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New Zealand and the Asia-Pacific Economic Decade

Abstract

The last decade has seen the Asia-Pacific region undergoing new patterns in economic development, driven by major changes in trade, capital and technology flows, together with demographic disruption. On top of that, the region is experiencing the resurgence of the Chinese economy, a defensive US response, climate change concerns, and the problems of Covid-19. This brings new worries about globalisation and challenges for New Zealand hosting APEC in 2021.

Keywords Asia–Pacific, economic growth, trade, globalisation, APEC

The Asia-Pacific economy has undergone significant changes over the past decade. During previous decades it enhanced the livelihood of billions of people. Now it is going through an era of intense uncertainty and turbulence. New Zealand has become

increasingly integrated into the region economically, but these changes spell big challenges ahead.

This issue of *Policy Quarterly* contains a series of articles examining aspects of this changing economic integration. Its publication coincides with New Zealand

assuming hosting responsibilities for APEC 2021. This introductory article sets the background for those that follow, introducing the major structural changes in the region and the responses from governments. It asks how these trends impact on New Zealand, and whether New Zealand policy is fit for purpose in this turbulent time.

Growth patterns

For some decades the APEC (Asia-Pacific Regional Cooperation) region enjoyed strong GDP growth, both overall and per capita, driven by positive demographics and a liberalised trading environment. This growth meant guaranteed generational improvement in income, and this encouraged a societal consensus for growth which papered over social inequities, environmental damage and political tensions. The economic model was based on the regional integration of production: raw materials from South East Asia, Oceania and Southern Cone countries feeding intermediate manufacturing operations in locations largely dictated by comparative labour costs and productivity in East Asia, financed by mobile capital,

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linked by sophisticated supply chains to assembly plants particularly in China, and via efficient container shipping to the affluent markets of North America.

Some structural changes are now disrupting that model. The high-growth period before the global financial crisis led to a large build-up in balance sheet debt, including over-investment in housing in the West, and in infrastructure in the East. The global financial crisis itself led to losses in asset value, financial institutions being more tightly regulated, and a growth in sovereign debt from bank rescues. In the West this has meant lower productivity,

slower to develop. However, the current industry and national battles over 5G networks and digital platforms are indicative of the huge commercial and political possibilities in the Internet of Things in coming years.

While manufacturing, energy and services trade are all changing, commodities trade has been less affected. Demand for raw materials continues, but the economics still favour the bulk shipment of relatively unprocessed product to be transformed in the factories of East Asia. The big New Zealand exporters of dairy, logs and meat have not managed to add much value

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slower trend growth rate, low inflation and near-zero interest rates.

Trade and capital flows

Trade growth had been the key economic driver for the region, but it slowed notably after the global financial crisis and has never returned to the previous highs. There have been several reasons: limits to the gains available from vertically dis-integrated production models; Chinese regional industry policy seeking to build domestic supply chains; US policies discriminating against foreign expansion; a pressure to onshore investment; and other results of the US-China trade tensions.

Another major trade change has been radical disruption to energy markets: huge new production capacity is turning the US into an energy exporter, OPEC market domination has been disrupted, environmental pressures are reducing the coal trade, and for the first time gas has become a major traded commodity in the region.

While the Asia-Pacific has been leading the world in the integration of manufacturing, trade in services has been

locally, instead increasing production volume domestically and continuing to sell into the regional supply chains. New Zealand commodity exporters will gradually face tougher environmental and animal welfare market requirements from Asian consumers. Some smaller entrepreneurs with branded, high-priced products such as pāua, salmon and mānuka honey have prospered in the new middle-class markets of Asia, but this constitutes a small share of New Zealand's export receipts.

A feature of East Asian growth has been the very high household savings rates that have funded the region's business and infrastructure investment. As the financial markets of the region have opened, there are increasing flows looking for diversification and better returns available through direct and indirect investments, from corporate funds and from wealthy families.

Direct investment in New Zealand in the past has been dominated by US, UK, Australian and Japanese flows, while Chinese money is increasingly available, though often politically contentious. East

Asian investment has often been associated with residency, education access, apartment purchase and business start-up, which contributes to policy complexity.

Demographic disruption

The composition of East Asian and Latin populations in the Asia-Pacific region has changed significantly. Birth rates have dropped, education rates have increased, child-bearing is occurring later, and households are moving from extended to nuclear or single-person. This marks the end of the 'demographic dividend'; workforces are no longer growing, but are higher-skilled, more costly and ageing. Lengthy retirement is a new phenomenon. These changes were predicted, but have happened faster than expected.

