Humanising productivity growth

KPMG Australia's response to the Productivity Commission's Inquiry into
Delivering quality care more efficiently

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Executive summary

As a leading professional services firm, KPMG Australia (KPMG) is committed to meeting the requirements of all our stakeholders – not only the organisations we audit and advise, but also employees, governments, regulators – and the wider community.

We strive to contribute in a positive way to the debate that is shaping the Australian economy, and we welcome the opportunity to provide a submission in response to the Productivity Commission's five productivity inquiries commissioned by the Government. In this response we have focused on the 'Delivering quality care more efficiently' Inquiry as our response focuses on labour-intensive services-based industries.

KPMG is pleased that the Productivity Commission has the so-called non-market services – health care and social assistance, education and training, and public administration and safety – as a key focus and believes it is time to humanise the productivity growth discussion. This involves broadening the discussion to include services that provide not only readily measurable benefits to society, such as rising incomes but also those that do not show up in the official productivity statistics, such as people living longer, healthier lives.

As noted above, measuring productivity in non-market services can be extremely challenging. What is the productivity of a nurse or an aged-care worker, for example? How much GDP do they produce per hour worked? What is a police officer's or a firefighter's productivity, or the productivity of a member of the defence force? Their productivity is difficult to quantify, yet these are essential services.

Such measurement problems for the expanding non-market services sector create an impression that Australia's productivity slump is worse than it is. The Reserve Bank estimates that the rising share of employment in non-market services has lowered Australia's measured productivity growth by around 0.3 percentage points per annum over the last seven years[1], in total accounting for more than half the fall-off in measured productivity growth.

The rise of these types of services, as valuable as they are both economically and socially, makes returning to Australia's glory days of high measured productivity growth in the 1990s an unrealistic proposition.

The productivity of the health sector is typically measured by the resources it takes for a hospital or other health providers to deliver a particular service. Applying this approach, Australia's measured annual healthcare productivity[2] growth was a negligible 0.1 per cent in the previous decade, compared with a market sector average of 0.8 per cent.

However, these measured productivity growth statistics are not picking up large productivity improvements in the services sector. In a large segment of Australia's healthcare sector that the Productivity Commission has studied, annual healthcare productivity grew by a strong 3 per cent, four times faster than that of the market-based economy. Australia is third among 28 high-income countries in these health disciplines.

This is the discussion we need to have – where and how can we improve productivity in the health sector and other non-market services while knowing such improvements, though vital to our standard of living, might not show up in the official productivity statistics?

The Productivity Commission has come to the view that increasing the productivity of services will require a tailor-made approach. Australia can equip service providers with the latest technologies while not compromising on the quality of care. In these services, we are only seeing the early days of opportunities arising from the deployment of artificial intelligence (AI).

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[1] Reserve Bank of Australia (2025), "Why productivity matters," speech by Michael Plumb, Head of Economic Analysis Department, Sydney, 27 February, https://www.rba.gov.au/speeches/2025/sp-so-2025-02-27.html

[2] The Productivity Commission's study of healthcare has been done for multifactor productivity. See Productivity Commission (2024), Advances in Measuring Healthcare Productivity.

If Australia succeeds in these endeavours, living standards can continue to rise despite an ageing population. While the benefits of these reforms might not be fully reflected in the official productivity statistics, we will have humanised productivity growth by delivering higher-quality services at lower cost.

We look forward to continuing to work with the Productivity Commission on this important topic. If you would like to discuss this submission further, please do not hesitate to contact us.

