



# PC update

No 43 | April 2009 | [www.pc.gov.au](http://www.pc.gov.au)



## Feature

### Promoting better environmental outcomes



## Other Highlights

- ▶ **Report on Government Services**  
Measuring the performance of governments
- ▶ **Australia's productivity growth**  
What has happened to productivity growth and why?
- ▶ **Evidence-based policy**  
What is it? How do we get it?



## Contents

---

|  |    |
|--|----|
| <b>Promoting better environmental outcomes</b>                       | 3  |
| <b>Australia's gambling industries</b>                               | 7  |
| <b>Report on Government Services</b>                                 | 8  |
| <b>What has happened to Australia's productivity growth and why?</b> | 10 |
| <b>Evidence-based policy making</b>                                  | 12 |
| <b>Parallel importation of books</b>                                 | 14 |
| <b>Commission news</b>   | 15 |
| <b>Current commissioned projects</b>                                 | 16 |

---

The Productivity Commission is the Australian Government's independent research and advisory body on a range of economic, social and environmental issues affecting the welfare of Australians.



## Australian Government Productivity Commission

|                                      |   |
|--------------------------------------|---|
| <b>Chairman</b>                      | Gary Banks AO   |
| <b>Deputy Chairman</b>               | Mike Woods  |
| <b>Commissioners</b>                 | Neil Byron<br>Robert Fitzgerald AM<br>Steven Kates<br>Angela MacRae<br>Judith Sloan<br>Louise Sylvan<br>Philip Weickhardt                                       |
| <b>Head of Office</b>                | Bernard Wonder  |
| <b>First Assistant Commissioners</b> | Michael Kirby (Melbourne)<br>Terry O'Brien (Canberra)   |
| <b>Principal Advisers Research</b>   | Lisa Gropp (Melbourne)<br>Jenny Gordon (Canberra)   |
| <b>Media and Publications</b>        | Clair Angel (Media Director)<br>Ph: 02 6240 3239<br>maps@pc.gov.au  |
| <b>Melbourne Office</b>              | Locked Bag 2<br>Collins Street East<br>Melbourne VIC 8003<br><br>Level 28, 35 Collins Street<br>Melbourne VIC 3000<br><br>Ph: 03 9653 2100<br>Fax: 03 9653 2199 |
| <b>Canberra Office</b>               | PO Box 1428<br>Canberra City ACT 2601<br><br>Level 2, 15 Moore Street<br>Canberra City ACT 2600<br><br>Ph: 02 6240 3200<br>Fax: 02 6240 3399                    |
| <b>Website/Email</b>                 | www.pc.gov.au<br>webmaster@pc.gov.au  |

---

Requests to be placed on the mailing list for PC Update are welcome. Contact the Media and Publications Unit (03 9653 2244 or email maps@pc.gov.au). Copies are also available on the Commission's website.

# Promoting better environmental outcomes: Productivity Commission roundtable

**Relying on prescriptive regulations to solve environmental problems can generate high costs without necessarily achieving the desired outcomes. Market-based policy instruments offer an alternative approach, but must be well designed to ensure net community benefits, according to roundtable participants.**

Under what conditions can governments improve environmental outcomes? What form should policy intervention take to ensure effective and efficient results? These questions were the subject of a roundtable, 'Promoting Better Environmental Outcomes', convened by the Productivity Commission in late 2008. Keynote addresses were presented by Professor Gary Libecap from the University of California, and Professor Robert Stavins from Harvard University.

## How effective are existing approaches?

Governments can use a variety of policy instruments to address environmental challenges. Prescriptive regulations have tended to dominate policy responses, but there is growing recognition of the role that markets and market-based instruments can play in improving environmental outcomes.

### Promoting better environmental outcomes: key messages

- Government intervention to solve environmental problems can be justified in cases of significant market failure – but the form of the intervention is important to ensure that the objectives are achieved and the benefits outweigh the costs.
- Policies should have a strong evidence base, and clearly stated objectives.
- In general, market-based policy approaches are preferable to prescriptive regulation, which can be costly, inflexible and subject to industry capture.
- Market-based instruments are more likely to provide appropriate incentives for responding to environmental problems, but unless they are well designed, can also be costly and have significant redistributive effects.
- Policies should be subject to regular scrutiny to ensure that their stated objectives are met, and that the costs do not outweigh the benefits.
- Equity concerns are best addressed through adjustment support policies, rather than through constraints on market-based policy instruments.



There are advantages and disadvantages with each form of intervention. The optimal choice of policy instrument will depend on the nature of the problem and the available information. As Professor John Freebairn (University of Melbourne) said in his presentation to the roundtable:

---

**'A mixture of markets and government intervention ... will be required ... When government intervention is likely to improve upon market decisions, then in most cases market-based instruments such as taxes and tradeable permits offer more cost-effective ways of changing allocations and investments ...'**

---

## Prescriptive regulation often incurs excessive costs and may not achieve objectives

Governments have a natural tendency to adopt regulatory 'command and control' approaches. Several Commission inquiries have highlighted the costs of poorly designed regulatory responses to environmental problems in Australia.

The Commission's inquiry into the impacts of **native vegetation and biodiversity** regulations found that existing regulatory approaches are not fully effective while imposing significant costs; similarly the inquiry into **historic heritage** concluded that because heritage regulation does not sufficiently account for the costs of conservation, it can have perverse effects.

In an inquiry report into **energy efficiency**, the Commission argued that although government intervention to overcome failures in markets for energy efficiency technologies may be warranted, a light-handed regulatory response is likely to be preferable to more prescriptive and intrusive approaches.

Another Commission inquiry report found that state and territory **waste management** policies contain many inappropriate and inconsistent objectives, resulting in some unrealistic, and potentially costly, waste minimisation targets.

