
1 Introduction

Key points

- The latest drought has been severe and prolonged in many parts of Australia but such events are not new in the history of dryland farming. In contrast, the irrigation drought over the last three years in the Murray Darling Basin has been unprecedented. In the future, most expert predictions are that agricultural regions will experience increased temperatures and, for some, more frequent periods of very low rainfall.
- Drought policy has shifted from natural disaster management to a recognition that drought is a normal feature of Australia's climatic variability.
- Australian ministers for primary industries consider that current policy settings are no longer the most appropriate in the context of a changing climate. There are concerns about the extent of areas declared as being in exceptional circumstances and the duration of declarations in the latest drought period, and about the effectiveness and efficiency of current government programs in response.
- This inquiry is one of three studies contributing to a review of drought policy. The other two are a scientific assessment of the changing climate and its relevance to drought policy, and a report on the social and community impacts of drought by an expert panel.
- The Commission's report draws on the findings of these other two studies and addresses:
 - current business and income support measures
 - impediments to improving self-reliance and preparedness
 - the role that should be played by governments.

1.1 Drought policy — a continuing evolution

What constitutes a drought may seem readily apparent. But in fact it is difficult to disentangle a confluence of factors — for example: the quantity, location and timing of rainfall and runoff; temperature, evaporation and soil moisture; water storages and allocations; commodity prices and input costs; land values and equity levels; off-farm diversification and so on.

Drought is a recurring feature of Australia's variable climate. However, the latest drought has been one of the three most severe and prolonged in the last one hundred

years. For example, in relation to the Murray Darling Basin (MDB) the Bureau of Meteorology (BoM) considers that in terms of rainfall, ‘the post 2001 period, the 1937–1946 period and the 1895–1903 period (the “Federation Drought”) are essentially indistinguishable in broad terms’ (BoM 2008, p. 2).

Early last century, government drought policy centred on the construction of irrigation infrastructure in an attempt to ‘drought proof’ farms. Subsequently, a policy approach developed that saw drought treated as a natural disaster and in 1971, drought was incorporated under joint Commonwealth-State Natural Disaster Relief Arrangements (NDRA). In 1989, however, the Commonwealth decided to remove drought from the NDRA and commissioned a review of drought policy that found that drought support was poorly targeted and worked against farmers becoming self-reliant. The review recommended that a new national drought policy be developed (McInnes et al. 1990).

The National Drought Policy (NDP), announced in 1992, was based on the recognition of the recurrence of droughts in Australia. Farmers were expected to assume responsibility for managing drought risks, with the role of government being to provide an environment conducive to promoting self-reliance. Nevertheless, provision was made to assist those farmers with sound prospects who were temporarily experiencing financial difficulty during abnormally severe droughts. That is, the NDP made a distinction between normal droughts and ‘exceptional circumstances’ (EC) — rare events that do not occur more than once on average in every 20 to 25 years. That policy framework continues today (box 1.1).

However, subsequent policy reviews (*Review of the National Drought Policy* (Matthews et al. 1997), *Rural Adjustment – Managing Change* (McColl et al. 1997), *Consultations on National Drought Policy* (Drought Review Panel 2004), and *Creating our Future: Agriculture and Food Policy for the Next Generation* (Agriculture and Food Policy Reference Group 2006)) have all found that the actual drought assistance programs implemented by governments have been incompatible with the NDP objective of promoting farmers’ self-reliance.

Despite endeavours to establish a stable and credible foundation for drought policy, prolonged dry conditions have prompted various ad hoc changes to the design of the programs. For example, in response to the latest drought, new initiatives and modifications to existing measures have been introduced — including interim assistance arrangements, EC buffer zones, new forms of grants and transport subsidies. Some of these measures are only tenuously related to the agreed NDP objectives and others revisit approaches previously found wanting, such as the distortionary subsidies for the transport of fodder and livestock.

