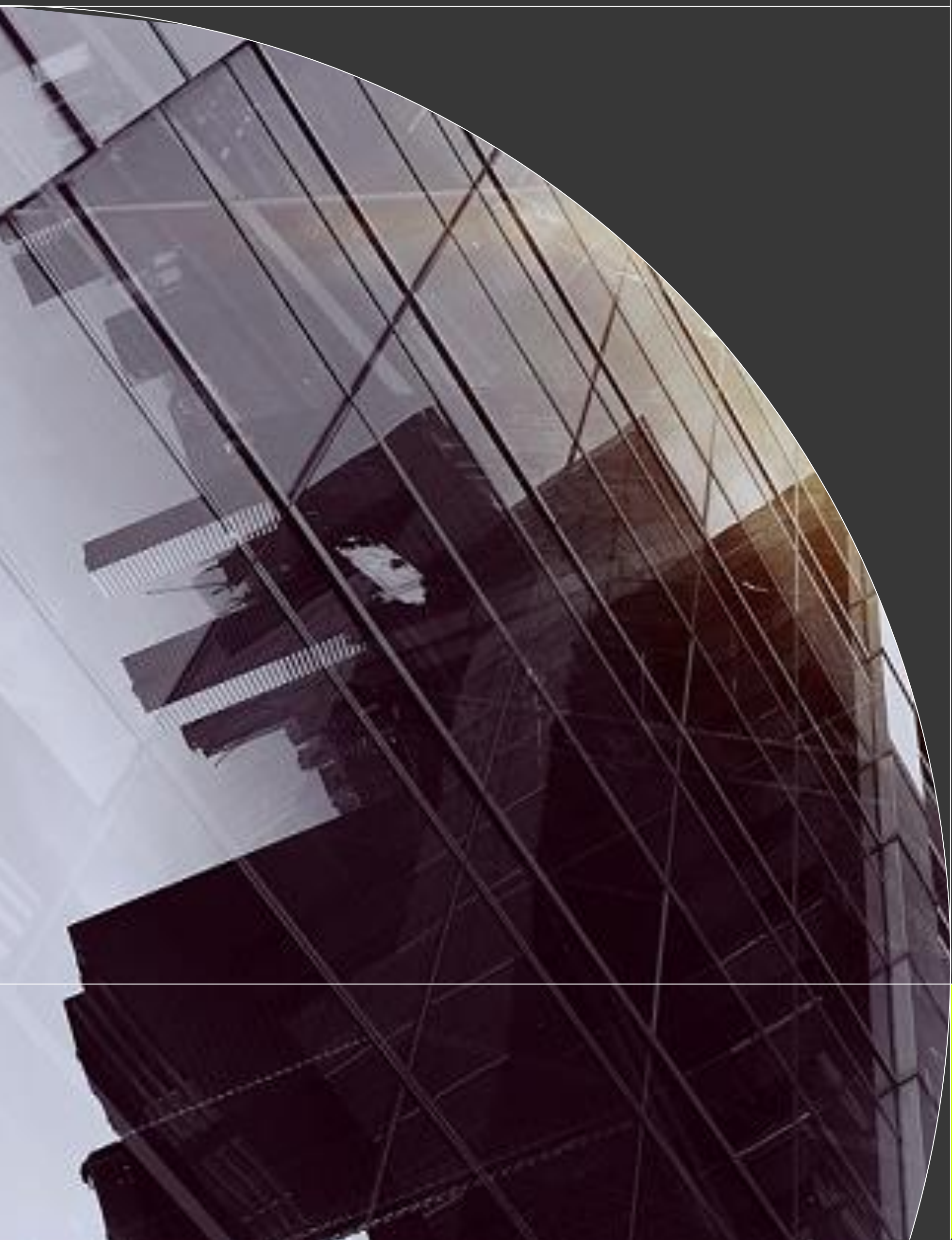
Jobs and Skills Summit – Maintaining full employment and growing productivity