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KPMG insights

Humanising productivity growth

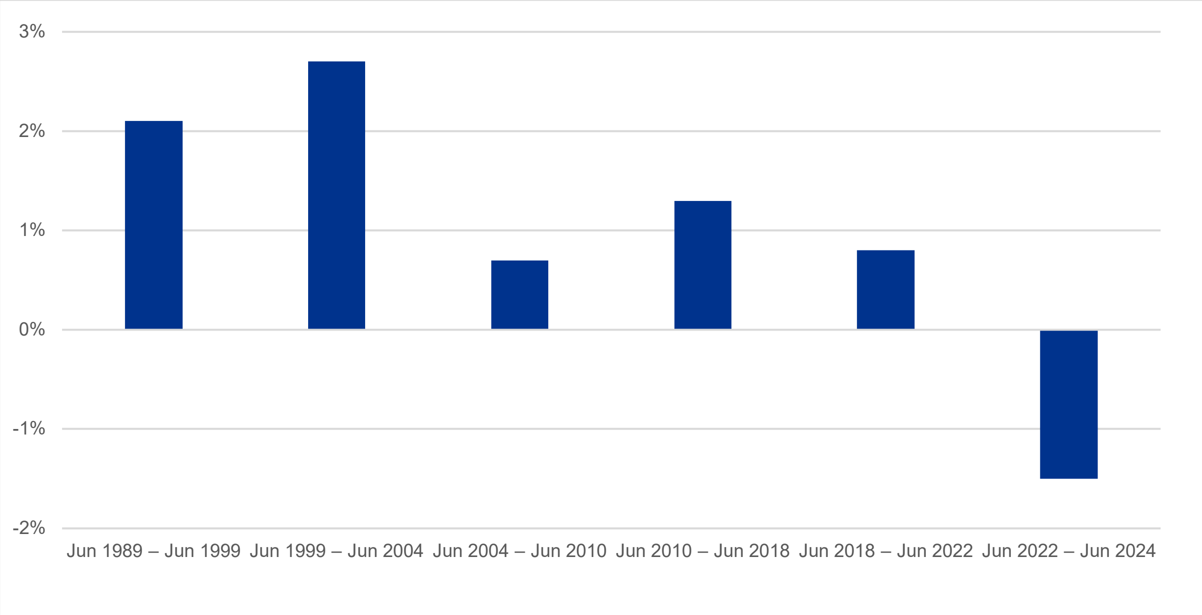
1. Productivity growth and Australian living standards

Productivity growth has been responsible for almost all the increase in Australia's prosperity since Federation.[3] In fact, after adjusting for inflation, GDP per person is about seven times greater now than it was at Federation.[4] Yet measured productivity growth in the decade to 2020 was at its slowest rate in 60 years.[5]

The 1990s are regarded as the benchmark against which subsequent productivity performance should be assessed. The stellar annual productivity growth of 2.2 per cent in the 1990s is broadly considered the reward of the economic reforms of the 1980s and 1990s, which created Australia's open, competitive economy.

Australia's weak annual productivity growth rate of 1.1 per cent in the period 2010-20 was just half the 2.2 per cent annual rate of the 1990s.[6] Since the pandemic, productivity growth has been weaker still (Figure 1).

Figure 1: Labour productivity growth – Australia: Non-farm GDP per hour worked (percent)



Source: Reserve Bank of Australia (2025)

Australia's productivity slowdown has not been unique. In fact, in the 15 years before the pandemic Australia's productivity slowdown was less severe than that of the OECD as a whole, including the US, Japan, the UK, France and Germany.[7]

[3] Productivity Commission (2020), Productivity Insights, p. 11.
[4] Productivity Commission (2023) 5-Year Productivity Inquiry: Key to growth (volume 2), pp. 1-2.
[5] Productivity Commission (2023) 5-Year Productivity Inquiry: Key to growth (volume 2), p. 27.
[6] Ibid, figure 2.2, p. 31.
[7] Ibid, figure 2.3., p. 32.

2. Why the 1990s productivity boom can't readily be repeated

2.1 The door to competition can't be opened twice but can be pushed wider

The economic reforms of the 1980s and 1990s were designed to transform the Australian economy from a closed, uncompetitive one protected by high tariff barriers, to an open, competitive economy. Reducing tariffs to no greater than five per cent, and in most cases to zero, coupled with National Competition Policy reforms and a shift away from a centralised wage-fixing system towards enterprise-level bargaining, all contributed to opening the Australian economy to competition.

The door to competition can be pushed wider through further national government reforms to competition policy and through the deployment of new digital technologies. These new technologies will enable workers and businesses to be more productive by working smarter, not harder. The federal government can also work with the states and territories to reduce productivity-stifling restrictions that prevent the easy movement of goods, services and skilled workers across borders.

