

6 June 2022

NSW Industry Policy Team
Investment NSW
Sydney NSW 2000

By email: industrypolicy@investment.nsw.gov.au

Securing future innovation and global competitiveness in NSW

Dear Sir/Madam,

As the industry association for private capital in Australia, the Australian Investment Council is pleased to present its submission to Investment NSW for the Green Paper titled *Securing Future Innovation and Global competitiveness in NSW*.

Private capital investment has played a central role in the innovation, growth and expansion of thousands of businesses and represents a multi-billion-dollar contribution to the Australian economy. Our members are the standard-bearers of professional investment and include private equity (PE), venture capital (VC) corporate venture capital (CVC) and private credit (PC) funds, alongside institutional investors such as superannuation funds, sovereign wealth funds and family offices as well as leading financial, legal, and operational advisers. Our members include both Australian domestic and offshore-based firms, who in turn invest capital on behalf of millions of Australian families and attract capital from passive overseas investors.

Private capital fund managers invest billions of dollars into Australian companies across every industry sector of the economy every year. Australian-based PE and VC assets under management reached \$42 billion in 2021 with an additional \$10 billion in equity capital available to be invested in the short-term. Private capital investment supports almost 475,000 jobs throughout Australia and contributes \$54 billion to the domestic economy, equivalent to 2.6% of GDP.¹ The private capital industry is a significant and growing contributor to, and driver of, Australia's economic recovery through an ability to drive innovation and develop industries of the future.

Australia relies on a steady flow of domestic and foreign financial and human capital. Efficient access to capital by Australian businesses is vitally important for the creation of Australian jobs and our economic future.

The Australian Investment Council has identified several key policy priorities that will enable NSW to maintain its economic momentum and evolve the NSW economy toward the next phase of prosperity for the state's citizens. Our recommendations are set out in this submission and focus on:

- 1) Addressing skills shortages
- 2) Supporting innovation
- 3) Streamlining tax inefficiencies; and
- 4) Maintaining a steady flow of investment capital.

The Council looks forward to participating in future discussions as Investment NSW develops the 'White Paper' phase of this consultation. If you have any questions about our submission, please do not hesitate to contact me or our policy team at policy@aic.co.

Yours sincerely



Jonathan Kelly
Interim CEO

¹ *Funding a brighter future*, EY, May 2022

SECURING FUTURE INNOVATION AND GLOBAL COMPETITIVENESS IN NSW



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1. Summary of Recommendations

The Council's recommendations are outlined below:

Investment capital

- Legislate NSW partnership law to enable the implementation of a LP CIV regime as the major outstanding component of a globally competitive fund vehicle regime for Australia.

Address skills shortages

- Work with the Federal Government to update the migration skills list to address immediate skills and talent gaps, particularly for the innovation economy
- Encourage post-graduate students with in-demand skills to remain in NSW after they graduate
- Promote NSW as a desirable destination for skilled migrants, tourists, and students to address current shortages
- Collaborate with the private sector to upskill workers for jobs of the future
- Work with universities to map skill requirements for the future in NSW
- Embed STEM skills into the NSW school curriculum, from primary school through to tertiary education, fast-track STEM skills development in secondary schools and the establishment of dedicated 'STEM schools'
- Map skills that can be translated from VET or tertiary education and combined with micro-credentials to address skills gaps

The innovation economy

- Establish a co-investment program to invest equity into growing NSW-based businesses and support entrepreneurs
- Increase incentives for corporate venture capital and public-private investment in high growth companies and innovation labs
- Develop a closer collaboration between industry and universities to accelerate commercialisation of research with best practice approaches and infrastructure

Rebuild regions

- Establish industry hubs and innovation precincts in regional locations with linkages to local university campuses

Remove tax inefficiencies

- Implement alternatives to payroll tax and stamp duty which act as inhibitors to business activity and move towards a user pay system of funding

Work towards net-zero

- Reduce planning red tape for businesses investing in new technologies
- Support clean energy initiatives for businesses and households

Secure supply chains

- Invest in NSW infrastructure that reduces bottlenecks and ensures the quick and efficient flow of goods through our ports, rail, and road networks

2. Overview

The Australian Investment Council has put forward recommendations in this submission which are focused on regenerating growth across every sector of the NSW economy through creating jobs, driving innovation, increasing productivity, and maintaining a flow of foreign and domestic investment capital. A key focus of these recommendations is that they support emerging industries that align with policies that will drive productivity, new industries, and employment opportunities right across the state of NSW and will ultimately drive transformational changes that will recalibrate the state onto a path of higher wages, living standards and investment.

