



SUBMISSION TO THE

PRODUCTIVITY COMMISSION INQUIRY

INTO THE IMPACT OF COMPETITION POLICY REFORMS

ON RURAL AND REGIONAL AUSTRALIA

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Executive summary

This submission discusses the impacts (actual and potential) of the National Competition Policy (NCP) on agriculture, fisheries and forestry industries and country Australia¹ in accordance with the Productivity Commission's (PC's) terms of reference to assess the impact (both transitional and ongoing) of the competition policy and related reforms introduced by governments under the three inter-governmental agreements signed in April 1995—the Competition Principles Agreement (CPA), the Conduct Code Agreement and the Agreement to Implement the National Competition Policy and Related Reforms. There is a particular emphasis on the need for measures to facilitate the flow of benefits and to reduce transitional costs and avoid unintended negative impacts on portfolio industries and country areas.

The agriculture, fisheries and forestry industries are affected by factors other than the NCP, such as globalisation, non-NCP reforms, social changes, and increasing acceptance of sustainable resource use. The submission notes that it may be difficult to separate these impacts from those of the NCP reforms. Further, many NCP reforms have not yet been implemented. The NCP reforms have been occurring at a time when these other significant forces have continued to affect rural industries and communities. For this reason, there may be a degree of confusion in rural communities between the particular effects of each of the above factors, as opposed to the impacts of the NCP. Further, much of the reform process lies ahead. This contributes to the difficulty in assessing the impact of the NCP as opposed to the impacts of other changes.

The implementation of the NCP has and will continue to cause pressures for adjustment in the economy and the community. There is also a dichotomy between the timing of the costs of reforms (which are much more immediate and concentrated on a particular industry and region) and the benefits (which can take some time to occur and are more diffuse). The cumulative impacts and temporal and spatial distribution of the costs and benefits of many reforms have not been fully investigated. Without such investigations, it is difficult to evaluate the relative costs and benefits of the reform process in particular places or time periods and to manage the structural adjustment process.

Portfolio industries in the Australian economy

Although there have been significant changes in the final decades of the 20th century, agriculture still occupies an important place in the Australian economy and Australian agriculture occupies an important place in global rural trade, particularly in Asian countries over recent times where many new markets have been forged for wheat, beef, fruit, sugar and dairy produce.

Employment in the agriculture, fisheries and forestry industries has increased slightly over the period 1990–91 to 1997–98 and, in addition, much employment is indirectly supported by these industries.

Many forces, eg. globalisation, policy changes, sustainable resource use and demography, have been impacting on portfolio industries. The NCP reforms have been occurring at a time when these other significant forces have continued to affect rural industries and communities. For this reason, there is a high degree of confusion and uncertainty in rural communities, about the particular effects of each of the above factors, as opposed to the impacts of the NCP.

Differences between country and metropolitan Australia

The submission notes that many regional economies are not economically diverse—much of the economic base of some regions is built around the production of a specific commodity, with that

¹ The term “country Australia” is used in this submission to cover rural and regional Australia.

dependence being a contributing factor to problems being faced in some areas. Economic diversity would help regional economies deal with external shocks and growth opportunities. Some rural and regional areas are geographically isolated and low population densities in rural areas increase problems of access to services. The financial and time costs associated with overcoming physical isolation place limits on access to social interaction, cultural and employment opportunities, information, and public and private sector services and facilities. Also, rural labour markets are characteristically more highly specialised and are smaller than urban labour markets. Rural labour markets reflect local economic conditions and also affect the resulting social and economic structure by influencing migration patterns and population densities. Also, about one third of the indigenous population lives in rural areas and on small islands and the agriculture, fisheries and forestry industries are major employers of aboriginal and Torres Strait Islands people.

Impacts of NCP on the economy and portfolio industries

In the longer term, the impact of the NCP reforms is likely to be positive overall for people in country Australia, as industries become more internationally competitive. The reforms will encourage increased competition, which should serve to encourage reduced input costs, generally lower prices, improved services and more efficient resource allocation.

At this stage of the NCP process there are three main reasons why it is not easy to be precise as to the extent of these broader economy-wide benefits, especially for portfolio industries. First, many of the NCP reform tasks lie ahead; second, the exact nature of any reforms to be implemented have either not been decided or implemented; and third, any such reforms can become intermingled with the effects of other changes. On the same grounds it is equally as difficult to be precise as to the costs of any adjustment.

The economic benefits to the nation of competition reform are considered to be substantial. The NCP reforms are likely to remove market imperfections and, thus, improve resource allocation. The overall benefit from the Hilmer and related reforms is a one off but persisting “gain in real GDP of 5.5 per cent, or \$23 billion a year (in 1993–94 dollars).” (IC 1995, p. 53) Across the electricity and gas sectors, the long term benefits of the reforms were estimated by the Industry Commission (1995) to be around \$5.8 billion real growth in GDP per annum, with a sizeable share of this coming from competition in the natural gas sector.

