

**The 10 numbers Australian governments need to  
change**

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# The 10 numbers Australian governments need to change

## 1 WHAT IS AUSTRALIA'S STRATEGY?

### 1.1 What does "strategy" mean?

"Strategy" is an over-used word. Often it is a synonym for "expensive", as in: "I am a strategy consultant". Sometimes it is a synonym for "unjustifiable", as in: "this is a strategic acquisition".<sup>1</sup>

At its best, "strategy" is a synonym for *choosing the important*, based on *rigorous analysis* and *prioritisation*. It requires "decluttering" the mind to focus on a handful of things that will make a big difference in the long run.

### 1.2 Strategy means a long-run focus

Commonwealth public sector leaders, Ken Henry and Terry Moran, have emphasised how good public policy needs to focus on the important *in the long-run*.<sup>2</sup>

This is hard. We are biologically hard-wired for the short-run. A Stanford professor of Psychology investigated delayed gratification. He put four year old children in a room with a marshmallow. He told them he was going out of the room for 15 minutes. If they could wait until he got back, without eating the marshmallow, he would give them two.

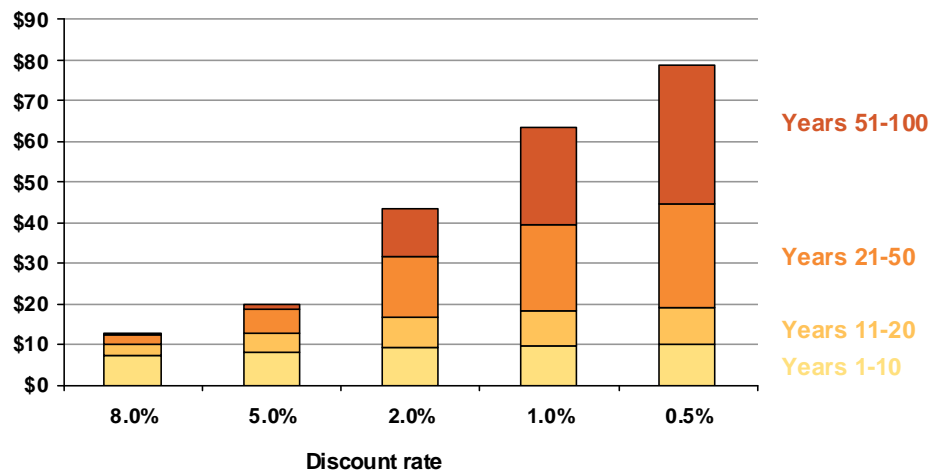
Two thirds of the kids couldn't wait.

The third that waited not only got an extra marshmallow, they went on to earn SAT scores 210 points higher than the kids who only lasted thirty seconds.<sup>3</sup>

Public finance theory can exacerbate short-termism. One of the basic questions in cost-benefit analysis is how to value short term benefits relative to long-term benefits. In classic finance theory, this is calculated using a discount rate. By applying a high discount rate, the benefits of the long term are small. Apply a low discount rate; the benefits of the long-term dominate. In choosing between a quick fix program and a long-term program, your decision will be driven by your discount rate.

#### Valuing the future

The value today of \$1 every year



Regrettably, public finance often uses higher discount rates. The analysis borrows from the private sector, but it does not always consider that governments are responsible for long-term inter-generational equity.<sup>4</sup>

This is the first number that Australian governments need to change: a small lever that will make a long-term difference.

The problems of instant gratification and future discounting are compounded by real politics.

Governments worry about re-election. They're media driven. We can hardly complain – we live in a democracy – that is the idea. But it is hard to stay with a few big priorities, without getting distracted.

### **1.3 Identifying what's important takes rigorous analysis**

Sometimes an issue is important because it sets in motion forces with collateral impacts. In America, President Obama has made e-health a key priority, not just because it will provide efficiency gains, but in the long-run it will enable analysis of which treatments work best.

The important can be simple – and so easily overlooked. For example, the Institute for Health Initiative in the United States identified what would make the biggest difference in health care. They found an initiative that halves death rates in surgery, and reduces complication rates by 35%.<sup>5</sup> Their “high-tech” initiative: a one-page checklist to be used in every operation that requires the nurse to ask such complex questions as “how shall I record the name of the procedure?”, and “how shall I label the specimens?”. Implementation, however, requires people to change their behaviour, often the hardest change of all.

