation and development of the Indonesian economy.

From initial emergency credits totalling $US170 million in
1966, the aid committed by the IGGI consortium, according to a rough formula under which the United States and Japan offered each one-third and the other donors the remaining third, rose to $US190 million in 1967, $US350 million in 1968, $US500 million in 1969, and $US600 million in 1970. A large, though diminishing, proportion of this aid was designed as balance of payments support, to supplement Indonesia's inadequate export earnings in financing minimum import requirements. This part consisted of BE (Export Bonus) credits or grants, in effect donor country currency sold by the Indonesian central bank to Indonesian importers in the free foreign exchange market for imports from the donor country of goods on a priority list, the rupiah proceeds accruing as counterpart fund revenue to the Indonesian development budget. The balance (which has this year risen to 43 per cent of the total) has consisted of commitments for project aid, as well as some food aid and technical assistance. Throughout, and especially in the case of project aid, there has been a tendency for actual expenditure to lag considerably behind commitments.

The Australian Government announced an initial emergency grant of $A0·5 million, as well as a gift of rice worth $A0·2 million, in 1966. In the next three years, Australia's aid commitment to Indonesia was successively raised to $A5·2 million in 1967/68, $A12·7 million in 1968/69 and $A15·0 million in 1969/70. Each commitment was the final outcome of an annual battle behind the scenes in which the Department of External Affairs, supported for its own reasons by the Department of Trade, fought for Treasury approval, in interdepartmental negotiations and finally in Cabinet. External Affairs fought the battle not only because, through its Aid Branch, it was responsible for Australia's aid program but because it saw aid to the Suharto régime as being in Australia's urgent national interest and because several of its senior officers had served in Indonesia and sympathised with her plight. The Department of Trade welcomed aid to Indonesia because, and to the extent that, it would promote Australian exports. Treasury not only performed its duty as the watchdog over all expenditure of public money but needed more than usual persuasion to be convinced that money given to Indonesia would not be money down the drain; its senior officials were particularly
sceptical about the BE system under which Indonesian importers were left free to buy what they would from a wide list, including food and other consumer goods.

Australia's BE aid ran into other difficulties. Some of these were associated with the complexities of the Indonesian foreign exchange market and with the efforts of the Indonesian authorities, by means of frequently changing regulations, to reconcile freer trading with priority allocation of scarce foreign exchange in a difficult period of transition from hyperinflation to price stability. These Australia shared with other donor countries. Australia, however, faced two additional problems. One was that under the Commonwealth's annual budgeting procedures, any amounts unspent by 30 June were forfeited to the Treasury. The other was that most of the products of Australian industries, even where they were competitive in quality and price, were unknown to Indonesian importers.

In 1966/67, the first instalment of Australian BE was made available to Indonesian importers on 25 September and was quickly bought, mainly for purchases of Australian wheat flour, urgently needed in the Indonesian rice crisis of that year and known to Indonesian importers for many years as Australia's main commercial export commodity. The second instalment, made available in November, also sold quickly and, following an Australian request, was used to buy some industrial products including vehicles, chemicals, and glass, as well as flour. In 1968/69, however, the program made very heavy weather. Indonesia, following a good rice harvest and substantial PL 480 (food aid) supplies from the United States, had much less interest in commercial purchases of flour. Australia had set aside $A3.5 million of the year's allocation to absolve a commitment undertaken earlier under the International Grains Arrangement (IGA) for food aid concluded in the course of the GATT Kennedy Round negotiations, and one-half of this was sold. But of the remaining $A7.2 million of the year's BE grant only $A1.5 million was sold by January. Since any amounts unspent by 30 June would have been lost to the aid program, last minute efforts were made to dispose of the balance in government-to-government commodity sales, consisting of fertiliser and carbon black, as well as the balance of the flour shipment. In the event, the $A12.7 million commitment for the year remained underspent by over $A1.5 million.
In 1969/70, the program ran much more smoothly. The total commitment of $A15 million was divided into $A3.6 million for Colombo Plan project aid and technical assistance, $A5.1 million for IGA flour (including $A1.1 million freight), $A1.8 million for commodity aid (including rice and carbon black, but also cables and landrovers) and $A4.4 million BE aid. The latter was offered in four quarterly instalments and sold easily for a wide range of Australian industrial products; reports indeed suggested that Indonesian importers would have taken up more had it been available.

In April 1970, the Australian Government announced that it had decided to make a grant of $A53.8 million ($US60 million) in economic assistance to Indonesia for the three-year period 1970/71-1972/73. Although the increase in annual aid envisaged is small, rising from $A15 million this year to $A17 million, $A18 million, and $A19 million in the next three years—unless inflation in Australia is kept below 5 per cent a year the increase will be negative in real terms—the announcement represented an important procedural advance in that it, for the first time, transcended the principle of annual budgeting. It should help the Indonesians to integrate Australia's aid in their own planning.

Throughout this period, Australia has continued to provide project aid and technical assistance to Indonesia under the Colombo Plan. In the first two years of the new régime, conditions were worse than ever for effective project aid. Order was only gradually brought into the country's economic and administrative chaos, and the government, in its efforts to get the raging inflation under control, suspended almost all development expenditure and sought balance of payments support rather than project aid. Australia's two current projects, the AFTN and the road project, continued under great difficulties, and in 1967 it proved possible to send a supply of spare parts and tyres for the Djakarta buses; but no new projects got under way and few students were sent to Australia for training. During 1968, following urgent pleas by the Indonesians, a number of new projects were discussed between the two governments, but except for an Australian mission of two experts to survey Indonesia's telecommunications system, nothing concrete emerged and the year's allocation for Australian project aid was underspent.

In this field, too, the situation improved in 1969. Following a
study of the condition of Indonesia's railway system, Australia supplied about $1 million worth of track and bridging equipment. The Australian telecommunications mission made progress with detailed planning for a trans-Sumatran micro-wave system, a more efficient version of AFTN which would be usable for telegraphic and telephone communications as well as civil aviation. Planning was begun for Australian help in improving the water supply for two Indonesian cities, Bogor and Denpasar. Maintenance equipment and experts were sent to continue the repair of Djakarta buses. Some equipment and technical assistance was also arranged for veterinary research institutes and a hospital. Finally, preparations were made to make Indonesian universities (especially faculties of agriculture and agricultural economics) the major beneficiaries of an Australia-Asia University Aid and Co-operation scheme to be financed by the Australian Government and administered by the Australian Vice-Chancellors' Committee.

Looking back over Australia's official aid to Indonesia in the past four years, there are grounds for both satisfaction and disappointment. The total amount of aid provided, while it has increased substantially from year to year, has hardly been spectacular, some $A34 million, equal to just under 6 per cent of Australia's total international aid expenditure (including New Guinea) or just over 2 per cent of total aid commitments by the IGGI countries during the same period. Considering the great importance Australia attaches to Indonesia and to her recovery under the 'New Order', her contribution might well have been expected to be substantially larger.

In defence against such criticism, the Australian Government could point to the fact that, alone of all the aid donor countries, Australia gives all her aid in the form of outright grants which avoids saddling Indonesia with further external debt. Australia's contribution would make a better showing if all aid were measured in 'grant equivalents' of aid credits. It can also be argued that, within the framework of BE and project aid agreed upon by the IGGI countries, Indonesia could hardly have absorbed more Australian aid during this period. As we saw, even the modest BE contribution proved hard to sell in 1968, and it is doubtful whether Indonesia's administrative apparatus was capable of making effective use of more project aid.

In relation to BE aid, the argument is valid, subject to one
major qualification. All Australia's BE aid, like that of all other IGGI donors (with the partial exception of the Netherlands) has been tied aid, Australian dollars to be spent on Australian products, not free foreign exchange. Australia's balance of payments has been in such a healthy condition during this period that Australia could well have afforded to give some of her aid in free foreign exchange. It is here that the combined vested interest of the Treasury, always fearful for Australia's balance of payments, and of the Department of Trade, solely concerned to act as salesman for Australia's export industries, has hitherto proved an irremovable stumbling block to greater generosity. It is perhaps not too much to hope that a more enlightened approach might be successfully pressed upon the two great departments of state in future. If all IGGI member countries could be persuaded to give part of their BE aid in free exchange, it might make only a marginal difference to the exports of any one of them; Australia might gain as much (or more) from leakages towards her products from the contributions of other countries as she would lose through leakages from her own contribution.

In relation to project aid, the defence also has substance but much of the fault for slow progress has also been on Australia's side. There has been an insufficient sense of urgency at the top political level from which alone sufficient priority for aid to Indonesia could have been imposed. Much delay has been caused by the perennial difficulty in reconciling two established principles of Colombo Plan aid: that the request for aid must come from the recipient country, but that the donor country has the responsibility for ensuring that each project is soundly conceived and efficiently executed. Australia, also, as a small donor country, concerned for political reasons to spread her aid among a considerable number of beneficiary countries, faces a problem of scale: small projects, costing $1 million or so, require almost as much preparatory work as large ones, yet the Indonesian authorities are naturally less interested in allocating scarce top-level administrative resources to negotiating them than to large ones on offer from the major donors. It is arguable that, for this reason, small donor countries like Australia would do better to give up direct project aid and use their aid money instead to help in projects financed and organised by major multilateral agencies, such as the IDA. If the Australian Government offered to contribute to IDA the cost of
any IDA project in Indonesia for which an Australian company had put in a successful tender, the export promotion objective of project aid would be achieved at much less overhead cost; and by giving the Australian role in finance and construction suitable publicity, even the goodwill objective of direct bilateral aid could be secured. The crux of the problem, however, has been the grotesquely inadequate establishment for the administration of Australia’s aid program through the Aid Branch of the Department of External Affairs. I do not want to raise here the much debated question whether aid would be better administered by a separate government agency, as in Canada. There is a good case for the view that, in terms of hard interdepartmental politics, the Department of External Affairs carries more guns for a generous aid program than would a separate department (inevitably under a relatively junior minister). But the Aid Branch has not had, and still lacks, anything like the staff, both in Canberra and in major diplomatic posts such as Djakarta, to handle a substantial and effective aid program. The fault lies not with the aid administrators, but with the failure of the powers-that-be to ensure that there are enough of them, and not part-time diplomats but specialists in the various administrative, economic, and business skills needed for aid administration.

Before leaving the subject of aid, I should add a few words about voluntary or non-governmental aid to Indonesia. Voluntary aid activity has been on the increase in recent years in Australia, and a good deal of it has been directed towards Indonesia. The Red Cross Society, Community Aid Abroad, the Council of Churches, and the Catholic Relief Service have provided useful small project and relief aid of a kind that usually falls through the meshes of a government aid program. A major enterprise by the Australian Institute of Agricultural Science for the establishment, with financial assistance from the Freedom from Hunger Campaign and the Australian Government, of an agricultural development institute to provide technical assistance in Indonesia has been in preparation for two years but appears to be making little progress.

The oldest, and perhaps the most fruitful, of all voluntary projects of aid to Indonesia has been the Volunteer Graduate scheme — now superseded by Australian Volunteers Abroad — under which, since 1953 some thirty-five Australian university graduates
have served in Indonesian government departments on regular Indonesian pay (though with some financial and other help from the Australian Government), working and living among Indonesian people. From among the volunteer graduates have emerged some of Australia's most authoritative experts on Indonesia and many others who have been successful interpreters of the two countries, one to the other.

Private Investment

One of the first acts of the Suharto Government was to reverse the Sukarno policy of hostility to private foreign investment in Indonesia. The new government took the view that Indonesia's domestic savings would for a long time be quite inadequate to provide all the capital needed for economic development at the required minimum rate to overtake population growth and ensure some rise in living standards. What capital aid could be expected to be forthcoming from foreign governments and international agencies would be needed to rehabilitate and develop the country's infrastructure. For investment to develop oil, mineral, and other natural resources and to promote industrial development, foreign private capital—and the managerial and technical know-how it could bring—would be indispensable.

A Foreign Investment Law was therefore passed in 1967 which offered tax and other incentives to foreign companies to set up subsidiaries in Indonesia, preferably in the form of joint ventures with national firms, and a Foreign Investment Board was set up to negotiate contracts with foreign investors under this law. By the end of 1969, some 220 foreign investment projects involving a total planned investment of almost $US1,200 million had been negotiated by the Board in mining, manufacturing, plantation, fishing, forestry, hotel and other service industries. In addition, some contracts had been concluded with foreign oil companies for oil exploration and development and eleven foreign banks had received approval to establish branches in Djakarta.

While these figures give impressive evidence of the interest aroused among foreign companies, they are liable to give a false picture of progress in actual capital inflow and actual development investment. A good many resource development projects, in oil exploration, mineral surveys, and forest exploitation are well under way, but great difficulties have met foreign investors in
manufacturing industry. It has been estimated that actual investment expenditure had in 1970 reached less than 10 per cent of planned investment under approved projects.

Of the 220 foreign investment projects approved by early 1970, only five were Australian. Australia is still a capital importing country, on a larger scale than ever in recent years. Mining, oil and other natural resource development opportunities at home far exceed what domestic capital can tackle. Moreover, Australian manufacturing industry, developed for decades for import substitution in the domestic market, has only recently begun to look for export markets and thus to have the main incentive that motivates industrial investment abroad in the world today—protection of established or potential export markets against local and foreign competition. Until recently, Australian official thinking has been discouraging, or at best indifferent, to overseas investment by Australian companies, though this has begun to change. In 1965, the Australian Government, through its Export Payments Insurance Corporation, provided facilities for investment insurance against non-commercial risks; but characteristically, this is still limited to investments which directly promote exports of Australian goods.

A 1969 survey by the Export Development Council found 80 Australian firms with 149 investments spread over 20 countries. Of these, New Zealand accounted for 64, the United Kingdom and Singapore 14 each, Malaysia 10, South Africa 9, New Guinea 8, and Indonesia 1. The single investment in Indonesia, we may guess, was the Naspro enterprise of the pharmaceutical firm, Nicholas Pty Ltd, which since 1950 has been processing and packaging aspirin, and recently one or two other products, at its small Djakarta plant. Since the survey was conducted, Australian investment projects, in Indonesia especially, have increased in number and range.

These developments date essentially from the PIBA (Pacific-Indonesia Business Association) conference held in Djakarta in August 1967. The Association had been formed a few months earlier, on joint Australian-American initiative, to promote interest in Indonesia among business firms in the developed countries of the Pacific. To the surprise of the organisers, it attracted enormous interest. Some 180 foreign firms, including over 60 Australian
companies, sent senior executives. Most of them had never been to Indonesia. The conference, to which they were attracted by the new business opportunities that appeared to be opening up there but also by an unmistakable sentiment of neighbourly goodwill, was an eye-opener. The initial enthusiasm of many quickly waned as the formidable problems confronting any intending investor in Indonesia were revealed to them. Although quite a number of projects were tentatively discussed and explored by Australian companies, including BHP, CSR, and the ANZ Bank, most of them lost interest in the following months.

But something has happened since then. The first Australian investment project to have got off the ground is a milk processing plant (producing sweetened condensed milk) on the outskirts of Djakarta established by the Australian Dairy Produce Board in a joint venture with a small local company. Indomilk secured government approval in 1967, went into production in June 1969, is now operating near capacity and hopes before long to expand its profitable business. Two other Australian projects got under way last year, a subsidiary of Kiwi Pty Ltd which produces boot polish and a subsidiary of Rheem Australian Industry Ltd which makes steel and plastic containers. Three more Australian manufacturing firms secured approval for joint venture investments in the latter half of 1969, James Hardie Asbestos Ltd, Aluminates Australia Pty Ltd, and Impact International Pty, to manufacture asbestos cement, aluminium sulphate, and collapsible tubes respectively.

There have also been reports of at least two oil exploration contracts with Australian participation and of five Australian projects for mining exploration at various stages of negotiation with the Foreign Investment Board. (Of the latter, two are believed to have since withdrawn, including Kathleen Investments which had joined an American-Australian consortium to look for tin in the Bangka-Billiton area.)

It would be very misleading to leave the account at this. The process of Australian investment in Indonesia is at its very beginning. The gestation period of investment projects, from the first conception and tentative planning to negotiation of contracts, mobilisation of staff, acquisition of land, shipment of equipment, building of plant, and gearing up for production, is always longer
than expected, and longer in Indonesia than in most other places. There is now a constant flow of Australian businessmen to and through Djakarta—the Australian Embassy reported almost 450 business visitors in 1969—and while the majority are looking for export business, a fair proportion have plans for investment. Negotiations in progress in recent months have covered a wide range of industries, from flour milling, food processing, pharmaceuticals and toilet articles, to steel fabricating, motor car assembly, timber extraction, fisheries, mining, commercial and industrial inks, cold stores, and such services as aerial surveying, dredging, and industrial consulting.

Among the most interesting of the projects in hand is a plan by a group of Western Australian firms to set up an industrial estate at Tjilatjap, the port on the south coast of Central Java. In Singapore and elsewhere, the industrial estate, which provides manufacturers with suitable land fully serviced with land and water transport, power and water supply, has been found to be the best answer to some of the basic problems facing individual industrial investors in less developed countries. In Indonesia, the government has not yet found it possible to construct such estates and is very receptive to foreign private initiative in this field. The Western Australian group have approached the Commonwealth Government for help, and an official mission is now at Tjilatjap conducting a preliminary survey for an aid project under which the government would assist by improving the harbour, wharfage and perhaps some other basic facilities, while the private firms would set up a variety of industrial plants. This is the kind of project, particularly with its marriage of official aid and private investment, which offers the best prospects for effective use of Australian taxpayers’ money in combination with Australian business enterprise and know-how, and it is very much to be hoped that it will be pushed ahead rapidly and attract other Australian manufacturers besides the Western Australian group.

The contribution that Australian private investment can make to economic development in Indonesia is bound to remain quite marginal. But provided it is handled in the right spirit, blending the Australian investor’s business objectives with regard for Indonesian national objectives, such investment can become one of the best links between the two countries, solidly grounded in mutual advantage.
Postscript

In the two years that have passed since this essay was written, Indonesia has continued to receive top priority in Australia’s bilateral external aid program. In 1971/72, the second year of the three-year aid pledge, aid to Indonesia was expected to total $A17 million, out of a total appropriation for bilateral external aid of $A47 million (with another $A8.5 million going to multilateral aid and $A131 million to Papua New Guinea). Some $A9 million has been allocated for BE aid, $A4 million for food aid (wheat) and the rest for project aid, technical assistance and training.

Progress has been made with most of the major projects that were mentioned in the essay. The AFTN project has completed eight of the nine telecommunications stations which are designed to give Indonesia a modern aircraft control system, and Australia has accepted responsibility for the maintenance of the network. Planning has gone ahead for the microwave telecommunications system for Sumatra for which Australia is providing some of the equipment and supervision of construction and installation of 52 stations. An amount of $A2.5 million has been allocated for technical assistance and equipment for the improvement of the water supply in Bogor (West Java) and a similar project is under way for Denpasar (Bali). Progress in the Australian Government’s contribution to the rehabilitation of the port of Tjilatjap has been slower, but there is a fair prospect that the joint (government-private and Australian-Indonesian) venture for the industrial development of the port will go ahead.