The Commission's report on **water quality** in the Great Barrier Reef catchment argued that existing water quality policies, based largely on prescriptive controls, should be replaced with measures tailored to particular land uses, locations, and pollutants, providing land users with the flexibility to choose abatement actions best suited to their property.

## Prescriptive regulations can be ineffective as well as costly

Professor Libecap noted that prescriptive regulation of inputs and/or outputs to solve environmental problems has a number of disadvantages including high costs, inflexibility, ineffectiveness, and industry capture. Importantly, regulatory decisions take place in the absence of information about alternative uses that market trading can generate.

Once in place, state regulations can create political constituencies which mould regulatory policy to suit their interests, with inflexible and inefficient outcomes. Professor Libecap commented that the US experience with many central regulatory regimes has not been satisfactory: fisheries continue to be depleted; air pollution abatement targets have not been achieved; and water has not been managed effectively.

## Market-based instruments have advantages but are difficult to implement

Attention has now shifted to the assignment of property rights and market mechanisms to solve environmental problems. Potential advantages of market-based instruments (MBIs) include flexibility, least-cost abatement, information generation, and better alignment of incentives for conservation or investment in the resource. Costs include information and input requirements in defining, allocating, measuring and enforcing property rights.

MBIs are being used increasingly for environmental management (including in Australia), but not all of these instruments have been well directed, appropriately designed or effectively implemented, leading in some cases to limited environmental gains and high regulatory costs. Professor Libecap cautioned:

---

**'Despite the attractions of property rights, they remain controversial, limiting or slowing their adoption. They generally are adopted only late, after conditions have deteriorated for many regulated resources. Allocation is one of the most controversial aspects because of the distributional implications involved in moving from open access or central regulation to a property regime.'**

---

Recognising the costs of property rights regimes, Professor Libecap argued that when the value of the resource or the cost of the externality is relatively low, prescriptive regulation can be a more cost-effective and politically acceptable option. However, Suzi Kerr (Moto Economic and Public Policy Research, New Zealand) outlined the advantages of the early introduction of markets in the case of New Zealand fisheries – in particular, that simple and efficient processes could be introduced with little political conflict. In contrast, US fisheries were facing significant adjustment issues with very entrenched local communities.

Professor Libecap warned that property rights are often controversial because they can have significant re-distributive effects. How property rights regimes are implemented – especially any compensation arrangements – will also affect their efficacy in addressing environmental problems.

## Institutional design is crucial

The effectiveness of both international and national institutional arrangements for responding to environmental issues was discussed by roundtable participants.

### Formulating international climate architecture

Professor Stavins examined the challenges of designing a successor to the Kyoto Protocol. According to Stavins:

---

**'... meaningful reductions of carbon dioxide and other greenhouse gas emissions will be very costly ... In the United States it will be approximately equivalent to the cost of complying with all other federal environmental regulations combined. And that is just for the relatively modest, short-term targets of the Kyoto Protocol ... This does not mean that it is a bad idea to take action, but it does mean that the costs should be recognized if governments are to design meaningful policies that will be environmentally effective, economically sensible, and politically feasible.'**

---

Professor Stavins described three potential approaches to developing a post-Kyoto policy architecture:

- international agreement (addressing some of the weaknesses of the Kyoto Protocol) based on country-level quantitative emissions targets established over specified time frames
- harmonised domestic policies, focusing more on national policy action than on goals – for example, harmonised national carbon taxes
- coordinated and unilateral national policies – a bottom-up approach relying on domestic politics to drive incentives for participation and compliance.

Professor Stavins argued that the third approach – such as linking independent national and regional tradeable permit systems – could be effective, and may be evolving spontaneously. This contrasts with the centralised, targets-and-timetables approach typically thought of as the

successor to the Kyoto Protocol. However, he stressed that the key questions were what architecture and what circumstances will bring China and other key developing countries into the coalition of action.

### Designing a national emissions trading scheme

In his presentation to the roundtable, Henry Ergas (Concept Economics) commented on the design of the proposed Carbon Pollution Reduction Scheme to be introduced by the Australian Government in July 2010. Under the scheme, revenues from the sale of pollution permits will be used to help households and businesses adjust to the impact of the introduction of carbon pricing, and for the promotion of 'clean energy', including for investment in low emissions R&D.

Henry Ergas questioned the usefulness of such revenue earmarking. He argued that while hypothecation can have some beneficial effects, it can also reduce efficiency in public expenditures. Ergas argued that, at least from an aggregate welfare point of view, revenue earmarking proposed in the Carbon Pollution Reduction Scheme is unlikely to increase the quality of public expenditures.

Echoing Professor Libecap's remarks, Henry Ergas also cautioned that earmarking revenue for specific purposes could build a constituency of beneficiaries with a vested interest in the continued operation of the scheme regardless of its overall effectiveness. He said a better approach would be to use the revenues from the scheme to reduce distorting tax rates – for example, by flattening the structure of personal income tax.

### Implementing policy across multiple jurisdictions

The challenges of implementing policy requiring coordination across multiple jurisdictions was discussed in a presentation to the roundtable by Murray-Darling Basin Chief Executive, Wendy Craik. While decision making requiring the agreement of multiple parties can be time-consuming and resource intensive, Dr Craik identified a number of potential success factors. These included: achieving active agreement from all implementing parties (to avoid passive non-implementation); setting clear objectives and targets – and reporting against them; and establishing clear roles and responsibilities for partner governments including for funding arrangements, so all have a stake in the outcomes. ►

## What are the implications for public policy?

Summarising the lessons emerging from the roundtable discussion, Professor Geoffrey Brennan (Australian National University) said environmental issues could be divided into two categories: those that are primarily global in nature (such as climate change and greenhouse gas issues) and those that are national or sub-national (such as water extraction in the Murray–Darling Basin).