August 2022



BCA
Business Council of Australia

Contents

1. Overview

The problem

- There is a lack of an agreed fact base around the interactions between unemployment, productivity and wages growth.
- Slow wages growth has raised doubts over the link between productivity and real wages. But real wages growth has slowed because productivity growth has also slowed.
  - Recent Productivity Commission analysis shows that last decade saw the slowest productivity growth in 60 years. It was also the slowest decade for incomes growth in 60 years.
- The labour market is close to full employment. The challenge is to ensure the labour market is flexible and efficient so workers can be better matched to higher paying jobs and that wage setting is aligned to productivity outcomes, including through enterprise bargaining.
  - The unemployment rate is near 50-year lows, job vacancies are at record highs and there are about as many unemployed people as there are jobs available.

The reset needed

- Agreeing at the Summit that the only way to sustainably drive real wages growth is to lift productivity growth.
  - This includes agreement over the key drivers of productivity – investment and innovation – and support for an efficient process for translating productivity gains to real wages growth, such as enterprise bargaining.
- Acknowledging that the fundamental objective of growth is to increase the size of the economy and improve living standards through productivity growth. The next objective is to then develop industrial relations and tax and transfer systems to share those benefits fairly and improve incentives to work.
- Agreeing to a definition of productivity as one that involves an ongoing process of improving the use of our human and physical capital (such as from training and upskilling workers, and changes in management practices), and innovating to produce existing goods and services in a better way or developing new ones. It is also about government policy providing an enabling environment that allows our resources to be allocated where they can create the most value.
  - The ancillary benefits of productivity growth include safer workplaces, more rewarding jobs and better living standards.
- Striving for sustainable full employment is a central objective of the government and will be a key focus of the Summit. Regardless of definitions of full employment, the focus should be on policies to drive ingenuity, innovation, and jobs and industry creation by removing the frictions that hold back new investment, damage our global competitiveness and constrain greater productivity. Work is also needed to drive greater flexibility, particularly to increase women's workforce participation. The nation needs policies that aid the diversification of the economy and positions us to take advantage of the growing Asian middle class, advances in technology and digitisation, and the global energy transition.

The actions

- The Summit establishes targets for productivity, GDP and wages growth as anchors against which to assess policies proposed during the Summit and white paper process.

- Aim for Australia to sustain real GDP growth at the long-run average of 3.3 per cent a year and wages growth above 3 per cent a year.
- Aim for Australia to return to the top five income per capita countries in the world. Australia was ranked fifth in the world in 2011 and is currently ranked 10^{th} (on a US dollar basis).
- An example of the consequences of slower productivity growth was outlined in the latest Intergenerational Report. If average annual productivity growth is downgraded from 1.5 per cent to 1.2 per cent, the average Australian would be $13,300 worse off and the budget deficit would almost double by 2060-61.

■ Agreement from government that policies should be assessed against how they would affect productivity and ultimately drive sustainable real wages growth and improved living standards.

■ Summit policies must deliver modern and efficient regulations to drive investment and innovation, while allowing businesses and workers to realise productivity benefits from these investments.

- National Cabinet should re-examine the Productivity Commission's landmark 2017 *Shifting the Dial* report and prioritise a work agenda in response. Lifting services sector productivity is critical.
- National Cabinet should identify national priorities to improve productivity, including streamlining overlapping regulations and improving state-based planning approvals processes. Incentive payments could be introduced to support reforms.
- Australians must prepare and adapt to an economy increasingly driven by technology and the shift to a net zero economy. This requires a reset in what 'industry policy' means in Australia. It is about setting the economy up for future industries and jobs, not pining for a nostalgic, idealised past.
- Modernise the industrial relations system, simplify awards, and restore the original purpose and function of the enterprise bargaining system. EBAs should be part of a system that encourages innovation and collaboration, not just an "award plus".
- This can be driven by the principles of:
  - a simpler, less litigious enterprise bargaining process that encourages innovation and collaboration
  - recognition that productivity is volatile in the near term, particularly with the ongoing effects of the pandemic and heightened uncertainty
  - greater respect for the views of the negotiating parties, and
  - expanding the coverage of enterprise agreements more broadly across the workforce.