2.2 Employment is shifting into industries with lower measured productivity

Along with all other advanced economies, Australia's economy has shifted from the high-productivity, capital-intensive production of goods to the lower-productivity, labour-intensive provision of services.

In 1950, agriculture, mining and manufacturing were responsible for around half of Australia's GDP and employment, with services production contributing the other half. Services now contribute around 80 per cent of GDP and 90 per cent of employment.[8]

The transition to services is a sign of a mature, advanced economy[9] and, as such, should not be resisted or reversed. All other advanced economies have undergone the same evolution. China, too, has started down this path, as lower-value manufacturing moves offshore to low-wage countries and the Chinese economy provides services to an increasingly affluent and ageing population. As the Productivity Commission explains:

"Almost all advanced economies have had rapid growth in their service sector (and relative shrinking of their manufacturing sector). This is the case even for the 'workshop of the world', China, since 2005."[10]

Consider a mine worker driving a massive truck laden with iron ore. One trip by one truck could move thousands of dollars' worth of iron ore. This mine worker, equipped with a large amount of capital, is highly productive.

Now consider an aged-care worker who helps residents shower, eat and move, and provides one-on-one human interactions with them.

While these two roles are highly valued by society, the mine-worker's measured productivity is considerable while that of the aged-care worker is unable to be properly calculated. If the productivity of the aged-care worker could be measured, it could be increased by doubling the number of residents under her or his care. But without qualitative assessment this would be a misleading statistic since the increase in 'output' might have been achieved at the expense of service quality.

Similarly, each nurse in a hospital could be required to provide care to a larger number of patients with no extra resources, but the quality of care would deteriorate. And the productivity of a school teaching could be increased by doubling class sizes from 25 to 50 pupils. However, it is reasonable to question whether we want these changes to happen, all in the name of productivity growth?

The structural shift in an economy from the production of goods to services is an indication of success, as productivity-enhancing economic development enables greater leisure time, better health care and, as life expectancy increases, better aged care for the growing number of elderly citizens.

Commenting on concerns about fears that Australia's shift towards services and away from manufacturing could cause a drag on productivity, the Productivity Commission explains:

"For the most part, these fears are unfounded."[11]

Policymakers, therefore, should not aim to shift an advanced economy back to high-productivity goods at the expense of reducing the price and quality of the non-market services sector. Rather, the challenge is

[8] Productivity Commission (2021), PC Productivity Insights: Things you can't drop on your feet – an overview of Australia's services sector productivity, figures 2 and 3.
[9] Ibid, p. 1.
[10] Ibid, p. 1.
[11] Ibid, p. v.

to lift the productivity of the services sector while at the same time increasing the quality of services provided.

2.3 Measuring productivity in the services sector

In the national accounts, services are categorised as market and non-market services. Market services comprise distribution, personal and business services, and utilities and construction. Non-market services are education and training, public administration and safety, and health care and social assistance.[12]

Measuring services productivity is much harder than measuring goods productivity. A unit of goods productivity is readily identifiable; it might be a tonne of ore, a bale of wool or an air-conditioning unit. But in market services, what is a standard haircut – a men's short back and sides, or a lady's style, cut and treatment.

A unit of non-market personal services such as policing and nursing care, firefighting and national defence is even more difficult to define.

The value of the output of agriculture, mining and manufacturing is the quantity produced multiplied by its competitive market price. But non-market personal services such as policing, national defence and public administration do not have a market price as such. This does not mean they have no value; just that their value cannot be easily measured.

As the Productivity Commission has pointed out:

"Because of these difficulties, output estimates in the non-market sector traditionally have been based on the total cost of production (that is, the total cost of inputs, also known as an 'output – input' model). By definition, this means measured productivity is zero, as output is determined directly by growth in inputs".[13]

Yet we should not reduce the provision of health, education and public safety just to increase Australia's measured productivity growth.

