

Australia's strategic hedging in the Indo-Pacific: a 'third way' beyond either China or the US

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Abstract

Australia's growing economic relations with Beijing in the past decade, in the midst of the rise of China, has sparked a continuing debate inside Australia about whether China is a friend or foe of Australia and accordingly about the premium that ought to be placed on the Australia-US security alliance. It has given rise to some assessments that Australia is now faced with a choice between China and the US. This paper, however, puts forward an argument that this binary choice is misplaced and that Canberra should avoid choosing one side at the expense of another. It makes the case that as a middle power, Australia should instead use 'strategic hedging', a combination of engagement and indirect/soft balancing strategy, to insure itself against the potential of China's regional domination amid uncertainty about US strategic commitment to the Asia-Pacific region. Australia should continue its economic engagement with China and maintain its robust political and military ties with the US while seeking the opportunity to broaden the breadth and depth of its relations with other regional states. The 2017 Australian Foreign Policy White Paper has, to a certain extent, implicitly adopted this hedging policy by promoting the use of a mixture of balancing and engagement strategies to counter China's regional domination. However, Australia's hedging policy has yet to reach its full potential and can currently be described as 'under-hedging', i.e., not doing enough to reduce uncertainty about the future and risk. While the Turnbull government (2015-2018) had showed a strong commitment to working with the US, Japan and India in building a 'free and open Indo-Pacific', and the Morrison government has maintained this commitment, the weakest links of Australia's hedging are in the failure to institutionalise the Quad, the informal strategic dialogue comprising Australia, the US, Japan and India, and to enmesh regional powers, notably India and Indonesia. Without enlisting more partners more firmly to its side, Australia is often sidelined by the other three members of the Quad and acts quite alone in the Indo-Pacific region.

‘As a sparsely settled continent on the edge of Asia, dependent on global markets for its prosperity and on distant allies for its security, Australia has faced as the central question of its foreign policy not whether it should engage actively with the world, but how it should do so’ (Gyngell, 2005: 99).

Introduction

Since the end of the Second World War, Australia has relied on the US as its security provider, and is regarded as a ‘dependent’ ally of the US in the Asia-Pacific (Bell, 1988). It is a member of the Five Eyes intelligence sharing arrangement as well as a staunch supporter of the Australia-New Zealand-United States security alliance (ANZUS). However, Australia’s ever-deepening economic ties with China in the midst of China’s ascendancy has caught it in between China and the US (Lieto, 2016). Increasing concerns about Chinese influence in Australia have sparked a continuing debate about whether China is a friend or foe and accordingly, about the premium that ought to be placed on the Australia-US security alliance.

Strategist Hugh White (2010) bluntly pointed out that Australia would almost certainly be faced with an unpleasant choice between its biggest trading partner (China) and its long-standing security provider (the US). A looming problem for Australia, White observed, was that while it hoped its economic relations with China would continue to grow, it simultaneously expected America to remain the strongest military power in the region and to maintain its commitment to serving as Australia’s ultimate protector. To achieve these twin goals, White urged Australian policymakers to act as a mediator between Beijing and Washington and nudge them into forging a power-sharing arrangement in the region. Since then, the debate about the role and position of Australia between the US and China has continued and intensified, noticeably among policymakers and in the academic and policy analysis circles within the country.

Some argue that Canberra has not had an independent China policy and should pursue one, establishing a greater policy autonomy from Washington. For example, Malcolm Fraser (2014), a former Liberal prime minister, pointed out that the Australia-US alliance embodies ‘dangerous’ strategic ties with Washington. Paul Keating, a former Labor prime minister, criticised Australia’s ‘tag-along

rights [to] foreign policy [with the US]’ and advised that ‘it’s time to cut the tag’ with American foreign policy as Australia cannot risk supporting the US at the expense of its trading relationship with China (Sales and Wearing, 2017). In academic circles, some also proclaim that China has ‘wooned Australia’ by ‘aggressively promoting the importance of China’s demand for natural resources to the Australian economy’ (Kurlantzick, 2007: 214). As the largest trading partner of Australia since 2007, China has made use of its economic and commercial ties to usurp a role previously held by the United States. As Ikenberry (2016) has observed, there is a ‘dual hierarchy’ in the Asia-Pacific region. Previously the US upheld both economic and political hierarchies. However, as the second largest economy of the world and the largest trading partner of many countries in the region, China is now dominating the economic hierarchy while the US can only take the helm of the security hierarchy. Australia’s economic relations with China ‘[have] generated a degree of alliance drift between Australia and the United States’ (Thomas, 2015: 846).

However, opposing views with respect to Australia’s choice between the two powers also abound. Some argue that Canberra needs to maintain its strong military and political relations with Washington and join American efforts to balance against China’s rise. The reason they proffer is that Australia shares the same values, i.e., a democratic political system, liberal economy and a commitment to the rule of law, with the US (Shearer, 2011). In analysing Australia’s response to a rising China, Manicom and O’Neil (2010: 23) reached the conclusion that ‘while there is some evidence of Australia accommodating Chinese strategic preferences in Asia, there is no indication that it is realigning itself strategically towards China and away from its long-standing ally, the US’. Tow (2012: 79) also observed that Sino-Australian relations ‘would not occur at the expense of the Australia-American relationship’. In describing the interrelationship between economic factors and alignment decisions, Reilly (2012: 393) sums up that in the Australian case, economic dependence and security alignment ‘are inversely related’ – ‘greater economic dependence encourages balancing behaviour’.

The lively debates on how Australia ought to manage its relationships with China and the US appear to have become more robust in the wake of the release of Australia’s 2017 Foreign Policy White Paper, the first such document since 2003. Not only does it

provide a broad blueprint on how Canberra should safeguard its national interests in terms of its economic prosperity and national security when the international environment is ever-changing, it specifies, more crucially, how Australia should respond to the rise of China, especially in light of allegations that China attempted to meddle in Australian domestic politics by funneling political donations to Australia's major political parties through Chinese business diaspora in the country (Cave, 2017a).

However, the above analyses are premised on the hidden yet mistaken belief that there is only a 'binary choice' – either China or the US – without any viable 'third way' or alternative available to Australian policymakers. In contrast, this paper asserts that there is an alternative to this binary choice: hedging.

What is hedging?

The term 'hedge' comes from investment and finance circles. The simplest explanation of hedging is 'insurance' – that is, insuring against a negative event or expected shortfall. In order to minimise exposure to various risks, investors seek the optimal hedging strategy to offset the risk of a negative event (Branger and Schlag, 2004). Buying homeowner's insurance is one example of a hedging strategy. Obviously hedging is not without its costs as, to use the homeowners insurance example, the hedger has to pay for the insurance to mitigate unexpected losses and uncertainty. It contains a speculative element and is motivated by a desire to protect from loss and to offset the risk of any negative event by using different instruments strategically (Johnson, 1960).

In the field of international relations, hedging can be broadly defined as a strategy composed of 'engagement and integration mechanisms' on the one hand, and 'realist-style balancing in the form of external security cooperation' on the other. Yet, the state which pursues strategic hedging does not 'openly [talk] about such hedging strategies per se, especially the security balancing' (Medeiros, 2005: 145). Australian National University academic Evelyn Goh adopts a similar but more rigorous definition of hedging, which she describes as 'a set of strategies

aimed at avoiding (or planning for contingencies in) a situation in which states cannot decide upon more straightforward alternatives such as balancing, bandwagoning, or neutrality.¹ Goh argues that states instead 'cultivate a middle position that forestalls or avoids having to choose one side at the obvious expense of another.' Using Southeast Asian states as case studies, Goh's research finds that the hedging policy adopted by these countries includes three major elements. It entails, first, indirect or soft balancing with the need to persuade the US to counter China's influence; second, engagement with China at various levels; and, third, involving regional powers to ensure a stable regional order (Goh, 2005: viii). She describes how a 'hedger' employs a mixture of balancing strategy in addition to engagement as '*insurance against the uncertain present and future intentions of target states*' (emphasis added). For her, hedging is a 'luxury of the relatively weak only' because great powers cannot lay claim to hedging strategy. Hedging should be used by a relatively weak state to adopt a middle position, a combination of engagement and indirect/non-specific (including soft) balancing, towards another state (Goh, 2006).

