# Dragoman Digest.

**9.10.2020**

**Where are Australian companies investing overseas?**
*Proximity has not translated into a greater investment footprint in Asia*

The Australian Bureau of Statistics (ABS) has provided a picture of Australia's foreign direct investment through a survey of the 275 Australian parent enterprises with a controlling interest in Australian-owned foreign affiliates. Despite much talk of the opportunities provided by the 'Asian century', Australia's investment profile is still overwhelmingly Anglo-centric. The **US**, **UK**, **New Zealand** and **Canada** comprised four of the top five destinations for Australian-based companies. In the 15 years since the ABS last undertook such a survey, the top-five list has actually become increasingly Anglo, with Canada replacing **Malaysia**. Of the 5,176 Australian-owned foreign affiliates, approximately 22 percent have operations in Asia – a similar proportion to 2002-03. Of these, approximately half are Australian-based subsidiaries of multinational corporations.

While sales margins are higher in UK (28.4 percent) than Asia (13.2 percent), the latter figure is higher than the US (12.6 percent). Return on equity for Australian businesses in Asia was 6.7 percent, better than in the US (5.5 percent), or UK (5.8 percent). Asia undoubtedly poses unique risks, though superior returns are on offer for those who can manage these challenges effectively. As Asia's demographic profile and growth prospects becomes increasingly favourable over the Anglosphere, Australian companies risk missing out.

**Australian Federal Budget 2020**
*Coalition embraces big government recovery*

Unprecedented times call for unprecedented measures. Whilst the government has retained some of its traditional liberal economic ethos by bringing forward income tax cuts, it has embraced a Keynesian program of big government spending to resurrect **Australia's** downtrodden economy. Gone is any mention of the debt and deficit 'disaster' or 'back in black' rhetoric. Instead, the Government expects to spend a record A$677 billion or 35 percent of GDP this financial year. This is up from 27.7% last financial year and the previous record of 27.6% that occurred in 1984-5. With interest rates at a record low and the core tenets of monetary policy coming into question, fiscal policy increasingly appears to be taking precedence over monetary policy.

Politically, this makes for interesting times. Centre-right and conservative parties throughout the English-speaking world are gravitating away from their small government bearings as they attempt to appeal to disaffected, traditionally blue-collar constituencies and the aspirational working class. COVID19 has clearly exacerbated this trend. This has left centre-left parties in somewhat of a bind. Keen to avoid being outplayed at their own game, the clear temptation for centre-left parties is to attack the government for not spending enough. Opposition leader Anthony Albanese's budget reply focused on those that had 'missed out' in the budget. The electoral success of this strategy – and whether economics will continue to defy political stereotypes – remain to be seen.

**No easy way out for Argentina**
*Debt restructuring deal provides only temporary relief*

The depreciation of **Argentina's** newly created sovereign bonds suggests August's debt restructuring deal was merely a band-aid solution. The debt restructuring deal reduced

Argentina's debt payments by 27 percent and was expected to instill confidence in bond investors. Despite this, confidence has remained shaky and the bonds have fallen to near-default levels.

The growth rate of Argentina's COVID19 caseload is an additional headwind to investor confidence – Argentina is recording almost 15,000 cases per day. Argentina already recorded a second quarter GDP contraction of 19.1 percent. Government debt is projected to increase from 89 percent to 104 percent of GDP due to emergency social welfare programs. Inflation has hovered around 40 percent. A protracted recession would throw into question the long-term sustainability of Argentina's debt. President **Fernández**, paralysed by internal power struggles with his Vice President Cristina Kirchner, has failed to decide on a clear path of economic management.

There is much work to be done on Argentina's economic recovery. IMF talks are yet to come – with a deal not likely before March next year. Attracting investment and stimulating exports will be crucial to Argentina's economic stability as the country attempts to re-integrate itself back into the global economy. Private debt restructuring was thus necessary but not sufficient to ensure Argentina's sustainable economic future.

**A tale of two tracks**
*Contrary to popular perceptions, Japan is actually a larger investor in Southeast Asian infrastructure than China*

Compared to **China**'s much-hyped Belt and Road Initiative (BRI), **Japan**'s role in funding Southeast Asia's infrastructure gap has been somewhat understated – and often more successful. As of mid-last year, Japanese investment in Southeast Asia's six-largest economies was worth $US367 billion, far surpassing the value of Chinese-backed projects at $US255 billion – although it is worth mentioning that Chinese FDI has generally trended sharply upwards over the last decade.

The case-study of two different railway tracks in **Indonesia** is illuminating. In September 2015, a consortium of Chinese railroad companies won the rights to build Southeast Asia's first bullet train from Jakarta to Bandung. Speedy completion (in under four years) and the consortium requiring no state funds from Indonesia, made the Chinese bid particularly attractive. Fast-forward five years and the 142km track is only 56 percent complete. Local NGOs have accused the consortium of violating at least six local laws and causing considerable environmental damage. Doubts have also been raised about the project's economics.

The contrast to the Japan-backed 720km Jakarta-Surabaya project is considerable. Although more modest in only being a 'medium speed' train, the project – which uses mostly existing infrastructure – looks set to avoid the legal and environmental pitfalls of the Bandung line. In what appears to be a face-saving way of facilitating Japanese involvement in the Chinese-backed Bandung line, the Indonesian government in June proposed merging the two railway projects. With growing wariness over the BRI, Japan's track-record of delivering sustainable and quality infrastructure holds it in good stead to continue to compete with China.