

Productivity Commission Green Paper

Continuing
the productivity
conversation



Executive Summary

Productivity is the most powerful tool we have for improving our economic wellbeing. It represents the organisation, capital and technology we apply in the production of the things we need and want.

Our productivity grows as we learn how to produce more (and better) goods and services, using less effort and other resources. From antibiotics to the smartphone, we can use goods and services today that the wealthiest people of a century ago could not imagine, let alone buy. This progress flows from rising productivity.

Productivity growth should not be taken for granted, though. Looking back at history, it tends to come in cycles. The invention of new technologies—such as the computer—makes it easier and cheaper to produce things and drives waves of strong growth.

The strong productivity growth in the 80s and 90s also followed a period where governments made some tough decisions, reducing barriers to trade and freeing financial markets, reforming industrial relations, allowing the Australian dollar to move with market forces, and changes to competition policy.

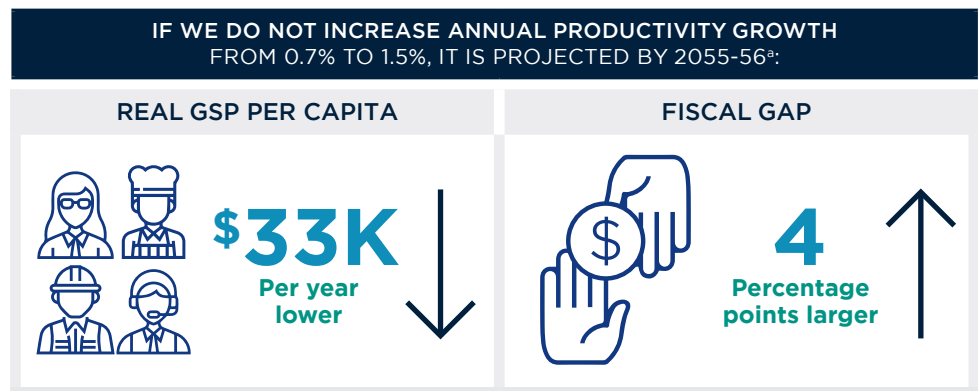
In contrast, the past two decades have seen a slowdown in productivity growth. Labour productivity—the measure of what we produce each hour that we work—has gone backwards in recent years. And the new challenge of the COVID-19 pandemic has in many ways made it harder to work and do business. That will damage productivity, at least in the short run.

The consequences of weak productivity growth are serious. The 2016 NSW Intergenerational Report assumed that labour productivity growth would lift back up to a long-run average rate of 1.5 per cent per year. If, instead, it continues to grow at the rate it has for the past decade—0.7 per cent—the NSW economy would be \$33,000 per person each year worse-off by 2056 (Figure ES). To see the impact more

clearly, think of how an extra \$33,000 per person per year would improve the living standards of your family.

To put productivity back on the right track, New South Wales will need to adapt. We have already seen how much change we can make in the face of crisis. Now it is time to look to how the choices we make today can have long-lived benefits for the people of our State.

FIGURE ES: PRODUCTIVITY'S LONG-TERM POWER



Source: NSW Treasury. Note that 0.7 per cent is the annual average growth rate from 2011-12 to 2018-19; 1.5 per cent is the long-run annual growth rate assumed in the 2016 Intergenerational Report.

Where does this paper fit in?

Although Australia is a federation with a powerful central government, state governments control many of the levers most crucial for raising our productivity.

The Commission has focused on practical recommendations that meet four criteria:

- They provide the **greatest productivity gains** at the lowest social cost.
- It is **feasible** to identify and address the problem.
- New South Wales can **implement reforms directly**, without complex and lengthy negotiations with the Commonwealth, or other States and Territories.

- They **align with other NSW Government priorities**—particularly the Premier's Priorities for enhancing quality of life, the NSW 2040 Economic Blueprint, the Treasurer's goals for the Commission, and the Government's 3R (Respond, Recover, Reform) response to COVID-19.

The Commission invites readers to comment on our draft recommendations. We will use this feedback to refine them before we present them to the NSW Government.

