ASR's Response to the Australia in the Asian Century Issues Paper

Introduction

Thank you for this opportunity to contribute to the Asian Century White Paper process.

Australia has an historic opportunity to be a high value services provider to the Asian region. This timely review is an excellent opportunity for Australia to build the policy framework for success, based on sound economic analysis. In turn, these policies need to continue to promote the development of a 21st Century economy for Australia, with strong domestic and export growth in services, able to take full advantage of the Asian Century.

To achieve this, we need to get our domestic and international policy settings right.

1. **Understand the potential of our services sector as the basis of an export industry**
   - Services already represent 80 per cent of the Australian economy and 85 per cent of employment.
   - The sector is growing: employment in services has grown by 2.3 million since 2001
     - In professional and technical services, Australian total wages and salaries exceed the total for the manufacturing sector;
     - Australia's exports of professional services are double the value of Passenger Motor Vehicles exports;
   - Employment in manufacturing and agriculture has contracted; jobs growth in resources sector has been incremental.
   - Services exports exceed those of manufacturing (in 2010-11 Exports of Manufactured goods were $ 41.3 billion, while exports of services were $50.6 billion[1]).
   - China has already become the world's most competitive manufacturing economy with a supply chain, technical resources, skills and scale that are unrivalled, and is set to become the world's largest services market. Our services exports can tap into this economic activity to help build a resilient and sustainable Australian economy.
   - Services export and services development strategies are becoming common across Asia.
   - The Federal Government should work in partnership with business to develop a Services Roadmap to identify opportunities and impediments and to raise public understanding.
     - ASR in partnership with ACILTasman and in consultation with leading services businesses and key Australian government departments has scoped the work involved in undertaking a Services Roadmap in the report *New Economic Challenge: responding to the rise of services in the Australian economy*.

[1] Department of Foreign Affairs & Trade, Composition of Trade, Australia 2010-11, Market Information and Research Section, December 2011.

2. **Improve Australia's readiness to capitalise on the incredible opportunity provided by our proximity to Asia and the demand in Asia for services.**
   - The rise of China and economic growth elsewhere in Asia presents substantial policy challenges for Australia in terms of national security, trade and a range of issues.
     - The Asian Century presents challenges to our longstanding ties to Europe and the United States.
     - But there is a strong presumption in Australia that our economic future is tied closely to Asian growth.
     - Many Australians are already engaged in services business with Asia and this will increase.
   - Demand for services from the expanding Asian middle class will increase well above existing trend lines.
   - Supplying services (including tourism, education, finance and high value niche manufacturing services, mining services and agriculture services) are reliant on understanding and meeting customer needs, and as Asian services markets mature continued success depends on:
     - Greater ease of people to people contact and business linkages, through improved visa, professional recognition and business establishment rules;
     - Higher level of Asian cultural and communication skills across the Australian community.
   - Asian supply of services to Australia will increase – nearly all Asian countries have services export strategies and rapidly growing skills and capabilities in services;
     - Increased services imports and inwards investment are important in building the business and people linkages to support increased services trade with Asia.
   - China will be an important source of capital for Australia, which is a net capital importer.
3. **Align domestic and international policy settings to drive innovation and growth in the sector.**
   - Although our manufacturing base is under pressure, our high value services are world class and have immense growth and export potential.
   - International efforts like the International Services Agreement being led by Australia and the United States in the WTO need to be inclusive of our regional trading partners China, India, Korea, Japan and the ASEAN nations.
   - A priority for the Australian government should be on balancing the regulatory and other settings around Chinese and other Asian investment and commerce in Australia, with the need to promote viable, sustainable links across a range of sectors to promote mutual commerce. This should include:
   - Building stronger business to business links;
   - Excellent university and research linkages are a platform to do this;
   - Appropriate facilitation and management from the Commonwealth public service;
   - An efficient, productive and innovative domestic services sector is the soundest base on which to build services export success:
     - The domestic reform agenda needs revitalisation;
     - Information and Communication Technology capabilities and infrastructure are a platform for services trade growth.

The Australian Services Roundtable

The Australian Services Roundtable is the peak body for the services industries in Australia.

The ASR brings together Australia's leading services firms. We provide a forum for dialogue for the services sector, including financial services, professional services, tourism, energy, education, the research community and industry.

We are committed to raising the profile of the sector and advocating for sustainable policy responses that drive innovation and productivity.

Sectors represented include financial services (banking, insurance, securities, fund management), professional services (accounting, legal, engineering, architecture), health services, education services, environmental services, energy services, logistics, tourism, information technology, telecommunications, transport, distribution, standards and conformance, audio-visual, media, entertainment, cultural and other business services.

Key Contact

James Bond
ASR President
M: 0423 394 533
E: jbond@fsc.org.au

Andrew McCredie
Executive Director
M: 0408 253 660
E: exec@servicesaustralia.org.au

ASR Board

President: James Bond (Economist, Financial Services Council)
Vice-President: Stephen Jaggers (Partner in Charge, Canberra, Mallesons Stephen Jaques)
Treasurer: George Karagiannakis (Senior Adviser External Relations, Insurance Australia Group)

