Ten Policies to Drive Australian Productivity Higher

For the last twenty years, Australian governments have frequently discussed productivity reforms but have taken little action. Australia's GDP per capita recession over eight of the last nine quarters highlights the economic malaise since the Financial Crisis. Government policy over this period has often been characterised by excessive and wasteful government spending, government debt being accumulated with little benefit to the vast majority of citizens and policy decisions made for political purposes rather than the benefit of the country. Government is the cause of much of the productivity problem and the primary barrier to fixing it.

The ten sections that follow focus on policy reforms that the Federal Government can either implement directly, or with assistance from State Governments, who would be incentivised to act by having a much greater share of their funding from their own dedicated revenue sources.

Tax Reform

A good tax system encourages individuals to work, save and invest. Australia's tax settings, when combined with the RBA Cash Rate and welfare settings, encourage Australians to bludge, borrow and speculate. Numerous tax reviews have called for reform including:

- Shifting the tax base from income to consumption (GST),
- Replacing stamp duty with a broad-based land tax, and
- Strengthening measures against tax evasion, capturing the tens of billions of potential tax revenue lost each year to the black economy.

The recommendations below have had minor updates since first being published in a 2015 paper.

Company, Trust and Personal Income Tax: 20-25% Flat Rate

A flat tax rate supplemented by an earned income tax credit for low-income earners is optimal. Earned income tax credits allow only low-income earners to have a tax-free threshold, with higher income earners paying the same tax rate on each dollar earned. Closing loopholes, eliminating special interest deductions (e.g. removing lower rates for capital gains) and add-ons (the Medicare levy and surcharge) will greatly eliminate complexity. Closing loopholes is an extremely progressive change as the wealthiest companies and individuals take the most advantage of loopholes and tax structuring techniques. Negative gearing and franking credits will be far less attractive if a low flat tax is implemented. The inclusion of trusts is a simple correction that ensures all structures that receive income are taxed evenly.

Whilst it is often argued that a lower company tax should be prioritised, both companies and highly skilled individuals are easily able to relocate to other countries. Australia should not only encourage the best companies to operate here, but also the most productive and talented individuals to work here as well. A large pool of highly skilled workers is one of the biggest attractions for multinational companies in determining where their offices will be located.

GST: 15-20% with Minimal Exemptions

The GST needs to be raised and almost all exceptions removed, just like New Zealand. Some additional welfare assistance may be necessary for the poorest 10-20% of the population, but the remainder of the population will benefit from lower rates of income tax and will not need additional assistance.

Land Tax: 0.8%-1.25% Per Annum on All Land

Economic research almost always agrees that the most efficient major source of tax revenue is land tax. The property industry and political class in Australia have long forgotten that property is firstly a place for people to live and work, and secondly an investment opportunity. Introducing a land tax will help correct the excessive debt and speculative investment attracted to property and will shift that capital to far more productive sectors of the economy.

In terms of social impacts, lowering the cost of housing (primarily rent but also the cost of purchasing) is the most pressing issue for low-income households. Affordable housing near public transport hubs is rare for most capital cities. Reducing the cost of housing will greatly decrease the welfare expenditure for both State (public housing) and Federal (unemployment benefits and pensions) governments. Vacant properties (occupied less than six months per year) should face triple land tax rates, increasing the rental supply and revitalising local economies.

Small Business and Personal Tax Evasion

Three relatively simple measures of mandatory record-keeping and payment methods would significantly reduce tax evasion among small businesses. Every sale should be electronically recorded, with a receipt available. Businesses should also be required to offer a form of electronic payment. The upcoming credit card surcharge reforms will assist this transition. Mandatory electronic payment of wages will increase tax compliance and reduce wage theft.

Once the acceptance of electronic methods of payment is required, the job of monitoring and enforcing tax compliance becomes far easier. ATO employees/contractors and the public could retain receipts, which can then be cross-checked against business records. If a sample of transactions reveals some are undeclared for GST or income purposes, it likely indicates tax evasion, triggering a full audit.

A second, powerful measure is the introduction of a national tax lottery. The ATO should operate a well-advertised online and phone service allowing citizens to report suspicious activity, such as offers of discounts for cash payments or refusal to issue receipts or accept electronic payments. Each report would grant an entry into a nationally broadcast monthly lottery with a substantial prize pool (e.g $50 million). Prizes could include ten winners of $1 million and 40,000 winners of $1,000.

Large Business Tax Evasion

Large business tax evasion often involves complex, multiple-jurisdiction schemes. Gathering evidence frequently requires whistleblowers with inside information, such as employees, accountants, bankers and lawyers. While well-crafted whistleblower protections sound good in theory, they frequently fail to prevent retaliation, including dismissal, demotion or being sidelined. Employees who report white collar crime often risk their careers and may become unemployable in their industry once exposed.