Implementation of the COAG water reform framework can be expected to result in long term economic, social and environmental benefits for those individuals and rural communities based around irrigated agricultural industries, although there may be some shorter term adjustment costs. Where water is allocated to the most economically and environmentally optimal uses there are significant benefits available, eg. through trade in water between low value and high value production.

It is also worth noting that competition in the global marketplace is trending towards supply chain versus supply chain competition. Given the importance to rural industries of the full production and distribution chain, reforming links in the chain that have not previously been exposed to competition, eg. electricity supply and roads, will mean that Australian rural produce will become more competitive, both domestically and internationally.

The NCP offers the scope for measures that are designed to increase competition to be introduced that can potentially increase incomes in the economy, and this needs to be taken into account in any examination of the consequences of particular NCP reforms, especially those that may impose costs of adjustment. An overall increase in incomes can lead to increased demand for goods and services, including those from country Australia.

The costs of adjustment involved in increasing competition are highly visible (being concentrated on one region or industry) and relatively immediate, whereas the benefits tend to be diffuse and

occur throughout the economy and over the longer term. It is therefore not surprising that there can be considerable debate as to the merits of the NCP and some initial public concerns about policy changes that may eventually benefit the national economy, and the particular region or industry in the longer term. Costs from the NCP could arise due to differences in its timetabling and operation between jurisdictions. In addition, parallel or successive reforms could impose higher structural adjustment costs on particular industries, potentially reducing the industry's capacity to respond to change. Examples could include the cumulative effect on irrigated industries of reforms in the areas of water and in statutory marketing arrangements. The NCP should also give consideration to conditions in the international market, particularly with regard to exporters being able to exploit any potential bargaining power.

AFFA supports moves to increase efficiency in the economy, however, it believes that transitional arrangements should be utilised in order to ease adjustment (which should reduce the overall costs of reforms and make them more publicly acceptable). The implementation of the NCP has and will continue to cause pressures for adjustment in the economy and the community. Although the overall costs and benefits of reform may have been estimated, the temporal and spatial distribution of the costs and benefits of many reforms have often not been fully investigated. In addition, the cumulative impacts of the various reforms and other changes have not been analysed. Where they can be undertaken, such studies could help to evaluate the relative costs and benefits of the reform process in particular places or time periods and to manage the structural adjustment process.

Structure, competitiveness and regulation

The NCP will undoubtedly be a major force in any structural changes which occurs in portfolio industries. It is difficult to say with any certainty how the structural changes resulting from the NCP will impact on country Australia as many reforms are yet to occur. However, with any NCP reforms which increase competition, there should be greater efficiency and more effective (less costly) regulation. However, there will be transitional effects. Depending on particular circumstances, adjustment costs can be high. There is a need to monitor the changes and work with industry through transition periods so that particular groups do not suffer unduly as the broader community benefits from the overall positive effects. Continual monitoring and review in relation to the impacts on portfolio industries will be desirable as the NCP and other policies are implemented, so that the likely gains can be realised without undue dislocation and hardship for the few.

Economic and social impacts

NCP reforms will have both beneficial and adverse impacts on rural and regional areas. However, there are several reasons why the impacts may impose higher costs in country Australia.

With respect to employment, the NCP could cause a wide range of impacts, however, its contribution may be difficult to detect due to the array of other shifts occurring both cyclically and structurally in the rural economy and socially. Areas where reforms are concentrated or which do not have a diverse economic base could suffer higher employment losses in the short term if the reforms have a negative impact, eg. if the result is a contraction of a major industry. However, even where the initial employment impacts are negative, employment prospects should improve in the longer term.

Social welfare and equity could also be affected by NCP reforms. For instance, the price of some services that are sensitive to distance, eg. electricity, may increase. With respect to water, the requirement for prices to reflect the full economic cost of supply and the elimination of subsidies means that rural water users will pay higher prices for water. However, the impact expected to result from price rises will be offset to some extent through the implementation of other elements of the framework aimed at improving water use efficiency, such as changes to institutional

arrangements. Due to rationalisations of services (which could be a result of the NCP or due to other changes, such as commercial decisions and population movements) their availability may be only at some distance. This means that rural communities may incur greater costs in using services than their metropolitan counterparts, for example, by the need to travel to a large regional centre.

The NCP could also result in social dislocation through the restructuring in some portfolio industries. The NCP has the potential to affect the inter-relationship of small rural communities, large rural centres and metropolitan centres, eg. through reducing cross subsidies. The result is that the community as a whole is less interdependent and less cohesive. By reducing cross-subsidies, the NCP could create pressure for economic and social adjustment. Reduced economic activity and services can become self-reinforcing through loss of scale, loss of function and perceptions of decline. AFFA believes that the reduction in the cohesiveness of rural communities should be factored into the costs of the NCP reforms, with due regard to the heavier social costs that are likely to be imposed on these areas as a result of the NCP reforms. In particular, direct consultation with rural communities should occur and adverse social welfare and equity effects should be dealt with directly by governments. A specific issue for further research is whether the competitive impacts of reforms further down the supply chain should be examined to ensure that the benefits of reform are shared equitably.

