



Submission to House of Representatives Standing Committee on Economics'

Inquiry into Promoting Economic Dynamism, Competition and Business Formation

31 March 2023

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Introduction

Microsoft welcomes the opportunity to provide a submission to the House of Representatives Standing Committee on Economics (the **Committee**) in its inquiry into promoting economic dynamism, competition and business formation (the **Inquiry**).

Founded in 1975, Microsoft is a global technology company that develops and supports software, services, devices, and solutions. This year, we will celebrate 40 years of participating in and contributing to the Australian economy. Today, Microsoft works with over 9,000 partners who employ over 200,000 Australians across all States and Territories.

We believe that technology is a powerful force for good and are committed to fostering inclusive growth by helping companies of all sizes digitally transform. Our company mission is to empower every person and organisation on the planet to achieve more. The Inquiry's focus on supporting healthy competition and boosting productivity in the Australian economy aligns with our mission and values.

As Australia embarks on our post COVID economic recovery, it is important to consider appropriate steps and regulatory settings to support and encourage businesses of all sizes to innovate and grow. As set out in more detail below, we welcome the Committee's focus on fostering diverse and dynamic business environment that enhances productivity and resilience. We also urge the Committee to recognise the heterogeneity of the tech sector when examining the different reasons and impacts of consolidation in Australian markets. Finally, we encourage the Committee's consideration of steps to decrease economic and other barriers to the productivity benefits of the digital economy by improving regulatory coherence and coordination.

1. Impact of technology on competition and productivity

1.1 Size and growth potential of the tech sector

Australia has a vibrant and diverse tech sector encompassing a wide range of companies and individuals who develop digital technologies, including hardware, software, computing infrastructure, online platforms, digital products and services, or any combination of these products and services.

Our tech industry has grown into a critical pillar of the economy and contributes AU\$167 billion to GDP per year, equivalent to 8.5% of our total GDP.¹ This is made up of a direct contribution from tech-related industries of \$76 billion and an indirect contribution of \$92 billion.² If the tech sector were classified as its own industry, it would be equivalent to the third largest contributor to GDP in Australia – just behind mining and finance and ahead of healthcare, construction, and retail.

Digital technologies have great potential to drive future growth and productivity in Australia. The economic contribution of the tech sector has increased 79% since 2016, more than four times the average growth rate of other sectors. A study by CSIRO and Data61 forecasts that AI and other digital technologies will add AU\$315 billion to the Australian economy by 2028. The extraordinary growth potential of the tech industry means that it is likely to surpass the GDP contribution of the primary and manufacturing industries in the next decade – see Figure 1 below. In addition, many segments

¹ Tech Council of Australia and Accenture, [The economic contribution of Australia's tech sector](#), August 2021, p8.

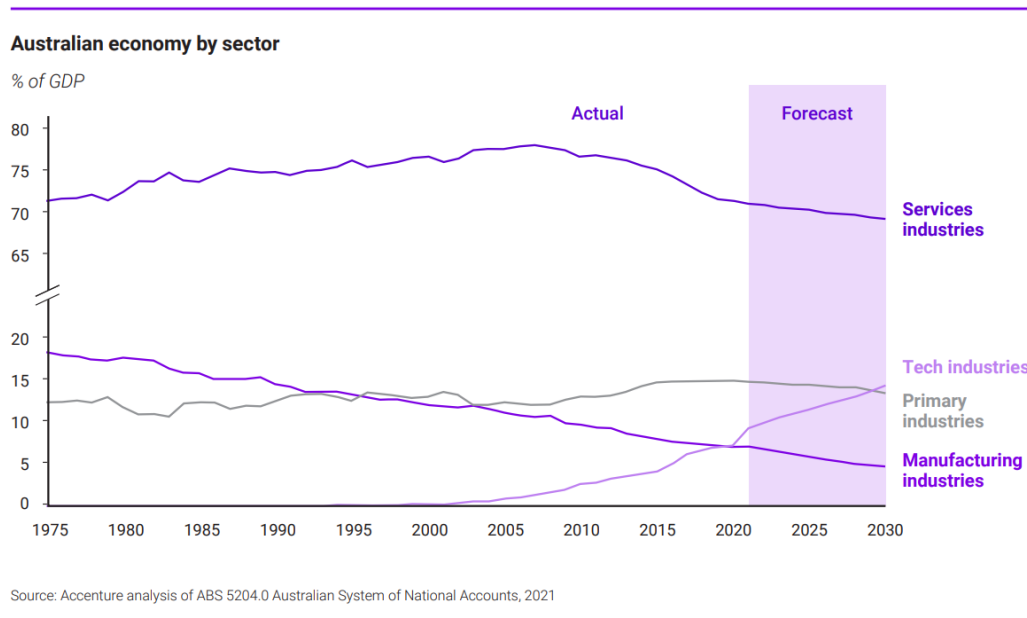
² Ibid.

where Australia is producing a higher-than-average level of start-ups coincide with industries that are traditionally areas of strength in the Australian economy such as Mining Tech, Lending, AgTech and EdTech.

