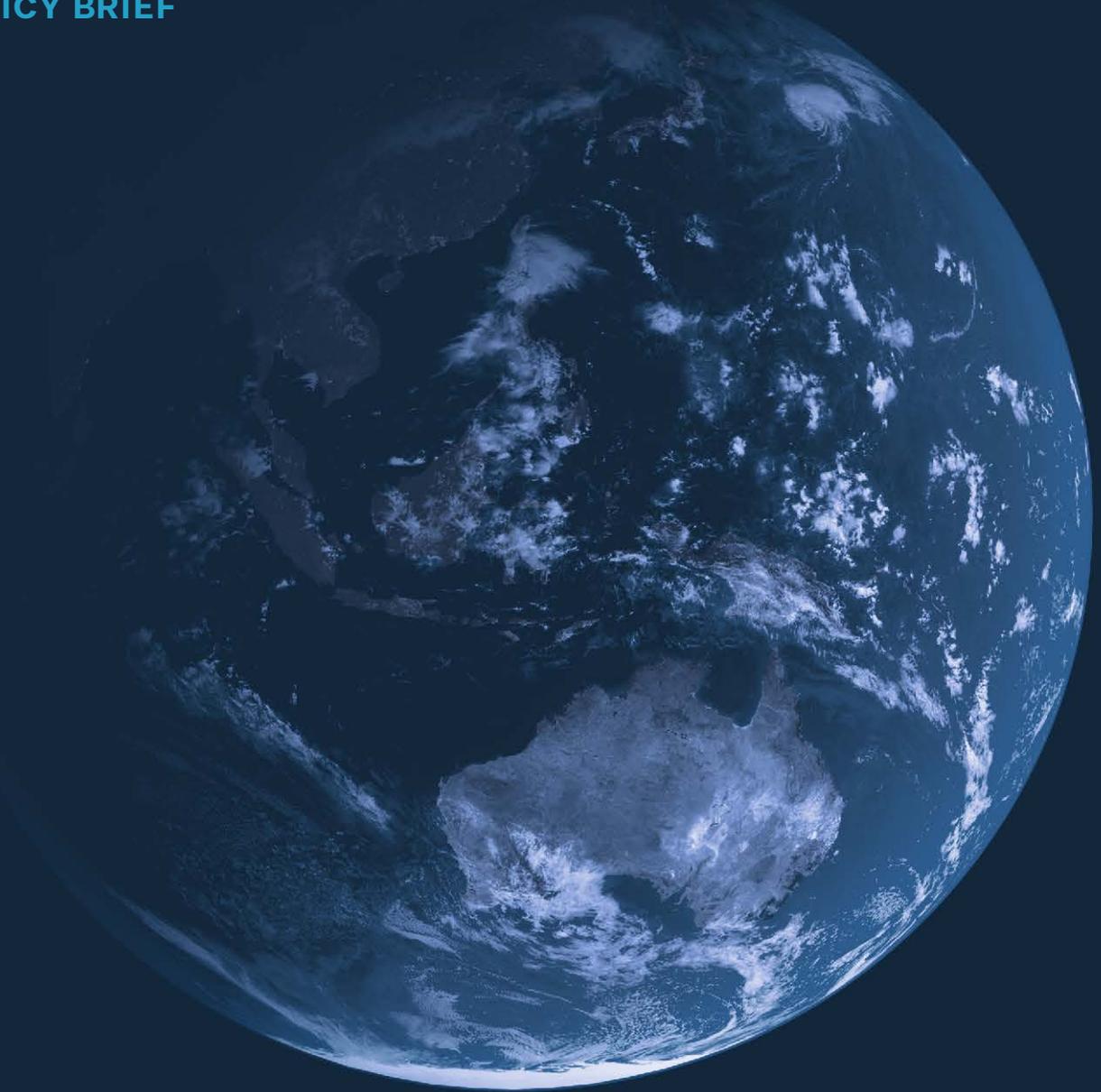


**LOWY  
INSTITUTE  
POLICY BRIEF**



# **Emerging from COVID: Policy Responses to the Pandemic**

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**JUNE 2020**

## **EMERGING FROM COVID: POLICY RESPONSES TO THE PANDEMIC**

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## INTRODUCTION

**In this new feature, Lowy Institute experts provide policy recommendations for Australia to address issues that are critical to our nation's — and the world's — successful emergence from the pandemic**

ALEX OLIVER

The fight against COVID-19 has been the greatest challenge the world has faced since the middle of last century. As countries have fought to control the disease, they have closed borders, quarantined their citizens, and shut down economies almost entirely. The ramifications will reverberate for years, if not decades, to come.

In April 2020, the Lowy Institute published a digital feature in which twelve Institute experts examined the ways in which the COVID crisis would affect Australia, the region and the world. In this new feature, Lowy Institute experts provide policy recommendations for Australia to address issues that are critical to our nation's — and the world's — successful emergence from the pandemic.

Countries have turned inwards in an attempt to fend off the threat of an infection that is oblivious to borders. Some have seen globalisation as the cause of the crisis, and have focused on solving problems without recourse to the international institutions of global security and prosperity, including the United Nations, the World Health Organization, and the G20. Yet global problems require international solutions.

As the world emerges from the crisis, cooperation between nations will be more important than ever. Nation states cannot revive their economies purely through national solutions. They cannot address global threats, including the possibility of further pandemics, alone.

Australia's achievements in managing the COVID crisis have been exemplary. It has handled the health and economic emergency with great competence. But this is just the beginning of our crisis recovery. The challenges in our region, and the global problems that existed before COVID, have only been exacerbated by the pandemic.

Australia has already done much to address the domestic economic and health issues from the COVID crisis. But to shape a prosperous and secure future, it will also need to work in cooperation with other nations, large and small, allies and partners, on a much broader array of international issues ranging from the economic disruption across the region, pressure from China on trade, and development challenges in the Pacific, to increasingly competitive relations between the United States and China, the weakening of the World Health Organization, and the declining utility of the G20.