More than ever, ongoing shifts in the global economy are highlighting the need for government, industry, and businesses to work together to ensure there is a common goal and readiness to tackle complex problems and take hold of the big issues. Collectively, we face major challenges – including political instability and global trade issues, the increasing pace of technological change, and changes to financial conditions around the world that could have significant impacts on financial markets and the NSW economy.

Positive economic fundamentals such as low unemployment and stable economic growth shouldn't be discounted, however, many businesses face challenges such as accessing debt capital and lower business confidence and finding employees. Productivity challenges, investment in skills and talent, and technology are just some of the issues that policymakers and industry leaders alike must turn their minds to.

Private capital investments are closely aligned to emerging industries identified by the NSW government, such as medical and life sciences, defence and aerospace, digital systems and software, clean energy and waste and recycling, agriculture, education, travel, and leisure.

To this extent, the Australian Investment Council's recommendations focus on the themes of:

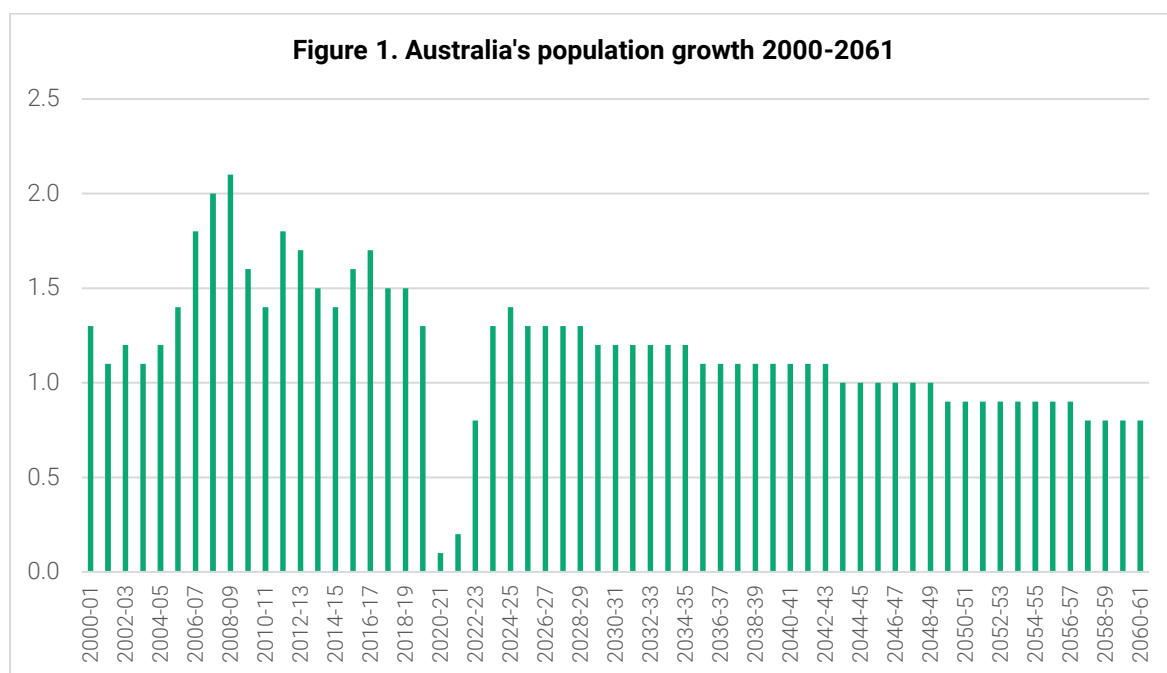
- Addressing skills shortages
- Supporting innovation
- Maintaining a steady flow of investment capital
- Removing taxation inefficiencies.

3. Finance capital and immigration – important economic levers

As a desirable destination for migration and investment, Australia has long been a net importer of both people and capital. However, during the past few years these important economic drivers have seen a reversal with net overseas migration in the year to June 2021 negative for the fifth consecutive quarter a net loss of 88,000 people, as well a net \$74 billion of capital exported from Australia in September.

While the pandemic and border closures can be partly attributed for the impact on these two critical economic levers, policies that shift the dial on this continued decline will be critical for Australia to effectively compete with other jurisdictions for people (Figure 1).