Directors

Jonathon Cartledge (Director of Policy, Consult Australia)
Alan Dormer (Science Leader, Government and Commercial Services, CSIRO)
Jane Drake-Brockman (Managing Director, Tesol Pty Ltd)
Kaaren Koomen (Director Government Relations, IBM Australia and New Zealand)
Philip Kelly (Managing Director, Northcote Management Services Pty Ltd)
Pamela Kinnear (Director Policy and Analysis, Universities Australia)
Michael Morgan (Director, Kreab Gavin Anderson)
Gary O'Riordan (Deputy CEO, Australian Tourism Export Council)
David Parken (Chief Executive Officer, Australian Institute of Architects)
John Richardson (Director, Cox Group)
Iain Sandford (Special Counsel and Director, International Trade Group, MinterEllison)
Kee Wong (Managing Director, e-Centric Innovations Pty Ltd

Responses to Issues Paper Discussion Points

Discussion points on community engagement

There is a need for community engagement about the Asian Century. The best way of signalling the significance of the transformation involved for all Australians is through a major symbolic initiative such as compulsory Asian language teaching in all primary schools[2]:

- Community interest in abstract messages that seemingly don't connect to their lives is limited;
- Government resources needed to develop an excellent Mandarin teaching program for primary schools would be substantial – the public debate would engage the community, and would involve technology but would be outcomes rather than technology driven;
- School children would 'educate' parents, raising community understanding of Asian culture, and receptiveness to information about the Asian Century.

Over the coming decades Asian economies are expected to liberalise their services markets so that they become the major global services market, and also Asian-based services businesses are expected to become the major suppliers of international services. Australia already has many internationally leading services businesses, so the growth of Asian services trade should be good for Australia.

The key risk that services companies raised with ASR in workshops on international services trade sponsored by DFAT in late 2010 is that public understanding of these issues is low. Australia's competitive position within global services supply chains is based on our capacity to manage and coordinate multinational and multidisciplinary teams and our no fuss outcomes orientation. Business concerns about the potential for inflexibility in relation to supply chain management, eg political or workforce insistence on particular activity being done in Australia, is a factor impeding development of Australia as an international high value services centre. There is very little public understanding and media discussion about services and these issues, and much that does occur is poorly informed:

- There are no regular academic or media commentators on services; and Australia lacks university schools of economics with a strong services focus or research interest, even though services comprise 80 per cent of the Australian economy;
- The intangible nature of much of services business means that there are difficulties in collecting and interpreting services data, particularly trade, investment and productivity data – these difficulties should not be so significant as to prevent a better public discourse about services, but no priority has been placed on addressing them;

[2] The symbolic significance of this would resonate in Asia as much as in Australia. It would demonstrate the strength of Australian commitment to realising the vision of being a high value services provider to the region. Ideally schools would teach Mandarin, but in deference to Australian tradition of relative school autonomy, schools could choose an alternative language if they so choose. Note Swedish introduction of universal English language teaching in schools in the 1960s and Chinese introduction of English language teaching in the 2000s in both instances have been remarkably successful, not just in terms of language skills acquisition, but also in symbolising and accelerating the broader societal changes needed to succeed in the global economy.

- The inconsistent reporting of the size of Australia's services economy including by Commonwealth Government Departments does not help public understanding and debate;
- ABS's publication 5204.0 - Australian System of National Accounts, Table 5. Gross Value Added (GVA) by Industry, Percentage of GVA at basic prices, current prices, columns DM-EG should be the agreed source of information about industry share of the economy, see table 1 below, and if for particular purposes some services sectors such as construction and/or ownership of dwellings are to be excluded from the definition of services, then it should be made clear that that is what is being done.

