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A PERSPECTIVE OF THE AUSTRALIAN ECONOMY: A JAPANESE VIEW

Kiyoshi Kojima

and

A CURRENT PICTURE OF THE JAPANESE ECONOMY AND ITS PROBLEMS

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AUSTRALIA-JAPAN RESEARCH CENTRE

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INTRODUCTION

Australia is certainly "a lucky country". Its 14.5 million people, approximately the population of Tokyo, enjoy a mature welfare economy on a vast resource rich continent which covers an area over twenty times that of Japan. There is every reason why Australia should be envied not only by Japan but also by overpopulated neighbouring Southeast Asian countries, such as Indonesia, the Philippines, Thailand, Malaysia and Singapore, and even by the small island nations of the South Pacific.

Australia can be characterised as a "rich middle-size economy". Her present high standard of living and splendid welfare state economy have been realised as much through appropriate policies for national economic development on the part of her government and her people (including immigrants) as by sheep, wheat and a fortunate succession of discoveries of underground resources (Section II).

The most significant aspect of her recent history is the great change in her external economic relations. Since the end of World War II, Australia has moved decisively away from her traditional orientation towards the United Kingdom (the "mother country") and Western Europe and towards Asia, more precisely, the Western Pacific (Section I). This has indeed been a "great transformation". If, however, Australia wishes to complete her transformation into one of the leaders in the Asia-Pacific region successfully, and to live and prosper with Asia, she will need to change her present economic policy which has been excessively concerned wih welfare and the protection of domestic industries. What direction should Australia take to transform and develop her economy further? Upon this depends not only the future of the Australian economy, but also its relations with neighbouring economies (Section III).

I. THE GREAT TRANSFORMATION

Mother Country Oriented Economic Development

The British began to settle in Australia in the late 1780s, 80 years prior to the Meiji Restoration in Japan. After that and perhaps up to World War I, Australia promoted her economic development along the lines of so-called "staple theory". Put simply, Australia specialised in the production of wool for export to the United Kingdom, which was a captive market. The Gold Rush of the 1850s provided the stimulus for economic development, and the production and export of a staple food, wheat, was expanded. On the other hand, Australia imported from the mother country almost all manufactured products, such as consumer goods, investment goods, railways and shipping. In short, its economic development was dependent upon the United Kingdom, and oriented entirely to Europe.

Emergence of Mercantilist Trends

Industrialisation in Australia began only in the 1920s. Australia keenly felt the urgency of industrialisation as a substitute for imports during World War I, because of the unavailability of European manufactured goods. The world depression of the 1930s made further industrialisation essential in order to maintain and expand employment opportunities. But Australia's small population scattered over a vast area, together with the high cost of inland and coastal transportation, meant small compartmentalised markets and the production of a wide variety of manufactured goods in small-scale factories. Rivalry among the states inhibited the establishment of large-scale factories in the most suitable location, and led to smaller and inefficient factories being established in each state. Thus Australia was unable to achieve economies of scale in the manufacturing sector and efficiency remained low. Complex protection measures at levels higher than in most developed economies and various governmental interventions were therefore required to prevent foreign competition. Kasper and others call this the "Mercantilist Trend".[1] In a wider sense, it could be called the "Welfare State Trend", since this depends heavily on mercantilist external economic policies.

By contrast, the United States of America (present population 240 million), also a colonial economy, shifted from the export of staples (wheat and raw cotton) as early as the end of 18th century, and embarked on the industrialisation which resulted in its becoming the world's greatest industrial nation. Its success was due to the advantages of economies of scale. On the other hand, Malaysia, whose population of 13 million is about the same as Australia's, has remained basically a staple exporter, with far less advanced industrialisation and a per capita income about a quarter of Australia's.

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1. "One we call 'the Mercantilist Trend' which amounts to a continued short-sighted, interventionist muddling on, whose results we do not find disastrous - simply unattractive, unpleasant and unjust to large segments of the community, especially the young."

   "The other scenario we call 'the Libertarian Alternative'. Libertarian is used to capture the ideas of a market-oriented economy for both outputs and inputs, in which firms and individuals rather than government make and take responsibility for decisions and where market prices, rather than bureaucratic regulations and political lobbying are met by direct forces of change. Distribution objectives are met by direct income transfer arrangements rather than by intervention in commodity and factor markets."

   Wolfgang Kasper, Richard Blandy, John Freebairn, Douglas Hocking and Robert O'Neill, Australia at the Crossroads: Our Choices to the Year 2000, Harcourt Brace Jovanovich Group, Sydney, 1980, p. x.