According to Professor Brennan, unilateral policy action in response to global issues is unlikely to be effective. Australian policy to reduce carbon emissions will only have a proportionate effect on Australia's climate if all other countries impose the same reduction in emissions. Issues such as whether carbon taxes, cap-and-trade systems or a hybrid of the two, represent the best policy mechanism only become relevant when the cooperation of all nations in reducing emissions is secured. In contrast, governments are able to implement effective policy responses to domestic environmental issues. Moreover, resources deployed by the Australian government for tackling global warming are resources that could otherwise be used for tackling national environmental problems (such as water buy back).

### Assessing the efficiency and effectiveness of policy options

Over the past decade, the Commission has undertaken inquiries, prepared submissions and pursued its own research on a range of environmental policy topics. The focus has been on the efficiency and effectiveness of different policy options. Recent Commission reports on environmental issues include:

*Towards urban water reform (2008)*

*The Stern Review: an assessment of its methodology (2008)*

*Submission on emissions trading (2007)*

*Waste management (2006)*

*Rural water use and the environment (2006)*

*Conservation of historic heritage (2006)*

*The private cost effectiveness of improving energy efficiency (2005)*

*Impact of native vegetation and biodiversity regulations (2004)*

*Water quality in the Great Barrier Reef (2003)*

### Challenges of implementing a water market: the Murray–Darling Basin

In her presentation, Dr Arlene Buchan (Australian Conservation Foundation) discussed the policy challenges of improving environmental outcomes in the Murray–Darling Basin. Over-allocation of water for irrigation purposes, exacerbated by ongoing drought, has resulted in significant environmental deterioration throughout the Basin. Improving environmental outcomes will require the reallocation of a substantial amount of water from irrigation back to the environment.

In 2004, COAG agreed to the National Water Initiative (NWI) – a commitment by governments to achieve a nationally compatible market, regulatory and planning system for managing Australia's water resources. According to Dr Buchan, 'the NWI failed to drive change at the scale and pace required ... A focus on investing money in water infrastructure and on-farm efficiencies resulted in very slow progress in water recovery'.

In 2007, the National Plan for Water Security was announced, with the aim of enhancing the NWI and providing increased funding to drive reform. In 2008 the Water for the Future Plan was implemented to prepare for the impact of climate change on Australia's water supplies. The Plan included the 'Restoring the balance program' to purchase water entitlements for the environment.

Dr Buchan argued that because the NWI currently sets a cap on the amount of water that can be permanently traded out of irrigation areas, water reallocation is constrained. Moreover, there is a 'huge information gap' about the hydrological needs of the environmental assets of the Basin. 'A first priority is ... to address this, so that water recovery can be tailored to provide water with the characteristics to meet ecological needs', she said.

Hence, he considered that Australian policy should focus on domestic environmental problems. On the global front he felt that resources would be better focused on adapting to the fact of global warming rather than on potentially ineffective attempts to prevent it. ■

### Promoting Better Environmental Outcomes

Productivity Commission Roundtable Proceedings

Released March 2009

## New public inquiry

# Australia's gambling industries

**This public inquiry will look again at a range of matters covered in the Commission's 1999 review of the gambling industry, as well as examining the impact of harm minimisation strategies, and recommending policy and regulatory improvements.**

As well as considering a broad range of social and economic issues related to gambling, the Commission has been asked specifically to look at the impacts of measures aimed at reducing some of the adverse effects of gambling ('harm minimisation').

### Some key findings from the Commission's 1999 report

- Gambling provides enjoyment to most Australians, over 80 per cent of whom gambled in the last year — spending about \$11 billion — with 40 per cent gambling regularly.
- Gambling is a big and rapidly growing business in Australia, with the industries accounting for an estimated 1.5 per cent of GDP.
- The main benefit from the liberalisation of gambling has been consumer gains from access to a service that gives people enjoyment. Net gains in jobs and economic activity have been small.
- Around 130 000 Australians (about 1 per cent of the adult population) are estimated to have severe *gambling* problems, and a further 160 000 adults are estimated to have *moderate* problems. Taken together, 'problem gamblers' represent just over 2 per cent of Australian adults.
- The prevalence of problem gambling is related to the degree of accessibility of gambling, particularly gaming machines.
- Policy approaches for the gambling industries need to be directed at reducing the costs of problem gambling — through harm minimisation and prevention measures — while retaining as much of the benefit to recreational gamblers as possible.

Productivity Commission 1999, *Australia's Gambling Industries*

The Commission released an issues paper in December 2008, which outlined the key questions the inquiry will seek to answer. These include:

- What are the policy challenges associated with internet gambling?
- What factors explain trends in gambling expenditure, particularly gaming machine expenditure, since 1999?

- Have the nature and extent of the costs of problem gambling on individuals, their families and the wider community changed since 1999?
- Have measures aimed at protecting consumers been effective and what new initiatives should be considered?

The inquiry stems from a COAG decision in 2008 and is intended to provide policy recommendations on gambling for consideration by all Australian jurisdictions. Public submissions are due by 31 March. A draft report will be released for public comment in September and a final report will be sent to the Australian Government in November 2009 for consideration by COAG. ■

## Gambling

Productivity Commission Issues Paper released December 2008

Contact: Monika Binder 02 6240 3238  
mbinder@pc.gov.au



# Report on Government Services

The 2009 Report on Government Services, released in January, provides a wealth of information on the performance of government services across Australian jurisdictions.

The 2009 issue is the fourteenth edition of the Report on Government Services. The Report is produced by a Steering Committee of senior officials from Australian, State and Territory governments for the Council of Australian Governments (COAG). The Steering Committee is chaired by Gary Banks, Chairman of the Productivity Commission.

The Report, which presents information on the efficiency and effectiveness of government services in Australia, covers six broad service areas: education, justice, emergency management, health, community services and housing. Service areas covered in the Report accounted for \$132 billion in government expenditure — almost 13 per cent of Australia's gross domestic product.

