IMPROVING OPPORTUNITIES FOR SOUTH AUSTRALIAN INDUSTRY

MAY 2011

Ai Group Submission on 2011-12 South Australian Government Budget Priorities

EXECUTIVE SUMMARY

The Australian Industry Group (Ai Group) is a peak industry association in Australia which along with its affiliates represents the interests of more than 60,000 businesses in an expanding range of sectors including: manufacturing; engineering; construction; automotive; food; transport; information technology; telecommunications; call centres; labour hire; printing; defence; mining equipment and supplies; airlines; and other industries. The businesses which we represent employ more than 1 million employees.

We are an organisation committed to helping Australian industry with a focus on building competitive and sustainable industries through global integration, skills development, productive and flexible workplace relations, infrastructure development and innovation.

Our organisation provides practical information, advice and assistance to help members run their businesses more effectively. It ensures through policy leadership that members have a voice at all levels of government, by representing and promoting their interests on current and emerging issues.

Ai Group members operate small, medium and large businesses across a range of industries.

Ai Group is closely affiliated with more than 50 other employer groups in Australia alone and directly manages a number of those organisations.

Our organisation has formal and long standing links with more than 80 overseas employer organisations such as the Confederation of Indian Industry; the Chinese Machinery Industry Federation; The Osaka Chamber of Commerce and Industry; the Federation of Malaysian Manufacturers; the US National Association of Manufacturers; the Confederation of British Industry and Business New Zealand.

Ai Group employs more than 300 staff and 550 apprentices and trainees through its training arm, Australian Industry Group Training Services. Our professional staff includes workplace relations advisers, lawyers and employment and business specialists who provide services to members in the areas of: workplace relations; legal; human resource management; occupational health and safety; workers' compensation; the environment and energy; international trade and export; economics; business growth and skills.

For reasons outlined in the following submission this State Budget is a crucial budget in the context of the global and local economic challenges in which we find ourselves.

We urge the government to continue to show restraint and ensure that Ai Group's members, many of whom are experiencing extremely difficult times, do not have their competitive position further impeded.

SUMMARY OF RECOMMENDATIONS

Recommendation 1

We urge the Government to deliver a budget that will focus on maintaining the states AAA credit rating and keep its future interest payments low by incorporating appropriate expenditure restraint.

Recommendation 2

Recognise through the Budget that Asia continues to be an area of emerging importance for our State and national economy and recommend that the Government orientate its support for industry to take advantage of future opportunities in the region.

Ai Group recommends that the Government:

- Invest in measures to improve South Australian business' "Asia skills" and Asian literacy through in-school education and greater skills support in the workforce;
- support export initiatives that encourage local manufacturers to export to the growing economies of the ASEAN region through an enhanced Federal *Export Market Development Grants* (EMDG) Scheme;
- continue support for SME exporters with export assistance grants through the *Gateway Business Program; and*
- consider export proposals that have proven successful in other jurisdictions to assist exporters to access new markets, such as Victoria's *First Step Exporter.*

Recommendation 3

Ai Group recommends that the Government:

- Continues to improve the state's competitive tax position.
- Importantly focus on reviewing payroll tax rates and thresholds.
- closely considers the outcomes of the *Henry Tax Review* and develops an active program in support of replacing inefficient state taxes (such as

stamp duties on conveyances, insurance contracts, transfer of ownership on motor vehicles and other financial transactions) with more efficient forms of taxation and improving other state taxes.

Recommendation 4

The Government oversee whatever is necessary in terms of an appropriately resourced public sector whereby public sector employees as a percentage of total employees is the equivalent of the average of the other mainland States.

Recommendation 5

Ai Group recommends that the Government:

- commit significant resources to improving the literacy and numeracy levels of the state's workforce, as well as providing all students with the opportunity to participate by supporting and implementing actions from the *National Foundations Skills Strategy*;
- fully implement recommendations contained in *Skills for All: The Strategic Direction for Vocational Education and Training in South Australia 2011-2014;*[1]
- continue to invest in facilities in schools to support school-based apprenticeships and traineeships;
- engage and consult more closely with industry (well before significant expenditure) on ensuring that that the most appropriate training, skills and VET infrastructure is developed, particularly in relation to machinery and equipment purchases.

Recommendation 6

Ai Group Recommends that the State Government support Ai Group's national migration focus, and advocate this position to the Commonwealth Government, by:

- acknowledging that *balanced* (skilled) migration has a role to play in addressing the nations short and long term skills needs;

[1] See the Final report of February 2011 at: http://www.dfeest.sa.gov.au/LinkClick.aspx?fileticket=c7XGLnOx9Do%3d&tabid=267

- pressing for the Commonwealth's 2011-12 *Immigration Program Planning Levels* to return numbers in the order of 190,000; and

- joining with Ai Group in recognising that South Australia and the nation require both skilled trades and tertiary qualified migrants, but that changes are required to redress the allocation of fewer points to skilled trades (as compared with university qualifications).

Recommendation 7

The Government continue to provide a capital expenditure program which aims to put in place projects which improve the states productivity and efficiency.

Ai Group recommends that the Government:

- maintain its commitment to significant levels of investment in the State's infrastructure, to drive investment, improve productivity and enhance the competitiveness of the State's economy;

- commit to an upgrading of the *South Australian Industry Participation Policy* such that 'local' firms that can demonstrate best value for money should be given every opportunity to participate in government procurement and major projects. This would include the Policy being applied in respect of goods and services, as well as major projects.

Recommendation 8

The solid waste levy is directed towards programs that reduce waste or improve energy efficiency and no further increase of the levy occur in the short term.

THE ECONOMIC OUTLOOK NATIONALLY

The latest Ai Group/Deloitte CEO Survey: *Business Prospects in 2011,* points to unbalanced growth across sectors in 2011.

Our report, released in late February 2011, highlights sharp differences between business expectations across various sectors. Key findings of that Report are that:

- on balance, the services sector anticipates making gains across all the economic indicators surveyed except for capital investment and R&D expenditure;
- the construction sector is also expected to perform strongly in 2011, on the back of the resources boom and pent up demand;
- while the economic outlook for the manufacturing sector is also expected to marginally improve in 2011, there are some areas of concern:
  - there is an expectation of a significant decline in capital investment; a decline in employment within the sector; and weak real growth in sales;
  - expenditure on both R&D and training is expected to remain flat; and
- the vast majority of CEOs across all three sectors consider both their exports and import-competing production to be uncompetitive at the prevailing AUD/ USD exchange rate.