2. Key Facts

2.1 Unemployment

- The labour market is close to what economists call "full employment", with an unemployment rate of 3.4 per cent in July 2022. This is below the pre-pandemic rate of 5.2 per cent and the lowest it has been since the early 1970s.
  - The youth (age 15-24) unemployment rate was 7.0 per cent in July 2022 – the lowest on record.
- There are 474,000 unemployed people, around half of whom typically find a job within three months.
  - Around 80,000 people have been unemployed for more than two years. They represent a growing share of the unemployed, increasing from 5 per cent prior to the GFC to around 15 per cent today.
- There are around 48,000 people who have been on JobSeeker (previously Newstart) for more than 10 years. They represent around 6 per cent of JobSeeker recipients.
- There are 480,000 job vacancies. This is the first time on record there are as many unemployed people as there are jobs available.

2.2 How does productivity growth drive real wages?

- Labour productivity is measured as output per unit of labour input (e.g. hours worked).
- Labour productivity increases the value of labour to businesses. This drives up real wages (through higher nominal wages and lower consumer prices) and labour demand.
- A business will hire an extra person when the value of what that person produces at least matches the wage paid.
- When a business invests in new machinery, equipment or the skills of its employees, they expect to increase revenues and profits (and taxes), which contributes to business employing more people and increases in output per worker. This allows higher wages to be paid as profits also rise.
- Of course, there can be differences between productivity and real wages from year-to-year or between industries and businesses. It can be affected by factors such as the tightness and/or fluidity of labour markets, delays in adjusting wages under multi-year agreements, or the efficient operation of the enterprise bargaining system. But the aggregate, economy-wide link is clear.

Examples

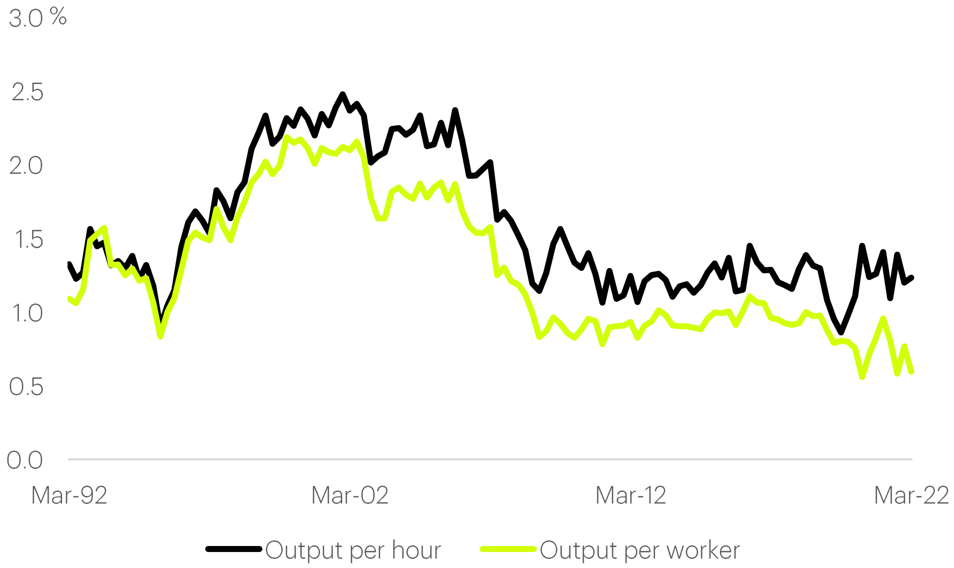
- Nurses spend a lot of time on paperwork. Better IT systems that cut down on paperwork could free them up to spend more time with patients.
- Farm Foods in Geelong supplies the sausages and rissoles we buy from Coles and Woolworths. With new equipment they can ramp up production, further tap into global markets, and hire more workers.
- Manbulloo Mangoes in North Queensland uses technology to track a mango from the tree to the table to guarantee it has come from Australia. They can use this to help export mangoes to South Korea at a price of up to $22 a mango.
- Supermarkets have evolved significantly over time through the introduction of barcodes, self-serve checkouts, apps to find items within the store and home delivery.
- The Bunnings Product Finder App saves time for customers and reduces the need for workers to guide customers around the aisles seeking out a product, freeing them up to provide valuable DIY advice and other assistance.