The Report helps to improve the performance of government by:

- enhancing measurement approaches and techniques in relation to aspects of performance, such as unit costs and service quality
- helping jurisdictions identify where there is scope for improvement
- promoting greater transparency and informed debate about comparative performance across jurisdictions.

The 2009 Report contains a number of improvements, including:

- a revised ambulance performance indicator framework
- reporting for the first time on: hospital readmissions and community follow up after an episode of mental illness; maintenance of individual functioning from the Transition Care Program for aged care; response times for child protection services; and school attendance data for students in years 1 through 10.

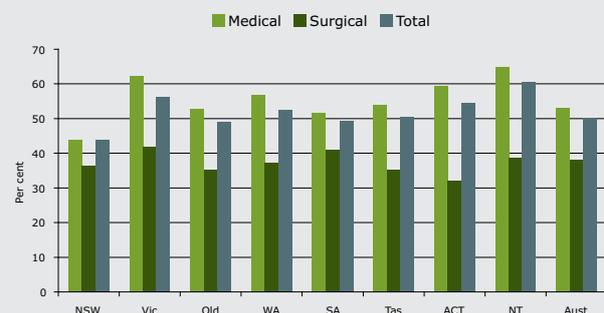
## Services to Indigenous Australians

The Report presents a variety of data on services to Indigenous Australians. New indicators in the 2009 Report include:

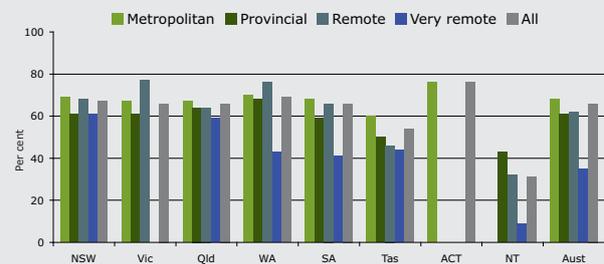
- school learning outcomes for Indigenous students by remoteness area for each State and Territory
- data for Indigenous preschool attendance
- age standardised imprisonment rates for Indigenous and non-Indigenous prisoners
- improved reporting of Indigenous hospitalisations data.

## Report on Government Services 2009 – Sample indicators

**Proportion of medical, surgical and total separations that were same day, public (non-psychiatric) hospitals 2006-07**

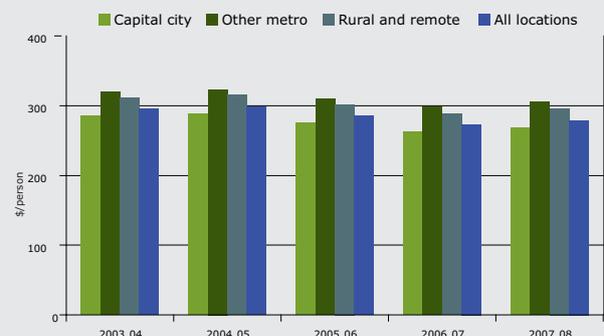


**School completion rates, year 12, by geolocation, 2007**



The data included in this figure are not complete or not directly comparable

**PBS expenditure per person, by urban and rural location, 2007-08 dollars**



Source: Data, sources and caveats for these figures are available from the website for the Review of Government Service Provision [www.pc.gov.au/gsp/reports/rogs/2009](http://www.pc.gov.au/gsp/reports/rogs/2009)

## Services to Indigenous Australians: selected statistics

### School education

- The proportion of Indigenous students achieving national benchmarks in years 3, 5 and 7 reading, writing and numeracy was lower than for all students almost without exception in 2007.
- Indigenous students are, on average, less likely to stay at school through secondary education – in 2007, the Indigenous retention rate from year 10 to year 12 was 48.5 per cent, compared to 75.6 per cent for all students.

### Health

- In 2002–06 overall rates of mortality for Indigenous people in Queensland, WA, SA and the NT combined were almost three times as high as rates for non-Indigenous people.
- Indigenous infant mortality rates in 2004–06 were markedly higher than for all Australian infants in those jurisdictions for which data are available.

### Housing

- Nationally, 57 per cent of Indigenous and 72 per cent of non-Indigenous public housing tenants were either satisfied or very satisfied with the overall service provided by their state housing authority in 2007.

### Corrective services

- Indigenous people were far more likely to be in prison custody in 2007-08 than non-Indigenous people – after adjusting for the different age structures of the populations, 2156 out of every 100 000 Indigenous adults were imprisoned, compared to 123 out of every 100 000 non-Indigenous adults. However, almost three quarters of all prisoners are non-Indigenous.

## Services covered in the 2009 Report on Government Services

### Early childhood, education and training

- Children's services
- School education
- Vocational education and training

### Health

- Public hospitals
- Primary and community health
- Breast cancer detection and management
- Mental health services

### Justice

- Police
- Court administration
- Corrective services

### Community services

- Aged care services
- Services for people with a disability
- Protection and support services

### Housing

- Public and community housing
- State-owned and managed Indigenous housing
- Commonwealth Rent Assistance

### Emergency management

- Fire and ambulance services

## The Government Services Review is under review

During 2008, COAG emphasised the importance of performance reporting in its reform of Specific Purpose Payments. New National Agreements (covering healthcare, education, skills and workforce development, affordable housing, disability and Indigenous reform) set out agreed objectives, outputs, outcomes and performance indicators, which will be monitored by the COAG Reform Council. The Steering Committee for the Review of Government Service Provision will provide relevant performance information to the Council. COAG has initiated a review to ensure the Report on Government Services is appropriately aligned with the National Agreements, and to examine improvements to the Report's scope and processes.

The Report on Government Services 2009 is available in hard copy, CD and on the Review's website <http://www.pc.gov.au/gsp>. Fact sheets, providing a summary of results from each of the service areas, are also available from the website. ■

## Report on Government Services 2009

Released January 2009

Contact: Lawrence McDonald 03 9653 2178 [lmcdonald@pc.gov.au](mailto:lmcdonald@pc.gov.au)

# What has happened to Australia's productivity growth and why?

The current economic challenges facing Australia lend urgency to policy efforts aimed at raising national productivity.

