

Committee For Melbourne Briefing Note

Securing Victoria's Economy - Baillieu Government Policy Document

On 21st December 2012 the Premier released the Baillieu Government's economic action plan "*Securing Victoria's Economy – Planning. Building. Delivering.*"

The following is a briefing note that outlines some of the key discussion points and action items, in particular as they relate to numerous issues the Committee has been engaged with recently. In addition, a copy of the paper is also attached for your interest.

Briefing Note

Executive Summary

The paper opens with the following comment that is reiterated throughout the paper and is a key marker on which the Baillieu Government is positioning themselves as fiscally responsible:

Victoria is now one of only two states (along with resource-rich Western Australia) forecasting consistent budget surpluses over the next four years. It is the only state with a triple-A rating and stable outlook from both Standard & Poor's and Moody's.

The paper goes on to state that the key aims of the Baillieu Government's economic action plan is positioning Victoria as:

- *the state with the strongest finances, best able to contribute funding to major, productivity enhancing infrastructure as well as ongoing investments in new roads, public transport and other assets required to keep pace with population growth and maintain liveability;*
- *the state with the most cost competitive government sector, which responds to business and new investment, and delivers high quality and efficient services to Victorians;*
- *the state best positioned to accommodate and sustain growth and expansion;*
- *the Australian capital of the knowledge economy, with the most skilled workforce;*
- *the state with the strongest health, science, medical research and technology sectors;*
- *Australia's most globally-focused economy, and most Asia-capable workforce;*
- *a state with world class strengths in business services, food and fibre, freight and logistics, manufacturing, tourism, major events and cultural services; and*
- *Australia's arts and cultural capital.*

The key action items listed to achieve this strategy are:

- *Building a world class road network to link people, products and markets both in Melbourne and across Victoria.*
- *Working more effectively with the private sector to deliver new infrastructure projects, including using more competitive procurement processes.*

- *Implementing a clear framework for consideration of unsolicited private sector proposals for infrastructure investment.*
- *Streamlining Government processes for identifying surplus land and bringing it to market*
- *Accelerating planning and environmental approval reforms to increase certainty for businesses looking to invest in Victoria.*
- *Establishing new criteria for the Minister for Planning to act as the Responsible Authority to approve major developments.*
- *Establishing Major Investment Victoria (MIV) to proactively seek and attract new and productive investment in Victoria.*
- *Establishing a Coordinator-General of Investment to oversee all private sector investments facilitated by the Victorian Government.*
- *Cultivating Victoria's food and agriculture industry to strengthen Victoria's position as the nation's top agricultural exporting state.*
- *Undertaking the next wave of regulatory and public sector reforms aimed at reducing costs to taxpayers, business and the community*
- *Implementing a new regulatory reform agenda to reduce the regulatory burden on the community and business.*
- *Building on additional investment of \$1 billion in vocational training to create a more vibrant and higher quality vocational education and training (VET) system that responds to industry skills needs.*

Fiscal and Economic Context

Australian economic conditions and outlook

In an overview of the current economic conditions across Australia, the paper notes that conditions:

“were around trend in 2011-12 and while Australia's economy has generally been stronger than other advanced economies, performances vary across the nation. Trade-exposed industries like manufacturing, tourism and international education are experiencing significant pressures caused by the enduring high Australian dollar and global competition”.

Interestingly the paper notes that *“business confidence is being inhibited by policy uncertainty at the national level”*. Feedback we have received across sectors in Victoria however would allow one to feasibly extrapolate this particular insight to the State level as well.

Thinking positively, the State Government feel that *“concerns about the negative impact of a two speed economy on large and diverse economies like New South Wales and Victoria appear to have been exaggerated”* and that *“even with the challenges associated with a high exchange rate, the Victorian economy performed solidly over the last five years”*. This is based on the Gross State Product (GSP) result which showed an increase by an average annual rate of 2.3 per cent over this period, which was broadly in line with the Australian growth rate (2.7 per cent).

In regard to the labour market, the papers notes that *“conditions softened over 2011-12, with annual employment growth close to the low point recorded during the 2008 global financial crisis”* and further that the *“labour market outlook remains relatively soft, with job advertisements and business sentiment subdued”*.

Outlook for the Victorian Economy

Challenges for the Victorian economy

According to the Baillieu Government the key challenges for the Victorian Economy are mounting construction costs and productivity growth.

Mounting construction costs: and a series of substantial cost overruns on major infrastructure projects added to Victoria's costs of building essential infrastructure. Australian construction costs are higher than international benchmarks. Compared to the Canadian, German, United Kingdom, and American construction industries, Australia has some of the highest construction costs; in particular, for high-rise apartments, CBD offices, hospitals, schools and roads.