The NSW economy relies on a dependable and steady flow of foreign human capital and skilled migration to drive economic growth and job creation. It is therefore vitally important for the economy and NSW jobs, that businesses can quickly and efficiently access human capital and skills from domestic as well as offshore sources.



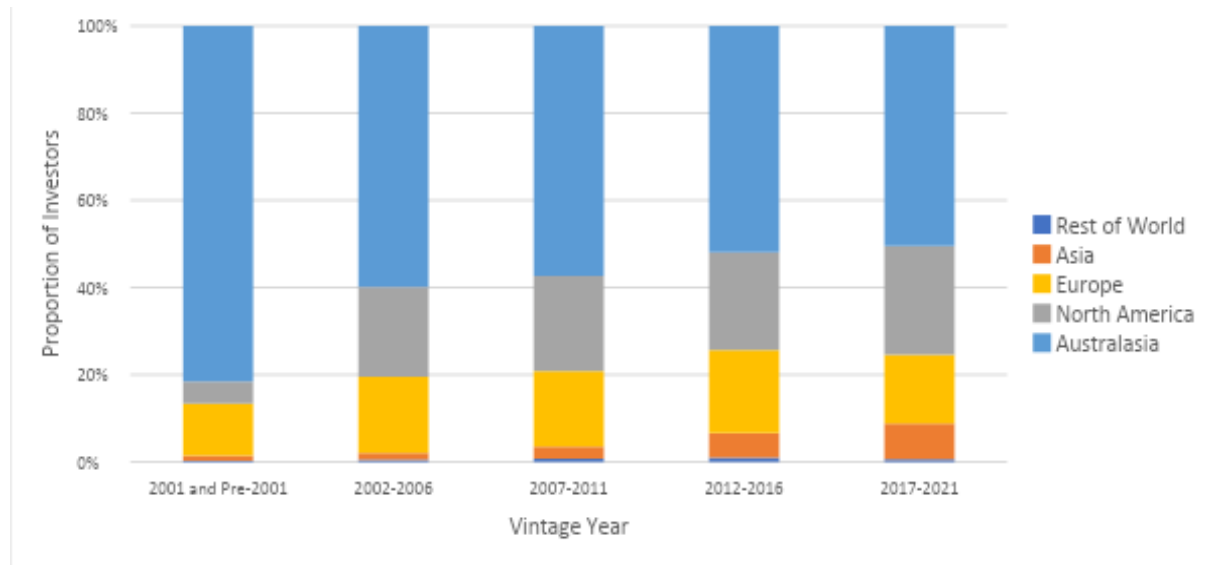
Source: 2021 Intergenerational Report, The Treasury, Australian Government June 2021

While the ongoing capacity to continue to attract foreign capital will be essential for funding new investments that will in turn create new high- jobs, this cannot be assumed. Challenges to increasing investment into the domestic economy have been further exacerbated by excess savings during the pandemic which is reflected in the account surplus since the June quarter 2019 averaging 2.6 per cent of GDP. While this account surplus is expected to reduce as the economy emerges from the pandemic, policies that focus on increased investment, rather than savings, will be required to boost economic growth. Increasing migration would help raise investment demand and fill skills and talent gaps in local businesses.

