

BUILDING A RESILIENT FUTURE

POLICY BLUEPRINT
APRIL 2022

FOREWORD

Australia is at a most critical juncture which has the ability to redefine the nation and its economy since World War II.

The last two years have tested Australia's capability to adjust to uncertainties, but they have also demonstrated the ability of businesses to innovate and find new opportunities and markets faster than ever before.

This experience has highlighted industries and expertise within the domestic economy where there is deep knowledge and capability which, if harnessed with the right policies and infrastructure, will build a resilient future for generations to come. However, if left untended, this will result in declining productivity and potentially living standards.

Advancing economic and social policy reforms that support economic growth are critical for providing a stable framework for investment capital that drives productivity gains, improved market competition, and employment growth.

The policies outlined in this document capture the macro issues for building economic growth, creating jobs, and increasing sustainability and the six reform priorities to put Australia back on the map as an attractive destination for investment.

These are not optional policy reforms, but are essential for building a resilient future.

Jonathan Kelly

Interim CEO



AUSTRALIA IN A GLOBAL CONTEXT

After 28 years of continuous economic growth, a GDP which has performed well compared to other advanced countries, and a relatively high standard of living, there is much work to be done to transition Australia into a more knowledge-based, high value-adding economy.

As a nation, Australia is still largely beholden to an old-world economy that has not always kept pace with the development in complexity and technological transformation of other economies.

This is particularly apparent in measures of economic complexity when Australia ranked 86th globally, the lowest of all developed economies, and lower than many developing countries – according to the latest rankings developed by Harvard University’s Center for International Development (**Figure 1**). Since 1995, when Australia was placed 55th globally for economic complexity, the nation has dropped 31 places.

Furthermore, Harvard University concludes that “Australia is less complex than expected for its income level. As a result, its economy is projected to grow slowly”¹, with Australia’s growth projection to 2029 ranked 101st out of the 133 countries assessed.

This outcome is backed by the 2019 Global Innovation Index (GII), which ranked Australia 22nd globally, down from 20th in 2018, behind nations such as the United States, the Republic of Korea, China and Iceland. “The 2019 GII found Australia to be weak across knowledge and technology outputs, creative outputs, and business sophistication, relative to the top 25 innovation nations globally.”² This shows that we need to do much more if we want to build and future-proof a sustainable and growing economy that can attract talent and capital from international markets.

It is therefore important that the economic challenges that Australia faces are recognised and tackled through leadership in long-term and visionary policy reforms.

Figure 1: Australia’s Economic Complexity Index Ranking
1995 to 2019



Source: The Growth Lab at Harvard University (2019) “Growth Projections and Complexity Rankings, V2”

1 Harvard University’s Center for International Development, Atlas of Economic Complexity October 2021

2 Cornell University, INSEAD, and the World Intellectual Property Organization, Global Innovation Index 2019

In addition to falling behind on productivity, Australia has continued its decline in educational outcomes (**Figure 2**). Mathematics results in Australia are now below the OECD average³ and an increasing number of students are failing to meet the minimum national standard across writing, reading and mathematics.

It is therefore important that the economic challenges that Australia now faces are recognised and addressed through leadership in long-term and visionary policy reforms. The fact that Australia has not kept pace

with the development in complexity and technological transformation of other economies should sharpen the focus on this agenda.

Industry as a whole has a role to play in informing and engaging with all sides of politics on these challenges. This includes the private capital industry, which invests in a wide range of Australian companies, be they early stage tech start-ups or long-established agricultural or manufacturing businesses. It is only by working together that we can build a resilient future.



As a nation, Australia is still largely beholden to an old-world economy that has not always kept pace with the development in complexity and technological transformation of other economies.

Figure 2: Trends in performance in Reading, Mathematics and Science





MACROECONOMIC ENVIRONMENT

Despite having enjoyed a long period of continual growth, Australia is facing some very strong headwinds as it begins to open international borders. These headwinds come from geopolitical and economic pressures from the war in Ukraine, and the recent flooding natural disasters in southern Queensland and northern New South Wales.