On the other hand, the medium-sized "White Australian" economy has succeeded in creating a rich welfare state while maintaining both staple exports and small-scale inefficient industry. The difficulty facing Australia, however, is the realisation that the status quo is imposing limits to further economic development, but at the same time being unable to find an easy way to throw off protectionism.

Towards an Asian-Pacific Orientation

After World War II, leadership of the world economy and the role of providing the mainspring of development shifted from the United Kingdom to the United States. The United Kingdom had been interested in the European Economic Community since its formation in 1958 and, after some vacillation, formally entered the European Community in 1973. Australia (and New Zealand) thus abandoned by the mother country, lost all the protection and preferential captive markets which the United Kingdom had provided, and trade with United Kingdom was no longer the "engine of growth" for Australia.

In the Asia-Pacific region, the Japanese economy made a successful recovery in the 1950s, rapidly developed heavy and chemical indstries in the 1960s and became a huge market for overseas products, especially natural resource goods, raw materials and food. The resource-poor newly industralising countries (NICs) - South Korea, Taiwan, Hong Kong and Singapore - have grown rapidly, and the other ASEAN countries, not to mention China, can be expected to take off in modernisation and industrialisation in the not too distant future.

The development centre in the world economy has shifted from Europe or the Atlantic basin to the Asian or Western Pacific region, which contains great potential for rapid growth. If we include the already enormous markets of the U.S.A., Canada and some Latin American economies, the Pacific Region is really a huge new frontier with which Australia should intensify interdependence and share economic development and prosperity.

Since World War II, the Australian economy has experienced transformation in its orientation. The share of Australian exports going to the European Community, including the United Kingdom, rapidly decreased from 54 per cent in 1955/56 to 14 per cent in 1977/78, while the share going to North America remained almost constant at 15 per cent and 13 per cent in the respective years. On the other hand, Japan's share of Australia's exports increased rapidly from 14 per cent to 32 per cent, while China, Northeast Asia (South Korea, Taiwan and Hong Kong) and the five ASEAN countries taken together, have steadily increased their share from 6.8 per cent to 17.2 per cent over the same period.

II. ECONOMIC DEVELOPMENT WITH DUAL STRUCTURE

Australian Trade with Japan and Asia

Since World War II, Australia has turned her eyes towards Asia: but has she achieved the kind of transformation of economic development strategy appropriate to closer interdependence with Asian economies? The answer is "no". On the one hand, her staple export trade in primary products has been intensified by the mining boom, but on the other, export-substitution type industrialisation based on inefficient, small-scale enterprises has been further promoted under heavily protectionist policies. In short, dual-structure economic development and welfare state policies have been maintained and intensified.

In response to the rapid growth of Japanese heavy and chemical industries in the 1960s, Australia experienced a mineral resources boom in iron ore, coking coal, bauxite, and so on. As well as mineral resources, exports to Japan of agricultural products such as wool, beef, butter and cheese, feedgrains and sugar expanded rapidly, and this rapid expansion of trade with Japan worked as a major engine of growth for the Australian economy. Japan had faith in Australia as a highly dependable supplier of food and raw materials, and the Japan-Australia economic relationship became very close and significant to both countries.

In the 1960s, Japan had a large trade deficit with Australia (for example, in 1962 the import and export value was US$435 and US$135 million respectively, or a ratio of 3 to 1). By 1978, Japan's imports had increased twelve-fold to US$5,300 million and her exports had increased twenty-fold to US$2,692 million, so that her import surplus ratio was reduced to 2 to 1. There has been pressure within Japan to find markets for manufactured goods to correct this trade imbalance, but these pressures have been modified since Japan recognises that a trade deficit is inevitable, given the benefits of procuring natural resource based goods from Australia. Australia is currently experiencing a second mineral boom, and is exporting steaming coal, uranium, natural gas and so on to Japan. On the other hand, Australia continues to maintain high protective measures on manufactured goods, so as a policy solution incentives have been provided for Nissan and Toyota to engage in direct foreign investment behind the protective barriers. There is some doubt as to how satisfactory a solution this will prove. In this way, the Japan-Australia relationship has maintained reasonable stability by means of a two-pronged policy, namely, approval of Japan's huge trade deficit and expansion of enterprises overseas instead of exporting.