Grattan Institute will always be aiming to use its analysis to identify the wood from the trees.

### **1.4 Acting on what's important takes ruthless culling**

Many businesses aim to do 30 things for the year, and then wonder why they haven't done the four things they really cared about.

The scarcest resource is senior management time. These are the people with the authority to push other things out of the way. Their time is limited: they can't afford to shepherd many things. It is hard to make change happen; it's even harder to stop things, which always seems to involve killing somebody's pet project. But stopping things creates time to do the stuff that really matters.<sup>6</sup>

Single minded focus gets stuff done: deregulating Australia's financial markets despite Treasury opposition; imposing a goods and services tax; privatising Victoria's State utilities. Whether good, bad or indifferent reforms, they were achieved despite enormous political hurdles through single-minded focus.

### **1.5 Grattan Institute will encourage Australian governments to do better in pursuing the important over the long-term**

Politicians enter public life to make a difference. Public life, however, inevitably drags them into the short-term.

Think tanks have the rare privilege of being outside of the news cycle. We can be the angel on the shoulder of senior decision-makers, encouraging them to do the important rather than the urgent. We can also elevate the community debate and engagement on issues. When you win the hearts and minds of the public, politicians tend to follow.

The public are smart and want to do the right thing, but they are also busy. We can *identify* the important, explain *why* it is important, and *remind people* of the important. We have

more time, we have the analytical resources, and we have the ability to speak the truth publicly without fear of the consequences.

This is why think tanks need to be fiercely protective of their independence.

In theory, governments understand that long term projects, divorced from the electoral cycle improve the “commonweal”.

That’s why both Victorian and Commonwealth governments provided substantial contributions to Grattan Institute’s endowment – a perpetual fund that provides the freedom to speak without fear or favour.

## **2 IN PURSUING STRATEGIC ENDS WHAT ARE THE FUNDAMENTAL AIMS OF PUBLIC POLICY?**

Is it all about money?

### **2.1 That depends on your political philosophy and ethics.**

I know that it’s risky using those words in public in Australia where it’s OK to talk about conga lines, but philosophy is seen as some kind of French disease. At an Ideas Festival, I’m going to take the risk.

Grattan Institute is committed to improving Australia as a “liberal democracy in a globalised economy”. This implies that there is value in both the individual’s freedom to choose, and the collective pursuit of the common good – enabling each individual in society to experience the fulfilment of the many ends that constitute a good life. This implies a need for pragmatism and balance rather than pursuing any one value to the exclusion of the others.

### **2.2 As a “*liberal*” country we believe that we ultimately get better results if people can choose for themselves.**

Choosing itself can be intrinsically valuable, and individuals may often choose more wisely than a central government. It is also implicit that our basic values all boil down to *individuals* experiencing the various good things in life – rather than the success of a group of people being an end in itself.

However, choices are often influenced by information and surroundings, to which governments contribute. As one lab rat said to another, “this scientist is well-trained to provide cheese whenever we run down the right-hand alley of the maze.”

### **2.3 As a “*democracy*” we believe that we ultimately get better results if public elections determine the shape of government.**

And there is an egalitarian aspect to liberal democracy which implies that we are pursuing the common good – so that the under-privileged as well as those who are well-off can experience meaningful lives, including the ability to make choices for themselves.

Again, we need to be careful about what version of “equity” we impose. Otherwise we join “Napoleon Pig” in claiming that, “we are all equal but some pigs are more equal than others.”<sup>7</sup>

### **2.4 As part of a “*globalised economy*” we believe that we ultimately get better results through international trade.**

But this economy relies on government regulation to set up markets in the first place, and to ensure that their side effects are managed.

## **2.5 Good public policy requires us to balance *all* these values**

We cannot simply assert that one value consistently trumps the others. Choice is not the only thing that matters, and nor is equity. And I suspect that many Australians, with varying political allegiances, have the same attitude.

Similarly, Grattan Institute has no preconceived view on whether or how government should promote the common good on any particular issue. Our role is to identify the evidence of what will work best in the circumstance. And this approach also fits with Australia's founding myths; the bush philosophy of pragmatism rather than following theory irrespective of the consequences.

Sometimes this will make Grattan Institute's life more complicated – because ideology doesn't constrain our solution set. It should make our recommendations harder to predict. We will be driven by the evidence, and balance the relevant values in the circumstances.