2.4 Difficulties in quantifying productivity in non-market services have dragged down Australia's measured productivity growth

The Reserve Bank has estimated that the rising share of non-market services has lowered the economy-wide measure of labour productivity growth by around 0.3 percentage points in the last seven years.[14] This compares with around 0.15 percentage points – or half as large – over the previous decade, so the recent effects have been much greater than in the past.

Looking through the volatility in the data caused by the COVID-19 pandemic and other supply disruptions, the Reserve Bank estimates measured labour productivity to have grown over the last seven years at a meagre 0.2 per cent per annum. It follows that the expanding non-market services sector has accounted for more than half the recent falloff in Australia's measured productivity growth.

2.5 Some services have inherently low productivity

Other factors also contribute to the low measured productivity in non-market services. Since the government is the main funder, supplier and regulator of these services, the characteristics of the market sector, such as competition, entries, exits and cost-reflective pricing that help stimulate innovation and productivity growth are mostly absent.[15]

To understand how quickly the non-market sector will continue to grow and what implications this could have for productivity growth, the Productivity Commission developed a simple model of the economy out to the year 2060-61, the timeframe of the Intergenerational Report.[16]

In most scenarios, the non-market sector will likely continue to grow as a share of GDP and employment. The Productivity Commission concludes that labour productivity growth rates will continue to decline as this sector continues to grow.[17]

[12] Ibid, box 1, p. 4.
[13] Productivity Commission (2017), 5-Year Productivity Review, Supporting Paper No 2, Non-Market Productivity Sector, p. 4.
[14] Reserve Bank of Australia (2025), "Why productivity matters," speech by Michael Plumb, Head of Economic Analysis Department, Sydney, 27 February, https://www.rba.gov.au/speeches/2025/sp-so-2025-02-27.html (p. 9).
[15] Productivity Commission (2023) 5-Year Productivity Inquiry: Key to growth (volume 2).
[16] Treasury (2023), Intergenerational Report, p. 45 and Appendix A5.
[17] Productivity Commission (2023) 5-Year Productivity Inquiry: Key to growth (volume 2).

3. The use of quarterly productivity statistics in setting monetary policy is fraught

In each of its board meetings last year, the Reserve Bank took account of the ABS productivity statistics in deciding on its cash-rate settings. But the Productivity Commission[18] has conducted an analysis of revisions to quarterly productivity estimates, concluding that:

"… measured labour productivity does not approach a 'true' estimate; rather, the figure is consistently changing" (p. 4) and

"… revisions are equally likely to be either upward or downward" (p. 11).

The Productivity Commission warns that the unreliability of the quarterly productivity estimates:

"… warrants caution in interpreting the meaning behind the numbers in any particular quarter."[19]

In the minutes of each of its meetings held in 2024 and 2025, the Reserve Bank Board has referred to Australia's measured productivity performance as influencing its monetary policy decisions. Similarly, the Reserve Bank covers the productivity data extensively in its Statement on Monetary Policy released several times a year and provides forecasts of productivity growth.

The unreliability of quarterly productivity statistics and the problem of measuring the productivity of the services sector – especially non-market services – suggests that the Reserve Bank Board should not place much weight on the official quarterly or even annual productivity statistics released with the national accounts in determining its monetary policy settings.

4. Boosting productivity in the services sector

4.1 Services-sector productivity matters

Despite the structural shifts in the Australian economy towards labour-intensive services, including non-market services, we should still care about Australia's weak overall productivity performance. Returning to the productivity boom years of the 1990s is an unrealistic proposition as it would require, at a minimum, taking the 'personal' out of personal services. We should want optimal not necessarily just larger class sizes at schools, and we should want more GPs, more child-care workers and aged-care workers.

But we can improve the efficiency of service delivery through policies such as reducing unnecessary red tape, linking up systems so that the same data is required only once not multiple times, and providing advice online where a direct interaction is not required. Further, the productivity of service-industry workers can be increased through better education and training, including vocational education short courses.

4.2 Lifting service-sector productivity through digitisation

Digitisation has sharply reduced the cost of providing many services, increasing the productivity of those services. The availability of rental accommodation in specific localities can now be ascertained through search sites instead of personally needing to visit real estate agents' premises. Information can be found online about the availability, cost and reputation of different restaurants.