Recent trends in Australia's productivity performance are examined in the Commission's latest Annual Report.

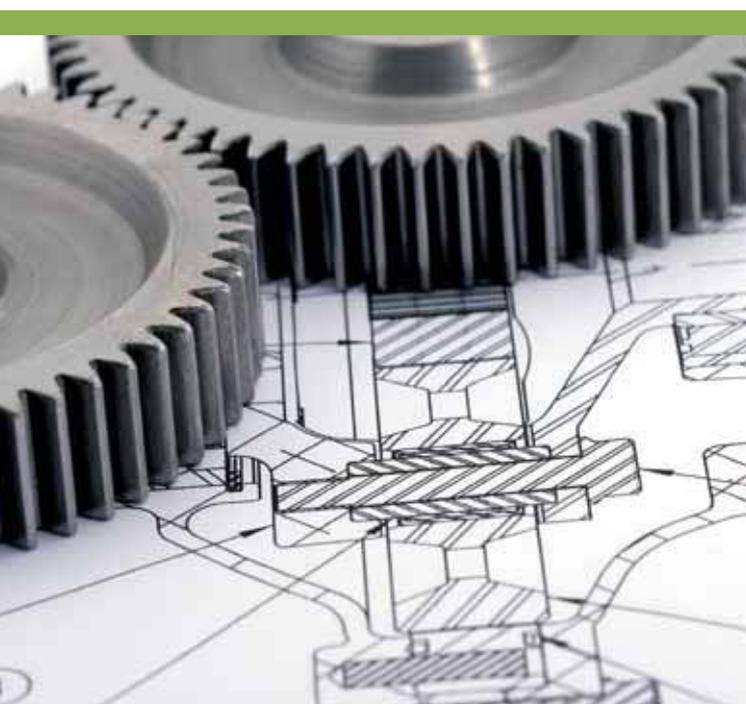
## Why is productivity important?

The ultimate objective of public policy is to improve the wellbeing of the community. While the concept of wellbeing has numerous dimensions, income growth and its distribution are central. Productivity growth contributes to growth in per capita income because it increases the outputs of goods and services produced per unit of physical input.

## Australia's productivity growth has slowed

Following a surge in productivity in the 1990s, Australia's productivity growth rate over the last decade has slowed to below the long-term average. Multifactor productivity (MFP) growth declined from 1.6 per cent over the 1990s to 0.6 per cent in the period since 2000.

**Slower productivity growth was the flip side of rising terms of trade and greater utilisation of labour and capital.**

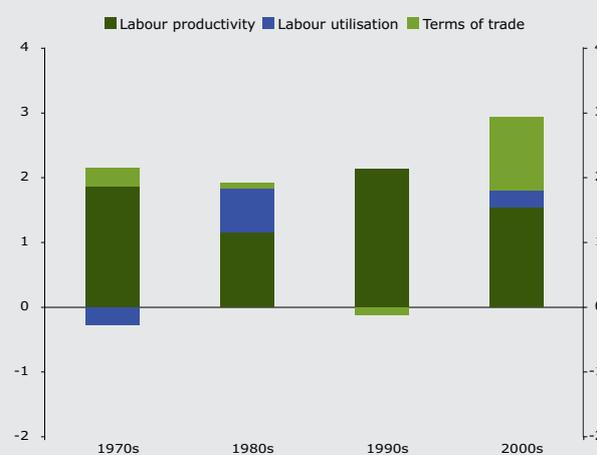


Strong growth in employment and investment, together with a rise in Australia's terms of trade, have generated significantly greater prosperity in recent years, despite the relatively weak productivity performance (figure 1). Compared with the 1990s, more effort seems to have gone into expanding production through investment and new hiring, rather than cost cutting.

While productivity growth in all sectors has slowed, the agricultural and mining sectors stand out, recording negative productivity growth over the period since 2000. These industries explain more than half of the fall in Australia's productivity growth below the long-term average growth rate (figure 2).

**Figure 1 Sources of income growth**

Contributions to annual average growth in real gross domestic income per capita, percentage points per year



Data source: Commission calculations.

**Figure 2 Multifactor productivity**



1999-2000 = 100

Data source: Commission calculations.

## Why has mining productivity declined?

The mining industry has contributed significantly to Australia's recent prosperity – with favourable terms of trade over the period 2003-04 to 2006-07 contributing to increased incomes – but productivity in the sector has fallen markedly. According to Australian Bureau of Statistics estimates, MFP in the mining sector declined by 24 per cent between 2000-01 and 2006-07.

A new Productivity Commission Staff Working Paper\* examined the reasons for this decline. The paper argued that conventional measures of productivity growth in the sector should be interpreted carefully for two reasons.

### Resource depletion effects

Resource deposits are non-renewable, and depleted by ongoing extraction. As deposits are depleted, the quality and accessibility of remaining reserves generally decline. This typically results in the need for increased inputs of capital and labour per unit of output, and therefore acts as a drag on conventionally measured MFP. The Commission paper estimated that, over the last three decades, with resource depletion effects removed, MFP in mining grew at an average rate of 2.5 per cent per year, compared with 0.01 per cent per year as conventionally measured.

### Long investment lead times

Evidence indicates that there is a delay of approximately three years between initial investment in new mining projects and full output capacity. Since new investment is generally recorded immediately as an increase in capital inputs, a surge in investment in mining can have a temporary negative effect on MFP. Short-term movements in MFP may therefore reflect changes in investment patterns, rather than the fundamental efficiency with which inputs are combined to produce outputs.