Australia has a strong track record of developing and adapting new technologies as well as launching globally successful tech companies – 2.3% of the world’s tech unicorns (US\$1 billion companies) have come from Australia, despite our much smaller 1.6% share of global GDP. And there is considerable scope to accelerate our success further by embracing the diversity of our thriving tech ecosystem.

Additionally, there is great potential for technology to support economic growth via the diffusion of innovation. As noted by the Productivity Commission in its recent report, fostering the diffusion ‘of new and established technologies and ideas across the majority of enterprises in the economy represents a significant opportunity to increase productivity.’³ Small technological improvements across many firms add up to considerable productivity gains. This applies both to established technologies (such as accounting software) and to cutting-edge technologies (such as artificial intelligence applications to business processes).⁴

Figure 1 – Growth potential of the tech sector in Australia⁵



1.2 Leveraging technology to boost competition and productivity

Technology is a key driver of productivity and economic growth by enabling more efficient and innovative production of a vast variety of goods and services. As our CEO Satya Nadella has said, ‘digital technology is a deflationary force in an inflationary economy’.⁶ It is important to appreciate the ways and extent to which digital technologies increase allocative efficiency and dynamic competition, which are both important goals of competition policy.

³ Productivity Commission, [Advancing Prosperity](#), Volume 5: Innovation for the 98%, 7 February 2023

⁴ Ibid, p2.

⁵ Tech Council of Australia and Accenture, [The economic contribution of Australia's tech sector](#), August 2021, p13.

⁶ Microsoft, [Earnings Release FY22 Q1](#), 26 October 2021.

First, **allocative efficiency** refers to the optimal allocation of resources and output among consumers and producers in a market, such that consumer surplus and producer surplus are maximized. Different digital technologies can enhance allocative efficiency in many ways, such as by reducing transaction costs, increasing transparency, facilitating price discrimination, and enabling better matching of supply and demand. For example, online search can lower search costs for consumers and sellers, and online marketplaces can reduce transaction costs by connecting buyers and sellers across geographic boundaries.

Second, **dynamic competition** refers to the process of innovation and entry that drives productivity growth and consumer welfare in the long run. Digital technologies can foster dynamic competition by lowering the entry costs for new challengers to disrupt incumbents by offering innovative products or services at lower costs or higher quality. For example, research from the Tech Council of Australia has found that the early presence of global tech companies in Australia – IBM for 90 years, Microsoft for 40 years, Google for nearly 20 – is an important factor contributing to the success and oversized impact of Australian's software industry.⁷ Access to leading cloud technologies and infrastructure drives down costs and improves efficiencies, helping companies of all sizes to accelerate their productivity, innovate quickly, and compete on a global scale. This has facilitated the emergence and rapid expansion of Australian-based software-as-a-service platforms which, in turn, has lifted the productivity of other small businesses who leverage these platforms to grow. This is why we believe the cloud is a great democratiser that makes the best of innovation, security, and performance capabilities accessible and affordable to all businesses and organisations regardless of size. For example, Australian start-up LiveTiles was founded in 2014 with 10 employees and is now a global platform with 130 employees across Australia, the US, Europe, and the Asia Pacific.⁸ LiveTiles attributes its success to early support from Microsoft, including help building robust, secure, and scalable products, and benefited from being able to leverage Microsoft's cybersecurity expertise to gain an edge.⁹

See case study box below for a further discussion of research showing the ways in which available of cloud computing services can improve the productivity of the broader economy.

Encouraging the **diffusion of innovation** is likely to boost both allocative efficiency and dynamic competition. Notably, Australian businesses have been found to be slower adopters of certain digital capabilities, like big data analysis and artificial intelligence, relative to other OECD countries.¹⁰ And as found in separate research from the then Department of Industry, Innovation and Science, many Australian firms have found success with the strategy of seeking out, adapting and implementing existing innovations.¹¹ We therefore welcome the recent recommendation by the Productivity Commission that: 'Innovation policy should broaden and give more emphasis to the spread and adoption of new technology and best practice. Adoption of digital technology, such as AI, and the

⁷ Tech Council of Australia and McKinsey & Company, [Turning Australia into a Regional Tech Hub](#), August 2022, p9.