## CHANGING AUSTRALIA'S CONVERSATION ABOUT CHINESE ECONOMIC COERCION

**Getting away from the narrative of dependence would be a starting point for a more sensible national discussion — one that is more robust to economic threats that may come our way**

NATASHA KASSAM, RICHARD MCGREGOR, ROLAND RAJAH

Last month, China banned meat imports from four large Australian slaughterhouses for “technical” reasons, and imposed tariffs of more than 80 per cent on Australian barley after a long-running WTO investigation at China’s instigation. This month, China warned its citizens not to travel to Australia for “safety” reasons. This flurry of punitive measures, and suggestions there could be more, has magnified concerns about Australia’s economic dependence on China and the belief that Beijing can use this to exert political pressure and constrain Australia’s ability to prosecute its interests. Calls for diversification away from China have consequently intensified.

Australia should have more confidence in its ability to withstand China’s punitive measures. The overwhelming narrative of ‘dependence’ leads the national conversation in unhelpful directions. Rather than dependence, the Australia–China relationship is mostly one of interdependence — which means that Australia’s exposure to, and ability to resist, economic threats from China is far more manageable.

It is true that China buys about a third of Australia’s exports of goods and services. But more than 70 per cent are resource commodities — vital inputs for China’s steel, construction, and other industrial sectors that are still central to its economy (and employment), especially in recovering from COVID-19. Finding alternative suppliers at scale in these areas would be difficult for China.

As long as China’s demand for these commodities remains strong, so too will global demand — benefitting the Australian economy

either directly by selling to China, or indirectly if exporting elsewhere, because international prices will remain robust. The past two years have seen Australia placed in China's so-called 'diplomatic freezer'. Yet, the total value of Australia's merchandise exports rose by 30 per cent during that time. Merchandise exports to China rose by 50 per cent. That is also in keeping with the international experience of China's attempts at economic coercion, which tend not to have a material impact on overall trade but instead punish specific sectors and firms.

That is, of course, cold comfort for those being targeted. And in Australia's case, the potential targets are expanding as the economic relationship shifts from resource commodities towards agricultural exports, higher education, and tourism.

It is important, however, not to exaggerate the costs of standing up to China where Australia needs to. The value of what Australia sells to China in these areas is still only a little more than one percent of Australia's national income. That is important and should not needlessly be jeopardised. But Australia's national interests are hardly served by artificially dividing national security and the economy.

Importantly, the flipside of interdependence is complementarity. Diversification might be desirable, but the prospect for doing so in any significant way is likely to be very limited. India and Indonesia cannot match China's combination of growth and scale. Nor are they particularly open economies or easy places to do business, at least no more so than China.

Australia's relationship with China is entering a new, more difficult phase, for which there are no easy answers. Getting away from the narrative of dependence would be a starting point for a more sensible national discussion — one that is more robust to economic threats that may come our way.

## SHAPING THE US APPROACH TO CHINA AND THE RULES-BASED INTERNATIONAL ORDER

**Canberra should urge a more sophisticated and sustainable approach, drawing on America's political and economic strengths, rather than its military weight, and be more inclusive of allies and partners**

BEN SCOTT

The US–China relationship is more adversarial and brittle than at any time since ties were normalised in 1979. Having claimed victory over COVID-19, Chinese President Xi Jinping has turned to subduing supposedly hostile ‘foreign forces’ on fronts from Hong Kong to India. Eager to shift blame for his failure to manage the pandemic, US President Donald Trump has injected increasingly confrontational rhetoric into Washington’s sporadically competitive China policy. The UN-centred order was built up to help manage great power tensions like these, but has shown itself to be battered and ineffective.

Canberra faces a particularly daunting challenge. It is deeply enmeshed with the United States — its longstanding security ally — but has China as its dominant trading partner. The continuing US–China escalation could, as well as weakening international cooperation against COVID-19 and its economic impact, see China further restricting Australian access to its markets. And, though US–China military conflict is still unlikely, the risks are growing. Any war would be especially catastrophic for our region.

To forestall escalation, Australia should pursue three broad lines of effort.

First, Canberra should engage Beijing diplomatically, while understanding that there is not much Australia can do to moderate China’s current threat perception.

Second, Australia should collaborate more with like-minded middle powers to salvage the rules-based order and increase cooperation.

This work is well underway, but remains extremely difficult without US leadership.

Third, Australia should seek to shape Washington's approach to China and the rules-based international order.

Australia wants the United States to balance Chinese power and deter Chinese coercion. Washington's new bipartisan willingness to compete with China broadly accords with Australia's interests.

But Canberra should urge a more sophisticated and sustainable approach. That would draw on America's political and economic strengths, rather than its military weight, and be more inclusive of allies and partners. It would also balance competition on national security issues, with cooperation on matters such as health and mutually beneficial trade.

From Canberra's perspective, the ideal US policy would be like Goldilocks' perfect porridge — not too hot, not too cold. That's a big ask, but still the best objective for Australia's near-term efforts.

The US elections in November could open a window of opportunity for change. Admittedly, a Biden Administration would be domestically focused and may have little appetite for committing scarce resources to countering distant China. But those resource constraints could also compel America to compete with China in a smarter way.

A Biden Administration would be receptive to Australian views. Canberra has standing in Washington, especially on China. Australia has arguably accepted more risk to its China equities than any other country as it has hardened protections of its political life and communication networks, and has sought to investigate the origins of COVID-19.

Australia's first goal should be inducing the next US government into a modified (and better-named) version of the CPTPP (Comprehensive and Progressive Agreement for Trans-Pacific Partnership). This agreement embodies a more sophisticated, rules-based, approach to balancing China. The United States would clearly accrue economic benefits and, despite rising protectionist sentiment, Vice President Joe Biden has sounded more positive about this approach than the last Democratic nominee Hillary Clinton did. Still, Australia should work to make the deal more

attractive. In the aftermath of COVID-19, existing signatories should be receptive to adding mechanisms for securing medical or other critical supply chains. That would also give the agreement new salience in Washington.

Australian leaders and diplomats should make these arguments soon, and do so more publicly than they ordinarily would in the lead-up to a US election. The stakes are high, as are Australia's stocks in the wake of its successful COVID performance. But social distancing will preclude the discreet discussions of more normal times. So the time to speak up is now.

