



**Submission to the Productivity Commission Inquiry on
Childcare and Early Childhood Learning**

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1. Introduction

As the Inquiry’s Terms of Reference and Issues Paper acknowledge, the provision of childcare and early childhood learning has the dual aims of supporting workforce participation and enabling children to learn and develop. Both are important.

This submission focusses on the first aim – specifically, on increasing Australia’s rates of female workforce participation as a means of boosting economic growth and enabling women to achieve and maintain financial security.

Other submissions to the Inquiry will be better placed to comment on many aspects of this complex issue, including the importance of early childhood education and care for maintaining long-run productivity growth, and how governments should consider the trade-offs required when seeking to make high-quality care available at an affordable price.

2. Women’s workforce participation in Australia

2.1 Relatively low female workforce participation

As Grattan Institute showed in its 2012 report *Game-changers: economic reform priorities for Australia*, Australia has relatively low rates of female labour force participation relative to comparable countries.¹

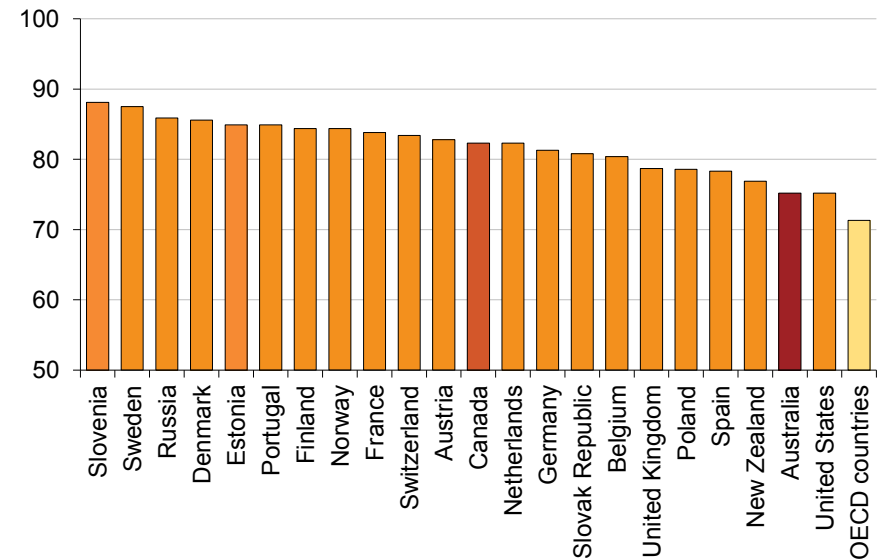
Only 67 per cent of women aged 15-64 are currently in paid work, compared with 78 per cent of men.² While 55 per cent of

¹ Daley, *et al.* (2012)

² ABS (2012a) ABS (2012b) – this excludes those looking for work, and is different to the ‘participation rate’ of 82.3% for men and 70.4% for women.

employed women work full time, 85 per cent of employed men do, with the remainder working part time.³ These rates are substantially lower than in many other OECD countries, as shown in Figure 1. While Australia is just above the OECD average, that average includes countries with very low participation rates, such as Greece.

Figure 1: Participation rates women aged 25-54, selected OECD Percent



Source: OECD (2010).

³ ABS (2012a)

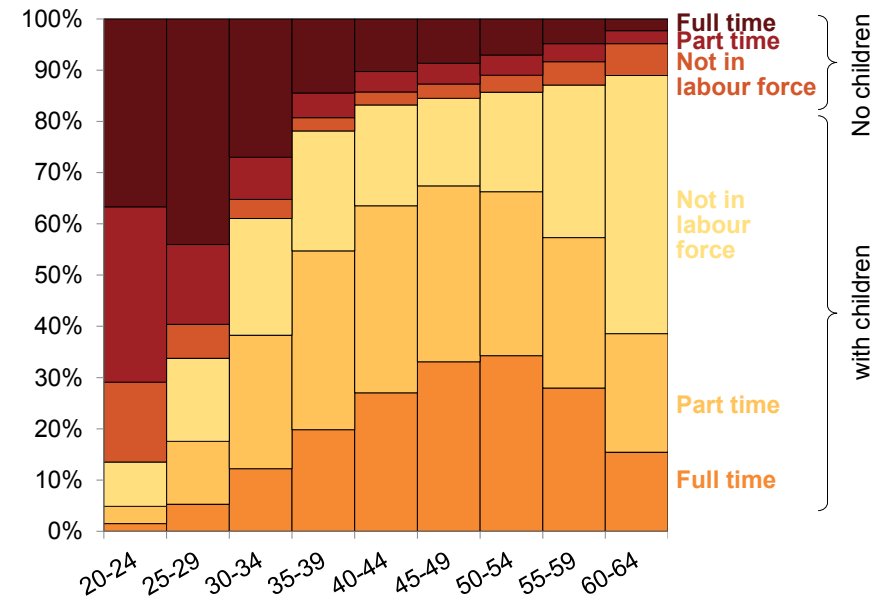
Some of these are northern European countries with a distinct social compact which may not be easily replicated in Australia. However, female workforce participation is also substantially higher in Canada, a country that is culturally, economically and institutionally similar to Australia.