Perhaps the most important development to be recorded is a much enlarged and improved establishment for the administration of Australia’s aid program. About the time the essay was written, the Aid Branch of what is now the Department of Foreign Affairs was being reorganised. As a result of this reorganisation, ten officers are now employed full time at Canberra on various aspects of Australia’s aid program to Indonesia. A separate subsection, headed by an officer trained in economics and with experience in Indonesia, was established in the Aid Policy section to deal with policy matters concerning aid to Indonesia. The Projects section now has six officers working full time on aid projects in Indonesia at Canberra and there is a three man team headed by a Counsellor (Aid) in the Australian Embassy in Djarkarta. Other
embassy staff are engaged part time on training, food aid, voluntary aid and on the activities of the Australian-Asian Universities Cooperation Scheme which are mostly directed towards Indonesia.

These changes have unquestionably ensured greater efficiency and expedition in the administration of aid at the Australian end. But they have not thereby resolved the larger questions raised in the essay relating to the size, composition and administration of aid. There are no clear-cut answers to any of these questions, but they deserve more public discussion.
Crystal Gazing

Economic forecasting consists in delimiting the range of possible outcomes and assigning probability estimates to the more interesting among them. Anyone who thinks he can forecast the economic future of Indonesia 10 to 20 years ahead is ill informed. But the general approach is sound enough and I shall attempt to follow it. It will be useful and pleasant to begin with an optimistic scenario, tracing the sort of development that can reasonably be hoped for if the economic recovery of Indonesia of the last few years continues and the sober objectives of the present economic policy makers for this and subsequent Five Year Plan periods are realised. This will serve to set an upper limit. I shall then list the factors that are most liable to prevent this favourable outcome. This may give some indication, not of the lower limit, but at least of degrees of likelihood. Finally, I shall make some remarks about the extent to which Australian national interests seem likely to be involved and to which Australian policies may influence the course of events.

An Optimistic Scenario

In the past four years the accelerating decline of the Indonesian economy during the preceding decade has been halted and reversed. Hyperinflation was brought under control in 1967 and 1968 and during the past two years the cost of living has been rising little more than in most Western countries. The deficit in the current budget was substantially eliminated in 1967 and since 1968 rapidly rising tax revenues—by 40 per cent in 1970/71—have contributed increasing surpluses towards the capital budget. Considerable progress has been made in restoring orderly administration and effective budget control, in dismantling the more vexatious direct controls especially over foreign trade and pay-

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ments, in straightening out the banking system and in bringing relative prices such as public utility charges more into line with costs.

A good deal has been done to rehabilitate the main roads, harbours, railways, and telecommunications. Exports have been recovering at an annual rate of 12 to 15 per cent, led by the oil industry whose output has increased by 60 per cent in three years and by new industries such as timber, but with useful contributions, through increased production—and a shift back from smuggling to legal trade—by the traditional export industries, rubber, copra, tin and others. Output of rice and other food crops has fluctuated considerably with seasonal conditions but appears to have risen sufficiently to meet rising domestic demand without any further increase in annual food imports. Local manufacturing industries, though still beset with many difficulties, are working much nearer capacity and there has been a marked increase in building and construction activity.

Foreign private investment has been encouraged in every possible way. While the figure of $US1·3 billion of 'intended' investment (excluding oil and banking) is somewhat misleading, many major projects in mineral, oil, timber and fisheries development and some 200 smaller manufacturing projects are under way. Indonesia's balance of payments has been underwritten by the IGGI consortium of non-communist donor countries which have provided program and project aid in increasing volume, rising to $US600 million in 1970 and $US640 million in 1971. Although reliable estimates are still lacking, average per capita real income, which was barely stationary during the 1950s and declined during 1960-6, has probably been rising by some 2 per cent a year in the past two years.

It is not inconceivable that the economic progress recorded in Indonesia in recent years will continue and even accelerate through the 1970s and into the 1980s. The target growth rate for real GDP in the current Five Year Plan period (ending 1973/74) is a modest 5 per cent per annum. Given continuation of the present economic policies and some more years of administrative and institutional reform at the pace of the last few years, one may reasonably look forward to an average growth rate of at least 6 per cent.
Since nearly half of Indonesia's national product still originates in agriculture, a 6 per cent growth target for GDP requires a not much smaller rate of growth of food production. The current Five Year Plan in its original form envisaged a very high rate of growth of rice output of 8.5 per cent per annum (50 per cent in five years). Something like this rate of increase appears to have been attained in the last few years, with the aid of fortunate seasons, but production of other food crops has risen much more slowly or declined. If current plans for rice intensification, based on increasing use of the new high-yielding varieties, are reasonably successful, it is not unrealistic to expect food production to match the growth of domestic demand implied in a 6 per cent per annum growth of GDP and substantially to reduce, if not entirely eliminate, the need for food imports by 1980.

If food production grows at something less than 6 per cent a year, the more dynamic non-food sectors will have to grow considerably faster. If only to keep the balance of payments problem within bounds, the burden will fall largely on oil and the newer export industries and on import replacing industrial development. The recent very rapid growth of exports during the period of recovery from the low level of 1966 is unlikely to be sustained. The phenomenal growth of oil output, for example, has been almost entirely from existing Caltex fields developed earlier and is expected to slow down, while the yield of the new offshore and onshore areas will not begin until 1971 and is inevitably uncertain. All the traditional agricultural export industries face uncertain or adverse world market conditions, and it will be some years before the new mineral developments in copper, nickel, bauxite, etc., will contribute substantially to Indonesia's foreign exchange earnings. But the potential for Indonesia's exports now looks very much brighter than was commonly assumed a few years ago. There is the virtual certainty of an ever growing Japanese market for most of the oil, minerals, timber, and fisheries products that Indonesia can produce for export. Even the traditional export industries can withstand low prices because of low labour costs and could be made to yield substantial increments of foreign exchange over the next decade. Finally, there is much scope for industrial development to contribute to the balance of payments, as well as to growth of income and employment, partly
by processing of timber, minerals, and other raw materials and partly by the establishment of light consumer industries both for export and for import replacement in the home market.

Growth at 5 to 6 per cent a year will require capital investment at a rate far higher than Indonesia will be able to finance from domestic saving for many years to come. After a decade, possibly three decades, of disinvestment, there is an immense backlog of infrastructure, productive and social overhead capital to be made good. (A recent IBRD report mentions that $US140 million will be needed to restore the state railways to their 1939 condition. Much the same applies to most sectors of the economy.) But the problem of finding the required capital is not insuperable. At present, Indonesia receives $US600 million a year in program and project aid from the IGGI donor countries. Private foreign capital is beginning to flow in, this year at a rate of some $US150 to 200 million. While tax revenue cannot continue to rise at the extraordinarily rapid rate of the past two years, both public and private domestic saving should rise a good deal faster than GDP for some years yet. Provided foreign aid continues at something like the present rate for another (say) five years and then tapers off not too precipitately, provided private foreign investment gains momentum and provided the domestic saving ratio can be raised, with rising national income, from the present 10 to 12 per cent towards 15 to 20 per cent over the next decade, the capital needs of Indonesian development can be met.

It is possible, therefore, to envisage for Indonesia an indefinite period of sustained economic growth at an average annual rate of 5 to 6 per cent. Even this will not make Indonesia a prosperous country in the 1980s. Indonesia's rate of population growth is now estimated at over 2.5 per cent a year—we still have no precise information—and is still accelerating. On the most optimistic assessment, family planning cannot hope to do more in the next decade than to prevent the annual rate of population growth from rising above 3 per cent. A 3 per cent rate of growth will raise Indonesia's population from the present figure of 121 million to 220 million by 1990. It will leave only one-half of a feasible 6 per cent per annum growth of GDP for rising income per head. Average per capita income will have risen from (say) $US100 now to $US135 in 1980 and $US180 in 1990. At the latter figure it will still be less than Malaysia's average today.
Is this the best that can be hoped for? Higher rates of growth have been achieved by Japan and by some of the communist countries in the past two decades and by a few developed and developing countries for shorter periods. Perhaps it is unreasonable to make firm predictions about the upper limit even for Indonesia for as long ahead as 1990. But he would be a bold man who put the upper limit higher for 1980.

What we have sketched so far is an optimistic scenario. There are many reasons, unfortunately, why so favourable an outcome may not be achieved.

Four Hydra Heads
While an optimistic scenario can stick to economic facts and possibilities, any assessment of alternatives must take politics into account, both because political developments may impede economic progress and because economic failure is bound to have political repercussions. Moreover, once things begin to go seriously wrong for any reason, political and economic forces are liable to interact in ways too complex for even the most intrepid crystal gazer. But one must start somewhere. Let me therefore isolate four factors that seem to be most likely to cause economic progress in Indonesia in the next decade or two to fall short of the favourable outcome predicated in the optimistic scenario. The four factors I have selected are: premature decline of foreign aid; rising economic nationalism; public impatience and social revolt; and "begging down".

Premature Decline of Foreign Aid
The optimistic scenario assumes that Indonesia can count on foreign aid continuing at something like the present rate of $US600 million a year for at least another five years and on aid tapering off thereafter at a moderate pace. This is an optimistic assumption. One-third of the burden is at present being carried by the United States, another third by Japan. Balance of payments difficulties or domestic pressures towards more inward-looking policies may make it difficult for US Governments to maintain the American contribution, and while Japan and some of the smaller donors may be willing to raise theirs somewhat, the flow of aid is bound to be a precarious matter for negotiation from year to year, liable to be endangered by any adverse turn of events in Indonesia.
Yet, an adequate flow of aid is indispensable, not only to fill the large and indeed still growing gap in Indonesia's balance of payments (to which rising external debt service is contributing significantly) but also because aid counterpart funds provide the bulk of finance for the Indonesian Government's development budget. If foreign aid were to fall off sharply in the next few years, balance of payments difficulties might make it increasingly difficult to maintain the recently restored freedom of foreign trade and payments, tempting or compelling the Indonesian authorities to resort again to hampering direct controls, and shortage of finance for public investment would slow down the development effort.

**Rising Economic Nationalism**

Voices are already being heard in Indonesia protesting against the country's dependence on foreign aid which is said to deprive her of her freedom to pursue an 'independent' foreign policy, against the role of the World Bank, the IMF and foreign advisers, against the 'sell-out' of Indonesia's natural resources to foreign capitalists, and against foreign competition with Indonesian 'national' enterprises in domestic industry. As yet, the voices are isolated and muted. But already there is continuous pressure on the government to take protective measures and to circumscribe the area of permitted operation of foreign capital, and this is bound to grow. The Suharto Government is committed to the present outward looking course. So long as it remains politically firm in the saddle and things go reasonably well economically, these pressures will affect its policies only marginally. But it is unreasonable to expect Indonesia, alone among developing countries, to keep economic nationalism indefinitely on the leash. If things go wrong, it will once again become the spearhead of discontents, and even if things go well dependence may come to be increasingly resented.

At this stage it is difficult to imagine that Indonesia will revert to the extremes of berserk nationalism of the Sukarno era. As in Ghana and other countries that have passed through such a phase, the very memory of the consequences provides a degree of immunity. But it is almost certain that the present euphoric climate for foreign advisers and enterprise will not last. If it deteriorates too rapidly, the deterrent effects of pinpricks and restrictive measures on foreign aid, technical assistance, and private invest-
ment will show themselves in a variety of ways most of which will be adverse to economic development.

Public Impatience and Social Revolt

The economic improvement of the last few years, impressive as it has been, has as yet done little to alleviate the condition of the people, and in some respects things have got worse. The severe economies in government expenditure dictated by the stabilisation program fell particularly heavily on social expenditures in education, health, housing, etc., while the effort to restrain further expansion of the government civil and military payroll has closed the Sukarno era's main safety valve against rising unemployment. In the past year or two, revival of economic activity in manufacturing, building and construction and trade has probably kept demand for labour ahead of additions to the workforce. But there is massive unemployment in the cities, not least among high school and university graduates, and under-employment in the countryside reflected in low productivity and incomes. Wages in government and private employment are miserably low, and even our optimistic scenario promises only marginal improvement, say by one-third on average, during the coming decade. Meanwhile, the 'New Order' has opened opportunities for a minority of individuals in power—mostly conspicuous in uniform—and some in more or less legitimate business, to enrich themselves.

How long will the patience of the people last? I do not think there is a serious risk of explosion of social discontents in Indonesia in the foreseeable future. Party politics may liven up, and there will be politicians to stir and organise. But all the evidence points to continued control of political power by the armed forces for a good many years ahead, enough control at least to prevent effective regrouping of the PKI (communist party) or other organised leadership for social revolt, and without such organised leadership social discontent rarely becomes politically effective.

There is perhaps a greater risk, in the short run, of impatience on the part of right-wing groups, Moslems and the military, demanding a greater share of resources for their own purposes, religious buildings and education in the one case, and military hardware in the other. Such demands could make serious inroads into finance available for economic and social development but would not sharply alter the course of events.
Perhaps the most serious, because most probable, threat to the realisation of our optimistic scenario is nothing as dramatic as the other three factors, but mere failure to keep up the pace of economic reform and development. There are cynics, Old Indonesia Hands, who ridicule the optimism of foreign observers of the recent recovery and point to the analogy of the early 1950s when, they say, there were similar high hopes which were all frustrated as economic progress and reform bogged down in the politics of underdevelopment. It could happen again. A slackening of drive at the top, friction among the policy-making leadership, failure to push administrative reforms through the entrenched bureaucracy or legislation through parliament, excessive delays in the planning and implementation of major development projects, a run of two or three bad seasons, expensive trouble in West Irian, a worldwide recession depressing the prices of Indonesia's exports, diversion of energy into issues of domestic or foreign politics—a combination of some such circumstances could cause the rate of economic growth to relapse. In terms of the rate of growth of per capita income, the margin between our optimistic scenario and stagnation is only 3 per cent a year, and once the pace slackens all the other threats—decline in foreign business confidence, less aid with more strings, increased hostility towards foreign scapegoats, domestic social discontent and political unrest—are liable to become more real.

It could happen again, but the odds at the moment are that it will not.

The Lower Limit

Let us, as part of the exercise, imagine the worst. Can we set a lower limit to Indonesia's economic prospects for the 1980s?

In economic terms, the answer, for once, is simple. Things could hardly get worse than they were in the last years of the Sukarno régime, with external bankruptcy, domestic hyperinflation, far-reaching dissolution of orderly processes of government, near standstill in industry and declining productive capacity in almost every sector of the economy. Of course, the economic consequences for the masses of a population swollen meanwhile by tens of millions would be worse, there would be more malnutrition, more unemployment, more misery, but only in degree. As in the
years 1960-5, it would be a politically highly unstable situation, domestically and internationally. But history does not repeat itself. If only because it has happened before, it seems exceedingly unlikely that things would once again be allowed to reach such a pass. Some time before they do, another probably more authoritarian régime, more likely of the right than of the left, more likely in control of the whole country than split into autonomous regional states, assisted by renewed international effort from some sides, will seek to propel the economy forward again.

**Australian Concerns**

What are the implications for Australia of the optimistic scenario of Indonesia’s economic future?

The most predictable would seem to be that we shall get more involved. As a very underdeveloped country, competitive rather than complementary in its trade pattern, Indonesia has had little economic intercourse with Australia. If Indonesia achieves the sustained economic growth predicated by our optimistic scenario, scope for two-way trade will steadily increase, partly in primary and processed materials (Indonesian tropical produce, timber, sea foods for Australian wheat, dairy products, steel and other metals) but increasingly in manufactures (Australian engineering, chemical and other technology and capital intensive products for Indonesian consumer goods) and in tourist and other services. Australian business will also be increasingly interested in direct investment in Indonesia. Australia will acquire an economic stake in Indonesia that it has never yet had.

The optimistic scenario, however, will also make demands on Australia. It presupposes that Australia, with other developed countries, gives access to her domestic market for Indonesia’s exports of primary products and especially of manufactures. It presupposes that Australia, with other developed countries, will sustain at least the present level of foreign aid. Indeed, Australia, as Indonesia’s one developed neighbour, may need to do more, both by stepping up her own aid if American and Western European aid should diminish, and by intensifying her efforts as Indonesia’s ‘friend at court’ in the councils of the IGGI.

Does the optimistic scenario hold any threats to Australian national interests? As Indonesia recovers and gains in economic strength, her aspirations to a more prominent role in international
affairs and in southeast Asia in particular will grow. I leave it to others to assess what implications this might have for Australia. In purely economic terms, Australia can only gain by increasing Indonesian prosperity. Some may fear the possibility that growing economic strength may in the long run give rise to manifestations of economic imperialism, including perhaps demands for relaxation of Australia's restrictive immigration policy. But in Indonesia's case, this is surely looking ahead much beyond the 1980s. (Before that time comes, Australia and Indonesia may want to harmonise their interests as fellow members of Japan's co-prosperity sphere!)

It is much more difficult to forecast how Australian interests are liable to be affected if things do not go well in the Indonesian economy. One is tempted to fall back on the historical analogy of 1960-5. Sukarno's foreign adventures, West Irian and 'Confrontation', were in part an escape from unmanageable domestic economic problems. If things should once again go from bad to worse, a revival of subversive movements, seeking and receiving foreign support, is conceivable. But for the reasons given above, I would regard any such developments as a remote risk for the coming decade and even beyond. The most predictable consequence for Australia of a partial failure of Indonesia's present plans for economic development is the loss of the economic benefits that this development promises to Australia and probably still greater moral pressure on us to aid in the next attempt.
OTHER NEIGHBOURS
Japan: Dependence or Partnership?

To an extent that, I am sure, no one foresaw twenty-five years ago, Australia has become economically involved with Japan, and all the signs suggest that this involvement will steadily increase in the next twenty-five years. The reasons are obvious enough. The basic ones are Japan's spectacular economic growth and the high degree of complementarity of the two economies. Japan's economic growth is dependent on a huge and growing volume of imports of raw materials and foodstuffs which Australia is able to supply, in the case of a range of essential minerals, to an extent undreamed-of a few years ago. There is also increasing scope for 'horizontal' trade in manufactures between the two most highly industrialised countries of the Western Pacific. In both kinds of trade, relative proximity with its attendant economies in transport costs gives both countries some advantage over competitors in each other's markets. In recent years, Japan has, in addition, reached a stage in her economic development where she can hope to supply some of the capital and technology Australian needs for rapid economic development. Both countries, moreover, have actively sought to take advantage of the basic opportunities for closer economic relations and have co-operated to reduce barriers to bilateral trade.