Box 1.1 The NDP and ‘exceptional circumstances’

The objectives of the NDP are to:

- encourage primary producers and other sections of rural Australia to adopt self-reliant approaches to managing for climatic variability
- maintain and protect Australia’s agricultural and environmental resource base during periods of extreme climate stress
- ensure early recovery of agricultural and rural industries, consistent with long-term sustainable levels. (Crean 1992)

While self-reliance is a key objective, the NDP allows for short term drought assistance where there are rare and severe drought events — exceptional circumstances (EC) — that are beyond the ability of even the most prudent farmer to manage.

To be classified as an EC event, the event:

- must be **rare**, that is, it must not have occurred more than once on average in every 20 to 25 years
- must result in a **rare** and **severe** downturn in farm income over a prolonged period of time (e.g. greater than 12 months), and
- must be a discrete event that is not part of long-term structural adjustment processes or normal fluctuations in commodity prices. (DAFF 2008e)

As the New South Wales Government submitted:

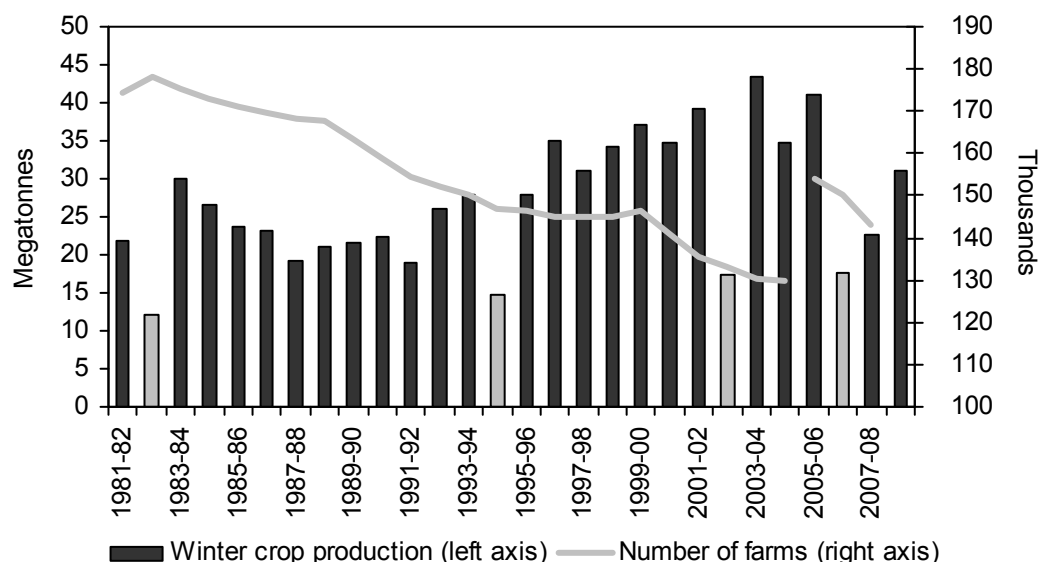
The NDP approached drought as a foreseeable business risk for Australian farmers, and focused on helping farmers to assess, manage and mitigate this risk. Since then, both Commonwealth and State drought programs have been modified by increasing the availability of welfare to drought-affected farmers, loosening eligibility criteria for assistance, and continuing or reinstating State transaction-based farmer subsidies that had previously been ceased. These changes may have slowed the NDP’s drive towards a preparedness and risk management approach to drought. (sub. 90, p. 1)

This inquiry provides another opportunity to address the uneasy nexus between policy intent and governments’ reactions when droughts occur. It also enables an examination of the relationship between drought policy, rural adjustment, and greater productivity in agriculture.

The impact of the more recent droughts of 1982-83, 1994-95, 2002-03 and 2006-07 on winter crop production are demonstrated in figure 1.1. But that figure also shows an increasing, but variable, winter crop output over time (as influenced by natural climate variability and improving farm productivity) and continuing adjustment (declining farm numbers). How government drought policies impinge on long term adjustment across the range of agricultural industries is a critical issue.