In an environment of sustained low interest rates and demand for residential housing (especially as employees continue to work from home flexibly), residential housing prices have continued to rise (Figure 3). This has resulted APRA writing to banks and other Authorised Deposit Taking Institutions in October 2021 with a request to increase their interest rate buffer for mortgage lending to at least 3.0 percentage points above the loan rate.⁴

The Reserve Bank has also now signaled to the market that it intends to discontinue the target for the yield on the April 2024 bond and Governor Lowe has indicated that banks may start increasing interest rates by the end of the calendar year. At the same time, the unemployment rate has hit 4.0% (being the lowest in 13 years), employment participation is high, whilst cost of living pressures are rising including for food and from higher fuel prices. Given developments in the US which have resulted in the US Federal Reserve lifting rates and scaling down its bond purchases, there is a risk that Australia will not be immune from global interest rate rises.

Household saving reached a record high of 22 per cent in June 2021 which RBA Governor, Phillip Lowe attributed to

the boost in incomes from government support, limited opportunities to spend and households feeling uncertain about the future.⁵

There is evidence that business confidence is low with overall business investment falling significantly over the past six years as a share of nominal GDP. (Figure 4)

These are concerning trends, which combined with low national productivity and higher inflation on the horizon, will place Australia in a challenging situation as international borders open and businesses, workers and regions adjust to the post COVID environment.

While Australia's economic performance over the coming months remains to be seen, the fiscal budget position and pressure beyond fiscal stimulus will continue in less direct ways. Examples of where this may occur are structural shifts in healthcare including the ongoing management of COVID-19, vaccine boosters and ongoing management of the virus, a decrease in international student numbers in universities and increasing pressure for research commercialisation.

This highlights the critical need for policies that support the funding and growth of Australian businesses, support the flow of investment capital, boost innovation and address skills shortages.

Given falling business investment after the end of the mining boom, it will be important that the economy re-tool to address industries of the future.

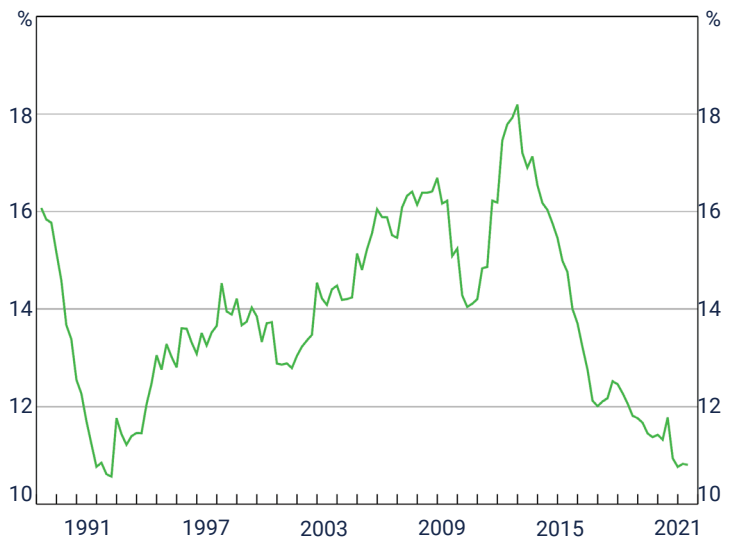
Figure 3: Housing Prices and Household Debt*
Ratio to household disposable income



* Household disposable income is after tax, before the deduction of interest payments, and includes income of unincorporated enterprises.

Sources: ABS; CoreLogic; RBA

Figure 4: Business Investment*
Share of nominal GDP



* Adjusted for second-hand asset transfers between the private and other sectors.

Source: ABS

⁴ APRA increases banks' loan serviceability expectations to counter rising risks in home lending, Media Release, 6 October 2021

⁵ From Recovery to Expansion, Keynote address to the Australian Farm Institute Conference, Phillip Lowe, RBA Governor, 17 June 2021

AUSTRALIA'S PRODUCTIVITY CHALLENGE

Australia's future prosperity and living standards rely on a revival in productivity growth. The 2020 Intergenerational Report shows that productivity has slowed to an annual average of 1.2 per cent since 2005 and needs to return to 1.5 per cent to be consistent with the 30-year historical average to 2018-19.⁶

To positively impact productivity, the 2019 House, Income and Labour Dynamics in Australia (HILDA)⁷ survey showed that there is a real need to move away from a reliance on commodities and property to a pro-growth productivity agenda that will provide real, sustainable growth. Such an agenda will shift productivity from its current downward trajectory which, according to analysis by Trading Economics, shows Australia as one of only two G20 countries to score below 100 points for productivity.

It is clear that Australia needs to look beyond the resources and property sectors for productivity growth. Australia's national comparative advantage will increasingly be built on

the quality of our ideas and our human capital. This will help to address Australia's skill shortages and the flow of new technologies and businesses.