The object of this paper is to consider some of the implications for Australia of this increasing economic involvement with Japan. There has been a great deal of discussion of every aspect of economic relations with Japan in Australia in recent years. But it has been almost entirely confined to officials, businessmen, academics, and sections of the press directly concerned with, and in

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favour of, the promotion of trade and financial relations between the two countries. There has been remarkably little public expression of fear of, or prejudice against, Japan which, one cannot help suspecting, is still widespread among considerable sections of Australia's 'silent majority'. Nor have the economic nationalists of the political right and left who are so vocal in their protests against 'foreign domination' of the Australian economy by American or British capital so far raised their voices about the danger of excessive economic dependence on Japan (except in the limited context of Australia's role as a 'quarry').

This stands in marked contrast to much overseas comment, especially from Britain and Europe, which treats Australia's future as an economic satellite of Japan as a fact obvious to the naked eye. A visiting British journalist whose Sydney taxi driver saw Australian-Japanese relations in the perspective of World War II commented: 'Clearly my cab driver lost his war but I think he will never know.' A French magazine told its readers: 'The Japanese with their wonderful contracts have to date been content with the easy role of the big customer and straight dealer. Will they stop when they hold the fate of the Australian economy in their hands?' An Italian business journal expressed the view last December: 'The Japanese presence, by way of both investment and trading, and generally in development of raw material sources in Australia, is so great as to be almost overwhelming.' The American futurologist, Herman Kahn, in his recent book on Japan foresees an increasingly profound Japanese influence on Australia, socially and culturally as well as economically, forcing Australians away from 'their rather parochial and inbred life into the most stimulating and cosmopolitan existence'.

**Japanese Trade and Investment**

Between 1958/59, the year following the conclusion of the first post-war trade agreement with Japan, and 1969/70, the value of Australia's exports to Japan quintupled, from $A200 million to over $A1,000 million. Japan's share in Australian exports rose from 13 to 25 per cent, almost equal to the combined total share of Australia's next two largest export markets, Britain and the United States. Australia's imports from Japan have risen even faster, sevenfold since 1958/59, though at a lower level. Australia
retains a large favourable balance of trade with Japan, the value of exports being more than twice the value of imports.

The growth in trade between the two countries has been accompanied by striking changes in its composition. In 1958/59, three-quarters of Australian exports to Japan consisted of agricultural products, wool alone accounting for two-thirds, while minerals contributed only 10 per cent and manufactures only a trickle. By last year, over one-half of Australia's exports to Japan consisted of mineral ores, concentrates and metals, the value of iron ore exports alone on the point of surpassing that of wool. Four-fifths of Australia's exports to Japan consisted of bulk raw materials, but exports of refined metals had reached $A50 million and a beginning had been made with exports of manufactures for which Japan had become Australia's fourth largest market (next to New Zealand, the USA, and New Guinea). Among Australia's imports from Japan, there had been a marked shift from textiles and other products of light industry towards heavy manufactures, especially motor vehicles, machinery and equipment.

Australia's share in Japan's total trade is very much smaller than Japan's share in Australia's and it has not increased in the past decade. Australia still supplies about 7 per cent of Japan's imports and takes about 3 per cent of Japan's exports. In a sense, Australia has merely held her own in the enormous expansion of Japanese trade that has accompanied Japan's economic growth. But this understates the economic importance of Australia to Japan. Australia is the major supplier of some of the key raw materials needed by Japanese industry, accounting in 1969/70 for four-fifths of Japanese imports of wool, nearly half of bauxite, one-third of coking coal, one-quarter of iron ore and concentrates, and similar proportions of others smaller in value but also indispensable. Australia has also become Japan's leading market for exports of motor vehicles and steel products.

The benefit to Australia's economic health and development of the phenomenal economic growth of Japan and of the consequent growth in Australian-Japanese trade is obvious. For twenty years it has been a major factor in sustaining demand for Australian wool and other products of rural industries in the face of slowly growing or shrinking markets elsewhere overseas, and in the past ten years the Japanese market has provided the prime stimulus to
the exploration and development of huge mineral resources which have transformed the prospects for Australia's balance of payments and are making a major contribution to Australia's overall economic growth. Conversely, Australia's mineral discoveries have considerably relieved the raw material supply problems of Japanese industry, and Australia represents for Japan a useful source of foodstuffs and market for manufactures.

All the signs are that the growth of Australian-Japanese trade will continue unabated in the next ten years. There is confidence in Japan that the phenomenally high rate of economic growth of the past decade will be maintained at least through the 1970s. The official five-year plan for 1970-5 conservatively projects an average annual rate of growth of real GNP of 10·6 per cent. The unofficial but authoritative Japan Economic Research Centre estimates that real GNP will rise at an annual rate of 12·4 per cent to 1975 and at 10·8 per cent to 1980. Even at the lower official rate of growth, Japan's national product would double by 1976; her per capita income would surpass that of Britain by 1974 and might reach that of the United States by the mid-eighties. To sustain this growth, enormously increased imports of raw materials will be needed. Japan's total imports are expected to increase from $US13·5 to $US54 billion by 1980. Import requirements of oil, iron ore, coal, copper, bauxite and alumina, nickel, lead, and zinc are expected to double or more by 1975, while rising per capita incomes will greatly expand demand for foodstuffs, especially of the higher protein kind such as meat and dairy products, and for imported manufactures whose share in total Japanese imports is expected to rise from 11 to nearly 20 per cent by 1980.

Australia is well placed to meet much of this demand. It has been estimated that, on present trends, Japan will by the end of the decade take 38 per cent of Australia's exports and supply 19 per cent of her imports; with increasing complementarity, these shares may rise as high as 42 per cent for exports and 26 per cent for imports. This would imply that by 1980 Australian exports to Japan would reach $A4 billion, equivalent to Australia's total exports this year. Much of the increase would be accounted for by crude and processed minerals whose share in total exports to Japan would rise from just over half to nearly three-quarters. More recent projections of Australian mineral exports are still
more daring, suggesting that the total may reach $A3,000 million by 1975, much the larger part to Japan. Australia may then account for considerably more than the 40 per cent share in iron ore and 50 per cent in coal imports of the Japanese steel industry projected a year ago.

The more optimistic of these forecasts assume not merely that the projections of Japanese economic growth will be realised but that Australia’s capacity to meet Japanese import needs at competitive prices expands sufficiently rapidly and that both countries further liberalise their trade with each other. The projections of Australian mineral exports to Japan imply very large further investments in Western Australian iron ore, New South Wales and Queensland coal, Queensland and Northern Territory bauxite and much other mining development and in port and transport facilities. Still larger investments will be needed if, as seems likely, both Japan and Australia, for different reasons, seek a shift towards processing of Australian minerals before export to Japan.

In relation to the other components of Australian-Japanese trade, the optimistic forecasts assume that Japan will further relax her measures of agricultural protectionism in return for freer access to the Australian market for her manufactures and that Australian manufacturers will be able to secure a larger foothold in the Japanese market.

These assumptions gloss over complex issues of commercial policy in both countries. In particular, while in Japan agricultural protectionism is in the longer run almost certain to give way to domestic economic and political pressures, one must be sceptical whether any real inroads can be made into Australian industrial protectionism by unilateral or even internationally negotiated tariff reductions. It is this doubt that has given rise to the idea of industrial integration which is believed to have formed a major element in Mr McEwen’s ‘concept’ for the future development of economic relations between the two countries shortly before his departure from the political scene: the idea that through agreed specialisation among major Australian and Japanese manufacturing industries, negotiated by the companies concerned, somewhat on the lines of the current Chrysler-Mitsubishi agreement, both countries, but especially Australia as much the smaller of the two, would benefit from economies of scale in selling in the combined market, while the new employment opportunities im-
mediately opened up by enlarged export sales would in Australia provide the only politically practicable basis for contraction of uneconomic lines of manufacturing production. As yet, industrial integration between Japan and Australia is no more than an idea in the minds of very few people. Even if it is followed up energetically it is unlikely to make a significant impact on Australian-Japanese trade in the next five years. But over the next decade or two it could bring another major strand to the mutual economic involvement between the two countries.

Japanese investment in Australia is a very recent development. Until a few years ago, the official attitude to investment abroad of Japanese capital was not unlike Australia's. Japan thought of herself as a country short of capital—though her policy, unlike Australia's, was to confine capital import to fixed interest borrowing and to discourage direct investment as liable to offer excessive competition to domestic industry—and with balance of payments difficulties which precluded any substantial capital outflow.

In the last two or three years, there has been a sharp change in this respect. The main impetus has come from the reversal in Japan's balance of payments situation, from worrying deficits to ever growing and almost equally worrying surpluses. By the end of March of this year, Japan's international reserves reached almost $US5 billion and projections of her balance of payments forecast a surplus on current account of $US3.5 billion by 1975. The worry now arises from increasing pressure on Japan by the major deficit countries, including the United States and Britain but also the less developed countries with most of whom Japan has substantial export surpluses, to relieve the pressure on their balances of payments by appreciation of the yen. Rather than accept the need for such a change in the exchange rate which would deprive Japanese industry of some of its competitive advantage both abroad and at home, Japan has in the past year or two sought to correct the imbalance by the alternative methods of liberating imports and expanding capital outflow through aid and direct investment.

This motive has been reinforced by a sense of urgency in securing the raw material supplies needed by Japanese industry through direct investment in natural resource development projects all over the world and in securing export markets for Japanese capital goods in competition with the other major industrial coun-
tries by direct investment in manufacturing, especially in less developed countries. Rising labour costs and growing public protest against pollution, as well as the formidable costs of shipping ever larger volumes of raw materials to Japan, have provided additional reasons for locating more of Japan's manufacturing and processing industries abroad. Finally, in relation to Australian mineral developments for the Japanese market, Japan is now anxious to secure at least a share in the equity of the controlling companies and consortia so as to be able to exercise some influence on their marketing and price policies.

Australia has generally welcomed this change in Japanese policy with open arms. Australian Governments, Commonwealth and State, are keenly conscious of the huge amounts of capital needed to develop Australia's mineral resources at the rapid rate required to maintain the desired rate of growth of exports and national product. Australia has her own reasons—promotion of overall industrial development and the need to provide a broader economic base for the new mining settlements in the sparsely populated north—for favouring increased domestic processing of minerals before export and would welcome the help of Japanese capital and technology in this. For some time it has been official Australian policy to encourage Japanese direct investment in Australian manufacturing industry, to the point of putting pressure on Japanese motor car manufacturers to move towards assembly and manufacture in Australia. In the hope of enlisting Japanese interests in the struggle to secure easier access to the Japanese market for Australian agricultural products, Australia is also said to favour Japanese investment in beef cattle and other agricultural development projects.

At present, Japanese investment in Australia is still quite small. Total Japanese capital invested in Australia is believed to be less than $A70 million, compared with $A3.5 billion of American, $A4 billion of British and more than $A1 billion of other foreign capital. (These are the cumulative totals for private overseas investment in companies in Australia for the period July 1947 to June 1970, as estimated by the Commonwealth Statistician.) The major Japanese equity investments are minority shares in three iron ore mining consortia (Mt Newman, Robe River, and Savage River) and the large coal mining joint venture between Mitsui and Thiess Brothers. There are also a few smaller Japanese-Australian
joint ventures in motor car assembly and distribution, electronics, scientific instruments, textiles, wood chip production, and cattle raising. In other cases, Japanese interests have contented themselves with loans linked to sales contracts, as in the case of the Bougainville copper project, or equipment loans to finance the purchase of Japanese mining and other industrial machinery.

But in the past year or so, Japanese interest in equity investment in Australia has very greatly intensified. With government encouragement and offers of financial assistance, a wide range of Japanese companies have expressed their interest in equity participation in Australian mining developments and joint ventures in other fields. Several companies, including some Japanese banks, have recently established Sydney and Melbourne offices to be on the scene. Very large figures for prospective Japanese investment have been mentioned in the press. A more conservative forecast by the Japanese Ambassador that Japanese investment in Australia would rise from $A70 million to $A200 million 'in the next few years' is probably more realistic. For most of the Japanese companies involved, direct investment overseas is charting new seas, and while Japanese government and business can be expected to throw themselves into the new policy with their customary vigour, it will take time to develop the necessary infrastructure of financial institutions in Japan and to negotiate mutually satisfactory arrangements with Australian joint venture partners and with the American-British-Australian consortia that at present control the main mineral developments. Looking further ahead, however, Japanese capital seems certain to play an increasing role in financing, and sharing in the control of, much Australian business.

Risks of Dependence

In the average reasonably sophisticated Australian, the story of Australia's economic involvement with Japan which I have summarised is liable to evoke a mixed reaction. On the one hand, appreciation of Australia's luck in being so favourably placed to benefit for her own economic development from Japan's rapid economic growth and need for the products Australia can supply. On the other hand, nagging doubts about the risk of growing dependence on Japan, first economically and later perhaps in other respects. What are the risks? And how can we hedge against them?
On the evidence of the present state of Japanese-Australian economic relations, and their likely growth over the next few years, there is so little reason for such fears that their occasional expression in Australia must be attributed to ignorance or prejudice and abroad to sour grapes. Japanese investment in Australia is a small fraction of British and American and Japan’s share in Australia’s trade is less than half of the United Kingdom’s share throughout Australia’s history until World War II. Few mainly primary exporting countries enjoy as wide a spread of export markets as Australia today, with the United States, Western Europe, the United Kingdom, and the southeast Asian-Pacific countries each taking about 15 per cent and Japan 25 per cent.

It is true that Australia’s dependence on the Japanese market is much greater for her exports of iron ore and coal, and is likely to assume similar proportions for several other minerals in the next few years. But here dependence is not one way. Almost comically, the Japanese seem quite as worried about their excessive dependence on Australian raw material supplies as Australians are about their excessive dependence on the Japanese market. With nearly half the iron ore and coking coal that the Japanese steel industry needs to keep going from month to month coming from Australia, there is continuous concern in Japan about the risk of interruptions of supplies through cyclones in the west or strikes in the east. In the longer run, there is concern whether Australia has the capital needed to step up production and export of mineral products at the rate envisaged in Japan’s procurement projections. If agreed specialisation among and within Australian and Japanese manufacturing industries develops, this too will be a two-way involvement.

The economic relationship between Australia and Japan is, therefore, and will remain one of mutual dependence. But, some will object, it is unrealistic to talk of the mutual dependence between the United States and Guatemala or even Canada. The disparity in size and economic power between Japan and Australia is already great and will grow with every decade if current projections of a much higher rate of growth in Japan are realised. Nor, it will be said, can this disparate relationship be indefinitely confined to the economic sphere. Superior economic power is bound sooner or later to spill over into political and cultural relations. Is Australia in danger of drifting within the next two or
three decades into the status of a satellite to the Japanese Super State? It is worth confronting this question frankly, for such fears are undoubtedly latent in this country.

There is no doubt that the sheer difference in size between the two economies already means that Japan is economically more important to Australia than Australia is to Japan, and this gap will widen. The analogy with Guatemala is absurd and even that with Canada exaggerated—geographic distance and differences of history, language, and culture will for long keep Australia and Japan much further apart than Canada and the United States. But if in ten years' time Australia sells nearly half her exports to Japan, Australia's economic prosperity will in considerable degree be linked to that of Japan. What are the risks of economic dependence?

From the point of view of Australia's own economic stability and growth, dependence on Japan holds little grounds for concern. As an 'outboard engine' for Australia's economic growth, no other major trading partner can rival Japan. The Japanese economy has experienced recessions and will do so again. In the early months of 1971 coal stocks accumulated at Newcastle because of some slowing down in Japanese steel production; this kind of thing will happen from time to time. But superimposed on an annual rate of growth of over 10 per cent, the Japanese recessions have been little more than short breathing spaces before the next advance. Japan's economic growth will slow down if, as seems likely, Japanese public opinion will demand a larger share of the country's economic resources for social welfare and environmental control and as, with rising per capita income, demand shifts towards service industries which offer less scope for measurable productivity increase. Dr Okita has recently commented on the diminishing status of business and growth among the younger generation in Japan and predicted that 'economic growth may not be a very important concept in their era'—but he defined this as 'in perhaps 20 years or so'. Short of a domestic social upheaval or other drastic change in the orientation of Japanese policy which is unlikely in the foreseeable future, Japanese economic growth at a rate at least as high as Australia would aim at is as reliable as anything in an uncertain world.

More to the point is that dependence of so large a part of Australia's total exports, and especially of the major mineral indus-
tries, on a single market may render Australia vulnerable to the exercise by Japan of what economists call monopsony power. In this connection stress is often laid on the extent to which Japan’s leverage as a single buyer is increased by the habit of co-operation among Japanese business firms and between business and government. But the degree to which Japan can exert pressure on Australia through the exercise of monopsony power is limited by her dependence on imports from Australia, the element of monopoly power that Australia enjoys vis-à-vis Japan. Japan will be able to exert pressure on Australia, whether to secure Australian products at lower prices or to obtain other commercial concessions, such as tariff reductions on imports from Japan or perhaps offshore exploration or fishing rights or shipping concessions or more liberal equity participation or local financing facilities for Japanese investors in Australia, only to the extent that she can secure the raw materials she needs more cheaply or reliably from other countries. This applies as much to particular business deals, such as iron ore or other export contracts, as to overall commercial policy.

There is no reason to believe that Australia has been worsted in her mineral contracts with Japan so far. On the contrary, the large iron ore discoveries in the Pilbara came early enough to give Australia some initial advantage in price over alternative suppliers. Complaints that Australia is selling her minerals to Japan ‘at bargain prices’ or is becoming a ‘quarry for Japan’ have little rational foundation. They are usually made in ignorance of the economics of building up mineral processing and refining plants and in bland disregard of the enormous capital costs involved in a process which will take time and in which, as we have seen, Japan is, for her own reasons, very ready to assist. Nor is there any rational ground for concern about the participation of Japanese capital in Australian development projects. The relatively small amount of Japanese equity capital that is likely to come in the next five or even ten years will in most cases, by diversifying foreign ownership, reduce such risks as there may be in foreign control, and unlike American companies the Japanese do not insist on 100 per cent or even majority ownership.

As the importance of Japan in Australia’s trade increases during the 1970s and beyond, relative to that of Australia’s older trade partners, relations between the two countries will inevitably
Australia and Asia

become closer in other respects, in government, business and personal contacts, in financial and cultural matters, even in foreign policy. An example, not in itself very important, is the policy issue that may present itself to the Australian Government before long if Japan should, after all, decide to revalue the yen. There is already a strong case for an appreciation of the Australian dollar as the most appropriate means of counteracting a domestic inflation largely imported from abroad. An appreciation of the yen would add to these pressures unless Australia also appreciates. Unfortunately, the fact that most of Australia’s export contracts with Japan, including the large iron ore ones, are denominated in US dollars, will be held to weigh against such a step. But as Australia’s trade with Japan grows further, it will be to both countries’ advantage to use one or the other of their own currencies in their mutual trade, and Australia may increasingly lean towards aligning the Australian dollar with the yen.