The solution is a revenue-sharing arrangement. In the US, the tax service (IRS) and the securities regulator (SEC) pay up to 30% of the additional revenue collected to whistleblowers. This substantial incentive encourages the reporting of tax evasion and financial crimes. It creates major headlines when large fines and penalties are imposed and when significant payments are made to whistleblowers. This system deters financial misconduct, increases the likelihood that impacted whistleblowers are compensated and increases government revenue.

NARROW ROAD CAPITAL

Decrease Government Spending

One of the great truisms of modern economies is that economic growth and prosperity increase fastest when government spending is a small share of the economy and economic freedom is maximised. If we want Swiss-level wages and wealth, we should reduce government spending to Swiss proportions. Studies have repeatedly shown that the private sector drives almost all productivity growth, with the government sector typically neutral or negative. It is therefore no surprise that the global productivity slowdown has coincided with increased government spending since the Financial Crisis.

Examples of wasteful government spending include the NDIS, infrastructure blowouts, bailout and subsidy schemes, programs for remote communities and numerous Defence initiatives. These highlight a lack of accountability among politicians and public servants; spending other people's money on other people is a recipe for inefficiency.

Some suggestions to improve the attitude to spending amongst politicians and public servants:

- Requiring government reports to consider both the loud minority asking for increased spending on their areas of interest and the silent majority who would prefer a tax cut,
- Bonuses for politicians who keep government spending growth below inflation, with a double bonus if nominal spending declines,
- Bonuses for public servants who cut spending and sackings for those overseeing wasteful projects, and
- Starting parliamentary and department meetings with an acknowledgement of taxpayers and the historical waste of taxpayers' funds.

Reduce and Sharpen Migration

Australia's migration system shifted from prioritising quality to pursuing quantity around 2006. Since 2022, record-high migration levels have brought in large numbers of low-wage workers and students enrolled in low-cost courses. The obvious impacts include:

- Skilled migrants earning less than the median Australian worker, indicating their purported skills are not translating into workforce participation,
- Capital shallowing, with population growth outpacing investment,
- Sharp rises in housing costs, despite higher interest rates, and
- Reduced savings and increased speculative investments in housing over productive business activities.

A recent paper on this topic highlights these issues and the obvious policy solutions, including:

- Limiting skilled migration predominantly to those with a job offer paying at least $150,000 per year,
- Restricting international students primarily to high-value courses, and
- Requiring international students to depart shortly after completing their courses, unless they have a job paying at least $150,000 per year.

Increase the RBA Cash Rate

Over the last decade, CPI inflation has averaged 2.78%, within the RBA's inflation target range of 2-3%. Despite this, the RBA Cash Rate has averaged 1.84%. After adjusting for the top tax rate of 48.5% (including the Medicare Levy and Medicare Levy Surcharge), a measly 0.95% nominal return is left, which equates to a -1.83% real return. This blatant subsidisation of borrowers, at savers' expense, undermines the RBA's mandate "to promote economic prosperity and welfare of the Australian people, both now and into the future".

The most noticeable outcome is Australia's obsession with residential property fuelling high house prices, excessive debt and distorted capital allocation. The speculative diversion of capital into property reduces business investment, increases financial instability and perpetuates boom-bust cycles.

Two policy changes would help correct this:

- Adjusting the inflation target from 2-3% to a ceiling of 3%, acknowledging that low inflation is a benefit of productivity improvements,
- Requiring the RBA to set the Cash Rate at a level that ensures all Australians can earn a positive after-tax real return over the medium term.

Curtail Corporate and Middle-Class Welfare

Corporate Welfare

There's an old saying in economics that "Governments are bad at picking winners, but losers are good at picking governments." Politicians typically ignore the much larger pool of jobs lost when taxpayer funds are wasted on unprofitable activities and industries, compared to the small number "saved" by them. Australia's decades-long subsidisation of the car industry and the continued support for aluminium smelters and steelworks are prime examples. Taxpayers have paid billions to delay inevitable closures, preventing workers and capital from moving into more productive sectors.

Australia's high costs for electricity, labour, property and regulation mean it cannot compete in most manufacturing sectors. We need to get past the idea that we should be a manufacturing powerhouse; our decisions in other areas (e.g. renewable power, minimum wages, excessive migration) make manufacturing in Australia uncompetitive.

The default answer to corporate welfare requests should be "no", except in industries critical to national defence. This includes declining to support farmers and small business owners, especially those operating in disaster-prone areas.

Middle-Class Welfare

Taxing middle-income Australians, wasting a substantial portion on bureaucracy, then handing it back as welfare is inefficient and discourages families from working. Reducing middle-class welfare alongside substantial income tax cuts would make this reform easier and fairer.