Key findings and opportunities for reform



Best-practice teaching will lift school results

Despite higher funding and recent reforms, NSW student outcomes are getting worse. Students are now more than a year behind their counterparts of twenty years ago. Throwing money at the problem does not work. School reform must stop tinkering at the edges, and focus on a single, evidence-based goal: best practice teaching in every classroom.

Key findings

To drive better education outcomes, the NSW Government must put a laser-like focus on improving teaching and learning in every classroom across the State.

The quality of teaching is the single most important factor for student learning. To lift the quality of day-to-day teaching, reform must focus on embedding best-practice teaching across all classrooms, using data to track student progress and teacher effectiveness.

Lifting teaching quality will also require attracting, developing and supporting highly effective teachers. Fast-tracking high-quality entrants into teaching works, especially in shortage areas like maths. Reform must strengthen evaluation practices for all teachers, especially classroom observations.

NSW needs new career paths that reward our best teachers and keep them in the classroom, teaching students and training teachers.

Summary of draft recommendations

Design and implement faster and more flexible pathways into teaching to broaden the supply of quality teachers and address workforce gaps (Recommendation 2.1).

Improve the ways we evaluate teachers so school leaders can better identify and address teachers' development needs (Recommendation 2.2).

Develop an 'instructional lead' career pathway for highly effective teachers as an alternative to an administrative career (Recommendation 2.3).

Create a culture of continuous improvement that drives best-practice teaching in every classroom. Embed strategies, resources and support that are tailored to individual school needs. Make schools accountable in implementing evidence-based best practice (Recommendation 2.4).



A modern VET system to deliver the skills we need

The State's vocational education and training (VET) system must reform to deliver the skills we need in a post-COVID economy. Chronic skills shortages show the system is unresponsive to industry and unattractive to students. Reform should focus on introducing more modern, flexible training pathways and addressing poorly-aligned incentives.

Key findings

The NSW Government controls key VET levers such as the delivery of training, the running of TAFE NSW, and the targeting of course subsidies.

Despite many reviews of VET in the past decade, few reforms have modernised learning modes, career pathways, or VET's relationship with industry. Bias against VET is still strong, with universities seen as the default pathway, especially for HSC graduates.

COVID-19 has displaced thousands of workers and accelerated structural changes to the economy. Many jobs will not return, requiring workers to reskill or upskill.

Chronic skills shortages in trades are the result of unsuitable and limited training pathways beyond apprenticeships. Low wages and a lengthy, inflexible training structure deter potential trades workers.

Poorly targeted subsidies have encouraged many students to enrol in courses of low value to employers and students. The mismatch between skills delivered by VET and industry needs has further contributed to poor employment outcomes.

There is growing interest in micro-credentials from industry, students and government. Micro-credentials are a highly targeted and efficient method of skills delivery and are well-suited to life-long learning.

Summary of draft recommendations

Respond to the COVID-19 skills challenge with an 'earn or learn' strategy, focusing on the skills needed for the post-pandemic economy (Recommendations 3.1).

Introduce new pathways to trade qualifications aimed at HSC graduates and mature-aged workers. New pathways should allow students to complete the institutional requirements of a qualification before gaining on-the-job experience (Recommendation 3.2).

Target Smart and Skilled subsidies more effectively by refining the NSW Skills List. Funding should be targeted at skills shortages and emerging business needs (Recommendation 3.3).

Promote the development and recognition of micro-credentials. Prioritise their funding in line with business needs (Recommendation 3.4).



Forward-looking regulation supports innovation and competition

Regulations can help us adapt to economic change, or they can slow us down. Overly complex and burdensome regulations stifle innovation and slow down productivity growth. New South Wales needs smarter, more flexible regulations that support innovation, competition and economic growth.

Key findings

Temporary changes introduced by the NSW Government in response to COVID-19 have demonstrated the benefits to consumers and businesses of adaptable regulation.

Flexible, outcomes-focused regulation will speed up the recovery from COVID-19.

We have identified sixteen opportunities to modernise NSW regulations.

New South Wales, like many other jurisdictions, faces the ongoing challenge of adapting regulations to keep pace with change.