More important are the longer-run implications of Australia’s increasing economic involvement with Japan for Australia’s foreign and defence policies and for cultural relations between the two countries. To discuss these would take me beyond the scope of this essay. But I cannot refrain from a brief comment on the application to Japanese citizens of Australia’s present immigration policy. There is no reason to believe that large numbers of Japanese want to migrate to Australia, and as living standards rise in Japan and labour shortage becomes more acute, the former motives for large-scale emigration will become less and less relevant to Japan. Japan has solved her overpopulation problem by economic development and birth control. What has been at issue from time to time in recent years is the freedom of Japanese businessmen, tourists, students, and others to enter Australia and reside here for shorter or longer periods as freely as their American or European counterparts. We have it on the authority of the Japanese Minister for International Trade and Industry that ‘for all practical purposes, we don’t have any complaints to make about your immigration laws’. No one wants to promote a large flow of Japanese immigrants into Australia. But I can see no case for making it more difficult for Japanese citizens than for other foreigners to pay temporary visits to Australia or in individual cases to acquire Australian citizenship.

To sum up this part of my argument, I would regard fears of
excessive economic dependence of Australia on Japan in most respects as unwarranted, at least for the coming decade. But it is only realistic to recognise that, as the relative economic power of Japan and Japan's share in Australia's trade grow, Australia will become more vulnerable to pressures. What can Australia do to minimise this risk?

**Minimising Risks**

Let me first dispose of two lines of approach which seem to me wrong-headed.

An editorial in the *Australian* on 13 February 1970 argued that by the end of the century Japan will be a post-industrial society and a super power. Japan, together with the USA, will dominate the Pacific. They will be enjoying per capita incomes up to five times higher than Australian unless the growth rate of the Australian economy is lifted. If such disparity develops, Australia can forget about keeping any meaningful degree of cultural and economic independence by the end of the century. Australia will have some chance of avoiding satellite status only if we can move into the post-industrial era at about the same time as Japan. This is possible only if there is a complete change in the philosophy behind our economic policies. What is required is a commitment to economic growth.

Allowing for exaggeration—the writer is not the first to have frightened himself by extrapolation of compound rates of growth—we may agree with the statement of the problem but hardly with the proposed solution. We may or may not aim at a still higher rate of economic growth in Australia, for our own reasons. But to make keeping up with the Japanese Joneses—perhaps I should say Tanakas—the overriding objective is neither sensible nor necessary nor realistic.

Much has been written in the last few years about the sources of Japan's unrivalled economic growth. An Australian who knows Japan well has put it this way:

The Japanese economy grows because the Japanese people as a whole put in much more than they take out, and because they work together, rather than against each other's interests. . . . In Japan individualism has never been important. . . . The basic feudal principles of group cooperation and fulfilment of obligations for mutual benefit continue to be the basic principles of Japanese life. . . . For the first time we are witnessing a Western
style economic system based not on our Western principles of free competition but on cooperation. Workers cooperate with management, companies cooperate within an industry, industries cooperate with each other, and industry, banking and government cooperate for the growth of the nation’s economy.9

We may wonder how long these social attitudes will withstand the changes that ever greater industrialisation, urbanisation, and (in some respects at least) Westernisation are bringing to Japanese society. Meanwhile, we cannot help but admire these qualities of the Japanese because the virtues of group loyalty and cooperation have formed a strand in the ethics of our own society from its own feudal origins. But with us they have become mixed with other values, individual freedom and initiative, the right of the ordinary man to go his own way, to look his boss in the eye and not be pushed around, which form an uncomfortable amalgam with the older ones but which we would not willingly give up. I do not believe emulating the Japanese way of organising their society or running their economy is the answer for Australia. We cannot transform our society into a Japanese-style one even if we want to. That is why I look askance at suggestions that we must learn from the Japanese ‘cooperation among business firms’ or ‘cooperation between government and business’. They are liable to mean rather different things in the Australian context.

What, then, are more realistic and promising ways of minimising the risks of economic dependence?

The first is, to put it crudely, to do everything we can to increase Japan’s economic dependence on us, by increasing our capacity to supply to Japan the things she needs, reliably and at competitive prices. This means using our own economic resources efficiently, minimising waste through excessive protection for inefficient domestic industries, taking advantage of what help we can get on reasonable terms and conditions from foreign, including Japanese, capital and technology—not cutting off our noses to spite our faces in the pursuit of a narrow spirit of economic nationalism.

The second is to make continuing efforts to diversify our own export markets. This means not merely vigorous promotion of exports to markets other than Japan, but also throwing our weight wherever possible behind the maintenance of a multilateral world trading system, against the formation of exclusive economic blocs.
We may not wish or be able to prevent Britain joining the European Common Market but we should support all initiatives that aim at breaking down protectionism, whether for agriculture in Europe or for industry in the United States and elsewhere. This, basically, is why I am wary of schemes such as PAFTA (Pacific-Asian Free Trade Area) for a new regional bloc centred on Japan. On the other hand, the same reasoning argues in favour of multilateralising our commercial policy relations with Japan within as wide as possible a regional grouping in the Pacific. The establishment of an Organisation for Pacific Trade and Development (OPTAD) advocated by Dr Drysdale and Professor Kojima could serve this purpose.

Thirdly, there is much we can do to minimise the risks of dependence by developing our relations with Japan into a many-sided partnership. As Peter Robinson has well put it: 'The simple business relationship, which almost by definition must be hard-headed and unsentimental, is plainly inadequate to cope with the emotional problems that will inevitably arise between two countries which are so deeply dependent on each other.' The desirable relationship, as another writer has said, is one of 'rigorous negotiation, tough competition and imaginative cultural and business interflow'. Not the least important task is to educate ourselves. Australians should start out from the assumption that 'the Japanese come from a rich and varied cultural background; that they are talented and honourable; that they are good people to do business with and that they have many admirable qualities from which we can learn something'. The man who wrote this may have been too pessimistic when he added: 'Unhappily, it looks as though a generation gap must be closed before even this modest and reasonable start can be made.' But talking and listening to a good many average Australians, one realises we have a good way to go.

Finally, while applauding the notion of a partnership with Japan, let me add a warning. There has been a good deal of talk recently, mainly emanating from official and unofficial quarters in Japan but sometimes echoed in Australia, about Japanese-Australian partnership in relations with southeast Asia, 'joint action' in aid and joint ventures in natural resource and industrial development. The idea appeals to some Japanese partly because they are conscious of southeast Asian reactions to Japanese economic penetration of the region and believe that joint action
with Australia might help to soften the image. I am all in favour
of co-ordination of our aid with Japan, and agree that there is
scope for joint ventures which will marry Japanese capital and
technology with Australian raw material supplies (as well as
capital and skills) and southeast Asian labour to everyone's mutual
advantage. But here, too, multilateral is to be preferred to bilateral
action. Australia has little to gain and much to lose by anything
that gives grounds for fears in southeast Asia of a ganging-up by
the two rich countries of the region.

Postscript
In the few months since this essay was written, the Japanese
economy has received a severe shock from the economic measures
announced by President Nixon on 15 August 1971. While there
is good reason to believe that most of the adverse effects will prove
to be only temporary, these developments demand some reassess­
ment of the prospects for economic relations between Japan and
Australia.

The most important of President Nixon's measures were a
demand for appreciation of the stronger currencies of the world,
backed by suspension of convertibility of the US dollar into gold
and by a 10 per cent surcharge on American import duties. Their
primary object was to correct the severe imbalance in the US
balance of payments. Their impact on Japan was the most drastic
because the Japanese yen had become the strongest currency as
a result of ever growing surpluses in the Japanese balance of
payments, not least vis-à-vis the United States.

As was pointed out in the essay, Japan had for some time
resisted demands for an appreciation of the yen, and the im­
mediate reaction of the Japanese authorities to the Nixon measures
was to do all they could to prevent such an appreciation. To hold
the exchange rate, hundreds of millions of US dollars were bought
by Japanese banks, a misguided step which still further reinforced
reluctance to appreciate, on the almost wholly fallacious ground
that paper losses would be incurred on the accumulated dollars.
Meanwhile, there was a dramatic loss of business confidence in
Japan. The stock exchange slumped, and export trading almost
came to a standstill because Japanese bankers and traders found
themselves unable to cope with the uncertainties caused by floating
Japan: Dependence or Partnership?

Exchange rates for the major world currencies. Economic growth levelled off. Industrial production actually declined for some time.

By November, it had become clear to the Japanese government that a realignment of the world's major currencies including the yen was unavoidable, and the yen was allowed to float upwards, relative to the US dollar, by some 10 per cent. Prolonged and difficult negotiations among the Group of Ten major trading countries, of which both the United States and Japan are members, finally brought agreement just before the end of the year. The United States agreed to devalue the dollar by 8 per cent and to lift the import surcharge, in return for a revaluation of the yen by 17 per cent (and of the major European currencies by smaller percentages) and for trade concessions by Japan to US agricultural exports. The Australian dollar was devalued, on average, by 1.75 per cent which implied an appreciation of 6.3 per cent against the US dollar and a devaluation of about 11 per cent vis-à-vis the yen.

In retrospect, it is clear that the whole episode was badly mishandled by the Japanese government, though its reluctance to move until the major European countries had agreed to assume part of the burden of adjustment is understandable, and it was undoubtedly under strong political pressures at home. A quick decision in August to revalue the yen by 12 to 15 per cent might have given Japan better terms than she had to accept in the end, while avoiding most of the setback in domestic business activity.

This is not to minimise the effects of the currency realignment on the Japanese economy. Japan's export and import competing industries have lost much of the price advantage in international competition they have enjoyed in recent years (although, to the extent that the remarkable growth in this price advantage during the past decade was due to a faster rate of growth of productivity in Japan, it may gradually reappear). While it should not take the Japanese economy more than a year or so to recover from the present recession, Japanese economic growth in the coming decade seems likely to be much less dominated by production for export. Indeed, one of the effects of the revaluation of the yen is a substantial improvement in Japan's terms of trade which means that she can henceforth secure a given increase in the volume of imports she needs at a smaller real cost in terms of exports and the resources required to produce them.
Some Japanese economic planners are envisaging a drastic re-orientation of the Japanese economy from export-led growth towards public investment in social capital to improve the quality of life in Japanese cities, and they claim to be confident that this can be achieved without a diminution in the projected annual rate of economic growth of 10 per cent during the 1970s.

If these plans are realised—and past experience discourages scepticism about what can be accomplished in Japan—there is little reason to revise downward the optimistic projections for the future of Australian-Japanese trade that were quoted in the essay. In the short run, Australian mineral exports to Japan will be adversely affected by the recession in Japan, and Australian companies exporting iron ore and some other minerals to Japan under long-term contracts denominated in US dollars will suffer a cut in earnings through the appreciation of $A relative to $US. The question of the most appropriate currencies in which to conduct bilateral trade between Australia and Japan, particularly in long-term contracts, which was foreseen in the essay, remains to be resolved.

The changes in exchange rates between the various currencies will have complex effects on Australian trade. The 11 per cent devaluation of the Australian dollar vis-à-vis the yen will make Japanese manufactures less competitive in the Australian market and will give Australian exports some price advantage over domestic producers in Japan, though the extent of the benefits of this for Australian export trade will be affected by the still greater advantage accruing to American exports, especially of agricultural commodities, from the greater devaluation of the US dollar and from the concessions exacted from Japan. They will also depend on whether Japan resorts to offsetting measures of commercial policy to protect some of her own industries or continues her recent policy of import liberalisation.

Looking further ahead, much will depend on the success with which the Japanese economy adjusts to the changes of 1971. If the optimism of Japanese economic planners that the projected growth rate can be maintained proves justified, even a substantial reorientation from export production towards public investment should make little difference to Japan's demand for Australia's minerals and rural exports. The reduction in Japan's export surplus which the change in the exchange rate is designed to bring
about will reduce one of the motives behind the expansion of Japanese investment abroad. But the main motives—the development of assured raw material supplies, reduction in transport costs and pollution through overseas processing of minerals, and export promotion for capital goods—will remain. The trend towards increasing investment of Japanese capital in Australia seems likely, therefore, to continue.

Thus, all in all, the optimistic prognosis reached in the essay stands in much less need of revision than seemed likely in the immediate aftermath of the bombshell of August 15. But it should perhaps now be interpreted as having been made by the author—with his fingers crossed.
China's Trade

Professor C. P. Fitzgerald, in his 1971 Roy Milne Memorial Lecture, expressed a view widely held in Australia at present when he said that 'economically China can become extremely important to this country'.¹ Others have put it even more strongly. Dr Rex Patterson has spoken of China as 'our fourth biggest trading customer in the world' and stated that 'China could [be] one of Australia's most important customers in the future and could [absorb] an expansion of Australian rural exports'.² A recent editorial in the Australian referred to 'China, potentially a huge market for almost everything we produce'.³

The object of this essay is to subject these prognostications to critical scrutiny.

The Myth of the China Market

The notion that China, with its teeming millions, constitutes a huge potential market goes back to the earliest days of the opening of China to Western traders. 'The Treaty of Nanking [1842] led to a great outburst of optimism among the industrialists and merchants of England. "The heads of staid manufacturers of Lancashire" were turned by the prospect of 300 million Chinese customers waiting to buy their shirtings.'⁴

In 1843, 1844, and 1845, when the northern ports had just been opened, the people at home were wild with excitement. An eminent firm at Sheffield sent out a large consignment of knives and forks, and declared themselves prepared to supply all China with cutlery. The Chinamen, who know not the use of knives and forks (or, as they say, abandoned the use of them when they became civilised), but toss their rice into their mouths with chopsticks, would not look at these best balance-handles . . . A London house of famous name sent out a tremendous consignment of pianofortes. The speculation was based, probably, on the

¹ First appeared as 'The Role of China in World and Australian Trade', Economic Record, March 1972.
In 1926, a writer on China's foreign trade commented on the phenomenon:

It may be remarked that the limited size of China's foreign trade has usually been veiled by expressions which call attention to the 'vast potentialities'. The trade of China has always exerted a certain power over the imaginations of those who have written from the point of view of export promotion. Such writers commonly accept four hundred million as the population of China and proceed upon this doubtful fact to build the most fanciful calculations of the magnitude of the trade to be expected... Every advance in the penetration of foreign trade has brought out exaggerations of this sort... The international jealousies exhibited in China throughout the period from about 1885 to the present day cannot be understood without bearing in mind the extravagant hopes that have been entertained of a vast and early increase in the foreign trade of the country.

In Australia, H. D. Black wrote in 1935 about 'China as a Possible Market for Australian Production'. He began by pointing out that

it is customary to regard China as a country of great potential demand. This indeed is a version of the oft-quoted remark of Wu Ting Fong which has currency in China, that if only her 400 million of people could be induced to lengthen their nether garments, what an increase in the demand for cotton cloth could be anticipated! Few beliefs are more firmly or widely held than this belief in the vast 'potentiality' of demand in China... But potential demand in China as elsewhere does not mean effective demand.

China's Role in World Trade

China has never yet played a major role in world trade. In the late 1920s, China, with more than one-fifth of the world's population, accounted for less than 2.5 per cent of world trade. Since then, China's share in world trade has declined very much further. It fell from 2.3 per cent in 1928 to 1.7 per cent in 1958 and 0.8 per cent in 1968. In the decade 1958-68, while the shares in world trade of Japan and Taiwan doubled, that of China halved.

Perhaps the most dramatic way of putting the present role of China in world trade into perspective is to point out that in 1969 the value of China's total foreign trade (exports plus imports)
amounted to only four-fifths of that of the city state of Hong Kong. It is, therefore, not surprising that there are few countries for whom China is at present a major trade partner. China is believed to account for about 70 per cent of the trade of Albania and 25 to 40 per cent of the trade of North Vietnam and North Korea. The only other countries of whose trade China accounted for more than 5 per cent were Ceylon, Hong Kong, the Sudan, and Singapore, while Tanzania, Malaysia, and Pakistan carried on 3 to 5 per cent of their trade with China, Rumania about 2.5 per cent, and Japan, Morocco, and Australia about 2 per cent. China’s share in the trade of the Soviet Union had fallen to 0.25 per cent.

These figures will come as a surprise only to those who unthinkingly assume that trade goes with size—of population or area. There are three reasons why China’s role in world trade must be expected to be relatively small and which, in fact, largely account for the situation exhibited in the statistics.

The first is her very size. Huge countries, such as China, the Soviet Union, and the United States, tend to have relatively low ratios of trade to national income because they are able to satisfy a large proportion of their requirements from their own resources.

The second is China’s poverty. The countries which dominate world trade are those with a high national income per head. China’s per capita income, estimated at around $US130, is still one of the lowest in the world. China’s trade is relatively small partly because the average productivity and therefore the average purchasing power of her 750 million people are still very low by international standards.

The third is China’s economic system. All the communist countries, or ‘centrally planned economies’ to give them their official designation, have tended to show relatively low ratios of foreign trade to national income, partly because of their desire to minimise trade dependence on the capitalist world, which at various times has been reinforced by political and practical obstacles to trade between communist and non-communist countries, but partly because the system of central planning is itself inimical to foreign trade: exports to uncertain world markets are difficult to plan for, foreign trade tends to be limited to making available exportable surpluses to pay for minimum import needs, and the practice of intergovernmental bilateral barter deals still further circum-
China's Trade

scribes the scope for participation in the worldwide network of trade. Communist China has never relied on bilateral intergovernmental barter trade to the same extent as the Soviet Union and the eastern European communist countries; for the most part she has bought and sold in international markets. On the other hand, since her political rift with the Soviet Union and its European Comecon partners, China has been even more reluctant to become dependent on trade with them than on trade with the capitalist world.

A ranking of the more significant trading countries of the world in order of the value of their foreign trade per head of population strikingly illustrates the significance of the three factors that have been mentioned. In the top bracket, with per capita trade of more than $US1,000, are the smaller of the rich open economies—and Singapore. In the second bracket are some of the larger industrial countries of Western Europe, together with Australia and New Zealand—and Hong Kong. The third bracket, with per capita trade of $US150 to 500, contains three 'dual economies' (Italy, Spain, and South Africa), two very large industrial countries (the United States and Japan) and the richer of the socialist countries of eastern Europe (Czechoslovakia, East Germany, Poland, Rumania, Yugoslavia). The USSR is to be found in the $US50 to 150 bracket with some of the more developed trading countries of Asia (Taiwan, Korea, Philippines, and Thailand), Latin America (Mexico and Colombia) and Africa (Morocco). Finally, in the lowest bracket are to be found some of the very poorest of the small less developed countries (Haiti, Chad, Upper Volta, Mali, and Ethiopia) and the four poor giants, Pakistan, Indonesia, India and—right at the bottom—China with a figure of $US5.