Incentivise Reliable Power Generation

Australia has shifted from having some of the most affordable electricity in the developed world to some of the most expensive. Unlike countries with nuclear power, Australia's historical reliance on coal is now a hindrance in a decarbonising world. Current policies have made the system less stable and more costly. Temporary subsidies masking price rises will end, likely triggering consumer backlash and demands to halt the energy transition. System-wide blackouts, as recently seen in Spain and Portugal, are expected to increase, undermining consumer confidence and business profitability. The wave of bailout requests from high-power users this year is a predictable outcome of flawed policies.

The solutions involve three parts:

1. Incentivising reliable, around-the-clock generation through intra-industry payments. Unreliable producers (wind and solar) should compensate those who provide stability (base load, peak producers, hydro and storage),
2. Requiring generators that demand significant grid expansions to share the costs, favouring those who build near retiring coal plants where infrastructure is already in place, and
3. Taxing gas production on both extraction (royalties) and profits, ensuring hydrocarbons are treated like most other commodities. This should be part of a broader federal review aimed at a national royalty framework. Alternatively, governments could trade-off royalties in exchange for a guaranteed affordable supply of gas.

Simplify the Minimum Wage

Australia has two major problems with the minimum wage: it is too complicated for small businesses to easily comply with, and it is too often not being paid in full to workers. Small businesses should be able to access a government-run website offering a simple one or two-page guide explaining the minimum wage and key conditions (leave, casual loadings etc.). They shouldn't have to navigate complex industrial awards. There should be a single national minimum wage, with businesses free to negotiate better terms with workers or unions. Workers would always retain the right to move between employers in search of better conditions.

Once a clear, standard minimum wage is established, excuses for underpayment disappear. Systemic and deliberate wage theft should result in prison terms, just like other forms of fraud or theft. Business owners and managers should face punitive damages payable to affected workers, along with significant government penalties to cover enforcement costs. Wage theft is a widespread scourge, robbing workers, honest competitors (who pay the minimum) and other taxpayers. The brazenness of wage theft in the hospitality industry has been well documented, with universities and supermarkets also recently exposed for widespread underpayment.

Get Unemployed Australians into Work

Australia's unemployment system currently allows recipients considerable freedom to apply for jobs that they want, not necessarily those they are suited for. It also allows for "cash in hand" work while receiving unemployment benefits.

A better approach for medium and long-term unemployed Australians receiving benefits (e.g. 6+ months) is to require them to select from nearby job openings and start work immediately. In many suburbs, there are likely to be a range of entry-level roles in cafes, restaurants, supermarkets, transport and delivery services or cleaning. The ideal time to implement this is now, when the unemployment rate is low and job vacancies are abundant.

From a productivity perspective, the benefits are clear:

- Lower welfare payments and higher tax collections,
- Increased tax compliance,
- Improved long-term employment prospects for participants, and
- Broader society-wide benefits including reduced crime and better mental health outcomes.

Enable School Choice

Research from the US consistently shows that non-government schools deliver better student outcomes at a lower cost to taxpayers. While the quality of outcomes remains debated in Australia, it is clear that non-government schools cost taxpayers less. Australia should join the growing group of nations that give poorer families school choice, just as wealthier families already have. Well-run government schools have nothing to fear, they are likely to attract students from underperforming schools.

The structure of voucher payments is simple; state governments calculate the per-student cost in public schools, factoring in teachers, administration, capital/building costs and materials. This amount forms a voucher parents can use towards private schooling. To avoid favouring elite schools, there can be a declining scale to taxpayer contributions as the fees increase. For example, the first $2,000 of fees do not reduce the voucher, but from there on the voucher reduces by 50 cents for each dollar of fees. Schools charging more than a set fee level, say $15,000 per year (primary) or $25,000 per year (secondary) would be ineligible for voucher funds.

Make Childcare Tax-Deductible

French economist Frederic Bastiat famously said, “Government is the great fiction through which everybody endeavours to live at the expense of everybody else.” The Federal Government’s ever-increasing subsidisation of childcare is a prime example, aimed at buying votes from young families. These subsidies have pushed up demand, inflated prices and allowed lower-quality operators to gain a foothold. Government-driven wage increases, the growing regulatory burden and Australia’s high property prices further compound the issue.

The Productivity Commission found that recent changes (increasing subsidies and the relaxation of requirements to work) have had little impact on the supply of labour, which is the primary reason for subsidising childcare. Paying people to care for children while the parents do little or no paid work is inherently unproductive.

The solution is simple and effective: remove direct subsidies and allow childcare costs to be tax-deductible when all parents in the family are working. This would target support to higher paid working families, ensuring benefits flow to those expanding the economy and easing the excess demand pressures.

Written by Jonathan Rochford for Narrow Road Capital on 21 July 2025. Comments and criticisms are welcomed and can be sent to info@narrowroadcapital.com

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