STRATEGIC REPORT

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The global power shift: defending Australia's independence

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The world is witnessing a new form of strategic dominance. Countries that excessively depend on foreign borrowing risk losing their sovereignty, being "colonised by purchase rather than conquest".

Warren E. Buffett, Fortune, October 26, 2003

A. Overview

For 200 years Australia has depended on first the British and then the US strategic umbrellas for military protection.

Over this period Australia welcomed foreign investment, first from Britain and later from the US and nations of the Western Alliance. This investment was vital to the development of Australia's resources, infrastructure and industries.

Today the economic and strategic climates are changing dramatically, such that Australia's over-reliance on foreign investment and massive foreign borrowings are putting this nation at risk of losing its sovereignty, not by military takeover, but to economic colonisation by China which is ruled by a one-party dictatorship and has global strategic ambitions.

This emerging threat derives from a combination of serious structural weaknesses in the Australian economy – particularly the foreign debt and over-reliance on foreign investment – at the same time as the world is undergoing the greatest shift in geo-political power since the beginning of the industrial revolution. The world's centre of economic power is shifting rapidly from the US and Europe to China, India and Russia.

Should these deep flaws in the Australian economy precipitate a serious domestic financial crisis, a country like China – with a rapidly expanding, resource-hungry economy, boasting massive domestic savings and huge government-controlled sovereign wealth funds – may find itself in a position to buy out Australia's biggest strategic industries.

Such an economic buy-out poses a serious threat to Australia's sovereignty.

The danger for Australia is made more immediate because the international financial markets are currently under threat of collapse from the worst financial meltdown since the Great Depression.

B. The geo-political shift of power

The distinguished *Foreign Affairs* journal is published by the US Council on Foreign Relations. Its editor James F. Hoge Jnr noted that "Global power shifts happen rarely and are even less often peaceful." Only a century ago, the failure of the imperial order to adjust to the aspiring ambitions of Germany and Japan resulted in conflicts that devastated the globe.[1]

Today's major players in this power shift – China, India and Russia – make up about half the world's population and are growing in economic power at the expense of Australia's traditional allies, the UK and the US. These emerging economies are now the main drivers of world economic growth. According to Albert Keidel, of the Carnegie Endowment for International Peace, in 20 years, the economy of China will be larger than the US economy; in 50 years, India's economy could well be larger than China's.[2]

Accompanying the shift in economic gravity will be a major shift in political and military power and influence. The twentieth century belonged to the Americans. In the twenty-first century, China and India will be contending world powers with economies eventually much bigger than those of the US and EU.

These new powers will demand their fair share of the world's resources, demand their place at the table on key world decision-making bodies and will inevitably wield their new-found international military and political power in their own national interests. Competition between them and the West will be inevitable.

For example, the scramble for access to energy resources gives an indication of the potential for economic and possibly military conflict.

Amy Myers Jaffe, an energy expert at Rice University, told a US Congressional hearing this year that in 1973 the United States imported 35 per cent of its oil. Today it imports over 60 per cent.[3] The Gulf states account for 23 per cent of US imports.[4] Currently, it is unclear whether in the future the US will maintain its dependence on Middle East oil, or increasingly rely on new fields opening up in South America and elsewhere.

A 2005 European Union Green Paper[5] on energy stated that:

- By 2030, the EU will be 90 per cent dependent on imported oil, compared to 45 per cent in 2000.
- Gas imports will have jumped from 40 per cent to 80 per cent over the same period.

Regarding China, Mikkal E. Herberg, of the National Bureau of Asian Research, in his submission to a US Committee on Foreign Relations hearing in 2005[6], said that China will be:

- 80 per cent dependent on Persian Gulf oil by 2030;
- a net importer of coal by 2015; and
- importing 40 per cent of its natural gas by 2025.