Prospects for the Future

There are reasons to believe that the situation described in the preceding section has begun to change, that the role of China in world trade reached its nadir in 1968.

The virtual stagnation of China's foreign trade in the past decade—even the 10 per cent rise from 1969 to 1970 failed to bring the value of her trade in the latter year to the previous peak attained in 1959—reflected a decade of stagnation in her domestic economy, or rather of violent fluctuations which left the country
no better off economically than ten years earlier. The chart showing the course of China’s total foreign trade since 1950 at first glance resembles one for the American economy during the interwar years: a boom followed by a catastrophic depression and after some years of recovery a further, less severe, recession. The great depression followed the disastrous Great Leap Forward of 1958/59; the milder recession reflected the Cultural Revolution. A further factor which pulled down China’s foreign trade was the rift with the Soviet Union which led to a steep decline in her trade with the communist (Comecon) countries throughout the 1960s.

In the past two years, China’s domestic economy and her foreign
trade have been recovering quite rapidly. The Cultural Revolution is over and there has been a marked change in Peking's posture towards the rest of the world. At home, the emphasis is once again on expanding production in agriculture and industry. Abroad, the Chinese government appears interested in normalisation of relations with the non-communist world (though hardly yet with the Soviet Union). There is every reason to expect that, so long as Peking stays on the new course, China's foreign trade will expand.

The change of course in Peking has, once again, 'led to a great outburst of optimism among the industrialists and merchants' of the West. Once again, there is a danger of 'the heads of staid manufacturers' being 'turned by the prospect of [750] million Chinese customers waiting to buy their shirtings'.

There can be no doubt that a steadily expanding Chinese economy will offer opportunities for steadily expanding trade with the non-communist world, especially while China remains reluctant or unable for political reasons to resume close trade relations with the Soviet Union and eastern Europe. To support an expanding economy, China needs much industrial equipment and a variety of industrial raw materials which she cannot yet produce at home on an adequate scale. While a new emphasis on agricultural development in domestic policy has already reduced China's dependence on wheat imports and may do so further, in the long run the difficulties of expanding food production in step with population growth are immense. Finally, if Chinese consumer spending is permitted to rise, there is a large potential market for imported consumer goods, high protein foods as well as manufactures.

But, once again, it is important not to be carried away by the prospect. There is as yet no evidence that China has moved, or is at all likely to move, away from the autarkic approach to foreign trade that has characterised her policy since 1949, a desire to minimise dependence on the outside world by aiming at maximum self-sufficiency. In any case, China's capacity to import, like that of any other country, is limited by what she can pay for. Unless she is willing and able to rely on large-scale foreign credits, which is most unlikely, she will depend on her capacity to expand production and sales of exports, mainly of textiles and other consumer goods. This is a market in which she will have to compete with
other industrialising countries—some of which, such as Hong Kong, Taiwan, and Korea, have a head start over her—and in which she is liable to come up against protectionist barriers in the advanced industrial countries.

Finally, one has to remember again the very small base from which any future expansion of China's foreign trade starts out. Assume that all goes well. Peking maintains its new relatively pragmatic line in domestic policy and relatively accommodating attitude in foreign affairs. There are no new domestic upheavals, no international wars. Assume that economic development within China proceeds apace in the coming decade and that her foreign trade, overcoming all obstacles, grows even faster. Let us make the optimistic assumption that China's real GNP grows in the coming decade at an annual rate of 7 per cent and that her foreign trade grows at 10 per cent a year. This will increase her relative share in world trade from 0.75 per cent in 1968 to 0.93 per cent in 1980 if total world trade grows at 8 per cent a year and to 1.17 per cent if total world trade grows at only 6 per cent a year. Even on the more extreme, and hardly realistic, assumption that China's foreign trade grows at an annual compound rate of 20 per cent, while the trade of the rest of the world grows at only 6 per cent, China will by 1980 only just have regained the relatively modest share in world trade she had in the 1920s.

Of course, these are crude global projections. For individual countries, such as Japan, which have advantages as competitive suppliers to China, trade with China may grow at a significantly faster rate than that of the rest of the world. Nor should anything that has been said in this section be interpreted as reflecting on the desirability of expanding trade with China. Such expansion is obviously in everyone's economic interest and cannot help but improve the chance of peaceful coexistence. But it is as well to maintain a sense of proportion about the prospects ahead.

**China's Role in Australian Trade**

To turn now from the world at large to Australia in particular. For Australia, China has been an important trade partner in the past decade. In some years, China has accounted for as much as 6 per cent of Australia's exports and has stood fifth as an export market, next to Japan, the United States, the United Kingdom, and New Zealand. But almost all of it has been wheat. In the
decade up to 1965, China made significant purchases of Australian wool, but these have shrunk to negligible figures in recent years. Wheat aside, Australian exports to China in the last four years have averaged about $A7 million, rather more than to Nauru, rather less than to Kuwait. Australian imports from China have risen gradually but have not yet reached 1 per cent of total Australian imports. The story of Australian trade with China so far is therefore almost entirely the story of Australian wheat sales.

Wheat

The role of wheat in Australian trade with China is not a post-war phenomenon. Wheat and flour were the main items in Australia's modest exports to China for much of the inter-war period. But the wheat sales to China of the past decade have dwarfed any that went before.

They began, quite suddenly, in December 1960. As farm output in China declined in the aftermath of the Great Leap Forward, the Chinese Government found itself compelled to make available scarce foreign exchange for large-scale wheat imports to fill the gap in overall grain supplies from domestic production. Throughout the 1960s, China imported some 4 to 6 million tons of wheat annually, from Australia, Canada, Argentina, and France. As domestic farm production recovered, the overall domestic food deficit receded as the prime motive for these imports. In some years, the Chinese Government felt able to divert part of the wheat purchased to Albania, Cuba, Tunisia, Morocco, North Korea, and North Vietnam in pursuit of larger political objectives. Wheat imports also enabled Peking to compensate for domestic transport difficulties in ensuring adequate supplies to the population of the northern cities. With world wheat prices depressed by surpluses in the main producer countries, it became profitable for China to import wheat cheaply, export rice, soya beans and other products at relatively high prices and use the net foreign exchange earnings for purchases of capital equipment and industrial raw materials.

For Australia, and especially for her wheat farmers, China's wheat purchases were a huge windfall. Overnight China became the largest single overseas market for Australian wheat, accounting in most years of the 1960s for about one-third of total wheat exports (and one-quarter of wheat production). The result was
unprecedented prosperity for Australian wheat farmers and an expansion of wheat acreage and production to unprecedented levels. In 1968/69 the crop of 544 million bushels was some three times the size of the average harvest of ten years earlier.\textsuperscript{8}

From the beginning, qualms and warnings were voiced in Australia about thus ‘making hay’ out of wheat, with little thought for the morrow. Economists pointed out that ‘it is unlikely that China will continue for long making such large orders as in the last five years . . . With the present large acreage, a sudden halt to purchases by China would mean much more dislocation to Australia. Our wheat growers, spoilt by unprecedented prosperity in the last five years, could be hard hit.’\textsuperscript{9} They drew attention to the fact that the Australian Wheat Board was selling wheat to China at prices not only well below the home consumption price but even below prices charged to other overseas customers.\textsuperscript{10} The Australian consumer and taxpayer was, in various ways, being made to subsidise not only the Australian wheat farmer but also China.

Few informed observers would doubt that within the existing Government policy framework the [Australian Wheat] Board has done the best job possible. The weakness lies in the present unrealistic basis for fixing the home consumption price, the guaranteed export price and the size of the guaranteed [production] quota, as well as in other forms of subsidization of our wheat industry.\textsuperscript{11}

Some were concerned that, quite apart from economic or commercial considerations, China might use Australia’s increasing dependence on her wheat purchases to exert political pressure. ‘I would not be surprised if China soon “confronted” Australia for “aggression” in South East Asia and our China sales might cease as suddenly as they began five years ago.’\textsuperscript{12} Others discounted this risk. The then Minister for External Affairs, Mr Paul Hasluck, staunchly announced in Parliament: ‘If China tried to blackmail Australia into supporting its admission to the United Nations by curtailing its purchases of wheat, Australia would respond as you should respond to a blackmailer. That means you tell him to go jump in the lake.’\textsuperscript{13} A newspaper correspondent took him to task: ‘The inference that China would resort to blackmail, or that she would use wheat sales as the medium, are both in the realm of phantasy, not politics . . . China buys our wheat for one
reason only. Because she needs it. If her need recedes, or if better terms can be obtained elsewhere, our sales will fall.\textsuperscript{14}

The warnings went unheeded. Australia was earning ample foreign exchange, the wheat industry was booming, China was paying punctiliously. As late as 1970, the Commonwealth Government decided to increase the wheat production quota for 1971 by 31 million bushels, even though the wheat carryover had reached 256 million bushels. Quite apart from the greatly reduced export prospects, as one commentator pointed out,

\begin{quote}
the main reason why it was wrong policy to increase the 1971 wheat quota is that it will induce thousands of growers to make wrong management decisions. There is nothing more important for the individual grower than to diversify his land use into growing more coarse grains (including maize and sorghum), oil seeds (including more rapeseed and safflower) and producing more meat (especially beef and veal).\textsuperscript{15}
\end{quote}

Wheat policy in Australia remained

\begin{quote}
not a product of careful economic calculus, but rather a fortuitous consequence of the peculiar constellation of the political parties in Australian politics. With the country vote exercising its disproportionately powerful influence, the question naturally poses itself: Has economic prudence a fair chance of prevailing over political expediency?\textsuperscript{16}
\end{quote}

‘Australia's Chinese chickens came home to roost' in 1971.\textsuperscript{17}

In April, it became known that the Australian Wheat Board had given up hope of securing its annual wheat contract with Peking. In July, the Chinese Government announced that it would buy wheat only from Canada, not from Australia: 'When China needs to import wheat it will continue to give first consideration to Canada as a source of supply.'\textsuperscript{18}

The prime motive in the Chinese decision was generally recognised to be reduced need. The year 1970 had yielded China a bumper wheat crop of 240 million tons, at least 40 million more than the average of the preceding five years.\textsuperscript{19} The greatly improved domestic supply position, with 40 million tons in storage above the commune level, permitted a sharp cutback in total wheat imports, and the fall in the world rice-wheat price ratio made the former swap trade policy less worthwhile. The decision to buy the balance from Canada rather than Australia may have
been influenced by quality differences and by the fact that Canada's wheat contracts with China each covered a period of years, while Australia's were for one year at a time.

China's decision, however, coincided with China's new foreign policy of seeking diplomatic recognition by Western countries and admission to the United Nations (on her terms) and with a change in the international political climate in which more and more non-communist countries were willing, even anxious, to form closer, or at least more normal, relations with China. It also coincided, in Australia, with the most severe crisis for her rural industries since the great depression of the 1930s, the combined effect of a drastic downturn in wool prices and the threat to several minor rural industries implied by Britain's impending entry into the European Common Market. The question of wheat sales to China became mixed up with political controversy over foreign policy.

The opposition Labor Party saw an opportunity to belabour the government and win wheat farmers' votes by attributing the Chinese decision to the government's political hostility towards communist China. It decided to send a delegation to Peking to secure new orders for Australian wheat, at least when a Labor Government was returned to office at the next elections. When the delegation reached Peking, the Chinese Government readily obliged—not with wheat orders but with the explanation that non-recognition by Australia and a generally hostile political attitude had been key factors behind the Chinese decision to give preference to Canada (which had recently recognised Peking). It is quite likely that there was at least an element of truth in this. Given the easier domestic supply position, and China's current foreign policy objectives, Peking had something to gain and nothing to lose by playing a little politics with wheat.

The future of Australian wheat exports to China is quite uncertain. If domestic production in China should fail to keep up with domestic requirements in the years to come, it would be surprising if she stuck to her boycott of Australian wheat, whatever Australia's foreign policy. If China is able to do without wheat imports, she will not buy from Australia, even under a most warmly disposed Labor Government. Only in a marginal situation, as this year, can she afford the luxury of mixing trade with politics. But for Australia it is only prudent to discount the likelihood of a resumption of large wheat orders from China, to
China's Trade

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do all she can to diversify both her wheat export markets and her rural industries. As it happened, wheat exports reached a record level in 1971/72, despite the loss of the Chinese market, confounding the dire predictions of those interested in magnifying the consequences of China's decision. With expanding sales especially to the UAR, eastern Europe, Japan, South Korea, and Taiwan, most of Australia's 518 million bushel surplus was sold, leaving a carry-over of only 150 million. But this achievement owed something to poor crops in the United States and the Middle East and will not be easy to sustain in the next few years. Prospects for diversification of crops depend largely on the courage of the government in the face of domestic political pressures. Some of it is already going on, but a good deal more may be needed, the more so as the Australian wheat farmer can no longer rely on wool as his standby.

Other Trade

There is little that needs to be said about the rest of Australia's past trade with China. On the export side, wool was 1963/64, sales to China have fallen to minute figures, disappointing earlier high hopes entertained in Australia. It appears that Australian wool has been a commodity that China has been able to do without, as, in the drive for self-sufficiency, domestically produced cotton has increasingly displaced wool and efforts have been made to expand domestic wool production (partly by importing Australian stud merinos). At various times in the past ten years, Australia has also sold to China modest quantities of tallow, zinc ore, oats, iron and steel products, and rutile. In the past year, following an easing of Australian government restrictions on exports to China of 'strategic' exports, several Australian firms are reported to have secured export orders, including a BHP contract for $A6.5 million of iron and steel products, a Comalco contract for aluminium ingots, and a Western Australian order for $A1 million of scrap metal.

Australian imports from China have risen steadily, from $A4 million in 1956/57 to $A32 million in 1969/70, raising China to fourth place among the less developed countries of Asia in the Australian market (next to Hong Kong, Malaysia, and India). The imports have consisted of a wide range of goods, including fish, meat and poultry products, bristles, gum resins, vegetable
oils, and food additives, but mainly and increasingly of cheap cotton and other fabrics, textile furnishings, ready-made garments and some durable goods, such as alarm clocks. China, like other communist less developed countries, has not yet been given the benefit of Australia's scheme for tariff preferences for less developed countries. (Australia does not select the beneficiary countries herself but leaves it to them to apply to GATT for status as 'less developed countries'.) On the contrary, Chinese textile exports have been among the chief victims of Australian protectionism. As recently as June 1971, the Australian Confederation of Apparel Manufacturers hit out at Australian retailers who import cheap garments from China and demanded additional protection from such low wage competition. The Labor Party delegation to Peking was told that the erection of almost instant tariff barriers against Chinese products in Australia, had been among the main motives for the Chinese decision to stop wheat purchases from Australia.

If the new course in Chinese foreign policy continues and the Chinese economy stays on its present upward trend, Australia can expect a steadily growing market in China, especially for steel products and conceivably (though improbably, because China's refining capacity is insufficient even to process domestically produced ores) for various minerals. There may also be again a market for wheat and wool, and certainly for some types of machinery and equipment. China's willingness to buy from Australia will depend more on the competitiveness of her products than on any Australian policies, and more on Australian commercial policy towards Chinese exports than on her foreign policy.

Such expansion of Australian-Chinese trade is to be wholly welcomed, whatever views may be held of China's political and economic system. But we should beware of falling victim, once again, to the myth of the China market, particularly when it comes to trading off prospective commercial gains for broader national interests. Even last year, when wheat sales were at their peak, our exports to China were worth only one-eighth of our exports to Japan. This is a figure that should be kept well in mind.
Economic Co-operation
Across the Pacific?

The theme of a conference held at Viña del Mar, Chile, in September 1970 was ‘Latin America turns to the Pacific’. The starting point was what was seen as the problem of ‘dependence’ of Latin America on the United States and particularly on the large American corporations. The question posed to the conference was whether this dependence could be reduced, at least for Chile and other countries of the Andean Group, by diversification, by closer economic and other relations with other countries of the Pacific basin, especially Japan, Canada, Australia, and New Zealand, and perhaps southeast and east Asia. This essay attempts to summarise the economic side of the conference proceedings.

Trans-Pacific economic co-operation was the subject of only one or two papers, although discussion touched on various aspects, especially towards the end of the week. The main reason was that so many papers were devoted to ‘dependence’ itself which, in all its aspects, became the dominant topic in the first few days.

A second major topic, tangentially related to the other two, was regional economic co-operation, particularly in the form of actual or proposed schemes for regional common markets or free trade areas, both among Latin American countries and among other countries of the Pacific, including Australia.

‘Dependence’
Dependence was the theme of numerous papers. It was also an undercurrent in several more and an aspect of the thesis, propounded by one or two participants, of the threatening dominance of the world by the great multinational corporations. Since in all cases dependence was presented as primarily on the United States,

it was a pity that no one was there to act as counsel for the defence of the accused.

As a newcomer to Latin America, I admit I left powerfully impressed by the intensity of anti-American emotion in Latin America. I was reminded of a statement by my old friend and master, Paul Rosenstein-Rodan: 'Perhaps the most valuable contribution of the U.S. to the Inter-American system is the fact that its presence constitutes the only common link between Latin American countries which is the resentment of the United States.'

The conference heard during the week a truly formidable list of charges against the United States, against US government and business policies towards Latin America.

In relation to trade, speakers denounced the excessive dependence of the Latin American countries, giving the United States power, deliberately or incidentally, to damage their economic interests by depressing the prices of their raw material exports, destabilising their export earnings and closing the domestic US market by protectionist policies.

In relation to aid, there were two complaints, not easy to reconcile: on the one hand, too little aid, on excessively onerous terms, and use of aid to exert political and economic pressure in favour of US foreign policy and of US business interests; on the other hand, the debilitating effect of aid in undermining national self-reliance.

In relation to US business investment in Latin America, numerous charges were laid against the operations of the multinational corporations, an almost limitless catalogue of evil effects, economic, political, social, and cultural.

In the economic sphere, the main grievances were the high cost of capital (profits), aggravated by monopolistic pricing, evasion of local taxation through transfer pricing and pressure to grant excessive tax concessions; adverse effects on the industrial structure of Latin American countries because US technology is unsuited to local factor proportions; inhibiting effects of the import of (often antiquated) technology through direct investment on local initiative in technological research and innovation; displacement of local business enterprise; and, according to one view, even adverse effects on the host country's balance of payments.

In the political sphere, two problems were stressed: the extra-territoriality problem, that is, the compulsory application to US
subsidiaries of US laws, e.g. on trading with communist countries or anti-trust legislation; and support for reactionary governments and vested interests, partly in favour of US business, but also of the ideology of private enterprise generally.

Finally, in the social and cultural sphere, speakers mentioned the reinforcement of domestic social disintegration, inequality of wealth and income, poverty, malnutrition, unemployment, appalling health and housing conditions, and economic stagnation; distortion of the productive system and allocation of resources in favour of 'consumerism', mainly for the benefit of the economically privileged classes in Latin America, from motor cars to mashed potatoes; last but not least, destruction of national identity, weakening of the national will, and domination of weak national states by the ever growing power of multinational corporations.