When compared to similar eastern capital cities (Sydney and Brisbane), Melbourne rates as the most expensive city for construction across a range of residential, commercial, industrial and infrastructure-related projects.

Productivity Growth: Over the last decade Victoria's productivity growth, which determines long run economic prosperity and living standards, has been easing. In the five-year productivity growth cycle ending 2003-04, Victoria's average annual labour productivity growth increased by 2 per cent, above the national average. In the latest incomplete cycle (ending 2011-12), it grew by an average of only 0.5 per cent, well below the national average of 1.1 per cent.

Opportunities for the Victorian economy

Amongst a range of opportunities for growth, the following are noted:

Australia's strongest finances - the paper reiterates the importance of budget surplus and the AAA rating:

Victoria is now the state with Australia's strongest finances. It is one of only two states forecasting consistent budget surpluses over the next four years. It is the only Australian state with a AAA/Stable outlook from Standard & Poor. The triple-A rating allows Victoria to minimise borrowing costs and provides capacity for expenditure on infrastructure and frontline services. If Victoria lost its triple-A rating it would face increased borrowing costs of around 0.44 percentage points, which would increase Victoria's interest bill by around \$226 million by 2015-16.

One of the discussions the Committee has had with a number of members recently is the question of just how much actual head room there may still be in borrowing capacity before the AAA rating is breached, and further, how integral the AAA rating is in the context of the cost of failure to stimulate the economy through investment in more major building projects, versus the cost of the additional interest that may be applied under a AA rating. While we don't have a definitive answer to this question, it is an issue that certainly bears more scrutiny.

As part of their **Economic and Fiscal Strategy**, the Baillieu Government lists rebuilding budget capacity as a key item and sets the following medium-term fiscal strategy and parameters:

- infrastructure investment of 1.3 per cent of GSP (calculated as a 5-year rolling average);
- reduced general government net debt as a percentage of GSP over the period to 2022;
- fully funded superannuation liability by 2035; and
- a net operating surplus of at least \$100 million and consistent with the infrastructure and debt parameters.

Australia's pre-eminent knowledge state. The importance of knowledge in a State that has few natural resources and is relatively small in size is highlighted.

Victoria has several of the best universities in Australia. According to The Times 2012-13 Higher Education World University Rankings, Victoria is home to Australia's top ranked university and is the only Australian state with two universities in the international top 100. In its first global rating of the best student cities, the London-based QS organisation recently ranked Melbourne fourth in the world – behind only Paris, London and Boston.

Valued at \$4.4 billion in 2011-12, education is Victoria's largest service export, constituting 30 per cent of Australia's total education exports.

Positioning Victoria as the knowledge capital of Australia is identified as a key element of the Government's **Economic Action Plan**. To achieve knowledge excellence, action items include:

Implement a range of governance changes for TAFE providers to place them on a stronger competitive basis with the private sector and support TAFEs to become financially sustainable by freeing them to negotiate their own enterprise bargaining agreements, reducing their reporting obligations, and encouraging and enabling them to improve the utilisation of their assets.

Capitalising on Victoria's world class universities: Consolidate Victoria's global leadership in international education to attract more international students seeking high quality education and experience living abroad in one of the world's most friendly, cosmopolitan and liveable cities.

Australia's freight and logistics capital. An effective and efficient transport network is identified as an essential foundation of any advanced, service-driven economy. The Government lists some of the key initiatives in achieving the aim of being Australia's freight and logistics capital as:

- *a \$1.6 billion port expansion project (at Swanson and Webb docks), including developing a third container terminal and a purpose built automotive facility at Webb Dock.*
- *development of the Port of Hastings will be advanced to provide a new container port with essential container handling capacity to provide for Victoria's import/export growth in the medium-term.*
- *providing high capacity connections linking regional Victoria, Melbourne's outer metropolitan industrial precincts and the State's export gateways as critical. The Regional Rail Link from Bendigo, Ballarat and Geelong is noted as a key aspect of this connectivity.*
- *Curfew free status of Tullamarine and the recent upgrade of Avalon airport to international status*

Victoria's six priority infrastructure projects as follows, are also listed as keys to freight and logistics:

- *East West Link connecting the Eastern Freeway to CityLink, the Port and M80 Ring Road.*
- *Melbourne Metro nine-kilometre rail tunnel between South Kensington and South Yarra, including five new stations at Arden, Parkville, CBD North, CBD South and Domain.*
- *Port of Hastings upgrading as an international container port, including planning for transport links such as the Western Port Highway.*
- *The Dandenong Rail Capacity Program staged construction of a series of projects along the Dandenong Rail Corridor.*
- *The Western Interstate Freight Terminal precinct at Truganina.*
- *The M80 Upgrade between Laverton North and Greensborough.*

Australia's largest exporter of food and fibre. Food and fibre export is seen as a significant opportunity for growth, particularly export into China:

Despite having only three per cent of Australia's arable land base, Victoria accounts for 29 per cent of Australian food and fibre exports. Victorian food and fibre exports were worth almost \$9 billion in 2011-12.