India imports 70 per cent of its oil requirements today, and that is likely to increase to 91 per cent by 2020, with 45 per cent coming from the Middle East.[7]

Australia will have shifted from importing only 20 per cent net of its oil in 2000, to importing 80 per cent by 2015.[8]

C. Competition or conflict?

Whereas the twentieth century saw the US and Europe foster the spread of democracy as a moral obligation of the West, China's twenty-first century political example to the world is totalitarian rule. It has no ethical framework from which to begin even shifting towards democracy. The communist system is built on 2,200 years of centralised, authoritarian rule over China. Further, Beijing's leaders still regard China as "the middle kingdom" between heaven and earth. They intend to build the economic and military strength of China so that it can retake its rightful place as the leading/dominant nation on earth. Rapid economic growth is vital for the Communist Party to retain its legitimacy. Hence, rather than helping China move towards democracy, raw, unbridled, capitalist economic growth has helped entrench the communist political system and the drive to restore China to its middle kingdom status. In the process, rather than moving towards democracy, China has supported many of the world's most odious political regimes, like Burma, Sudan and North Korea.

In the late twentieth century, America and the West using international free trade principles as the means of allocating resources between countries. Resources and goods were traded to the highest bidder. This economic approach to distributing resources ensured that the world's resources were allocated peacefully. The international market trading system replaced the age of empires, when competition for resources was settled through carving up the under-developed world into European-controlled empires that were engaged in endless military conflict over access to resources, markets and trade routes.

For example, when the first world oil shock occurred in 1973, Western nations found that scrambling for control of oil resources was a zero-sum game which only worsened the problem by reducing market flexibility and efficiency and by intensifying international rivalries over supplies.

This led to the creation of the International Energy Agency to avoid the risk of national competition for supplies. Since then, Western policy has focused on promoting diversified sources of oil and letting the market determine the most efficient allocation of resources worldwide. This kept oil supplies flowing and prices down for all.

In a retrograde step, Herberg says that for Beijing

> "energy has become a matter of 'high politics' of national security and no longer just the 'low politics' of domestic energy policy. Energy security is too important to be left entirely to the markets as China's economic prosperity is increasingly exposed to the risks of global supply disruptions, chronic instability in energy exporting regions, and the vagaries of global energy geopolitics. Energy has become a central concern for Beijing and the global search to secure future energy supplies has taken on great urgency ...
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> "China's rapid economic growth is highly dependent on finding the growing energy supplies needed to fuel this economic 'Dragon'. The erosion of the ability to rely largely on domestic energy supplies has created a powerful sense of energy insecurity rooted in a deep-seated fear among the leadership that energy supply disruptions and unpredictable price spikes could undermine China's rapid economic growth and job creation. To the leadership, slow economic and job growth raise the real spectre of social instability which, in turn, calls into question the continued power and political control of the Communist Party. Hence, there is a visceral and profound connection in the minds of the leadership between reliable energy supplies, political and economic stability, and continued Party control."[9]

This mercantile approach to foreign investment and trade by China has sparked nations like India and other emerging Asian nations to also move towards mercantile trade and foreign investment policies, as they compete with China for supplies of essential resources around the globe.

For example, in 2006 China won the sole right to exploit one of biggest untapped iron ore deposits in the world, an estimated one billion tonnes of reserves with an estimated iron content of 65 per cent in Gabon, west Africa. The Chinese will invest US$3 billion in the project. This mine will help China reduce its dependence on iron ore from Australia. Australian miners negotiated an iron ore price increase of over 80 per cent with China in 2008.

Mercantilism is fundamentally at odds with free trade principles. It has the potential for escalating economic tensions into military conflicts, as competing nations strive to ensure their control of vital resource supplies.

Resource-hungry nations like China and India view Australia as a nation with a huge landmass, abundance of all major resources and comparatively small population. Indeed, the old Chinese and Japanese written characters for Australia are the same, and it broadly means "land of plenty over the sea". Prophetically, Jane's *World Armies* warned in 1996 that it was Australia's good fortune – and lack of population – that "made it a glittering strategic prize" and that "in the longer term it would be surprising if during the next century, the country's defences were not tested".

That test could come more in the form of an economic buyout than from military threats.

D. Risks to Australia: structural economic flaws

Australians have not awoken to the global power shift under way or to the major challenges it poses. After a quarter-century of embracing the economic theories of radical free trade and deregulation, to an extent not seen in any other country, major imbalances and deep structural flaws have developed in Australia's economy. The first flaw is the burgeoning foreign debt; the second is the nation's over-reliance on foreign investment, particularly in the resources sector.

The foreign debt is now over $600 billion and proportionally about twice that of the US. Both the rapid growth of the foreign debt and the heavy dependence on foreign investment in mining and other industries threaten to make Australia vulnerable to a major economic downturn. Together, they put Australia's economic sovereignty at risk.