### Growth in underlying MFP

According to the paper's authors, the effects of resource depletion and long investment lead times explain a large amount of the variability in mining MFP. The authors estimated that after removing the influence of these factors, other factors (such as technological improvements in production efficiency and improved management techniques) raised MFP by 8 per cent over the period 2000-01 to 2006-07.

\* Topp, V., Soames, L., Parham, D. and Bloch, H. 2008, *Productivity in the Mining Industry: Measurement and Interpretation*, Productivity Commission Staff Working Paper

The electricity, gas and water supply sector has also detracted heavily from measured productivity. The reforms of the mid-1980s drove rapid productivity growth in the sector over the 1990s, but a 20 per cent fall in productivity during the current decade subtracted 0.7 percentage points from market sector MFP. As the benefits of earlier reforms in utilities are reflected mainly in higher underlying productivity *levels*, productivity *growth* could reasonably be expected to slow, but the reason for the significant decline is unclear.

## Innovation is the key to long-term productivity growth

The current economic challenges confronting Australia lend urgency to policy efforts to raise national productivity.

Innovation is the key to achieving this. Sustaining and advancing reforms to enhance market competition and to reduce regulatory constraints on enterprise flexibility remain fundamental to stimulating innovation, and should continue to play a central policy role.

There is also an important role for government in building human capital and supporting R&D where the knowledge will be made generally available. Program design is crucial, however, and the Review of the National Innovation System's emphasis on sound cost-benefit evaluation of programs to support innovation, is well founded. ■

**Productivity Commission  
Annual Report 2007-08**

Released October 2008

## Evidence-based policy making

**What is evidence-based policy making? How can it contribute to better policy outcomes? Productivity Commission Chairman Gary Banks addressed these questions in a recent speech to the Australian and New Zealand School of Government. An edited extract of his speech follows.**

Addressing senior public servants in April last year, the Prime Minister observed that ‘evidence-based policy making is at the heart of being a reformist government’. Tonight I want to explore why that is profoundly true; what it means in practice, and some implications for those of us in public administration. In doing so, I will draw on the experience of the Productivity Commission – which with its predecessors has been at the heart of evidence-based policy making in Australia for over three decades – to distil some insights into what is needed across government generally if we are to be successful.



Gary Banks, Chairman, Productivity Commission  
© Newspix/Stuart Mcevoy

Policy decisions will typically be influenced by much more than objective evidence, or rational analysis. Values, interests, personalities, timing, circumstance and happenstance – in short, democracy – determine what actually happens. But evidence and analysis can nevertheless play a useful, even decisive, role in informing policy-makers’ judgements. Importantly, they can also condition the political environment in which those judgements need to be made.

### Most policies are experiments

Without evidence, policy makers must fall back on intuition, ideology, or conventional wisdom – or, at best, theory alone. But the resulting policies can go seriously astray. A few examples from recent Productivity Commission reviews come readily to mind:

- in our research for COAG on the economic implications of Australia’s ageing population, we demonstrated that common policy prescriptions to increase immigration, or raise the birth rate, would have little impact on the demographic profile or its fiscal consequences (indeed, higher fertility would initially exacerbate fiscal pressures);
- our report into road and rail infrastructure pricing showed that the presumption that road use was systematically subsidised relative to rail was not borne out by the facts;
- in our inquiry into waste management policy, we found that the objective of zero solid waste was not only economically costly, but environmentally unsound;
- our recent study on Australia’s innovation system reaffirmed that, contrary to conventional opinion, the general tax concession for R&D mainly acted as a ‘reward’ for research that firms would have performed anyway, rather than prompting much additional R&D.

Among other things, policies that haven’t been informed by good evidence and analysis fall more easily prey to the ‘Law of Unintended Consequences’ – in popular parlance, Murphy’s Law — which can lead to costly mistakes. For example, the Commission found, in a series of reviews, that the well-intentioned regulatory frameworks devised to protect native flora and fauna, and to conserve historic buildings, were actually undermining conservation goals by creating perverse incentives for those responsible.

I am not saying that policy should never proceed without rigorous evidence. Often you can't get sufficiently good evidence, particularly when decisions must be made quickly. And you can never have *certainty* in public policy. All policy effectively is experimentation. But that does not mean flying blind – we still need a good rationale or a good theory.

## The essential ingredients

For evidence to support good public policy, however, it needs to be the right evidence; it needs to occur at the right time and be seen by the right people. That may sound obvious, but it is actually very demanding. The essential ingredients in achieving that are:

- use of appropriate methodology
- availability of good data
- transparency – real evidence is open to scrutiny
- recognition that evidence-building takes time
- capability and expertise, especially in quantitative methods and other analytical and evaluation techniques
- analytical independence
- a policy-making environment that is actually receptive to evidence.

## Implications for the Public Service

Some observations follow about how those of us in the Public Service can advance evidence-based policy making.

- *Make better use of existing vehicles and frameworks within government* – the recently upgraded regulation assessment requirements are ready-made for that purpose. There is also scope to enhance some of the requirements for spending programs, particularly strengthening ex ante evaluation and ex post review.
- *Establish effective COAG arrangements*, including an appropriate balance between frequency of meetings and the time needed to gather the evidence required for informed decision making.
- *Build greater institutional capacity* – recruit into the Public Service more graduates in the social and economic sciences; develop a 'research culture'; and promote 'institution-building'.
- *Make better use of external contracting* – give greater attention to defining the task and identifying how contractors can best contribute. Getting the right consultant for the task is fundamental.

- *Resource evaluations properly* – ensure that all government programs are designed and funded with future evaluation and review in mind, including data needs. And building in more time, where it is needed to come up with robust evidence that is adequately tested.