While the 2017 Australian Foreign Policy White Paper makes no mention of the word 'hedging', it is not hard, if the paper is deciphered carefully, to find that it aims to use a mixture of balancing and engagement strategies, echoing much of Medeiros' and Goh's descriptions about 'hedging' (Australian Government Department of Foreign Affairs and Trade, 2017a). More specifically, it attempts to insure its sovereignty and security against any formidable uncertainty. On the one hand, Canberra has cultivated economic engagement and partnership with China and the Association of Southeast Asian Nations (ASEAN). On the other hand, it simultaneously pursues strategic alliance with the US and informal alliance with other like-minded democratic countries such as via the Quadrilateral Security Dialogue (the 'Quad'). This forms a hedge against military threats from or domination by China, particularly in the South China Sea, through which trade worth US\$3,370 billion passed through in 2016 (Council on Foreign Relations, 2018), as well as a soft balancing against China's rise.

A successful hedging policy is required to insure Australia against negative future scenarios or unexpected shortfalls. This paper aims to analyse

1 While realists, such as Stephen Walt (1987), argue that the motivation for states to choose either bandwagoning or balancing is similar and they both have the same goal to achieve greater security, Schweller (1994) rebuts this argument and asserts that realists have overlooked the opportunistic aspect of bandwagoning. The motivation for bandwagoning is completely different from that for balancing. While balancing is purely driven by the desire to protect national security and always entails costs, bandwagoning is driven by the opportunity for gain and is often done voluntarily.

Australia's strategic hedging in the broader Indo-Pacific and argues that Australia has yet to reach its full potential. If one considers a hedging spectrum² in which to situate Australia with respect to its Indo-Pacific policy – ranging from 'under-hedging' to 'hedging' to 'over-hedging' – Australia's current hedging policy is 'under-hedging'. One may need to bear in mind the difficulties of crafting and implementing an optimal hedging policy. Although all accept that hedging as a risk management strategy is designed to reduce uncertainty about the future and risk, one may not be able to give a correct assessment of the level of risk involved. An analogy is that in purchasing an insurance policy, one may under-assess or over-assess the potential risk, giving rise to under-hedging (the gains from the offsetting investment being far below the loss) and over-hedging (paying excessive premium for a risk that rarely happens) respectively.

This paper proceeds in three steps to unfold Australia's hedging policy: (1) What are the negative scenarios that Australia seeks to hedge and insure against? (2) How can Australia hedge – what options are available for Australia? (3) How far has Australia pursued the hedging policy in successfully achieving both prosperity and security?

What to hedge and insure against?

Broadly speaking, there are three different scenarios Australia seeks to hedge and insure against. They are: (1) China's regional domination; (2) economic insecurity and downturn due to shrinkage in trade and investment; and (3) national security threats.

1. Insuring against China's regional domination

Australia's foremost concern is China's domination of the Asia-Pacific politically and militarily. Many policymakers in Australia have been pondering whether an undemocratic China, ruled by the Communist Party, can be restrained by international law, norms and rules. With newfound power, will China become a revisionist and expansionist state, posing an existential threat to Australia as well as regional peace and security? China's refusal to participate in the proceedings of the arbitral tribunal with regard

to the South China Sea territorial disputes with the Philippines and to accept tribunal's ruling against it in July 2016 was alarming.³ China's policy stances and preferences have been changing over the course of the growth of its material prowess. During the Third United Nations Conference on the Law of the Sea negotiations (1973-1982), China was a low-income developing state. It sided at the time with other coastal developing states in opposing a proposal from the more developed Japan and the Soviet Union that their 'historic rights' to the fishery resources in the waters of coastal states be preserved. Now as a much more powerful state, China paradoxically argues that it has 'historic rights' to living and non-living resources in what has become the exclusive economic zone (EEZ) of a coastal state in the South China Sea (Beckman, 2016: 179). Australia therefore cannot rule out the danger that China is not prepared to comply with international law if it is not to its liking or does not suit its prevailing interest. Regional peace and order may only be effectively preserved by a balance of power, as suggested by geostrategic analyst Brahma Chellaney (2018) among other neorealist thinkers. It is not in Australia's interests to jump on the bandwagon of China for economic gain without considering regional peace and security.⁴

In the security realm, Canberra takes a tough position towards the rise of China and reemphasises its security alliance with Washington. During a visit to Los Angeles in January 2017, then-Foreign Minister Julie Bishop called for 'more US leadership, not less' in the region (Wroe, 2017). To further align with Washington's call for a 'free and open Indo-Pacific' (FOIP), the 2017 Foreign Policy White Paper stressed the importance of the Australia-US strategic alliance for the region and calls for a 'rules-based' regional order. It states that 'our alliance with the US is critical to Australia's approach to the Indo-Pacific ... [t]oday, China is challenging America's position' (Australian Government, 2017). Overall, the White Paper calls for stronger engagement with the US in order to fend off security risks to Australia. One of the strategies to balance China's rising power in the Indo-Pacific is to ally with like-minded regional states, notably the United States, Japan, and India, in reactivating the Quad as a hedge against military threats from a rising

2 This term was inspired by Bob Carr, Director of the Australia-China Relations Institute (ACRI) at the University of Technology Sydney (UTS). My thanks go to Professor Carr and James Laurenceson, ACRI UTS Deputy Director, for pointing out this 'hedging spectrum' in our email correspondence.

3 See Permanent Court of Arbitration (PCA) case number 2013-19. The tribunal was constituted under Annex VII to the 1982 United Nations Convention on the Law of the Sea (UNCLOS) <<https://pca-cpa.org/wp-content/uploads/sites/175/2016/07/PH-CN-20160712-Award.pdf>> .

4 See Schweller (1994) for a classic study of bandwagoning in international relations, and note 1 above.

China, thereby maintaining peace and security in the South China Sea.⁵

The Quad was initially established in 2007. However, just a year after its establishment, Canberra withdrew from it in 2008 following the election of the Australian Labor Party, led by Kevin Rudd. Rudd took Canberra out of the Quad 1.0 arrangement for fear that the strategic alliance would adversely affect its economic relations with China (Shearer, 2017; Wyeth, 2017). Ironically, Australia's renewed interest in the Quad, resulting in Quad 2.0, is also largely due to China. The common perception across all four members is the potential challenge by a rising and more assertive China towards regional stability and the rules-based order (Carr, 2018). Concerns vis-à-vis China itself notwithstanding, the fear of China's domination of the Asia-Pacific also grows out of America's waning commitment to the region. As security analyst Euan Graham (2018: 4) has pointed out, the potential value of the Quad is 'in strategically tethering a more unpredictable, self-focused United States' and that Australia cannot afford 'to be squandered' from the Quad. In sum, while Australia's interest in the revival of the Quad is mainly due to China's growing assertiveness in recent years, it is simultaneously part of an attempt to keep America in the region in order to counter China's regional domination.

2. Insuring economic security and growth

Australia is seeking to insure against isolation from the major engines of economic growth in the Asia-Pacific or over-dependency on any single market. Australia has witnessed an influx of Chinese foreign direct investment into its mining and agricultural industries since 2005. China has been the primary source of Australia's economic growth in the past decade, being its largest export market since 2009. Since then, China has become Australia's indispensable trading partner, largely due to China's insatiable demand for mineral resources and agricultural products. In the past few years bilateral trade has also extended beyond merchandise goods

(i.e., grain, mineral resources) to services (tourism, education, finance and insurance, etc.).