The pandemic accelerated the digitalisation of businesses in a matter of months, which under 'normal' conditions may have taken years, as many Australians worked from home and businesses adapted to e-commerce solutions. This may have a positive impact on productivity and counter balance the effect of border closures and the downturn in migration. It has also demonstrated the ability of the nation to pivot during a time of crisis.

Australia now has an opportunity to build upon the productivity-enhancing impact of businesses underpinned by technology with robust policies that support the growth and expansion of businesses aligned with core focus industries of the future. These will need to be underpinned by pillars to build resilience and support a stronger, smarter, better Australia.



6 2021 Intergeneration Report, The Treasury, Australian Government

7 The Household, Income and Labour Dynamics in Australia Survey, Melbourne Institute, 2019



STRONGER, SMARTER, BETTER

We believe that seven pillars will underpin a resilient future for Australia.

1 MAINTAINING MOMENTUM

The pandemic has been a catalyst for businesses and individuals to rapidly deploy new technologies at an accelerated rate from enabling remote working environments, telehealth and secure payments platforms, to more flexible supply chains. Continuing to embrace the use of technology will maintain the momentum and support new technologies that will contribute to innovation and a skilled labour force with the capacity to directly contribute to economic output and to indirectly lift productivity, global competitiveness and create jobs across the economy.

Achieving material gains in innovation and technology will generate sustainable economic and income growth for all, and position the Australian market with a competitive edge against other developed economies around the world. In turn, this will enhance the attractiveness of Australia to domestic and offshore investment capital. It will also support the objectives in government's *Digital Economy Strategy*⁸ launched as part of the FY22 Federal Budget to build a 'modern and leading digital economy' for a resilient future.

2 KEEPING AUSTRALIA OPEN

Now that Australia has reopened international borders, the challenge will be remaining open for business in the future and ensuring that prudent measures are in place to prevent any future long-term lockdowns should a pandemic or other catastrophic event occur.

A robust framework and investment in infrastructure for dealing with unforeseen circumstances will be central

for maintaining investor confidence and attracting entrepreneurial businesses and skilled migration to Australia. This includes measures for effectively and efficiently dealing with quarantine, for maintaining supply chains and forging trade agreements that cross multiple jurisdictions.

3 ENSURING A FLOW OF INVESTMENT CAPITAL

Australian jobs and industry rely on a steady flow of capital to support investment into growing businesses across all sectors of the economy. Our nation's demand for capital continues to be greater than the domestic supply. As a result, Australia is a net importer of capital.

The ability to attract foreign capital relies on the ease of doing business and making investments that are aligned with growth opportunities. To this extent, the development

and expansion of the digital economy will be a drawcard in maintaining Australia's attractiveness as an investment destination, particularly in digital and growth industries where our nation has a comparative advantage. As the innovation sector continues to mature, consideration should be given to how superannuation funds can be incentivised further to invest into the digital economy.

4 BUILDING DIGITAL CAPABILITIES

Building a digital future will require further investment in technological infrastructure to ensure businesses and individuals have access facilities that are world class. Upgrading the NBN to a gold and future-proof FTTP standard and building 5G and future 6G capabilities will be integral to this process.

The transition to a digital economy can be further fast-tracked through providing businesses with incentives to improve their digital capability and to increase digital skills through education and training programs. Research & Development can be tailored to focus on investment into industries aligned with the future digital economy.

5 PROTECTING AGAINST CYBER THREATS

Protecting Australians, Australian businesses, infrastructure and citizens through cyber security initiatives implemented in a time critical manner is essential in protecting the security of our nation in an environment where cyber threats are more prevalent and more sophisticated than ever before. Cyber protection that continuously aligns with the evolution

of cyber threats will contribute to the protection of Australia's national security and economic security. This includes education for all Australians and Australian businesses on cyber security awareness and emergency plans that can be deployed in the event of a cyber threat.

6 ACHIEVING NET ZERO

As outlined in the 2020 Intergenerational Report, the likely physical effects of the transition to a lower carbon emissions economy will mean that some sectors will need to adjust to falling demand for some exports while new opportunities will be created in other sectors. In many respects, these factors will be outside of Australia's sovereign ability to control, and ultimately these costs will be passed on to Australian consumers and other businesses. There are a number of areas where Australia has a comparative advantage such as in solar and wind energy and in regenerative farming transformation and can be a world-leader in the export of clean-tech solutions that

will underwrite the global shift towards more sustainable economies.