- BHP has developed a tool to enable machinery diagnostics from a further and safer distance, while reducing the time to diagnose faults, shortening service time and getting machinery back to work faster.
- NSW public transport commuters can catch the train by simply tapping their phone or card, compared with the previous experience of queueing to buy a ticket.
- The Aged Care Ecosystem tracks medications, personal care and meal requirements for aged care residents in real time. This means it can be readily shared with staff coming on shift, reducing handover times from up to 90 minutes to as little as 10 minutes.[1]

Recent productivity trends

- Productivity growth has slowed and plateaued for two decades. This is at the core of the recent weakness in GDP, real incomes and real wages growth in Australia.
- The weakness in labour productivity growth is even more pronounced when calculated on an employment basis compared with an hours worked basis.
  – This is due to falling average hours worked per person and points to the importance of lifting participation.
- Productivity growth has slowed across most advanced economies in recent years, but the cause of the slowdown is contested. By global comparisons, the productivity performance of Australia's goods sector is relatively strong while services sector productivity is weaker – but improving.[2]

Figure 1 **Rolling 10-year average labour productivity growth rate, hours vs employment basis**



Source: ABS.

[1] https://www.abc.net.au/news/2021-05-08/canberra-aged-care-home-sees-improvements-from-it-trial/100120756
[2] Productivity Commission 2022, *5-year Productivity Inquiry: The Key to Prosperity*, Interim Report, Canberra, July.

Productivity and real wages

- There is an undeniable link between productivity growth and real wages growth.
  - Productivity Commission analysis concludes "almost all wage growth since Federation appears to be due to labour productivity growth".[3]
  - Treasury analysis of company-level data found "productivity growth tends to be passed-through to workers in the form of higher wage growth, consistent with the idea that firms share rents with their workers".[4]
  - Further Treasury analysis of company-level data found "more productive businesses pay higher average real wages", "larger businesses are more productive and also pay higher real wages", and "exporters and foreign owned businesses have higher real wages and are more productive".[5]
  - United States Studies Centre analysis of the past 40 or so years finds a 1 per cent increase in productivity lifts real producer wages around 0.9 per cent in the long run.[6]
- The recent slowdown in wages growth reflects weak productivity growth. A key driver is weak investment growth, which is due to a range of factors such as the end of the resources investment boom, a slow recovery in confidence from the global financial crisis, a growing services sector, a change in business strategies and low risk appetite, increased uncertainty driven by domestic/global issues and policies and technological change, a high tax and regulatory burden, and energy affordability and reliability.
  - Long run productivity growth is around 1.6 per cent a year, but this is above recent trends.
  - Productivity growth averaged less than 0.5 a per cent a year the five years prior to the pandemic.
- Labour productivity is driven by investment and innovation. Each of these components has driven the recent weakness in labour productivity growth:
  - Capital deepening (i.e. how much companies invest) growth has declined as total new business investment is at an almost 30-year low as a share of GDP.
  - Multifactor productivity (i.e. how innovative companies are) has barely grown since 2001-02, and fell the past three years.
- Labour productivity has been by far the single most important driver of Australia's economic growth over the long term. It has accounted for around 80 per cent of the improvement in average income growth over the past 40 years.
- At the same time, both the Productivity Commission and the Treasury have acknowledged the importance of investment for Australia's long-run growth prospects. Over the past 40 years, investment has been the main driver of labour productivity growth, accounting for around two-thirds of the growth.
  - This means investment has driven half the improvement in living standards (average income growth) over the past 40 years.
- The weakness in the core drivers of labour productivity growth should therefore be of paramount concern. To illustrate, the contribution of capital deepening to labour productivity growth fell significantly over the past five years. If instead it had held up at its 20-year average, average incomes could be around 5 per cent higher today, or around $4,000 per year.