Despite the global financial crisis of 2007-2008, Australia-China trade relations have continued to flourish. In 2016, Australia-China bilateral trade accounted for nearly one-third of Australia's total external trade. Nearly a third (32 percent) of Australia's total exports in 2018 went to China (Trading Economics). Both countries signed the China-Australia Free Trade Agreement (ChAFTA) in 2015, which entered into force later that same year. Since then, bilateral trade volume has surged rapidly, from A\$137 billion in 2015 to A\$165 billion in 2017, up 17 percent within two years (Australian Government Department of Foreign Affairs and Trade, 2018a: 90). Under ChAFTA, Australia is expected to benefit considerably from tariff cuts.⁶

However, there is ample evidence to show that China has used its economic ties with other countries as political leverage, retaliation or deterrence to pursue its national interests.⁷ Not too long ago, China has more than once used coercive economic statecraft after a spike in political tensions with Australia. For example in 2017 with China in mind, Australia reviewed its espionage laws and moved to ban foreign political donations. This triggered a diplomatic spat between Beijing and Canberra. In February 2018, after an accusation by then-Minister for International Development and the Pacific Concetta Fierravanti-Wells of China's infrastructure aid to the Pacific as 'white elephant' projects, China swiftly retaliated by issuing a safety warning to all Chinese students in Australia, posing a threat to Australia's A\$28 billion international education exports, of which Chinese students account for more than 31 percent (Smyth and Hancock, 2018).

In November 2018, China launched a year-long anti-dumping investigation into Australian barley, one of Australia's major export products. It was seen as one of its tit-for-tat strategies retaliating for Canberra's decision to expand its naval base on Manus Island in order to counter China's growing influence in the

5 The Quad originated in the 2004 Boxing Day tsunami along the coasts of most landmasses bordering the Indian Ocean, which caused immense damage. Four democratic powers – Australia, India, Japan and the United States – proposed an informal cooperation to offer military hardware and humanitarian relief to the affected areas (Shearer, 2017). This event highlighted the potential maritime cooperation between these four democratic states. Japan's Prime Minister, Shinzo Abe, in 2007 initiated the transformation of this informal alliance into a more strategic partnership with a desire to balance the rise of China. This four-way strategic dialogue, known as the 'Quad', was designed to preserve the common interests among them. The Australian government also signed a Joint Declaration on Security Cooperation with Japan that year.

6 Under ChAFTA, China's tariff for products of Australian origin is eliminated on the day of entry into force or uses the tariff rate in 2013 as a 'base rate' to gradually lower the percentage and that will be eventually reduced to zero (Australian Government Department of Foreign Affairs and Trade, 2016a: 6).

7 For example, Lai (2018) uses China's economic sanctions towards North Korea, Japan, the Philippines and Norway as cases to examine China's coercive diplomacy; and Zhou & Zhang (2017) look at how China uses anti-dumping measures as a way of protection, retaliation, industrial development and export promotion.

region (Lockett, 2018). Under ChAFTA, China pledged to eliminate the tariffs on barley from Australia and, as such, more than 67 percent of Australia's barley is exported to China, accounting for A\$1.2 billion annually (Lockett, 2018; Australian Export Grains Innovation Centre, (no publication date)). In light of China's practice of economic coercion in responding to any diplomatic row, Australia should insure itself against external economic coercion in order to reduce its economic dependency on China and to protect its economic growth.

3. Insuring its national security

As mentioned earlier, Australia has relied on the US as the security provider for a long time. However, Australia may view with equal scepticism US current policy to the region. What will happen if the US withdraws part of its security commitment under Trump's 'American First' policy? Staying aloof from the world had long been a defining feature of US foreign policy until World War II (Rose, 2019). In light of the strained relations between the US under the Trump administration and its traditional allies in Europe, Australia must not be complacent about American sustained engagement and alignment with its post-war partners in Asia. In addition, Australia has to be mindful of the ideological proclivities of Trump. He (and John Bolton, his current National Security Adviser) have a strong aversion to multilateralism. His administration has declared withdrawal from several international agreements, including the Trans-Pacific Partnership (TPP), the Paris climate agreement, the Iran nuclear deal (formally known as the Joint Comprehensive Plan of Action) and the Intermediate-Range Nuclear Forces Treaty of 1987. Trump has been critical of international institutions such as the United Nations (UN), the World Trade Organisation, the European Union and the North Atlantic Treaty Organisation.⁸ In addition, there are signs that Trump himself is not interested in Asian affairs. He has not taken part in the East Asia Summit (EAS) since November 2017 and also skipped the Asia-Pacific Economic Cooperation (APEC) meeting in Papua New Guinea in November 2018 (Mahtani, 2018).⁹

Last but not least, Australian political leaders may need to be concerned about Trump's transactional

approach to foreign policy, as clearly shown in the murder of Saudi dissident and *Washington Post* columnist Jamal Khashoggi in 2018. Trump has refused to confront Saudi Arabia, particularly its Crown Prince, Mohammed bin Salman, because of his concerns over job losses in the US military industry sector and Iranian influence in the Middle East. He would not be prepared to harm US-Saudi relations if Saudi Arabia in return took action to press down the oil price (Hohmann, 2018; Mazzetti & Hubbard, 2018). As early as 2016, during his presidential campaign, Trump explicitly indicated that other countries had to pay the US for security protection. Asian countries, particularly those that have heavily relied on the US for security protection, started to harbour doubts about the reliability of the US commitment as a counterbalance to China (and North Korea) in the region. South Korea and the US were once at loggerheads over the Korean share of the cost of stationing 28,500 American troops on the Korean soil. In the five-year (2014-2018) agreement about cost sharing, South Korea paid ₩960 billion (US\$848 million). The Trump administration asked the South Korean government to increase its contribution by 50 percent to more than ₩1.4 trillion while Seoul did not want to commit more than ₩1 trillion (Korea JoongAng Daily, 2019; Shin, 2019). Eventually in February 2019 they reached a short-term deal for a year only in which South Korea would pay ₩1.04-1.05 trillion (US\$925-930 million) (Choe, 2019; Song, 2019). Trump has demonstrated in the cases mentioned above his reluctance to take up the global responsibility for preserving the liberal international order, including the protection of human rights and democratic values. For him and his supporters, it is too costly for the US to play the role of the sole global hegemon maintaining the liberal international order. Australia cannot therefore take his rhetorical commitments to East Asian security and the Quad for granted, and must be prepared to invest in institution-building in the region jointly with other like-minded states and to demonstrate its strategic utility to the region in order to make a 'deal' with the US to persuade it to remain.

One may ask whether a president following Trump would lessen the need for a hedging foreign policy. This is probably unlikely because a bipartisan consensus on a hardened China policy has taken

⁸ The US, under the Trump administration, announced its withdrawal from the UN Educational, Science and Cultural Organisation (UNESCO) in October 2017 and from the UN Human Rights Council in June 2018. See also Trump's speech to the UN General Assembly in September 2018 in which he stated that his government rejects globalism: <https://news.un.org/en/story/2018/09/1020472>.

⁹ The year 2018 is the second consecutive year that Trump has skipped the East Asia Summit. In November 2017, Trump toured five states in Asia in 12 days. The last stop was in Manila, the Philippines where he was then supposed to attend the East Asia Summit. However, he left Manila a few hours earlier than planned and skipped the East Asia Summit on November 14 2017 (Reuters, Associated Press 2017).

shape at the national level in the American polity. The emergence of this national, bipartisan consensus is less due to Trump's policy preferences and personality than to the growing perception in both Democratic and Republican national leaders that a non-democratic China is posing imminent threat to US security, as shown in the alleged 'technology theft', espionage (discussed further below), massive acquisition of Western technology firms, China's military modernisation and its militarisation of the disputed (artificial) islands in the South China Sea, China's leadership in the creation of new international institutions (such as the Asian Infrastructure Investment Bank (AIIB)) and the Belt and Road Initiative (BRI),¹⁰ and the strengthening of Xi's dictatorial leadership of the Chinese Communist Party and the state¹¹ (Shambaugh, 2018; Leung and Depp, 2019). A Democratic US president may be more receptive to a multilateral approach to handling the 'China threat' but is unlikely to soften US policy towards China. More importantly, irrespective of who is US President, s/he will not change China's policy preference and behaviour.