Uber services are readily available on mobile devices, forcing the taxi industry to follow suit in also making its services available on mobile devices. This allows the service provider to locate and track the ride, and vice versa, while also integrating fare payments – improving the quality of the service by making the experience easier, more efficient and safer.

Businesses and government agencies, spurred on by the physical distancing restrictions associated with the COVID-19 pandemic, are now more heavily utilising digital meeting technologies such as Microsoft Teams to reduce the travel time and costs associated with physical meetings. Beyond the direct cost savings, reductions in physical travel can also save on new transport infrastructure and traffic congestion, providing a further boost to productivity.

Artificial intelligence (AI), properly developed and deployed, has enormous potential to further increase the productivity of business and personal services in a multitude of ways. The utilisation of AI is

[18] Productivity Commission (October 2024), Revisions to Quarterly Labour Productivity Growth.
[19] Productivity Commission (September 2024), Quarterly Productivity Bulletin.

increasing exponentially, prospectively representing the dawning of a new era of productivity growth in both the goods and services sectors.

Early studies are demonstrating the potential for AI to improve productivity. A Harvard Business School study involving management consultants found that the use of AI made them significantly more productive and produced higher quality results. Tasks were completed 25 per cent more quickly with more than a 40 per cent improvement in quality when compared with a control group.[20]

4.3 Productivity improvements in the health sector

As the economy shifts further into services, bespoke solutions to lifting productivity will be increasingly appropriate. As Michael Brennan, former chair of the Productivity Commission, explains, in relation to the Commission's work on innovation in care for chronic health conditions:

"It was a bottom-up approach based on understanding the specifics of what happens in individual hospitals, clinics and GP practices.

"Could something similar be said of policy in general? Possibly. We might find that the policy mix required to foster productivity growth in service firms and industries is less like the big bang reforms of the past and consists more of bespoke approaches tailored to the specifics of that industry."[21]

The productivity of the health sector is typically measured by the resources it takes for a hospital or other health providers to deliver a particular service. Applying this approach, Australia's measured healthcare productivity growth has been negligible, at 0.1 per cent in the previous decade, compared with a market sector average of 0.8 per cent.

But this approach ignores the *quality* of the service provided. Taking quality into account, it turns out that in the one-third of Australia's healthcare sector by spending in the previous decade that has been studied by the Productivity Commission, annual healthcare productivity grew by a strong 3 per cent, placing Australia third among 28 high-income countries for healthcare productivity.

The areas studied were healthcare used to treat cancers, cardiovascular disease, blood and metabolic disorders, endocrine disorders and kidney and urinary diseases. The improved quality showed up in longer and healthier lives but would not be captured under conventional productivity measurement approaches. Much of the improvement has come from quickly adopting new treatments, which is a lesson for the direction of federal-state reforms in the health sector.

As the Productivity Commission observes:

"Quality improvements, not cost reductions, were the big contributors to productivity growth. Health practitioners' ability to understand, diagnose and prescribe has been transformed by medical advances. These quality improvements have made us vastly better off. Indeed, the biggest contribution to productivity growth has come from advances in saving lives."[22]

The Productivity Commission further found that Australia has been particularly successful in reducing smoking rates but far less so in dealing with its high rates of obesity and alcohol consumption.[23]

KPMG has worked with Medibank in assessing the net benefits of:

- Rehabilitation in the home for hip and knee replacements; and
- Home hospital services in South Australia.

Greater use of patients' homes for care and rehabilitation, enabled by digital technologies to monitor patients, can be a win all round – for patients who prefer recovering in their own homes with family and pets, sleeping in their own beds and eating their preferred meals when they choose, and for the health system through reduced reliance on scarce and expensive hospital beds and facilities.

KPMG found that rehabilitation in the home for hip and knee replacements achieved similar clinical outcomes as rehabilitation in hospitals but with substantial savings in hospital beds and facilities.