Childbirth and childcare have a big impact on female workforce participation. Figure 2 shows that the vast majority of women who do not do paid work, or who work part-time, have children. As illustrated in Figure 3, women who provide care for their own children have significantly lower participation rates than those who do not. Female workforce participation can only change significantly if more mothers have jobs.

Before they have children, young women are as likely as young men to do paid work. However, most women have children in their 20s or 30s, and thereafter are much less likely to do paid work.⁴ Those who continue in the workforce tend to work for shorter hours over the rest of their lives, as shown in Figure 2.⁵

As Figure 2 shows, there are some women without children who do not work,⁶ but they are a relatively small proportion of the potential workforce.

Figure 2: Female workforce participation
Percent of age cohort



Note: Refers to women who have ever had children. Women who are unemployed and looking for fulltime or part time work are included in the FT and PT figures. Those who were employed but did not state their hours have been included here as a proportion of FT and PT work for their age bracket.

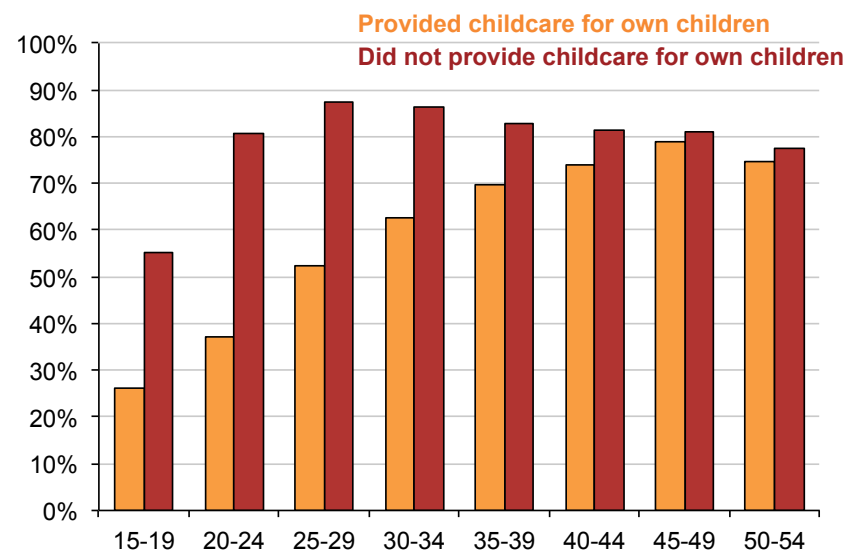
Source: ABS (2011c)

⁴ Women *without* children also participate less in full time work from their 30s onwards:ABS (2011c). However, this is a comparatively small group, as Figure 2 shows; there are also probably cohort effects at work here.

⁵ Apps (2010)

⁶ ABS (2011c)

Figure 3: Female workforce participation by provision of child care
Participation rate

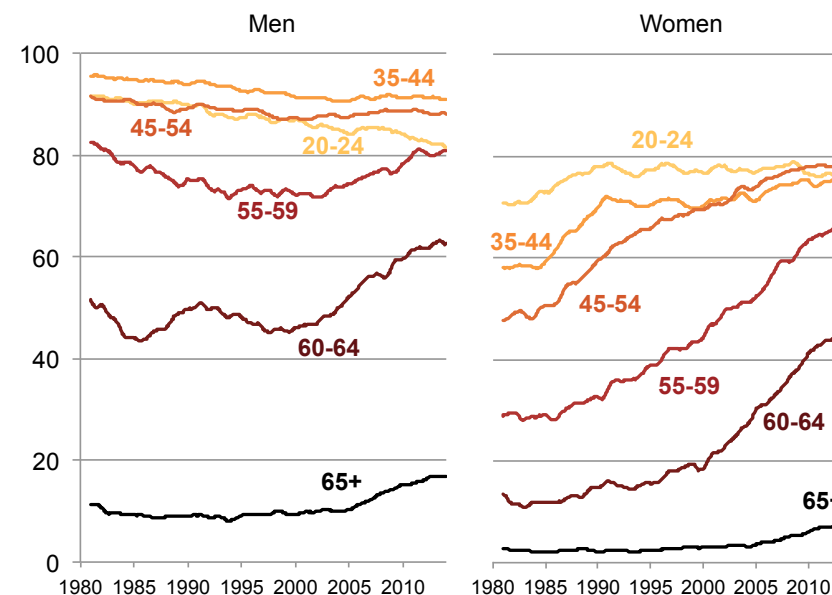


Source: ABS (2011); ABS (2012b)

Female workforce participation has increased substantially in Australia, as illustrated in Figure 4, particularly amongst older workers. This change has been driven primarily by improved health, higher levels of education, and partners also working later in life.⁷ However, participation of 35-44 year olds has barely changed since 1990.