In comparison with South Korea and other Asian countries, as well as with Japan, Australia's natural resource based goods sector is overwhelmingly strong compared with its manufactured goods sector. Progress in the industrialisation of the latter group of countries results in a welcome opportunity for the growth and diversification of Australia's markets for natural resource based goods, eliminating the fear of over-dependence on the Japanese market alone. To realise this opportunity, however, Australia must be prepared for a influx of labour-intensive manufactured goods from Asian countries. Australia's response to industrialisation in the NICs and ASEAN should not result in policies similar to those hitherto directed at Japan. In order to "live and prosper together with Asia", Australia must undertake a fundamental structural reorganisation of her manufacturing industries and excessive welfare-state policies.

Mining Boom Reconsidered

Australia is regarded as a "lucky" country. Not only is she endowed with agricultural products such as wool, wheat, sugar, butter and cheese, but also, during the 1960s, there was rapid development in exports of iron ore, coke, bauxite, etc. Given her large reserves of uranium, steaming coal and natural gas, the potential for wider export specialisation is increasing. However, there is a stream of thought emerging in Australia which suggests that rapid expansion of the mining sector is not necessarily beneficial for economic growth in general, and, in particular, for employment expansion. Gregory's model is representative.[1] As labour and capital were competitively attracted to this sector, they consequently received a rise in their rates of remuneration. In addition, both the inflow of foreign capital and the increase in export earnings caused an appreciation of the exchange rate and an acceleration of inflation. All these factors have led to the weakening of the manufacturing sector. It cannot be denied, however, that the development of export-oriented large-scale mining brought about a substantial increase in incomes and in demand for domestically manufactured goods.

A similar dilemma exists in Indonesia and other oil-exporting countries. Although endowed with strong advantages in primary product exports, industrialisation has been a major objective. With the rapid increase in oil exports, industrialisation has been retarded. The problem is that industrialisation is impeded by the abundance of natural resources.

Let us roughly compare the Australian industrial structure in 1955 and 1975. In the following, the first figure indicates the share of each industry in GNP (i.e., total value-added), while the figure in parentheses shows the share in the total employment. The agricultural sector declined from 16.1 per cent (13.4 per cent) to 7.2 per cent (6.2 per cent). The mining

1. R.G. Gregory, "Some Implications of the Growth of the Mineral Sector," The Australian Journal of Agricultural Economics, August 1976.

sector changed from 2.1 per cent (1.7 per cent) to 3.9 per cent (1.3 per cent), meaning that its share in value-added increased while that in employment decreased. The manufacturing sector decreased from 28.0 per cent (28.0 per cent) to 22.4 per cent (21.4 per cent). Tertiary (service) industry rapidly increased from 53.8 per cent (57.0 per cent) to 66.5 per cent (70.8 per cent).[1]

If the first figures are divided by the figures in parentheses, we obtain an index of the value-added per capita or productivity for each sector. This productivity index (a) decreased slightly in the agricultural sector from 120 in 1955 to 116 in 1975; (b) increased rapidly in the mining sector from 120 to 400; (c) increased slightly in manufacturing sector from 100 to 105, both figures were lower than those in the agricultural sector; and (d) remained steady (more precisely, decreased very slightly) at 94 in tertiary industry.

The above trends clearly show that the Australian style of economic development, based on dual structure, has continued and intensified over the past two decades, rather than improving. The Australian economy consists of a very high productivity mining sector and a high productivity agricultural sector on one

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1. Statistics are drawn from W. Kasper, et al., [Australia at the Crossroads], op. cit., pp. 269-270.

hand, and, on the other, a low productivity manufacturing sector and very low productivity tertiary sector.

The reorganisation or revitalisation of inefficient, small-scale manufacturing industry has been discussed but, in the interests of the welfare state and particularly of maintaining full employment, it has not been done. For the same reasons, the inefficient service sector is being rapidly extended, with more than 70 per cent of the work force being employed in the service sector in Australia. Although the same trend is becoming common in advanced economies, it does raise the possibility that it might be the result of excessive welfare state policy.

Welfare State Policy Reconsidered

I am not qualified to describe how intensive and extensive the Australian welfare state measures are, but I would like to mention a few of their symptoms. For instance, there are the powerful labour unions, frequent strikes, a unique wage arbitration system which makes it possible to raise the wage level in excess of increased productivity, and unemployment insurance. Secondly, comprehensive medical treatment and pensions are well provided for, and government expenditure for education is enormous. Thirdly, the number of federal and local government bureaucrats has increased tremendously with the increased welfare state measures and government interventions, and the bureaucrats are the most prestigious and well-paid occupational group in Australia.