Table 1: Services Share of Australia's Economy

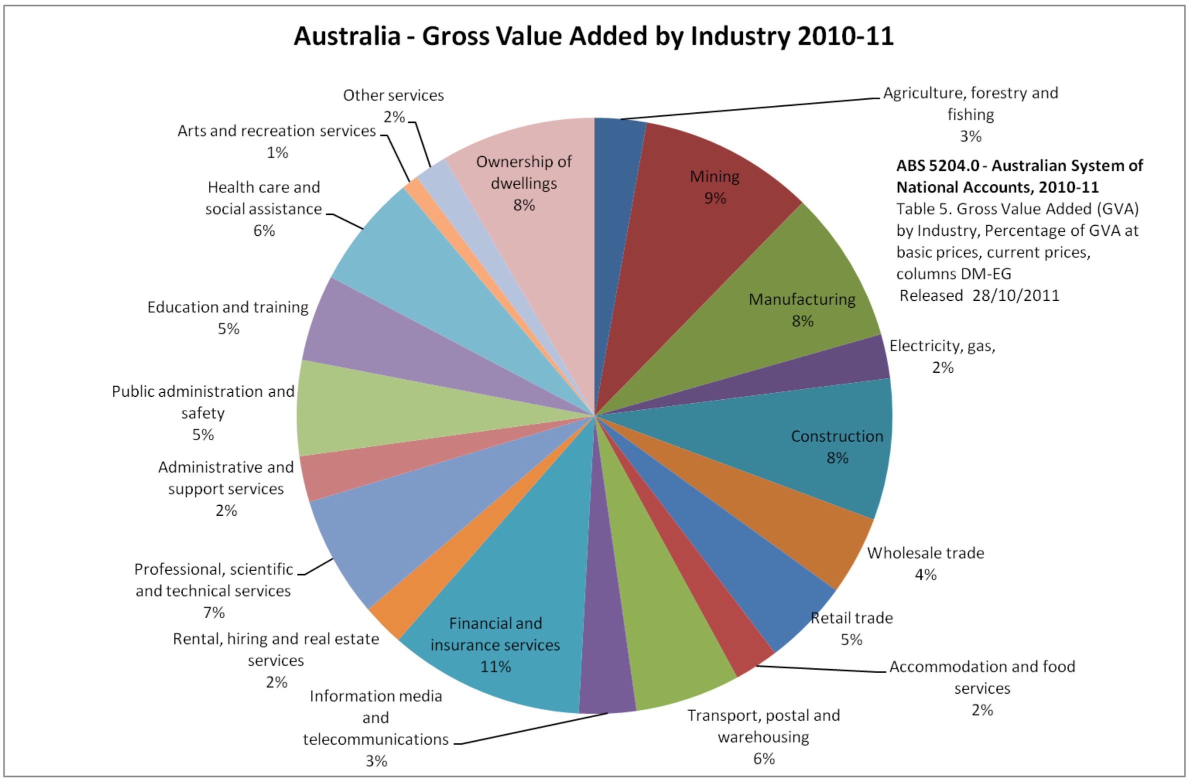
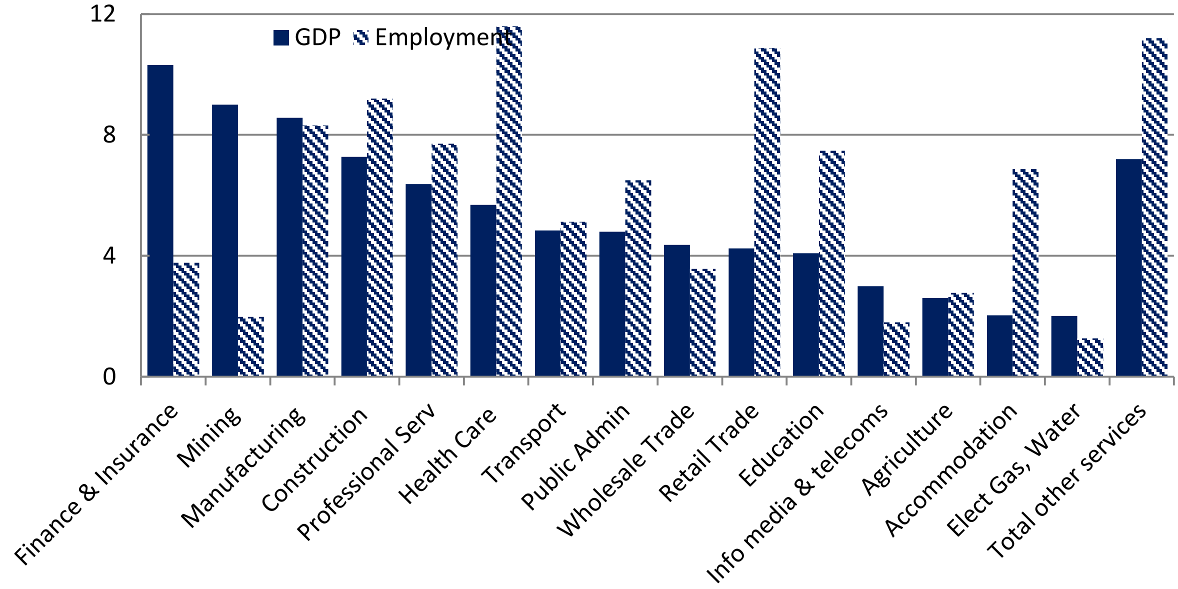


Table 2: Industry Share of GDP, Employment, per cent



Services represent around 80 per cent of the Australian economy and 85 per cent of employment, including 93 per cent of graduates. Over the past decade, employment in services has grown by 2.3 million jobs compared with negative growth in manufacturing and agricultural jobs and minor growth in resources jobs

Services are also the global economy's largest sector and the largest employer. The development of information and communications technology has reduced the cost of exporting services. And the pent-up demand for services of all types can be a principal driver of growth worldwide, for decades to come. Lack of public understanding in Australia, in Asia and worldwide has meant that global services trade reform has languished. A recent report commissioned by the United States Coalition of Services Industries has set out the public case for services trade liberalisation through an International Services Agreement.[3]

Public understanding and communication of the breadth of issues requires a whole of services approach. To do otherwise risks limiting community engagement to just a few sectors (eg education, tourism, financial services), whereas in fact there are implications of the Asian Century for all of the 85 per cent of Australians employed in the services sectors. Furthermore, the detail involved in specific services sectors acts to obscure and confuse the high level whole of services messages that need greater public attention and understanding. We note and welcome services strategies in specific services sectors eg financial services and tourism with international education set to join this list, but this work should be seen as providing a sound base on which to build an overall message about services, not an alternative to doing so. Note the language used in relation to international engagement in the goods sector (ie exports of manufactures, resources, food) typically is dismissed by services employees as not being relevant to them.

---

[3] Edward Gresser 2012, Services Trade Liberalization as a Foundation of Global Recovery, Director, Progressive Economy Project, Global Works Foundation for the Coalition of Service Industries February 24, 2012

Services export and services development strategies are becoming common across Asia and there is value in Australia undertaking a Services Roadmap to identify opportunities and impediments and to raise public understanding.[4] ASR in partnership with ACILTasman and in consultation with leading services businesses and key Australian government departments has scoped the work involved in undertaking a Services Roadmap in the report *New Economic Challenge: responding to the rise of services in the Australian economy*. ASR is working in partnership with the South Australian Government on developing its Knowledge Intensive Services strategy.[5]

What are the defining elements of the 'Asian Century'? What is new and different about what is happening in Asia across economic, political, strategic and social dimensions?