⁷ Headey, *et al.* (2010), pp.104-120

Figure 4: Workforce participation by age group
% of cohort



Note: 12 month trailing average. Source: ABS (2012b)

2.2 Economic impact of higher participation

Increasing female workforce participation would have a substantial impact on the Australian economy. If Australian women did as much paid work as women in Canada – implying an extra 6 per cent of women in the workforce — Australia’s GDP would be about \$25 billion higher. On both Productivity Commission and Grattan Institute calculations, such increases in female workforce participation and economic productivity are feasible in Australia.⁸ There would also be substantial benefits to

⁸ See also Abhayaratna and Lattimore (2006)

government budgets as the number of income tax payers increased.

Improving female workforce participation would also mean a better return on Australia's investment in higher education. Women now make up 58 per cent of Australia's tertiary education enrolment.⁹ If these tertiary graduates do not work, Australia loses their substantial potential economic contribution.

Some might be concerned about where all the jobs will come from for additional women moving into the workforce. It is sometimes assumed that an increase in labour force participation would mean higher unemployment. However this concern, known in economics as the 'lump of labour fallacy', is misplaced. There is no fixed amount of work available in an economy. When someone enters paid work, more is produced. In the medium run, household demand tends to increase accordingly. Nor do those moving into the workforce depress wages in the medium term. With more labour, capital earns higher returns. This induces more investment, increasing the demand for labour, and restoring wages to their original level. Australia's history over the last 30 years illustrates these trends. Female workforce participation has risen rapidly, as shown in Figure 4. Unemployment did not rise materially as result, and average household incomes rose quickly.

2.3 Intangible impacts of female workforce participation

The unpaid work of women is an extremely large social and economic contribution to Australia.¹⁰ While it is not generally included in economic statistics, this work would have a very substantial economic value if paid at market rates. In 1997, the Australian Bureau of Statistics put the total value of unpaid

⁹ Norton (2012)

¹⁰ Manne (2008)

household work at \$237 billion, and estimated that women did 65 per cent of it.¹¹

Despite increased participation in the workforce, women still do significantly more unpaid domestic work than men, even in couples where both partners work similar hours.¹² Interestingly, in Canada where women do more paid work, men have been spending more time on housework over the last three generations, and Gen-Y men do roughly the same amount of household work as their partners.¹³

It is unclear whether non-parental child care substantially affects children's well-being and development, despite extensive study.¹⁴ Studies differ on whether non-parental or parental care is better for cognitive and emotional development, social skills and academic performance.¹⁵ The weight of evidence is that parental care for a child's first 6 months results in better development outcomes, but beyond 12 months there are fewer clear developmental benefits to parental care (although this depends heavily on the measurements used).¹⁶ Either way, formal

¹¹ Putting a dollar figure on unpaid work is very difficult due to conceptual and measurement issues in defining what is and isn't unpaid work. The 1997 ABS report compared the 'market replacement cost' with what it would cost to hire someone to provide childcare/cooking/cleaning etc with the 'opportunity cost' - what an unpaid worker would earn if they were spending the same amount of time in paid work as they were on unpaid activities. See Trewin (1997).

¹² In other words, working mothers in couple families are likely to simply add paid work to the significant unpaid work they already do, a phenomenon that has been described as a 'second shift' by some researchers. Smith (2007); Chesters, *et al.* (2009)

¹³ Marshall (2011)

¹⁴ For children from disadvantaged backgrounds, there is significant evidence that quality early child care can make a positive difference in their development. Burger (2010).

¹⁵ Barnett and Ackerman (2006); Shpancer (2006)

¹⁶ Productivity Commission (2009)

childcare has little impact relative to other factors such as quality of parental care and level of socio-economic advantage.

Some might be concerned that higher female workforce participation might lead to lower volunteering rates in the community. However, on a simple comparison, volunteering rates are *higher* for women in paid work than for those not working, as shown in Figure 5. More thorough regression analysis — taking into account education levels, socio-economic status, having children and income — suggests that, on average, a woman who works full time does about one hour of volunteering less per week than a woman who doesn't work at all.¹⁷

Working mothers are likely to have significantly less free time and leisure time than mothers who don't work. Reforming the current tax-transfer system so mothers can profit more from paid work would not compel mothers to give up leisure time, but simply give them more choices.