⁸ Tech Council of Australia and Accenture, [The economic contribution of Australia's tech sector](#), August 2021, p38.

⁹ Ibid.

¹⁰ Productivity Commission, [Advancing Prosperity](#), Volume 4: Australia's data and digital dividend, 7 February 2023.

¹¹ Department of Industry, Innovation and Science, [Australian Innovation System Report 2017](#), 1 November 2017.

better use of data by businesses can boost productivity and should be encouraged by government action.¹²

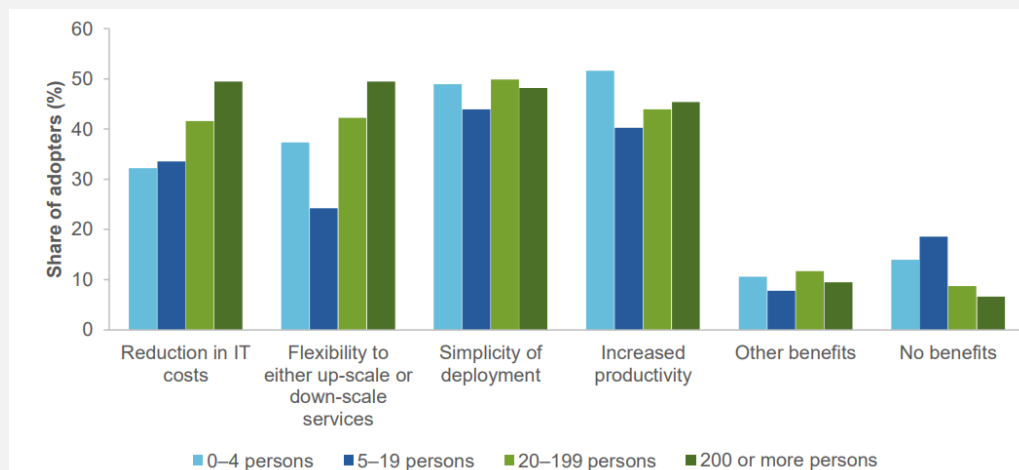
Case study: cloud computing as a driver of competition and productivity

Cloud technologies enable the digital transformation of businesses across the Australian economy. Our work in cloud computing services focuses on developing technologies that can be used by *any* company, non-profit, or Government agency as an input to increase productivity and help build and enhance their own products or services in pursuit of innovation and growth.

According to research by the Productivity Commission: 'There is good evidence that cloud services improve productivity. Such services allow businesses to tailor their computing resources more flexibly to their organisational needs, avoiding the large fixed costs of conventional computing solutions, and enable new ways of working'.¹³ Moreover, the Productivity Commission's analysis found that 'cloud technology is associated with higher firm turnover per worker and higher wages per worker', with larger effects for regional businesses for which cloud technologies assist in overcoming the tyranny of distance.¹⁴

As depicted in **Figure 2** below, large shares of organisations of all sizes experience benefits associated with cloud technology, including reduction in IT costs, flexibility to up-scale or down-scale, simplicity of deployment, and increased productivity. Importantly, the research further indicated there were large numbers of firms that would benefit from cloud technologies but have not adopted them. It is important, therefore, to have the right policy settings in Australia to facilitate and encourage the use of different computing services and deployment methods to enable organisations, large and small, to innovate quickly, increase efficiency, accelerate productivity, and compete on a global scale.

Figure 2 – Share of Australian adopters experiencing benefits¹⁵



¹² Productivity Commission, [Advancing Prosperity](#), Recommendations and reform directives, 7 February 2023, p17.

¹³ Henry McMillan, Tim Murray, Catherine de Fontenay and Ralph Lattimore, Productivity Commission, [Head in the Cloud: Firm performance and cloud service](#), 26 October 2022, p3.

¹⁴ Ibid, p5.

¹⁵ Ibid, p6.

1.3 Market concentration and anti-competitive conduct

The Committee is directed to consider '*[t]he extent to which anti-competitive behaviour and changes in industry structures have contributed to rising market concentration in Australia*'. We believe that a full examination of this issue in the technology sector requires a nuanced understanding of the different businesses and business models that operate in the industry.

