

## **Global Economic Threats to Australia: Been There, Done That <sup>1</sup>**

John Edwards

Asked to list them at a conference hosted by the *Kokoda Foundation* in Canberra in late October 2005, we had difficulty thinking up plausible, grave threats the global economy might present to the Australian economy. We thought of mentioning financial collapses, terrorism, unprecedented imbalances, assets price bubbles, wars and oil prices, but in all categories the global economy has been there, done that, and kept going. After all, in just the last eight years the global economy has flourished despite a financial collapse in South East Asia, Korea, Russia and Brazil, the collapse of a major United States hedge fund, the collapse of a global tech stocks bubble and a subsequent downturn in global growth, a thirty per cent US dollar depreciation, the destruction by terrorists of two iconic towers in New York and a wing of the Pentagon, the doubling of global oil prices, a major war in the Middle East and a continuing insurgency which has already cost the lives of 2,000 American service men and women, a global respiratory disease epidemic, and large and continuing current account deficits in the United States and corresponding surpluses elsewhere – a list of unfavourable developments by no means complete.

It is true that rapid globalisation has increased interdependency, which is usually thought to increase vulnerability. In the case of the global economy, however, it has also increased durability. It has increased the number of alternative markets, allowed compensatory capital flows, and introduced a wider range of complementarities to each national participant in the global economy. It is clearly durable, but the contemporary global economy that we struggle to understand is also of very recent origin.

Although the United States, the United Kingdom, Europe and Japan re-established its foundations over half a century ago, it was not until 1971 that capital flows were liberated, not until 1979 that Deng Xiao Ping began to move China towards a market economy, not until 1989 that the fall of the Berlin Wall allowed the incorporation of Eastern Europe and then Russia into the global economy, not until 1992 that India began serious market reforms, and not until 1994 that Brazil followed. The acceleration of globalisation in the last decade, which Federal Reserve Chairman Alan Greenspan has rightly called the most remarkable development of our era, has been much

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more rapid than the development of either the institutions of global economic governance or our notions of how it works. If there is a long term difficulty it is probably there – most notably in the management over the next several decades of the increasingly symbiotic relationship between China and the United States, now central to the continuing success of global economy. On purchasing power parity terms the United States now accounts for 20 per cent of the global economy and China 13 per cent. Over the next half century their relative positions will reverse. It will not be an easy transition. For Australia, with ties of increasing importance to both major economies, it will be the most sensitive issue in foreign policy.

For the short term, however, the most threatening scenario is easy to pick. It is unquestionably a flu epidemic. It would hinder trade, travel, work, shopping, and all the ordinary business of commerce on which economic globalisation depends and on which both Australia and New Zealand have come to depend. Compared to that threat a downturn in global growth, rising in oil prices, dramatic currency realignments - even another major terrorist attack - are merely the usual run of calamities.

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