Besides the initial boost to economic growth that comes from increased labour force participation, there are longer-term benefits for both individual women and for the country as a whole. The longer women stay out of the labour force after having children, the more difficult it is for them to return to work, and the more likely they are not to return at all.¹⁸ When they do return, they may do so on lower wages. Because they earn less over their lives, they end up with much lower retirement savings than would otherwise be the case.¹⁹ Not only does this leave many women

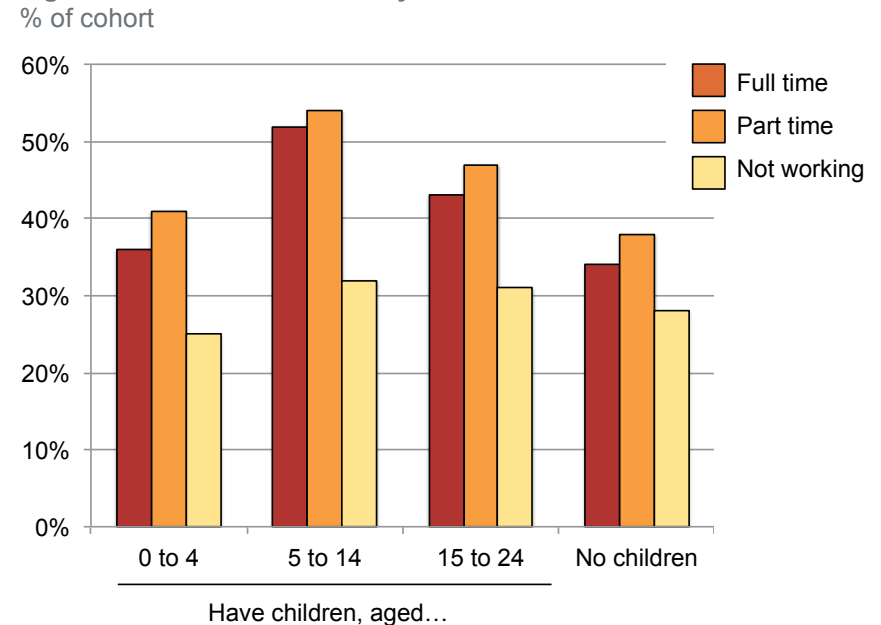
¹⁷ Grattan Institute regression analysis of determinants of volunteering, available on request.

¹⁸ OECD (2011)

¹⁹ Women on average forgo 31% of their lifetime earnings when they have one child, an additional 13% for two children and a further 9% if they have three. This is more pronounced for less educated women. See Breusch and Gray (2004) Women across all age groups have lower superannuation balances than their male counterparts. See ABS (2011a)

economically vulnerable as they age, but it also increases the number reliant on the Age Pension and other government support services. Given that the Age Pension is one of the faster-growing areas of government expenditure, this places further pressure on government budgets.²⁰

Figure 5: Female volunteers by work status and children



Source: ABS (2010)

²⁰ Daley, *et al.* (2013)

Box 1: GDP gains and child care.

It is sometimes assumed that when women return to paid work, they transfer unpaid work (like home child care) to paid work in the workforce, and therefore there is no real gain in output.

However, the GDP effect of increasing women's participation is not simply a switch from unpaid work to paid work. The economic value of a parent's paid work is usually higher than the economic value of childcare — captured in the fact that hourly wages are usually substantially higher than the hourly cost of childcare. Non-parental childcare offers efficiencies of scale and specialisation, so that net productivity usually increases with higher rates of female participation. Unpaid care (for instance, by relatives or friends) also has a positive GDP effect if it frees up the labour supply of parents who are then able to work.

This strictly economic analysis does not take into account the intangible benefits of caring for a child within the family. Views differ on the value of those benefits. The choice is usually left as a matter of personal preference, though Australia's current tax and benefit system implicitly puts a very high value on parental care — particularly for women who would otherwise be in lower paid work.

Clearly there are trade-offs between work hours, parental child care, unpaid and volunteer work, and time spent on leisure and personal activities. However, the current system strongly discourages mothers from paid work. As a result, policy settings significantly distort the choices that women make about benefits and disadvantages of paid work. As the next section shows, without these distortions, it is likely that many more women would elect to work, a choice that would reflect their preferences, *and* contribute to substantial economic growth.

If women, in consultation with their families, choose not to work while their children are young, that is up to them. Similarly, women who want or need to return to work before their children start school should have that option. But at the moment, policy settings make returning to work so financially unattractive for many women that they remain out of the workforce for long periods, with negative long-term consequences for them and for society as a whole.

3. Drivers of women's workforce participation

The drivers of women's choices about labour force participation are complex, and it is beyond the scope of this submission to consider all of them. For mothers with dependent children, they may include:

- The income available from paid work, after accounting for tax paid, family benefits lost, and child care costs.
- The availability, affordability and quality of child care.
- The availability of job opportunities that are suited to their skills, appropriately located, and sufficiently flexible to enable them to balance work and family.
- Personal and cultural beliefs and preferences about how children should be raised, and the role of women in the family and society.