It therefore makes sense for Australia, as a middle power, to use a combination of engagement and indirect/soft balancing strategy to insure itself against both economic downturn and dependency, and China's regional domination, in light of the uncertainties about Chinese intent in and US strategic commitment to the region. In practical terms, Australia should continue engaging with China and other regional states in multilateral trade and investment; but it is simultaneously sensible for it to strengthen partnerships with regional states and the US to counter-balance China indirectly and softly in the security realm.

How to hedge: Australia's hedging options

How can Australia hedge against the aforementioned potential negativities in the Indo-Pacific region in order to insure its economic and national securities? What options are available for Australia? The hedging options can be divided into three groups, namely (1) engaging China economically; (2) keeping the US on board; and (3) involving regional powers such

as ASEAN, India and Japan. The last two may be conceived of as the key elements of a soft-balancing policy.

1. Engaging China economically

Engagement is in the interests of both Canberra and Beijing. Figure 1 shows that China is currently the largest trading partner for Australia. Their two-way trade reached A\$183 billion in 2017, of which Australia enjoyed a huge trade surplus with China. Australia's total trade with China was also much higher than that with its second largest trading partner, Japan (nearly A\$72 billion), by more than A\$111 billion. As previously mentioned, China has been Australia's top trading partner since 2007. Although Canberra declined to endorse Beijing's proposal to align and link Australia's A\$5 billion Northern Australia Infrastructure Facility to China's BRI, both countries did sign a memorandum of understanding (MOU) on cooperation in investment and infrastructure in third countries during Chinese Premier Li Keqiang's visit to Australia in March 2017.

However there is also a growing concern over China's acquisitions of Australia's land and major infrastructure in the country. The decision of the Northern Territory government to lease part of the Port of Darwin to Landbridge Group, a Chinese company, for 99 years, in 2015, sparked a heated debate about that deal. The Australian Strategic Policy Institute (ASPI), a think tank based in Canberra and set up by the government, slammed this transaction, arguing that it was 'a strategic risk for Australia' and that the government should reconsider 'how Australia deals with the national security implications of foreign investment proposals' (Barnes et al., 2015). ASPI alleges that Landbridge is well connected with China's military and the lease will potentially allow the Chinese government to spy on American marines based in Darwin (Barnes et al., 2015; Forsythe, 2015).¹² However, the link between Landbridge and China's military has not been confirmed. It was Landbridge, according to *The Australian Financial Review*, which wanted use the acquisition to build ties with the Chinese government 'rather than Landbridge being a cog in Beijing's strategic ambitions at the time it purchased' (Grigg,

¹⁰ Note that *both* the Obama and Trump administrations share in not signing up to the AIIB and not endorsing the BRI.

¹¹ China's legislature, the National People's Congress, made a constitutional amendment in March 2018 that scraps the two-term limit on the country's presidency, effectively allowing the incumbent Xi Jinping to rule the country for life (Buckley and Myers, 2018).

¹² Under the 'strategic rebalance to Asia' policy undertaken by the Obama administration, Canberra and Washington agreed to deploy 2,500 US Marines to Darwin in 2011 and both countries have since then been running joint military exercises in Darwin.

2017).¹³ In addition, the Australian Department of Defence also stated that there were no defence or strategic grounds for opposing Landbridge’s bid for the Port of Darwin. Julie Bishop, then the Foreign Minister, also aligned with the Defence Department, reiterating that the government had ‘no security concerns’ about the Landbridge investment (Bishop, 2018; and Laurenceson, 2018: 73).

Nevertheless, since the Landbridge acquisition of the Port of Darwin, there have been growing concerns over increasing Chinese influence. Australia has often used a ‘one-size-fits-all’ policy to block all high-profile Chinese investment in Australia, including in the electricity company Ausgrid, in the beef producer S. Kidman & Co (which ultimately received approval to sell its 10 million-hectare farm to Australian mining magnate Gina Rinehart and a Chinese company in 2016, with the Chinese company taking a one-third minority stake), and in the exclusion of Huawei and ZTE from involvement in Australia’s 5G mobile network in 2018. While this paper asserts that Canberra should be more vigilant about China’s investment, especially in relation to

investment from Chinese state-owned or controlled enterprises (SOEs/SCEs) (see pp. 10-11 on state capitalism), it should consider Chinese investment case by case, rather than use a broad-brush approach. Economic engagement with China should remain one of the core strategies of Australia’s hedging policy.

2. Keeping the US on board

Australia, as a liberal democratic, Western country, still remains closer politically and ideologically to the US than to China. However, it is simultaneously concerned about Trump’s abdication of US global leadership. Not only Australians, but also many people in the world do not believe that the US now has the qualities a global leader should have. According to an extensive survey conducted by Gallup in 134 countries around the globe in 2018, the approval of American leadership has substantially dropped by nearly 20 percent in less than one year after Trump took over the office from Obama in early 2017 (Baker, 2018).

¹³ Accordingly it was the chief executive of Landbridge, Ye Cheng, who tried to bring the port to join China’s BRI after the acquisition in the hope of accessing cheap funding from the Chinese government (Grigg, 2017).

Table 1. Australia’s top 10 trading partners in 2017 (Unit: A\$ million)

Country	Exports	Imports	Total bilateral trade
China	115,996	67,397	183,393
Japan	47,240	24,612	71,852
United States	20,972	47,491	68,463
Republic of Korea	23,366	31,930	55,296
India	20,160	7,276	27,435
New Zealand	14,036	13,396	27,433
United Kingdom	11,536	15,092	26,628
Singapore	11,961	13,413	25,374
Thailand	5,781	17,238	23,019
Germany	4,046	16,694	20,739

Source: Australian Government Department of Foreign Affairs and Trade (2018)

While currently China cannot dominate the region militarily unless the US lets it do so, Australia should not stand idly by and wait for the US to lead. Rather, it should have a more independent and more proactive foreign policy. From a historical perspective, Australia has not had any war with China – whereas India, Japan and the US have – and so it would be in a better position to play a leadership role in the region. The essence of hedging espoused in this study is not to choose between China and the US (a binary choice) but to bring more partners to the side of Australia. To achieve this, Australia should formalise the Quad, ally with other like-minded democracies to strengthen its diplomatic and military capacity to counter China’s domination and assertiveness, and develop a more independent yet multilateral foreign policy. Simultaneously, it can also strengthen its bilateral relations with other regional powers including other Quad members, while keeping the US on board.

Multilateral arrangement: A more formalised Quad

Multilaterally Australia may ponder leading the institutionalisation of the Quad, with its Secretariat stationed in Canberra, to make it less ad hoc and more functional, and to make the new notion of the Indo-Pacific operational at policy level.

In his proposal of a concert of Indo-Pacific democracies, Brahma Chellaney (2018) suggests that Japan and India should be the cornerstone of efforts to ‘institutionalise’ the Quad initiative. But on how they should conceptualise the institutionalisation, Chellaney provides few details. So far all four countries of the Quad have only managed to rhetorically emphasise the importance of their cooperation for protecting the freedom of navigation and maintaining a rules-based order in the Indo-Pacific. However, there is not much substance in this rhetorical sloganeering. It is also argued that ‘[the four countries of the Quad] tend to say what the Quad is not rather than what it is’ (Curran, 2018). Japanese Prime Minister Shinzo Abe emphasised that all four countries of the Quad ‘share strategic values’; however, he at the same time pointed out that the revival of the Quad ‘does not mean necessarily engaging in any military activities’ (Stutchbury and Grigg, 2018). This ambiguity is perhaps largely because it was only revived in November 2017 with Australia’s return to it and still remains an informal grouping.