Services are the defining economic and business element of the Asian Century as the structural change occurring in Asia, particularly China (following that of Japan, Korea, Taiwan, Hong Kong, Singapore, Malaysia), but also to a lesser extent India and ASEAN counties more broadly, involves the development of an urban, educated, middle class, resulting in a services dominated economy. This impact is further amplified by the growth of services in all economies, including developed economies like Australia. There are a number of reasons why services have grown in the 21st Century to be the dominant sector of all modern, advanced economies, including:

- growth in financial and legal services resulting from increased use of markets to allocate resources, particularly resulting from Privatisation/Deregulation/Outsourcing of services functions;
- growth in international trade and particularly investment by services businesses
    - growth in international services value chains (slower initially to occur in services than in manufacturing, but has accelerated in 21st century);
- expansion of knowledge and the business capacity to capture value from knowledge – including through managerial, professional and education services;
- information and communications technology as services in their own right, sometimes replacing traditional manufacturing activities eg books and music, but also as a factor in increasing the tradability and value of services eg within global value chains, and in driving innovation and productivity growth in all sectors;
- increased understanding and application of innovation in services systems which in the 20th century had tended to be under-explored:
    - Increased realisation of economy of scale and customisation processes
    - Self service/ better understanding the client interface
    - Co-creation through value chains/ open innovation and standards
    - Application of research, including social sciences, humanities and arts as well as science, technology and mathematics;
- Health services increasing in importance as a function of wealth and ageing;
- Rise of cities and urban living – cities' value production is primarily services.

[4] Asian interest in Services export strategies will be further stimulated by the 2012 World Bank report **Exporting Services: a developing country perspective** by A Goswani, A Mattoo and S Saez

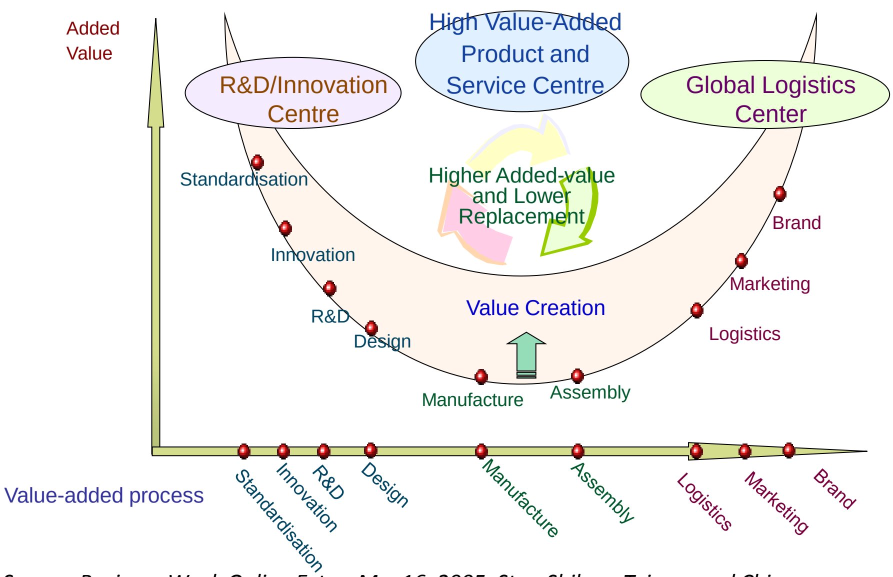
[5] Department of Manufacturing, Innovation, Trade, Resources and Energy 2012, *Knowledge Intensive Services: A strategy for Growth 2012-14,* Government of South Australia, www.dmitre.sa.gov.au/kis

The growth in business importance of services to some extent has been obscured by the rise of Asia, particularly as a result of the manufacturing-centric economic development strategies used by many Asian economies. This has had the effect in most developed countries of focussing public opinion and political attention on manufacturing, leading to the impression that this is and will continue to be the main impact.

The fact is that Asia is already the largest and most competitive manufacturing region in the world, and the implications of this already can be seen and understood. What is new and different is that the historic shift in economic wealth and power to Asia expected to occur as the Asian Century progresses can be expected to result in Asia becoming the largest consumer and most competitive producer of services, including professional and financial services.

Figure 1

"Smiley Face": conceptual model of the shift to a high value added, globally integrated, services economy



Source: Business Week Online Extra, May16, 2005. Stan Shih on Taiwan and China

Figure 1 above shows the growing importance of services within the manufacturing supply chain. The Smiley Face was used by the ACER chairman to explain why it was necessary for ACER computers to manufacture laptops in China, as part of a strategy to establish the ACER brand and move ACER from being a contract manufacturer for US brands.[6] It illustrates the issues that need to be addressed in raising public understanding of services supply chains.

Discussion points on economic development

How will economic growth and structural change in Asian economies evolve? What are the risks and opportunities ahead for Asian economies?

