

## Chapter 22

# Competing from a High Cost Economy: What is the Challenge to Australian Public Policy?

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### ABSTRACT

*The starting point for this chapter is that Australia is a high-cost economy with a fading resources boom and a diminished domestic manufacturing sector. The chapter explores the fresh challenge that these structural developments present to public policy. It argues that this requires a shift from the dominant neo-classical policy paradigm, which has to date provided the intellectual muscle for a transformation of Australia's political economy. The chapter makes the case for policies framed to foster innovation and knowledge as the approach needed for Australia to succeed in an environment characterised by the new international distribution of manufacturing, the impact of new technologies, and the prevalence of global supply chains. To realise innovation-based economic renewal requires capacities for much more targeted interventions that engage business at cluster, sectoral, and/or regional levels. The chapter concludes by considering the obstacles to, and the possibilities for, policy change.*

### INTRODUCTION

Australia is a high cost economy with a fading resources boom and a diminished domestic manufacturing sector (Roos, 2012, 2013). This chapter explores the fresh challenge that these structural developments present to public policy. This, so it argues, involves a shift in the focus of policy towards innovation, with particular attention to manufacturing and start-ups. This

approach already receives rhetorical - and limited substantive - support from federal and state governments.<sup>1</sup> As the chapters in this book suggest, this is insufficient. The challenge is fundamental and wide ranging. It involves assimilating a new policy paradigm (Hall, 1983), which cuts across the current conventional wisdom, based in neo-classical understandings of economic dynamics. Since 1983, this stream of conceptual and policy ideas has provided the intellectual muscle for a

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transformation of Australia's political economy. But, as has recently been convincingly argued, the new international distribution of manufacturing, the impact of new technologies and the prevalence of global supply chains combine to create a new international economic context (e.g. McKinsey Global Institute, 2012; Gereffi and Lee, 2012; Herrigal and Zeitlin, 2010). This coincides with the end of the resources boom in Australia and the emergence of substantial new domestic economic challenges including employment, skills and growth (e.g. Garnaut, 2012; Parkinson, 2012).

This is encapsulated in the broad idea of a 'knowledge economy'. This phrase points to the transcendence of commoditised activity, which remains the basis of much economic and industrial practice. In this world, knowledge is often secondary to other considerations like scale or efficiency – but in the context of a given technology. In the past decade, commoditised manufacturing has moved to low cost and low wage settings. Opportunity now lies in products and services that are much more responsive to individual tastes or business needs – indeed in the best case they shape these tastes and needs – and to a dynamic based on technologies that cut costs and enhance quality. A myriad of contemporary innovations sustain these opportunities. Indeed fully realised the idea of a knowledge economy extends beyond any narrow technical conception. A knowledge economy is embedded in a society that nourishes creativity, imagination and risk taking, one that welcomes these disruptions to conventional ways. In the best case, this is the vision of an open society, one whose citizens are alert to emerging economic and other challenges and who do not balk at the adjustments that adaptation requires. Utopian? Perhaps. But, to sustain their ways of life, economically advanced societies would seem to have few alternatives.

So knowledge-driven innovation and entrepreneurship may hold the key to economic renewal (Roos, *op cit*). But realisation requires a new conception of the economic role of the state and

new capacities for federal-state collaboration. It requires capacities for much more targeted interventions that engage business at cluster, sectoral and/or regional levels: in other words, relationships that are different from the arms-length and hands-off philosophy that currently prevails. A theoretical framework for this approach is available in the concept of a knowledge economy and its associated focus on the development of specific economic capabilities (e.g. Lipsey et al, 2008; West 2013; Pedersen, 2010). This concept represents both a next step beyond the neoclassical focus on economy-wide deregulated markets and a response to the competitive challenge in a high cost economy.

This is now well recognised in economies whose economic maturity and basic cost structures more or less resemble those of Australia, notably the United States. There, as well as in Britain and Canada, a variety of programmes that involve new catalytic and leadership roles for the state are either being implemented or discussed. These include collaborative engagement and strategy development at regional and sectoral levels. They involve a focus on economic capabilities that are based in shared infrastructures, most importantly concerning knowledge development, but also involving training, communications, logistics, finance etc. They ask if relevant upstream, downstream and spill-over capabilities are appropriate to the needs of particular contexts. In this exercise, business, universities and other research and industry bodies are partners. In other words, in a knowledge economy, relevant actors collaborate in thinking systemically about common sources of economic leverage. In a federation like Australia, this especially involves working across levels of government. Moreover start-ups present a special case. Where innovation is concerned, their consolidation can become a particular priority for public policy (Mazzucatto, p. 37-39).

Such roles for the state are a world away from the conventional wisdom that currently informs policy in relation to industry. They include a posi-

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