Although in theory these factors could apply to both mothers and fathers, in practice they fall disproportionately on women. There are a variety of reasons for this. Women are much more likely to

take time off work to care for young children, whether due to biological needs soon after birth, traditional ideas about women's role as the primary caregiver, or the tendency for women to earn less than men. Adding to this are cultural understandings that child care costs come out of the woman's income when she returns to work in a two-income family, even though they are more appropriately thought of as a family expense.

These factors will play out differently for different women and their families, who will make different choices about trade-offs. Even so, there is very good evidence that the major influences on female workforce participation are marginal tax rates and the net costs of childcare.²¹ In Canada, female workforce participation increased substantially above trend levels when marginal taxes and the net costs of childcare were reduced, as discussed in Box 2.

This is not surprising: mothers face a high opportunity cost in seeing less of their children and in dealing with the stress of juggling work and family responsibilities.²² The net financial return of working, including the impact of tax, welfare, childcare costs and childcare benefits, matters to them.

Paid parental leave also influences female workforce participation. Paid parental leave at levels relatively similar to previous earnings, can encourage women to return to paid work after having children.²³ However, international experience suggests

that government support for childcare has about double the impact of spending on parental leave.²⁴

Education levels are important too, though already more women than men go to university in Australia.²⁵ Governments have less control over other factors that influence female workforce participation, such as overall unemployment rates, security of employment and social attitudes.²⁶

Australian experience seems consistent with international trends. Australian women with children change their behaviour depending on effective marginal tax rates.²⁷ And caring for children is the major reason why Australian women between 25 and 44 who work part time do not work full time, as shown in Figure 6: Reasons why women working part-time do not seek full-time work
Percent

6.

Why are Australian women choosing not to work after they have children? While it is intuitive that childcare-related issues are probably involved, few Australian studies distinguish whether the issue is the *cost* of childcare, the *availability* of childcare, or a preference for the *quality* of childcare provided by a child's family.

Availability does not appear to be a major issue in Australia. In the last ABS survey, only 2 per cent of families with preschool children were "currently looking" for additional preschool or formal care primarily for work-related reasons.²⁸ There is little data on

²¹Tsounta (2006); Schwarz (2012); *ibid.*

²² Losoncz and Bortolotto (2009); Losoncz (2011)

²³ See discussion in Productivity Commission (2009), Ch 5, pp. 26-38. After controlling for industry and education levels this may not be a particularly strong effect — see Buddelmeyer and Fok (2007), p.5 and cross-country studies suggesting that it has half the impact of government spending on childcare in Schwarz (2012); *ibid.* p.24

²⁴ Schwarz (2012); *ibid.* p.24

²⁵ Norton (2012), p. 25

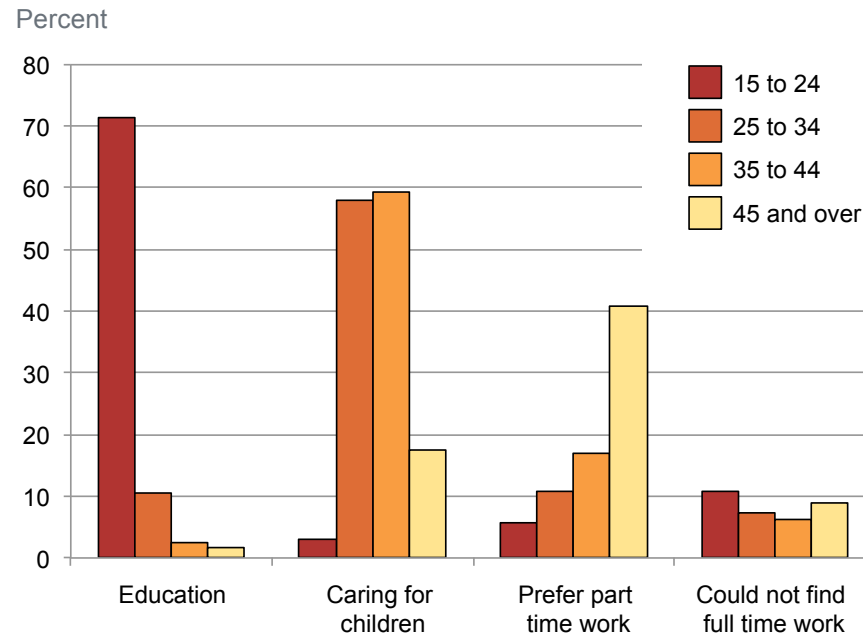
²⁶ Tsounta (2006); security of employment was proxied using union membership rates, and social attitudes were proxied using female parliamentary representation and government political ideology.

²⁷ Apps (2006); Kalb and Thoresen (2007)

²⁸ ABS (2011b)

the effects of *quality* of child care on parents' decisions to use care.²⁹

Figure 6: Reasons why women working part-time do not seek full-time work



Source: Abhayaratna *et al.* (2008)

International evidence suggests that the *costs* of childcare are a major disincentive for many mothers who would otherwise seek work. Experience in Canada — where female workforce participation is substantially higher than in Australia — suggests that affordable childcare is crucial to participation rates.³⁰

It is most plausible that household choices are influenced by the cumulative effects on net take-home income of income tax, foregone welfare benefits, child care costs, and child care benefits. Take-home income, net of these effects, amounts to the financial incentive to work relative to staying at home.