[6] For a more full discussion of global value chains and Stan Shih's 'Smiling Curve', see A McCredie, *Multinational Companies in Australia*, in Competing From Australia, CEDA Growth no 58, July 2007

The conjunction of the rise in business and economic importance of services with the expected development of Asia (particularly China) as the dominant global consumer and producer of services has the following implications:

- Asian services markets, where Australian businesses have had much success, will grow rapidly but will be become much more contested including by increasingly capable domestic businesses;
    - The professional skill gap between Australian and Asian professionals will narrow, making market information, integration with Asian supply chains and development of niche capabilities increasingly important;
- Asian-based multinationals, particularly in China and India, will be increasingly important in global services supply chains;
    - For example IBM is setting up 70 offices across China to offer Business Process Outsourcing (BPO) to regional Chinese firms, its new Melbourne Research laboratory has in its mission R&D in support of IBM's China BPO operations;
- While there is an expectation of liberalisation in Asian services markets, this outcome is not assured;
    - Access to Asian services markets remains very constrained with no significant progress made in multilateral or bilateral trade negotiations over the past decade
        - We need to learn the lessons from the past decade of failure;
    - Poor foreign access to Asian services markets actually is a major barrier to improved productivity and poverty alleviation in Asia – lack of understanding about services and their role in the economy is the major barrier to trade reform in services. [7]
- Asian consumers and services producers can be expected to gain more political power leading to a relative decline in support/subsidy to manufacturing
    - Economic need to address global imbalances will also have this effect;
- Asian and developing economies more broadly are placing increasing focus on services development strategies, especially for export:
    - 'the share of developing countries in the exports of world services increased from 11 per cent in 1990 to 21 per cent in 2008'; 'developing countries are exporting not just traditional services such as tourism, but also modern services, notably high-value, skill-intensive services such as computer and information services and other business services'.[8]
    - Services imports from Asia to Australia can be expected to increase rapidly, indeed facilitating this growth may well be necessary to enable Australian business to access Asian services markets and to build partnerships in global value chains.
- Political issues associated with services may become more significant in Europe and the United States (possibly Australia also if unemployment rises);

---

[7] See PECC Task Force on Services 2011, *Services Trade: Approaches for the 21st Century*, published by PECC and ADBI. http://www.adbi.org/book/2012/02/01/4848.services.trade.approaches.21st.century/ The World Bank report *China 2030: Building a Modern, Harmonious, and Creative High-Income Society,* discusses these policy reform issues in the context of avoiding the Middle-Income trap; ASR has highlighted these same issues as being part of a toolkit to enable developing countries to 'leapfrog' in services productivity.

[8] A Goswani, A Mattoo and S Saez 2012 *Exporting Services: a developing country perspective* World Bank

  - Australia needs to foster a constructive and open international debate about international services trade and investment, and to resist attempts to ring-fence Asian economies, eg in the discussion on International Services Agreement occurring in the WTO[9], Trans-Pacific Partnership etc;
  - Australia needs to build people to people links between 'friends of services' at the political, business, professional, bureaucratic, think-tank and academic levels;
  - Australia needs an active trade, innovation and economic development strategy to build links with emerging Asian multinational giants that seem likely to dominate services value chains of commercial interest to Australia;
    - Business needs to remain sceptical about accepting advice about the potential security implications of commercial engagement with these firms, especially where US and European competitors do not seem to be similarly constrained;
- The mercantilist thinking that dominates international trade and industry development issues is especially inappropriate for services:
  - The intangible nature of most services means growth in the value of services production and consumption does not have the resource implications of similar growth in goods;
    - New jobs and economic growth can be created in services without the impact on environmental sustainability of growth in goods consumption;
  - Stagnant productivity growth in services is a more significant threat to jobs and wages than innovation, and trade and regulatory reforms;
    - For example, there is evidence that the opportunities for job creation from services business growing internationally are greater than the job losses from offshoring[10];
    - Better public understanding about the value of services productivity is needed equally for reform in Asian economies and Australia;
- Financial services and investment are particularly significant examples where major change can be expected:
  - Over the past decade China's total outward direct investment has grown tenfold US$298 billion in 2010, and over the same period Hong Kong's total outward direct investment has grown almost threefold to US$948 billion[11];
  - In 2010 Chinese direct investment in Australia is small, ($13 billion from China and an additional $7 billion from Hong Kong versus $120 billion from the United States)
  - Over the coming decade, China is likely to become Australia's largest investment partner unless growth in both inwards (Chinese investment in Australia) and outwards investment (Australian investment in China) remains constrained by regulation/public attitudes;
  - On present trends, China is likely to become the major global centre for financial services sometime during the period of the Asian Century.

[9] ASR is working with its partners in the Global Services Coalition to gain international business consensus on the priorities for international Services Trade reform.

[10] Lanz, R., S. Miroudot and H. K. Nordås (2011), "Trade in Tasks", OECD Trade Policy Working Papers, No. 117, OECD Publishing. http://dx.doi.org/10.1787/5kg6v2hkvmmw-en

[11] UNCTAD, *World Investment Report 2011*

Discussion points on economic opportunities and challenges for Australia

What are the opportunities of the transformation occurring in Asia for Australia's economic performance, trade, investment and financial markets?

The continuing demand for resources from Asia will provide Australians with wealth from these exports, but few jobs.[12] Australia's continuing economic success relies in the maintenance of an internationally competitive economy across all sectors, with prospects for good jobs and engagement in the global economy widely available. While the opportunities to do this through manufacturing have diminished with the rise of Asia, there are new opportunities in high value services, including services to manufacturing.

The impediments to realising opportunities in high value services are both domestic and international. The global economic impact of services trade and investment restrictions has been assessed to be several times the cost of restrictions placed on goods trade, and while services demand is growing rapidly, the Asian region remains plagued by high barriers to services trade.

How well placed is Australia to take advantage of these opportunities? Are Australia's policy settings appropriate? Will our market, regulatory and institutional arrangements enable our ongoing success and maintain social support for integration?