Achievement of such a welfare state is fine as long as it does not adversely affect economic development. But there must be a limit to the capacity of the less than 30 per cent of the national work force in the material production sector to sustain material welfare and full employment. An excessive welfare-state policy may be the fundamental cause of the so-called "British (or American) disease". As heavy protection and high-wage labour reduce the already low international competitiveness of manufacturing industries, they ask for further protection. Australia faces the dilemma that she must increasingly restrict imports of manufactured goods, especially labour intensive products, in order to maintain full employment and welfare-state policies. This dilemma is more serious in Australia than in the American or advanced European economies, because Australia is a middle-sized dual economy with a long history of welfare-state policies.

Thus, Australia may be characterised as being physically located in Asia, but still European in spirit. The future of the Australian economy hinges upon how it is able to live with Asia in spirit, as well as physically.

III. HOW AUSTRALIA CAN PROSPER WITH ASIA

The Libertarian Alternative

Recently, many people in Australian government, academic and business circles have come to feel the need for an immediate and decisive change in economic development strategy and for structural adjustment. In one of the best articulated formulations, the Kasper group, as I have already mentioned, has posed the choice between "the Mercantilist Scenario" and "the Libertarian Alternative". The major policies on which the Libertarian scenario of the future is predicated are:

> "free international trade; i.e., the gradual elimination of all tariffs and quotas over a period of five years;
>
> acceptance of the structural changes implied by new technologies and the removal of protection;
>
> reduction of the government's role as a producer of many basic services, including education, health and welfare ..."[1]

It is most impressive that the Kasper group reaches the conclusion that, "Within the short span of twenty years, per capita incomes in Australia could be about $5,000 (in constant 1973 prices) if the Mercantilist Trend is pursued, or about $9,500 if the Libertarian Alternative is adopted ... These

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1. W. Kasper et al., op. cit., pp. 247-248.

figures compare with \$3,900 at the beginning of the 1980s (in 1973 values)".[1]

It may be too much to expect that the Australian economy could completely abandon its traditional welfare-state intervention measures in favour of complete Libertarianism. However, the surprisingly large difference in the future living standard between the two scenarios suggests that even partial liberalisation, if it included some of the key elements, would have considerable favourable effects. The kinds of structural adjustments which would be worth undertaking would be to develop large scale, internationally competitive chemical and heavy industries based upon Australia's rich natural resources and, at the same time, to contract small-scale, inefficient domestic manufacturing industries by increasing imports of labour-intensive products from developing Asian countries. Only in this way can Australia reduce excessive welfare-state protection and integrate herself with Asian economies.

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1. Ibid., p. 247.

Beyond the Welfare State

The basic character of Australia as a wealthy middle-sized economy is unlikely to change. The "White Australia Policy" has been modified and immigrants from Asia are now welcome. Including immigration, Australia's population is unlikely to increase by more than 1.1-1.2 per cent a year. It would be quite impossible to receive, say, 10 million immigrants within a short period and even if it were possible it would be of little help to the Asian population explosion.

Australia's welfare-state policy also is unlikely to change fundamentally, because her people would prefer to retain it if possible. But its excesses must be rectified. First of all, the tendency towards heavy protectionism for the sake of maintaining excessive domestic welfare must be reduced. Secondly, Australian's concern for welfare should be extended beyond the national frontier towards neighbouring Asian countries with the aim of establishing a Western- (or Asian) Pacific welfare region.

What is really needed for Asian developing countries is an appropriate augmentation of their own self-help efforts by trade, official aid, direct investment, and technology transfers - let us call them <u>en bloc</u> "international complementation" - to the national economic development process of developing countries. At the same time, instead of encouraging Asian immigration, Australia could make up for her small population by spreading her direct investment in neighbouring countries, producing efficiently labour-intensive manufactured and other consumer goods, and importing them back. Australia can also play an important role in diffusing and elevating education and other social infrastructure for economic development in neighbouring countries.

Specialisation in Heavy and Chemical Industries

Australia will have to make a dynamic structural adjustment to its economy if it is to complement the Asian countries. The Crawford Report has emphasised, in the following terms, the road Australia should follow:

> "Alternatively, Australia may choose to exploit its rich resource base and to specialise in capital and skill intensive products destined for world markets. While this would not be without problems, it would launch the economy on a new growth path."[1]

This proposal is related to the processing of natural resource-based goods and is in accordance with recommendations made by

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1. (Crawford Report), Study Group on Structural Adjustment, Report, Vol. 1, Australian Government Publishing Service, Canberra, March 1964.

myself.[1] Which industries are likely to have such export potential for Australia? Because of the overwhelming comparative advantage of natural resource based goods, industries based on them can also maintain a strong comparative advantage. An additional advantage of the Australian economy is that with the tremendous rise in oil prices, it can utilise its abundant energy resources at cheaper cost than can other industrialised countries.

