

Business
Council of
Australia



MR HUGH MORGAN AC

PRESIDENT, BUSINESS COUNCIL OF AUSTRALIA

SPEECH TO THE NATIONAL PRESS CLUB

**"The Business of Reform - Challenges and
Opportunities for a
4th Term Howard Government"**

15 JUNE 2005

- Ladies and Gentlemen, Members of the National Press Club and our sponsors today, the National Australia Bank
 - I would like to begin by thanking the Press Club for inviting me to speak today.
 - It is very timely.
 - In fact, by the end of lunch, I hope you will agree that there is a real urgency to the issues I want to address.
 - I'm talking of course about economic reform.
-

- But before I do, let me state why the companies I represent as President of the Business Council of Australia have such a vital interest in economic reform.
- All the BCA's Member Companies are modern manifestations of the corporation – that much maligned but seemingly little understood concept.
- Yet they are at the heart of an economic system which has provided Australians and other citizens of Western democracies with an unprecedented level of prosperity.

- Through tax payments, job creation and goods and services provided, corporate Australia has made a magnificent contribution to the welfare of Australians.
- As an organising principle of capitalism, the corporate structure remains highly successful because it is still the most effective way of aggregating capital, managing risk and promoting innovation.
- Member Companies of the Business Council – which represent Australia’s leading 100 corporations - collectively account for some 20 per cent of the output of Australia’s economy.
- They employ directly a million Australians and indirectly, probably three times that, when their dealings with suppliers and small businesses are taken into account.
- Together, BCA Member Companies account for a third of all Australia’s exports and return \$18 billion a year in dividends to shareholders, superannuation funds and savings institutions.
- Drawing on economies of scale, they provide a wider range of goods and services to consumers, suppliers, employers and shareholders than would otherwise be possible.

- In a global economy, they are an important conduit for the rest of the world.
- The sheer scale of taxes paid by corporations is fundamental to every Australian's well-being.
- The corporate tax take is the second biggest revenue stream to the Commonwealth, and the fastest growing.
- In the financial year 2001-02, the corporate tax take amounted to 27 billion dollars.
- As the first chart in the handout provided shows, Treasury's projections for the next financial year show a total corporate tax collection of 48 billion dollars.
(Chart 1 - Company Tax as a Percentage of GDP)
- That figure itself equates to the cost of most of the new tax cuts and social services announced over the past 12 months and more.
- We are not expecting gratitude – but don't think that this high company tax burden goes unnoticed by the global investment community.
- I will say more about this later.

- In summary, the modern corporation is intrinsically linked to the prosperity and well-being of Australian society.
 - The BCA, as the representative body of Australia's corporate sector, sees itself as having prime responsibility in advocating policies that seek to lock in the conditions for continuing economic success.
-

- Economies that support and encourage competitiveness are invariably those that are the most successful.
- As the pace of globalisation increases, the reality is that Governments are in competition with each other.
- This means the primary role of Government is to establish and foster the conditions for an economy that can compete effectively with the rest of the world.
- The tools at their disposal are many – a tax system that rewards and therefore attracts investment and skills, flexible workplace relations and an efficient scheme and system of business regulation.
- In other words, the challenge for Government is not to simply redistribute the rewards of growth.

- It needs to be at the forefront in driving changes that enable the economy and business to remain competitive.
 - We have done extremely well as a nation because successive Governments over the past 20 years have put in place policies that have allowed the country to compete successfully in the global economy.
 - Above all, these policies have acknowledged that aggressive global competition amongst business and economies – competition for investment and labour - is a fact of modern life.
 - In many ways, Australia not only has to keep up, but run harder than our competitors.
 - We must overcome the tyranny of distance AND THEN be able to compete head on in global markets.
 - If you draw a 10,000 kilometre circle around Sydney you will capture 28 per cent of global GDP.
 - Do the same for London and businesses there have access to 94 per cent of global GDP.
-

- Due in large part to reforms that have focused on improving our competitiveness over the past two decades, Australia's economy has grown by an average 4.3 per cent a year.
 - That means the economy is more than 40 per cent bigger than it was a decade ago.
 - Since 1995, over 1.8 million jobs have been created and the unemployment rate has fallen from over 8 per cent to below 5.5 per cent.
 - Over the same period, youth unemployment fell from nearly 20 per cent to below 15 per cent.
 - Real wages during that period have risen by almost 20 per cent.
-

- Yet, perhaps because of Australia's unbroken record of growth, we now seem to have forgotten the vital links between reform, competitiveness and prosperity.
- Policy directions that helped achieve unprecedented levels of growth and prosperity are now more likely to be seen as pandering to the big end of town.