If the foreign financial markets lose confidence in the Australian dollar, and they are showing nervous signs at the moment, this could trigger an economic crisis in the form of a run on the Australian dollar and a flight of capital.

As Joseph Stiglitz, one of the world's best-known economists has warned, in such crises countries like Australia will repay their debts. This is because they have

> "the capacity to repay: they could presumably raise taxes and cut expenditures enough to generate the required revenue. The value of the country's assets exceeds by a wide margin the value of what is owed. But the cost to the country can be enormous, beyond what its citizens are willing to pay."[10]

In such circumstances, neither of Australia's historical protectors, the UK and the US, are in a position to bail it out of such a predicament. The US economy is holding the largest debt in history. The UK does not have the resources to bail out Australia.

Hence, one consequence could be the prospect of the International Monetary Fund placing punitive costs on a bailout of some kind. This would undoubtedly involve allowing sales of more Australian assets to foreign buyers – including China.

Or Australia could face a worse scenario.

With great vision, Warren E. Buffett, the famous American investor and economic commentator, has warned in *Fortune* magazine that the world faces a new form of strategic dominance. He cautioned that any country that excessively depends on foreign borrowing would become a nation of wage-earners rather than property-owners. Such a nation risks losing its sovereignty, being "colonised by purchase rather than conquest".[11]

At the same time as the foreign debt has been mounting, Australia has also been heavily relying on foreign investment to develop the resource industries that are supplying the new global powers like China and India.

Under Beijing's "Go Abroad" policy — aimed at securing access to important raw materials, advanced technology and brand names — Australia has suddenly become a major target for Chinese investment. Chinese government-controlled investments in Australia have jumped from a trickle three years ago, to $6.8 billion in 2006, and potentially $30 billion this year. While no single investment in Australia poses any threat to our sovereignty, a flood of major investments over time could see the Chinese regime become a major player in Australia, with profound political and strategic ramifications.

Currently, China has amassed an estimated US$1.3 trillion in foreign reserves, while ordinary Chinese have another US$2 trillion sitting in savings accounts earning negative interest. These funds are now being directed through the new State Investment Company, which is modelled on Singapore's Tamasek Holdings, to investment abroad. World-wide, government-controlled sovereign wealth funds – state-controlled funds of big exporting nations, particularly oil exporters – are expected to grow from US$3.85 trillion to as much as US$15 trillion by 2015, according to the International Monetary Fund.[12]

Herein lies the emerging risk to Australia. The more the Beijing regime has invested in Australia at the moment of a major economic crisis, the greater the likelihood that China would literally buy out Australia using its massive savings pool, foreign reserves and sovereign wealth funds. It has the potential to bail out Australia's foreign debt, but the price could be China taking effective control of key national assets – minerals, energy, possibly banks and the retail sectors.

If this were to happen, Australia would have lost its sovereignty. Decisions affecting Australia's future would not be made in Canberra in Australia's national interest, but in Beijing in the interests of China. History has shown that foreign debt crises can develop rapidly, with little warning, as the current financial crisis gripping the US demonstrates. Similarly, a crisis that could threaten Australia's sovereignty could also develop rapidly.

Strategically, Beijing would find drawing Australia into its orbit, and away from the US, utterly irresistible. One of Beijing's deepest fears is the US policy of soft encirclement and containment of China, using economic, diplomatic and military means. Currently, the Beijing regime is expanding its political influence all the way to the Persian Gulf, and is seeking port facilities along that route. It is also developing an increasingly sophisticated military, particularly its naval power.

E. Australia's foreign investment dilemma

The Australian government has found itself caught on the horns of a dilemma. Earlier this year, Treasurer Wayne Swan said on a visit to China that Australia's foreign investment policy was non-discriminatory and aimed at having decisions driven by market forces — not external political or strategic considerations. This was followed by a steep rise in investment applications from Chinese state-owned companies, with the federal Treasurer approving new Chinese investments at the rate of one every nine days.

Then, while approving Chinalco's 11 per cent stake in Rio Tinto, the Treasurer put a 90-day hold on a major Chinese planned takeover of mining company Murchison Metals by Sinosteel Australia, a wholly owned subsidiary of the Chinese state-owned Sinosteel company.