Australia is an advanced services economy, and in many areas of international services performs well above its global economic weight, eg international education; tourism; and in the number of engineering, architecture and law firms in global top 100. Australia's international financial services capabilities are growing from a relatively low base – the policy changes resulting from the Johnson Report on Australia as a Global Financial Services Centre are important.[13] Australia's information and communication technology (ICT) services has the capability to succeed in Asia markets, but needs better links into Asian value chains and market access.

There are some areas of services trade, such as international health services, where Australia seemingly has the potential to be very successful, but because of domestic regulation/policy has not been able to develop international business. Heath services are an increasingly important target for international investment by Asian firms.[14]

ASR has long advocated a renewed commitment to domestic reform, efficiency and innovation as a necessary pre-condition for success in Asian services markets, see **box 1** for key reforms below.

Included in these reforms is a major level increase in Asian language and culture education in Australian schools. Services typically involve deeper people to people communication than transactions involving goods. Community attitudes also are important if Australia is to succeed in expanding its services trade and investment links with Asia. Asian language teaching should be

---

[12] Technological change is further diminishing the role of mining as a generator of jobs. For example, Rio Tinto has announced it is moving to driverless trains – *End of Line for 500 train drivers*, Paige Taylor, *The Australian* 21 Feb 2012

[13] For example, the Asian Funds Management Passport initiative would provide the regulatory framework for Australian Funds Managers to compete for Asian Funds management work, and an initial phase of work was recently approved by APEC Finance Ministers at the 2011 Honolulu meeting.

[14] UNCTAD, *World Investment Report 2011*

compulsory in Australian primary schools – not a tokenistic one day a week exercise, but at least one hour every school day with a properly resourced effort taking advantage of ICT (perhaps providing links to China-based Mandarin teachers) and modern language training techniques.

There are concerns about the decline in mathematics and science teaching in schools and universities and the related lack of production in engineering and ICT graduates. Australian school performance has dropped in mathematics, science and literacy whereas that of a number of Asian economies has jumped significantly. A Grattan Institute study[15] finds that this jump in performance is a result of innovation in the classroom – not Confusion culture, hard work or more money. It results from a relentless, practical focus on learning and the creation of a strong culture of teacher education, collaboration, mentoring, feedback and sustained professional development. [16] In Shanghai, the average 15-year old mathematics student is performing at a level two to three years above his or her counterpart in Australia, the USA and Europe.

The Asian innovation that even average students can make great gains in mathematics and literacy performance when well taught needs to be emulated in Australia. Too often Australia's high school system leaves the impression that its primary function is ranking students, not improving their performance. Education and skills are critical in determining wages in a globalised services market; multinational firms are already setting up operation in Shanghai because of the high quality skills available.

The success of exports of Australian education has masked the need for competitive level of government support if current performance is to be maintained. Australian higher education institutions have not had sufficient incentives to make the additional investment necessary to properly prepare students to succeed in new disciplines, combined disciplines and sub-disciplines particularly in demand in international services markets, eg finance, engineering, law and other professions. Given Australian ambitions and our competitive position within global value chains it is essential that Australian universities be able to offer world class teaching in important new areas of knowledge that may provide niche opportunities for Australians to succeed in global supply chains.

An example of the inertia within major disciplines is the teaching of services economics[17] within Australian universities. Despite the rise in services to around 80 per cent of the Australian economy, and its employment of 93 per cent of university graduates, from what they are taught most Australian economics graduates would be barely aware of the services economy and the micro-economic factors that underlie its value creation and productivity growth.

---

[15] Ben Jensen 2012, *Catching up: learning from the best school systems in East Asia* - A Grattan report

[16] The Gratton institute report actually does not use the term 'innovation', but gaining better outcomes from the same resources through process improvements in a service system is a service innovation. Service innovation as a process is becoming better understood and the systematic application of this understanding across services systems including education has substantial underdeveloped potential. ASR is working closely with research organisations including CSIRO, NICTA and the CRC for Smart Services, universities, and members such as IBM Australia, Disciplined Innovation Pty Ltd and Standards Australia in raising understanding of services innovation, and in identifying priorities and opportunities for implementation.

[17] There is a long and well regarded history of Australian applied economic research in agriculture and resources. Perhaps the slowness of the Australian applied economics discipline to engage with the services dominant nature of the modern Australian economy is a contributor to its relatively poor citation performance.

The application of ICT is beginning to make a substantial impact on the teaching and training processes, and as it progresses it will most likely impact upon business models. With the strong understanding of the link between education and training and wealth creation in Asia, it is very likely that Asia will be a lead market and developer of new education and training technologies and new education and training business models.

As well as ICT capability and infrastructure becoming an increasingly important platform for education and training, they underlie just about every service export. Given that the major business cities in Asia have advanced ICT infrastructure, including the 2nd tier cities in China, extension of this capability to Australia's regional cities will be open up opportunities for services businesses in regional Australia to trade with Asia.

ICT also has the potential to drive services productivity in all sectors, including manufacturing, mining and agriculture; and to be a mechanism for reducing the regulatory and tax reporting burden on business. ASR President James Bond raised the potential for ICT to lower regulatory burdens in an Opinion Piece in the Australian Financial Review. [18]

Services export and services development strategies are becoming common across Asia and there is value in Australia undertaking a Services Roadmap to identify opportunities and impediments and to raise public understanding. ASR in partnership with ACILTasman and in consultation with leading services businesses and key Australian government departments has scoped the work involved in undertaking a Services Roadmap in the report *New Economic Challenge: responding to the rise of services in the Australian economy*.