- Few people seem to recognise competitiveness is the reason why we are here in the first place and crucial to our continuing prosperity.
- The reality is no economy can ever achieve a state where ongoing competitiveness can be taken for granted.
- Success, or otherwise, is a direct result of the commitment and efforts of policy makers to remove impediments to growth and increasing competitiveness.
- Now, I acknowledge that given the community feels that things are doing well, one has to ask why the BCA wants to focus again on a new reform agenda.
- On the surface, Australia's current prosperity, high employment, low interest rates, general business performance and a host of other factors make it difficult to convince people or Governments of the need for yet more change.
- However, beneath the surface of growth and prosperity a number of blockages and imbalances have emerged.
- If left unchecked, they are likely to become major roadblocks to future prosperity and growth.

- So, see this as more about an opportunity ahead to lock in prosperity, not a threat, an opportunity.
 - The test for Australia's policy leadership, including the BCA, is to judge performance not on where we've been, or even where we are – but where we are heading.
-

- On that note, two key international reports on the performance of Australia's economy point to a worrying decline in our overall competitiveness.
- The annual World Competitiveness Yearbook was released recently by one of the world's leading business schools, Switzerland's IMD (Institute for Management Development).
- This report is used by Governments around the world to promote their economies as the best places to invest.
- It showed that despite being the most resilient economy in the world, Australia fell from a ranking of 4th in 2004 to 9th in 2005.

- A similar conclusion can be found in the 2004-05 Global Competitiveness Report of the World Economic Forum.
- Australia fell in this report from a ranking of 10th in 2003 to a ranking of 14th in 2004 in the Growth Competitiveness Index.
- These are the reports that the international investment community reads. They are external reports that put us on notice that action is needed.
- The question is,
- Well, many of you will be familiar with the significant policy work initiated since October of last year and published over the past few months by the Business Council of Australia.
- For those who aren't, we have focused on four major areas.
- They are taxation, infrastructure, industrial relations and business regulation.
- The four areas our Members Companies believe are fundamental to Australia's future competitiveness.
- They build on the work which has been a focus of our work at the BCA in recent years.

- In 2004, the BCA focussed in particular on improving the quality and outcomes of our education and training system.
- Many of our recommendations received strong bipartisan support, particularly in an Election year.
- We have also focused on enhancing our international trade and investment relationships – contributing to and supporting the negotiation of important free trade agreements including with the United States.
- Let me emphasise that the four policy areas the BCA is now focussed on represent an integrated package.
- They need to be implemented as a whole, not ‘cherry picked’ by opportunistic politicians.
- Each policy and its recommendations has been thoroughly researched and backed by an independent assessment.
- I want to stress that our policy proposals do not represent a log of claims, but a clear statement of the community task ahead of us.
- Importantly, each of the policies has sought to benchmark Australia’s current performance against that of our key competitors.

- In each case, we have found to be lagging.
-

- Starting with **workplace relations**, from 1990 to 2003 labour productivity in Australia grew by an average annual rate of 2.3 per cent.
- This was a good outcome by world standards.
- Despite these increases, productivity levels remain lower than a significant number of our economic peers.
- In recent years, Australia's productivity has begun to slow dramatically.
- So now again I refer you to the second chart in the handout which shows a significant drop-off in Australia's productivity growth – in fact, the latest figures show we are going backwards. **(Chart 2 - Australia's Productivity Record)**
- Our level of productivity compared to others ultimately determines our competitiveness and relative standard of living.

- The gap between Australia and its peers highlights that we have to do better.
- The Government's recently-announced changes to workplace relations will go a long way to making sure the productivity gap between Australia and its competitors is narrowed.
- As such, they deserve the applause of business and the support of the community.
- The reforms continue the process of deregulation and simplification of agreement-making between employers and employees which started 20 years ago.
- Along with higher levels of productivity, they will mean fewer barriers for employers to create jobs.
- More flexibility will lead to higher participation, particularly among those groups in the workforce Australia will depend on to offset the impacts of an ageing population and skills shortages.