With income growth has come a surge in middle-class populations. Typically these are urbanised apartment dwellers, and their consumption patterns are changing. They are paying more for branded/imported/exotic/safe/environmental products, they are spending on services such as health, education and travel, and they have expectations of government provision of social and environmental services. They are more likely to search, purchase and pay on hand-held digital devices. These middle-class households have significant savings, and they are more mobile.

Asia-Pacific regional integration has involved large (but highly regulated) population flows. By 2018 there were over one million student movements in the region, considerable travel by business people with cross-border commercial interests, a growing trade in health tourism, and a huge regional tourism industry.

The most complex of all these flows is labour movement: there has been major growth in shorter-term professionals in Pacific Rim countries flocking to buoyant financial and business services sectors. Businesses themselves, especially those that are digitally based, have also become more mobile. There has also been growth of limited-term migrant labourers employed for home care, construction and other low-wage duties, drawn from the poorer South East Asian and South Asian countries, highly regulated by hosts and remitting wages back to households. However,

migration for permanent residency has been very limited and mainly restricted to wealthy/business/professional groups.

The New Zealand economy has benefited from ongoing immigration from the region, though the balance and composition has sometimes been contentious. On the other side of the account, New Zealand has lost a considerable amount of talent – Kiwis who have benefited from state-funded education and health, but have then emigrated for lengthy periods, particularly to the diaspora attractions of Pacific Rim cities. Many local small technology companies have benefited from the New Zealand start-up environment and then moved offshore.

Emigration of people and businesses raises the question of appropriate tax policy in an Asia-Pacific region where capital and labour have become so mobile. New Zealand's tax structure, which eschews capital and inheritance taxes, does not look resilient when New Zealanders, their trusts and their businesses can enjoy state-funded benefits, then move offshore so easily, avoiding income tax and offering their human capital to other jurisdictions.

Technology change

In previous decades the important technological improvements mainly affected the physical movement of goods – containerisation, port handling, container ship developments, and the partial automation of large-scale production processes; labour costs were still important enough to determine choice of location through the region.

The technology changes of the last decade, commonly labelled the Fourth Industrial Revolution, have focused more on advanced intelligent automation, leading to more highly capitalised production facilities with reduced labour content. It is still too early to be sure of the consequences for the region with regard to location, scale and supply chains.

Of particular interest to New Zealand is the increased availability of new 'tradetech' and 'fintech' – digital technologies that offer automated sourcing, tracing, marketing, trade financing and payments systems. These have opened up interesting new business opportunities for long-distance exporters of biological

production like New Zealand, trying to capture value onshore.

There has been massive spread of knowledge and ideas in the region, increasingly encapsulated in electronic data, and sometimes regulated through intellectual property laws and privacy rules. These flows have grown far faster than other cross-border flows, and that trend will continue. However, there are growing tensions: so far, most of the region's consumer data is collected and owned by US technology giants, the exception being China, where local technology conglomerates are now looking to

bilateral trade surpluses and capital flows adding to the region's economic tensions. China has launched some major regional initiatives (Belt and Road, the Asia International Investment Bank, the New Development Bank), and these have mainly been welcomed in the region, while some more assertive Chinese security moves in the South China Sea have been regarded with suspicion and worry.

These are all concerns felt by New Zealand. New Zealand's export trade, as in many countries, is now dominated by Chinese markets. Their vigour has kept commodity prices strong, but has given no

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penetrate parts of the region. The international rules of digital engagement are still fluid: there are major regional disagreements over data ownership, participant privacy, cybersecurity, tax liabilities, 5G and 6G standards, and digital platform design.

China's resurgence

China's accession to the World Trade Organization (WTO) in 2001 marks the moment when a huge cheap labour force began to power the region's economy, resulting in new, highly competitive production structures and cheaper consumer products. Today its workforce has peaked, and the Chinese economy has entered a new phase, marked by massive capital investment and technological advances. The sheer size of the country means that this has an impact the whole region, and it has already led to redesign of regional production and supply chains.

The US administration has viewed these developments with suspicion: what used to be seen as complementary to Western economies has become a highly competitive relationship, with large

encouragement to increased local processing. By contrast, the US is now only New Zealand's fourth-largest trading partner, though it is far more important in terms of foreign investment, technology transfer, digital development and related security issues. New Zealand is trying to learn from ASEAN countries how to balance its economic interests in China with its security interests in the US.

Anti-globalisation

Public attitudes to economic regionalism have changed significantly in some Asia-Pacific economies, but not in others. As a generalisation, Western countries have this decade shown more concern about the loss of jobs and offshore business which they have (not always accurately) attributed to globalisation. In some cases, this has hit particular skills, regions or generations in a way that is breaching the social consensus for globalisation. In turn, this has had an impact on domestic politics and policy, most obviously in the US.