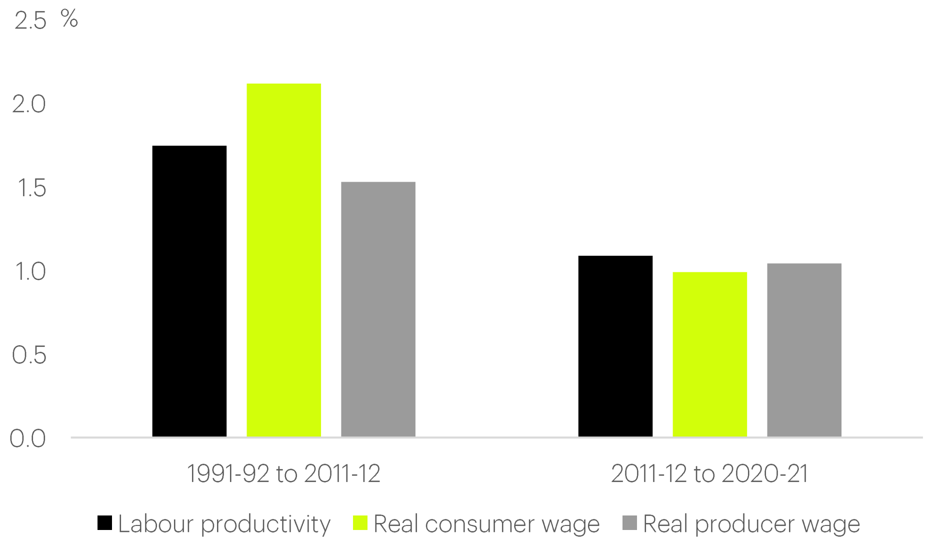
---

[3] Productivity Commission 2020, *PC Productivity Insights: Australia's long term productivity experience*, Canberra, November.
[4] Andrews D, N Deutscher, J Hambur and D Hansell, 2019, *Wage Growth in Australia: Lessons from Longitudinal Microdata*, Treasury Working Paper, July.
[5] The Australian Government the Treasury, 2017, *Analysis of wage growth*, Canberra, November.
[6] Kirchner S, 2019, *Unbroken: Productivity and worker compensation in Australia and the United States*, United States Studies Centre at the University of Sydney, March.

3. Key Issues

- The only way to sustainably grow real wages is through faster productivity growth.
  – Recent weakness in wages growth has been attributed to a range of factors, including changes in job security and bargaining power. But, at its core, the recent weakness in wages growth has been fundamentally driven by slow productivity growth (Figure 2).
  – For example, labour productivity growth averaged 1.7 per cent a year for the two decades up to the end of the mining investment boom. This compares with average annual real consumer wage growth of 2.1 per cent a year, and 1.5 per cent a year for real producer wages.
    - Real *consumer* wages are wages from a consumer's perspective and compare wages with the cost of goods and services bought.
    - Real *producer* wages are wages from a producer's perspective and compare wages with the price of their goods and services sold.
  – Since the end of the mining investment boom, labour productivity growth slowed significantly to 1.1 per cent a year, with real consumer and producer wages matching this slowdown at 1.0 per cent a year.
  – There is clear evidence of a strong link between wages and productivity growth, but limited evidence to demonstrate a fundamental breakdown of this relationship.