Working women clearly face a wide variety of circumstances that may affect their decision to seek work. However, no single issue appears to affect the choice to work as directly as the marginal costs of tax, welfare and childcare.

Women might also be more prepared to work if their hours were more flexible. While this issue is frequently raised in the debate about women's participation, it is not clear how much of a difference it would make. Many women are already working in part-time or casual jobs, as shown in Figure 2, but whether these are genuinely flexible in a way that meets the needs of women caring for children, or mostly structured for the benefit of the employer, is difficult to tell.³¹

Anecdotally, at least, the length of the school holidays in Australia also appears to be an issue. Many parents and employers acknowledge that even when part-time work is available with flexible hours and reasonable pay, many parents face substantial logistical challenges in covering up to 15 weeks of school holidays per year. There is some evidence of demand for more vacation programs for school-aged children.³² However, there is no rigorous data on the impact of the length of school holidays — it has not been included in major Australian surveys about barriers to workforce participation.

Social attitudes can be important, too, but their effects are unknown. It is likely that high marginal tax rates, welfare and

²⁹ For a survey of child care attitudes see Rush (2006)

³⁰ Tsounta (2006)

³¹ Abhayaratna, *et al.* (2008)

³² Newspoll (2008)

childcare costs have the greatest material impact on decisions to work. It seems likely that if these were changed, resulting in more women choosing to work, social attitudes would also gradually change.

4. Effective marginal tax rates

Many Australian second income earners have limited financial incentives to work, or to work full time, as demonstrated by analysis of net take-home income conducted for Grattan Institute by the National Centre for Social and Economic Modelling.³³

For example, a family of two parents earning \$40,000 each per year, with one child in long day care, take home only around half of the second worker's earnings – \$320 more per week – if the second income earner (typically the mother) chooses to work full-time, as shown in Figure 7: Reductions to take home pay of second income earner earning \$40k, one child aged 2

Percent

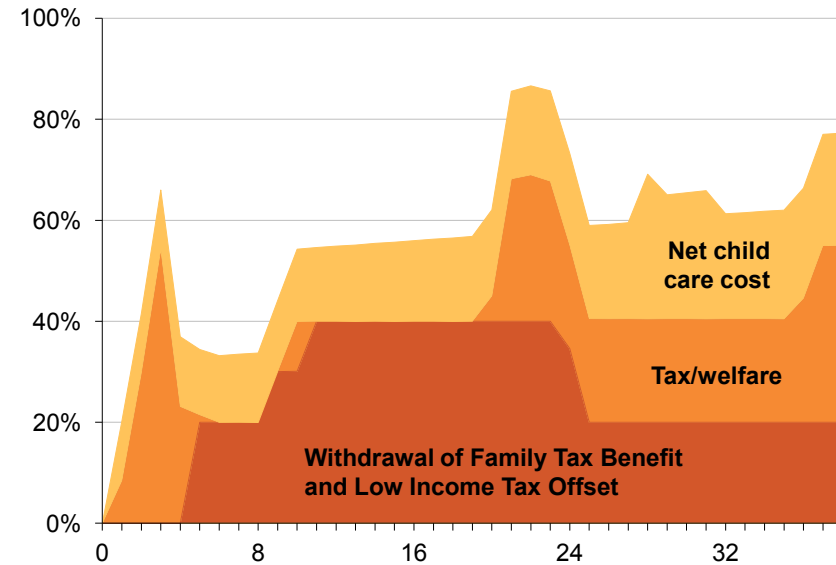
7.

The problem is worse for families with two children. In a family where the first wage earner earns \$70,000, and the second wage earner would earn \$70,000 if working full time, and there are two children in long day care, then the family only takes home 20

³³ This modeling is based on income tax and welfare rates as of 1 July 2012. The modeling takes into account income tax, welfare benefits, the Medicare Levy, Low Income Tax Offsets, Childcare Benefit, and Childcare Rebate. It assumes that childcare is required for 25% more hours than are worked (i.e. if working an 8 hour day, then childcare is required for 10 hours), and that childcare costs \$8/hour/child. This modeling does not take into consideration the increases to the FTB announced in the 2012-13 federal budget. However, because these benefits are means tested, they are likely to reduce the financial incentive to work.