The Report forecasts that business conditions will continue to build slowly on the recovery commenced in 2010, and that whilst patchy, the economy overall is anticipated to grow despite the impacts of recent severe weather events and the very difficult conditions in trade exposed industries arising mainly from the strength of the domestic currency.[2]

The results of the survey, which canvassed the views of CEOs from 530 businesses across manufacturing, construction and services, are decidedly less optimistic than official forecasts issued by the Treasury and RBA. Of particular note are substantial differences relating to prospects for capital investment in the coming year.

General market forecasts for aggregate investment in 2011 are much stronger than Ai Group's sector-specific results, which suggest that both the manufacturing and services sectors are expecting a decline in capital investment, while growth in investment in construction is expected to be subdued.

In our view, the outlook for manufacturers highlights the significant challenges associated with a high exchange rate, competition for resources from the mining sector, higher interest rates and the cumulative impact of slow productivity growth over the past decade. Trade-exposed businesses are now feeling the impacts of the poor national productivity performance over this period.

In our view, it is only with concerted policy action from governments at all levels, together with cooperation with the business community to raise productivity and

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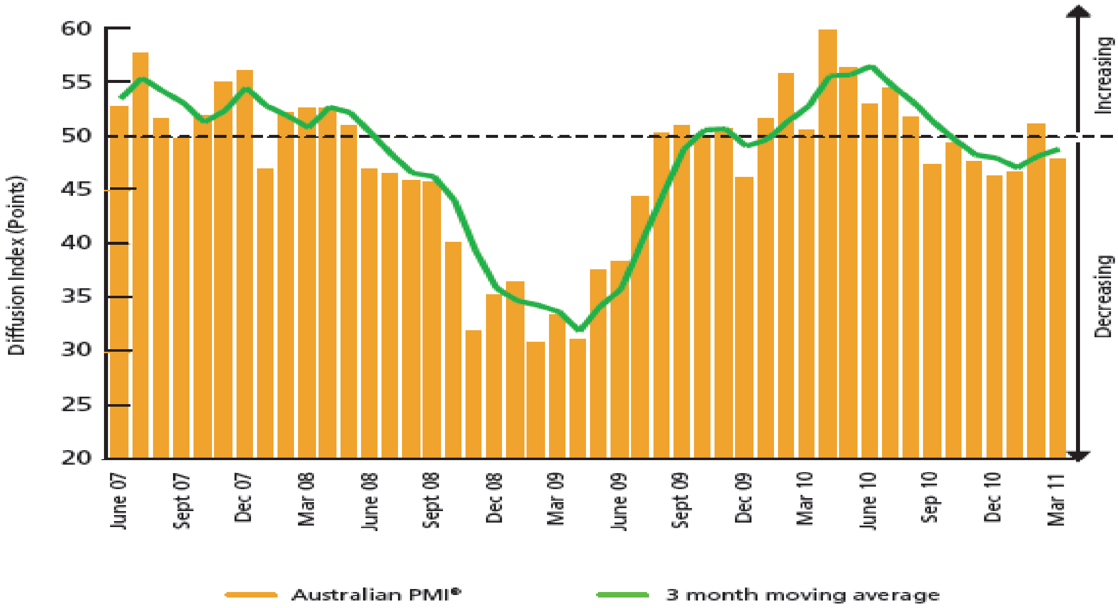
[2] Bearing in mind that the Survey was taken before the disaster in Japan, which is expected to have some impact on the national and State economies. For example, a limitation on key car components such as Hitachi air sensors out of Japan could well have a significant (although lagged) effect on production at GM Holden's Elizabeth plant.

competiveness, that these impediments can be overcome to achieve a more balanced and sustainable growth path in 2011 and beyond.

The *Australian Performance of Manufacturing Index* (PMI)

To monitor the state of manufacturing within Australia, Ai Group and PriceWaterhouse Coopers generate the monthly *Australian Performance of Manufacturing Index* (PMI).[3]

The recent (March) PMI was published on 1 April 2011 and showed that after a brief lift in February, new orders were down again in March 2011. The manufacturing sector has now been experiencing contraction for 6 of the last 7 months.



The associated commentary indicated that the strong Australian dollar together with weak domestic demand, rising overseas competition and the increasing cost of raw materials pushed the manufacturing sector back into the red in March.

In March 2011, the seasonally adjusted Australian PMI® fell 3.2 points to 47.9 in March, bringing it below the 50 points level separating expansion from contraction.[4]

Manufacturing activity again contracted in South Australia, along with New South Wales, Tasmania and Victoria. Only the 'resource states' of Queensland and Western Australia experienced any expansion. The decline in manufacturing activity was most pronounced in the clothing & footwear, food & beverages, textiles and fabricated metal sub-sectors.

[3] See the Ai Group – PwC *Australian Performance of Manufacturing Index* (PMI) at: http://www.aigroup.com.au/

[4] Note that readings below 50 indicate a contraction in activity.

THE SOUTH AUSTRALIAN ECONOMY

Over the last decade, South Australia's economy has performed moderately well against other Australian states.

From 2000-01 to 2009-10 the state achieved an average growth rate of 2.8% which was marginally below the Australian average at 3.2%.

This was an improvement on the average annual growth rate from 1990-91 to 1999-00 where South Australia was at the bottom of the economic table with a 2.4% average growth rate compared to the Australian average of 3.8%.

Over both decades South Australia averaged 2.7% growth rate compared to an Australian average of 3.4%, as set out in the table below.

	Average annual growth rate (1990-01 to 1999-00)		Average annual growth rate (2000-01 to 2009-10)		Average annual growth rate (1990-01 to 2009-10)
Qld	4.9	WA	4.9	QLD	4.5
WA	4.5	QLD	4.2	WA	4.4
Australia	3.8	NT	3.5	NT	3.4
NSW	3.8	Australia	3.2	Australia	3.4
VIC	3.7	TAS	3.1	VIC	3.2
NT	3.2	VIC	2.9	NSW	3.0
ACT	2.9	**SA**	**2.8**	ACT	2.8
TAS	2.5	ACT	2.7	**SA**	**2.7**
SA	**2.4**	NSW	2.3	TAS	2.6

It is noteworthy that South Australia does have an improving economic performance over this period. It will be important that this budget implements policy decisions that will enable this improvement to continue.