-
- Yet these first significant changes to workplace relations in a decade are only one part of the reform equation.

- The BCA's policy agenda has highlighted significant lags in our competitive performance in the other three areas.
- In **regulation**, business competitiveness is under real threat by a rising and largely uncontrolled tide of red tape.
- This tide is soaking up massive amounts of productive resources and creative energies among our larger corporations and small and medium-sized businesses.
- The figures which are outlined in the BCA's *Action Plan for Regulation* are simply staggering – as Chart 3 of the handout demonstrates. **(Chart 3 – Pages of All Australian Legislation Passed Each Decade)**
- Our *Action Plan* calculates that the number of new laws and regulations is now increasing at 10 per cent a year – three times faster than Australia's average rate of economic growth.
- The Commonwealth and State Parliaments added 33,000 pages of new laws, rules and regulations in 2003 alone.

- Half of the legislation passed by the Commonwealth Parliament since Federation has occurred in just the last 14 years.
- The NSW Parliament produces on average 300 pages of new laws, rules, regulations and by-laws each week it sits.
- Queensland added 8,700 pages of new laws and rules just in 2003.
- This regulatory blow-out not only diverts huge levels of private sector resources, but also massive amounts of public wealth on compliance and policing.
- It is ironic that compliance is added to GDP. This is phony – it should be subtracted, not added.
- The level of regulatory obesity is not just an Australian problem – it is a Western disease.
- The 2004 survey of global CEOs by PricewaterhouseCoopers found that over-regulation was considered to be the biggest threat to business growth prospects.
- Many countries such as the UK and Netherlands are already addressing this issue.

- Given the stranglehold of red tape over many other Western economies, countries that deal with the problem head-on will gain a significant competitive advantage.
- We already start from a significant disadvantage.
- Our small and disparate markets already weigh on cost structures and competitiveness.
- That is why it is incumbent on Australian Governments at all levels to address the problem now.
- In Australia, the problem is such that the sheer volume of regulation has overwhelmed the scrutiny and accountability mechanisms that are supposed to ensure quality regulation.
- As part of its *Regulation Action Plan*, the BCA is proposing a three-step process to reform the model of regulation-creation.
- Government regulation should actually serve the community, not the other way around.
- We say Governments should:

- firstly, make sure that all new regulation fully takes account of costs to business and is subject to regular review;
 - two, clean up the stock of existing regulation to improve or eliminate unnecessary, duplicate and outdated regulation; and
 - three, tackle the overall problem of lack of coordination between the Commonwealth and States, and between States themselves.
- The details of our recommendations can be found in the BCA's Business Regulation Action Plan.

-
- Turning to Australia's **tax system**, business acknowledges the significant work on tax reform the Government has undertaken.
 - The GST and the reform of numerous business taxes as part of the Ralph report have significantly improved our competitive position.
 - The measures announced in this year's Budget, particularly moves to reduce the tax burden on skilled workers, were also welcome.

- As I said before, the modern day reality is that Governments are no less in competition than business for labour, capital and markets.
- Tax is the one area which Governments can proactively structure to enhance competitiveness.
- Other Governments around the world are building far more competitive tax policies than we have had to confront in the past.
- Our key regional neighbours have long ago ensured that they are highly competitive but the Europeans are now recognising the necessity for tax reform.
- Poland has just announced that it will introduce a flat tax system by 2008 at 18 per cent, on all personal income and corporate profits.
- And if they get voted out that's OK because the Opposition is proposing a 15 per cent flat tax.
- Romania's new Government has implemented a 16 per cent flat tax on personal income and company profits.
- Russia now has a corporate and small business tax rate of 24 per cent and a flat 13 per cent on personal income tax.