Businesses will play a pivotal role in driving innovation and in developing new technologies that will reduce carbon emissions and will also lead the way through policies that commit to and ensuring actions that reduce carbon emissions and in leading new business practices and investment decisions. Businesses will increasingly find it important that credible green credentials are provided to consumers, their business partners, financiers and investors.

7 MANAGING THE ECONOMY

Against the backdrop of a higher inflationary environment, it will be critical for any Government to manage a range of competing issues in order to maintain economic growth. These challenges include balancing rising job vacancies in a recovering economy which has not seen significant wage increases in recent years, with effective management of the

increasing cost of living pressures.

Targeted policies will need to carefully balance the needs of all economic participants while instilling confidence in the Australian economy and allowing investors to make confident investment decisions.



CHARTING THE FUTURE

We believe that sustainable long term economic growth will require adoption of policies that focus on the design of Australia's tax system, the provision of relevant infrastructure assets, and policies which support the funding and commercialisation of innovation. These should be underpinned by government's digital economy strategy to secure Australia's future economic, employment and productivity growth through the acceleration and development of domestic technology as an enabler of businesses across all sectors of the economy.

Six policy reforms central to building a resilient future are outlined below.



REFORM TAXATION

Reforming Australia's taxation regime is broadly considered to be the policy area with the greatest potential to reinvigorate Australia's economy over the long-term but which has had a very difficult political pathway.

Australia's taxation system has been the subject of numerous reviews over past few decades, and many of the most significant recommendations set out in reviews remain relevant today.

The most comprehensive of the recent reviews is the 2010 Australia's Future Tax System (AFTS) Review, led by former Treasury Secretary, Dr Ken Henry and the Johnson review, also from 2010 titled: "Australia as a financial centre: Building on our strengths" and aspects of the cancelled Federation White Paper from 2015.

Many of the recommendations from those reviews are yet to be progressed. Taken as a whole, the tax reform blueprint set out in that work represents a compelling, growth-enhancing plan for a staged transformation of the tax mix across federal and state-based tax regimes. While some state within Australia have adopted or indicated a review of their tax policies, a coordinated national approach has not been agreed and many inefficient and globally uncompetitive tax practices remain.

During this time, many of Australia's competitors have adopted policies which have transformed them into global financial centres, increasingly outpacing Australia, despite its historic strength in financial services.

RECOMMENDATIONS

Some of the key priority reforms set out in the AFTS Review, as well as other growth-orientated analyses of Australia's taxation system, revolve around reducing the headline corporate income tax rate for all businesses, a step that would deliver income growth for all Australians and also lift Australia's competitive standing in the global market for capital and talent.

A reduction in the corporate income tax rate will form an important part of a broader strategy of shifting the nation's 'tax mix' by reducing reliance on direct taxes – such as personal and corporate income taxes – and re-balancing towards greater reliance on 'user pays' pricing mechanisms and indirect taxes. In the technology-enabled global marketplace in which Australian businesses operate, such a shift is vitally important to building a stronger and more sustainable budgetary position for governments at all levels into the future. Measures that could be considered are those potentially hindering investment in Australia and support for policies which encourage investments in high-growth businesses in order to help the post-pandemic economy recover.

Alignment of state-based tax regimes needs to be considered in order to avoid the red-tape of businesses dealing with multiple differing and competing regimes.



Reforming Australia's taxation regime is broadly considered to be the policy area with the greatest potential to reinvigorate Australia's economy over the long-term but which has had a very difficult political pathway.



REDUCE RED TAPE

Red tape and regulatory cost burdens tend to move in cyclical phases every 10-15 years. Removing red tape and introducing greater efficiencies drive increases in productivity, competitiveness and high-value jobs growth. Past experience in Australia suggests that attempts to reduce red tape at a federal and state level have sometimes been narrow in scope, and therefore failed to achieve the desired economic and business outcomes.

Yet, there are existing policy documents which may be instructive in supporting the work of Government's Deregulation Taskforce launched in December 2020 with the primary tasks of reducing overlapping or duplicated cross jurisdictional regulatory burdens, modernising business communications, improving occupational mobility and improving the efficiency of Australia's excise duty regimes.

In 2013, the Government issues a report titled 'Boost Productivity and Reduce Regulation'⁹ which outlined a whole-of-government framework to reduce the red and green tape burden by at least \$1 billion per year. Amongst numerous recommendations, the report recommended at least two Parliamentary Sitzings be dedicated each year to repeal counterproductive or unnecessary regulation, and that COAG meetings – now National Cabinet – include deregulation and red tape as standing items for discussion and review throughout the year.