When you do the analysis, there are often "no regrets" actions that are worthwhile no matter how you trade-off different values. To take one of the most vexed examples in US politics, abortion, President Obama suggested recently that while pro-lifers and pro-choicers disagree on much, they should agree on committing more resources to reducing unwanted pregnancy.<sup>8</sup>

## **3 SO WHAT MATTERS IN OUR SOCIETY?**

One grouping, similar to the analysis of the Australian Bureau of Statistics, "Measuring Australia's Progress",<sup>9</sup> categorises the ultimate aims of our lives into personal fulfilment, social interaction and sustainability. You will note that economic welfare – GDP – does not get a mention. Let's put economics in perspective: it is purely a means to ends.

What are the important issues for each of these aims?

### **3.1 Personal fulfilment**

We have some evidence about what leads to personal fulfilment. Happiness correlates with being in a relationship with another person, being in good health, having post-school education, and being employed.<sup>10</sup> But it is perfectly possible to be fulfilled without being in these categories. There is much more we need to know about what government policy can do to improve feelings of personal fulfilment. I would guess that peoples' personal environment also has a big impact – not so much the size of their kitchen as the quality of their street. It's certainly worth finding out.

### **3.2 Social interaction**

Good measures of social interaction include whether people feel they would have support in a time of crisis, trust institutions such as local police as well as each other, do unpaid voluntary work, and feel safe.<sup>11</sup> However, we have not measured these things across Australia, or over time.

As a result, again we need to know much more about what government policy could do to improve social interaction.

### **3.3 Sustainability**

Australians today see climate change and water as the two most pressing sustainability concerns.<sup>12</sup> Salinity, land management, biodiversity and fishery depletion are also major issues. Again, we could afford to know more about the best government policy to improve our response.

### 3.4 Productivity

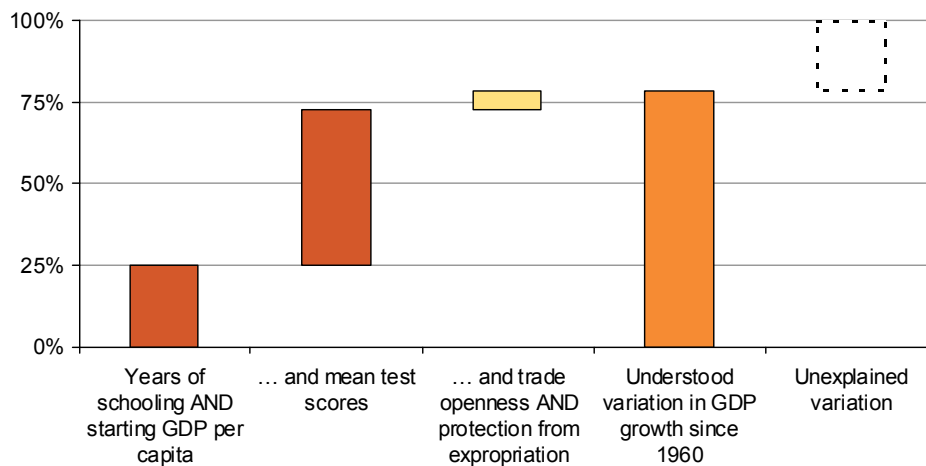
Economic productivity, although only a means to an end, is easier to measure and analyse.

In discussions of economic productivity, we tend to hear a lot about industrial relations changes, reducing regulatory burdens and increasing competition. These matter, but the evidence shows that education and health reforms would make the biggest difference to GDP in Australia.

The work of Hanushek and Wößmann for the World Bank showed that better school test results correlate with substantially higher growth in GDP per capita across a number of countries and time periods.<sup>13</sup> School outcomes are the dominant driver of GDP growth. Along with openness to international trade and protection against government expropriation, they explained 78% of the variation in GDP growth between countries.<sup>14</sup> This analysis is a powerful explanation of why some countries grow faster than others.

#### Impact of drivers of GDP growth

Explanation of variation between countries in national GDP growth since 1960



Source: Hanushek and Wößmann, *Education Quality and Economic Growth*, World Bank 2007

A recent McKinsey report came to the same conclusion.<sup>15</sup>

On Hanushek's analysis, increasing Australia's PISA scores by 50 would ultimately increase GDP by 1% per year, *every year*. This amounts to many billions of dollars in the long term.

Australia's school outcomes are already good relative to the rest of the world. But there is opportunity to go from good to great, and every reason to believe that this would make a big difference to economic growth.