Figure 1.1 **Drought policy and adjustment in agriculture, 1981-82 to 2008-09^{ab}**

Broadacre production



^a Comparable time series data on farm numbers are not available after 2004-05. See chapter 2 for details. ^b 2008-09 is an ABARE forecast.

Data sources: ABARE (2008a); ABARE (2008d); ABS (*Principle Agricultural Commodities, Australia, Preliminary, 2007-08*, Cat. no. 7111.0).

Inherent climate variability and climate change

As noted in box 1.1, the NDP allows for the provision of assistance in circumstances of ‘exceptional’ events. In practice, in recent years, a significant proportion of Australia has been declared as experiencing EC. As at January 2009, some areas had been declared as experiencing EC for 14 of the past 17 years.

This is the first time, however, that Australia has experienced a widespread ‘irrigation drought’. There had been an expectation that most irrigation districts were drought proof, but the substantially lower inflows into the MDB, coupled with a significant over-allocation of water resources and reduced runoff, have resulted in severely reduced water allocations for many producers.

The climate change outlook prepared by BoM and CSIRO (Hennessy et al. 2008) reports that:

- the extent and frequency of exceptionally hot years have been increasing and are projected to continue, with exceptionally hot years likely to occur every 1-2 years, on average, over the period 2010–2040

-
- while trends in rainfall are highly dependent on the period of analysis due to large inter-decadal variability, exceptionally low rainfall years are projected to become more frequent in southwest Western Australia, the South Australian agricultural region, Victoria and Tasmania
 - exceptionally low soil moisture is projected to become more frequent in line with the projected increase in exceptionally low rainfall years.

Given this outlook for agriculture, the need for government programs to encourage and assist self-reliance and preparedness is accentuated.

1.2 The national review of drought policy

The Primary Industries Ministerial Forum in February 2008 (PIMF 2008a) and the subsequent meeting of the Primary Industries Ministerial Council in April 2008 (PIMC 2008) identified the need to reform drought policy. Australian primary industries ministers agreed that current approaches to drought and EC are no longer the most appropriate and that drought policy must be improved to create an environment of self-reliance and preparedness and encourage the adoption of appropriate climate change management practices.

Subsequently, the Minister for Agriculture, Fisheries and Forestry stated that:

The band of climate variation is shifting ... confirmed by a growing body of credible science ... Against this background, the government believes that it is time for Australia's farming community and rural policy makers to reconsider the meaning of EC for the future.

By undertaking reform to drought policy now, we can help farmers to adapt and respond to climate change, as well as develop closer links between the objectives of drought policy and the challenges of climate change. (Burke 2008c, pp. 4–5)

The Commission's public inquiry into government arrangements for drought support is one of three studies that constitute the Commonwealth Government's national review of drought policy, with the other two comprising:

- the assessment by the BoM–CSIRO of what a changing climate means for drought in Australia (Hennessy et al. 2008)
- an expert panel's assessment of the impacts associated with drought (Kenny et al. 2008).

This report draws on the results of these two studies, together with the Commission's own analysis of the material presented to it, to provide a comprehensive assessment of the economic, social and environmental dimensions of rural self-reliance and preparedness.

What the Commission is tasked with

In relation to farmers, farm businesses and farm dependent rural small businesses, the terms of reference request the Commission to:

- report on the appropriateness, effectiveness and efficiency of governments' business and income support measures to help manage drought
- identify impediments to improving self-reliance and preparedness for periods of financial difficulty
- identify the most appropriate, effective and efficient responses by governments to build self-reliance and preparedness to manage drought.

In undertaking the inquiry the Commission is to:

- report on the impact that the provision of drought support has on performance and productivity at the individual, business, industry, regional and state levels
- draw lessons from the range of support measures that are broadly available to the Australian community
- take into consideration the objectives of the NDP and the Commonwealth Government's Expenditure Review Principles.

The terms of reference (TOR) are at the front of this report.