China is Victoria's top market for food and fibre exports, accounting for 21 per cent. The market more than doubled over the last four years. Victoria's 10 most valuable food and fibre export markets in 2011-12 were: China, Japan, New Zealand, Indonesia, Malaysia, USA, Singapore, South Korea, Hong Kong and Vietnam.

No specific action items for achieving this aim are identified in the paper other than to note that a strategy will be developed.

Australia's largest manufacturing centre. Despite the decline in manufacturing in some areas, the paper notes a number of positives on the manufacturing front:

Victoria is the hub of Australia's manufacturing industry. The sector is the State's single largest full-time employer, and a significant source of exports and investment. The manufacturing sector currently employs more than 300 000 people in Victoria.

Victoria's manufacturing sector has experienced significant adjustment to respond to intensifying competition, a high dollar, globalised supply chains, shorter product cycles and more sophisticated customers.

Some parts of the manufacturing sector expanded, including pharmaceuticals, cosmetics, confectionery and heavy engineering (following investment by the mining industry). These trends underscore the sector's increasingly specialised and customised product offering and its ongoing convergence with the services-based economy. As the sector transitions to higher value added products and niche manufacturing, management capabilities and workforce skills will become vital factors in business performance and competitiveness.

As part of the **Economic Action Plan**, assisting Victorian industries in a changing economy is a target area for Government, and while it is noted that "while governments cannot stop structural change, they do have a role in helping industries and workforces in transition". Action items listed to facilitate change include:

- *The Government's \$58 million manufacturing strategy, 'A More Competitive Manufacturing Industry: New directions for Industry Policy and Manufacturing'.*
- *The Victorian Government jointly funding with the Commonwealth a \$35 million program to support firms in the automotive supply chain to broaden and strengthen their product and customer base so they are less dependent on orders from local car makers.*
- *The Government has provided a \$4 million fund to attract new investment to Geelong.*

World-class liveability and tourist destination – the 'experience' economy. The importance of the sport, arts and culture to tourism is noted:

Tourism is worth \$15.9 billion to the Victorian economy, provides for 204 000 jobs and is the State's second largest export.

One of the areas missed by the paper in this context is the conferences and conventions sector, which is also a major contributor to the economy. The contribution these sectors combined make to the Victorian economy was highlighted in a recent Events, Conferences and Sport Forum help by the Committee in November last year.

Infrastructure and Transport

Infrastructure and transport is a priority item in the Baillieu Government's *Economic Action Plan*.

Entrenching Victoria's position as the state with the strongest finances and best ability to fund major infrastructure is seen as a key priority with the targeted aim of increasing the percentage of Government's infrastructure spend funded from operating surplus rather than new borrowing from 44% in 2010-11, to 84 per cent by 2014-15 under the Government's fiscal strategy.

The paper notes the *"Government's strong financial management enabled investment of \$5.6 billion in new roads, public transport, health and other infrastructure this financial year"*.

A key item of note from the Committee's perspective is the following support for the concept of using **Value capture to fund infrastructure**:

Not all the infrastructure that the State needs can be funded through the budget or other traditional means. There is a need to engage with the private sector to bring forward funding options for new infrastructure projects.

The Government will actively pursue opportunities for private investors to contribute to infrastructure projects by allowing a degree of private sector value capture to help fund these projects. This could take the form of development rights on land associated with infrastructure improvements or other forms of value uplift which a project facilitates. In some instances local authorities could partly co-finance projects which offer significant local benefits.

The Government will approach the market to sound out interest in value capture opportunities. Options will include bundled level crossing elimination projects as well as unsolicited private sector proposals for infrastructure investment which may involve innovations in project scope or financing structures. The Government will do this through a high level Ministerial committee, chaired by the Treasurer, to oversee the development of options for privately funded infrastructure projects. The committee will be supported by a group consisting of the Deputy Secretary, Commercial, Department of Treasury and Finance and private sector experts.

As you will be aware the concept of using direct and indirect user pays mechanisms to help fund infrastructure was raised in the Committee's *Moving Melbourne* paper released last year. This paper aimed to stimulate conversation and thinking on alternatives to Government only funding options, and we have discussed this paper and its concepts widely with both State and Federal Government and Opposition.