4. Australia relies on a flow of foreign capital

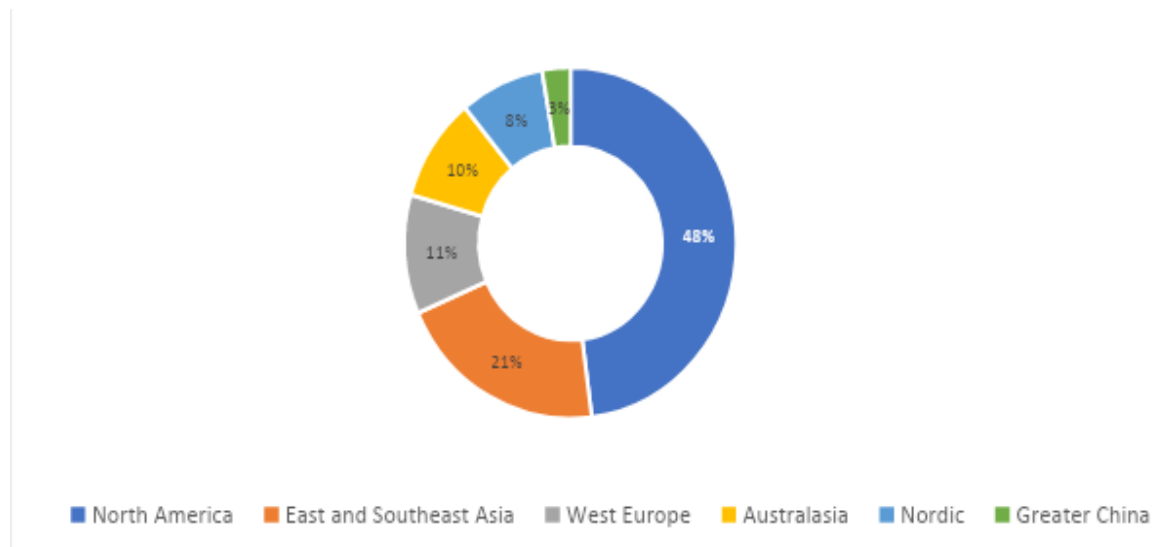
Foreign investment into Australia has grown over the years from just 18% of investors into Australian private capital funds two decades ago to almost half (49%) in the past five years (**Figure 2**). Australia is appealing to foreign investors for its relatively stable political environment, strong economy, robust governance, and dynamic market conditions. However, there is no room for complacency as Australia continues to compete head-to-head with more mature jurisdictions like the USA, UK and Canada who have more established track records in fundraising and larger scale due to a range of factors including bigger populations and economies and private capital ecosystems which have been operating much longer than Australia's.

Figure 2: Foreign investment in Australian Private Capital Funds ²



Of the foreign investors North America accounts for 48% of the funds that have received foreign funding in the past five years (**Figure 3**) with many US and Canadian Institutional investors, particularly pension funds, having publicly expressed confidence in Australia and have been long-term investors in the country.

Figure 3: Foreign funding in Australia by region ³



4.1 Maintaining a steady flow of investment capital

As a net importer of capital, the domestic economy relies on a dependable and steady flow of foreign capital to drive economic growth and job creation. At this critical juncture, it is vitally important for our economic recovery, and NSW jobs, that businesses can quickly and efficiently access capital from domestic as well as offshore investors to support the growth and expansion of existing businesses as well as the development of the new businesses and industries that underpin Australia's innovation ecosystem.

A strong investment regime anchored by policies that are commensurate with other jurisdictions is important for maintaining a stable and transparent investment framework that is attractive for domestic and foreign financial services providers to ensure that investment flows remain open, transparent, and stable, thereby enabling our investment industry to continue to support portfolio companies during this time of heightened uncertainty.

However, the industry's ongoing capacity to continue to invest greater amounts of capital into innovative businesses, leading to the creation of new high-value jobs, cannot be assumed – policy must continue to support, enable, and encourage capital investment into the domestic market. While the private capital industry currently has more than \$10 billion in available capital to support investment into new deals in the period ahead, the sector's ability to continue to grow the pipeline of funding available to high-growth businesses over the coming years will be increasingly dependent on inbound capital from offshore investors.

Domestic capital works alongside foreign capital in providing the investment needed to support emerging and fast growth businesses. As the Australian private capital market has continued to grow and mature, domestic fundraising has improved in recent years as the ecosystem has built scale through a lived experience. However, there is still work to be done to continue to grow domestic fundraising capabilities.

4.2 Limited Partnership Collective Investment Vehicle (LP CIV)

World-class, competitive CIVs are essential for building and expanding the pool of capital that can be attracted into the Australian economy, and the NSW economy given that Sydney is Australia's financial capital. Accordingly, it is important that a flow-through, internationally best practice LP CIV – the globally accepted private capital vehicle of choice – be introduced as soon as possible, keeping in mind that the original introduction date of 1 July 2018 has not been met. Supporting the broader policy objectives of building Sydney as a financial services hub, such a vehicle could transform the flow of capital into high growth Australian businesses, helping to facilitate Australia's transition to a knowledge-driven economy.

For many years, the Council has urged the Federal Government to prioritise the development of the LP CIV regime. Despite a commitment in the May 2016 Federal Budget to the introduction of a new LP CIV from July 2018, the most recent announcements in the 2018-19, 2021-22 and 2022-23 Federal Budgets did not include any specific references to the introduction of the LP CIV regime. It is unclear whether the LP CIV will be introduced and whether the Government still has a commitment to the measure.