A desire to export minerals or metals in a more highly processed form has been evident in Australia since the beginning of the 1960s. Nevertheless, the issue of to what extent processing will be carried out still remains. Processing low-grade iron ore into pellets is hardly good enough. I suggested once that, in addition to the existing steel output, Australia should construct a new blast furnace of 5 million to 10 million tons capacity. Then, if high quality raw materials were produced, automobile, precision machine and general machine industries, which utilise those materials, would be able to develop. Considering the expansion of related industries including the services sector, the employment and income effects would be considerable. Similar arguments apply to extending the processing of bauxite, alumina and aluminium into aluminium-using

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1. Kiyoshi Kojima, "An Impression of the Oceanian Economy," The Economic Record, March 1964.

   This issue is further discussed in Kiyoshi Kojima, Australia's Trade with Asia: Some Policy Issues, Hitotsubashi Journal of Economics, June 1980.

manufactures. The processing industries of coal, natural gas and uranium, and the wood pulp and paper industries should also be regarded as promising.

Heavy and chemical industries such as these must consist of plants large enough to achieve economies of scale. The greater part of their output must be destined for the domestic market, but if local demand is limited, the feasibility of this approach would depend on whether or not a large overseas demand is guaranteed. Development of this export market will require horizontal specialisation in manufacturing in relation to the kinds of goods already specialised in by Japan, the United States and nearby Asian countries.

Given the expansion in Australia's exports of natural resource based goods to the Asian economies, it is perhaps natural that there should be persistent demands from Asia that Australia should import large quantitites of labour-intensive manufactured goods. Australia should take advantage of this pressure as an opportunity to push forward with structural reorganisation in order to facilitate the rationalisation, reduction and restructuring of its inefficient smaller-scale enterprises, and the nurturing of large-scale specialised heavy and chemical industries.

Conclusion

Not only Australia but also Japan and the U.S.A. need to foster structural adjustment to accommodate rapid and successful industrialisation in Asian countries. They should form an intra-industry specialisation network with nearby Asian countries. Undoubtedly, the Japan-Australia relationship will be the mainstay for Australia in successfully developing large-scale specialised heavy and chemical industries. If intra-industry specialisaion were initially established between Japan and Australia, the economies of scale due to the international division of labour would inevitably result in additional output, and opportunities for exporting to Asian countries would increase. In promoting this, it is most important to utilise appropriately international complementation, especially through direct foreign investment to Asian economies. Thus, the strengthening of Pacific economic cooperation is the way for both Japan and Australia to live and prosper with Asia[1], and becoming integrated in this wider region is the only way for the Australian economy to overcome the restraints of medium size.

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1. See, Kiyoshi Kojima, "A New Capitalism for a New International Economic Order," Hitotsubashi Journal of Economics, June 1981.

A CURRENT PICTURE OF THE JAPANESE ECONOMY AND ITS PROBLEMS

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This paper was presented at a Public Lecture at the Australian National University on 25 March 1982, on the occasion of the Eighth Joint Committee Meeting of the Australia-Japan Research Centre.

CONTENTS

I. SLOW DOWN OF THE GROWTH RATE AND CHANGES IN INDUSTRIAL STRUCTURE

After the oil crisis of 1973, the growth rate of the Japanese economy decreased to about half its former level. During the 15 years before the oil crisis, the Japanese economy had grown at an annual rate of over 10 per cent, but in 1974, for the first time, it witnessed a growth rate of minus one per cent. The growth rate was two per cent in 1975, five per cent annually between 1976 and 1979, and for 1980 and 1981 it was about four per cent.

On the other hand, the growth rate of North America and the industrialised countries of Europe went down to about half of the pre-oil-crisis level, around two to three per cent. Relatively speaking, the growth rate of Japan is still higher than that of the European countries and America.

The dramatic rise of 400 per cent in the price of oil in 1974 brought serious confusion to the Japanese economy, and in the spring of 1974, prices increased more than 30 per cent over the previous year. Japan's international balance of payments situation deteriorated rapidly. However, thanks to the policy of stabilisation adopted around 1977, prices stabilised and there was an amelioration in the balance of payments situation.