Approaches to containing regulation such as red tape reduction targets and staged repeals have not been effective.

Summary of draft recommendations

Extend the operation of some COVID-19 regulatory changes, such as more flexible trading hours and digital solutions for legal and administrative processes (Recommendations 4.1-4.2).

Review existing regulatory regimes in fields such as pharmacies, packaged alcohol sales, drones, genetically modified technology, and childcare (Recommendations 4.5-4.7, 4.9, 4.16, 4.11, 4.18).

Pursue automatic mutual recognition, or if that is not possible, unilaterally recognise licenced occupations so that workers can move to New South Wales from other Australian jurisdictions (Recommendation 4.3).

Implement or reform regulation to support new technologies and competition in fields such as personal mobility devices, mandatory professional development, retail trading, rice marketing, rail access, and e-conveyancing (Recommendations 4.14, 4.4, 4.8, 4.10, 4.12, 4.17).

Update competitive neutrality policy to, among other things, remove outdated arrangements and improve complaints processes (Recommendation 4.13).

Create a best-practice regulatory policy framework underpinned by rigorous evidence, and new tools to improve regulator performance, including local government regulation (Recommendations 4.19, 4.15).





Meet the challenge of sustainable, well-priced water and energy

Water

Population growth and rainfall variability will continue to challenge the water sector. Better water management can ensure households and businesses continue to have access to safe, reliable and affordable water services.

Key findings

The water sector's functions are spread across a number of agencies and corporations. That makes coordinated long-term decision-making harder.

Integrated water cycle management can achieve better economic, social and environmental outcomes—but some barriers still remain to its uptake in New South Wales.

Many regional water utilities face operational challenges because they are small and remote, and cover large areas.

Managing demand for water can ease supply pressures, but it can also have social and economic costs.

Summary of draft recommendations

Improve governance by setting a vision and a plan for the sector, clarifying roles and responsibilities, and improving collaboration and cooperation (Recommendations 5.1-5.3).

Remove unjustified barriers to water recycling to 'keep all options on the table' for safe, affordable and reliable water services (Recommendations 5.4-5.5).

Improve the way regional utilities are funded, to target those that need it most and encourage efficient operation (Recommendation 5.6).

Ensure the way we manage water demand maximises benefits for the community (Recommendations 5.7-5.8).

Energy

The energy sector is going through a major technological transition. The growing role of renewable generation presents both opportunities and challenges. Energy policy must evolve to maximise the benefits of the transition, create an environment that attracts investment, and ensure the sector operates efficiently.

Key findings

Reliability of electricity generation and transmission networks is important—but improvements can come at a disproportionate cost to customers.

Ongoing uncertainty around carbon dioxide reduction policy is acting as a brake on investment in new generation. That risks pushing wholesale prices higher over time.

Demand management has a role in optimising the electricity system, but inadequate metering technology holds it back.

Energy sector regulation is fragmented and dispersed across several overlapping agencies. This both raises its cost and reduces its effectiveness.

New South Wales will face gas shortages as early as 2024. Despite significant domestic resources we produce little of our own gas. Land-use restrictions in particular have impeded development of gas fields.

Energy subsidy programs are numerous and complex.

Summary of draft recommendations

Make sure government energy reliability policy is consistent with consumer willingness to pay (Recommendation 5.9).

Adopt an integrated market-oriented climate change and energy policy that is technology-neutral and prices carbon dioxide emissions (Recommendation 5.10).

Investigate how technology can improve electricity pricing (Recommendation 5.11).

Improve energy governance by bringing regulation responsibilities under one roof (Recommendation 5.12).

Make sure regulation on land use manages multiple land uses to the benefit of the community (Recommendation 5.13).

Streamline energy subsidies (Recommendation 5.14).



Smarter infrastructure will support jobs and communities

Infrastructure underpins the bulk of economic activity in modern societies. It helps people get to work, makes it easier for businesses to get products to customers, and provides access to critical services such as electricity, education and healthcare. Investing in the right infrastructure is powerful lever by which the Government can raise productivity.