Not all who were concerned about the problem of dependence, in Latin America or elsewhere, would go all the way on all these points with the most extreme exponents. But few Latin American voices were raised in dissent from the general position, and at least one representative of the extreme view had been found from Canada, Australia, and New Zealand.

One or two participants from the western Pacific, while conceding the existence of the problem of excessive dependence in Latin America and Canada, were prepared to question whether all the problems of Latin America could be laid at American doors and the Indonesian word 'scapegoatism' was heard once or twice.

**Economic Nationalism**

There was much discussion of economic nationalism. When some critics characterised the majority view as an expression of extreme economic nationalism, majority spokesmen staunchly upheld nationalism as a necessary defence against US domination and against the multinational corporation. Both sides meant more by this than nationalism as 'pursuit of the national interest'. The critics claimed that there was far too much economic nationalism in the sense of policies hostile to foreigners even when such policies were against the longer-term interests of the country and of reluctance to co-operate with other countries for fear of giving up an ounce of national sovereignty. The majority argued that a resurgent economic nationalism was essential for the maintenance of national identity, as a precondition of any national effort to-
wards development and as a necessary basis for international economic co-operation.

From the discussions, three main lines of approach to the problem of dependence emerged:

2. Regional economic co-operation, e.g. through free trade area arrangements.
3. Diversification of external economic relations.

**Defence against Multinational Corporations**

At one extreme, supported by several though never stated explicitly, the only effective defence was seen in the overthrow of capitalism and its replacement by some form of socialism: nationalisation of foreign enterprise; exclusion of further foreign investment; and the establishment of a socialist system in which the state would control the economy, promote economic development and social justice by socialist policies. An Australian exponent of this view gave as models of successful nationalist economies: Japan, communist China, North Korea, and North Vietnam.

Others suggested various ways in which the adverse effects of foreign investment might be reduced. Legislation and administrative measures could provide for minimum local equity participation, to reserve key sectors or industries for local enterprise, to counter extra-territoriality claims, to limit local financing by foreign firms, to require disclosure of information, etc. New 'modalities' of transfer of capital and technology should be explored. Among the possibilities canvassed were investment-cum-import ('production-sharing' in Indonesian terminology), loans-cum-management contracts, equity to be transformed into loan capital. Other examples given included possible forms of marrying official aid with private investment for more efficient and directly productive use of aid funds; linking of foreign investment with regional integration plans in Latin America; and ways of 'untying' the package deal of capital, technology, and management, e.g. by following the Japanese example of relying on purchase of technology through licensing arrangements rather than on direct investment, and by state action to foster domestic research and technological innovation. Some put the emphasis on correction of short-sighted domestic policies which, they thought, were often
the real cause of high costs or low benefits of foreign investment, such as excessive tariff protection or tax incentive concessions.

At one extreme, there were those who did not believe that national governments in Latin America, caught up in the network of national and international capitalism, would have the will or the power to take the necessary steps. At the other, there were some who questioned whether excessive restrictions would not lose the benefits of foreign investment, necessary to rapid economic development especially in low-income countries.

**Regional Economic Co-operation, especially through Common Market or Free Trade Area Arrangements**

The papers and discussion on this subject fell into two quite distinct groups: groupings among Latin American countries; actual or proposed groupings among other countries of the Pacific region.

*Latin American groupings* were conceived primarily as a possible means of reducing dependence, partly by promoting economic development, through a more efficient allocation of regional economic resources and in other ways, and partly by strengthening the bargaining position of member countries vis-à-vis the United States. There was also a suggestion that the Andean Group might be an instrument for trans-Pacific economic co-operation.

Experience so far was not encouraging. The Latin American Free Trade Area had bogged down after an initial round of narrowly circumscribed tariff cuts. The Central American Common Market had over a longer period achieved considerable trade liberalisation and some expansion in intra-regional trade but had achieved little else and was now in a profound crisis owing to the mutual hostility of two member countries.

The left-wing view was that free trade areas and other forms of trade liberalisation constituted an altogether wrong approach to the problems of economic development, especially in Latin America. They were the intellectual product of antiquated ‘traditional economics’, a cover for the machinations of the multinational corporations and a weapon of the economically strong against the economically weak. Such trade expansion as had occurred in Central America had benefited only the multinational corporations. At best, advocacy of trade liberalisation reflected false values, overemphasis on economic efficiency and growth relative to social justice and the quality of life.
Others argued with no less conviction that, while it may be reasonable for the rich United States with its vast social problems to worry more about the quality of life and less about economic growth—and the same may soon become true also for Japan—rapid economic growth in the less developed countries of Latin America was essential if they were to keep up with population growth and to raise living standards, to have the resources for better education, housing, and social services, and that free trade had an important contribution to make through better static allocation of resources and by providing dynamic incentives to efficiency.

All agreed, however, that trade liberalisation was not enough, that regional economic co-operation should include positive measures, some urging regional planning of industrial development, others emphasising regional co-operation in specific sectors, finance, shipping, civil aviation, research, etc.

There was measured optimism that the Cartagena Pact which formed the Andean Group might be the start for a more successful experiment in regional economic co-operation, partly because it avoided any supranational institutions which would affront national sensitivities, partly because it was conceived as outward looking—a determination 'to opt in, not to opt out' of the world.

**Free Trade Area Schemes among other Pacific Countries**

Various papers put forward or discussed schemes for trade liberalisation among other countries of the Pacific. On closer inspection, they seemed only marginally relevant to the problems of Latin America. The Australia-New Zealand free trade area agreement might have been considered as a possible model, cautious but useful, for Latin American countries, but was in fact treated by a New Zealander as an example of the dangers of freer trade to weaker countries. The Japanese 'Pacific-Asian Free Trade Area' scheme for free trade among the five developed countries of the Pacific, it became clear, would have direct relevance to the Latin American countries only if and in so far as they were granted associate membership, which appeared to mean mainly possible non-reciprocal tariff concessions by developed member countries. From the Latin American side, fears were expressed that such a 'Rich Men's Club' would aggravate the difficulties of
less developed countries on either side of the Pacific in securing markets for their products.

Free trade, it was said, was the natural policy for Japan, which has grown into an industrial giant by protectionist policies. It was regarded as unacceptable even for Australia and New Zealand. Even a Canadian participant's balon d'essai about a Canada-Japan free trade area appeared designed mainly to impress on Japan the magnitude of the reciprocal concessions she would have to make, although he also held out a hope that such a proposal might jolt American policy makers into reconsideration of the increasingly restrictive trade policies of the United States.

**Scope for Trans-Pacific Economic Co-operation**

Relatively few papers dealt directly with this, the central, theme of the conference, although several dealt with, or gave background information on, co-operation in specific areas, such as shipping, civil aviation, and trade in minerals.

The central point that emerged was the almost total lack of contact and the mutual ignorance between Latin America and the countries of the western Pacific. Neither side plays a significant part in the trade of the other, though Japanese trade with Latin America (and on a much smaller scale Australian trade with Chile, Peru, and Mexico) has been increasing in recent years. The main obstacles hitherto have been: lack of complementarity among the national economies, mostly exporters of primary products and importers of manufactures; and distance, implying high transport costs and lack of mutual contact and knowledge.

The new interest in trans-Pacific economic co-operation on the Latin American side, especially in Chile, has its starting point in a desire to reduce dependence on the United States by diversification of external economic relations, trade, investment, finance, and technology. What are the prospects and possibilities?

A clear inference from all the papers and discussions is that prospects for diversification of Latin American trade across the Pacific centre overwhelmingly on Japan. Japan's phenomenal economic growth in the past decade, with its voracious demand for industrial raw materials, has already been responsible for a substantial shift of trade of all other Pacific countries from the Atlantic to the Pacific, and projections suggest that this trend will continue and intensify, based on projected growth rates of
Australia and Asia

the Japanese economy of 10 to 12 per cent per annum for at least another decade. Japan's growth will dwarf all other possible developments and policies in bringing about closer trans-Pacific economic relations and diversification of Latin American trade and investment.

The increasingly dominant role of Japan in trade and investment in the Pacific region is viewed with mixed feelings in the smaller countries, both developed (Australia and New Zealand) and less developed (southeast Asia and Latin America). A recurrent topic was the question whether it heralded exchanging dependence on the United States for dependence on Japan.

There was general agreement that, in the first instance and for some time to come, the emergence of Japan as a major trade partner would be advantageous to the smaller countries in one obvious respect: it would introduce an element of diversification, reduce dependence on a single dominant economic power, and open opportunities for playing one against the other—that Japan might in turn have opportunities to play one competitive supplier of primary products against the other was thought rather than openly said.

There was, in addition, the possibility that Japan would prove more flexible and accommodating than the United States to the needs of smaller countries. Japan's interest was primarily in assuring supplies of raw materials and markets for manufactures; for this reason, Japanese foreign investors were more willing to form joint ventures and less insistent on 100 per cent equity control. Japan also appeared more willing to facilitate industrial development in less developed countries, processing of raw materials and manufacturing (if only to take advantage of cheap labour and to export pollution problems). Japan's own experience of industrial development, based on purchase of foreign technology, may make the Japanese more sympathetic to the desire of Latin American countries to 'untie' the package deal of direct investment. Japanese economic policy has been consciously directed at structural adjustment of Japanese industry from labour-intensive towards capital and technology intensive industry and may therefore be readier than other developed countries to give increasing access to the Japanese market for manufactures of less developed countries. In the long run, finally, there were also prospects of increased Japanese demand for foodstuffs (of
special interest to Australia and New Zealand) though at present agricultural protectionism was still very entrenched.

A cynic was heard to remark that in twenty years' time, Latin Americans might look back wistfully to the good old days when they had only Americans to cope with. Meanwhile, it was nice to think that there were some reasons for optimism about what closer relations with Japan had to offer.

All other Pacific countries offer prospects quite secondary by comparison with Japan.

Canada's interests in Latin America are concentrated outside the countries of the Andean group. To some they are suspect as representing American corporations at one remove.

Australia has some trade with Chile, Peru, and Mexico and a few small joint ventures are under consideration. Both will increase but in the overall picture their significance is and will remain minute. Shipping is a major obstacle, but this is a chicken-and-egg problem. Possibly Australia has something to offer to Latin American countries from her own experience, e.g. in developing relatively efficient industrial plants of medium size suited to smaller markets.

New Zealand may be forced to diversify further her export markets if Britain joins the European Economic Community, but it is difficult to believe that Latin America offers substantial outlets for New Zealand's main export products.

With southeast Asia there are hardly any contacts as yet, though there may be scope for some trade with the rapidly growing industrial economies of Singapore, Hong Kong, Taiwan, and Korea.

Communist China and the Soviet Union were mentioned, the former as unquestionably an important factor in Pacific trade some time in the future, the latter as a tough trading partner and competitor with Chile as a producer and exporter of copper.

There was no reference at all to European countries, Britain, Germany, France, Italy, Belgium, Scandinavia. All these are still significant trading partners and at least one, Germany, a major investor in Latin America. One wondered whether the Latin American countries, in their obsession with the US ogre, are not ignoring opportunities for diversification in this direction. Interesting examples of opportunities outside the Pacific region were given in relation to copper: a joint venture between Chile and
Rumania, trading arrangements with Yugoslavia, the CIPEC association with copper producing countries in Africa (Zambia and Congo). Perhaps there is some danger in excessive concentration on one region in a world economy?

What Can Be Done?

Even the greatest enthusiast for trans-Pacific economic cooperation cannot believe that it can make a decisive contribution to the solution of Latin American problems. This must come from within Latin America, and it is not for an outsider to suggest what forms it should take. But perhaps I may be allowed the fool's licence of a few presumptuous comments.

I could not help being impressed, and I confess a little dismayed, by the conviction so apparent among the Latin American participants that socialism is the answer, and by the overtones of willingness among prominent intellectuals to depart, if necessary, from the constitutional road to achieve this objective. I was a convinced socialist for many years. But the experience of socialism in operation in many parts of the world in the past twenty-five years has made me sceptical. In the communist countries, the price paid in terms of human suffering during revolution and civil war and in terms of freedom under ruthless dictatorial régimes is as daunting as the increasingly apparent inefficiency of a centralised command economy, if only because of the incidence of planning errors of catastrophic proportions. In Western economies, the traditional panaceas of democratic socialism, replacement of private by state enterprise, central planning, and direct controls have been found to be either irrelevant to the main problems of stability and growth or positively deleterious.

No one wants a return to laissez-faire. The state obviously has a positive and increasing role in the economy. But its major function, as I now see it, is to facilitate, and create an environment conducive to dynamic enterprise, whether public or private, and for this purpose the carrot and stick of competition in the market is still the most efficient instrument available. Protection of high-cost producers is sometimes necessary, but in the long run it is the greatest enemy of efficiency and economic progress. In this context, removal of trade barriers has an important role to play.

Above all, there is the point stressed by several speakers: the scarcest resource is not capital, still less mineral deposits, but
human capital, the skills needed to develop and adapt and use modern technology. Some will say that capitalism must be got rid of before education and research will receive adequate attention. Others may feel that more would be done now if so much of the energy of intellectuals and political leaders were not devoted to the politics of getting rid of capitalism.

 Enough of this. Granted that trans-Pacific economic co-operation can make only a marginal contribution, how can this contribution be enhanced?

Relatively few substantial suggestions for deliberate policies came out of the discussions, apart from the almost automatic expansion of trade with Japan.

Here is a list which others will, I hope, amplify.

There is some scope for promotion of trade between Chile (or the Andean Group as a whole) and the smaller countries of the western Pacific—by trade missions, in some cases by mutual official representation or bilateral trade agreements.

Efforts should be made to develop more regular shipping services, if necessary by trade commitments which will ensure adequate base cargo.

As both Latin American and western Pacific countries develop more export-oriented industries, there should be increasing opportunities of trade in manufactures.

Here and there, e.g. between Australia and Chile or Peru, joint ventures in manufacturing, especially processing industries, may be feasible.

There may also be scope for co-operation among the major producers of minerals, such as copper and iron ore, e.g. Australian and perhaps Indonesian co-operation with CIPEC and between the major suppliers of iron ore to Japan.

At a rather different level, there is scope for consideration by the developed countries of the Pacific, Japan, Australia, New Zealand, and Canada, whether they should not do more to direct towards Latin America some of the development assistance, in aid and trade, that they have in the past concentrated on less developed countries nearer home. A vertical relationship has developed in aid and trade among developed and less developed regions—of Japan (and Australia) with southeast Asia, of the United States with Latin America and of Europe with Africa—which has undesirable features. One paper outlined the needs of
the less developed countries of Latin America for preferential treatment in trade and other areas, to offset in some measure the existing inequality of wealth, competitive ability, and bargaining power between rich and poor.

Finally, there is an irrefutable case for one line of approach. In Dr Wionczek's words:

While some possibilities can be envisaged for opening Latin America to the so-called Pacific market for capital and technology, perhaps the most urgent and most beneficial in the short run for Latin America would be to open communication and information channels between 'the strangers in the Pacific basin'.

In this task the conference made a useful start.
Private Investment in Asia

In April 1969, the Australian Council for Overseas Aid, the umbrella organisation of voluntary foreign aid societies and agencies, held a seminar in Sydney on 'Joint Ventures and Investment in Developing Countries of Asia and the Pacific'. It was something new for ACFOA, the reflection of a growing feeling among its leaders that some of the money contributed by the Australian public for aid to less developed countries might be better spent in promoting a better understanding of the problems of economic development, and of ways in which Australia could contribute to their solution, than on the usual activities of voluntary aid organisations. The topic was chosen in the belief that direct investment by Australian companies, even if it was actuated by business motives, could make such a contribution.

The seminar was attended by representatives of almost 150 Australian firms actually or potentially interested in direct investment in southeast Asia. It was addressed by the Commonwealth Treasurer, by the Vice-President of the Asian Development Bank and other specialists on problems of economic development, by a group of Australian businessmen with personal experience of successful ventures of this kind and by representatives of some Asian countries who explained their governments' policies towards foreign investment.

Motives for Investment

The seminar itself was a joint venture of a kind, but the objectives of the partners differed in various ways.

The Council for Overseas Aid represents voluntary bodies whose motives are primarily humanitarian, that is they are

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primarily interested in what Australia can do to help our neighbour­
bouring countries. The businessmen, inevitably and properly, are
concerned with the business interests of their companies; their
object is profit or at least the expansion of their business. And
the Australian Government clearly is concerned with Australia’s
national interests as it sees them.

Of course, these three groups have something in common. Their three objectives can in some degree be reconciled, because mutual benefit can be obtained from the process of overseas in­
vestment. Just as we in Australia benefit from overseas capital
while the overseas companies come here for the benefits they
obtain, so it is reasonable to assume that, while overseas invest­
ment by Australian companies will contribute to the economic
development of the countries in which this investment is under­
taken, it will also yield profits to the companies and may in various
ways contribute to Australia’s national interests in trade and
development.

But even if we allow for this mutual benefit, the fact remains
that, while the Council for Overseas Aid is primarily concerned
with the benefits that such overseas investment can give as aid to
the development of our neighbouring countries, overseas invest­
ment will in fact be undertaken by Australian business firms only
to the extent to which they can see opportunities for profitable and
safe investment; and before the Australian Government gives any
positive help it needs to be convinced that such overseas invest­
ment is in Australia’s self-interest, however enlightened the inter­
pretation they give to this self-interest.

In the past, neither the former motive, the business motive for
businessmen, nor the latter, the national interest motive of the
Australian Government, has induced much Australian investment
abroad. In 1967/68 total overseas investment was of the order of
$A30 million. Of this $A17 million went to Papua New Guinea,
$A2 million to the Pacific countries, and only $A3 million to the
whole of Asia.

The explanation for these small figures is simple. The main
motives, both from a business and from a national point of view,
which have induced the very large volume of direct foreign invest­
ment by the major investing countries in the past two decades,
have not been of much significance for this country, nor are they
likely to be for some time.
In the case of Japan, official policy in favour of direct investment overseas has been motivated mainly by two factors of great importance to the Japanese economy. One has been the need to develop resources and ensure raw material supplies which Japan needs and must get from abroad. The other has been the need for markets for the heavy industries which have increasingly replaced the light consumer goods industries in relative weight in the Japanese economy and which require export of capital together with export of capital goods. More recently, these motives have been reinforced by the mounting surpluses in the Japanese balance of payments; export of capital has been the alternative to an appreciation of the yen which would adversely affect the competitive strength and profitability of Japanese export and import competing industries.