In 1979 and 1980, the second oil crisis took place as a result of a series of oil price hikes, but the Japanese economy coped with this challenge relatively well, and succeeded in preventing the aggravation of inflation by managing to stop the steep rise in the price of oil from spreading to other prices. This was made possible by the combination of several factors:

First, in order to cope with the first oil crisis, efforts were made in the private sector to rationalise management and to increase productivity;

Second, large investment was made in order to economise on the consumption of energy, especially oil consumption;

Third, in 1978 and thereafter, the Government adopted belt-tightening fiscal and financial policies with the view of restraining consumption and investment;

Fourth, in view of the rising oil price and in the interests of the national economy, the labour unions adopted an anti-inflationary policy of voluntary wage restraint.

Consequently, the consumer price rose by 4.9 per cent in 1981, compared with an 8.0 per cent rise in 1980. A rise of only 3.4

per cent had been registered for the 12 months to February this year.

The second oil crisis created a considerable deficit in Japan's balance of payments, but in 1981 Japan ended up with surplus of 4.8 billion dollars in the current account. During all this time, the unemployment rate remained around 2 per cent, and Japan managed to avoid the occurrence of the near double-digit unemployment rate of the United States and Europe.

However, the improved performance of the Japanese economy has reinforced the competitive power of its exports, and has resulted in trade frictions in the European and American markets.

Since the oil crisis of 1973-74, there has been marked and rapid change in Japan's industrial structure. Apart from changes to the general economy of energy, the following changes took place in response to the steep rise in oil prices:

First, the relative share of energy-consuming industries declined; Second, technology-intensive industrial sectors such as electronics and computers developed considerably; Third, as a result, the industrial structure has changed from energy-consuming to one where the value added is created with a relatively small consumption of energy.

Thus, for example, between 1973 and 1980, the import of crude oil decreased by 10 per cent, but at the same time GNP rose by 32 per cent in real terms. Meanwhile, the number of persons employed in the service sector quickly expanded, and tertiary industry came to account for up to 55 per cent of the total labour force in 1980.

Industry accounts for 50 per cent of Japan's energy consumption. This percentage is considerably higher than that of other industrial nations. However, in the energy-consuming industries, substantial economies in oil consumption have been achieved. For example, in comparing oil consumption in 1980 with that of 1973, the 1980 figure is 36 per cent of the 1973 figure in the iron industry, 42 per cent in the cement industry, 70 per cent in aluminium industry, 81 per cent in the electric power industry and 82 per cent in the paper and pulp industry.

This impressive economy of oil consumption was made possible partly because oil consumption per unit product was reduced, but also because progress was achieved by the use of alternative energy such as natural gas, coal and atomic energy. Atomic power increased from one per cent of total primary energy consumption in 1973 to 5.2 per cent in 1980. Steam coal imports increased from zero to a volume of 7.1 million tons in that time. The share of imported natural gas increased form 0.8 per cent to 5.8 per cent. At the same time, the share of imported oil in primary energy decreased from 77 per cent to 66 per cent.

During the same period, the production of crude steel declined from its peak production of 120 million tons in 1973. Due to the rise in the cost of energy, the import of overseas aluminium products increased while home production shrank considerably. The same can be said of the petrochemical industry. As for the steel industry, thanks to the modernisation of plant equipment and to the economies in oil consumption, its competitiveness has still been maintained in the world market, but because of the stagnant home market, the production of crude steel fell to 100 million tons in 1981.

Forty five per cent of Japan's iron ore needs and 65 per cent of its bauxite requirements are imported from Australia, but the import of these raw materials for heavy industry has decreased in recent years. As for coal, although the import of coking coal diminished slightly, imports of steaming coal increased. This increase came mostly from Australia.

The recent change in the oil market, with scarcity being replaced with overabundance, must have some effects on the economies in oil consumption and on the use of alternative energy, but it is still too early to judge its precise consequences. However, the efforts made so far will be continued with the aim of reducing Japan's dependency on oil to 50 per cent by 1990. This means that Japan's dependency on Australian energy resources such as coal, natural gas, uranium and liquefied lignite will increase, but because of the new situation in the oil market, it can be expected that the rate of the shift to alternative energy may be slowed down somewhat.

II. EXTERNAL ECONOMIC RELATIONS

The Japanese economy has recently been confronted with trade friction with the United States and Europe. For the past ten years, trade friction between Japan and the United States have resulted from the increase in Japanese exports of textiles, steel, colour TV sets and cars to the American market. On the other hand, the United States had demanded that the Japanese market be opened to American products such as beef, oranges, tobacco products and communications equipment, and this has also created friction. Until now, each specific case was settled by mutual concessions, but since last year, there has been a strong demand in the United States for Japan to throw open the Japanese market to American products on the grounds that the trade imbalance between the two countries continues to increase. At present, this is the single most important diplomatic issue between the United States and Japan.