The comments in the Securing Victoria's Economy paper appear to be quite a shift in the previous "we will not toll existing roads" rhetoric of the Baillieu Government and provides some confidence that we can make some movement forward in eliminating our infrastructure backlog by considering more innovative funding options.

Bringing a more **commercial focus to infrastructure procurement** was also highlighted as a key action item.

In relation to PPPs, the Government released a consultation paper on 28 November that details options to reform the PPP model in Victoria, from an improved framework for assessing value for money, to initiatives to reduce the bid costs for PPP projects.

The Government will implement new reforms to make the model more attractive to potential bidders, as well as strengthening elements which protect the interests of taxpayers.

The Government will implement a clear framework for consideration of unsolicited private sector proposals for infrastructure investment.

On behalf of Members, (and with key input from PwC, Abigroup, E&Y, GHD, Bates Smart & Corrs, Chambers, Westgarth) the Committee made a submission to the PPP consultation paper identifying some areas where we felt change to existing practice was prudent.

Planning reform and land development

As part of their strategy to stimulate sustainable economic growth, the Baillieu Government have identified planning policy reform as a key item.

The Government's strategy is to stimulate sustainable economic growth. This will be done as an element of planning policy, which will promote flexible land use and economic adaptability. In addition, the Government will pursue a new approach to the appropriate development of public land, including a strategy to bring substantial areas of surplus government land to market. This strategy will unlock and maximise the economic value inherent in Victoria's land assets.

Amidst a range of action items, two areas that have been raised by Members as issues of concern in particular are planning approval processes and absence of a long term vision. The Baillieu Government indicates they will take action to:

- *Accelerate and streamline planning and environmental approval processes to increase certainty for businesses seeking to invest in Victoria.*
- *Build confidence in Melbourne's planning system and support for its long-term vision by re-engineering the structure and functions of the Departments and Agencies involved in policy development and implementation to align with the Government's policy objectives.*

Private sector investment and employment

The paper identifies Victoria's diverse sectors as keys to new opportunities to drive investment and growth. Victoria's proximity to Asia also presents new investment partnership opportunities in major projects.

The Government states it will be "*more proactive and aggressive in investment attraction and facilitation to identify, promote and support private investment into the State*" in order to ensure Victoria remains a leading state in attracting private investment and footloose capital.

Some of the initiatives noted to achieve this outcome are:

- *Establish a new investment body – Major Investment Victoria, to attract new and productive investment to Victoria. MIV will have as its mission to pursue significant investment opportunities for the State to assist economic growth. The new body will have an independent and expert Board*

and Chairman, reporting direct to the Premier. Its role will be to raise Victoria's investment profile across Australia and internationally by proactively advising on, identifying and capturing significant investment opportunities.

- *Establish a Coordinator-General of Investment to oversee all private sector investments facilitated by the Victorian Government.*
- *Develop and release a 10-Year Victorian Investment Attraction Strategy.*
- *Create Investment Agreements for all major investments facilitated by Government to improve accountability and transparency.*
- *Cultivate Victoria's food and agriculture industry to strengthen Victoria's position as the nation's top agricultural exporting state and capitalise on export opportunities.*
- *Make Victoria a global hub of mining and mining services, to help Victorian businesses better participate in the mining boom and develop Victoria's earth resources to unlock the value of this sector, for example by pursuing further development of Victoria's brown coal reserves to maximise the benefits of the resource and its contribution to the State's economic activity and development.*

Public sector reform to boost growth

Given that Victoria's Government sector comprises around 15% of GSP, making the sector more competitive and responsive is seen as key. The Action Plan to achieve this outcome includes initiatives to:

- *Extend the Essential Services Commission's (ESC) focus to encompass a wider range of government entities providing services to, and imposing costs on, households and businesses.*
- *Establish a Cost Control and Efficiency Unit within the Department of Treasury and Finance. This will augment the ESC's price regulation and benchmarking role, and provide focused and specialised in-house advice to government entities to generate ongoing efficiencies in their operations.*

Taxation reform

Taxation reform is also noted in the paper, and while much of the taxation responsibility falls at the Federal level, two important State focused initiatives are noted:

- *Work with other states and the Commonwealth to identify opportunities to reduce states' reliance on narrow, economically inefficient stamp duties.*
- *Review state taxes to identify opportunities to reduce the tax burden and cut the compliance costs of existing taxes.*

In closing, the above outlines some of the key aspects of the Baillieu Government's strategy for securing Victoria's economy as they relate to some of the key items the Committee has discussed in recent times. This brief is an overview only however, and there are many other initiatives and actions that are not included in this brief but can be found in the full strategy document.

The Committee will continue to work on these issues and many others as 2013 progresses.



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