## MAINTAINING AUSTRALIA'S SECURITY AS AMERICAN POWER RECEDES

**We cannot build a defence force that could defeat a major power such as China, but we can create one that will make it too costly for China to defeat us**

SAM ROGGEVEEN

With US–China relations now at their lowest point since Nixon met Mao, and even Chinese Foreign Minister Wang Yi warning of a new Cold War, the world seems poised on the brink of dangerous confrontation. For Australia, the stakes could not be higher — one of these superpowers is our largest trading partner, and the other our key military ally.

But unlike the struggle between the United States and the Soviet Union that scarred the latter half of the twentieth century, one key element is missing this time, one that is likely to see the US back away from confrontation rather than challenge China. That element is motive. The United States simply does not have a good enough reason to engage in a multi-generational, whole-of-society struggle with the largest economy in the world, a struggle that would dwarf the Cold War in the resources it would consume.

Yes, COVID-19 has raised the temperature of US–China relations, but ultimately the pandemic will reinforce the sense that the biggest threats to America's future are domestic, not foreign. America has been turning inwards for some time; the drift away from exceptionalism and towards becoming a more 'normal' great power began during the Obama Administration.

COVID-19 only increases the urgency of repairing America's domestic institutions. By contrast, despite the rancour caused by China's mishandling of the pandemic, the virus does not offer a compelling reason to resist Beijing's ambitions in Asia.

Despite China's size and rapidly increasing military might, it will never be a direct threat to the United States, which will remain a great power with enormous economic resources, powerful armed forces, and nuclear weapons. Moreover, China will remain

constrained by Asia's other great powers — in particular India, but also Japan, Russia, and in the future even Indonesia, and perhaps a unified Korea.

As a consequence, Washington lacks the motive to maintain its commitments to allies in the region, such as Australia. That means we will need to be more self-reliant than ever.

Canberra has been reluctant to embrace this sobering conclusion, though there are signs this is changing. The Morrison government's March deal to re-establish an Australian fuel reserve is a small indicator that it is taking national resilience and self-sufficiency more seriously. This should be the spark for a much more difficult discussion about strategic independence: can Australia defend itself against a major power without America's help?

It can be done, but it will be expensive. Australia will need a bigger military with large stockpiles of weapons and strategic materials so that we are self-reliant in a crisis. We cannot build a defence force that could defeat a major power such as China, but we can create one that will make it too costly for China to defeat us. We should focus on 'denial' capabilities such as submarines and other anti-ship systems which will make our northern approaches too dangerous for any adversary. And our defence diplomacy efforts should have a laser-like focus on Indonesia, as we both have a clear interest in ensuring China does not become the dominant maritime power in Southeast Asia.

To pay for it all, we will need a larger population. And depending on the pace of America's withdrawal from Asia, Australia may ultimately need to confront the grim question of whether we should acquire nuclear weapons.

## STRENGTHENING THE WHO BY GIVING IT LEGAL TEETH

**The best political choice for Australia now would be to promote greater legal authority and powers for the WHO. No other organisation can fill this role**

HERVÉ LEMAHIEU

COVID-19 was no ‘black swan’ event. In September 2019, an expert panel convened jointly by the World Health Organization and the World Bank warned of the “very real threat” of a global pandemic. Presciently, they noted that “the lack of continued political will at all levels” to prepare for a global health emergency would cost the world economy up to 4.8 per cent of global GDP.

Despite the warnings, the international community has struggled to deliver a coordinated response to what the UN Secretary-General has termed the largest global crisis since 1945. Quite apart from a health emergency and economic crisis, COVID-19 has unleashed a political pandemic of disinformation and blame that has increased the sense of disarray.

The magnitude of human lives lost from COVID-19 calls into question the WHO’s fitness for purpose in a global health emergency. Australia has an opportunity to strengthen a beleaguered but vital organisation. However, leading the charge will require us to address head-on the imbalances of power and responsibilities between the WHO and its member states that exacerbated the spread of the virus.

The WHO is the only global institution responsible for identifying when domestic public health issues become global ones. But the organisation has limited resources and no real legal authority to take countries to task for obfuscating an emerging epidemic. This has led to costly mistakes and compromised the WHO’s perceived neutrality and independence, which are both vital for the organisation’s work and its global legitimacy.

WHO leaders likely chose to laud China’s coronavirus performance in order to overcome Beijing’s reluctance to share vital information about the virus and secure access for its investigation teams into

the country. This show of deference may have succeeded in clearing a political bottleneck, but it came at a significant reputational cost to the organisation and contributed to the political storm that followed.

The question of China's influence on WHO decision-making is controversial and will no doubt be formally reviewed. But we must be careful in drawing conclusions. Pursuing a change in WHO leadership would, on its own, do little to address the structural flaws that often compel the WHO Secretariat to walk on political eggshells around its member states.

Instead, if we are serious about ensuring the WHO's independence and ability to deliver on its global health security mandate, Canberra has no alternative but to commit to deeper reforms. These include setting stronger international agreements on disease preparedness and response, a stricter set of International Health Regulations (IHR) under international law, and a bolstered WHO epidemic transparency and accountability mechanism to monitor non-compliance with the IHR.

In a stocktake of its performance, the WHO's successes are as important as its failures. It took just four days from when the virus' genome became available on 12 January, for the WHO to develop and share a test that laboratories around the world could use to detect the novel coronavirus in patients.

By 23 January, less than a month after the first cases of pneumonia with unknown causes were reported to the WHO, member states had all the basic information on fatality rates, severity, and transmissibility they needed to accurately judge the risk of COVID-19. By contrast, it took nearly six months to identify the virus responsible for the 2002–03 SARS outbreak.

If this did not prompt rapid action by political leaders in Europe and the United States, it is at least in part because Western leaders responded to the WHO's alerts with extraordinary indifference.