Recommendations in the Productivity Commission's Shifting the Dial¹⁰ review in 2017, should be reconsidered particularly in respect of the opportunity for National Cabinet to adopt a formal joint reform agenda.

Reinstatement of the core principles set out in the 2013 report, and the adoption of recommendations from the Productivity Commission's 2017 analysis, should form part of a comprehensive and clear commitment to eliminate red tape costs for businesses over the short and medium-term.

RECOMMENDATIONS

Governments and regulators should always assess new laws and regulations with a 'no red-tape framework' and only regulate where there is a clear and unavoidable need, for example where industry is not able to independently react to market ineffectiveness or likely consumer harm. Where new laws or regulations are required, they should be implemented through enabling technology. Wherever possible, business practices should be streamlined to enable businesses to scale up and expand through a conducive regulatory environment.



⁹ Coalition's Policy to Boost Productivity and Reduce Regulation, July 2013

¹⁰ Shifting the Dial: 5 year productivity review, Australian Government Productivity Commission, August 2017



BUILD A WORLD CLASS INVESTMENT REGIME

As a net importer of capital, Australia's economy relies on a dependable and steady flow of foreign investment to drive economic growth and job creation. At this critical time, it is imperative that businesses can quickly and efficiently access capital from domestic as well as offshore investors. However, an ongoing capacity to invest greater amounts of capital into Australian businesses cannot be assumed and must be supported by policies that continue to enable and encourage capital investment into the domestic market.

Given the impact of the COVID19 pandemic and the uncertain times that lay ahead, and as a net importer of capital, Australia's economy relies on a dependable and steady flow of foreign investment to drive economic growth and job creation. At this critical juncture, it is vitally important for our economic recovery, and Australian jobs, that businesses are able to quickly and efficiently access capital from domestic as well as offshore investors.

Collective Investment Vehicles

The Council has been a long-term advocate for the introduction of globally competitive collective investment vehicles (CIV) in Australia to replace current complex trust structures which are constraining foreign investment. In principle, the Council welcomed the introduction of the new Corporate Collective Investment Vehicle (CCIV) regime by 1 July 2022. This was a re-commitment in the May 2021 Federal Budget, however, unlike previous announcements, no re-commitment was made to introduce a Limited Partnership CIV.

World-class, competitive CIVs are essential for building and expanding the pool of capital that can be attracted into the Australian economy. Accordingly, it is important that a flow-through, internationally best practice LP CIV – the globally accepted private capital vehicle of choice – be introduced as soon as possible, keeping in mind that the

original introduction date of 1 July 2018 has not been met. Supporting the broader policy objectives of building Australia as a financial services hub, such a vehicle could transform the flow of capital into high growth Australian businesses, helping to facilitate Australia's transition to a knowledge-driven economy.

Foreign Investment Framework

Ensuring that the policy environment around foreign investment remains stable is one of the key ways in which the government can help maintain Australia's reputation as an attractive investment destination.

The government should commit to maintaining policy certainty within the existing foreign investment framework, and make no unnecessary changes that would restrict future foreign investment into Australian private capital funds or businesses. Given the desire to attract foreign investment into Australia, policies for foreign investment need to consider whether the foreign investor is an active manager or taking advice from Australian investment managers.

RECOMMENDATIONS

Introduce a flow-through, international best practice LP CIV as a priority as soon as possible to support the broader policy objectives of building Australia as a financial services hub and major supplier of global financial services.

Ensure Australia is an attractive destination for foreign investors by ensuring their policies around foreign investment provide clarity and certainty to market participants.



STRENGTHEN TRADING TIES REGIONALLY AND GLOBALLY

In a globalised economy, trade interdependencies and global mobility will continue to play an important role in a global economic rebound. Reducing barriers to trade and investment, the movement of people and skills and introducing frameworks within trade agreements on a regional and global scale to create more diverse opportunities and will lead to better trade and investment opportunities.

RECOMMENDATIONS

Ensure policy settings through bilateral and multilateral agreements encourage trade and investment and ensure that reciprocal arrangements can be made in relation to the framework for the flow of foreign investment capital and human capital.



BUILD THE NEXT GENERATION OF LOCAL TALENT

Science, Technology, Engineering and Mathematics (STEM) capabilities are particularly important to building and developing a knowledge-based nation. As outlined in the Australia 2030 Prosperity Through Innovation report growth in jobs and occupations requiring STEM skills are outstripping overall employment growth across the economy. This is a critical gap that will require both short-term focused initiatives, such as migration, and longer-term initiatives, such as re-tooling the education system to embrace STEM subjects and to equip students with the knowledge and skills to contribute to productivity in the workforce.