Later, while at the Olympics, Mr Swan addressed a gathering of Chinese businessmen. He asked the Chinese to invest in new mining projects rather than take over existing projects, and to invest via joint ventures rather than hostile takeovers.

Subsequently, the Treasurer approved the $1.3 billion takeover of Midwest by Sinosteel, making it China's first successful hostile takeover of a foreign company in Australia, and a 49.9 per cent stake in Murchison Metals.

The Australian government appears bewildered and unsure how to proceed. While concerned about future political consequences of investments by foreign state-owned enterprises and sovereign wealth funds (SWFs), it can't bring itself to say "no" to such investments from China.

Australia's foreign SWF guidelines were reassessed at the end of 2007 and, according to a federal parliamentary briefing paper on the issue, SWF applications for investment would be reviewed around *"the question of how far the commercial agency of any foreign government operates independently and commercially and suggest if a proposal from a SWF is consistent with Australia's national interest."*[13] (The emphasis is theirs.)

Clearly, the new rules are inadequate to deal with the magnitude of the problem now facing Australia.

Other nations are becoming vigilant about investment by foreign government-controlled funds. For example, new foreign investment rules are being introduced in Europe, with Germany leading the way.

Germany has proposed that moves from non-European Union controlled investment groups or companies to buy a stake of 25 per cent or more in strategic parts of German industry can in future be blocked. This followed concerns over the Chinese attempt in 2007 to acquire "a 10-percent stake in the US private equity house Blackstone, which has a key holding in German-based Deutsche Telekom AG, Europe's biggest phone company. [It also] followed moves by Russian state bank VTB to carve an interest in Europe's sensitive aeronautic and defence sector by seeking out a stake in the European Aeronautic Defence and Space group (EADS), which is the parent company of the European aircraft maker Airbus."[14]

F. How China and Russia restrict foreign investment

Ironically, some SWF nations — such as Russia and China — while complaining about new investment rules abroad, have imposed tight controls on foreign investment in their own strategic industries.

China's foreign investment policy has evolved. Under the recently revamped rules, China now restricts or prohibits investment in industries it has already mastered (like toys, furniture, shoes and clothing) or in industries with high usage of resources or energy (like steel, aluminium, paper, cement and other basic industries).

It has shifted its emphasis to quality rather than quantity of investment, with more emphasis on advanced technology and management. It maintains substantial restrictions on publishing, media, market and social research, and an absolute prohibition on investment in real estate and real estate brokerage firms.

Russia, with its new found oil wealth, recently declared 42 "strategic" sectors — including the nuclear industry, aerospace, armaments industries, oil, gas, fishing and the mass media — in which foreign companies cannot own more than 50 per cent and foreign companies owned by governments cannot own more than a 25 per cent stake.

Investors now have to seek authorisation from a commission made up of economic and security advisors.

Australia should heed the advice of one senior Chinese official who, in commenting on his own country's restrictive foreign investment policy, said, "China intends to use foreign investment rather than be used by foreign investors."[15]

G. Triggers to a foreign debt crisis

In embracing the ideology of free trade and deregulation with enthusiastic excess, Australian policy-makers have denied that the foreign debt poses any serious risk to Australia. Theoretical arguments have been used to dismiss the debt as merely involving the private transactions between consenting adults. Hence, we are told, private sector debt doesn't matter.

This is clearly false, given that excessive private sector debt was a major factor behind the 1997 currency and foreign investment crisis in East Asia.

There are possible triggers for a financial crisis in Australia.

1. The financial meltdown in the US could precipitate a deep, prolonged recession in the world's largest economy. If this contagion spreads, it could see Australia's source of foreign capital dry up. The risk is that the crisis will lead to a major credit squeeze. Already the markets are twitching.

   Several leading Australian bank officials have called on the Federal government's tax inquiry to offer tax concessions for savings as the lack of Australian savings is a major reason for the banks borrowing offshore and running up the foreign debt. The National Australia Bank's chief financial officer, Mark Joiner, said, "We have a deposit-poor banking system because just about every other form of investment in Australia has a tax incentive … We have got ourselves in a position with the Australian banks overly reliant on international wholesale funds because we don't have sufficient volumes moving around our domestic banking system." He said that when foreign debt investors compared banks across the world, Australian banks "stand out" because of this reliance on offshore funds. "That leads them down a path of saying, 'Is there something structurally wrong with the Australian economy? Should we have this much exposure?'"[16]

   Should Australia find that capital inflows have diminished or dried up, the situation could quickly turn into a capital outflow. Then Australia could face a foreign debt repayment crisis.