[18] James Bond 2011, *Seamless economy is unravelling*, Australian Financial Review Tuesday 22 Nov p63; ASR Supplementary Submission to Productivity Commission review on *Identifying and Evaluating Regulation Reforms,* 20 December 2011.

Box 1: Key Reforms to succeed in the Asian Century

Labour Market

Immigration

Competitive, efficient immigration system enhances integration with global economy and services competitiveness, necessary for completive international education sector, needed to address skills gaps, eg engineers, ICT specialists, medical practitioners etc.

Sustainability and liveability issues especially in cities need to be addressed to ensure popular support for immigration.

Education

School

Teaching of Asian languages in primary school especially Mandarin. More students undertaking advanced science and mathematics.

Universities

Universities are a key contributor to growth in the modern knowledge-based services economy.

This instrumental role of universities is not in conflict with the university's traditional focus on the quality of thinking across a wide range of disciplines –diversity is needed in a knowledge based economy.

Key issues:

- How do we maintain and improve quality of graduates
    - Role of technology
    - Business and professional linkages
    - Training scientists, engineers and ICT
- Research productivity in universities
- Funding

Participation

- Women
- Older workers

Workplace Relations

- Need to be better aligned with productivity agenda – eg penalty rates in tourism
- Outsourcing/offshoring issues
    - Tourism, QANTAS, banks

Seamless Economy/Regulation/Tax Reform

There needs to be increased bipartisan political support for the COAG 'seamless economy' reforms, particularly harmonisation of regulation covering:

- Professions
- Energy efficiency
- Procurement
    - Including reform to better delivery value for money through innovation
- Insurance

Slashing regulation/simplifying tax

- There has been a massive explosion in regulation over past twenty years
    - Regulation Impact Statements - too many exemptions, broadcasting regulation has grown from 100 pages to 1000 pages
    - New issues/technologies seem to multiply regulation when in principle they provide many opportunities to simplify regulation
        - Eg tax and planning approvals, media regulation
            - SBR business plan promise of $800m saving per year has yet to be delivered
- Services privatisation/competition policy has been responsible for much new regulation
    - Are there opportunities for a 2nd wave of reform that reduces regulatory burden but preserves social/political outcomes and business enterprise and competition?
- Adoption of systematic and transparent evaluation of public spending and taxation proposals in a manner consistent with legislation and regulation review

Cities and Planning

- Efforts to address city planning through COAG and Infrastructure Australia need to be accelerated and fully resourced
    - Australian architecture and engineering firms have been outstandingly successful in wining business in city planning and development in China, but the gap in performance between Australian practice and best practice in China is increasingly obvious
- Planning processes need to be supported by underlying, common databases on population, transport, energy, water etc.

Use of ICT

- Broadband applications in health, education, energy, business (eg telework, conferencing)Reform of Australia's payment system so that Australian financial services companies and their suppliers develop 21st century applications that have the potential for use in Asia

Subsidies

- Rationalise subsidisation, apply balance based on evidence and analysis across agriculture, manufacturing, mining and services.

What are the challenges and risks for Australia arising from Asia's transformation?

The major risk for Australia from Asia's transformation is a drift into protectionism and isolation from Asia because of concerns about competitiveness. These concerns are real, the OECD PISA results show that 26.6 per cent of Shanghai[19] students score at the highest level in mathematics, versus just 4.5 per cent of Australians (and the Australian result is good relative to countries like the United States). Last year's Ministerial Mission to China's second tier cities found that many companies attracted to set up in these cities because they have found skill levels nearly as good as in Shanghai, but with lower wages.

A retreat from the bipartisan approach to an open, dynamic economy would be very damaging for Australian welfare. In this context, it is worth recalling that the White Australia policy had at its heart protectionism. The alternative to working hard to build community understanding of how Australia can compete in global services supply chains with Asia, ultimately is to risk a protectionist reaction. The success and public acceptance of the reforms of the 1980s and 1990s owed much to the combined political leadership of Hawke, Keating and Button, supported by then Opposition leaders such as Howard and Hewson.

How can Australia promote flexibility in responding to structural change, including in areas such as innovation, business adaptability, labour mobility, education and training and capital market efficiency.

The best way to promote flexibility in responding to structural change is for Government to remove impediments to making this change, and to ensure that markets and regulations properly reward businesses prepared to invest.

Communication with the public to help them understand the nature of these changes and the opportunities that arise is also important. Workforces that are concerned about change and job losses loom as a potentially significant impediment to increasing business interaction with Asia.

Supporting the communication task needs to be economic statistics that properly reflect the nature of Australia's economy and its opportunities for increased value-add/productivity. In Australia's student-led education system is critically important that students and education providers have access to information about the skills required in areas of jobs growth. In recent years Australian employers have sourced over 60 per cent of their new engineering and ICT employees from foreign citizens as there are insufficient qualified Australians – which in turn stems from the fact that not enough students have the core capabilities to undertake these studies as they have not done higher level mathematics in high school.[20]

---

[19] For China, the OECD PISA survey only tested students from Shanghai.

[20] There is evidence that in their subject choice high school students are influenced by the prospects of gaining a high mark for entry into university. For example, most students know that Asian languages and mathematics are useful skills, but many will drop these subjects to avoid the risk of a lower mark. This is a significant factor in the decline in student numbers undertaking Asian languages and higher level mathematics; on the other hand students' responsiveness to university entry requirements suggests a way of reversing the trend. For example, university entry systems could address the anomaly that a student doing intermediate or basic level mathematics can gain a higher mark in mathematics than a student doing higher level mathematics based on

Information about the skills required in areas of jobs growth is also important if there is to be increased government intervention in jobs retraining and reskilling to help those who have lost their jobs as a result of increased importing or technological change.