Thus far, the revived Quad has yet to hold any joint exercises in the name of protecting freedom

of navigation (Grossman, 2018b). In view of the ambiguity and the overall perception of waning US commitment to Asia, US Vice President Mike Pence tried to reaffirm Asian countries of US commitment to the region and clarify the importance of the Indo-Pacific to Washington’s foreign policy. Before his tour of Asia, in which he represented the US in lieu of Trump in the ASEAN summit and APEC in November 2018, Pence elaborated that Washington’s Indo-Pacific strategy rests on three broad pillars: economic prosperity, security and the rule of law (Pence, 2018). In the security realm, the US will continue to work with like-minded states to confront threats facing the region. Trump’s US\$60 billion infrastructure fund is one of the measures to counter China’s economic and security influence (Pence, 2018). Amid rising anxiety about China’s infrastructure development in the Asia-Pacific region, Washington created a new development agency – the US International Development Finance Corporation (USIDFC) in early 2018. In addition to the government’s US\$113 million direct investment, USIDFC will raise its spending cap to US\$60 billion by crowding-in-private investment. It will allow American companies to compete overseas and create a ‘preference’ for US investors (Kuo, 2018). According to two analysts at the Center for Strategic and International Studies think tank, this new USIDFC is ‘absolutely ... a response to the challenge of China’ (Runde and Bandura, 2018: 4). US Secretary of State Mike Pompeo also indicated at the Indo-Pacific Business Forum in Washington in July 2018 that this initiative would involve a trilateral investment agreement among the US, Japan and Australia (Shi and Churchill, 2018).

Despite Pence’s assurance about US commitment to the region, Canberra should not solely rely on the US to act for its security protection. During a major speech at the German Marshall Fund in Brussels in December 2018, Pompeo not only criticized the UN and its agencies, but also questioned the value of multilateralism. According to him, based on ‘principled realism’, every nation must consider its responsibilities to its citizens and make sure that the ‘international order serves the good of its people’ (Pompeo, 2018). In other words, multilateralism must work for Americans in order for the US to support. By the same reasoning, we have to be mindful that the Quad must benefit the US in order for Washington to lend support for it.

To ensure that the Quad will not dissolve again, Australia should take the lead and try to make

the Quad more functional and make the notion operational at policy level. Setting up a secretariat in Canberra and upgrading the Quad's activities to ministerial level consultations are two viable options to institutionalize the Quad. Ultimately, it was Australia that pulled the plug on Quad 1.0 a decade ago, and was thus deemed to be one of the two weaker links (together with India) among all four countries (Graham, 2018: 5). To shed the negative image that Canberra might get cold feet and to affirm Canberra's long-term, strong commitment to this informal alliance, Australia needs to be more proactive in initiating a formal agreement among the members of the Quad. Therefore, instead of leaving it as a loose, informal setting, a more formalised and institutionalised Quad could serve as an enabler to strengthen security cooperation among four like-minded states under the framework of Indo-Pacific geographical concept (Singh, 2018). By doing so, the Quad could engage in more military exercises and should strive to put the Malabar naval exercises within its orbit.

Aligning with the US: Vigilance on state capitalism

We have witnessed the growing involvement of China's enterprises in infrastructure development spanning from Africa to the countries along the current BRI. Due to the growing concern over Chinese investment and the 'grab' of Australia's properties, the government released the figure of foreign owners of agricultural land in Australia in 2016. It indicated that 13.6 percent of Australian agricultural land was owned by or leased to foreign companies. However, China is by far not the biggest investor. It is the United Kingdom which holds 52 percent of agricultural land held by foreign investors, followed by the US, the Netherlands, and Singapore. Comparatively, Chinese investors only hold 0.38 per cent of Australia's agricultural land (Farr, 2016). At issue is why attention has been focused on Chinese investment and why it is that mostly Chinese companies are facing scrutiny. One of the reasons is that most of the Chinese companies are state-owned or -controlled enterprises (SOEs/SCEs). For example, on the 2018 Fortune Global 500 list, a ranking of the 500 largest global corporations based on revenue, 120 are Chinese companies. The number of Chinese companies on the list is second only to the United States with 126 companies. If 2018's figure is compared with previous years', China's achievement

is remarkable. In 2000 only 10 Chinese companies managed to be on the list; 10 years later in 2010, there were 46 Chinese companies (Cendrowski, 2015). The majority of the Chinese firms on the list are SOEs/SCEs, directly or indirectly controlled by the central government via the State-owned Assets and Supervision and Administration Commission (SASAC).

As the nexus between government and corporations is shaped top-down by the Chinese government, SOEs/SCEs are allegedly an important instrument of the Chinese authorities for achieving the state's economic and strategic objectives. Due to the state-controlled and strategic nature of Chinese investment, the US has led the calls for greater scrutiny of Chinese investment in the West. Huawei is a case in point.

Huawei is the world's largest supplier of telecommunications network equipment. While it claims that it is not a state-owned but an employee-owned enterprise, it is regarded as a 'state-controlled enterprise' (Wyeth, 2018).¹⁴ Many Western countries are concerned over the background of Huawei's founder, Ren Zhengfei, who was an engineer in the People's Liberation Army (PLA) in 1974-83. Its mysterious ownership structure, fuelled by the claim that Ren holds only a one percent stake in Huawei, further causes suspicions that the company is de facto run by the Chinese authorities behind the scenes and that its overseas 'commercial' investment is a cover for espionage (Davies, 2018). It is also suspected that Huawei's equipment may contain 'back doors' for use by Chinese intelligence officials. This security concern is further stoked by Chinese legislation which requires domestic firms to assist China when they are asked to (Weber, 2018). The retaliatory action taken by the Chinese government against Canadians in China in response to the arrest of Huawei's Chief Financial Officer Meng Wanzhou, the daughter of Ren, by Canadian authorities on suspicion of violating US trade sanctions against Iran deepens the speculation that Huawei is not a genuine private enterprise in China (Magnus, 2018). John McCallum, Canada's ambassador to China, revealed in January 2019 that Xi had been angered over the Meng's arrest and speculated that it might be because Huawei is 'a national flagship company of China,' 'not just any company' (Gilles, 2019).

¹⁴ Key to Chinese enterprises is not who nominally 'owns' the enterprises, but who has the right to use the property of the firms, who has the right to earn income from the property and who has the right to transfer the property to others. In state-owned or -controlled enterprises, it is always party-state cadres rather than the nominal owners hold the rights. In other words, all major decisions are made by cadres.

In 2008, Australia tightened its foreign direct investment (FDI) regime as a defensive move that targets Chinese investors mainly (Wilson, 2011). In August 2018, Chinese enterprises Huawei and ZTE were blocked from being involved in the building of Australia's 5G mobile network. Its bid for Australia's 5G network was considered posing a risk towards Australia's national security. In a joint media release in August 2018, Communications Minister Mitch Fifield and then-Treasurer Scott Morrison indicated, without directly naming the Chinese firms, that 'the involvement of vendors who are likely to be *subject to extrajudicial directions from a foreign government*' (emphasis added) would pose a security risk for Australia (Wyeth, 2018; Fifield, 2018).

Led by the US, liberal democratic countries have made a common approach to investment from Huawei and ZTE. As early as 2011, the House Permanent Select Committee on Intelligence under the US House of Representatives (the Intelligence Committee) initiated an investigation into the potential threat Huawei and ZTE would pose to US national security. The Intelligence Committee concluded in its 2012 report that although there was no conclusive evidence of wrongdoings of Huawei and ZTE, there were significant knowledge gaps about the 'companies' potential ties to the Chinese state'. The report also highlighted the 'potential security threat posed by Chinese telecommunications companies. It therefore recommended that the government 'block acquisitions, takeovers, or mergers involving Huawei and ZTE' on US soil (US House of Representatives, 2012). Since then, the US has tried to lobby its strategic partners, including the members of Five Eyes and Germany, Japan and India to block Huawei and ZTE from providing 5G equipment to their countries.