COVID-19 has laid bare the tension between the primacy of nation states and the efficacy of global institutions. It has reminded us that in a multipolar world, technical cooperation will always be political. But the best political choice for Australia now would be to promote greater legal authority and powers for the WHO. No other organisation can fill this role.

## CURING THE G20'S IRRELEVANCE

**Australia has more reason than most members to strive for substance in the G20's next meeting, as the Group is in danger of slipping into irrelevance**

STEPHEN GRENVILLE

A pandemic provides the perfect opportunity for a global coordinator to demonstrate its worth. Health and economic issues have international ramifications aplenty. The G20 — founded to provide precisely this kind of high-level global coordination — has been barely visible.

In normal times, the G20 is little more than a photo opportunity for leaders, with useful chats on the sidelines. The hope was that when substantive issues occurred, G20 would rise to the challenge.

This, however, requires leadership. UK Prime Minister Gordon Brown provided such leadership in 2009, with coordination of fiscal stimulus. This modest initiative fostered the hope that, when needed, the G20 could again play a global coordinating role.

The G20 is currently chaired by Saudi Arabia, which has little capacity for global leadership. President Trump is actively unsympathetic. Other members are absorbed with domestic aspects. Unsurprisingly, the ad hoc virtual meeting of leaders in March produced nothing beyond platitudes.

The meeting came too early in the crisis, when leaders were distracted. The virus blame game between America and China continued unabated. Since then, the trade spat has deepened into a strategic tussle, with other countries sucked into the vortex. 'Peak globalisation' is now behind us.

This is the current inhospitable environment for the G20. It may not matter for G7 countries, which have retained their own exclusive global club. But for mid-sized countries like Australia, heavily dependent on globalisation for their high living standards, the G20 provides a rare opportunity to play on the global stage.

What specific proposals could Australia develop for the November Leaders' Summit?

One urgent health issue stands out. A return to normality depends crucially on a vaccine. If one is found, the next issue is to speed its production and ensure an equitable distribution, prioritising those in greatest need. Leaving this to individual countries and companies is unlikely to be optimal. A few fine words in a communiqué is not enough. A plan with specific commitments is needed.

On the economy, here are two specific proposals:

- When the G20 finance ministers met in April, they agreed on a foreign-debt moratorium for 76 of the poorest countries. But it is not only the poorest nations that need debt relief: the substantial US dollar-denominated debt built up over recent years by many emerging economies is at risk of disruptive defaults as the pandemic worsens. This could trigger renewed capital outflows. Both debtors and creditors could benefit from delaying repayment until the uncertainty lessens, but someone needs to initiate a proposal. In the longer term, formal debt-rescheduling procedures are needed, especially for sovereign debt. But the urgent low-cost task is simply to postpone repayments.
- Another issuance of International Monetary Fund (IMF) Special Drawing Rights would be very timely for the emerging economies and would have minimal cost for the major Fund members.

Gordon Brown's 2009 initiative is remembered because it was relevant, substantive, and he lobbied tirelessly in support. Australia has more reason than most members to strive for substance in the G20's next meeting, as the Group is in danger of slipping into irrelevance. These three proposals would show what the G20 can do.

## FORMING A COALITION OF COMPETENT MIDDLE POWERS TO LEAD ON GLOBAL HEALTH PROBLEMS

**COVID-19 has shown that there are opportunities for creative diplomacy in a more horizontal world. Change will have to come not from a single power source, but from a networked grid of competent middle powers**

HERVÉ LEMAHIEU WITH ALYSSA LENG

The coronavirus is a powerful reminder that legitimacy and leadership on the world stage start with the capacity of leaders to govern competently at home. The reputations of both China and the United States have diminished as a result of their handling of the emergency. Both have written themselves out of global crisis leadership.

By contrast, recent Lowy Institute research reveals that a larger proportion of small and middle powers have done better at handling COVID-19 than their great power counterparts.

Countries such as Australia, New Zealand, Taiwan, South Korea, Vietnam and Denmark slowed the spread of the virus through bold policy interventions at an earlier point on their epidemic curve. This places many advanced middle powers in a unique position to carve out constructive roles for themselves in global pandemic response and recovery efforts.

The major dividing line in effective crisis response, according to Francis Fukuyama, has not been regime type, “but whether citizens trust their leaders, and whether those leaders preside over a competent and effective state.” Trust and state capacity are often comparative advantages for countries that have smaller populations, greater social cohesion, and capable institutions.

Australian government agencies, research institutes, and scientists are now at the forefront of what Lowy Institute Executive Director

Michael Fullilove has termed “coalitions of the competent”. These informal groupings have sprung up across international jurisdictions to lead the way in a multitude of policy areas: from the resumption of international travel through shared ‘travel bubbles’, to research on the development of a vaccine and therapies to treat the virus.

Middle powers have also shown that, when they work together, they can forge global consensus even in a multipolar and dislocated international system. When Australia and the European Union successfully steered a resolution through the World Health Assembly, they did so with the largest number of co-sponsors in the 72-year history of the WHO. The net result is the global health body’s handling of the pandemic will be open to scrutiny, but the organisation’s centrality to global health policy has not been undermined.