There has been increasing scrutiny from lawmakers in Australia and overseas on the unique challenges of regulating some digital markets. The ACCC has conducted numerous inquiries looking into the increasing ubiquity of some digital platforms in intermediating consumers' activity online and the impact this has on competition and consumers in Australia. In particular, the ACCC's Digital Platform Services Inquiry has identified concerns arising from the conduct of gatekeeper digital platforms and recommended reforms to enhance competition and innovation in digital markets.¹⁶

In considering any links between consolidation and anti-competitive conduct or reduced competition in digital markets, we urge the Committee to start by recognising the heterogeneity of the products and services that make up the tech sector. This includes understanding the many different business models prevalent in the tech industry, including their different customers, objectives, incentives, and competitive constraints. Common business models underpinning the large variety range of products and services in the tech sector can be just as varied and include one or more of: ad-supported; perpetual licenses, consumption-based, and subscriptions; open source; peer-to-peer, on-demand, e-commerce marketplace, and freemium. No one business model is inherently 'good' or 'bad', but each is accompanied by different incentives and constraints that affect what competition looks like and the likelihood and impact of consolidation.

For instance, cloud computing infrastructure services typically involve the supply of technology-enabling infrastructure as an input to other businesses for a fee. Adoption and development of cloud technologies requires substantial investment in infrastructure, which creates another avenue to spur economic growth. The high fixed costs involved in supplying cloud computing infrastructure can mean there is less churn than in other markets with lower fixed costs, but there is nevertheless vigorous and effective competition in this space due to the evolving variety of cloud offerings, rapid pace of innovation, and constant threat of new entry from well-resourced global firms.

2 Trade and supply chain resilience

In considering options for bolstering Australia's supply chain resilience, we urge the Committee take into consideration the substantial advantages of open trade and open foreign investment to the Australian economy.

As found in a recent Austrade report, '[o]ur success comes from being an open and adaptable trading nation that is deeply connected to the global economy'.¹⁷ Open trade allows Australian consumers and businesses to access larger markets and participate in global value chains. This increases competition, lowering the cost and increasing the quality of goods and services available in Australia. Trade contributes over 40% of Australia's GDP, with services and digital trade emerging as important areas of trade growth.¹⁸ As recently cautioned by the Productivity Commission: 'While supply-chain

¹⁶ Australian Competition and Consumer Commission, Digital Platform Services Inquiry, [September 2022 interim report – Regulatory reform](#), 11 November 2022.

¹⁷ Austrade, [Why Australia: Benchmark Report 2023](#), March 2023, p43.

¹⁸ Ibid.

issues need to be dealt with... the need for resilience must not veil revitalised protectionism or selective industry policy, given the inefficiency and rent-seeking they bring'.¹⁹

Given the relative size of the Australian economy, it is important to acknowledge that 'it is not optimal for us to invent everything domestically' and that 'many ideas and technologies will come to Australia from overseas'.²⁰ Indeed, exposure to new technologies and ability to expand into overseas markets is especially vital in the tech industry. And it is equally important and beneficial to be able to leverage the productivity-enhancing innovations that come from outside our borders.²¹ Policies to facilitate and safeguard open trade are critical for Australian tech businesses who want to grow, trade, and compete internationally.

Foreign investment is also a key component of accelerating the growth of Australian businesses. Foreign direct investment in Australia is growing fast and, as a percentage of GDP, has risen from 123% in 2001–02 to almost 200% in 2021–22.²² As observed by the Productivity Commission Deputy Chair Mr Robson, 'Openness to foreign investment can be an important source of competitive pressure and innovation'.²³ Overseas companies, including US-based companies, make valuable investments in the Australia economy. For example, the US investment footprint in Australia totals AU\$984 billion to-date.²⁴

3. Regulatory costs and barriers to productivity

Finally, we welcome the Committee's examination of the impact of '*economic barriers—such as regulatory costs and barriers to finance, infrastructure, suppliers, customers and workers*' in Australia.

3.1 Prioritising domestic policy coherence

The Australian tech sector is affected by many overlapping policy areas overseen by different regulators, Ministers, and Government Departments and currently subject to numerous interlinked policy proposals.

For example, current policy initiatives on the issue of data practices alone include: the 116 privacy reform proposals published in the Privacy Act Review Final Report; the Department of Prime Minister and Cabinet's Australian Data Strategy; the Minister for Home Affairs' 2023 Cyber Security Strategy; the e-Safety Commissioner's Online Safety Reforms; the ACCC's Digital Platform Services Inquiry; the Digital Transformation Agency's Digital Identity Legislation; the Department of Home Affairs' Critical Infrastructure Legislation; the Digital Transformation Agency's Data Hosting Certification Framework.