Key findings

Poorly coordinated land and infrastructure planning can create community resistance to change and costs the Government more.

Infrastructure investments are among of the most expensive and impactful decisions governments make. Identifying and prioritising the right projects can have long-lived benefits. Choosing badly can impose substantial costs on society.

Infrastructure congestion is a drag on productivity. Traffic and public transport crowding cost individuals and businesses valuable time and makes New South Wales a less attractive place to live and work.

Summary of draft recommendations

Plan for greater housing and business activity in areas where there is spare infrastructure capacity (Recommendation 6.1).

Improve transparency to create the right incentives for good infrastructure investment (Recommendation 6.2).

Ensure that agencies' business cases align with Government guidelines, and that funding is given to properly evaluate projects (Recommendation 6.3).

Investigate new ways of easing road congestion, such as reducing problematic driver behaviours and charging for congestion (Recommendation 6.4).

Assess how Opal fares and concessions can be used more effectively to ease demand in peak times, encourage greater use at other times, and support those that need it the most (Recommendation 6.5).



Plan for the housing we want and the jobs we need

Planning systems are enablers of productivity. In cities, they pool together talent, capital, and suppliers of goods and services. At the same time, they must manage the many costs of this process, such as congestion, pollution, noise, reduced personal space and increased pandemic risk. Overly prescriptive and complex planning regulations can stifle business competition and reduce housing supply. Changes to support the economy during the pandemic have helped—and they show how our planning system can be more responsive.

Key findings

Housing supply has failed to keep up with demand. That has led to an undersupply of housing, increasing the cost of living for households and making New South Wales a less attractive place to live.

Regulations on apartment design and car parking requirements add to the cost of housing and are out of step with the needs of the community.

Prescriptive rules on land use by businesses are inflexible and cannot accommodate innovative businesses and the evolving needs of the economy.

Development applications are taking longer to assess, restricting housing supply and reducing affordability.

As our population grows and our backyards shrink, access to open and green space is important for our productivity. It keeps people healthier, connects communities, and helps make cities more resilient to the impacts of climate change.

Infrastructure contributions are an important funding source to deliver infrastructure required to accompany growth. Over time the system has become more complex and is perceived as opaque and inefficient.

Summary of draft recommendations

Ensure planning instruments keep up with housing needs, while taking into account community interests (Recommendation 7.1).

Review apartment design and car parking regulations to accommodate consumer choice while maintaining minimum basic quality. (Recommendation 7.2).

Rationalise zones and restrictions on permissible business activities and produce strategies to use commercial and industrial land more productively (Recommendations 7.3-7.5).

Continue to cut red tape to make the planning system more effective and deliver on the Government's goal of reducing assessment times (Recommendation 7.6).

Develop a consistent way to measure the benefits of open and green space, and incorporate it into land use planning (Recommendation 7.7).

Use the Review of Infrastructure Contributions to find ways to deliver a principles-based, transparent and certain system (Recommendation 7.8).



A better mix of state and local taxes can encourage growth

The Government funds vital public services and infrastructure for a growing population. Yet some of our taxes are disproportionately distorting the economy and cutting productivity growth. Some notably discourage work or investment; others disguise the real cost of goods and services. New South Wales will be more productive and better able to fund services and infrastructure if we switch the tax mix towards taxes that cost our economy less.

Key findings

New South Wales is overly reliant on inefficient taxes. Property transfer taxes are the most costly and unreliable.

The existing rates mechanism does not sufficiently compensate councils for population growth. This leaves local governments with insufficient revenue to meet demand, and with an incentive to resist development.

Summary of draft recommendations

Replace inefficient taxes with more efficient ones. Start by replacing stamp duty with a broad-based land tax on unimproved land values. Coordinate payroll tax administration across states and territories (Recommendation 8.1).

Use the Review of Infrastructure Contributions to pursue reforms to deliver a more sustainable way to fund the infrastructure we need.

Evaluate reforms within three years and if reforms do not provide sufficient funds to deliver services, councils should hold a plebiscite of ratepayers to test support for abolishing of the rate peg (Recommendation 8.2).