The Council has previously identified the proposed new LP CIV regime as an area of policy focus for private capital. A globally competitive LP CIV would have a significant and profound impact on the capacity of our industry to invest billions of dollars into great Australian businesses spanning all corners of the economy, and at all stages of development – small, medium, and large scale – to help them realise their growth and expansion plans and create new employment for the future.

Given that partnerships are governed by NSW law, the introduction of this vehicle, together with appropriate adjustments to Federal tax settings would contribute significantly to Sydney remaining a global financial centre.

² Preqin & Australian Investment Council yearbook 2022

³ Ibid

Recommendations

- Legislate NSW partnership law to enable the implementation of a LP CIV regime as the major outstanding component of a globally competitive fund vehicle regime for Australia.

5. Addressing skill shortages

In addressing the skills and capabilities of the workforce of the future there are a number of key considerations to take into account which fall into three main categories of:

1. Addressing current skills and talent gaps
2. Redeploying skills within the economy
3. Building a pipeline of talent.

5.1. Addressing current skills and talent gaps

Australia has had a long history of supportive policies to attract business entrepreneurs. However, the rising global mobility of workers and heightened competition for talent means that it is important for Australia to have policy settings that are effective in attracting a critical mass of "new economy" skilled workers.

The Council's own research⁴ shows that job vacancies are continuing to grow in the innovation sectors with 5331 advertised job vacancies in the portfolio companies of eight of Australia's most active VC firms as at 31 December 2021, up from 3952 in the previous six months.

The growth of jobs in VC-backed businesses is a reliable indicator of where the demand for skills will be coming from into the future with the latest analysis highlighting the need for software engineers with cloud-based experience which accounted for 1446 of job vacancies, a 27% increase from 939 in the previous six months. However, more traditional roles in finance, law, risk, and compliance should not be overlooked and still have significant demand within the innovation ecosystem.

Recommendations

- Work with the Federal Government to update the migration skills list to address immediate skills and talent gaps, particularly for the innovation economy
- Encourage post-graduate students with in-demand skills to remain in NSW after they graduate
- Promote NSW as a desirable destination for skilled migrants, tourists, and students to address current shortages

5.2. Redeploying skills within the domestic economy

In addition to the programs already in place, there is a substantial opportunity to redeploy the skills of Australia's current workforce, so they are relevant for the future economy. One area that has been overlooked is for recent retirees or older workers who may have built significant experience and skills through their working careers and would like to continue contributing to the workforce.

One private capital-backed company, Forte, is working with governments around the world to upskill unemployed workers by matching skills to job demand. The company recently signed an agreement with the South Australian government to help redeploy people into the workforce.

Recommendation

- Collaborate with the private sector to upskill workers for jobs of the future

5.3. Building a pipeline of talent

Through our research, the Council has noted that the innovation sector seems to require multiple skills, for example, a software engineering role may also require marketing or web design capabilities.

A world-class innovation ecosystem needs to be supported by a world-class education system. The nature of work itself is evolving, driven by technological transformation. A leading education system should encompass skills that aren't

⁴ *Future Jobs Barometer*, Australian Investment Council, March 2022

traditionally taught in schools and universities, such as entrepreneurship, and provide the infrastructure to effectively deliver student outcomes starting from primary through to the tertiary phase of education. Australia is a net importer of not only capital but talent.

This extends further to the tertiary sector to consider expanding opportunities for double degrees to enable students to become more marketable in the workforce of the future.

Recommendations

- Work with universities to map skill requirements for the future in NSW
- Embed STEM skills into the NSW school curriculum, from primary school through to tertiary education, fast-track STEM skills development in secondary schools and the establishment of 'STEM schools'
- Map skills that can be translated from VET or tertiary education and combined with micro-credentials to address skills gaps

6. Supporting Innovation

6.1. Focussing on technology as an enabler for building employment and growth across the economy

Innovation investment is driven largely by the willingness of investors, such as private capital firms (and their investors), to take risks and invest in businesses that are creating new and innovative products and services, and in doing so, establishing markets that often do not even currently exist. These investments are often at the earliest stages of a new venture's life, or at key points in the life cycle of family business succession, both of which are considered to carry high risk for different reasons. Along with the provision of capital, this funding is accompanied by highly valuable strategic and operational advice and guidance to the founders and management teams of private, early-stage and fast-growth businesses. This model of working in partnership is often the 'x-factor' that can help these innovative businesses to realise their ambitions in domestic and global markets. The expansion and growth of such businesses leads directly to more revenue and sales, greater levels of investment into innovative market-leading research and development, and, is the key driver behind the creation of new high-value jobs within the economy and higher contributions to income tax and other government revenue streams, including GST.