## The bottom line

The goal of evidence-based policy-making is unquestionably important. However, measured against the various ingredients for an effective approach, it seems clear that current practice continues to fall short. Addressing this is now largely up to the Public Service. If we fail, it will compromise government's capacity to implement the beneficial reforms this country needs for the long term. ■

## Evidence-based policy and tariffs

'Evidence-based policy making is by no means new to this country. Probably the oldest example, or longest-standing one, would be tariff-making, which for many years was required under legislation to be informed by a public report produced by the Tariff Board and its successor organisations (notably the IAC). The nature of those evidence-based reports changed dramatically over time, however, from merely reporting the impacts on industries under review to also reporting the effects on other industries and the wider economy ...

The tariff story illustrates the crucial point that the contribution of an evidence-based approach depends on its context, and the objectives to which it is directed. Evidence that is directed at supporting narrow objectives – a particular group or sector, or fostering use of a particular product or technology – will generally look quite different to that which has as its objective the best interests of the general community.'

### Evidence-based policy-making: What is it? How do we get it?

Speech by Gary Banks AO, Chairman, Productivity Commission, to the Australian & New Zealand School of Government, Canberra, 4 February 2009

The full version of the speech can be downloaded from the Commission's website [www.pc.gov.au](http://www.pc.gov.au)

## Parallel imports of books

**In a draft report, the Commission has proposed a reduction in the period of protection for Australian publishers from the parallel importation of books.**

Australia has a diverse literary sector and a healthy consumer market for books of all styles and genres. New book sales in Australia are around \$2.5 billion annually, covering both the education and general reading markets. Parallel importation restrictions prevent Australian booksellers from importing commercial quantities of legitimately produced copies of a book from overseas, when a publisher with 'Australian rights' can supply the title.

### Weighing up the costs and benefits

While previous changes to the parallel import restrictions have addressed concerns about the timely availability of books in Australia, the Commission found that the restrictions put upward pressure on book prices in some segments of the market, to the detriment of consumers.

### The debate about parallel import restrictions

Some booksellers argue that the restrictions prevent them from accessing potentially cheaper or better-value editions of books and passing those benefits on to consumers.

Publishers and authors contend that the restrictions are necessary to support investment in Australian books. If the restrictions were removed, they argue, Australian publishing activity would be less viable, resulting in fewer Australian books being released, a contraction in local printing activity and a reduction in the cultural benefits to the community from books.

In addition, it found that Australian authored books can have a significant cultural value, although much of this value is enjoyed (and paid for) by book buyers. There are also some additional 'unpriced' cultural benefits to the wider community, but the restrictions are not a particularly efficient or effective means of targeting these benefits. This is partly because much of the support to copyright holders provided by these restrictions goes off-shore, to foreign authors and publishers.

While there are therefore some persuasive arguments for abolishing the restrictions, there is also considerable uncertainty about how the industry would adjust and the extent of the price benefits for consumers. Accordingly, the Commission's main draft proposal is for a reduction in the period of parallel import protection to 12 months following a book's release. This should maintain some investment certainty for publishers to market and distribute new books, while potentially allowing competitive editions of 'back list' titles into the Australian market, where price competition is currently less strong. The Commission is also proposing a further review of the restrictions in five years.

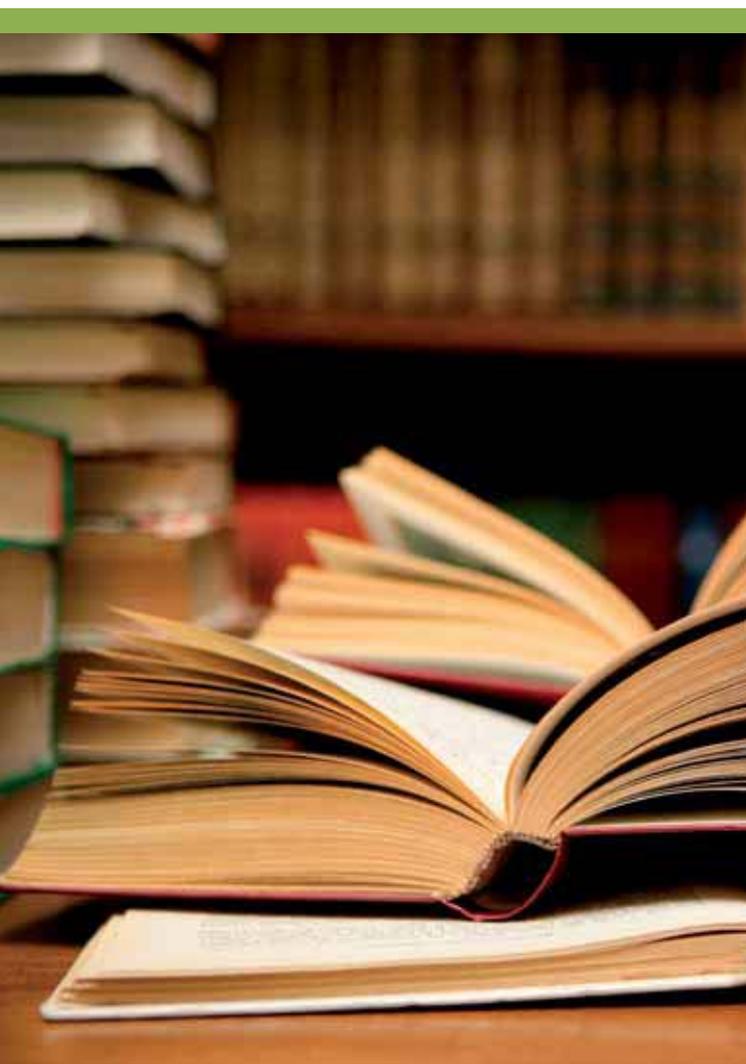
The Commission is due to deliver its final report to Government in May 2009. ■

### Copyright Restrictions on the Parallel Importation of Books

Draft report released March 2009

Contact: Andrew Irwin 02 6240 3350

Email: [books@pc.gov.au](mailto:books@pc.gov.au)



## Commission news

### New commissioned projects

#### Executive Remuneration in Australia

The Treasurer has asked the Productivity Commission to conduct a public inquiry into the regulatory framework around remuneration of directors and executives of companies regulated under the Corporations Act. A final report will be presented to Government in December 2009, with a draft report in September. Other key dates for the inquiry are posted on the Commission's website. Heading the inquiry are Productivity Commission Chairman Gary Banks (presiding), Commissioner Robert Fitzgerald and Prof Allan Fels from the Australian and New Zealand School of Government, who has been appointed as a part-time Associate Commissioner for the duration of the inquiry.