As result of its communications with Skills Australia, ASR is concerned about the paucity of information available about the international trade and technology effects on services employment, resulting in a substantial underestimation of the trade exposure of Australian services businesses and therefore an underestimation of the skills requirement needed to be successful in growing services export jobs.

Typically skills issues in Australia have not been seen as involving university graduates, but the services sector employs 93 per cent of Australia's university graduates and those involved in services exports are typically university graduates. Employment growth in the Australian economy also is overwhelming in those areas that employ university graduates, namely the professional and managerial occupations.[21]

It is a corollary of the increased knowledge intensity of business that the efficiency of higher education skills markets and the linkages between professional bodies, research institutions, employers and universities become more important. These issues need to be examined in light of the challenges and skills demands of the Asian Century and would be an integral part of undertaking a Services Roadmap.

ASR is working with the South Australian Department for Manufacturing, Innovation, Trade, Resources and Energy on the development of a Knowledge Intensive Services Strategy for South Australia. In the context of these skills and knowledge issues, consultation with services businesses has identified the following priorities:

- Universities and Research Organisations build collaboration with industry across multiple disciplines;
- Undergraduate and graduate internships within industry could be developed to ensure graduates are "industry ready" ;
- Australian university students study in Asian universities to understand their markets, business cultures and build networks.

The role of ICT within services innovation has been and will continue to be significant. Australia needs to continue to be an early adopter of ICT applications, such as via broadband, and should seek to engage with Asian multinationals as well as the traditional European and United States suppliers. A strategy needs to be developed to ensure that Australian firms can gain access to global supply chains via Asian multinationals, similar to the access they have traditionally been able to realise via European and US multinationals. Competition impediments need to be addressed to the adoption

---

relative performance not competence across the core mathematical concepts. Many universities used to have foreign language requirements for entry.

[21] Treasury reports that the number of high skill white collar professionals and managers has increased by more than 800,000 over the six year period from 2004 to 2010, by far the greatest area of occupational employment growth, see 2012 Budget paper 1, Statement 4 *Opportunities and Challenges of an Economy in Transition, chart 11*.

of significant new ICT systems with major potential economy-wide benefits, such as seems to be the case in the Australian retail payments system.[22]

A feature of Asian innovation has been a step change in price-performance not just an incremental change. As Asian business further develops its activities in services, Asian innovations in services will become more common.[23] For Australia to remain competitive in global services supply chains we will need to be an early adopter of such innovation.

How do we manage the economic transition in a way that spreads the benefits across society more generally?

It is a notable feature of the current resources boom that domestic costs have not blown out as they had in previous booms. The increased international dimension of the services economy is an important and under-appreciated factor. There needs to be a better understanding of this factor and its implications. To give just one example, fewer than 40 per cent of the new entrants into the IT and engineering professions in Australia are from Australian citizens.

How can Australia best address environmental, resource and capacity constraints that might arise?

The development of the services economy is not as resource dependent as the traditional sectors. Good city environments, attractive to mobile high-value knowledge workers, ICT infrastructure and applications, good universities and skills are the key factors for services.

How should Australia progress its economic agenda through bilateral, regional and global processes and arrangements?

Australia needs to take a leadership role in promoting the services reform agenda with the various international processes and arrangements, bilateral, regional and multilateral.

In APEC Australia should promote and take a leadership role in developing a high level Services Initiative. An objective of this would be to refresh and reinvigorate APEC's domestic reform agenda through the prism of the widespread objective by many developing countries to improve their services economy and services exports, and how a set of principles on best practice regulation for services might contribute to this.

In the WTO, Australia should continue to take a leadership role in developing an International Services Agreement.[24] ASR has set out its objectives for this agreement, namely:

- Competitive Neutrality: i.e. strategies to meet the OECD principle that business activities by state-owned or state-sponsored enterprises should not enjoy net competitive advantages over private sector competitors;

---

[22] A McCredie 2011, *Payments impasse needs to end* Australian Financial Review, Monday 12 December

[23] ABC TV's Foreign Correspondent program *The Ka-Ching! Dynasty* showed a thirty story hotel being built in nine days by the entrepreneurial Chinese company Broad.

[24] The benefits of ISA are well set out by Edward Gresser 2012, *Services Trade Liberalization as a Foundation of Global Recovery*, Progressive Economy Project at the Global Works Foundation.

- Freedom of Cross-Border Data Flows: i.e. strategies to enable freedom from requirements to host or process data on servers within a home jurisdiction, permitting data (the essence of services business) to flow more freely;
- Forced Localisation: i.e. a variety of measures through which a country constrains business by requiring it to be supported and conducted domestically rather than internationally (this has traditionally tended to focus on trade in goods, but has now spread to the supply of services).
- Improvements in rules to free up the movement and regulation of services business people, including professional recognition;
- Development of a set of principles providing best practice regulation for services
- Opening up of government procurement of services
- Disciplines in subsidies in services

In order to gain a critical mass of support for an International Services Agreement in the WTO it may not be possible to pursue all these issues to the extent that Australia would like, particularly development of a set of principles providing best practice regulation for services. Forums such as the OECD and APEC may provide an alternative.

How should Australia position itself as Asia's role in global economic decision making grows?

Australia should maintain its reputation for fair dealing and sound evidence based advice with everyone.