Figure 2 **Average annual growth in productivity and real wages**

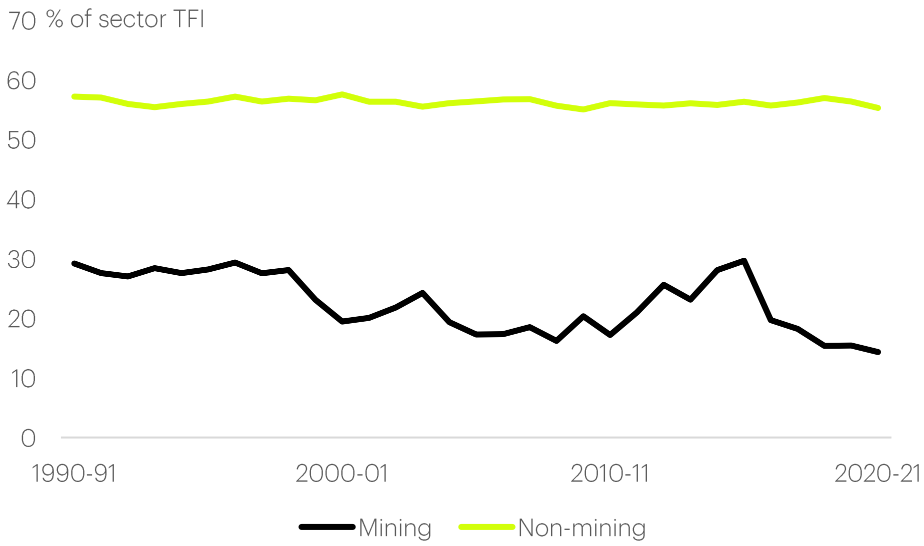


Source: ABS.

- Workers are sharing in the economic gains from growth.
  – Some have argued workers are not sharing in the benefits from economic growth, for example, because the wages share of total factor income has fallen in recent years.
  – The recent decline in the wages share of income has been driven in large part by the mining sector, with the mining wages share of mining income halving over the past five years. This reflects the increasing capital intensity of the mining sector following the investment boom, as well as the significant increase in commodity prices. By contrast, the non-mining wages share of non-mining income has been relatively stable over the same period, buoyed by more employment in labour-intensive industries (Figure 3).

- The non-mining wages share of non-mining income was 55.3 per cent in 2020-21, compared with a long-run average of 56.2 per cent.
- Mining employment is a small share of total employment. Non-mining wages accounted for around 97 per cent of total wages and around 98 per cent of total employment in 2020-21.