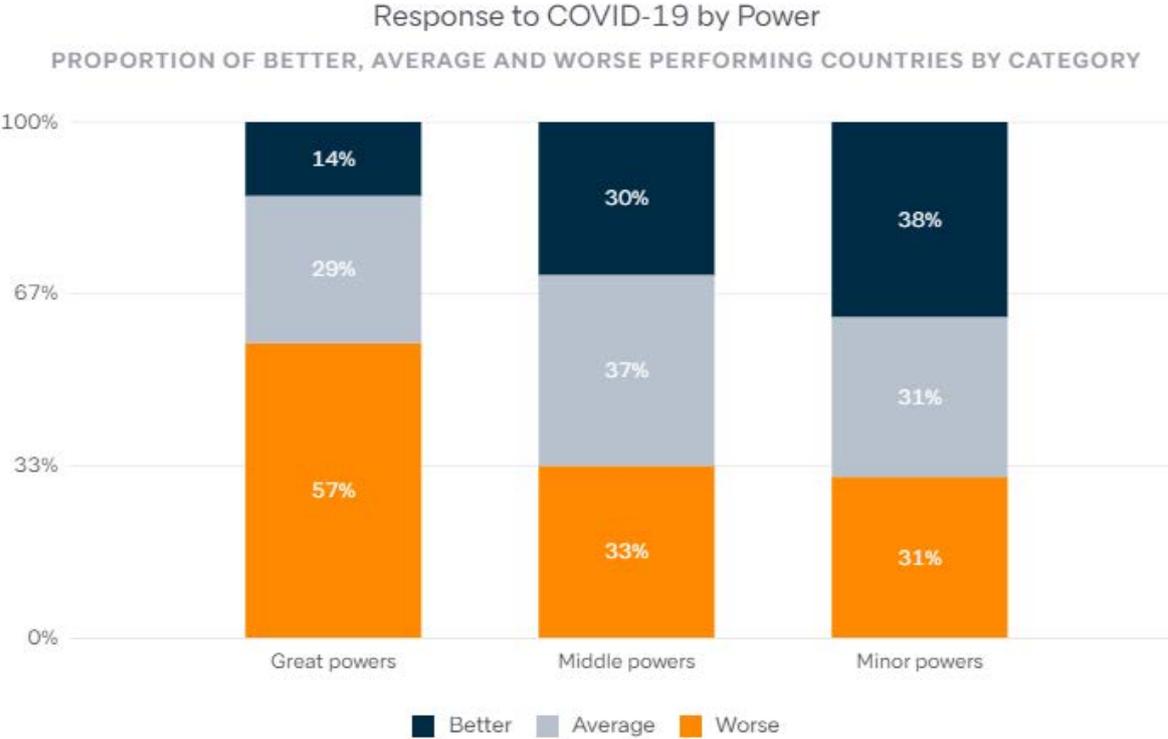
Now that the vote is won, other things become possible. Creative diplomacy will be required to strengthen global health governance. The pandemic has shown the need for reliable information to be shared equitably and rapidly between countries. To address this, middle powers should consider establishing an enhanced global monitoring facility, based in the WHO, but with independent accountability.

In the interim, a middle power grouping can also consider activating a dispute settlement mechanism under the International Health Regulations to clarify the application and interpretation of existing procedures. This may help improve the openness and transparency of the WHO Emergency Committee process, provide clarification for a stepped-up level of emergency alerts, and reassess the WHO Secretariat’s role in providing travel advice during a pandemic.

Finally, with the loss of US funding all but certain, the race is on for middle powers to fill the WHO’s most egregious financing gaps. Australia is already pivoting its aid program to work with the WHO on capacity building in its near abroad. This regional approach can be enhanced by working with a consortium of donors on a coordinated global funding strategy. Similar foresight and coordination will be required to replace the loss of a US voice at the World Health Assembly — particularly when the time comes to appoint the next Director-General of the WHO.

COVID-19 has shown that there are opportunities for creative diplomacy in a more horizontal world. Change will have to come not

from a single power source, but from a networked grid of competent middle powers.



Country performance in response to COVID-19 is determined by a composite score based on six equally weighted indicators: total confirmed cases and deaths, total confirmed cases and deaths per million people, total tests per confirmed case and thousand people.

## MANAGING AUSTRALIA'S ECONOMIC RECOVERY

**Matching its success in containing the pandemic with success in constraining long-term unemployment is Australia's next big challenge, and one no less formidable than the pandemic itself**

JOHN EDWARDS

After infecting more than 19000 Australians and killing over two hundred and fifty,<sup>1</sup> the coronavirus epidemic in Australia is fading, with fewer lives lost and less economic damage than first expected. Reckoning total COVID-19 fatalities compared to population running at less than one fiftieth of the rate in the United States and one seventieth of that in the United Kingdom, the handling of the pandemic by Australian governments, hospitals, health care workers, and public officials has been more successful than the experience of some similar societies.

Yet the damage is substantial, and will have lingering effect. The output loss compared to pre-COVID forecasts may well top 6 per cent of GDP. The number of unemployed will increase to over a million. With big spending programs to support employment and incomes, and government revenues falling, the record high 2019/20 budget deficit will be more than doubled for the current financial year. Business and household debt have also increased. In a sharp change to policy, the Reserve Bank of Australia has already more than doubled its holdings of Australian dollar government and private debt and announced a ceiling not only on the overnight or cash rate, but medium-term bond rates as well.

As the health emergency ends, it is apparent that the pandemic will change the terms of the political and economic debate in Australia — as it may change the debate in other Western democracies. Stubbornly high unemployment will now be the central issue at the next election, likely to be in 2022. The choice for Australia — as in Europe and North America — will be between the rapidity with which increasing government debt can be reined in, and the rapidity with which jobs can be created and unemployment reduced.

Although the fiscal challenge to the Australian government is formidable, it is well within Australia's means to manage the interest expense of the additional debt. Most of the fiscal deterioration arises from slower output growth over the next few years, rather than the direct cost of programs to support jobs and spending. Even given a severe contraction, net Australian government debt compared to GDP will likely remain well under that of most advanced economies. Because sovereign debt is very cheap and the cost of long-term unemployment is very expensive, it will not be sensible to aim for a rapid reduction of deficits at a time of high unemployment and fragile sentiment. On the contrary, the Australian government needs to find useful ways to extend deficits created by temporary spending. So, too, the Reserve Bank of Australia will likely find it needs to maintain very low short- and medium-term interest rates for several years to come – not least, to suppress an appreciation of the Australian dollar to uncompetitive levels. Matching its success in containing the pandemic with success in constraining long-term unemployment is Australia's next big challenge, and one no less formidable than the pandemic itself.

The challenge is all the more formidable because the emerging post COVID global economy will likely be less congenial to Australian prosperity. The pandemic has inflamed tensions between the US and China, encouraged protectionist trade policies, and for the foreseeable future locked major advanced economies into high and rising levels of government debt, much of it held by their central banks – a pattern which cannot be indefinitely sustained.