- The Netherlands is planning to lower its corporate tax rate to 26.9 per cent in 2007.
- Germany's Economics Minister has now urgently requested a tax reform blueprint in recognition that the nation's heavy tax burden is simply not competitive.
- The US Government has removed Federal tax on all dividends.
- And these are just some of the recent moves in the global market.
- The BCA's *Taxation Action Plan* which we released in April demonstrates that - like regulation - Australia's tax system continues to carry major competitive weaknesses.
- I illustrated earlier the increasing importance of Australia's corporate tax to Government, and therefore to the wider community.
- Increasing evidence suggests that despite the focus on our headline corporate tax rate, Australia's overall corporate tax burden is way above that of our peers.
- Look at Chart 4 of the handout - Australia's corporate taxation burden represents more than five per cent of GDP. **(Chart 4 – Corporate Income Tax Burden)**

- In the case of most of our OECD competitors, this figure is 2 or 3 per cent.
- If Australia had the same company tax burden as the OECD average, the company tax take in 2004 would have been nearly \$16 billion lower than it was.
- Let's pause on that for a moment.
- In other words, it is the sum of taxation rather than its components that determines whether Australia's tax environment for business is competitive.
- Let me be clear - less competitiveness ultimately means smaller returns - which in turn eventually means a reduced tax take for Governments.
- A major review of corporate taxes is only one of the fundamental debates we need to have about our tax system.
- We need a major simplification of the Tax Act which now totals some 10,000 pages compared with 3,000 pages ten years ago.
- We also need a far more competitive personal tax system.

- In a world where competition for skilled labour will increasingly determine a nation's economic performance, we cannot be wedded to tax structures and rates without considering their impact on the economy's competitiveness internationally.
 - We need to move beyond the piecemeal changes and the periodic catch-ups that characterise the current tax debate and put all our cards on the table now.
-

- The final area defined by the BCA in our policies is **infrastructure**.
- Infrastructure represents the basic building blocks of the economy.
- The state of our energy, water, transport and urban infrastructure systems is directly related to our capacity to support high levels of growth.
- Unlike other policy areas where problems and shortfalls can be addressed relatively quickly, infrastructure requires long-term planning.
- If we wait for the bottlenecks to fully manifest themselves, we have already missed the opportunity

to plan and develop solutions that invariably take some 10 or 15 years to put into train.

- The problem for Australia is that the warning signs are already there.
- The BCA's *Infrastructure Action Plan* found that by 2025, without major reform most key population centres will be demanding more water than is currently available and the story is the same for energy.
- By 2020, the gap between energy supply and consumer demand is estimated to be a gap of some 50 per cent.
- The amount of new investment required in developing additional energy supplies totals somewhere between \$30 and \$35 billion.
- As our report demonstrates, Australia's road and freight transport systems are straining and the situation if left alone will only get worse.
- By 2020, road freight movements will grow by 65 per cent.
- This will mean 900,000 more truck trips in and around our urban and suburban areas.

- The cost to the economy of traffic congestion will increase to an estimated \$30 billion a year by 2015 – compared to \$13 billion currently.
- The Federal Government recently announced a report on export bottlenecks.
- The BCA welcomes the report as a first step to addressing these issues.
- But the problem is not confined to export infrastructure.
- As the figures show in Chart 5 of the handout show, the shortfalls and problems are endemic across most of the economy's production and supply chain. **(Chart 5 – Australia's Infrastructure Shortfalls)**
- As a result, we need more than incremental or one-off solutions focused on the export end of the economy.
- Australia's economy has an infrastructure asset base worth an estimated \$300 billion.
- Yet, there is no coordinated plan or policy to make sure the country's infrastructure keeps pace with the economy.

- This points to a deeper issue about the lack of transparency and accountability regarding the capacity and health of Australia's infrastructure.
- The BCA's report called for a committee of COAG to require an audited and transparent report on the health of existing infrastructure assets to be published.
- We are pleased that COAG addressed this issue.
- COAG recently responded with a five-year audit of major infrastructure to address this information vacuum.
- The BCA, however, called for all infrastructure providers to make available a report on the health of their asset base – preferably on a three year rolling basis.
- A five year audit as proposed by COAG won't effectively deliver better systems of planning and investment.
- Like business, Governments should adopt shorter audit timeframes to ensure everyone has a clear understanding of Australia's infrastructure capacity at any point of time.

- We only need to remember how quickly the well-publicised bottlenecks on ports occurred to understand how quickly demands on vital infrastructure can occur.
- Business will help where it can – it has the investment resources to play a much bigger role in the funding of new infrastructure.
- But ultimately, no-one else can resolve these strategic and policy issues but Governments.
- Only when there is publicly available, up-to-date information can we have an informed debate and hold Governments accountable for their infrastructure policies and decisions.
- Because these issues extend beyond one electoral cycle, full accountability, transparency as well as bi-partisan support is absolutely vital
- This is why the BCA's *Infrastructure Action Plan* has called on Governments to form a special Federal-State body charged with responsibility for addressing the problem.
- The response from our political leaders is that there is no crisis at the moment.