Figure 3 **The non-mining wages share has been relatively steady**

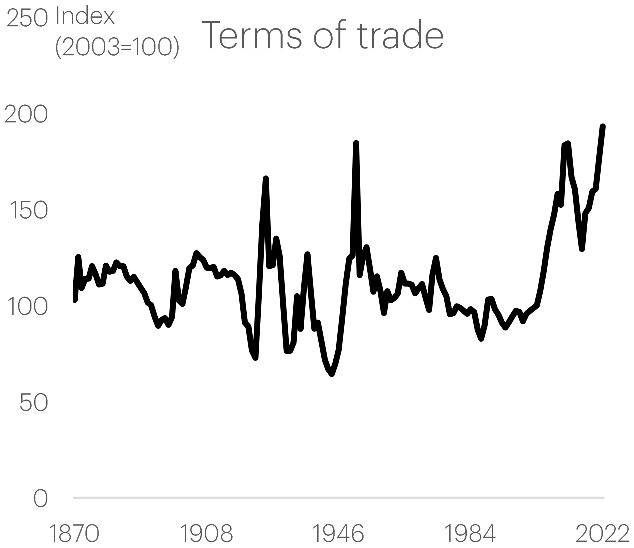


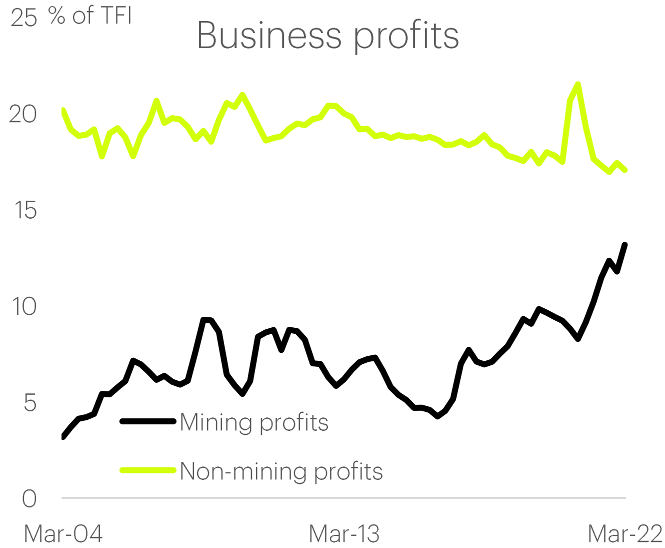
Source: ABS.

- Another way to demonstrate the impact of the mining sector on the wages share of total factor income is through the changes to mining and non-mining profit shares.
- As noted above, mining profits grew as projects came online following the investment boom and, more recently, due to the war in Ukraine and increased demand for commodities leading to record levels for the terms of trade (the ratio of export prices to import prices).
- The mining profit share of total factor income reached a record high of 13.1 per cent in March 2022, up from 7.0 per cent a decade ago. This reflects the huge investment boom and the benefits of the highest ever terms of trade, which history suggests will not be sustained indefinitely. Reflecting this, the mining industry paid $43 billion of company tax and royalties in 2020-21 and $254 billion over the past decade.[7] Long term tax decisions should not be considered in the context of short term trends and the mining sector has a key role to play in the energy transition.
- By contrast, non-mining business profits fell from 19.7 per cent of total factor income in March 2012 to 17.0 per cent today.
  - The recent spike in non-mining business profits largely reflects government COVID-19 support for business, such as JobKeeper.

[7] https://www.minerals.org.au/news/mining-industry-contributed-record-43-billion-company-tax-and-royalties-financial-year-2020-21

Figure 4 **Record high terms of trade have driven strong growth in mining profits**





Source: ABS and Gillitzer and Kearns (2005).

- Productivity growth is volatile and there is not an 'automatic' translation of productivity into wages.
  - Productivity is volatile in the short run because both output and hours worked are volatile, hence an approach that considers a multi-year period is often more meaningful and representative. Shocks such as natural disasters, supply chain disruptions, surges in demand or the pandemic can cause large fluctuations in productivity.
    - For example, productivity rose 3.2 per cent in the June quarter 2020 when Australia went into lockdown and 1.3 million Australians were stood down or lost work. In part, the productivity increase was due to a change in the industry composition of output, with lower productivity service industries closed while higher productivity industries such as mining remained open.
- Labour market flexibility and productivity
  - To strengthen the transmission of productivity gains to wages, we must ensure the labour market is flexible and efficient so workers can be better matched to higher paying jobs and wage setting is aligned to productivity outcomes, including through enterprise bargaining. This flexibility must similarly be reflected in the workplace as ultimately productivity gains will come at the workplace level, and will vary by business and industry.
  - Overwhelmingly, innovation happens at an enterprise level. 'One size fits all' approaches to wage setting risk ignoring the circumstances of each workplace including the unique features of enterprises, regional differences, international competitiveness and trade exposure.
  - A flexible and efficient labour market is one that fully utilises available workers by maximising labour force participation, minimising the unemployment rate and lowering barriers to labour mobility.