In particular the Government will require careful management of its fiscal responsibilities given the two speed nature of the current national economy which is very evident in this state.

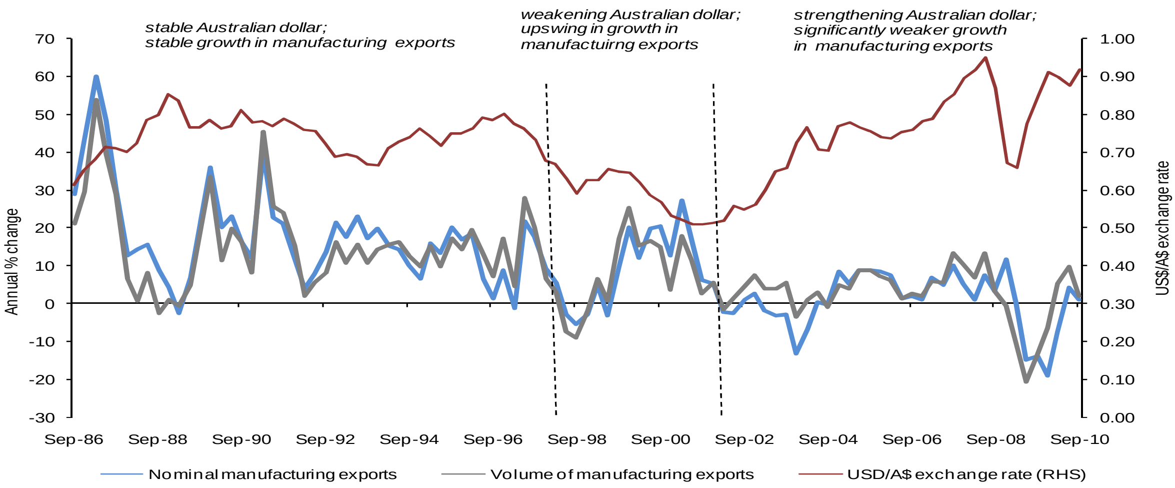
Our membership is being impacted diversely by this phenomenon whereby companies which are quarantined from the traded goods sector and aligned to growth opportunities particularly in mining are experiencing buoyant levels of activity. Conversely other companies which are effected by the high exchange rate are suffering in terms of competitiveness and export markets and heightened international competition in local domestic markets.

We do note however the state has before it a number of positive opportunities in the mining and defence sector which will add to the states prosperity and provide additional employment opportunities.

We understand there are some $80 billion worth of investment projects are in the pipeline and that the state presently has historically low unemployment levels, near record high labour participation rates and our population growth continues to be encouraging.

The following graph indicates the negative impact that the strengthening Australian dollar has had on export revenue and export volume of Australian manufacturers.

The negative impact of a strengthening Australian dollar on the export revenue and export volume of Australian manufacturers



ISSUES OF BUDGETARY IMPORTANCE

MAINTENANCE OF THE STATE'S AAA CREDIT RATING

We urge the Government to deliver a budget that will focus on maintaining the states AAA credit rating and keep its future interest payments low by incorporating appropriate expenditure restraint.

The handing down of a tough 2010-2011 State Budget was part of the strategy to maintain our AAA credit rating.

A very strong package of budget improvement measures was adopted to enable a return to net operating surpluses from 2011−12 and maintenance of a sustainable level of net debt across the forward estimates.

The Budget provided the necessary funding for the Government's election commitments and continuation of the significant infrastructure investment program.

The 2010−11 *Mid-Year Budget Review* (MYBR) indicated that parameter variations were likely to result in a small deterioration to the budget position. Since that time, there have been the flooding emergencies interstate that can be expected to draw heavily on Commonwealth funds. Any Federal funding decrease is likely therefore to have some impact on the State's finances.

Releasing the MYBR on 16 December 2010, the Treasurer was very clear that the State's financial position remains 'tight'. He also made it clear that strict fiscal discipline needed to be maintained.

The MYBR forecast that *if* the necessary strict fiscal discipline can be maintained, the State Budget could still return to surplus within a year, despite a further downward revision of GST grant revenue of over $170 million over the next four years.

We now understand that Federal Government forward estimates are indicating a significant decline in GST revenues to the States. In South Australia's case this could be $600m over the next four years.

In the light of this revenue shortfall we would urge the Government to maintain appropriate fiscal restraint.

Ai Group is aware of the calls on the Government to loosen the State's focus on fiscal discipline.

In our view, the pressures that underpinned the 2010-2011 State Budget remain as potent as they were last September, perhaps more so given that Commonwealth funding will not be delivered as expected.

Ai Group believes that at this critical time, it is absolutely crucial for the Government to adhere to a strict and disciplined approach to the State's finances.

SOUTH AUSTRALIAN EXPORTS

Ai Group Recommends that the Government:

- We recognise through the Budget that Asia continues to be an area of emerging importance for our State and national economy and recommend that the Government orientate its support for industry to take advantage of future opportunities in the region.
- Invest in measures to improve South Australian business' "Asia skills" and Asian literacy through in-school education and greater skills support in the workforce;
- support export initiatives that encourage local manufacturers to export to the growing economies of the ASEAN region through an enhanced Federal *Export Market Development Grants* (EMDG) Scheme;
- continue support for SME exporters with export assistance grants through the *Gateway Business Program; and*
- consider export proposals that have proven successful in other jurisdictions to assist exporters to access new markets, such as Victoria's *First Step Exporter.*

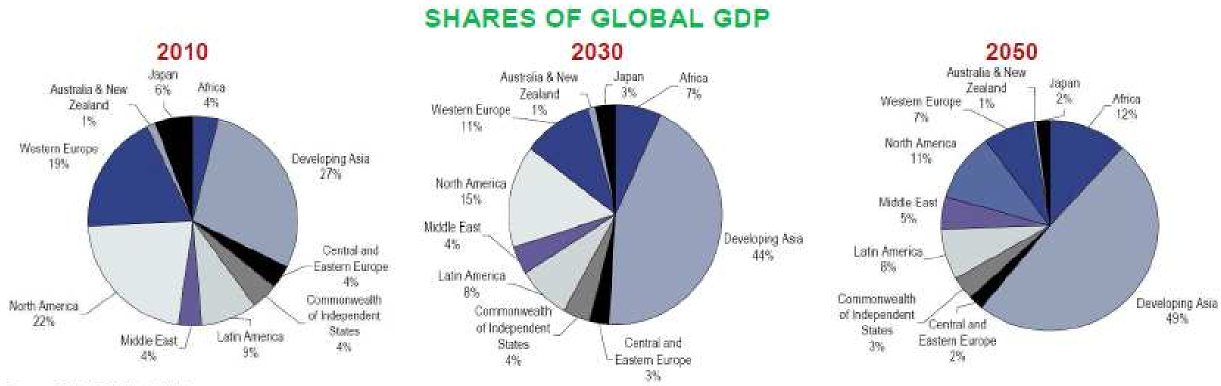
A closer analysis of the State's export data reveals that the resurgent rural and mining sectors are leading this strong rebound with income in those sectors tipped to surge by more than 20 per cent to beyond $10 billion this financial year - despite the impact of the strong Australian dollar.[5]