Among the Five Eyes, both Australia and New Zealand followed the US advice and in 2018 blocked Huawei's and ZTE's 5G bid on the grounds of national security (Smyth and White, 2018b). While preparing for its auction in 2019, the UK has also toughened its stance on Huawei. Its National Cyber Security Centre (NCSC) explicitly expressed concerns over a range of technical issues that would pose 'new risks in UK telecommunications networks' (Kynge et al., 2018) and requested the company to make a series of technical changes to its practices in the UK, which would cost Huawei US\$2 billion (Bond and Fildes, 2018). Together with the Department for Digital, Culture, Media and Sport, the NCSC warned several UK telecoms companies of the need to consider their

suppliers carefully when building 5G networks (Fildes, 2018). Although Canada has not barred Huawei from participating in the development of Canada's 5G mobile network, the Canadian government has applied numerous restrictions on how the company can operate in the country: for example, not being permitted to bid on federal contracts, nor to manage equipment from offshore locations, nor to bid on the core networks of Canada's telecommunications companies (Nossal, 2018).

India has also followed US move to exclude Huawei and ZTE from taking part in its 5G network in the country (Reichert, 2018) while Japan is simultaneously considering a ban on these two companies (Burton, 2018). In Germany, concerns over Huawei's potential involvement in building the country's 5G network are also gathering traction. While Germany has yet to demonstrate a firm position towards Huawei, 'the US influence on this has really intensified recently', as an anonymous German official pointed out (Kynge et al., 2018).

Not only does the US lobby its strategic partners against investment by Huawei and ZTE, it has also established a trilateral partnership with Japan and Australia in providing infrastructure and development assistance in the Indo-Pacific region in order to push back China's growing influence in the region. The Pacific countries were the first to find themselves at the centre of this great power wrestle over their infrastructure development. After effectively providing a counter offer to the Solomon Islands and stopping Huawei from building a 4,000km-long seabed cable from Sydney to the Solomon Islands in June 2018, Australia (together with the US and Japan) tried to make another similar counter offer to Papua New Guinea (PNG) in the same year (Smyth and White, 2018a). However, unlike the Solomon Islands, PNG refused the joint offer and upheld its original deal with Huawei in building the country's internet infrastructure project (Westbrook, 2018).

Australia's continued participation in the Five Eyes is premised on the confidence the rest four have in sharing secret and sensitive intelligence reports with it over the Internet. As US policy preferences in cybersecurity and cyber-threats are unambiguously expressed, Australia does not have much policy freedom but to align its policy towards China's state capitalism and its enterprises with other like-minded countries in the West, notably the US.

3. Involving regional powers

Another strategic hedging measure to insure Australia's security against any uncertainties is to broaden the breadth and depth of its relations with other regional actors, including Japan and the Republic of Korea in Northeast Asia, ASEAN and its member states – Indonesia in particular – in Southeast Asia and India in South Asia, in addition to a more formalised Quad. To insure against China's domination which arises not only from the spectacular growth of China's hard power and naval modernization but also from the unpredictability of the Trump administration, Australia should bargain and engage with China from a position of strength. This can be achieved by strengthening its economic and security ties with neighbouring countries. We may need to note that many Chinese officials and diplomats are strong adherents to neorealism, believing that only power matters in international politics. They show little respect for weakness. To employ a Thucydidean observation, they act in the belief that 'the strong do what they can, and the weak suffer what they must.' Kowtowing and making concessions to Beijing will not serve Canberra's long-term national interest. The US, India and Japan defy China in varying degrees. Both India and Japan have not formally endorsed China's BRI and have territorial disputes with it. But China still feels compelled to engage them because, among others, of the need to attract Japanese foreign investment and of India's military prowess (it itself has nuclear weapons) and its role in the Shanghai Cooperation Organization (SCO), the BRICS grouping, G20 as well as the developing world (the non-aligned movement).

The Quad may facilitate the enhancement of mutual ties between Quad states or even trilateral relations among Australia, India and Japan. This could serve as a strategic outreach for Canberra to further deepen its relations with New Delhi and Tokyo. Japan has proactively deepened its relations with several regional powers. Abe's effort and strategic outreach has made Australia¹⁵, Canada¹⁶ and potentially India¹⁷ sign the Acquisition and Cross-Servicing Agreement

(ACSA) with Japan. Japan is well aware that it can no longer afford to rely heavily on the US for security and defence. Japan's delicate balancing act is that it is skillfully mingling with China while allying with other regional powers to counter China's rising influence. For example, the day after a bilateral meeting with Xi Jinping in Beijing, Abe and Modi held their 11th bilateral talks in Japan (Japan Times, 2018).

Working with other regional powers is one of the means for Australia to make it diplomatically stronger than it is right now. Instead of heavy reliance on US security protection, Australia should follow the example of Japan. It makes sense for Australia to deepen its strategic partnership or political alignments with both India and Japan, to build up a more independent foreign policy, and strengthen its bilateral relations with ASEAN countries, particularly with Indonesia (this is discussed further in the next section).

Economically, while China remains Australia's top trading partner, it makes good sense for Australia to diversify its economic engagement beyond China with other countries, such as members of the Regional Comprehensive Economic Partnership (RCEP) and the TPP-11, to soft-balance against China's economic domination. RCEP and the TPP-11 are two elements of the economic soft balancing strategy against any pitfalls of an over-reliance on a single market. The RCEP consists of 16 member countries, namely the 10 member states of ASEAN and six of ASEAN's free trade agreement partners (Australia, China, India, Japan, Korea and New Zealand). RCEP accounts for almost half of the world's population, 31.6 percent of global GDP and 45 percent of global economic growth in 2015 (Australian Government Department of Foreign Affairs and Trade, 2018b). Australia is currently moving in the right direction in this respect.

In addition, Canberra has gone to great lengths to keep the TPP alive and uses it to soft-balance against China's overwhelming dominance over the regional economy. The 12-country TPP was reportedly

15 Australia and Japan signed their ACSA in 2013 and a new ACSA in 2017 in light of Japan's new security legislation that expanded the role of its Self Defense Force in early 2017. Under the ACSA, both countries set out the basic terms and conditions for reciprocal provision of supplies and logistical support between the Australian Defence Force and the Japanese Self-Defence Forces; (see: https://www.apf.gov.au/Parliamentary_Business/Committees/Joint/Completed_Inquiries/jsct/16november2010/report2/chapter2).

16 Canada and Japan signed the ACSA in April 2018.

17 India and Japan have been expanding their military and political cooperation swiftly. The two countries have held bilateral maritime exercises and joint army exercises. Japan was also invited to be a permanent member of the Malabar exercises involving the US navy (Pant, 2018). Their strategic partnership has also enabled the two countries to ally in funding infrastructure projects. They jointly set up the Asia-Africa Growth Corridor (AAGC) to finance developing countries' infrastructural investment to counter China's BRI. AAGC, which aims to link Africa with India, Bangladesh, Myanmar, Cambodia and Laos together by sea route, was proposed by both Japan and India during the annual meeting of the African Development Bank, held in Gujarat, India in May 2017 (Nair, 2017).

the largest pact governing international commerce, encompassing 40 percent of the world's economic output. It was deemed to be a key component of Obama's 'pivot to Asia' policy in countering China's regional economic dominance. In January 2017, however, the Trump administration decided to pull America out of the pact and as a result, it became the TPP-11.¹⁸ Despite the absence of the world's biggest economy, Australia, together with Japan and New Zealand, led the charge in reviving the TPP. Trade ministers of the 11 remaining TPP countries met in Hanoi, Vietnam in May and again in November 2017 in Danang, Vietnam. In March 2018, a Comprehensive and Progressive Agreement for TPP was signed in Santiago, Chile; and this agreement entered into force in December after Australia, the sixth country of the group, ratified the agreement domestically in October 2018 (Panda, 2018b). The TPP-11 has yet to have any intention to invite China to join the multilateral trade pact but the door is said to be open for the US to re-join it anytime (Murdoch, 2017).