4. Priorities

- Lifting weak productivity growth is an urgent priority and a key area of focus for the Jobs and Skills Summit. This means focusing on the drivers of productivity growth – investment and innovation – through:
  - Continuing the commitment to our migration program to ensure we attract individuals with new and emerging skills
  - Investing in our people to develop the capability for success
  - Supporting new industries to modernise and diversify the economy
  - Becoming a world leading digital economy by 2030
  - Maintaining an open economy that is more competitive on the world stage
  - Improving the infrastructure delivery system
  - Driving improvements in planning approvals and streamlining regulation to support housing supply and major projects
  - Reducing frictions in doing business through consistent and modern regulations
  - Tackling tax reform for more competitive and sustainable finances, improved decisions to work, save and invest, and increased worker mobility
  - Reforming government services to improve productivity in the public sector and manage funding pressures in key programs, and
  - Repairing the workplace relations system to better support the labour market.
- A critical element of productivity growth is ensuring businesses and workers can make the most of new investments and innovations. This includes modern regulations and a workplace relations system that does not inhibit the ability to realise productivity benefits from investments and innovations.
- This must be further supported by an efficient process for translating productivity gains to real wages growth, which includes an effective enterprise bargaining system. This is through a system that lifts productivity so employers can share the dividends of better performing workplaces with their workers through higher wages and better conditions.
- A focus on driving productivity through investment and innovation will also help support employment growth and keep unemployment low. This should be further buoyed by expanding employment opportunities for all Australians, including the most disadvantaged and long term unemployed.
- The Jobs and Skills Summit should assess policies on how they perform against these measures to ultimately drive sustainable real wages growth and improved living standards.

Appendix

Table 1 **Headline facts and figures**

	Labour productivity	Real consumer wages	Real producer wages	WPI	EBAs
Latest quarter	1.7%	1.1%	-0.3%	0.7%	2.6%
Latest year	2.8%	1.7%	-1.7%	2.6%	2.6%
Long-run average	1.6%	1.8%	1.3%	3.1%	3.6%

Source: ABS and Attorney-General's Department. Note: Long-run average is 30 years, or full time series for WPI (to September 1997). Real wages calculated as compensation of employees per hour, deflated by household consumption deflator (consumer wage) and GDP deflator (producer wage). EBA averages based on EBAs approved each period.

Table 2 **Labour productivity growth by industry**

	Last year	5-year average	10-year average	20-year average
Agriculture, forestry & fishing	29.4%	4.2%	1.7%	2.3%
Mining	-5.0%	0.4%	2.5%	-0.4%
Manufacturing	1.3%	-0.6%	-0.1%	0.7%
Electricity, gas, water & waste services	-7.4%	-3.9%	-1.9%	-1.4%
Construction	1.1%	-0.9%	0.2%	0.9%
Wholesale trade	1.8%	0.2%	1.7%	1.3%
Retail trade	2.4%	1.5%	1.9%	1.8%
Accommodation & food services	0.1%	-1.3%	-0.5%	0.5%
Transport, postal & warehousing	-6.2%	-2.6%	-0.7%	0.5%
Information, media & telecommunications	-3.9%	2.9%	2.9%	3.0%
Financial & insurance services	-3.4%	-3.0%	-0.7%	0.8%
Rental, hiring & real estate services	-0.2%	0.8%	1.9%	0.3%
Professional, scientific & technical services	2.7%	1.6%	1.2%	1.1%
Administrative & support services	-4.0%	0.8%	0.2%	-0.5%
Arts & recreation services	-6.2%	-0.6%	0.5%	1.6%
Other services	2.9%	0.8%	0.7%	0.8%

Source: ABS. Note: Quality adjusted hours worked basis.

BUSINESS COUNCIL OF AUSTRALIA

42/120 Collins Street Melbourne 3000 T 03 8664 2664 F 03 8664 2666 www.bca.com.au

BCA

Business Council of Australia