Australia's own National Reform Agenda argued that improved education and training would have the biggest impact on economic growth of any policy option.<sup>16</sup>

The Productivity Commission wasn't entirely convinced. However, the Commission's analysis of education assumed that the primary impact of improved school education would be better *completion* rates, which have a relatively limited impact on productivity.<sup>17</sup> The subsequent work of Hanushek and Wößmann shows that completion rates are not the key driver of economic growth – rather it is the *quality* of schooling that matters; and this has a far greater impact on economic growth than that suggested by analysis of completion rates.

If Hanushek and Wößmann are right, most other potential economic reforms pale into insignificance – over the long term.

Apart from its economic impact, school education also seems to be one of the most important levers for promoting individual happiness, increasing social interaction both in communities and through effective democratic participation,<sup>18</sup> increasing awareness and concern about environmental issues<sup>19</sup> and in overcoming disadvantage to promote equal access to fulfilled lives.<sup>20</sup> In dealing with Australia's appalling record on aboriginal disadvantage, the Cape York Institute has argued that education is an essential lever for progress.<sup>21</sup>

We need to change our political attitudes towards school education. Traditionally it has been a hot issue for parents. The analysis suggests that it's a big issue for every citizen.

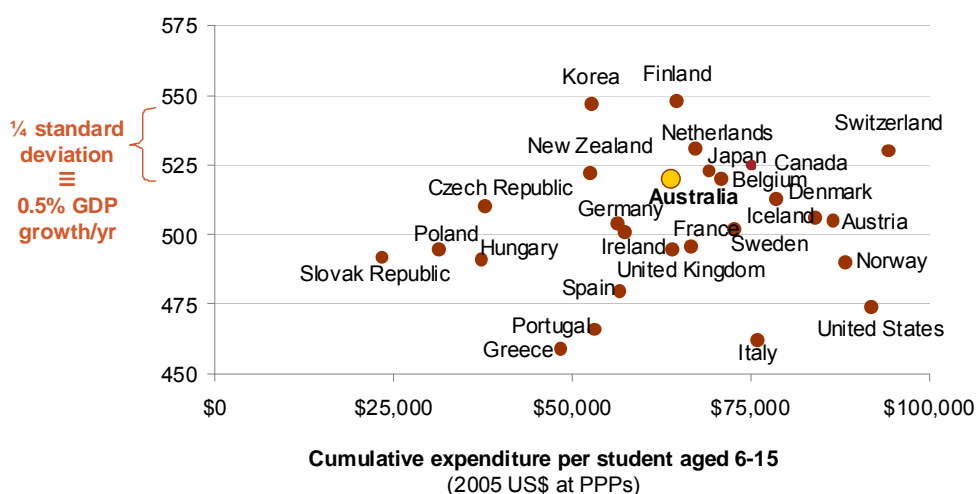
## 4 SO WHAT SHOULD WE DO ABOUT EDUCATION?

### 4.1 Money is not the answer.

Most of the countries with significantly better results than Australia are spending *the same* per student as Australia.<sup>22</sup>