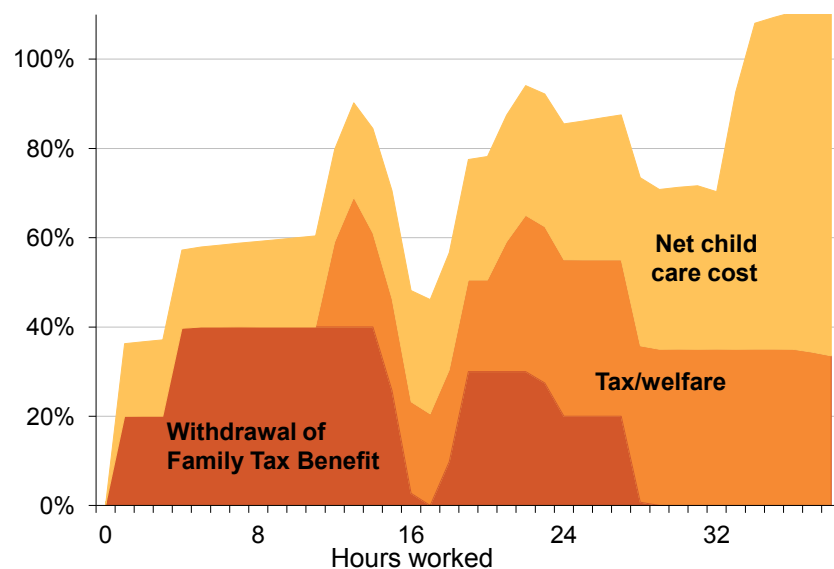
cents in each dollar earned by the second wage earner when working more than two days per week, as shown in Figure 8.

Figure 7: Reductions to take home pay of second income earner earning \$40k, one child aged 2
Percent



Source: NATSEM modelling for Grattan Institute . Note: this was updated on December 5 2012 as there was an error in the modelling provided.

Figure 8: Reductions to take home pay of second income earner earning \$40k, two children aged 2 and 4
Percent



Source: NATSEM modelling for Grattan Institute

Childcare costs (modelled here at \$8/hour for long day care) are so significant in these charts because in addition to paying the net costs of care after the Child Care Benefit and Rebate, a mother's increasing additional income as she works more hours reduces her access to these benefits. In many parts of Australia, childcare costs significantly more than this, which will reduce take-home pay still further.

These problems apply in a wide variety of scenarios, as summarised in Table 1.

Table 1 – Second income earner income after tax, welfare and childcare

Income per partner	No. of children	From the first 3 days worked		From the 4 th and 5 th days worked	
		Take home income/wk	Take home income as % of earnings	Take home income/wk	Take home income as % of earnings
\$40,000	1	\$218	53%	\$99	56%
\$40,000	2	\$156	35%	\$49	17%
\$70,000	1	\$458	54%	\$193	39%
\$70,000	2	\$284	37%	\$57	10%
\$100,000	1	\$735	61%	\$338	48%
\$100,000	2	\$565	47%	\$224	32%
\$150,000	1	\$1,077	55%	\$624	52%
\$150,000	2	\$1,040	48%	\$428	40%

Note: Assumes that the primary income earner works full time for the income listed, and the second earner would receive the same income if they work full time. This table was updated on 5 December 2012. Source: NATSEM modelling for Grattan Institute.

Even when families use little or no childcare — whether because their children are older, or they have informal care arrangements — effective take-home income can be relatively low. For low and middle income earners, even without childcare costs, effective rates of take-home pay are still less than 60 cents in the dollar due to the impacts of Family Tax Benefit, tax, and welfare withdrawal as illustrated in Figure 7 and Figure 8.

5. What can be done?

Smoothing effective marginal tax rates to reduce disincentives to work is a complex task, particularly in the constrained budget environment that Australia currently faces. However, given the

economic and fiscal benefits of increased female labour force participation described above, it is a problem worth tackling.

Canada provides a model of what can be achieved. As described in Box 2, reforms that reduced tax rates for low and middle-income families, and provided higher subsidies for child care, are correlate with a rise in rates of female labour force participation.

There is no doubt that reducing barriers to participation by reducing marginal tax and welfare rates is a challenge for government budgets. A substantial issue is the net impact of withdrawing means-tested benefits as incomes increase.

Reducing benefits themselves would be effective, but is likely to be seen as unfair. Reducing benefits over a wider range of income (sometimes described as ‘increasing the taper’) would increase effective take-home income, but at a cost to the budget. Means testing all benefits on the basis of the household’s higher income earner would reduce the disincentives for a second income earner,³⁴ but there would be winners and losers amongst existing households. Any budget impacts need to take into account the additional revenue as participation rates increase.

The policy direction is clear. It is hard to believe that the very high effective take-home income rates, particularly for lower income households, are an optimal policy solution. Identifying changes that remove disincentives are fiscally acceptable, and fair to low-income households should be a high priority given both the economic benefits and the social advantages.

These barriers could be substantially reduced by treating Family Tax Benefit as income in the hands of the family’s first wage-earner, and treating child care as a deduction in calculating tax and eligibility for welfare benefits. However, more work is required

to identify tax and welfare changes that would reduce barriers at an acceptable cost to the budget, after taking into account increased income tax collection as a result of higher participation.