Pleasingly from a manufacturing perspective, *road vehicles, parts and accessories* showed a solid boost of 22.6% in the 12 months to February 2011 (totalling 3% of the State's exports) but from a low base. More sobering however, was that *metal manufactures* further slumped by 2.3% in the same period. Together, these results cumulatively describe the multi-speed economy that we have discussed elsewhere in these submissions and its associated economic challenges.

In the context of the State Budget, it will be important not to place extra imposts on the state's exporters.

EXPORT LINKS INTO ASIA

In our view it is critical that we actively cultivate our growing links with the fastest growing region in the world - Asia. As the charts below indicate, we simply cannot afford to become complacent in our approach to this dynamic part of the world.



Source: Buiter & Rahbari, ibid.

5 Grain is expected to be the biggest export earner for the State this year, wheat shipments on their own reached $922 million in the first eight months of the year. Meat exports also increased strongly to $445 million in the eight months, compared to $350 million in the same period of the previous year. The mining sector also improved sharply with exports reaching $1.34 billion, up from $964 million in the corresponding period of the previous year.

Data recently released by Citi Group[6] indicates that the globe is in the midst of significant economic shift. During the second half of the 20th century, the global GDP 'pecking order' scarcely changed with North America and Western Europe continuing to generate about half of the world's GDP. Asia meanwhile slowly increased its share from 13% to 22%.

But that change is rapidly accelerating with Asia (including Japan) currently generating around 27% of global GDP (at market exchange rates). But by 2050 this will double, with Asia expected to contribute 51% to global GDP, whilst Western Europe & North America will produce less than a fifth of global output. South Australia needs to align to this strongly emerging Asia and be ready to trade with it.

A report by the Australian Industry Group and Asialink[7] has highlighted just how important the region is to our prospects but at the same time demonstrated that we need to do much more as a country to get the most out of the export and investment opportunities.[8]

74% of respondents to our survey - some already operating in Asia and some not – indicated they wanted to expand in the region and almost half of all businesses expect to undertake this expansion within the next twelve months.

These forays into Asian markets are delivering satisfaction also, with 82% of companies with current Asian interests rating their performance as having met their expectations or exceeded them. Only 9% of businesses reported their Asian performance to be below expectations. Businesses are also relatively optimistic about the economic outlook, with only 11% believing conditions are likely to worsen in the next six months.

However, while Australia's trade performance with Asia is strong, it can always be stronger and we note that beyond imports and exports, our direct business investment into Asia is comparatively low compared to the rest of the world.

While being very positive about the strength of the opportunities, the report did highlight a shortfall in the skills needed to work in the Asian region. More than half of those currently operating in Asia reported little board and/or senior executive experience of the region. There is a higher level of experience among senior executives – about 54% of companies reported that at least some senior executives have experience – but 65% of responding companies have no board members that have worked in Asia.

We know that in Asia, having quality partnerships and excellent networks are vitally important. Our report tells us that, as a nation, we need to do more to develop an "Asia-ready workforce".

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[6] Citi Group's Willem Buiter & Ebrahim Rahbari on 21 February 2011

[7] 3 March 2011 report by the *Australian Industry Group* and Asialink (The University of Melbourne) at: www.asialink.unimelb.edu.au/publications/asialink_and_australian_industry_group_survey?SQ_DESIGN_NAME=text&SQ_ACTION=set_design_name

[8] Ai Group and Asialink conducted a joint survey of Ai Group members during 2010 to better understand attitudes towards and knowledge about Asia among Australian businesses. The aim was to explore the extent to which Australian business is expanding into Asia and whether we have the skills and capacity to support this growth. Respondents told us, in no uncertain terms, that their prospects in Asia are strong – but they identified large gaps in their experience and skills.

In our view, this would include greater efforts by business and government to lift our "Asia skills" and improve our Asian literacy. This is a joint responsibility of Federal and State Governments and industry.

In the context of the above, we would like to see long term export initiatives that encourage local manufacturers to export to the growing economies of the ASEAN region, such as those that follow.

EXPORT MEASURES AND SUPPORT

Ai Group was pleased to see the Government's continuing support for SME exporters with $1 million in export assistance grants. Aimed at helping South Australian companies to develop overseas markets and grow their businesses, the *Gateway Business Program* offers market intelligence, on-ground business matching and support through a competitive grants program that allows eligible firms up to 50 per cent off export-related expenditure.[9]

Additionally, Ai Group would like to see a long term plan covering South Australia on ground representation and support.

State Government encouragement to rebuild an appropriate level of funding for the federally funded EMDG Scheme is another important aspect of building opportunities in Asia for South Australian exporters.

OTHER EXPORT ASSISTANCE

Ai Group submits that the South Australian Government might consider proposals that have proven successful in other jurisdictions to assist exporters to access new markets. An example is Victoria's *First Step Exporter*, which has proven to be useful to companies in accessing new markets.

As well, we would recommend consideration of a *Post Market Support Initiative,* similar to that previously run in NSW. This Program provides exporters with the resources to adequately follow up on market visits and successfully convert potential business into sustainable business.[10]

[9] A one-off grant capped at a maximum grant of $20,000 over two years.

[10] Anecdotal evidence from small businesses which are seeking to export, also suggests that companies find it difficult to arrange pertinent points of contact with potential buyers in overseas markets. Some companies are forced to use agents where they have little knowledge of that agent's expertise in arranging suitable meetings whilst others find it difficult to develop contacts with agents in the specific area. Industry would find it valuable to have assistance in developing those first points of contact. If adopted, Ai Group would propose that such grants be capped at $5,000 per company on a dollar-for-dollar basis, and only eligible to companies who have participated on a South Australian Government lead export initiative such as a trade mission.