According to the American statistics on bilateral trade between the United States and Japan, the balance of trade shows, on the American side, a deficit of 11.6 billion dollars in 1978, 8.9 billion dollars in 1979, 10 billion dollars in 1980 and about 16 billion dollars in 1981. This continual trade deficit has added fuel to the American insistence that a trade imbalance exists only because the Japanese market is impermeable. In addition, a combination of factors within the United States itself (for example, the recession of American economy; increasing unemployment; criticism of so-called Japanese "free ride"; and increasing Japanese competitiveness in the field of high technology like electronics) has brought about an escalation of American demand for the opening up of the Japanese market.

From the Japanese viewpoint, however, one of the major causes of the trade imbalance of the United States vis-a-vis Japan is the American high interest rate which resulted in a strong dollar and a weak yen. The depreciation of the yen against the dollar encourages Japanese exports while discouraging Japanese imports. In early 1981, one US dollar was equivalent to 200 yen, but by last August it was worth 247 yen, and now hovers around 240 yen.

However, according to the fundamentals of the economy, the yen should have appreciated more against the US dollar. The basic performance of the Japanese economy in terms of the rate of inflation and productivity increase is better than that of the American economy. Contrary to what might thus be expected, however, in reality, the yen depreciated against the dollar. This is principally because of the difference between American and Japanese interest rates. At present, the prime rate in Japan is about 8 per cent, while it is about 16 per cent in the United States. The difference is substantial. As a result, in capital transactions, money flows from the yen to the dollar, resulting in a strong dollar and weak yen. If the American interest rate goes down to a more reasonable level, the trade imbalance between the United States and Japan could be reduced considerably. For the moment, it is hard to see how and when this can happen.

From the Japanese viewpoint, another problem is that the trade imbalance is calculated only in terms of trade of goods between the United States and Japan. In 1980, the United States had a 10 billion dollar deficit in trade with Japan, but in the same year, the United States had 17 billion dollar surplus in trade with the European Community. On the other hand, Japan had a 30 billion dollar trade deficit with the Middle East and a 5 billion dollar deficit with Canada and Australia combined. The United States' balance of payments had a 25 billion dollar deficit in the trade of goods, and a more than 30 billion dollar surplus in the trade of services. Consequently, the United States had a 4 billion dollar surplus in its current account in 1980. Although Japan had a 2 billion dollar surplus in the trade of goods, at the same time it had a 13 billion dollar deficit in its invisible trade - that is, in 1980, Japan had a 10 billion dollar deficit in its current account.

In 1981, the United States and Japan had respectively 6.5 billion dollar and 4.8 billion dollar surpluses in their current accounts. It can be said that, at least over the past two years, the current account balance of the United States has been in better shape than that of Japan. In my view, it is not appropriate to overlook this overall picture and concentrate upon the balance of trade of goods alone.

As Japanese exports to Europe increased dramatically in 1980, criticism there of Japanese exports strengthened. However, due to the import controls exercised by the European countries and also to the self-imposed control on Japanese exports, the volume of recent Japanese exports to the European community is lower than a year ago. Thus, as far as the present balance of trade is concerned, the situation has improved somewhat.

However, in Europe there exist some apprehensions about the future of its competitiveness against Japan in the field of electronics and other industrial technology, and this is a major cause of trade frictions between Europe and Japan. The fundamental problem is the fact that the competitiveness of Japanese industrial products is reinforced by the rapid improvement of productivity and technology.

The basic solution to the problem of trade imbalance, therefore, can be found in the revitalisation of European and American industries. This will give a competitive edge to Europe and the United States against Japanese industrial products.

From the Japanese viewpoint, as Japan has to import most basic materials including foodstuffs and energy, it is imperative to sustain the competitiveness of its industrial products through technological progress, and Japan cannot afford to neglect such an effort. At the same time it goes without saying that Japan cannot remain an island of prosperity in the sea of world-wide depression, and general recovery of the world economy is desirable for the alleviation of trade frictions. It must also be said that Japanese enterprises should not be satisfied simply with the export of their finished products. It is now necessary for Japanese enterprises to join forces with foreign enterprises by building factories overseas and by creating joint ventures so that both sides can share profits. It is also necessary to continue efforts for the alleviation of quantitative restriciton of imports, especially of agricultural products, and also for the relaxation of standards for import inspection. In January this year, the Government of Japan decided on the relaxation of import inspection standards for 67 items, and measures are under review for the further expansion of imported volume of those items presently under quantitative restriction.