2. The rapid growth of China and other emerging economies has created a resources boom that has greatly benefited Australia. Skyrocketing mineral prices and booming exports volumes have driven economic growth. This has created a windfall in federal tax revenue and has forced up the value of the Australian dollar. Historically, the Australian dollar fluctuates in direct relation to commodity rices.

   At the same time, the high price of minerals has created a world-wide mining investment boom. Eventually, as new supplies of resources come on line, prices of commodities will fall. As prices fall, the weight of the foreign debt will drive the value of the Australian dollar down dramatically, risking a serious foreign debt crisis.

   Notably, Prime Minister Kevin Rudd has warned that Australia faces "waking up with the mother of all hangovers" because of its failure to address "a multitude of economic weaknesses" hidden by the mining boom.[17]

3. Australia is facing a huge rise in oil imports, as the nation comes to be 80 per cent dependent on imported oil by 2015 (see page 10 below). This could cause a major blow out in the foreign debt which the financial markets would be unlikely to fund, precipitating a financial crisis.

There is little evidence that the Australian government really understands, or is prepared to face up to, either the mercantile nature of Chinese government-controlled investment, or the strategic threat posed to the nation by its over-reliance on foreign investment, exacerbated by Australia's soaring foreign debt.

Australians generally are also largely unaware of these issues. In part, this blindness comes from being lulled into a false security from the nation's long trust in the US alliance and benign foreign investment. It also stems from the blind faith policy makers have placed in radical free trade theory over the past quarter-century.

H. Facing the challenges

Radical free trade and deregulation policies have structurally weakened the economy and left it vulnerable in a rapidly changing geo-political world. Facing up to the problem requires three important intellectual debates.

First, replace radical free trade theory with real trade policies, in order to clear the way for putting in place the financial and industry policies needed to reduce the foreign debt and ensure greater self-reliance in capital.

Real trade theory has been articulated by the likes of Ralph Gomory, IBM's former senior vice-president and director of IBM's outsourcing, and William Baumol, former president of the American Economic Association. Together, they wrote the seminal book, *Global Trade and Conflicting National Interests* (MIT Press, 2000). They show that in the industrialised world, radical classical free trade polices can lead to one nation benefiting at the expense of the overall welfare of another nation, rather than leading to an overall rise in the wealth of both nations, as held in classical theory. In part, their real trade theory leads to the conclusion that if governments don't implement deliberate industry policies they risk losing huge numbers of jobs offshore, without new jobs being created to replace them. This requires, not a rejection, but a modification of free trade theory to current trade practice, which is based more on trade in commodities, intellectual property and industrial goods rather than agricultural goods, as in classical theory.

The flaws in free trade theory leave countries like Australia vulnerable to being exploited by huge emerging economic powers pursing mercantile trade policies.

Second, the risk of the foreign debt to Australia's national interest has to be confronted. There is some evidence of this risk being recognised as a result of the credit crisis. Australian bank leaders are saying that foreign financial markets are asking: why is it that Australia is so reliant on foreign borrowings to fund housing and consumption? (see above). Three years ago, Chris Richardson, director of Access Economics, warned about the foreign debt risk. "OK, it's panic-button time … It will take longer than markets realise to rein in a current account deficit in the 'banana republic' range."[18] Even Prime Minister Rudd has asked, numerous times, what will happen to the economy after the end of the mining boom?

Bringing down the foreign debt is critical to reducing the risk of Australia being "bought out" by nations with huge government-controlled savings.

Third, Australia has to wake up to the potential threat of the People's Republic of China (PRC). Beijing has its own strategic ambitions, using ownership and control of vital resource supplies around the globe to enhance its strategic power vis-à-vis the US and it allies. Beijing becomes a threat to Australia primarily because of the structural weaknesses of the Australian economy if it is allowed to gain too large an investment stake in Australian industries. Australia can mitigate this risk by bringing down its foreign debt and by putting appropriate conditions on investment.

