



PRODUCTIVITY INQUIRY: **Update for Inquiry participants**

Thursday 7 April 2022

This Inquiry is to provide the Australian Government with an overarching analysis of Australia's productivity performance, and recommend an actionable roadmap to assist with productivity-enhancing reforms for the future, particularly in light of Australia's COVID-19 experiences.

The terms of reference for the Inquiry give the Commission considerable scope in choosing areas on which to focus. To inform this choice, the Commission has engaged with over 80 stakeholders across the economy and received a number of submissions and brief comments. We thank all participants for their contributions so far. This paper updates Inquiry participants on key areas of focus for the Inquiry.

How we chose the Inquiry focal areas

Productivity is about getting more out of our productive activities and endowments. It is not about working harder – quite the opposite. It is about producing more, a greater variety and better-quality goods and services from given inputs and work hours. Productivity growth also underpins improvements in our quality of life by generating the means to improve social and environmental outcomes. Productivity growth is thus fundamental to – almost synonymous with – rising living standards.

Past productivity growth owes much to technological advance, whether embedded in physical capital, new business models or institutional arrangements. But no one knows exactly where the next big technological wave boosting productivity and our living standards will come from. We do know that a range of underlying factors are important – the ability of, and incentives for, individuals and organisations to take risks to pursue growth; the capability of firms and individuals to absorb new ideas and approaches; the stability and fairness of underlying social institutions; the structure, efficiency and stability of regulations that govern economic transactions; to name just a few.

We also have observed that the pandemic, and Australia's responses to it, have led to considerable changes in the way firms, governments and consumers operate, most notably through digital adoption and diffusion, and work practices (most notably related to the location of workers). These changes may or may not be ongoing, and whether any benefit to long-term productivity can be derived from short-term changes will depend on a variety of factors, including: managerial attitudes, shifts in consumer preferences and technological literacy, and government policies and regulatory settings (subsidies for telehealth provides a simple example of the latter).

Beyond the short-term influences on productivity, the long-term changing nature of the Australian economy suggests considerable scope for productivity growth may lie beyond the 'traditional' goods industries of agriculture, manufacturing and mining, and with the diverse services sector that both supports them and meets consumers needs directly. It is possible that the path of productivity

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growth in the services sector could look somewhat different to the path it has taken in relation to goods production.

The starting point for the Inquiry will be a consideration of the long-term enablers of productivity growth and how these are changing. The Inquiry will ‘deep dive’ into selected areas where other reviews and our own research suggest that recommendations for reform would have the greatest impact. Important as they are for economic growth, some areas and sectors of focus suggested by Inquiry participants such as the taxation system or regulation of a specific industry could be touched on, but are unlikely to be able to be explored in depth in this inquiry. On some of these issues, the Inquiry will refer to detailed work which has been done through other processes

The three categories of productivity enablers will be considered, loosely picking up the key components of a standard economic growth model – capital (*dynamic firms, flexible markets*), labour (*the future workforce*) and technology (*leveraging new technologies and innovation*). The specific areas within these enablers that will motivate policy recommendations will develop with the inquiry process.

Focal areas for the Inquiry

Dynamic firms, flexible markets: The environment in which firms throughout the economy operate is indisputably different going forward compared to pre-pandemic. While many businesses have struggled to survive, others have found that their balance sheets are unexpectedly strong. Alternative ways of operating and meeting consumer demands, working through disruptions to supply chains and staff availability, have been coupled with new experiences of the role of government, regulators and regulatory arrangements. While many of these effects will not be enduring, the experience of them will certainly alter views of what is possible.

In this context, the Inquiry will consider the broad incentives for businesses to innovate, grow and invest, including the competitive and regulatory environments that they operate within. Flexibility in our labour markets to acquire the necessary skilled labour from within Australia or from overseas, and the additional regulatory burdens that businesses can incur when they take on different types of workers, are key to this. As too will be the need to adapt to climate change and undertake greenhouse gas abatement activities. De-carbonising the economy is inherently a productivity issue. It will require significant innovation, investment and structural change over the next few decades to reduce real costs across the economy.

The future workforce: The experiences of the past few years have highlighted the critical role our education system can play in providing both the basic training for our future workforce and options for supporting lifelong learning, including rapid reskilling of those displaced from their current jobs.

Skill formation is fundamental to future productivity growth. For example, improving the quality of labour in the services sector is likely to be key to delivering improvements in the quality and accessibility of services. Some tasks across the economy will continue to become automated and STEM skills will be important for those workers enabling an effective digital progression. But tasks that require the judgement, empathy or decision-making of a person will also likely remain areas where skilled workers are in demand. How our schools, higher education and vocational training



institutions, and other skills development processes can be most efficiently and effectively used to skill our future workforce, will be a focus in this inquiry.

Leveraging new technologies and innovation: Technology has driven big gains in many sectors, including agriculture, transport, manufacturing, and mining, where equipment can readily substitute for human speed and strength. It has proven harder in some service sectors to get substantially more or improved quality services from labour input. But digital technology and data use could be game changers across all sectors of the economy.

Some digital innovation is evident as cheaper inputs (such as software as a service), or as more effective combinations of capital and labour (such as medical imaging). But in other instances it involves a fundamental change to the consumer interface or experience (such as is the case with entertainment streaming), with new products being created. Data is often central: its use can improve firm decision-making and be a feedstock for idea generation, sometimes aided by AI. It can unlock new business models where the cost of production is partly defrayed by the value of associated data. Enabling access to and exploitation of existing and new data sets, in a regulatory framework built on consumer trust and data security, is a key focus for productivity growth.

COVID has accelerated digital take up and innovation. As pandemic restrictions limited old business models, new ones were developed. Existing trends in retail and payments have hastened, and the consequences of the very slow digital progression in key sectors such as health have sharpened. These COVID-induced changes may become a catalyst for ongoing innovation and its diffusion. Research and innovation that is readily translated to practical applications and system solutions is needed for productivity. Key questions are how to foster a culture of innovation across firms and sectors, and the respective roles of high-end innovation (big breakthroughs) vs. broad-based entrepreneurship (and any linkages between these two).

What's next?

The Commission is appreciative of the time afforded by all those who have engaged in meetings for the Inquiry to date and contributed material in submissions. Over the coming months we will be supplementing this information with research and preparing a number of interim reports for the focal areas described above, to elicit further insights on reform options that would improve productivity.

Figure 1 – Key steps in the inquiry