To increase Japan's import of agricultural products will certainly favourably affect economic relations between Australia and Japan, but the problem is how to contain the political opposition in Japan to such a move and achieve concensus on the home front.

With regard to agricultural products, Japan is self-sufficient in rice, but in wheat, soya beans, maize and sorghum, Japan's import-dependency rate is over 90 per cent. The United States is demanding Japanese liberalisation of imports of beef and oranges, but at the same time, it should not be overlooked that the United States is limiting its imports of Australian beef. Also, protective agricultural policies practised by the member countries of the European Community have often been criticised by countries which export agricultural products. One of the major problems of international trade in the 1980s may well be the speeding-up of import liberalisation of agricultural products.

This November, a ministerial meeting of GATT (General Agreement on Tariffs and Trade) will be held. It will be necessary then to review the GATT Articles and their interpretation so that these may be modified in such a way as to conform better with the realities of international trade. In 1947 when the present GATT Agreement was prepared, not much attention was paid either to the possibility of Japanese industrial products rapidly acquiring such a competitive edge, or to the possibility of increase in the export of industrial products from NICs (newly industrialised countries). Together with import liberalisation of agricultural products, such subjects as review of the safeguard clause, liberalisation of the trade of services, and the standard of international investment are likely to become important subjects for discussion.

III. ECONOMIC DYNAMISM IN THE NORTHEAST AND SOUTHEAST ASIA REGION AND PACIFIC BASIN COOPERATION

A notable phenomenon in the recent trend in the world economy is the comparatively high rate of economic growth of the East and Southeast Asian countries. In 1981, Hong Kong and Singapore realised 10 per cent growth; the Republic of Korea, Taiwan, Indonesia, Malaysia and Thailand seven to eight per cent; the Philippines five per cent; and Japan four per cent. The World Bank report submitted at a symposium on "Two Decades of Asian Development and Outlook for the 1980s", which was recently held in Tokyo, estimates the annual rate of growth for Thailand, the Philippines, Indonesia, Malaysia and the Republic of Korea at about seven to eight per cent through the 1980s. What further attracts our attention is the fact that manufactured goods have come to occupy a large proportion of those countries' exports in a short period, reflecting the rapid industrialisation in those countries. From 1960 to 1980, this proportion increased from two per cent to 43 per cent in Thailand; from four per cent to 38 per cent in the Philippines; from six per cent to 22 per cent in Malaysia; and from 14 per cent to 90 per cent in the Republic of Korea. This clearly indicates the evolution at a fast pace of a new pattern of trade in the region with the progress of industrialisation. The region has been achieving dynamic development at a time of world-wide recession, and is expected to occupy a far more important place in the world economy, say, in the year 2000. Japan's share in the world's total GNP was three per cent in 1960, but in 20 years it has grown to 10 per cent. A high rate of economic growth sustained over a long period implies a remarkable rise in the absolute level of economic activities.

The rate of Australia's economic growth in recent years is not really high. The Japan-Australia economic relationship is one of mutual complementarity, although in recent years the slow pace of Japan's economic growth and the slump of the Japanese steel and aluminium industries have resulted in the slowdown of the growth of exports from Australia to Japan. The progress of industrialisation in East and Southeast Asian countries, however, will expand the economic exchanges between Asian countries and Australia.

The future economic relations between Japan and Australia will extend beyond mere trade in agricultural products or mineral resources. That is, much more active cooperation will be necessary for the sake of development of Australia's resources-processing industry and related manufacturing industries. The two countries should also cooperate further for the promotion of development in Southeast Asian and Pacific island countries.

The Pacific rim region has the potential for the most dynamic development in the world. Japan and Australia, among others, have important roles to play. In September 1980, a Pacific Community Seminar was held at the Australian National University in Canberra. The report of the seminar was sent in the name of Sir John Crawford, Chairman of the Seminar, to the countries concerned. It is true that, in some of the ASEAN countries, apprehension exists that Pacific region cooperation might prove detrimental to the consolidation of ASEAN, or that Japan, Australia or the U.S. might exert a dominating influence over the ASEAN region. It seems to be historically inevitable, however, that economic exchanges in the Pacific region will expand further and that, some day, an organisation for Pacific region cooperation will become necessary. Japan and Australia should continue their efforts lest we should lose the momentum for the concept of Pacific regional cooperation.

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