#### School performance and funding

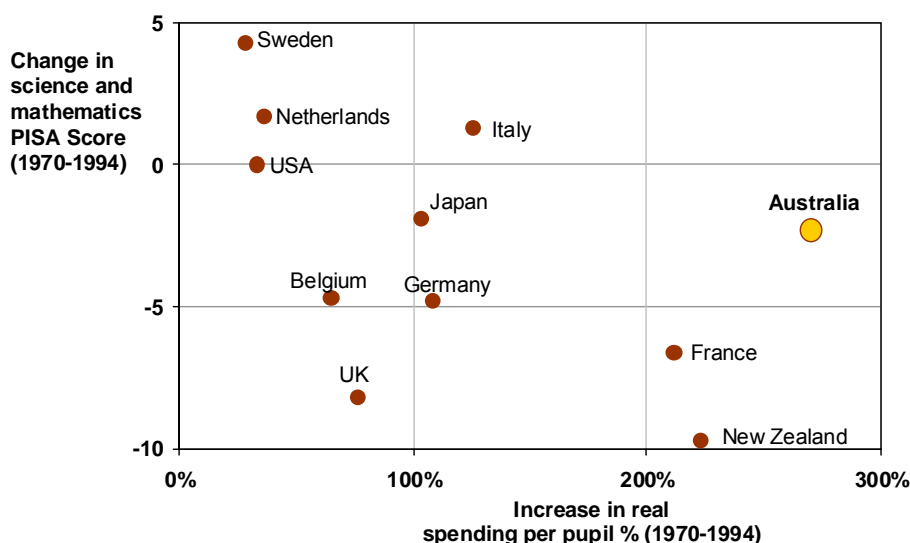
National PISA 2006 Maths Score



Note: Canada number includes only public sector spending  
 Several strong performers relative to Australia do not have available cumulative spend information (Taiwan, Hong Kong, Singapore Estonia)  
 Source: Education at a Glance: OECD 2008 ([www.oecd.org/edu/EAG2008](http://www.oecd.org/edu/EAG2008)).

Indeed, despite substantially increasing its expenditure per student over the last few decades (mainly to reduce class sizes), Australia has seen relatively little return in improved results.<sup>23</sup>

## Change in spending and changes in performance



Source: Pritchett (2003); OECD (1998; Table B5.1a) and *Education for all*, p 60.

The key determinant of education outcomes is teaching quality,<sup>24</sup> not the quality of the classroom building. A great teacher can inspire in a portable classroom; a poor teacher will fail however good the air-conditioning.

## 4.2 If better teaching is the answer, what policy changes would improve it?

On this issue, we are closer to the policy frontier and less sure of the answers.

We do know that some schools are better than others (even after accounting for the socio-economic background of their students).<sup>25</sup> And we know that some school systems are better than others. Texas has comparative demographics to California, and lower spending per student. But Texan students are around one *year* more advanced than Californian students.<sup>26</sup>

We know less about what drives these differences.

I suspect that the key is the entire gamut of people management from before teachers are hired until after they retire. None of these issues gets the airtime that we devote to any number of other issues that will have much less impact.

Given that we don't have unambiguous evidence about what will improve teaching quality, and therefore educational outcomes, we need a schooling system which learns from itself by systematically measuring the outcomes of reforms, and adapting accordingly. If school education is as important as the evidence suggests, this should be a top priority for governments everywhere.

## 5 WHERE NEXT FOR GRATTAN – AND AUSTRALIA?

Grattan Institute advocates a strategic approach to public policy that uses evidence to identify the biggest levers for the long term. The first number we must get right is the discount rate, which implicitly puts a value on the long-term. And to make sure the important things happen, we may need to select *fewer* priorities for change.

Grattan Institute wants to promote Australia as a liberal democracy in a globalised economy. This implies the values of people choosing for themselves and individual experience, as well as the value of public elections and striving for the “common good”. It acknowledges the value of international trade, and market regulation. We have no preconceived view on the role of government; rather the focus is on what will work best for each Australian to experience a meaningful life.

Grattan Institute acknowledges that public policy is trying to serve the ends of sustainability, personal fulfilment and community interaction, with economic outcomes merely a means to these ends. Rigorous fact-based analysis can clarify how best to serve these ends. When making the inevitable trade-offs between them, Grattan Institute will engage in a public conversation that respects that all of these ends matter.

I focussed today on school education because it is a substantial driver of both personal fulfilment and social interaction, and the evidence suggests it is the biggest lever for economic productivity. The second number we need to improve is our educational outcomes. Australia is doing well, but our performance has plateaued. We have the opportunity to go from good to great. We know that teacher quality is key. Substantial additional funding may not be the answer, although change will require governments to expend scarce *political* capital.

Apart from better education, many other factors contribute to sustainability, personal fulfilment, and social interaction. To set priorities we must work out what are the biggest drivers. Grattan Institute will be working on defining the key numbers that will make a difference, and how they can be improved. We have started programs in Energy, Water, Cities and Productivity Growth because the conceptual analysis indicated that these are important to the ends we are trying to serve. I look forward to talking to you in the future about what is most important, and how together we can make a difference.

## ENDNOTES

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My thanks to Andrew Nipe and John Harris for their assistance and insight in researching and developing this presentation, and to David Kemp and John Funder for their helpful comments. Remaining errors remain my responsibility.

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Relative to the definitions of strategy that I discuss, both place less emphasis on choosing *not* to do things, while Henry focuses more on external trends, and Moran focuses more on stakeholder management and leadership

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- 11 Potential measures, and their correlations are explored in N Biddle, E Davis, J Myers and R S Dodhy, *Exploring Measures of Low Social Capital*, ABS 2009,  
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