Importantly, in dealing with China, Australian policy-makers need to draw a distinction between the Chinese people, who aspire to a way of life similar to Westerners, and the Chinese Communist Party dictatorship, which has an appalling history of oppressing its people and a record of associating with the most authoritarian regimes on the planet.

At the same time, to Beijing' credit, it has adopted some crude market principles for its economy, so that by 2025 at the current rate of economic growth it will have dramatically reduced the nation's poverty rate. It will have lifted more people out of poverty at a faster rate than any other nation in history.

Therefore, Australia should not regard China as an enemy but as an emerging nation that has a very long way to advance before achieving democracy; before it starts encouraging democracies in other regions like Africa; before it understands and abides by broad market economy principles; and before it comes to respect universal human rights.

To this end, the object should be to structurally strengthen the Australian economy so that it:

- can survive the global economic and strategic power shifts underway; and
- engage and trade with China on Australia's own terms, from a position of economic strength and stability, not on Beijing's terms.

To achieve these ends, Australia must develop and pursue a strategy with integrated economic, foreign affairs, defence and social policies.

I. An economic strategy

The problems facing Australia are only partly caused by resource-hungry China pursing resource investments around the globe with "exuberant excess". Australia's home-grown structural economic problems have made the country vulnerable to emerging nations with insatiable appetites for Australia's resources.

The good news is that Australia has the means to solve these problems, if it has the political will.

The object of economic policy should be to rein in the foreign debt and become far more self-reliant in capital to develop the nation's resources and to supply our trading partners, while keeping ownership of strategic industries in Australian hands. Further, to keep down the foreign debt and for national security reasons, Australia needs to maintain greater self-sufficiency in food and energy supplies while rebuilding a strong manufacturing sector.

Several key steps are required to secure Australia's economic independence.

1. Foreign investment rules

Australia needs to further overhaul its foreign investment rules, especially regarding SWFs and foreign government-owned corporations, along the line of those being adopted in other countries such as Germany.

- Australia needs to declare a wider range of strategic industries in which foreign investment is limited or prohibited.
- In the most important strategic industries, acquisitions should be prohibited.
- In other strategic industries, foreign ownership by commercial companies should be restricted to 49 per cent, and for SWFs and foreign government-owned corporations, it should be limited to 25 per cent.
- Investment in the resource sector should be as joint ventures in new projects, not hostile takeovers of existing companies.
- Anti-avoidance legislation is needed to ensure the intentions of the rules are not undermined by such devices as the transfer of ownership to offshore holdings.
- The Treasurer needs to be given the power of divestiture to break up foreign ownership of a company when it is deemed that such foreign ownership is not in the national interest.
- The Treasurer should have the power to prohibit/limit foreign investment in the case of creeping acquisitions leading to overly concentrated ownership by one company.
- For serious breaches of the foreign ownership rules, forfeiture of ownership should be an option open to the Treasurer.

2. Shift towards greater capital self-reliance

First, this involves bringing down Australia's $600 billion foreign debt. Even the Australian banks – which hold the bulk of the foreign debt, most of which has been loaned for housing and consumption – are recognising that the current level of debt is dangerous and that Australia's foreign creditors are showing signs of unease. Key measures to reduce the debt include:

- Returning the $300 billion plus in super funds that are invested offshore and, through mechanisms such as a development bank, mobilise these funds for domestic investment and for refinancing the foreign debt into domestic debt or equity.

- In the face of a major foreign debt crisis, World Trade Organisation rules permit a nation to impose import restrictions, for example, a primage duty on imports.
- Build/expand export and import replacement industries, principally in the manufacturing and agricultural sectors.

Second, urgently boost national savings. The lack of domestic savings has in part led to Australian banks being forced to seek funds offshore. Australia should emulate Japan and other Asian nations that, in much of the post-war period, offered tax concessions on savings, helping to make them self-reliant in capital.

In addition, Australia's SWFs should be enlarged:

- The tax revenue from the mining boom should be saved for investment in national development projects; and
- As most foreign multinationals pay little or no tax in Australia, tax deductibility of interest for Australian acquisitions should be disallowed, or the government should insist that these companies pay a turnover tax with this revenue put into national SWFs.