TAX COMPETITIVENESS

Ai Group recommends that the Government:

- Continues to improve the state's competitive tax position.
- Importantly focuses on reviewing payroll tax rates and thresholds.
- closely considers the outcomes of the *Henry Tax Review* and develops an active program in support of replacing inefficient state taxes (such as payroll tax, stamp duties on conveyances, insurance contracts, transfer of ownership on motor vehicles and other financial transactions) with more efficient forms of taxation and improving other state taxes.

A *Centre for Independent Studies* report indicated that South Australia is a highly taxed State, as compared to our competitor States and Territories.[11] South Australia businesses also remain under other extraneous commercial pressures arising out of the high Australian dollar, skills shortages and other taxation measures.

Ai Group strongly believes that in the current climate, the Government's focus remain on reducing taxation for business wherever budgetary pressures allow.

Ai Group has consistently urged the Government to respond to the needs of the South Australian business community and assist business and industry to achieve higher productivity growth through the removal of inefficient state taxes.

The recent *Centre for Independent Studies* (CIS) evaluated the recent performance of the six Australian states in fiscal management, covering indicators such as debt, other financial liabilities such as unfunded superannuation, government spending, public sector job numbers, and taxation.[12] Significantly, that report found that:

> *"South Australia's performance is weighed down by a high level of negative net financial worth, high levels and growth rates of general government expenditure per capita, and high tax rates. The government has, however, made some effort in recent years to moderate tax rates and stabilise state public sector employment.*
>
> *The increase in net debt has been significant but not yet enough to threaten the state's AAA credit rating. South Australia will need to do more to make its state taxes competitive and curb the growth of government spending."*

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[11] *"Tax, Borrow, Spend: How the States Compare",* a report prepared by the Robert Carling of the *Centre for Independent Studies* and released on 17 February 2011.
[12] *"Tax, Borrow, Spend: How the States Compare",* a report prepared by the Robert Carling of the *Centre for Independent Studies* and released on 17 February 2011.

Whilst we applaud the Government for its efforts in recent years to moderate tax rates and stabilise public sector employment, the report indicates that the average business tax payment in SA is $281,744 - the highest of any state and significantly above the average of $265,796.

The report warns that unless these figures can be curbed, our fiscal position *"will undoubtedly deteriorate again."* It also indicates that the Government is spending at rate that is *"well above average"* to provide services to the public - $9,329 per head of population.[13]

The report also found that all states recorded jumps in the number of public sector employees in the three years to June 2010. We acknowledge the overall reduction in public sector numbers of around 1,700 in the 2010-11 State Budget, and we are also aware of your statement that the CIS ranking came about because *"the Rann Government has invested in more teachers, more doctors, more nurses and more police officers while committing $10.7 billion to improve infrastructure."*

Finally the report warns that whilst the State's increase in net debt has been significant, it is not yet sufficient to threaten our triple-A credit rating. As we have stated above however, we see the maintenance of the State's triple-A credit rating as a critical factor for the State's fiscal future. To that end, we firmly believe that the Government must resist incurring further debt to fund recurrent expenses.

PAYROLL TAX - RATE AND THRESHOLD

Ai Group has applauded the Government for prudently addressing payroll tax in recent years. We particularly welcomed the removal of payroll tax from wages paid to apprentices and trainees, as well as the initiative to provide a payroll tax rebate for employees utilised during the construction phase of renewable energy projects.

We are pleased to have observed that previous adjustments to the payroll tax rate and threshold have reduced the impost on businesses. The table below sets out the current situation in respect of payroll tax.

[13] A figure that is $668 a year more than any other state and well above the average for other states - $8,661.

Payroll taxation rates and thresholds for the various jurisdictions as at 30 June 2010 - Various sources.

	SA	NSW	VIC	QLD	WA	TAS
Threshold ($,000)	**600**	658	550	1,000	750	1,010
Rate (%)	**4.95**	5.45 from Jan '11	4.9	4.75	5.5	6.1

We believe that ongoing reviews of payroll tax, both rate and threshold remain important for the Government's consideration. Former Treasurer Foley acknowledged that payroll tax was an inefficient state taxation measure and was committed to its reform as the State's Budget would permit.

We would encourage the Government to embrace the opportunities that will be thrown up out of a close consideration of the *Review of Australia's Future Tax System* (Henry Tax Review) .

REFORM OF OTHER INEFFICIENT STATE TAXES

Ai Group believes the South Australian Government should take a lead role in taxation reform, as it has done in other areas.

Ai Group proposes that the South Australian Government consider closely the *Review of Australia's Future Tax System* (Henry Tax Review) recommendation to replace inefficient state taxes including payroll tax, stamp duties on conveyances, insurance contracts, transfer of ownership on motor vehicles and other financial transactions, with more efficient forms of taxation.
Such measures would help lower the tax burden for South Australian businesses and in doing so, lift productivity.

Ai Group recommends that South Australia extends its credibility as the leader of tax reform among the states by developing farsighted reform measures that draw on the *Henry Review* analysis and advocate them actively in the context of the national tax forum to be held later this year.

WORKCOVER LEVIES

Whilst we acknowledge that the Budget deliberations have no direct jurisdiction over WorkCover levy rates, the high levy rate in South Australia on a nationally comparative basis does add to the burden of doing business here in South Australia.

We acknowledge a range of measures are presently under consultation to improve the position in South Australia.

However, Government needs to be cognisant of the whole gamut of costs of doing business in South Australia, rather than just those in budgetary control.

PUBLIC SECTOR REFORM

That the Government, in meeting its AAA rating, oversee whatever is necessary in terms of an appropriately resourced public sector to ensure that South Australia is meeting an average level benchmark of the other states as measured by the percentage of public sector employees versus private sector employees.

Ai Group has analysed public sector numbers on a national basis, to try to ascertain how South Australia compares nationally. Based on the most recent *Australian Bureau of Statistics* data, SA ranked highest in terms of public sector employees as a proportion of total employees (as illustrated in the table below).

We do note however that these figures do not take into account the significant public sector restructuring program which was announced as part of the 2010-11 State Budget in September last year.