In the case of the older capital exporting countries, the United States and the industrial countries of Western Europe, the main motives for overseas investment have been to find markets for their capital goods but also to retain markets for a much wider range of manufactures in the face of tariff protection for local industrialisation in the developing countries; in other words, to keep their foot in the door. To some extent also, overseas investment has offered more profitable opportunities than investment opportunities available at home.

None of these motives is as yet of major importance in Australian economic policy. We do not have the Japanese motive of resource development to assure overseas raw material supplies. We are not yet a major producer of capital equipment or exporter of manufactures generally (though both these aspects are becoming more significant). Nor is there any lack of domestic investment opportunities; indeed they greatly outrun the supply of capital available from domestic saving. Inevitably in the circumstances we are and will remain a major capital importing country. This does not mean, as the government is beginning to recognise, that we cannot afford any capital export, but the pressures on Australian business to invest abroad are clearly not nearly as great as in some other developed countries.

**Climate for Investment**

Scope for overseas investment is, to quote one of the speakers at the seminar, partly a matter of the philosophy of investment in
the exporting country and partly of the climate of investment in the potential capital importing countries. In both respects, there has been a very great improvement in the last few years. The Commonwealth Treasurer's very firm statement to the seminar that the Australian Government is not opposed to overseas investment was one that would not have been made by a Commonwealth Treasurer five years ago. Indeed, the Australian Government has, as he pointed out, taken some steps positively to encourage such investment.

Similarly, as regards the investment climate in the Asian countries, there has been an enormous change in the last ten years or so. The seminar was not reminded sufficiently of the extent to which, even ten years ago and certainly in the post-war years, private foreign capital was unwanted in most of the Asian countries. India, Indonesia, and most others in various degrees, were positively hostile to private capital inflow in the form of direct investment, mainly as a reaction to the experience of past colonial exploitation and partly because in so many of these countries the prevailing ideology was hostile to private enterprise in general. It is a very important fact that there has been a marked change in this respect in most of these countries, though not in all. Burma, for example, which was hardly mentioned at all, still has an inward looking policy which is prepared to give up economic development rather than risk dependence upon other countries. But in India, and more recently in Indonesia, there is now a strong interest in attracting foreign capital and a very different attitude to private enterprise, domestic as well as foreign.

Indeed, as one listened to the salesmen of the various Asian countries exhibiting their wares and trying to lure Australian businessmen to their own countries, one could not help feeling that some of these countries may be a bit too anxious. Each of them has developed all sorts of incentives to attract foreign capital, in the form of tax holidays and the advantages of pioneer industry status. Some economists believe they may be going too far in this direction.

In providing such tax and other incentives, they compete with each other. The situation is assuming something of the character of competitive advertising of toothpaste which very largely cancels out. No one can afford not to advertise because he will lose his share of the market and yet, in the aggregate, total consumption
of toothpaste is not increased. The net result is considerable expenditure in selling costs for which we all pay in the price of the toothpaste.

Countries like Singapore and Malaysia appear to be engaging in such competition. They lose a good deal of tax revenue without adding to the total supply of foreign investment capital. It has been suggested that if only they could get together and in co-operation cut back these tax incentives, the desired effect on foreign investment might be accomplished much better by spending the extra revenues on the infrastructure, power and harbour, banking and other basic facilities, which are much more important to foreign investors than a tax advantage.

A recent study of foreign investment in Singapore has brought this out. Many of the foreign investors said in answer to questions on the point that the tax incentives were not very important to them because they were quite willing to pay what they regarded as 'reasonable' taxation, by which they meant the rates they are used to in their own countries. (This of course does not apply to double taxation arrangements which are very important but only to special concessions of the pioneer industry status type.)

The seminar heard about the sort of problems that face Australian firms thinking of overseas investment. It is my impression that the problems were rather understated, partly because the panel represented some of the most successful Australian firms, partly because they are large firms, and partly because they have operated in the countries where things have been relatively easy, such as Singapore and Malaysia. The problems are still enormous in countries like Indonesia and I suspect also a good deal greater in India than the very successful experience of the Repco company might suggest. Other countries were not mentioned at all, such as the Philippines, Burma, Pakistan. It would be interesting to know whether there is any experience of Australian attempts to invest in these countries.

It was suggested by a foreign visitor that Australian business firms enjoy special advantages, as compared with, say, American or Japanese or German or British, in investing in the smaller countries of southeast Asia. He suggested for example that because Australia is a country which has 'only recently crossed the threshold to prosperity' we have more sympathy with the under-developed countries. I do not think he realised that, as far as we
can tell, per capita income in New South Wales in the 1880s may have been the highest in the world. Australia's background is so very different from that of the Asian countries that, if anything, it is a handicap. Very few Australians, unless they have lived there for some time, have any idea of how different the problems and conditions of these countries are and how much they have to adapt their attitudes.

Again, the same speaker suggested that the proximity of Australia to the southeast Asian countries is an advantage. This is a very common and very doubtful proposition. When one looks at Australia's trade relations with Indonesia one finds two countries, each of them in its own right a very large trading country, immediate neighbours, and yet practically not trading with each other.

The fact is that geographical proximity is not in itself a reason for trade except to the extent that transport costs are lower, and for various reasons transport costs are not necessarily all that much lower between Australia and the southeast Asian countries. What matters above all is whether the countries are complementary in their economic structures, and the Australian economy in its foreign trade has been if anything competitive with the trade of most of the southeast Asian countries. Only recently, with the development of Australian exports of manufactures, has there been a measure of growing complementarity.

A very important point was made by one of the speakers. What matters in relation to the investment climate for Australian investors in these countries is not so much the law as it appears in printed form, but how the law is applied. One need only think of the example of Indonesia but in some degree this applies to all countries. The extent to which bureaucratic red tape, or delays in implementing the law, may affect him is something the investor can only find out when he goes there; he cannot get it from the printed text of the brochures or the law itself.

Several members of the seminar emphasised that the single greatest difficulty facing the investor is uncertainty about market prospects, arising partly from political risks inherent in political attitudes of governments, partly from the scarcity of statistical information, and partly from the very nature of economic development from relatively low levels of per capita income. Another problem stressed by several speakers concerns recruitment
of expatriate staff and staff conditions when a company sends people from Australia to these countries.

A point that was not mentioned and on which I would have liked to have heard some comment is the question to what extent expansion of Australian overseas investment is in any way restrained or hampered by the fact that many of our large companies are themselves subsidiaries of foreign companies. We know that, in the field of exports, restrictions placed on export franchises of Australian subsidiaries by the overseas parent companies have caused concern in Australia. In many cases they are international corporations with subsidiaries in several countries. They have marketing arrangements that divide the world into market areas and are reluctant to allow the Australian subsidiary to compete with sister organisations in Asian markets. One wonders how far there would be similar constraints on Australian subsidiaries of international corporations in considering overseas investment.

These are all important issues, but they are secondary as compared with those problems confronting the potential Australian investor which are simply the problems of underdevelopment. Indonesia is, of course, the supreme example of these problems, though it is important to recognise that many of them are still very important in some other southeast Asian countries and probably also in India.

There is, first, the problem of inflation. Attention was drawn to the high interest rates that prevailed in Indonesia during the years 1965-9. They were of course a reflection of inflation. The success of the Indonesian Government's stabilisation policies of the last two years gives reason for hope that some of these problems will be much less serious in future.

There are, secondly, the basic symptoms of underdevelopment: bureaucracy and red tape, corruption, inadequate transport and power supplies, ports and shipping, banking and practically every other facility that the Australian company takes for granted at home, but which present enormous problems in Indonesia. An example was the great difficulties the Kiwi Co. had in securing land to build its plant somewhere near Djakarta. There was plenty of vacant land but all of it had been taken over by people squatting there illegally, yet the Indonesian Government did not think it was politically possible to throw them off the land to hand it over to a foreign company.
Thirdly, another aspect of underdevelopment, there is the shortage of staff of adequate quality at every level from managerial and technical people to skilled workers. The countries of southeast Asia are looking for foreign investment partly as a means of imparting technical and managerial know-how to their own people. They therefore insist that foreign firms should increasingly employ and train local staff. Yet the difficulty of finding people with the necessary minimum qualifications and experience is very great in most of these countries. Just as we in Australia are not always prepared to acknowledge that Australian experience and know-how are inferior to those of Americans, so the people in these countries are not always prepared to admit that their own staff do not quite measure up.

What can be done by the Australian government to facilitate private investment in Asia? Let me summarise possible measures briefly under two headings. First, policies and techniques that are already in operation; secondly, suggestions for the future, some that were mentioned in the course of the seminar and perhaps one or two ideas of my own.

**Current Policies on Investment Abroad**

Under the heading of existing policy, there is first the point I have already referred to, that the Australian Government is not opposed to Australian overseas investment. Although overseas investment by Australian companies requires exchange approval, this is generally given for direct investment projects. (The Treasurer said 'generally'; it would be interesting to know of any cases where exchange approval was refused.)

Secondly, the government has taken a positive step to encourage such investment by the Overseas Investment Insurance Scheme which is essentially a scheme designed to enable investors to insure against political as contrasted with commercial risks.

Two questions about this arose in my mind. First, how far is this scheme an adequate substitute for the investment guarantee agreements that have been negotiated by the United States with various countries, and also by the Netherlands and some other capital exporting countries. I understand they are designed to fulfil the same purpose, but I am not sure whether the investment guarantee agreements go further and whether there would be a case for extending the Australian scheme in that direction.
The second point, which came out during the seminar, is that the scheme appears to have one or two loopholes that may be important. One speaker mentioned that the scheme covers only investment projects which will promote Australian exports. There may be projects, beneficial to the companies for the return they give and indirectly to Australia for the markets they will ultimately open up, which do not immediately involve any exports of Australian goods. Another gap appears to be that the scheme does not cover shipments to a company that is partly owned by the Australian concern, such as joint ventures. This again would appear to be a gap that might well be filled.

The Department's representative at the seminar expressed surprise that there might be cases of investment well worth undertaking even if they are not wholly designed to promote Australian exports. One cannot help but be surprised by the extent to which the Department of Trade considers itself to be purely a salesman of Australian exports. The Department might well consider whether some overseas investment is not worth promoting in its own right, apart from the indirect effect it may have in promoting Australian exports.

The third existing policy which is relevant and important relates to double taxation agreements. Most of these of course have been concluded with countries investing in Australia, but there is now an increasing number with countries in which Australia might want to invest. The discussion left me a little uncertain whether there are still significant areas in which the lack of a double taxation agreement is a serious deterrent to overseas investment by Australian firms. The case of double taxed royalties from Malaysia was mentioned, but I am not clear whether this is a serious problem. In any case, as was correctly pointed out, the Australian Government is more likely to be impressed by pressure for double taxation agreements exerted by a foreign government, such as the Government of Malaysia, rather than by any Australian business interests here.

Another point may be relevant. The Treasurer mentioned that these agreements are very complicated and take a long time to negotiate. Another speaker mentioned that efforts are being made to devise an international model double taxation agreement. Perhaps the use of such a standard model agreement might expedite legislation. I suspect that the Australian Government, and in many
cases the other government as well, would have so many special wishes that a standard model would not satisfy them, but the idea may be worth looking into.

Fourthly, the Treasurer and one or two others mentioned the LDC Preference Scheme, the scheme of the Australian Government for preferential tariffs for exports of manufacturers by less developed countries to Australia. This of course is not directly relevant to the theme of this seminar. But it is very important for the developing countries to expand and develop their export industries. For this reason it would be very desirable if some of the overseas investment from Australia and other countries went into export industries. The Government of Taiwan, which like many other countries insists on a minimum equity participation for local capital in any overseas investment projects, is prepared to trade this insistence against the export component of the output of the enterprise. The larger the proportion exported the smaller is the required local equity participation they insist on; if it is all exported they are prepared to allow 100 per cent foreign equity. They argue that the advantage that a foreign company can bring through its overseas contacts and its knowledge of foreign markets is well worth the price.

Let me throw out another idea in connection with the LDC Preference Scheme. Is there perhaps scope for using the scheme as an indirect way in which the Australian Government might give a little encouragement to Australian companies to invest abroad by in effect arranging for an automatic extension of overseas preferences to the products of companies established by Australian businesses in less developed countries? An assurance that the products produced, say, in Malaysia would be given preferential access to the Australian market might act as an incentive to an Australian company to go and invest there. In many cases, of course, it would not be relevant because they would be producing the very things they are producing in this country, but there may be some scope for this, for example, in processing industries.

Finally, among the existing policies, there is the Trade Commissioner Service. Their primary job is as salesmen. Trade Commissioners have not hitherto been much concerned with assistance to Australian firms interested in investing overseas. In fact, complaints were made at the seminar precisely on this point. It may
be desirable to treat this as an expanding function of Australian Trade Commissioners.

Some Suggestions

Finally, a brief comment on four suggestions that came up during the seminar, four new ways in which the Australian Government could further stimulate and assist overseas investment by Australian firms.

One idea that was mentioned several times is based on the example of investment corporations in various of the big investing countries, Japan, the United States, the Netherlands and elsewhere. The suggestion was made that Australian companies, whether in finance or in trade or in overseas investment, might get together and form a corporation which would provide equity funds for participation in such overseas investment schemes. It is my impression that this is premature for Australia. I find it difficult to believe that scope for overseas investment by Australian companies is as yet sufficient to warrant the establishment of a major specialised financial institution, though Australian participation in a multinational corporation of this kind is feasible and is, I understand, under consideration.

There may also be scope, not perhaps immediately but at least before long, for linking government aid with expanding overseas private investment by Australian business. It was pointed out several times that governments in some of the investing countries directly participate through the provision of equity funds to companies which in turn finance overseas investment. Would it be possible, for example, for the Australian Resources Development Bank to consider taking an active part in this field, by using its own funds or funds provided by the Australian Government for minority equity participation in some private overseas investment by Australian firms? The immediate reaction of Australians to any such idea is liable to be objection to the Australian Government making taxpayers' money available to private enterprise. Perhaps this hostility would not now be as strong as it would have been ten or fifteen years ago but it would probably still be a major deterrent.

There would be much less ground for such objections if the aid element were given more stress. Granted that the Australian Government is prepared to give economic aid to the developing
countries, why not channel some of it through Australian private investment overseas, but on the understanding that the equity capital contributed in the first instance to the Australian venture, particularly as a joint venture, would gradually over a period of years be turned over to the Asian partner? Most suitably, it would become the equity of the Asian host government. In some cases it might be vested in a foundation or trust in the Asian country which could use the income for educational and social purposes in the same sort of way as, in the United States in the nineteenth century, land development rights were handed over to educational institutions, the famous Land Grant Colleges. This might be a way of making effective use of Australian aid funds for economic development by linking it with the managerial and technical know-how of private investment.

Secondly, a number of suggestions were made at the seminar in the broad area of investment information, the need of Australian investors to find out more about the problems confronting them, whether they relate to the legal investment climate, or administrative arrangements and regulations, or problems of finding a joint venture partner. A group of firms has already done just this by establishing an investment centre in Djakarta. One wonders if this might be worth doing in other Asian cities.

A related point that came up in the discussion concerned investment information for Australian firms that might be interested in tendering for major construction projects in Asian countries, such as those financed by the Asian Development Bank, which are open to international tender. It was pointed out that the Asian Development Bank does not quite know whom to inform about such tenders in countries like Australia. Could some government or other body make itself responsible for collecting this information and making it available to Australian business firms periodically in the same sort of way as Commonwealth Government tenders are announced in the Government Gazette?

Thirdly, I might mention a project that is being promoted in Australia by the Australian Institute of Agricultural Science. This is the idea of establishing, probably in Indonesia, an Australian Agricultural Development Institute designed to make available to Asian countries the considerable expertise of Australians in the field of agricultural science and agricultural economics. Its primary object is to be research, but combined with training and extension.
This is relevant because a great many of the most important investment opportunities in the Asian countries are in the area of industries ancillary to agricultural development. These countries need a great many things, from fertilisers and pesticides to pumps and sprays and other kinds of agricultural machinery. It is in any case desirable that we should give this kind of technical assistance, but it is possible also that through such an Agricultural Development Institute Australian firms may become aware of opportunities for export, and perhaps investment in the manufacture, of these kinds of product.

Finally, let me stress a general point, made by several speakers, of which the others are to some extent examples, the idea that it ought to be possible to narrow and eventually do away with the gulf between government in the business of aid and private enterprise in the business of investment. There are ways of marrying the two activities, of channelling government aid in various ways through overseas investment. This, after all, was one of the main ideas of the organisers of the seminar. In stimulating thinking on these lines and throwing out a variety of suggestions the seminar amply justified their initiative.

Postscript

In the past two years, there has been some further expansion of Australian direct investment in Asian countries, though the amounts involved do not seem very large. Figures are hard to come by, since hardly any statistics are published in Australia and we have to rely on those published by some of the Asian host countries. The latest available figures show thirty companies with Australian participation operating in Indonesia, fifteen in Malaysia, six in Singapore, and an unknown number with a total investment of $A0.6 million in Thailand. Projects insured under the Australian overseas investment insurance scheme, as at 30 June 1971, also included projects in India, Cambodia, and Taiwan, as well as seven non-Asian countries.

The Australian Government is moving cautiously towards a more sympathetic attitude to such investment, with the initiative coming mainly from the Department of Trade and Industry. An inter-departmental committee is understood to be looking at ways in which the overseas investment insurance scheme might be liberalised, for example, by extending it to projects involving
Australian exports of services, such as consultant services, as well as goods. But the export promotion motive still seems strongly entrenched. Investment guarantee agreements are still officially dismissed as excessively ambitious. But some progress has been made towards double taxation agreements with Asian countries in which Australian companies invest. An agreement has been concluded with Singapore, and agreements with Malaysia and Indonesia are under consideration.

One other development to be recorded is the establishment of the multinational finance corporation for investment in Asia to which the essay referred as being planned. PICA (Private Investment Company for Asia) was incorporated in 1969, its shareholders consisting of major companies from the United States, Japan, and a third group including Europe, Canada, and Australia. The initial list of Australian shareholders comprises nine of Australia's largest companies, among them: BHP, CSR, CRA and the Bank of New South Wales. Early in 1972, PICA established an office in Djakarta to promote and finance investment projects, both foreign and domestic, in Indonesia.
Regional Economic Relations—Looking Ahead

In economic forecasting for a single country, one can focus in the first instance on a particular variable, the rate of economic growth, for which one can attempt to set likely upper and lower limits. For the pattern of economic relations between the countries of a region this is not possible. While the pattern will be influenced by the rate of economic development of the region as a whole and of particular countries within and outside the region—and about this one can make assumptions—the emphasis must be on the changing structure and directions of flows of trade in products and factors of production and on the economic, political, and institutional forces which will influence this changing configuration. There are no upper or lower limits. Only a maze of possibilities.