Has Australia hedged successfully so far?

Against the hedging options mentioned above, this section aims to evaluate how far Australia has succeeded in taking up a strategic hedging policy to achieve both security and prosperity. Hedging is not without cost. One may theoretically buy insurance policies to cover everything and every possible scenario but in reality few do so. The key question is which package is the optimal, risk-minimising policy to offset the likely negative scenarios. Would it be under-hedging or over-hedging?

On institutionalising the Quad: Since its revival in 2017, the Quad has become more proactive than a decade ago and held three different meetings within one year, focusing broadly on Indo-Pacific security and a 'free and open' region. The latest one was held in Singapore in November 2018 during Pence's visit for the ASEAN summit (Haidar, 2018). A new spatial term, the 'Indo-Pacific', has also replaced 'Asia-Pacific' as the new lexicon in policy circles among the four countries. In May 2018, the US military also announced that its Pacific Command was renamed

the Indo-Pacific Command (Ali, 2018). Prior to the name change of the US Pacific Command, Australia quietly renamed the 'Asia-Pacific Group' in its Department of Foreign Affairs and Trade (DFAT) the 'Indo-Pacific Group' in 2017.¹⁹ Australia under the Turnbull government (2015-2018) and the current Morrison government (2018-) has shown a strong commitment to working with the other three Quad members to build a FOIP. This is also due to the strategic environment in which all of them are maritime powers with stakes in the Indo-Pacific. Even the Labor Party which decided to withdraw from the Quad in 2008 now recognises its security value (Brewster and Medcalf, 2018).

However, the establishment of a formalised Quad institution is still a distant goal. All three Quad 2.0 meetings occurred on the sidelines of international meetings, such as APEC and the EAS, and they were limited at the assistant-secretary level. The meetings have been labelled 'US-Australia-India-Japan Consultations', rather than 'Quadrilateral Security Dialogue', which had been used in 2007 (Ayres, 2018; US Department of State, 2018). In addition, Australia's political instability has likely undermined Canberra's credibility at the international stage. Australia did not participate in the trilateral meeting among the other three Quad leaders during the G20 leaders' summit in Buenos Aires, Argentina in December 2018. This India-Japan-US trilateral meeting served as a symbolic movement to demonstrate the three countries' common interests in the Indo-Pacific (Panda, 2018a). One has to wonder why Australia was absent from or not invited to it, considering that it has been painstakingly constructing a FOIP among all four like-minded states. One may attribute it to the result of federal government changing hands frequently, with six prime ministers within 10 years, largely due to 'political coups' within their own political parties. It is hard for other countries' leaders to acquaint themselves with Australia's 'current' prime minister and to make deals with them.²⁰ Talking seriously with Canberra and making concessions to it would likely be a waste of time and effort. Canberra has to end this 'coup culture' in order to maintain its international image of stability and to ensure political leaders of other states to have

18 The TPP-11 members are Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam.

19 For the organisational chart of DFAT, see: <https://dfat.gov.au/about-us/department/Documents/dfat-org-chart-executive.pdf>. The Indo-Pacific Group was allegedly created after DFAT published its 2017 Foreign Policy White Paper. Personal conversation with Ian Hall of Griffith University in March 2018.

20 Three months since becoming Australia's Prime Minister, Scott Morrison met with the German Chancellor, Angela Merkel during the G20 summit in Buenos Aires, Argentina in December 2018. Merkel was seen to rely on a 'cheat sheet' to familiarise herself with the new Australian Prime Minister sitting next to her during their one-on-one meeting. Merkel's 'ignorance' of Morrison was interpreted as that she 'simply couldn't be bothered' as there might 'be another one along in a minute' (Wintour, 2018).

confidence in Australia's foreign policy standing and its consistency.

Another sign that Australia is not fully recognised as a Quad member state is that the four countries have yet to hold any joint naval exercises so far, despite their joint proclamation to preserve a FOIP. Since 2015, Canberra has been lobbying for inclusion in the Malabar annual naval exercises but has so far been excluded from it by India. Shortly after the Wuhan summit between Chinese President Xi Jinping and Indian Prime Minister Narendra Modi in April 2018, India decided that the 2018 Malabar naval exercises would remain a trilateral matter without Australian participation. Although it was widely interpreted as a concession made by India to China to allay China's security concerns over the emergence of an 'anti-China' military alliance, there were other grounds for India's rejection. They include: the lack of trust on the part of India in Australia's long-term commitments to the Quad; Australia's support for Pakistan in the Financial Action Task Force discussions; and Australia's refusal to share the over-the-horizon radar technology with India (Grossman, 2018a; Sundaramurthy, 2018).

In order to persuade India to include Australia in the Malabar naval exercises, Australia may need to allay India's lingering concern over whether Australia will withdraw from it again later. Canberra's leadership in formalising and institutionalising the Quad will contribute to rebuilding of trust between Australia and India by demonstrating its long-term commitment to the institution. Canberra might consider 'reminding' New Delhi of their shared primary interests in the region. To put it simply, the renewal of the Quad is largely due to China and the fear of China's regional domination. As all Quad members have yet to participate in China's BRI, there are reasons for these like-minded states to cooperate with each other. In short, Australia needs to take steps to restore the trust between India and itself, and to convince India and others of the advantages of including Australia in the Malabar naval exercises in the building of a free and open Indo-Pacific region.

On vigilance on state capitalism in the protection of national security: As argued earlier, being a member of the Five Eyes, Australia is given little room for policy freedom and is instead compelled to align with the alliance's other members, especially the US, in acquiring and sharing secret and sensitive intelligence information. Huawei's case is not simply

an issue of state capitalism but instead signifies a new US strategy to contain China under the Trump administration. American hawks believe that economic engagement with China has benefitted China more than the US. Steve Bannon, former senior White House adviser to Trump, had urged the government to confront China (Mitchell and Liu, 2018). Peter Navarro, a former economics professor at the University of California, Irvine, is said to be the mastermind behind the US's trade war with China (Lowrey, 2018). The author of *The Coming China War* (Navarro, 2008) and a co-author of *Death by China* (Navarro and Autry, 2011), he has been critical of China's unfair trade practices and currency manipulation. Pushback from the US was deemed to be necessary and the recent trade war is part of the containment and wider technology war. In 2015 China unveiled its 'Made in China 2025' policy, singling out 10 sectors, mainly high-tech industries, as 'core' areas to develop. In order to increase Chinese companies' competitiveness in global production and supply chains, Beijing often subsidised its SOEs to purchase western businesses and acquire their technology. As argued by Sinologist David Zweig (2018), the current 'fight over trade is merely a skirmish in a larger technology war' between two superpowers. The ultimate goal of Trump is to contain China's growth and expansion.

There is little room for Australia to stay neutral or indifferent in the feud between the US and China over Huawei and ZTE, as long as Australia wants to remain in the Five Eyes and to keep the US on board in its strategic hedging strategy. The US could bar the sharing of intelligence with Australia if Australia network were believed to be 'insecure' from China's influence or espionage. Western allies are taking steps at the policy levels to avoid or exclude Chinese companies in order to preserve their cybersecurity. Australia has to ally with the Five Eyes, mainly the US, in its policy towards China's state capitalism in return for maintaining its security ties with the US and the West.