6.2. Closer collaboration between industry and universities to accelerate research commercialisation.

The Council is supportive of innovation districts that connect universities with industries to create a culture of collaboration, innovation, and public engagement for the development of new businesses and industries. Innovation districts are central for knowledge-based and novel economic activities with distinct benefits stemming from the co-location of researchers and industry.

Establishing innovation precincts with a specific industry focus – such as the Melbourne Biomedical Precinct – would build significant opportunities for research commercialisation. The Melbourne precinct is amongst the top three biomedical research clusters in the world. It includes the University of Melbourne, Monash University, CSIRO, CSL Limited, Royal Melbourne Hospital, the Bio21 Institute, the Walter and Eliza Hall Institute and Biomedical Research Victoria. CSL's research and development headquarters is also located within the precinct.

The Council recommends government fast-tracks the commitment outlined in the *Statement of Principles for Australian Innovation Precincts Report* to create a future where innovation precincts are an integral part of the broader national innovation system by 2030.

Recommendations

- Establish a co-investment program to invest equity into growing NSW-based businesses and support entrepreneurs
- Increase incentives for corporate venture capital and public-private investment in high growth companies and innovation labs
- Develop a closer collaboration between industry and universities to accelerate commercialisation of research with best practice approaches and infrastructure

7. Rebuilding regions

After catastrophic bushfires and floods in NSW a, there is scope to focus on building precincts in regional NSW for industries in the future and aligning them with regional university campuses such as Southern Cross University in Lismore, Charles Sturt University in Albury, Orange, Wagga Wagga, Port Macquarie and Bathurst and the University of New England in Armidale.

For example, NSW could aspire to have the largest recycling innovation precinct in the Southern Hemisphere, supported through development of university research projects aligned with the CSIRO and investment capital through VC funds and the NSW Government.

Recommendations

- Establish industry hubs and innovation precincts in regional locations with linkages to local university campuses

8. Removing tax inefficiencies

Streamline the taxation system to remove uncertainties and to improve the nation's competitiveness in attracting investment capital from domestic and offshore sources.

This includes refining the 'tax mix' by reducing reliance on direct taxes – such as personal and corporate income taxes – and re-balancing towards greater reliance on 'user pays' pricing mechanisms and indirect taxes. In the technology-enabled global marketplace in which Australian businesses operate, such a shift is vitally important to building a stronger and more sustainable position for governments at all levels into the future. A measure that could be considered are those potentially hindering investment in Australia and support for policies which encourage investments in high-growth businesses to help the post-pandemic economy recover.

Alignment of state-based tax regimes needs to be considered to avoid the red-tape of businesses dealing with multiple differing and competing regimes.

Recommendations

- Implement alternatives to payroll tax and stamp duty which act as inhibitors to business activity and move towards a user pay system of funding

9. Working towards net-zero

As outlined in the 2021 Intergenerational Report, the likely effects of the transition to a lower carbon emissions economy will mean that some sectors will need to adjust to falling demand for some exports while new opportunities will be created in other sectors. In many respects, these factors will be outside of Australia's sovereign ability to control, and ultimately these costs will be passed on to Australian consumers and other businesses. There are several areas where NSW has a comparative advantage and can be a world-leader in the export of clean-tech solutions that will underwrite the global shift towards more sustainable economies.

Businesses will play a pivotal role in driving innovation and in developing new technologies that will reduce carbon emissions and will also lead the way through policies that commit to and ensure actions that reduce carbon emissions and in leading new business practices and investment decisions. Businesses will increasingly find it important that credible green credentials are provided to consumers, their business partners, financiers, and investors.

Recommendations

- Reduce planning red tape for businesses investing in new technologies
- Support clean energy initiatives for businesses and households

10. Securing supply chains

Local and global supply chains have come into sharper focus. Continued investment into state infrastructure is critical to reduce bottlenecks and ensure goods can flow through our ports, rail, and road networks safely, quickly, and efficiently.

Recommendations

- Invest in NSW infrastructure that reduces bottlenecks and ensures the quick and efficient flow of goods through our ports, rail, and road networks