3. Greater energy self-reliance

Greater oil self-sufficiency: According to Energy Minister, Martin Ferguson, "by 2015 … domestic oil production could be as little as 20 per cent of our needs compared with 80 per cent in the 1990s."[19] Belinda Robinson, of the Australian Petroleum Production and Exploration Association, says that this "deficit for oil, condensate and refined products is projected to increase to $27 billion a year by 2015 – around twice the 2005-06 deficit of $12.8 billion."[20]

These figures appear to be based on oil priced at about US$50 a barrel and the Australian dollar at about US80¢, in which case their estimates as to the cost of oil imports could be grossly underestimated.

If in 2015 the price of oil is in fact around $US150 a barrel, and the Australian dollar is at US50¢, after the tapering off of commodity prices, then net oil imports could be costing Australia a massive A$123 billion annually! That will be 9.6 times what it costs today.

Under this scenario, the foreign debt will be blowing out at around A$180-A$200 billion per year! Will the financial markets continue lending to Australia to finance a foreign debt blowing out at that rate? An oil shortage of this magnitude would induce a capital strike.

Consequently, Australia urgently needs to find new domestic oil supplies, and to have a wider distribution of LPG gas for motor vehicles.

Dr Walter Starck recently recommended: "Synfuel from coal and gas could supply all our needs here in Australia at less than half the current price of oil. This can be done using commercially-proven technology which can be implemented now with no uncertainties."[21]

Further, Australia needs to build a major ethanol industry based on sugar-cane, which would have three major advantages:

- It could form a major carbon offset program, as it would bring down carbon dioxide emissions as opposed to just taxing them;
- It would create a major new, high-value-added industry that could help Australia go a significant way towards energy self-sufficiency, without forcing up the price of food;
- It would save the sugar-cane industry, which is going to the wall.

Electricity generation: Australia has half the world's reserves of uranium and thorium, and vast deposits of coal and gas. Yet the nation struggles to build vital new power stations because of environmental restrictions.

Australia has an environmental lobby strongly opposed to further expansion of uranium mining, a domestic nuclear power industry and the expansion of coal-fired power stations.

Forget for a moment the debate over carbon dioxide-induced global warming. Eventually, if Australia does not exploit its huge energy reserves, other energy-starved nations will be tempted to come and exploit those reserves themselves.

4. Greater food self-reliance

The agricultural sector is in major crisis.

- Net farm incomes, all other things being equal, cannot but continue their long-term downward trend.
- Australia's top farmers are the innovators, the productivity drivers that other farmers follow. They are the ones leading the exit from agriculture.
- There is a serious lack of young people coming into farming.
- The on-going drought is bringing this crisis to a head.

According to OECD agricultural statistics, Australian farmers receive the lowest farm-gate prices in the developed world, roughly equal to the corrupt world prices. The statistics show that while in most developed countries farmers receive around 27 per cent of their gross income from subsidies and food products receive a 15 per cent consumer subsidy, Australian farmers receive just 6 per cent and consumers 2 per cent in subsidies.[22]

While all other developed nations ensure that farmers receive preferential access to their domestic markets — which is where farmers make most of their returns — under deregulation and free trade policies Australia has effectively forced farmers to compete on both the domestic and world markets at the highly subsidised, corrupt world price. These policies were to ready Australian farmers for the export market.

For about 25 years, Australia's policy makers have believed that the World Trade Organisation (WTO) would open up the markets of the US, Japan and the EU to free trade in agriculture. It did not happen in 1994, when the General Agreement on Tariffs and Trade (GATT) evolved into the WTO. More recently, the major economies have made it clear that they have no intention of pursuing free trade in agriculture, which is the reason for the failure of the Doha round of trade talks.

Consequently, opening Australia's borders to heavily subsidised imports has undermined the all-important domestic market, while the deregulation of agricultural industries has stripped farmers of any market power to obtain a just price for their product, given they sell most of their product to just two supermarkets. Even the nation' quarantine authorities have fallen prey to free trade policies and compromised our quarantine standards; and now governments are pushing free trade in irrigation water.