1. *This is an updated version of the article originally published in June 2020, with new data as at 6 August, 2020.*

## ASSISTING INDONESIA THROUGH THE ECONOMIC PANDEMIC

**Well-calibrated Australian support could make a pivotal difference to lower the risks and help Indonesia finance the budget deficit needed to get through the pandemic**

ROLAND RAJAH

Emerging economies everywhere are being especially hard hit by the economic pandemic unleashed by COVID-19. In Australia's region, the most consequential of the emerging economies is Indonesia, given its size, proximity, and general centrality to our economic, diplomatic, and security interests.

Indonesia now faces one of the most difficult outlooks in Asia. Its battle with the virus remains uncertain, while its reliance on foreign financing has left it exposed to capital flight and struggling to fund the fiscal response needed to keep its economy (and society) afloat through the pandemic. Without enough fiscal support, the economic damage from the virus will be far deeper and longer lasting — setting back its economic rise, leaving more people in poverty, and weakening its foundations for ongoing stability.

Australia has a clear national interest in helping Indonesia avoid this situation and, if requested, Canberra should provide Jakarta with large-scale financial support. Importantly, this could be done at little to no cost to the Australian taxpayer — which is crucial, given Australia is itself dealing with a steep economic downturn and massive domestic calls on its own budget that will necessarily take precedence.

Indonesia could theoretically turn to the IMF for assistance. But the IMF is still politically toxic in Indonesia — a legacy of the last crisis in the late 1990s. As it stands, Indonesia would probably not turn to the IMF until it was too late.

The Indonesian government has instead taken the unorthodox step of asking Bank Indonesia, the central bank, to help fund part of the budget deficit, effectively by “printing” money. This is feasible, if it

remains modest and investors see it as a temporary exigency. Yet the budget financing shortfall could prove much larger than expected. Indonesia's fiscal response to the virus (about 4 per cent of GDP so far) is also one of the smallest in Asia and could be usefully expanded.

Indonesia, therefore, faces a painful choice between potentially unnerving the market with greater central bank financing — risking more outflows of capital — or limiting fiscal support to a severely depressed economy. This is where well-calibrated Australian support could make a pivotal difference to lower the risks and help Indonesia finance the budget deficit needed to get through the pandemic.

Specifically, the Australian government should be willing to provide a large 'standby loan' facility — perhaps as much as A\$15 billion— that would be readily available if Indonesia were unable to raise enough from the market to finance its budget deficit. Canberra has done similar things before, but on a smaller scale. To enable large-scale support, the loan terms could be anchored against Indonesia's own sovereign borrowing costs during 'normal' times, instead of being a low interest loan as in the past. The cost to the Australian budget of extending the loan would then be minimal, since it would implicitly include pricing for the risk of default.

An Indonesian default is extremely unlikely. If it did happen, it would mean an Indonesian crisis so deep that default would be the least of Australia's concerns. Far more likely is that Australia will have helped a key partner get through an unprecedented crisis at little to no cost to itself.

## STEPPING UP IN SOUTHEAST ASIA

**This proposed step-up is not just about Australia demonstrating its commitment to Southeast Asia. The relationship goes both ways. Australia can only truly thrive again when Southeast Asia is back on its feet**

BEN BLAND

Australia should step up in Southeast Asia to help this vital region emerge from the pandemic and support the economic recovery of our second-biggest trading partner. This mission has become even more critical because of shifting geopolitics, with China intensifying its engagement in Southeast Asia and the reputation of the United States badly damaged.

There are three specific areas in which Australia and the region would benefit from further cooperation: tackling the pandemic, limiting the negative economic impacts of the health crisis, and mitigating social and governance challenges.

Canberra's Partnerships for Recovery policy sets out an ambitious vision for what Australia can do to help maintain stability, security, and prosperity in Southeast Asia as well as the Pacific. However, it is based on a redirection of the existing development budget, which has been shrinking in recent years. Australia cannot keep getting 'more for less'. The government should expand its budget for Southeast Asia, because this crisis is an important test of Australia's commitment to the region.

There are limits to what Australia can do alone in a diverse region of more than 650 million people. Therefore Canberra's response should be targeted and pragmatic. Australia should capitalise on its existing web of bilateral, minilateral, and multilateral relationships, not just with governments but with development banks, the private sector, and civil society.

The focus should be on working with committed partners to tackle specific challenges, from air travel protocols and trade facilitation to vaccine development and national stockpiles of medical equipment.

Bilateral engagement should be high-level but low-key. The real value Australia can add is not in handing over containers of face masks at public ceremonies, but in providing technical assistance and building trusted partnerships behind the scenes. Australia should work bilaterally and with the Association of Southeast Asian Nations (ASEAN) to improve the region's own pandemic response capabilities, in expectation of future waves of the novel coronavirus and other diseases.

On the economic front, Australia should work bilaterally and through the World Bank, Asian Development Bank, and IMF to ensure governments have the necessary policy support, as well as possible emergency funds, to emerge from the crisis as soon as possible. A particular priority should be given to assisting vulnerable groups, including those in poverty, children whose education has been interrupted, and the millions of documented and undocumented migrant workers who are often overlooked by governments. Australia should consider adapting the successful Prospera program — which provides wide-ranging technical support to the Indonesian government — to other countries in the region.

Canberra should also intensify efforts to deepen private sector economic engagement with Southeast Asia, building on the recently ratified Indonesia–Australia Comprehensive Economic Partnership (IA-CEPA) and the proposed Enhanced Economic Engagement Strategy with Vietnam. Although the pandemic will hit economic growth in the short term, it will present new opportunities for investment in health, technology, and education across Southeast Asia.

While other development partners bring more financial heft, Australia should leverage its own strengths, including its track record of cooperation with civil society. The pandemic has prompted a further spike in authoritarian behaviour by the region's governments, while the accompanying economic crisis has badly affected the finances of NGOs that were already struggling. Australia should support civil society organisations through this difficult time because governments alone cannot build resilient societies.

This proposed step-up is not just about Australia demonstrating its commitment to Southeast Asia. The relationship goes both ways. Australia can only truly thrive again when Southeast Asia is back on its feet.