Home hospital models replicate the level of care provided in traditional hospitals, providing acute care to patients in their own homes using a combination of technological interventions and direct face-to-face care by doctors, nurses and allied health practitioners. KPMG found *My Home Hospital* in South Australia

[20] Dell'Acqua, Fabrizio *et al*. (September 2023), Navigating the Jagged Technological Frontier: Field experimental evidence of the effects of AI on knowledge worker productivity and quality.
[21] Brennan, Michael (2021), Speech to McKell Institute: Services sector productivity.
[22] Productivity Commission (2024), Advances in Measuring Healthcare Productivity, pp. 2-3.
[23] Ibid, p. 3.

could achieve large savings in hospital beds and the need to build new hospitals as Australia's population continues to age. Satisfaction with *My Home Hospital* care was 98 per cent.

National partnership agreements for innovations in service delivery

Various approaches are worth trying to improve the quality of health services while reducing their overall cost. Federal, state and territory governments could identify best practice by private providers and trial those approaches in the public system.

A further possible approach is to give non-market, government-funded service providers a license to innovate. This is what the HealthLinks trial in Victoria involved. By changing the funding incentives and allowing public hospitals to take risks, the five hospitals in the trial all tried different innovations. Some were not successful, but others showed the potential for system-wide productivity gains.

An approach reminiscent of the national partnership agreements between federal and state and territory governments in the early 2010s is worth considering. These agreements could identify best practice in service delivery within a state or territory and encourage its adoption by other jurisdictions through incentive payments.

A complementary approach to national partnership agreements would be to develop and adopt a regulatory reform program to move Australia towards a seamless national economy. State and territory regulations would be harmonised, reducing interstate barriers to the movement of goods and licensed tradespersons. Progress was made by previous federal governments but it remains unfinished business.

A further example is the proposed Simplified Trade System, which would digitise the customs clearance systems for Australia's imports and exports, greatly reducing transaction costs, clearance times and administrative burdens for importers and exporters.

5. A revitalised national competition policy agenda

One of the main explanations for Australia's worsening productivity performance that has been put forward is declining market dynamism. In a presentation to the Melbourne Economic Forum in late-2024,[24] Chair of the Productivity Commission, Danielle Wood, suggested diminished competition was a factor, citing evidence that labour mobility is falling, non-mining investment has been stagnant since around 2007, Australian markets generally are more concentrated than their US counterparts and industry concentration in Australia is higher than in the 2000s.

In November 2024, the federal, state and territory governments signed up to a new National Competition Policy agenda. Modelling by the Productivity Commission of 19 of the potential reforms estimates a revitalised competition agenda could result in an ongoing boost to GDP of up to $45 billion, an increase of up to $5,000 for every Australian household each year.

Work is already underway on five reforms as part of the 10-year National Reform Agenda:

- Streamlining commercial planning and zoning systems;
- Fast-tracking the recognition of equivalent or superior overseas product safety standards;
- Supporting modern methods of construction;
- Boosting labour mobility for care workers; and
- Developing broader rights to repair, including for agricultural products.

Further reform rounds will be informed by new inquiries by the Productivity Commission.

This set of inquiries will examine:

- Creating a more dynamic and resilient economy;
- Building a skilled and adaptable workforce;
- Harnessing data and digital technology;
- Delivering quality care more efficiently; and

[24] Daneille Wood, Chair of the Productivity Commission, "Sluggish productivity – what's going on?" presentation to the Melbourne Economic Forum, 17 December 2024, at https://melbourneeconomicforum.com.au/wp-content/uploads/2025/01/Wood-Dec-2024.pdf

- Investing in cheaper, cleaner energy and the net zero transformation.

KPMG supports this reform program and notes that, as with past reforms, it will require incentive payments to the states and territories. The Australian government's $900 million National Productivity Fund can be expected to get the reform ball rolling.

6. KPMG is keen to contribute

KPMG is keen to contribute to the federal government's productivity-raising reform program through its expertise in tax reform, competition policy, a seamless national economy, digitisation, AI and the design of efficient delivery of health services as exemplified by rehabilitation in the home for hip and knee replacements and the home hospital model being adopted in South Australia.

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