

Another Trade War – This Time Without The US

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With all the news about the Trump Administration's trade disputes with China, Japan, Canada, Mexico, and the EU, the ordinary investor probably hasn't noticed one trade war which doesn't involve the US but could have serious consequences in East Asia. On 2 August 2019 the Japanese government removed South Korea from a "whitelist" of 27 countries which have blanket approval to buy certain sensitive Japanese exports. The whitelist exempts the specified countries from having to get individual approvals for the purchase of hundreds of commercially sensitive materials – for example, materials which have military as well as civilian uses.

Why is this decision important? Because Japan is the principal source of vital raw materials for South Korea's electronics industry. Hydrogen fluoride ("HF"), for example, is used in producing the silicon wafers which make up the microchips in electronic devices. More than 40% of South Korea's HF comes from Japan, so chipmakers and big electronics companies are rushing around in search of alternative sources of supply.

In fact, the whitelist change could affect more than 90% of South Korea's imports from Japan, which had a value of USD \$50 billion in 2018. Even if approvals are granted for each shipment, delays of up to 90 days are possible. (Like China's imports of Australian coal at present!)

How did this dispute start? The official Japanese explanation is "national security" – that South Korea has failed to provide sufficient information about the destination of certain South Korean export shipments, therefore Japan was concerned that South Korean export controls might be inadequate to prevent misuse.

The background, however, is that recent judgments of South Korean courts have opened up the possibility that the assets of Japanese companies might be seized to pay compensation of approx.. USD \$20 billion or more to the relatives of the 220,000-plus Koreans who were forced to work for the Japanese during World War II. The issue is one of many sore points arising from Japan's annexation of Korea in 1910, which led to the treatment of Korea as a colony and the use of Korean women as prostitutes for the Japanese army.

If the dispute is not resolved, it will damage the economies of both countries. Japanese exports will be delayed or reduced, and South Korean supply chains will be disrupted. The South Korean government has retaliated by removing Japan from its whitelist, but the impact is much smaller. More importantly, hostile public opinion in South Korea has mounted a boycott of Japanese goods and retailers.

But it's an ill wind that blows no one any good. Chinese suppliers may be able to replace some of the Japanese exports to South Korea, and Chinese chipmakers may be able to take market share from their

Korean rivals. The impact on Australia, however, is unlikely to be positive. Any slowdown in economic growth in Japan, China, or South Korea is likely to reduce Australian exports.

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