Attracting and retaining the world's best talent is particularly important for Australia as a net importer of not only capital, but also highly skilled talent. Ensuring the right settings are in place to grow local talent within the domestic economy is also of critical importance to Australia's long-term prosperity to develop a critical mass of skilled workers for the new economy.

The global search for talent is compounded by accelerated changes brought about by technology and innovation. While the pipeline of talent within Australia continues to grow, there are skills and talent gaps which need to be filled as a priority in areas such as quantum computing university research commercialisation, and engineering across all industry sectors.

Australia has a golden opportunity to be a destination of choice for high calibre talent through its attractive lifestyle, stable political system and future growth opportunities. The government's Global Business and Talent Acquisition Taskforce (GBTAT), Global Talent – Sponsored and Independent Programs and tertiary education reforms are positive steps towards acquiring and generating the

skills required in the future. Skilled migration will continue to be essential and further refinement of skilled migration occupation lists may be necessary to attract the specialist skills that are essential for the growth and expansion of businesses in the domestic economy.

RECOMMENDATIONS

Commit to world class education system that is dedicated to developing the right skills and experience for a knowledge-based economy.

The Government commit to turning around Australia's education results and embedding a strong STEM capability, through:

- Ensuring adequate funding of education at all levels, childcare through to post-graduate;
- Implementation of STEM initiatives, such as 'STEM Schools'; and
- Reviewing the methods and techniques deployed in countries with higher educational outcomes.

Continue to promote Australia as a destination for skilled migration through the GBTAT and Global Talent programs and continue to refine the skilled migration list to reflect the needs of a knowledge-based economy.



Attracting and retaining the world's best talent is particularly important for Australia as a net importer of not only capital, but also highly skilled talent.



REDEFINE UNIVERSITY COMMERCIALISATION

Enrolment of international students in Australian universities substantially declined during the pandemic and shows little sign of reaching pre-pandemic levels. With the reliance on international students as an integral part of funding, universities are challenged to rethink their business models. While Australian universities are ranked amongst the world's best for university research, a significant knowledge and translation research gap remains between universities and the private sector.

Building stronger collaboration between the university and private sectors to commercialise products and services aligned to Australia's digital future is one area that can be substantially developed within the domestic economy and contribute to redefining the business model for Australian Universities.

The 2022-23 Federal Budget initiative to de-risk research commercialisation in the early stages through vetting the merits of the research and providing financial support to develop proof of concepts is a step in the right direction. This would provide incentives for investors to work with the university sector and have the flow-on benefit of attracting investment capital to good ideas which would in turn lead to a greater pipeline of new innovative businesses. It would also provide direct benefits to universities, businesses, private investors and the economy as spin-out

companies and start-ups from research organisations can grow into large, innovative companies as we have seen in other jurisdictions such as Canada and the United States.

Establishing innovation precincts with a specific industry focus – such as the Melbourne Biomedical Precinct and the recently announced Sydney Biomedical Accelerator – would build significant opportunities for research commercialisation.

RECOMMENDATIONS

Incentivise closer ties between universities and private sector investors to commercialise university research.

Work with and incentivise universities, States and Territories as they establish and encourage innovation precincts and technology that connect universities with industries to create a culture of collaboration, innovation and public engagement for the development of new businesses and industries. Innovation precincts are central for knowledge-based and novel economic activities with distinct benefits stemming from the co-location of researchers and industry.



ABOUT THE AUSTRALIAN INVESTMENT COUNCIL

The Australian Investment Council is the national industry body for private capital investment in Australia. As the leading voice for the industry, the Council advocates on important policy issues, maintains a robust co-regulatory framework through a Code of Conduct, and delivers market leading knowledge and skills development programs for the private capital sector.

This work supports more than 200 members who are the standard-bearers of professional investment and include: private equity, venture capital, corporate venture capital and private credit funds, alongside institutional investors such as family offices, superannuation and sovereign wealth funds, as well as leading financial, legal and operational advisers.

FOR FURTHER INFORMATION

Contact: policy@aic.co

Published: April 2022

VISIT: [AIC.CO](http://aic.co)

Level 12, Aurora Place
88 Phillip Street, Sydney NSW 2000
T. +61 2 8243 7000