I therefore propose to select first, rather arbitrarily, four economic trends which are fairly predictable, though their consequences are not: population growth; economic growth in Japan; the Green Revolution; industrialisation. I shall speculate on their likely implications for regional economic relations in our part of the world. In doing so, I shall abstract from major political changes—wars, revolutions, takeovers—in the region. In the last section, after a brief discussion of the prospects for regional economic co-operation and of Australia's own economic role in the region, I shall take a look at what might be called a 'Comecon' scenario.

Population Growth

The population of the eight countries of southeast Asia (excluding Burma) is estimated to have totalled 240 million in 1970 and to have been growing at a (weighted) average rate of

nearly 3 per cent a year. While in Singapore efforts at population control have in the past ten years brought down the annual rate of growth to 1.5 per cent, in most of the region the rate of growth is still accelerating towards the Philippine figure of 3.5 per cent. Birth control is now officially encouraged in most of the countries of the region (including Indonesia, which accounts for nearly half the total population) but the most optimistic estimates of what population control can achieve in the region during the next decade do not go beyond holding down the annual growth rate to 3 per cent. With luck, some reduction in the rate from that level may become practicable during the 1980s. Assuming an average rate of growth of 3 per cent a year, the population of the region will reach 320 million in 1980 and 430 million in 1990.

While so much is almost certain, there is little one can say about the implications of population growth as such for economic relations among the countries of the region. Population growth in itself does not create markets. It creates a need for food and jobs. The important questions are whether agricultural development based on the new technology can expand food production ahead of population growth and whether industrialisation can be expected to proceed at a rate sufficient to keep the growth of unemployment within bounds, and these questions are best left for separate consideration.

Here it will be enough to mention three ways in which population growth in southeast Asia is likely, or liable, to affect regional economic relations. There is some risk that domestic food production will fail to match population growth, at least in some countries (most likely on Java) and in some years (of bad seasons or bad management). There may be years of famine or severe food shortage, with implications for domestic economic and political stability in the countries concerned and for food aid from potential donor countries. There is a more likely and serious prospect of unemployment reaching such dimensions in parts of the region (especially in Indonesia and the Philippines, but also perhaps in Thailand, Malaysia, and Vietnam) as to cause social and political unrest. Even if these threats are kept at bay, both agricultural and industrial development will contribute to urbanisation; unless policies for decentralised urban development prove much more successful than seems likely, the growth of the southeast Asian metropolitan cities from their present populations of
3 to 5 millions towards 7 to 10 millions will give rise to immense social problems.

**Economic Growth in Japan**

Recent estimates by the Japan Economic Research Centre, quoted in the Asian Development Bank report on *Southeast Asia's Economy in the 1970s*, forecast an annual rate of growth of real GNP in Japan of 12.4 per cent during 1970-5 and 10.8 per cent during 1975-80. In 1980, Japan's GNP will exceed that of the United States in 1969. The contribution of agriculture to Japanese national product is expected to fall from 10 per cent in 1965 to under 5 per cent in 1975, while output in the manufacturing sector is expected to grow at an annual rate of over 16 per cent to 1975 and only slightly more slowly to 1980. In consequence of these developments, Japanese imports of foodstuffs, mineral fuels, wood and wood products, and light manufactures are likely to increase sharply, whilst imports of textile raw materials will grow more slowly. The value of imports will rise from $US16.9 billion in 1970 to $US72.9 billion in 1980.2

These figures are so phenomenal that they are hard to grasp and harder to credit. Yet every past forecast of Japanese economic growth since 1950, not least by the Japanese planners themselves, has proved to be an underestimate. It is only prudent not to dismiss these projections as fanciful.

If the forecasts prove correct, Japan's economic growth will be the single dominant factor in the economic development of the region and by 1980 Japan will be by far the largest single market and source of imports of virtually every country in the region (including Australia). For southeast Asia, for which the Asian Development Bank report gives estimates, Japan's share in the region's exports is expected to grow from 23.5 per cent in 1967 to 53.5 per cent in 1980. Japan's share in the region's imports will grow even faster if Japanese capital export (aid or private investment) or further import liberalisation removes balance of payments obstacles. No corresponding estimates for Japan's share in Australian trade in 1980 are available. But there is no doubt that if Japan continues to grow so much faster than the rest of the world, her share in Australian trade will also continue to grow, in this case with a continuing large balance of trade in Australia's favour.
To the countries of southeast Asia, as to Australia, the pull of Japan's economic growth will appear as a mixed blessing. By providing a relatively nearby, large and rapidly expanding market for their minerals and other primary products (and increasingly also for a great variety of manufactures) Japan's growth will make all the difference to their own growth prospects, very greatly reducing and in some cases virtually eliminating what would otherwise be almost insuperable balance of payments obstacles to rapid domestic economic development. But the price of this inestimable benefit will be increasing dependence on the Japanese market for their exports and at least for the southeast Asian countries (much more so than for Australia) dependence on Japan as a source of external finance and capital goods and on Japanese firms as major partners in domestic enterprise.

Trade is a two-way business. Both partners benefit. The same is true, generally speaking, of international lending and borrowing and direct investment. There is no case for imputing to Japan sinister motives of 'domination' over her trading partners in the region. But it is undeniable that once a large country accounts for one-half or more of the trade of a smaller partner, it is in a strong position to bargain for economic, or even for non-economic, favours. Fear of Japanese domination will probably lead individual countries in the region to forgo occasional commercial advantage for the sake of minimising dependence on Japan and may induce attempts by Japan's partners in the region to strengthen their own bargaining position by collective action. But such policies are unlikely to make more than a marginal difference.

Apart from large-scale international conflict, there would seem to be only two circumstances that might put a sharp brake on Japan's economic growth and its consequences for the regional economy. One is a worldwide recession or depression, resulting from a breakdown of the international monetary system or from domestic recession in the United States or from a mutually destructive tariff war. Such an event would hit Japan particularly severely, but it is difficult to believe that it would continue for long unchecked and that it would interrupt Japanese economic growth for more than a year or two. The other possibility is domestic social and political pressure for a sharp shift in the allocation of Japanese resources from directly productive towards social overhead investment. Some such shift is now officially
planned, but it is an open question whether this will prove sufficient to meet public demand and whether a much larger shift would be compatible with the dynamics of the Japanese business system which is the engine of Japanese economic growth.

The Green Revolution

A great deal has been written about the prospects and implications of the Green Revolution in Asia and I need not go over all this ground. There is fairly general agreement that the effective application of the new agricultural technology in southeast Asia, first to rice and later perhaps to other crops, would for an almost indefinite period allow food production to keep ahead of population growth, but that in practice the obstacles to effective application are still very great: difficulties in meeting the very large demands of the new technology for irrigation water, fertiliser, and rural credit and extension services; difficulties in pursuing price policies which will give farmers adequate incentives to adopt the new techniques; difficulties in making the new varieties resistant to disease and palatable to consumers in different countries; and finally the risk of social unrest in rural areas if the Green Revolution greatly aggravates inequalities of income and wealth.

My concern here is to indicate some possible or likely effects of the Green Revolution on international economic relations in the region. If it is successful not merely in producing more rice to match the growth of population but in reducing the cost of production of rice, it can become the source of a large and sustained growth in the real incomes and purchasing power of the huge population of the region, both of the rural producers and of the urban consumers of rice. This, as much as rising real incomes through industrialisation, may be the basis for increased domestic saving and increased foreign trade. But while acting as a stimulus to the overall growth and trade of the region, the spread of the new agricultural technology may have favourable and adverse effects on the trade of particular countries and in particular products. If the drive towards self-sufficiency in rice in countries like Indonesia and Malaysia is successful, the traditional rice exporting countries, Burma, Thailand, and Vietnam, will face serious problems, although a marked fall in the world price of rice may open large new markets in Mainland China (which has hitherto preferred to buy cheap wheat and sell dear rice) and in
Korea. It will also remove the case for food aid (thus aggravating the budgetary problems of countries like Indonesia and the surplus problems of the wheat exporting countries) but possibly strengthen the case for fertiliser aid. Finally, it will greatly reinforce the economic case against subsidised rice production and in favour of reliance on rice imports in Japan—and perhaps in Australia.

**Industrialisation**

That all of southeast (and south and east) Asia will be much more industrialised in the 1980s than now there can be no doubt. On whether industrialisation will be sufficiently rapid to match the growing need for jobs, especially in the most densely populated countries, we can only gloomily speculate. (There is much discussion at present of more ‘employment-oriented’ industrialisation, but one cannot be very optimistic that deliberate attempts to promote more labour-using technologies or product-mix will have much effect on the overall result.) Here, as in relation to agricultural development, it will be more fruitful to highlight possible effects of industrialisation on regional economic relations.

A crucial issue will be the relative weight placed in the various countries of the region, advanced as well as less developed, on import substitution or export-oriented industrialisation. The last few years have brought a healthy reaction in southeast Asia against the strategy which, largely through Indian interpretation of the Soviet model, became fashionable in the 1950s: planned industrialisation based on import substitution in the home market and excluding foreign direct investment. The experience of many Latin American countries, as well as India, Pakistan, and the Philippines, has demonstrated the unfortunate effects of systematically fostering inefficiency. At the same time, the experience of Hong Kong, Taiwan, Korea, and more recently Singapore has given impressive evidence of the very rapid expansion of exports of manufactures that can be achieved by developing countries, without any special discrimination in their favour, by efficient domestic policies. But the obstacles to the adoption of efficient domestic policies are still so great, the pressures of domestic vested interests for protection of high cost producers in the home market so powerful, and the planning and control ideology so deeply entrenched, at least in the larger countries such as India, Pakistan, and Indonesia (but also in Ceylon and Burma) that the
most one can hope for is a gradual shift towards more export-oriented industrialisation.

There is very little doubt that such a shift would mean a higher rate of domestic economic growth, higher levels of average real income and more international trade. It would also mean a rather different commodity structure of trade in the region, with greater emphasis on natural resource based (mineral and other processing) and labour-intensive export industries in most of the less developed countries and on more selective development of capital and technology intensive industries in the advanced countries of the region, such as Japan and Australia.

A related issue arises from the much discussed concept of 'agreed specialisation'. There is no doubt that much more efficient allocation of resources throughout the region could be brought about by various countries agreeing to specialise, each in a limited number of manufacturing industries producing for the whole regional market. Even its advocates concede that agreed specialisation is feasible only among countries at similar levels of economic development, say among the less developed countries of southeast Asia, as the ECAFE Secretariat has proposed, or among the advanced countries of the Pacific (Australia, New Zealand, Japan, and perhaps Canada and the United States) as suggested by Kojima, Drysdale and others. Without being excessively optimistic about the rate of progress that can be achieved in this direction, it may well be that by the 1980s a measure of agreed specialisation in consumer goods industries among the ASEAN countries and in heavy engineering, chemical and mineral-processing industries among Australia, New Zealand, and Japan will have been brought about.

**Regional Economic Co-operation**

The last paragraph has already touched on some of the ideas for regional economic co-operation that are in the air. One cannot rule out the possibility that by 1980, or at least by 1990, some of the countries of the region will have formed something like a Maphilindo or ASEAN free trade area, but progress (if any) in that direction will be very largely dictated or circumscribed by political conditions. De facto rather than de jure, regional economic co-operation may by then be largely centred on Tokyo. The OPTAD (Organisation for Pacific Trade and Development)
proposed by Drysdale may well come into existence in the next few years and may develop into the framework of a 'Co-Prosperity Sphere' with or without the nasty overtones of the 1940s.

None of the more formal international agencies, such as the Asian Development Bank, ECAFE, or the proposed regional currency area, seems likely to make a major impact on regional economic relations. On the other hand, political circumstances permitting, it does seem likely that private foreign investment in the region will increase very greatly in the next decade, by Japan but also by other advanced countries including Australia and increasingly also among the less developed countries (there is already quite a lot of Philippine, Taiwan, Hong Kong, and Korean investment going into Indonesia). This may justify the creation of a 'GATT for Foreign Investment' for the region, such as has recently been proposed on a worldwide basis.4

Australia and the Region

I am inclined to leave it to the reader to assess for himself how all the developments I have sketched are likely to affect Australia. But I should make one point that is easily overlooked.

Next only to Japan (and perhaps China) the country whose economic growth will most influence that of the region as a whole is Australia. If, as seems quite possible, Australia's real GNP doubles in the next decade and her foreign trade grows at least in step, there will be a considerable spillover to the countries of southeast Asia. In 1967, Australia and New Zealand between them took less than 4 per cent of southeast Asia's exports and supplied only 4.6 per cent of the region's imports.5 By 1980, Australia's share alone will almost certainly be substantially higher, how much higher depending partly on the steps Australia will be prepared to take to allow easier access to her domestic market for the light manufactures of the less developed countries of the region.

By 1980, and certainly by the end of the 1980s, it is reasonable to expect Australia to have become a major supplier to the southeast Asian countries of heavy industrial products, durable consumer goods, chemicals, electronic and other equipment, perhaps also of quite a lot of military hardware. In addition, Australian industrial companies will have established subsidiaries or joint ventures producing such products in local factories in Indonesia.
and elsewhere. Australian banks, finance and insurance companies, consultants and accountants, airlines and tourist agencies, will have branches and offices in the region; even Australian-owned shipping may have come to play a substantial role. Quite a lot of Australian money will have been invested in or lent to southeast Asian countries.

In other words, by the end of the 1980s, political developments permitting, Australia will in a smaller way play something of the economic role towards the countries of southeast Asia that Japan will be playing towards both her and them.

A 'Comecon' Scenario

So far I have ruthlessly cast aside doubts that have assailed me (and no doubt the reader) about the realism of speculations about the southeast Asian regional economy on the assumption that nothing much will change politically through the 1980s. Let me therefore conclude by going to the other extreme.

Let us assume that by the 1980s all of Asia except Japan has become communist: Indochina swallowed by Hanoi; Thailand, Burma, Malaysia, Singapore more or less peacefully 'accommodated'; South Korea, Taiwan, Hong Kong taken over; Indonesia and the Philippines (and for good measure India, Pakistan, Ceylon) conquered by revolution. What sort of trade and other economic relations with a Comecon Asia can one envisage for Australia? (We will assume that Australia and New Zealand are not immediately threatened though no doubt, rather like Sweden, spending a lot on defence.)

Some may argue that it would make little difference because by the 1980s the communist monolith will have disintegrated, Hanoi an Asian Belgrade, trade across the Bamboo Curtain expanding as busily as across the Iron Curtain in Europe. Some such trend is possible, even likely, but its favourable consequences for regional economic relations are easily exaggerated.

East-west trade in Europe has been expanding, but the decisive fact is that 65 to 75 per cent of the trade of the European Comecon countries is still with one another. North Korea and North Vietnam have virtually no trade with non-communist countries except a little with Japan. Only China conducts the major part of her trade, willy-nilly, with the non-communist world. China has had to seek trade outlets with the rest of the world since her
quarrel with the Soviet Union has caused Sino-Soviet trade to languish. But the role of foreign trade in China's socialist economy is, and will almost certainly remain, much the same as in the Soviet economy, a necessary evil, kept to the minimum (determined by inescapable import needs and exports to pay for them) both by a desire to minimise dependence on the outside world and by the difficulties of fitting foreign trade into domestic planning in a centralised command economy.

Australia will certainly have trade with a communist Asia, but it will be very much smaller in volume and rather different in character: largely within a framework of bilateral inter-governmental trade agreements, aiming normally at bilaterally balanced trade, the Asian countries will order selected Australian industrial products (but almost exclusively producer goods) and perhaps considerable though fluctuating quantities of food grains (wheat and rice) and some minerals, offering in exchange light manufactures as well as some tropical produce.

With opportunities for trade expansion with the rest of Asia much reduced, Australia (and New Zealand) will become even more dependent on trade with Japan and will probably need to find ways of expanding trade with the Americas. If Japan, too, were to go communist . . .

The point of the Comecon scenario is not to suggest that it is probable. It is rather to inject a measure of realism about the likely consequences for the future of Australia's foreign trade of more limited communist territorial expansion in our part of the world.
Endnotes

TRADE RELATIONS

2 Mr R. G. Strange, quoted in *Export News*, Export Development Group of NSW, 5 August 1963, p. 3.
3 Crawford, op. cit., p. 233.
4 Ibid.

JAPAN: DEPENDENCE OR PARTNERSHIP?

1 I owe these three quotations to an editorial in the *Australian Financial Review*, 2 March 1971.
6 *Australian*, 2 February 1971.
8 Quoted *Canberra Times*, 28 April 1971.
12 Ibid.

CHINA'S TRADE

3 Ibid.
12 E. J. Donath, in the *Age*, 19 July 1965.
13 Quoted in the *Age*, 15 December 1964.
14 Ibid.

PRIVATE INVESTMENT IN ASIA


REGIONAL ECONOMIC RELATIONS—LOOKING AHEAD

2 Ibid., para. 36.
3 Ibid., Table 2.
5 Asian Development Bank, op. cit., Ch. iv, para. 45.
Further Reading


Official information on Australia's political and economic relations with Asia is provided in the monthly publication of the Department of Foreign Affairs, *Current Notes*; unofficial but authoritative analysis and comment in the two periodical publications of the Australian Institute of International Affairs, *Australian Outlook* and *Australia's Neighbours*. The *Australian Financial Review* gives the most comprehensive coverage of day-to-day developments.

On Australian economic aid to Indonesia, see the *External Aid Bulletin* of the Department of Foreign Affairs (e.g. November 1971). For a critical comment by a political scientist, P. Eldridge, 'Australian Aid to Indonesia: Diplomacy or Development?' *Australian Outlook*, August 1971. On the volunteer graduate scheme in Indonesia, Ivan Southall, *Indonesia Face to Face* (Lansdowne Press, 1964) is still worth reading.


The most valuable source for discussions of trade policy problems in the Pacific region are the successive volumes of proceedings of the Pacific Trade and Development Conferences: *Measures for Trade Expansion of Developing Countries* (1966), *Pacific Trade and Development* (1968) and *Pacific Trade and Development II* (1969), published by the Japan Economic Research Center, Tokyo, and *Foreign Investment in Asia and the Pacific* (ANU Press, 1972).

**China.** Little has been written on Australia’s trade with China. Apart from the references given in notes to the essay, mention might be made of a third article by J. Wilczynski, ‘Sino-Soviet Trade and Defence’, *Australian Outlook*, August 1966, and of a recent article by Audrey Donnithorne, ‘China as a Trading Nation’, *Bank of New South Wales Review*, December 1971.

**Private Investment in Asia.** In addition to the ACFOA pamphlet in which the original version of the essay was published, and the study of *Foreign Investment and Industrialisation in Singapore* mentioned in a note to the essay, and the book on *Foreign Investment in Asia and the Pacific* mentioned above in the section on Japan, readers will find interesting an earlier paper by Helen Hughes, ‘Australians as Foreign Investors: Australian Investment in Singapore and Malaysian Manufacturing Industries’, *Australian Economic Papers*, June 1967.
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