## HELPING THE PACIFIC RECOVER FROM COVID

### **Australia's Pacific Step-up is more relevant than ever, but it needs to be refocused on economic recovery**

ALEXANDRE DAYANT, SHANE MCLEOD

The Pacific's early success in fending off COVID-19 does not render the region immune to the far-reaching effects of the virus. Not only has the pandemic exposed alarming weaknesses in their health systems, but Pacific nations, which heavily rely on tourism and trade, are already feeling the devastating economic consequences of the pandemic. Some estimates put a regional economic contraction as high as 10 per cent for this year alone. Despite governments drawing on every domestic resource available to stimulate their economies and consolidating their health systems, the region is struggling.

International support has been forthcoming, in the form of in-kind medical donations, equipment and supplies as well as financial support. Australia committed a regional package of up to A\$100 million in direct budget assistance — a 'quick financial support' for Pacific countries hit by the pandemic and the ill-timed arrival of Cyclone Harold.

But these solutions do not fully address the needs of many nations.

First, Pacific Islands nations require additional support for their health systems. These countries are among the least ready for a pandemic, and most have limited capacity to test for the virus.

In the past five years, Australia's aid funding for health programs across the Pacific region has been reduced, even as Pacific nations have wrestled with health crises, including a catastrophic measles outbreak, polio, and drug-resistant tuberculosis. Instead, aid financing has been reprioritised to more geostrategically appealing infrastructure investments. This current crisis offers an opportunity to change the trajectory.

In the long run, investing in the health systems of the region not only makes those nations less prone to health emergencies, but it also improves the security of all Pacific countries, including Australia.

Second, most Pacific Islands nations need financing support to keep their economies afloat. While a few have some fiscal space to increase their expenditures, most do not.

Australia's Pacific Step-up is more relevant than ever, but it needs to be refocused on economic recovery.

Aid should be redirected towards the backbone of Pacific domestic economies, namely small businesses and the agricultural sector, as well as tourism and hospitality — both severely hit by worldwide travel restrictions. Fast-tracking the A\$2 billion Australian Infrastructure Financing Facility for the Pacific (AIFFP) would help to foster economic recovery through the construction of important infrastructure projects. Pacific labour mobility also needs to be increased, once travel restrictions allow.

Australia will need to make special provision in its response for Papua New Guinea. Its size and scale — and its land border with Indonesia — will make the coronavirus response an ongoing challenge. The economic and health system challenges faced by the entire region will be even more severe in PNG.

Finally, Australia should continue to take a leadership role in advocating for international assistance for the region. Prime Minister Scott Morrison's call at the March G20 meeting to support the Pacific must be reinforced.

Canberra should aim to be innovative and adaptable. Australia's early success in containing the virus has delivered what has been described as a 'Covid dividend'. It should spend some of that dividend wisely to benefit its Pacific neighbours, now and into the future.

## REVIVING AUSTRALIA'S AID PROGRAM

**In a region where crises amplify fragility and instability, the bill will be much larger for Australia if it does not act now to provide the right amount, and the right kinds, of support to its neighbours**

JONATHAN PRYKE

Since 2014, through successive budget cuts, a hasty merger of AusAID into DFAT, and the consequent attrition of development professionals, the Australian aid program has become a shell of its former self. The Coalition government has cut the aid program by almost a third from its \$5.5 billion peak in 2013–14, adjusting for inflation. The aid program, when measured as a portion of Australia's Gross National Income (GNI), is now the least generous it has ever been in Australia's history.

One thing that is clear as we emerge from the COVID pandemic is that Australia will find itself in a region much poorer and less stable than it was in 2019. Australia will no longer have the luxury of spending so little to help ensure regional prosperity and stability.

Australia stands out globally for its success in handling both the health and economic crises of the pandemic. This makes Australia one of the only countries with the means to take a leadership role in helping our region get back on its feet after COVID-19. Seventeen of Australia's closest twenty neighbours are aid recipients. Doing more to help our region is not only our moral duty; it is also in Australia's national interest.

Presuming the government does not cut the aid budget this year, the economic contraction Australia will face in 2020 will, by default, increase our apparent generosity. Thereafter, Canberra should increase our level of official development assistance (the proportion of ODA to Gross National Income) by 0.01 per cent each year until Australia at least meets the OECD average of 0.38 per cent. This increase, roughly \$400 million in the first year, should be focused exclusively on rapid economic stimulus in Southeast Asia and the Pacific. Even at this modest rate of growth, the aid program would not return to its 0.34 per cent peak for another 15 years.