Agriculture policy requires a major overhaul. Like all other developed nations, Australian agricultural policy needs to work on the principle of giving Australian farmers preferential access to the domestic market. This requires several steps:

- National Competition Policy has to be revamped to allow farmers to effectively bargain a fair farm gate price. Farmers are price-takers in markets where they have no market power over either the price of their inputs (like tractors and fertiliser) or their outputs, particularly when selling to just two dominant supermarkets.
- Anti-dumping rules need to be changed to the US model, where importers of food products have to prove the goods are not dumped.
- As quarantine authorities are primarily enforcement agencies, they should be transferred from the Department of Agriculture, Fisheries and Forestry, which is concerned about trade, to the Attorney-General's Department. The latter is responsible for other enforcement agencies like customs, the Australian Federal Police and national security.
- There needs to be a moratorium on permanent water-trading in the Murray-Darling Basin. Opening up the trading of farmer's permanent water entitle-

ments has been a disaster, risking the future of agriculture in the nation's major food bowl.

5. Building manufacturing industry

Australia must decide if it wants flourishing manufacturing industries. All developed nations have either a car industry, an aeronautics, electronics or chemical industry. Australia has only one such industry, the car industry and the nation is at risk of losing it.

Industries like motor vehicle production are vital to reducing dependence on imports and for export revenue. The main problem facing the Australian car industry is that it is entirely foreign-owned. To best ensure that Australia maintains that industry, some of the $7 billion in car industry subsidies should be converted into soft loans for an Australian consortium to buy out one or two foreign owned companies. Then the object should be to expand production into small and medium-sized cars, platform share across the car companies and expand production to one million units.

This would ensure Australia had a major manufacturing sector and considerably reduce the nation's over-dependence on imported product.

J. A new foreign affairs focus

Recently, the Prime Minister delivered a major defence speech to the RSL. Expressing concern at the military expansion underway in Asia, Mr Rudd's response was for Australia to build a bigger military force, particularly an expanded navy. However desirable, this is only a partial response to the problem. It fails to account for the growing economic threat to Australia. It fell well short of an adequate diplomatic response to the challenges being posed by China and other emerging powers.

First, Australia needs to develop a wide alliance of larger democracies – encompassing India, Japan, the US, Indonesia and Australia – to hold back China's mercantile approach to international trade and to pressure China in the direction of human rights and democracy. Australia will need to build close economic, diplomatic, security and cultural ties with these countries.

Further, Australia has taken its eyes off the small nation states in its arc of influence. Canberra urgently needs to refocus attention on these nations. Australia should help them evolve into stable, prosperous states, forming a buffer zone to the new regional power of China. Economic, trade and cultural policies are required to build these states as functional democracies and viable economies, integrated with the Australian economy.

Australian security agencies need to be expanded in order to focus on tracking China, as it seeks to expand its influence in Australia and its troubled neighbouring states.

K. Social policy

Given the strategic changes underway in our region, there should be a conscious population policy to rapidly build Australia's population, particularly to populate water-rich northern Australia.

Confronting this array of external issues facing Australia is made difficult when Australia is culturally divided, the product of the cultural revolution of the 1960s and of divisive, extreme multiculturalism. Promoting a common national values system, particularly aimed at strengthening the family, the cornerstone of society, is vital to building a strong, cohesive nation capable of confronting the issues challenging the nation's sovereignty.

L. Conclusion

Australia is yet to come to grips with the risks and dangers associated with the global power shift underway in the twenty-first century.

In the first instance, the risks are economic as countries holding massive savings and foreign reserves have the potential to "buy out" resource-rich, population-poor nations like Australia.

Australia is being left wide open to economic domination by a country like China because of its over-dependence on foreign debt and foreign investment.

Foreign debt and foreign investment, from which Australia has greatly benefited in the past, are now shaping up to be weaknesses that could cost Australia its sovereignty and its way of life.

Economic solutions will only be found when there has been a re-evaluation of the prevailing radical free trade theories and an acceptance of the need for real trade policies.

The good news is that, if Australia is prepared to make hard decisions, it has the means at its disposal to avoid such a crisis. The question is, does it have the foresight and the political will to act before it is too late?

The authors

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National Civic Council

The National Civic Council (NCC) was formed by B.A. Santamaria in 1941. Today, the NCC is concerned at the consequences for Australia of the growth of China, India and East Asia, particularly in light of the global economic turmoil.

The accompanying strategic shift in world power from the US to China will have far-reaching consequences for Australia.

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