On involving regional powers: For a long time, Australia has indulged itself as a Western white country, with abundant natural resources. Being 'down under', lying between the South Pacific and Indian oceans, its wealth and safety have enabled Australia to act as an 'insular and introspective nation', not interested in engaging with its Asian neighbours actively (Wesley, 2011: back cover page). However, the rise of Asia and its economic and political relevance towards Australia in the

21st century is a 'wake-up call' for Australia's complacency. Southeast Asia is particularly important for the success of the Indo-Pacific strategy:

The Indo-Pacific power highway takes the pivot of world power away from the northern Atlantic and shifts it to the southern and eastern coasts of the Asian landmass. It is here that the dynamism of the world economy will course, and where the rivalries and alignments that shape the way the world works will be played out. And one of the key arenas of the Indo-Pacific is Southeast Asia. Any of the rising or established powers that can dominate Southeast Asia will dominate the Indo-Pacific and beyond. In other words, the pivot of world affairs is moving inexorably closer to Australia's northern coastlines (Wesley, 2011: 89-90).

Southeast Asian nations can now play a balancing role with regional great powers. To insure Australia's economic and security against vulnerability to over-dependence on a single market, it is vital for Australia to actively engage with its neighbours, and Indonesia in particular due to its economic size and strategic importance in fighting against terrorism. However, Australian-Indonesian relations are fragile. Its intervention in East Timor in 1999, the phone tapping of Indonesian President Susilo Bambang Yudhoyono in 2013 and the recent recognition of West Jerusalem as Israel's capital by the Morrison government, have adversely affected the bilateral relations between Canberra and Jakarta.²¹

As the largest Islamic state in the world, Indonesia's support for Palestine is not merely a debt of its independence but also concerns religious identity politics. In 1945, Jakarta received support from Palestinian nationalists in persuading Egypt to recognize Indonesia's independence. Since then, Palestine has weighed in on Indonesia's foreign policy. Jakarta often expresses its solidarity with Palestinians over the Israel-Palestine conflict (Fathana, 2018). In addition, the year 2019 is an election year for Indonesia. At the height of general and presidential elections, this 'Islamic factor' has already been showing its weight in Joko Widodo's election campaign (Laksmana, 2018). Both countries were supposed to sign a bilateral free trade agreement, Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA), during

the EAS in Singapore in November 2018. However, the deal was abruptly suspended because of Indonesian concern over the Australian stance on Jerusalem. Indonesian senior officials indicated publicly that the deal would be put on hold until Australia clarified (or to be more precise, annulled) its decision to move its Israeli embassy to Jerusalem (SBS, 2018). A month later, in a move seen as a compromise, the Australian government announced that while it recognised West Jerusalem as the capital of Israel, its embassy would still remain in Tel Aviv. It framed this decision as a support for a two-state solution. The relocation of the embassy would wait until Israel and Palestine reach a peace settlement via the two-state solution (Bagshaw and Massola, 2019; Kwan, 2018). After a delay of three months, Australia and Indonesia managed to clear the hurdle and signed in early March 2019 the bilateral free-trade agreement. Upon ratification by both parliaments, the IA-CEPA will reduce or remove tariffs on 99 percent of Australia's trade with Indonesia, benefitting Australia's agricultural and mining industries, higher education and health service by opening a larger market in Indonesia (Hodge and Rayda, 2019).

A recent study has showed that the majority of the respondents (55 percent) in Southeast Asia welcome the Quad initiative and agree that it has contributed to stability and peace in the region. However, if looking at the individual country among them, Indonesia is the most ambivalent towards the Quad. Over 50 percent of Indonesians chose not to support the Quad (Le Thu, 2018: 11). Indonesia may also be dismayed by Australia's condescending attitude toward it. In the Jerusalem spat, Liberal Senator Eric Abetz, who chairs the Senate Foreign Affairs, Defence and Trade committee, implicitly expressed a sense of 'superiority' over their Asian neighbours by highlighting the 'poverty' in Indonesia and threatening the withdrawal of Australia's economic aid to Indonesia. He reportedly tweeted: 'If Indonesia really wants to dictate [Australia's] foreign policy on the Middle East, should we rethink the [A]\$360 million each year we give them in aid? Instead, how about we calmly finalise this [Free Trade Agreement (FTA)] which will lift many Indonesians out of poverty and assist Australian farmers and jobs' (Peatling, 2018).

Hence, while engagement plays a strategic role in Australia's foreign policy, the 'superior' mentality of our policy makers has adversely impacted on the success of Canberra's strategic hedging in the Indo-

²¹ Other regional powers, such as Malaysia, also slammed Australia's decision as 'premature' and 'humiliation' of the Palestinians and their quest for a homeland (Massola and Rompies, 2018).

Pacific. Australia not only missed the opportunity to diversify its economic markets beyond China (soft balancing against China's economic clout), but also undermined the strategic partnership with Indonesia and other powers in the region.

Conclusion

Where should Canberra situate itself in the midst of growing tensions between China and the US? There is a better option than choosing between China and the US and that is strategic hedging. As a combination of engagement and indirect/soft balancing strategy, it is the most viable option for Australia to secure its economic growth and national security. The essence of strategic hedging is to not choose between China and the US but instead to bring more partners to Australia's side. The fear of China's regional domination has grown out of two sources: (1) China's growing hard power and assertiveness; and (2) the unpredictability of the Trump administration and its abdication of US global leadership. To insure against China's regional domination, Australia should bargain and engage with it from a position of strength. A more formalised and institutionalised Quad can also serve as an attempt to keep US presence in the region and an enabler to strengthen security cooperation among four liked-minded states under the framework of the Indo-Pacific region. Working with and through the Quad is one of the best means for Australia to make it diplomatically stronger than it is right now. However, Canberra has so far not been very successful in establishing a formalised Quad institution, and it remains a distant goal.

Economically, while it is in Australia's interest to continue its engagement with China, it should simultaneously diversify its economic partnerships in order to insure against any economic downturn in or sanctions from its largest trading partner. Australia's participation in the RCEP and TPP-11 is part of a soft balancing policy to preserve its economic security from vulnerability to over-dependence on a single market. Australia should also actively engage with its neighbouring countries bilaterally, apart from through multilateral institutions. However, its insensitivity towards one of its key neighbours, Indonesia, has caused the country to miss the opportunity for soft balancing against China's economic clout. On the other hand, being a member of the Five Eyes, Australia has to ally with other members, particularly the US, in building a constructive vigilance against state capitalism.

In sum, with regard to the aforementioned hedging spectrum, Australia's current hedging policy is 'under-hedging'. The weakest links are in the failures to institutionalise the Quad and to enmesh regional powers, notably India and Indonesia. Without enlisting more emerging powers solidly to its side, Australia is often sidelined by other three members of the Quad and it is quite alone in the Indo-Pacific region. Seen in this light, this paper concludes that Australia is far from over-hedging but is in fact slightly under-hedging. The strategic discussion and thought within the country is still clouded by the less helpful debate on whether Australia should align with China or the US, without exploring enough the 'Third Way' of how to reach out to regional powers closer to its home.

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About ACRI



For the first time in its history, Australia's most important economic relationship is with a nation very different in governance, politics and values. In the past, Australia's dominating economic relationships had been with the British Empire, the United States and Japan.

Today our most important economic partner is China.

China contributes now more to world economic growth than any other country. China absorbs 34 percent of Australian goods exports. By 2030, 70 percent of the Chinese population is likely to enjoy middle class status: that's 850 million more middle class Chinese than today.

In 2014, the University of Technology Sydney (UTS) established the Australia-China Relations Institute (ACRI) as an independent, non-partisan think tank to illuminate the Australia-China relationship. ACRI was formally launched by Australian Foreign Minister the Hon Julie Bishop.

Chinese studies centres exist in other universities. The Australia-China Relations Institute, however, is the first think tank devoted to the study of the relationship of these two countries.

The Prime Minister who opened diplomatic relations with China, Gough Whitlam, wrote in 1973: 'We seek a relationship with China based on friendship, cooperation and mutual trust, comparable with that which we have, or seek, with other major powers.' This spirit was captured by the 2014 commitments by both countries to a Comprehensive Strategic Partnership and the 2015 signing of a Free Trade Agreement.

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