Public Sector Employees as a Proportion of Total Employees

	Public Sector Employees	**Persons employed**	**public sector employees as a proportion of total employees (%)**	**Mainland State Ranking**
	'000	'000		
NSW	547.5	3514.4	15.57876167	2
Victoria	409.9	2797.3	14.65341579	1
Queensland	373.9	2326.6	16.07066105	3
South Australia	**135.2**	**806**	**16.77419355**	**5**
Western Australia	196.5	1221.3	16.08941292	4
Australia	1843.6	14,638.40	12.5942726	

Source: Australian Bureau of Statistics: 6248.0.55.002 - Employment and Earnings, Public Sector, Australia, 2009-10 and 6291.0.55.001 Labour Force, Australia, Detailed - Electronic Delivery; Table 02. Labour force status by State, Capital city / Balance of state and Sex

Recent data published by the *Centre for Independent Studies*, indicates whilst all states recorded jumps in the number of state public sector employees per capita in the three years to June 2010, South Australia was the best performer in the nation on that basis (see indicator 9 below). [14]

[14] *"Tax, Borrow, Spend: How the States Compare",* a report prepared by the Robert Carling of the Centre for Independent Studies and released on 17 February 2011.

	SA	VIC	QLD	WA	NSW	TAS
Indicator (% p.a.)	**0.2**	1.8	1.0	1.4	1.0	1.9
Score (/100)	**48**	32	40	36	40	31

Indicator 9: Average annual growth in number of state public sector employees per capita, June 2007 to June 2010

Supporting the observation that the Government has *"made some effort to … stabilise state public sector employment"*, that same data, indicates that South Australia was 'mid-pack' in respect of the number of public servants per 1,000 of population.

	SA	VIC	QLD	WA	NSW	TAS
Indicator (no)	**66.6**	57.1	66.5	70.9	60.3	80.5
Adjusted (no)	**65.3**	59.4	65.8	66.7	61.5	74.1
Score (/100)	**42**	60	40	38	54	25

Indicator 4: State public sector employees per 1,000 of population, June 2010 adjusted for cost differences

Whilst we acknowledge the Government's ongoing program in relation to public sector numbers, Ai Group will be closely observing whether the states position improves vis a vis the other states in the short term.

We again point out the need for the State to maintain its strict fiscal discipline whilst the State's financial position remains 'tight', so that we can maintain our triple-A rating and thereby deliver the State Budget back into surplus.

SKILLS TRAINING & VET

Ai Group Recommends that the Government:

- commit significant resources to improving the literacy and numeracy levels of the state's workforce, as well as providing all students with the opportunity to participate by supporting and implementing actions from the *National Foundations Skills Strategy*;
- fully implement recommendations contained in *Skills for All: The Strategic Direction for Vocational Education and Training in South Australia 2011-2014;*[15]
- continue to invest in facilities in schools to support school-based apprenticeships and traineeships;

[15] See the Final report of February 2011 at: http://www.dfeest.sa.gov.au/LinkClick.aspx?fileticket=c7XGLnOx9Do%3d&tabid=267

- engage and consult more closely with industry (well before significant expenditure) on ensuring that the most appropriate training, skills and VET infrastructure is developed, particularly in relation to machinery and equipment purchases.

As discussed elsewhere in this submission, Ai Group has nationally been warning of severe skills shortages following our emergence from the global financial crisis, and that these shortages will be exacerbated by extensive reconstruction efforts required following Christmas flooding and the expansion of the mining industry.

As a central plank in strategies to build productivity and capacity, Ai Group has strongly urged all levels of government to maintain a major focus on skills in their most recent budgets.

Australian companies are committed to training. Ai Group's own research has found that employers look to source and develop skills locally as a first option to filling vacancies. [16]

Ai Group's most recent *CEOs Skills Survey* found that companies unable to fill vacancies were more likely to respond by upskilling their existing workforce than by pursuing any other option – including overseas recruitment. Companies are telling us that skilling is increasingly important to their operations, especially in a climate of skills shortages.

Further, that these skills must be updated more often, broadened over time and be at a higher level for industry to remain competitive and for productivity to grow. Notwithstanding this commitment, it has become clear that the intensifying skill shortages in our economy cannot be met by the training of our own workforce alone.

With this in mind, we do raise a number of industry concerns in relation to education and training. Briefly these are:

1. As noted above, South Australia's existing skilled labour shortages are likely to be exacerbated by the rebuilding in Queensland and other States resulting from January's flooding and this may necessitate looking overseas to fulfill our needs in the near term. This will particularly be the case if efforts in those States go beyond recovery efforts and into flood-proofing infrastructure investment. We note with concern that South Australia is already tipped to lose skilled labour to other states as part of the rebuilding effort;
2. According to the *Australian Bureau of Statistics*,[17] such difficulties are exacerbated by the fact that in respect of literacy and numeracy, almost half of all adult South Australians are below *"the minimum required for individuals to meet the complex demands of everyday work in the emerging knowledge based economy";*
3. Against this backdrop, South Australian companies are again facing skills shortages and responding to these skills shortfalls by upskilling their existing

[16] Ai Group and Deloitte National CEO Survey 2010 – *"Skills shortages: A high risk business"*
[17] ABS (2006) Adult Literacy and Life Skills Survey.

workforce. Low literacy and numeracy levels, together with increasing State unemployment[18] make this upskilling task particularly difficult.

IMPROVE LITERACY AND NUMERACY AT SCHOOL AND IN THE WORKPLACE

For some time now, Ai Group has been emphasising issues with literacy and numeracy skills.[19] There are clearly many South Australians below *"the minimum required for individuals to meet the complex demands of everyday life and work in the emerging knowledge based economy."*

Ai Group has become increasingly concerned about this issue and the release of our *National Workforce Literacy Project* report on employer views about workforce literacy and numeracy is a major step in tackling this fundamental issue.

There are significant consequences that arise out of poor literacy and numeracy skills. Our Report showed that workplace documents were poorly completed resulting in time being wasted as the most reported impact.

Poor literacy and numeracy also result in other important consequences, including ineffective work teams, materials wastage, ineffective training, financial miscalculations, workplace injuries and unsafe work practices and recruitment difficulties. Clearly, inadequate levels of workplace literacy and numeracy are having a detrimental effect on productivity and workplace safety.

However, the greatest single measure to improve employers' competitiveness was identified as the need to upskill their workforce.

As the State continues to grow, both students and the existing workforce will need to be better educated and better equipped to meet the demands of a diverse and globally competitive economy. From a governmental perspective, it is essential that all levels of government embrace a literacy and numeracy strategy to enable the workforce to effectively contribute to the economic future of the State as our economy diversifies.