#### Contribution of the Not for Profit Sector

The Commission has commenced a research study into the contributions to Australian society of the not for profit sector. A draft report will be released in September and a final report will be submitted to Government in December 2009. Former Commonwealth Statistician, Dennis Trewin, has been appointed as an Associate Commissioner.

#### Australia's Anti-dumping and Countervailing System

The Commission has been asked to review the effectiveness and impact of Australia's anti-dumping and countervailing system. An issues paper will be released shortly, and a draft report is due end August/early September. The final report will be presented to Government by 23 December 2009.

### Recent releases

All publications can be downloaded from the Commission's website [www.pc.gov.au](http://www.pc.gov.au)

#### March 2009

*Restrictions on the Parallel Importation of Books* (Discussion Draft)  
*Promoting Better Environmental Outcomes* (Roundtable Proceedings)

*Investments in Intangible Assets and Australia's Productivity Growth* (Staff Working Paper)

*Public Infrastructure Financing: An International Perspective* (Staff Working Paper)

#### February 2009

*Review of Mutual Recognition Schemes* (Research Report)

#### January 2009

*Report on Government Services 2009 2 vols.*

*Chemicals and Plastics Regulation: Lessons for National Approaches to Regulation* (Supplement to Research Report)

#### December 2008

*Productivity in the Mining Industry: Measurement and Interpretation* (Staff Working Paper)

*Performance Benchmarking of Australian Business Regulation: Quantity and Quality, Performance Benchmarking of Australian Business Regulation: Cost of Business Registrations* (Research Reports)

*Review of Regulatory Burden on the Upstream Petroleum (Oil and Gas) Sector* (Draft Research Report)

### Review of Mutual Recognition Schemes

The Productivity Commission presented its Research Report 'Review of Mutual Recognition Schemes' to Australian Heads of Government and the New Zealand Prime Minister in early February 2009.

In its assessment of the two main mutual recognition schemes – the Mutual Recognition Agreement and the Trans-Tasman Mutual Recognition Arrangement – the Commission found that they brought benefits through increased mobility of labour and greater movement of

merchandise between jurisdictions. However, ambiguities and omissions in the legislation create frictions in the operation of the schemes. Moreover, a lack of awareness of mutual recognition means that businesses, individuals and regulators do not always use the schemes fully or appropriately.

The Commission recommended a suite of changes to mutual recognition arrangements to enable the schemes to reach their full potential.

#### Review of Mutual Recognition Schemes

Research Report released February 2009

## Current commissioned projects

Log on to the Commission's website ([www.pc.gov.au](http://www.pc.gov.au)) for full details of all current projects

### **Executive Remuneration in Australia – Public Inquiry**

Issues paper released April 2009. Draft report due September 2009. Public hearings schedule to be advised. Final report to be submitted to Government December 2009.

Contact: Alan Johnston Ph: 03 9653 2147 Email: [exec\\_remuneration@pc.gov.au](mailto:exec_remuneration@pc.gov.au)

### **Contribution of the Not for Profit Sector – Commissioned Study**

Issues paper released April 2009. Initial submissions due 30 May 2009. Draft report to be released early September 2009. Final report to Government December 2009.

Contact: Scott Austin Ph: 02 6240 3253 Email: [nfp@pc.gov.au](mailto:nfp@pc.gov.au)

### **Australia's Anti-dumping and Countervailing System – Public Inquiry**

Issues paper to be released mid April 2009. Draft report due end August/early September 2009. Final report to Government December 2009.

Contact: Alistair Davidson Ph: 02 6240 3210 Email: [antidumping@pc.gov.au](mailto:antidumping@pc.gov.au)

### **Gambling – Public Inquiry**

Issues paper released December 2008. Submissions due 31 March. Draft report to be released July/August 2009. Public hearings September/October 2009. Final report to Government 24 November 2009.

Contact: Monika Binder Ph: 02 6240 3238 Email: [gambling@pc.gov.au](mailto:gambling@pc.gov.au)

### **Review of Regulatory Burden on the Upstream Petroleum (Oil and Gas) Sector – Commissioned Study**

Draft report released November 2008. Final report to Government by 9 April 2009.

Contact: Kate Maddern 03 9653 2209 Email: [upstreampetroleum@pc.gov.au](mailto:upstreampetroleum@pc.gov.au)

### **Copyright Restrictions on the Parallel Importation of Books – Commissioned Study**

Draft report released March 2009. Final report to Government 13 May 2009.

Contact: Andrew Irwin 02 6240 3350 Email: [books@pc.gov.au](mailto:books@pc.gov.au)

### **Performance Benchmarking of Australian Business Regulation: OHS and Food Safety – Commissioned Study**

Circular released December 2008. Issues papers April 2009. Initial submissions due April/May 2009. Draft reports August/September 2009. Final reports to Government December 2009.

Contact: Sue Holmes 02 6240 3351 Email OHS: [ohs@pc.gov.au](mailto:ohs@pc.gov.au), Email Food Safety: [foodsafety@pc.gov.au](mailto:foodsafety@pc.gov.au)

### **Annual Review of Regulatory Burdens on Business – Commissioned Study**

The Commission is undertaking, over five years, a series of annual reviews of the burdens on business from the stock of Commonwealth regulation.

To be released in 2009: *Social and economic infrastructure services.*