While marginal tax, welfare and childcare costs are the chief barriers to female workforce participation, individual circumstances vary enormously with levels of education, earnings, family circumstances and values. All these affect workforce participation. A married, tertiary-educated woman returning to work for an accounting firm faces very different issues to a single woman without tertiary qualifications seeking casual work in a supermarket. In identifying key levers for reform, we have tried to focus on those issues that appear to affect the largest number of women.

It should also be noted that current arrangements are highly regressive: women with lower earning capacity are more strongly discouraged from work. They take home a smaller *proportion* of any money they do earn — and a much smaller dollar amount. This may discourage them from workforce participation for several years, reducing their opportunities later in life.

We are confident that more women would do paid work if governments reduced effective tax, welfare, and childcare costs. However, there are many other issues on which further work would be valuable.

There is no rigorous study in Australia of the value of unpaid work by women, and how this might compare to the economic and social value of paid work. Many will remain unconvinced that the incentives to work should be increased until this issue is resolved.

³⁴ See Apps (2010)

Box 2: Women in Canada's workforce

Canada's experience shows that lower effective tax rates and subsidised child care lead to more women in paid work.³⁵

Female participation grew rapidly in Canada from the mid-1970s and is well ahead of Australia. Female workforce participation (aged 25-54) rose from 53.1 per cent in 1976 to 82 per cent in 2012.³⁶ In this age group, over 80 per cent of female workers are employed full-time.³⁷ In 2009, 64 per cent of mothers with children under 3 do some paid work.³⁸

In Canada, a range of reforms reduced the disincentives to work. Around 1997, tax cuts for low and middle income families reduced effective tax rates for second income earners.³⁹ At about the same time, Canadian governments committed to improving the accessibility and quality of childcare, including subsidising the cost. Quebec reduced childcare cost to \$5 per day,⁴⁰ and other provinces also have substantial subsidies. In 2000 employment insurance scheme for parental and maternity leave was extended so that parents could take 50 weeks leave with partial salary.⁴¹

As a result, after limited increases in the early 1990s, female workforce participation rose steeply from about 1997, particularly in Quebec, as shown in Figure 9.

Female workforce participation also increased in Australia over this period, presumably because tertiary participation increased. However, participation in Canada remains much higher than in Australia, and with more women working full-time.

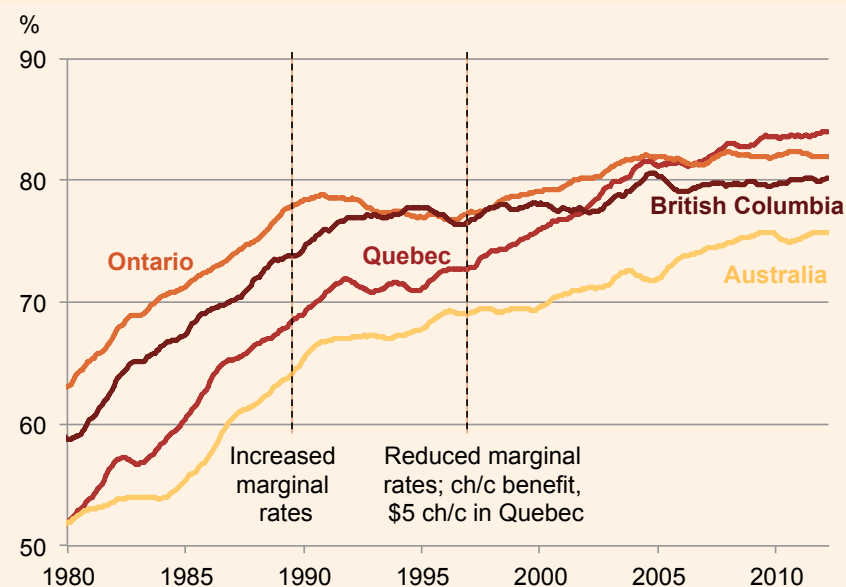
³⁵ Tsounta (2006)

³⁶ Statistics Canada (2012)

³⁷ Ibid.

³⁸ Statistics Canada (2011)

Figure 9: Female participation rates, 25-54 year olds, selected Canadian provinces, 1980-2012



Note: 12 month trailing averages. Participation rate includes those who are unemployed and looking for work. Source: Statistics Canada (2012); ABS (2012b).

³⁹ Tsounta (2006), p.9

⁴⁰ Ibid., p.11; Baker, *et al.* (2005)

⁴¹ Canada (2001)

The equity impacts of the policy changes suggested also need to be calculated. Who will be the winners and losers of the changes? Again this will depend on the precise parameters chosen.

Nevertheless, there appears to be compelling evidence that the cost of childcare after tax and welfare benefits is a substantial barrier to higher female workforce participation in Australia. Changing the cost of childcare would not be cheap, but it would increase female workforce participation, thereby increasing economic output as well as improving the long-term employment prospects of many Australian women.

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