

## **Full employment and low inflation: Can we pull it off?**

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**T**o know where we are going, we need to look at how we got to where we are now.

Our economy and the employment market has undergone massive upheaval in the past few years, driven largely by the immediate and lingering impacts of COVID and our subsequent response, after decades of relative stability and, one could argue, some underperformance, especially on the productivity front.

We are now in a period of relatively high inflation and relatively low unemployment as well as underemployment with cost of living and cost of business pressures weighing on both inflation and employment.

The old normal has been upended but our productivity challenge still looms large.

As we look to the future our labour market is drum tight, our skills needs are immense and the rapidly changing environment around us is challenging.

So, can we achieve the daily double of low inflation and low unemployment?

I want to look at the situation through the lens of “structural unemployment”, not just now but into the future, and look at how to address our needs starting with our basics, our foundations, in meeting our skills needs which will then drive better employment prospects and outcomes.

**Full employment and inflation**

In its Employment White Paper, the Government defines full employment as occurring when everyone one who wants a job can find one without having to search for too long.

We currently have official unemployment hovering a bit above 3.5% and official underemployment at about 6.5%.

In the Employment White Paper, the Government adds to this an estimate of unofficial unemployment and comes up with around 2.5 – 3 million people who either are not currently working but want work or who are working but want to work more hours.

At the same time, just about all the experts, and certainly those at the Reserve Bank, are saying that we are currently at the point where we have very little spare capacity in the economy.

To subdue inflation, which remains stubbornly higher than its preferred 2-3 per cent target range, we need activity to slow down.

And the Reserve Bank is saying it expects unemployment to rise to around 4.5% by the time it expects inflation will fall so that it is within the target range of 2-3%.

One way or another there is something of a disconnect here.

### **Structural unemployment**

A good part of the disconnect is explored extensively in the Employment White Paper in terms of “structural unemployment”.

The idea of structural unemployment was also raised by then Deputy Governor of the RBA Michelle Bullock back in June in a speech at an Ai Group function.

The notion that unemployment might have to rise as activity slowed as the result of inflation and interest rate pressures caused some consternation at the time. Quite why it caused that consternation is bemusing to say the least.

A key element in structural unemployment is the mismatches between available job vacancies and the skills of people who are looking for work.

The more extensive these mismatches, the greater the level of structural unemployment and the further we are away from ‘full employment’ as defined in the Employment White Paper.

When these mismatches and structural unemployment are high, the level of unemployment consistent with low inflation will also be high.

These mismatches are very real.

- Throughout 2022-23, job vacancies in Australia were consistently above 400,000 with more than a quarter of businesses reporting unfilled positions.
- Over the same year, the number of people officially recorded as unemployed averaged slightly more than 500,000.
- A leading reason for this disparity was the lack of applicants with suitable skills or experience with around 60% of businesses looking to hire reporting this as a reason for their difficulty in finding staff.
- This was more than matched by the number of businesses who reported receiving no applicants for positions at all. It's a fair bet that a large share of this was the result of applicants ruling themselves out of contention because they did not have the skills sought.

Let's look forward. What are factors bearing down on us as we seek to skill up, not just for now but for the future?

The trend lines are pretty clear. We like to look at them as a series of Ds: Disruption, diversification, digitalisation, decarbonisation, demographics and debt.

We live in a time of disruption. Look at the impact of geopolitics, military conflicts and pandemics.

We live in a time of diversification. Business is constantly looking for new product, new sources and new markets. Think of the China plus one strategy many businesses globally are adopting.

We are seeing massive digitalisation occur. Technological change is immense as business adapts to and embraces artificial intelligence, automation, robotics, machine learning and more.

We are pushing towards a decarbonised future with new energy sources and needs increasing driving business decisions.

Demographics are changing. We are ageing, urbanising and migrating more than ever before.

And we are saddled with debt - government in particular - as we face up to these challenges.

### **Towards “full employment”**

So, achieving real progress towards full employment as defined by the Government in the face of these challenges will require a wide range of measures aimed at reducing if not eliminating structural unemployment.

- Equipping future generations of workforce entrants with skills for in-demand jobs. This will require effort and improvements all along the learning spectrum.
- Early Childhood Education.
- Schooling.
- Vocational and other higher education.
- Life-long learning.
- Skilling programs for people who are currently unemployed and those who have been discouraged from looking for work. This is an enormous task – even in today’s tight labour market we are talking about something like 1.5 million people.
- Re-equipping people who are currently in the workforce so they are better prepared for future disruptions – both known and unknown.

In addition, we will need to make progress on:

- Reducing barriers to relocation – availability of housing and high costs of home purchase.
- Regional development policies.
- Policies targeted at areas of entrenched disadvantaged – for instance: indigenous Australians and people with disabilities.

### **The importance of foundation skills and workplace-based foundation skills development**

Where do we start?

While skills mismatches can conjure up images of too few highly qualified specialists available to fill top end positions, a leading contributor to the lack of suitability of job applicants is the deficit of basic skills in the areas of literacy, language, numeracy and digital capabilities.

According to a recent Productivity Commission Report an estimated 20% of Australians do not have adequate levels of foundation skills.

Those people are not only less likely to be successful in any particular job application, they are more likely to remain unemployed and are also more likely to be discouraged from continuing to apply for positions.

In a dynamic economy in which existing jobs can be threatened by shifts in markets, competition and technological developments, the challenge goes well beyond the greater likelihood of people continuing to be unemployed. It also goes to the vulnerability of the many people with low levels of foundation skills who are currently in the workforce.

They are currently employed but, particularly in the face of the sorts of disruption we know the economy is facing and will continue to face, they are vulnerable to the threat of future unemployment and underemployment.

And beyond that, a more complete set of foundation skills, is a gateway to further skilling opportunities.

We need focus more, much more, on workplace-based programs to develop the foundation skills of the existing workforce as an important complement to other channels – such as in early and school education and in programs targeted to particular groups.

Why workplace-based programs?

They can be linked to work and tailored to fit with particular workplace requirements.

They can tap into interests shared by employers and employees:

- The employer will often have a real business interest in the development of these skills and will be prepared to contribute to and facilitate the take up of workplace-based programs.
- The employer interest can stem from a lift in productivity; improvements in workplace safety; and as an assistance to employee retention.
- The employee interest can be related to job security, increased optionality and the prospect of higher pay.

The interests of employers and employees in the development of employees' foundation skills may well be able to secure a degree of resourcing for workplace-based programs of this sort.

That said, there is going to need to be the collaboration of public sector support. Funding support is vital particularly for smaller and medium sized businesses to ensure that gaps are filled and opportunities are not missed.

### **Closing comments**

We need to do more to do better on unemployment – and underutilisation more broadly – than we have done over the past half century.

It is a huge task ahead of us to adapt and upskill millions of people to make serious gains towards the Government's objective of full employment.

To put it bluntly, to have the jobs of the future we need the skills of the future.

It's a national effort that will require support of government, business, workers and educators. No one sector can do it alone.