- But it's a bit like someone on an empty road, watching a large truck approaching from a long way off...
 - We know that we can move out the way and that there's no need to panic.
 - But we also know that if we stay where we are, we're going to get run over.
 - Like most things in life....it's all about timing.
 - And that's where the urgency comes from.
-

- Few people presented with all of the facts would argue against the need for the reforms I have outlined.
- But many more do not appreciate that we have a limited time-frame for effective change.
- Each of the issues I have raised – tax, workplace relations, regulation and infrastructure – speak to a broader issue, one which I will briefly touch on here.
- Dig deeply into any of the four issues and you will quickly discover dysfunctional Federal-State relations are central to the problem.

- Our system of Federal-State relations is complicating almost every aspect of policy making through a duplication of funding, compliance and service provision.
- It inhibits transparency, increases costs and reduces accountability and effective decision making.
- The BCA is not arguing for major constitutional change – that is neither practical nor, I suspect, desirable.
- We are, however, arguing that we can and should do better within the parameters of the current system.
- The recent COAG meeting demonstrated the need for real reform and improved governance in Federal-State relations.
- The meeting was hailed as a major step forward.
- Yet, what other forum would be considered a major success simply because no-one walked out and the proponents spent fewer than two hours discussing key issues food by the nation?
- The BCA's strong view is that COAG remains the best vehicle to achieve reform.

- Yet we need more accountability, more transparency and more effectiveness in the decision-making process.
- Most of all, we really need far greater urgency.
- We take heart from the COAG communiqué which stated - and I quote ... “Australia’s productivity performance is under threat with further reform essential if the economic expansion of the last 14 years is to continue.”
- The BCA will play an active role and continue to make strong representations to the various COAG processes now underway to address issues such as skill shortages, infrastructure and national competition policy.
- We all have a responsibility to make sure reform does not become on the one hand, an internal bureaucratic process, or on the other sidetracked by political bickering.
- The important point here – and there could be no more appropriate place to make it than at the National Press Club – is that we all have a responsibility to put aside entrenched positions and partisan views to reach agreement on a program of real reform and action.

- The media is playing a vital role in this discussion and I would urge you to continue to do so.
- It is only through the media that ordinary Australians gain access to the underlying facts that show why change is necessary.
- By all means, let's criticise our politicians if we think they're getting it wrong....but we must also provide support when they show policy leadership.
- The current Government should be given credit for progressing a number of important reforms.
- They include strong leadership in securing bilateral trade agreements with key trading partners which will help position Australia in major markets over the long term.
- Reforms to Australia's competition laws, higher education structures, as well as reforms to personal, business and international tax arrangements have all played a major part in Australia achieving its current strong economic and fiscal position.
- Governments which articulate a vision for the future and have the courage to do what is necessary to achieve it should be encouraged.
- We can argue about the detail.

- But for goodness sake let's agree that we need to lock-in prosperity for the long-term.
- Of course business also must play a role which is why the Business Council has been happy to help lead this debate.
- We've set out a way forward, but this is not just about us getting our own way.
- We're delighted if someone has a better idea to meet the challenges we face as a nation.
- An integrated reform program will not only lock in prosperity.
- It will also help avoid the prospect of sharp downturns experienced by other countries that have failed to sustain growth momentum.
- Japan and the United Kingdom in the early 1990s and in the United States earlier this decade were largely in the same position as Australia finds itself now.
- Like Australia, all three economies experienced strong productivity growth in the years prior to recession..

- While we must be cautious about overlaying one economy's track record with another, the parallels are instructive - as the final chart in the handout shows **(Chart 6 – A Tale of Three Recessions)**.
- In each case, a so-called miracle economy failed to sustain prosperity because it chose not to address the issues that would take it to the next level of growth.
- It is vital that we ensure that Australia undertakes reform.
- Community support for change will be crucial.
- So is leadership.
- There is no option but for these proposals to be considered by Government – urgently.
- Thank you.