Reforms to the infrastructure industries will go a long way to improving the environmental outcomes for Australia, eg. the use of gas rather than coal, electricity market rules accounting for environmentally responsible fuel and energy management options (such as renewable energy), and water reforms resulting in sustainability of use.

Measures to facilitate the flow of benefits to country Australia

On the basis that there will be a net benefit to the whole Australian community over time, the NCP approach should continue. The pace of implementation is bound to be uneven across sectors and jurisdictions. There will be different short and long term effects for different sectors of the community, and different places. There are several measures needed.

The NCP should be administered with sensitivity to the possible short term dislocation effects and differential impacts. The current doubts and confusion reinforce the need for willingness to apply the public interest test positively as part of a transition process, to avoid implementation scenarios that result in long term beneficial changes for all Australians at high cost to some segments of the economy. To avoid this, the public benefit test should cover all possible options to ensure that the best alternative is chosen. The public benefit test should explicitly include an assessment of the temporal, spatial and cumulative effects of the reforms. In particular, the adjustment costs and the flow-on impacts of reform in other industries and regions should be clearly highlighted in the public benefit test. Consultation with rural communities that are likely to be directly affected by particular reforms should be a requirement of the public interest test. Government programs, at all levels of government and covering all agencies, should be considered as part of the public benefit test, in terms of the costs and benefits of reforms and whether the programs will effectively meet any adjustment costs.

The risk of negative impacts for country Australia from implementation, review and development of the NCP would be reduced if, at the same time, efforts are made to address the following key issues which would assist country Australia to become more resilient in the face of changes:

- the need for effective information services to address failures in information markets and to provide a basis for best practice decision making;
- the need for access to telecommunication services at the standard taken for granted in metropolitan areas;

- the requirement for education and reskilling to allow individuals and businesses to cope with the modern business and operating environment;
- improved market responsiveness and increased uptake of new technology and business practices to respond to the imperatives of globalisation and best practice, including attracting investment in appropriate infrastructure;
- the requirement for new skills in self management to assist individuals to cope with new business, family and social pressures; and
- the need for support and facilitation to assist communities to realise their potential and take responsibility for their own well-being.

AFFA believes that there are strong social reasons why essential or important services should be subsidised for rural and regional communities. This should optimally be done through Community Service Obligations (CSOs), transparently funded through government budgets. Also, governments should consider measures to assist industries to set up in rural areas, where there are impediments to this occurring. The development of new regional industries would assist in overcoming some of the costs of the implementation of NCP in some cases, as well as address changes arising from other causes.

One of the most important outcomes of this Inquiry will be an increase in our knowledge of the impacts of the NCP. We should also learn more about the extent to which different forces are affecting country Australia. AFFA believes that research on NCP and other effects should be increased, so that more sensitive and cost effective structural adjustment and transitional arrangements can be developed as needed. This will result in a greater capacity to predict changes and impacts on those most vulnerable, and to develop well tailored programs to smooth the way.

Conclusions

The submission's conclusions are as follows:

AFFA supports the continuation of the NCP as it allows portfolio industries to become relatively more efficient and competitive in overseas markets in the long term. However, the short term impacts on industries need careful management so that the longer term benefits are not put at risk.

AFFA sees merit in further study of the spatial, temporal and cumulative effects of the NCP reforms to better target any necessary adjustment initiatives.

AFFA believes that where competitive reforms are recommended, all benefits and costs which arise from the implementation of these reforms should be clearly identified and communicated to rural communities.

AFFA is of the view that the public benefit test provides some criteria against which to assess the net public benefit of restrictions on competition, although it is silent regarding weightings for each criteria, and that it provides transparency in decision making.

AFFA believes that, given the sensitivity of the NCP to rural communities, the public benefit test should explicitly include an assessment of all the effects of the reforms. In particular, the adjustment and social and community costs and the flow-on impacts of reform in other industries and regions should be clearly highlighted.

Rural communities, whether positively or negatively affected by particular reforms, should be consulted when assessing the costs and benefits.

AFFA believes that transitional arrangements would facilitate the speedy adoption of reforms without undue cost. Structural adjustment assistance would be useful in this regard. The

competition payments to the States and Territories provide an incentive to undertake reforms and should be used to provide structural adjustment assistance.

Measures to deal with costs that are incurred in rural communities indirectly as a result of the NCP reforms should be considered by government on a case by case basis.

Continual monitoring and review in relation to the impacts on portfolio industries will be desirable as the NCP and other policies are implemented, so that the likely gains can be realised without undue dislocation and hardship for the few.

Where reforms do not seem to have the expected benefits, a review should be undertaken to ascertain why this has not been the case and whether reforms further down the supply chain are needed to gain the full net public benefit from NCP reforms.

More effort should be applied to communicating with rural communities on the benefits of the NCP and to explaining the differences between the NCP and other independent policies/developments.

AFFA supports the use of transparently funded CSOs to provide support for essential or important services that increase in price as a result of the NCP (and other) reforms.