In practical terms this will necessitate the Government committing significant resources to the provision of training assistance for the State's workforce. Ai Group remains keen to work with the State Government in progressing these recommendations.

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[18] *Australia Bureau of Statistics* data released on 10 March 2011, showed that South Australia's unemployment rate for February bucked the national trend and is up from 5.4 per cent to 5.8 per cent compared to January 2011. As well, the ABS figures show that 50,300 South Australians were unemployed in February 2011 compared to 40,000 in February 2010.

[19] In May 2010, Ai Group released its *National Workforce Literacy Project.*[19] It is clear from this and other research that low levels of workplace literacy and numeracy forms a significant issue in Australia. This is no less the case in this State:
http://www.aigroup.com.au/portal/binary/com.epicentric.contentmanagement.servlet.ContentDeliveryServlet/LIVE_CONTENT/Publications/Reports/2010/8783_Workforce_Literacy_Project_Report.pdf

IMPLEMENT *"SKILLS FOR ALL"*

Over the course of 2010, the Government progressively developed its *"Skills for All – The Strategic Direction for Vocational Education & Training in SA 2011-2014".*[20] Now finalised, Ai Group is very pleased to support this Program. We agree that such reforms should help to address many of the challenges currently confronted by both industry and individuals.

As a major industry association, we are particularly pleased to see *Skills for All* aspires to renew the partnership with industry, particularly with the future aim of:

- strengthening the apprenticeship and traineeship system;
- based on industry advice, funding higher level qualifications for existing workers in priority industry sectors*;*
- funding designated skill sets for individuals for licensing and regulatory requirements or in partnership with industry (once Certificate III qualifications have been achieved);
- the Government co-investing in workforce development strategies with industry;
- promoting a culture of training with industry; and
- providing students with improved advice on careers and training options.

Having completed this important piece of work, we would call for the Government to fully implement all of the recommendations contained in *Skills for All: The Strategic Direction for Vocational Education and Training in South Australia 2011-2014.*

In its 2011-12 Budget the Commonwealth Government announced up to an additional $1.75 billion to the States to leverage 'ambitious reforms of the vocational education and training system'. Adopting a transparent approach to vocational education and training provision, with an emphasis on innovation will place South Australia well to access this funding.

SKILLS INFRASTRUCTURE

Looking closely at the skilled labour issue, Ai Group believes that the development of new TAFE and VET facilities will be critical to our future skills base. According to *Skills Australia*, the nation will require an additional 2.4 million people in the workforce with qualifications at Certificate III and higher by 2015, increasing to 5.2 million by 2025 to meet projected industry demand.[21]

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[20] See the Final report of February 2011 at:
http://www.dfeest.sa.gov.au/LinkClick.aspx?fileticket=c7XGLnOx9Do%3d&tabid=267

[21] *Skills Australia* has released *Creating a future direction for Australian vocational education and training*, a discussion paper seeking input and ideas in shaping the future direction of the VET sector. The paper outlines a number of issues for discussion that can help set the future direction Australian vocational education and training might take. Many of the issues will be familiar to those working in and with the sector.

Overall, Ai Group strongly supports the 2010-11 measures announced by State Government in respect of vocational education and training (VET)[22] and we were very pleased to support the Government's $200 million plus commitment to upgrades and new facilities for TAFE SA since 2008.[23]

Ai Group is keen to play its part in assisting the Government to meet its commitment to creating 100,000 additional jobs over by 2016, driven by growth in key industries such as mining, defence, renewable energy, and manufacturing through apprenticeships and training places in all skill levels. We are heartened to hear that the Government will continue to invest in facilities in schools to support school-based apprenticeships and traineeships.

We also acknowledge the Governments commitment to the *Trade Schools for the Future* initiative, with infrastructure construction completed at 10 secondary schools.

The draft *Strategic Infrastructure Plan for South Australia* identifies the following strategic priorities in relation to the infrastructure needs for VET:

- Improve levels of utilisation of key TAFE sites through various strategies including shared use with other educational organisations;
- Implement a systematic management program for TAFE assets that is predicated on investment in infrastructure that matches the changing needs of the community and industry;
- Develop and implement an infrastructure model that supports the achievement of equity and economic objectives through: (1) the provision of multi-purpose basic facilities across a broad spectrum of campuses; (2) the consolidation of more specialised activities on lead campuses; and
- Ensure that investments in training infrastructure to support training in particular market segments (e.g. international students) or geographic areas take account of broader requirements for student accommodation and related services.

We would recommend that well before significant expenditure on VET infrastructure occurs, that the Government engages much more closely with industry to ensure that that the most appropriate infrastructure is developed, particularly in relation to machinery and equipment purchases.

MIGRATION

Ai Group recommends that the State Government supports Ai Group's national migration focus, and advocate this position to the Commonwealth Government, by:

- acknowledging that *balanced* (skilled) migration has a role to play in addressing the nation's short and long term skills needs;
- pressing for the Commonwealth's 2011-12 *Immigration Program Planning Levels* to return numbers in the order of 190,000; and
- joining with Ai Group in recognising that South Australia and the nation require both skilled trades and tertiary qualified migrants, but that changes are required to redress the allocation of fewer points to skilled trades (as compared with university qualifications).

Ai Group holds the general view that *balanced* (skilled) migration has a role to play in addressing Australia's, and South Australia's, short and long term skills needs – with the keyword being 'balanced'.

In the short term, migration can provide the right workers in the right places at the right time. Retraining and higher participation rates among adults will provide part of the answer to skills shortages, but so too will immigration. Without the right response, it will only get harder to find anyone from a doctor to a tradesperson in coming years.

Industry's critical need for workers, especially skilled workers, received strong attention in the Federal 2011-12 Budget. The overall migration program will bring in 185,000 people in 2011-12, up from 168,700 in 2010-11. 125,850 of those places will be reserved for skilled migrants, up from 113,850 in 2010-11. A boost of nearly 10%, this takes immigration levels very close to their pre-global financial crisis levels.

Also notable were several measures to increase immigration to regional Australia, including a 60% increase (to 16,000 places) in the Regional Sponsored Migration Scheme component of the migration program. This program, which offers concessions in a number of areas in comparison with the 457 program, is of particular relevance to South Australia as this targeted program it has the potential to significantly alleviate skill shortages in our State.

