

# Reflections on our shared past and future

By Dr Martin Parkinson, PSM

Forty years ago, on 21 December 1972, in a prescient move by then Prime Minister Gough Whitlam, Australia established diplomatic relations with the People's Republic of China.

Back then, our bilateral trade was worth around \$100 million. Fewer than 500 Chinese visitors came to Australia and there were no Chinese students studying here. Only a handful of Australians either visited or studied in China.

The establishment of diplomatic relations marked a turning point in our relationship and was followed by a raft of agreements, dialogues and a deeper relationship between the two countries. From our perspective, Australia was one of the first countries to establish a Treasury representative in China, back in 1994. Since that time, Treasury has seen the economic relationship with China expand rapidly and our ties with counterpart Chinese institutions deepen significantly.

Now, 40 years on, China is Australia's largest trading partner, with total bilateral trade worth over \$121 billion last year. China was our third largest source of short-term visitors in 2011 (over half a million) and is our biggest source of international students (almost 50,000 student visas granted in 2011-12). This flow of people is not just one-way – over 369,000 Australians, almost 2 per cent of our population, visited China last year. To put this in context, as a share of population, that's equivalent to over 20 million Chinese visitors to Australia annually.

This is more than just a reflection of how far our bilateral relationship has come. It is also the story of China's own development and growth.

It is a myth that you can see the Great Wall of China from the moon – no man-made structure is visible from such a distance. But what should be seen as greatness by any independent observer is China lifting over 660 million people out of poverty in only 30 years. Deng Xiaoping's opening up and reform policies in 1978 have driven growth-enhancing reforms sufficient to make China the world's largest exporter and second largest economy in purchasing power parity terms.

As its economic weight has grown, so too has its strategic weight, and China is returning to its historic place as one of the most significant players on the world stage. This has led to considerable debate about the implications for the global order.

For Australia, this has found us in the position where our largest trading partner is not one of our major strategic partners. As a result, there has been much speculation and the suggestion that we must choose between our historical partnerships or alliances and our largest trade partner.

Those who focus on the inevitability of that choice fail to understand the depth of our present relationships. To my mind, the strong trade, economic and growing cultural links with China sit very comfortably next to our deep cultural, economic and security ties with the United States.

The US and UK will continue to be important economic and strategic partners for Australia. This will not change any time soon – as at the end of 2011, the US and the UK held 27 per cent and 23 per cent of our total stock of investment respectively, while China represented less than 1 per cent.

Our unequivocal security relationships are founded on common concepts and experiences of shared history and values which change only slowly and often together. Most Australians would consider these relationships to be instinctive, and they are also fundamental to the national interest.

But our relationship with China will continue to develop and deepen, and not just on economic and trade issues. Our cultural ties (including our people-to-people links built through families and through tourism, education and sporting exchanges), science, immigration, technology and research links, and defence and political exchanges are all growing apace, resulting in a more rounded relationship. Mandarin is now the second most common language spoken at home in Australia. Such exchanges make us richer and are changing the face of Australia, resulting in greater diversity and a greater appreciation of the region in which we live.

Australia and China may not always share the same positions or views on issues. But our relationship is mature enough that we can acknowledge and express our differences while seeking to build on the positive aspects, not least our shared interest in regional stability and security – an interest that we both also share with the US.

Some have expressed the concern that Australia is too dependent on China economically, that we are placing all our eggs in one basket, and that a downturn in China will have disastrous effects on Australia. Certainly, Australia would not be immune to a serious downturn in China, but Australia's sensitivity to economic conditions in our major trading partners is neither new nor avoidable, and we have a proven record of coping with slowing growth in key export markets (such as Japan) and other external shocks (such as the Asian Financial Crisis and Global Financial Crisis). Forgoing the opportunities of engaging with China because of timidity would ultimately make us poorer.

Furthermore, although China's economy has certainly slowed from the heady days of double-digit growth, its economic expansion still has some considerable way to run, with industrialisation and urbanisation contributing to its ongoing growth. A more economically and environmentally sustainable growth rate of 7-8 per cent would still see the Chinese economy roughly doubling in size in a decade. And according to the International Monetary Fund, China is on track to become the world's largest economy by the end of this decade in purchasing power parity terms.

This is not to say it will be all smooth sailing. China faces economic and demographic challenges. As is the case in Australia, sustained economic growth depends fundamentally on productivity growth. In China, there is still plenty of scope for reforms in finance, state owned enterprises and the labour market to boost productivity. We know from our own experience of 'reform and opening up' Australia's financial and labour markets in the 1980s that this means placing long-term national interest above vested interests. Fortunately, China's policymakers are aware of the challenges they face – and the comprehensive economic reforms outlined in the 12<sup>th</sup> Five Year Programme (2011-2015) provide a guide for how to get there – although they will nevertheless have to make some tough economic and political decisions along the way. But they are far from alone in that regard, especially given current global challenges.

This special China edition of Treasury's quarterly Economic Roundup, published to coincide with the 40<sup>th</sup> anniversary of the establishment of diplomatic relations, begins with an overview of our bilateral relationship, with an emphasis on the economic aspects of that relationship, followed by three articles examining some of the key medium-term economic issues facing China: structural challenges and China's evolving growth model; the so-called 'rebalancing' towards greater consumption-driven growth; and the competitiveness of, and prospects for, its export sector. How China responds to these issues is obviously important for China itself, but will also have profound and lasting implications for Australia, presenting opportunities and challenges in our bilateral relationship, and for Australia domestically – opportunities and challenges to which I am confident Australia will rise to meet.