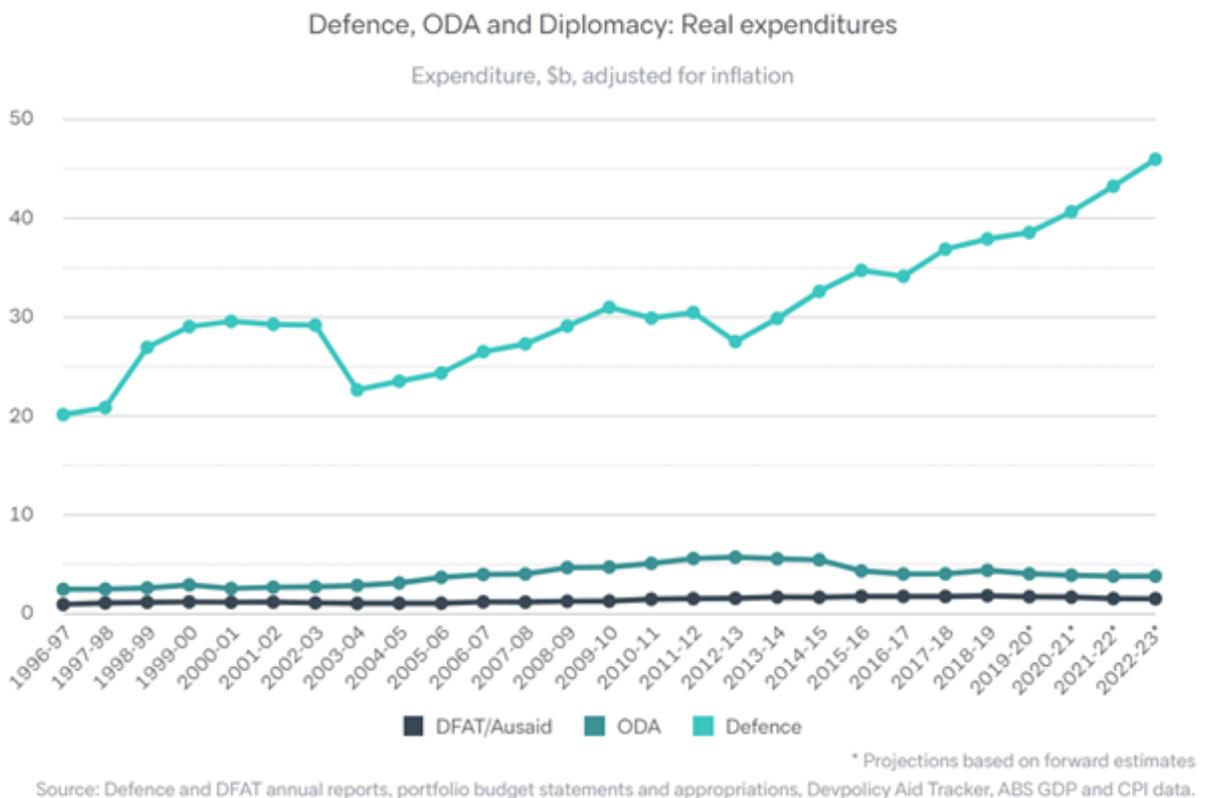
Increasing the aid budget without significant reform will not be enough, however. As aid volumes have declined, so too has capacity. The government recognised this in calling for a development review last year, which has rightly been put on hold during the COVID crisis. This review should not, however, be abandoned but instead expanded by appointing an independent review team, similar to the 2011 Hollway review, to give it real teeth. The objectives of Australian aid, the governance and management of aid within DFAT, the accountability and measurement of aid performance, and the modalities of aid delivery are all areas in need of reform.

Increasing and improving the aid program will be a tough sell in a climate where Australian voters are already facing an intergenerational tax burden. But in a region where crises amplify fragility and instability, the bill will be much larger for Australia if it does not act now to provide the right amount, and the right kinds, of support to its neighbours.

## REVALUING AUSTRALIA'S DIPLOMACY

**With an increasingly assertive China and a weaker America embroiled in internal discord and external competition, the deft management of Australia's international relations is becoming ever more crucial**

ALEX OLIVER



The story this picture tells has been told with monotonous regularity by the Lowy Institute in research projects since 2009. The “diplomatic deficit” — the title of the Institute’s 2009 investigation into the instruments of Australia’s international relations and their fitness for the twenty-first century — has become global shorthand for the underfunding and undervaluing of diplomacy worldwide.

The predicament the world finds itself in at the turn of the decade shows just how important diplomacy is. Of course, national responses have been critical in suppressing the spread of COVID-19

within borders. But COVID has also revealed the limits of sovereign control. Globalisation has melted borders, making the job of containing the spread of the virus virtually impossible. Almost every aspect of national responses has involved diplomacy in some way — whether in closing borders, helping evacuate stranded citizens, engaging with the World Health Organization, or delivering assistance to vulnerable neighbours. From Australia’s perspective, one of the most recent demonstrations of the value of diplomacy has been our work behind the scenes with the European Union to establish an investigation into the origins and global response to the pandemic. A less conspicuous example of several years of diligent diplomacy was the ‘Quad-Plus’ meeting in late March between officials from the United States, Japan, India and Australia (the Quad countries), along with representatives from New Zealand, South Korea and Vietnam. The goal was to discuss pandemic response coordination as well as plans for reviving regional economies. If there is a revised G7+ grouping, as mooted by President Trump, that will also require a concerted effort from Australian diplomats to ensure it does useful work.

This strenuous diplomatic agenda requires a diplomatic corps operating at peak ability. Yet for decades, Australian diplomacy has been sapped by increasingly strained budgets, relentless ‘efficiency dividends’ and workforce cuts. In real terms, its budget has not just flatlined, it is declining, and in 2022 will be smaller than it was 15 years earlier, in 2007. Australia has the world’s thirteenth largest GDP and defence expenditure, but only the twenty-seventh largest diplomatic network. There are fewer Australian diplomats posted overseas today than there were 30 years ago. That number, now 860 diplomats, is dispersed across 84 countries and must manage the full spectrum of Australia’s foreign and trading relations, including providing consular assistance to Australians abroad — a very public function that has been scrutinised closely in the COVID crisis. Since March, DFAT has facilitated the evacuation and repatriation of more than 26 000 Australians; the biggest consular operation in its history.

With an increasingly assertive China and a weaker America embroiled in internal discord and external competition, the deft management of Australia’s international relations is becoming ever more crucial. Diplomacy must be valued, and it must be funded accordingly. In 2008, US Secretary of Defense Robert Gates took the highly unusual step of publicly calling for the proper funding of US diplomacy and international development assistance. Attesting

to the need to properly value diplomacy and Australia's diplomats, Sir Angus Houston, former Chief of the Australian Defence Force and Lowy Institute Board member, cites Australia's response to the MH17 downing. As the prime minister's special envoy, Sir Angus relied heavily on the knowledge and expertise of Australia's highly-experienced diplomats on the ground. Their relationships with key players enabled access to the crash site and working with like-minded partners in securing an investigation.

In strategically uncertain times, Australia has rightly invested in its defence, expanding its capability with significant purchases of materiel and increasing its operating expenditure. But Australia's diplomacy must also be re-funded, and its diplomatic corps valued and strengthened. This requires more diplomats posted abroad, boosting numbers at small posts, adding posts where there are gaps, building teams everywhere else, and valuing their advice. This must not be done by reducing the teams at headquarters that provide leadership, strategic thinking, coordination, and regional expertise. The defence of Australia and the preservation of its prosperity requires the wielding of pen, word, and sword in better balance.



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