¹⁹ Standing Committee on Economics, Inquiry into promoting economic dynamism, competition and business formation, [Productivity Commission public hearing transcript](#), 16 March 2023.

²⁰ Productivity Commission, [Advancing Prosperity](#), Volume 3: A competitive, dynamic and sustainable future, 7 February 2023, page iv.

²¹ Productivity Commission, [Advancing Prosperity](#), Volume 5: Innovation for the 98%, 7 February 2023, p4.

²² Austrade, [Why Australia: Benchmark Report 2023](#), March 2023, p46.

²³ Standing Committee on Economics, Inquiry into promoting economic dynamism, competition and business formation, [Productivity Commission public hearing transcript](#), 16 March 2023, p4.

²⁴ Jared Mondschein, United States Studies Centre, [The role of US innovation in securing Australia's economic future](#), 20 August 2020.

Notably, inconsistent and unpredictable regulation has been identified as a key barrier to innovation and capturing the benefits of digital technologies.²⁵ As found in recent research by the Tech Policy Design Centre, siloed tech policy development from a narrow focus on addressing one problem inadvertently creating new challenges in other areas.²⁶ Multiple intersecting regulatory reforms bring considerable uncertainty and complexity for Australian businesses of all sizes as well as duplication and dilution of efforts across policymakers. Moreover, separate consideration of different and sometimes competing policy goals may create conflicting outcomes and result in further regulatory instability. And persistent legal gaps may remain underregulated despite a proliferation of regulatory proposals.²⁷

Cultivating greater coordination between the different Government Ministers, Departments, and agencies responsible for tech regulation in Australia would facilitate more comprehensive and considered development of tech policy.²⁸ Therefore, a key aspect of reducing regulatory barriers to tech-led productivity gains requires the Government taking a collaborative approach to develop a coherent domestic regulatory framework that meaningfully balances different rights, policy objectives, and stakeholder interests to achieve effective regulatory outcomes.

3.2 Enhancing international regulatory coordination

In the digital economy, all businesses should be born global. Ensuring Australia's regulations are globally aligned not only supports international companies wanting to do business with and in Australia, but it also supports local businesses wanting to grow, trade and compete internationally. As found by the Australian National University's Tech Policy Design Centre, enhancing international coordination with comparable jurisdictions will help make Australia a more attractive place to do business.²⁹

In addition, globally consistent regulations will drive better outcomes across different markets by increasing legal certainty and lowering regulatory burden by avoiding inefficiencies and the creation of a complex web of incompatible standards.

Policies to facilitate trans-national data flows are particularly indispensable to enhancing both productivity and security. Trans-national data flows have become indispensable to many industries and trusted cross-border data flows are key to growth, innovation, and cybersecurity. Transformative technologies, such as artificial intelligence, can be leveraged to help businesses of all sizes grow. These technologies are powered by large amounts of data and cannot thrive without cross-border data flows. Importantly, facilitating cross-border data flows can also have significant benefits on cybersecurity – as cyberattacks are often trans-national and fast-moving, strengthening cybersecurity often requires swift and effective data-sharing on a global basis.

Conclusion

Technology can be leveraged to boost productivity and economic growth in Australia by increasing innovation and fostering a more dynamic and competitive economy. This includes both the

²⁵ Tech Council of Australia and Accenture, [The economic contribution of Australia's tech sector](#), August 2021, p7.

²⁶ Tech Policy Design Centre, [Cultivating Coordination](#), 21 February 2023, p8.

²⁷ Ibid.

²⁸ Ibid, p6.

²⁹ Ibid, p8.

development of cutting-edge new innovations as well as boosting Australian businesses' uptake of established technologies. In particular, cloud and artificial intelligence technologies can be leveraged to accelerate the growth and global competitiveness of Australian businesses of all sizes and drive a tech-led productivity boost in Australia. Moreover, we note the importance of open trade and foreign investment for Australia's economy and supply chain resilience in providing access to larger markets, increase competition, and allow for exposure to new technologies. With the right regulatory settings, Australia is well-positioned to reap the considerable benefits of a flourishing tech ecosystem that boosts the overall Australian economy. To realise this unique opportunity, we urge the Committee to consider ways of lowering economic barriers and decreasing regulatory uncertainty by prioritising the collaborative development of a coherent domestic policy framework as well as coordinating with overseas regulatory outcomes.

We appreciate the Committee's consideration of our views on promoting economic dynamism, competition, and business formation in Australia and look forward to engaging further with the Committee on this issue.