$10 million will be provided to speed the processing of 457 visa applications, and the path to securing permanent residency for workers brought in on 457 visas will be simplified.

However, a cut of $198.2 million was announced to the Department of Immigration and Citizenship's funding for corporate support, policy and program design and service delivery functions. It is critical that these savings not impact the speed and efficiency of the migration program or undermine efforts to speed 457 visa processing.

Ai Group's position is that we need the permanent migration program to remain focused on skill needs and we have welcomed the Government's emphasis in this regard. We also need to keep temporary programs, such as 457 visas, accessible to business and not further tightened.[24]

In determining the policy settings for access to the program, all governments should take account of forecasts that show that our economy is in need of both skilled trades and tertiary qualified migrants. Ai Group holds significant concerns about the decision to

[24] Ai Group believes that the 457 visa program will again have to be the 'shock absorber' during this impending skills shortage. Section 457 visas include a broad range of skilled occupations right through from company CEOs to skilled trades. Ai Group is of the view that tightened restrictions on the issue of 457 visas are now more than fair. We would see these, together with an increase in the skilled immigration target back to where it was before the GFC, as very sensible developments.

give fewer points to the skilled trades compared with university qualifications, as this does not adequately reflect the current critical need for trade skills in our economy.[25]

Further, there is concern in the way that the new test would disadvantage prospective migrants from non-English speaking backgrounds.[26] Ai Group has urged the Federal Government to be open to further changes that would better balance the needs for both tertiary and trades skilled migrants.[27]

Additionally, the *Migration Program* has a role to play in addressing labour shortages that extend to unskilled and semi-skilled occupations. By way of an example, hundreds of mines operate in Western Australia; all have vacancies for mining jobs with no experience required.[28]

The *Migration Program* needs to be set with an eye to two years out as this can be the length of time taken between application and arrival. The Australian economy is growing strongly, with unemployment set to fall further and the budget on track to return to surplus in 2012-13.

Treasurer, this issue is one that the State needs to embrace directly, as we stand to lose skilled workers to other resource rich, and as part of the reconstruction program for the eastern states. Skilled migration will be vital for South Australia to be able to meet its potential as defence, construction and resources all look to source skilled labour.

INFRASTRUCTURE AND CAPITAL WORKS

Ai Group recommends that the Government:

- maintain its commitment to significant levels of investment in the State's infrastructure, to drive investment, improve productivity and enhance the competitiveness of the State's economy;

25 Under the changes, university graduates receive 15 points while the skilled trades receive 10 points. This differential could mean the difference for some applicants in what is a much tighter points test. For example, it would give applicants with undergraduate degrees five more points than highly skilled electricians or diesel mechanics whose skills are in particularly high demand in the mining, manufacturing and construction industries. According to a *Skills Australia* report, there is very little difference between the projected demand levels in Australia to 2025 between trade level and university qualifications. On that basis, both should be given the same priority in the points test.

26 Not allocating any points for English at the 'IELTS 6' level may compound the disadvantage faced by applicants with trades rather than university training. This would also limit the pool of potential skilled migrants for Australia in what is a highly contested international market at a time when Australia's demand for skills is set to grow exponentially. IELTS 6 is a fluent level of English. We would expect applicants to have completed their schooling and further studies in English at this level.

27 For example, we believe the new Points Test for the independent skilled component of the program should recognise that different levels of English are required for different skills.

28 Due to the global demand for minerals, the mining industry in Western Australia has an all time high demand for unskilled labour. This doesn't only have an impact on WA, pre the Global Financial Crisis Ai Group observed workers, both skilled and unskilled, move from non-mining sector states (including South Australia) to WA which further intensified skills and labour shortages in these states – see the West Australian Job Seeker Website: http://westjobs.com.au/jobseeker/mining-jobs-no-experience.html

- commit to an upgrading of the *South Australian Industry Participation Policy* such that 'local' firms that can demonstrate best value for money should be given every opportunity to participate in government procurement and major projects. This would include the Policy being applied in respect of goods and services, as well as major projects.

Ai Group urges the Government to maintain its commitment to significant levels of investment in the State's infrastructure, as this will drive investment, improve productivity and enhance the competitiveness of the State's economy.

Clearly, the projects outlined in the *South Australian Infrastructure Plan* will involve the expenditure of billions of dollars. In our view, the optimal outcome for the State would be that as much of this money as possible flows to local businesses through the provision of improved opportunities for companies to participate. Such localisation will boost local firms' reputations, whilst driving technology transfer, innovation, research and development and world's best practice.

Critical to the roll-out of the Plan's major infrastructure projects in this State, Ai Group has been closely liaising with DTED and advocating that the *South Australian Industry Participation Policy* (SAIPP) be similarly strengthened to deliver better local (Australian and New Zealand) participation outcomes.

We believe that the SAIPP could be substantially remodelled to ensure greater local industry participation by encouraging bidders to genuinely and systematically consider local SME suppliers when preparing their tenders.

To achieve this, the Government must adopt the notion that 'local' firms that can demonstrate best value for money should be given every opportunity to participate in government procurement and major projects when Government money or approval is required. Importantly, the SAIPP should be particularly applied to major projects, as well as in respect of goods and services.

ENVIRONMENT AND ENERGY

Ai Group recommends that the Government direct the solid waste levy towards programs that reduce waste or improve energy efficiency and no further increase of the levy occur in the short term.

THE SOLID WASTE LEVY

The 2010-2011 South Australian State Budget included announcement of an increase in the solid waste levy to $35 a tonne in metropolitan Adelaide (from $26) and $17.50 in non-metropolitan Adelaide (from $13), effective from July 2011.[29]

Post 2012, the levy is forecast to progressively increase to at least $50 per tonne, although no specific time has been announced for these further increases.

At the time of the last State Budget, Ai Group commented in the media that whilst this may not be a widespread issue for industry, these increases are substantial for those caught by them.

We also stated our view that a proportion of these funds should ideally be allocated to scientific research and testing in areas where industry believes waste products can be reused which would enable the key regulator, the EPA, to verify such processes.[30]

In our view there should be no further increase in the solid waste levy.

[29] The Solid Waste Levy is applied to all waste disposed to landfill and revenue collected will continue to fund programs and activities associated with the diversion of waste from landfill into reuse and recycling programs.

[30] In this respect, industry is wearing both the scientific and testing costs and the increased levy charges at the current time.