These developments have affected trading conditions around the Asia-Pacific, as the US administration has withdrawn

support from important political institutions (the Trans-Pacific Partnership, the WTO, the Paris Agreement on climate change, the World Health Organization), as its policies are confronted by an assertive rising China, and as the bilateral trade and technology tensions grow. The two superpowers appear to be increasingly locked in a trade/technology/financial war, with decoupling and self-sufficiency policies. Consequently, third countries like New Zealand have had to take the lead in promoting regional reforms.

The impact of this in the region has been ongoing concern in agencies such as APEC about the future of trade-driven growth; churn as supply chains are reconfigured to reduce political risk; distortion to commodity trade from US and China policies (including bilateral trade deals and domestic production subsidies for soybean, pork and dairy); increased domestic industrial policy protection; and regional concern about balancing US and Chinese economic and security interests. So far, the US–Chinese tensions have not significantly hurt New Zealand's economy, but there are clearly risks ahead if these tensions prove long-running.

The US is now suspicious of globalisation; many East Asian economies want more of it (but on their own terms). New Zealand is caught in the middle, reliant on regional trade but with pockets of discontent.

Climate change

Policy attention to the risks of climate change has grown quickly through much of the Asia-Pacific region. Recent extreme weather trends have raised visibility and exacerbated impacts, particularly in East and South East Asia, where the huge delta-dwelling populations are extremely vulnerable. The upstream damming of rivers, saline infiltration into rice paddies, flooding of deltas, temperature rise in inland regions, and typhoon damage in archipelagos make this the most affected zone in the world.

There is no agreed climate change policy in the region. Individual countries are reducing coal use and becoming more

assertive about emissions taxing, carbon trading and rubbish trading. But there is little leadership, with unresolved arguments about responsibility for emission legacies, and a focus in East Asian countries on carbon in consumption in response to the West's offshoring of production emissions.

The New Zealand economy has been alert to concerns about climate change far longer than many others in the region. New Zealand has its own climate change challenges. However, the impact on Asia will likely increase demand for food stocks, increase the need for emergency assistance, change the nature of infrastructure investment, tighten requirements for climate-friendly agricultural production, and result in the displacement of populations and increased environmental migration.

Covid-19

The Covid-19 pandemic has had huge impacts in the region in 2020. These include concerns about ongoing pandemic risks emerging from densely populated areas in East Asia; accusations and tensions particularly in the US-China relationship; experience that authoritarian, centralised Asian governments have been able to control the covert spread of the virus more effectively than many democratic governments; and evidence that East Asia has, subsequently, suffered less economic damage than the Americas.

Throughout the whole region, travel restrictions have meant massive problems for migrant labour, business travel, diaspora populations, health services, student movements and the tourism industry. Still ahead are challenges to improve identification, treatment and inoculation against ongoing Covid-19 and other epidemics. The trade in protective equipment and pharmaceuticals has exposed further tensions, and these may worsen with vaccine nationalism, despite cooperative efforts by APEC and ASEAN. Globalisation has brought many advantages to the Asia-Pacific region, but with its international spread, Covid-19 has become the most obvious example of its costs.

The impact of Covid-19 on New Zealand has been a significant lockdown

contraction, closed borders, slower growth prospects and rising debt. East Asian markets have bounced back more than American and European ones, and that has helped New Zealand maintain positive terms of trade. But Asian students for New Zealand tertiary education, Chinese, Japanese and other tourists to New Zealand, and other business interests have all been hard hit. On the positive side, New Zealand's relative success in limiting the spread of the disease has made the country an attractive safe haven in both Asian and American perceptions.

Leadership in the region

The Asia-Pacific economies have altered significantly over the past decade. New Zealand has been insulated from some of these changes and has benefited from others. However, there are some major hurdles ahead, and these may intensify New Zealand's traditional regional weaknesses – low export value-add, and leakage of talent and value overseas.

As an open economy with major trading interests, New Zealand has traditionally played an active role in the region, promoting trading opportunities and (less successfully) championing the liberalisation of agricultural trade. It has done this through formal regional initiatives (e.g. the P4 arrangement), pan-regional trade agreements (such as the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) and Regional Comprehensive Economic Partnership (RCEP)), international reform initiatives (WTO) and pathfinder projects (e.g. the New Zealand–Singapore Digital Initiative).

As New Zealand hosts APEC in 2021, this will be a key year for such economic leadership. After several years of debilitating regional trade tensions and the unproductive experiences of previous APEC hosts, expectations are high for New Zealand to produce a year of useful initiatives, helping APEC to come to terms with the economic regional challenges of this decade. This is made difficult by the spread of Covid-19 and the resulting need to run APEC by virtual technologies. Much will depend on New Zealand thought leadership and institution rebuilding.