1.3 Contextual matters

The TOR refer to three classes of recipients (farmers, farm businesses and farm dependent rural small businesses), at least eight policy measures (EC relief payments, EC interest rate subsidies, exit assistance, farm management deposits, professional advice and planning grants, irrigation management grants and rate rebate schemes) and three assessment criteria (appropriateness, effectiveness and efficiency). Further, the TOR request the Commission to report on the impact of drought support on 'performance and productivity' at five levels (individual, business, industry, region and state).

A systematic matrix-based approach to the TOR would involve 72 permutations for the five levels. Such a formalised analysis would be infeasible in the allotted time and unnecessarily complex in presentation. Accordingly, while the Commission has examined all of the identified matters throughout this report, it has focused primarily on:

- drought support measures in relation to their:
 - welfare impacts on farmers and farm households
 - economic impacts on farm (and farm-related) businesses

-
- impediments to the rural sector improving self-reliance and preparedness for times of financial difficulty
 - the role that governments should play in facilitating that improvement.

This focus is also consistent with the Commission's economy-wide remit as specified in its enabling legislation. Among other matters, the Commission must have regard to improving the overall performance of the economy in order to achieve higher living standards for all members of the Australian community.

The following sub-sections discuss key terms and concepts specified in the TOR.

Appropriateness, effectiveness and efficiency

Appropriateness, effectiveness and efficiency appear in the TOR in relation to current and future drought support measures.

In simple terms, policy measures and initiatives should be:

- appropriate — based on sound economic and/or social rationales
- effective — achieve the government's (ideally, appropriate) objectives without unintended consequences
- efficient — provide targeted support that achieves the greatest positive net benefit.

It is self-evident that policy objectives should be appropriate, albeit that an inappropriate objective could still be met effectively. However, appropriate objectives will not be met if the measures chosen to pursue them are ineffective, or will be met at a higher cost than necessary if the measures are inefficient.

Self-reliance and preparedness

Governments place a high priority on farmers and their communities achieving self-reliance over the long term and preparedness for periods of financial difficulty. These terms are often used interchangeably. For example, having sources of off-farm income as a diversification strategy could be regarded as: increasing self-reliance; increasing preparedness for drought; a risk-management strategy; or even a reactive response once a drought event has commenced. While the latter response may not constitute ex ante preparedness, it could reflect a management approach of devoting resources to on-farm activities until it is necessary to do otherwise.

An expression of self-reliance was presented in the 1990 drought policy review which emphasised the respective roles for agricultural producers and governments:

... self-reliance recognises the primary responsibility of individual producers for the commercial performance of their enterprises and for ensuring agricultural activity is carried out in an economically and environmentally responsible manner.

This concept also recognises that governments should not intervene to distort market prices or outputs. Government policy must work within the confines of the marketplace, by removing distortions or disincentives to appropriate activities, and by providing positive incentives where markets fail to provide sufficient inducements to act in the community interest. (McInnes et. al. 1990, vol. 1, p. 9)

Typically, preparedness is understood as the ability of farmers and farm businesses to develop strategies to enable them to prepare for, manage, and recover from, drought. This includes building a strong capital base in terms of the farm's natural resources and infrastructure, and the business' balance sheet in good years, to be able to withstand poor years, as well as enhancing the farmer's skills.

A common element of both self-reliance and preparedness is risk management. Business risks can arise on several fronts — shifts in farmers' terms of trade, changes by competitors, climate variability and natural disasters. Such risks are fundamental aspects of the business of farming. Risk management is a systematic process of identifying and evaluating risks, what can be done to prevent them eventuating and how to deal with them if they arise.

As noted by the McColl review:

A range of mechanisms are available to handle many aspects of risk. These include on-farm practices such as changing production mixes and the use of meteorological forecasting instruments, and off-farm measures such as price hedging, fixing, capping or collaring interest rates, use of insurance and employing instruments to smooth income ...

There are impediments to the uptake of some of these approaches both on- and off-farm. Many of them add to the complexity of the management task. Furthermore, government intervention in the past, particularly in marketing and adjustment, has limited the development of risk management instruments and raised expectations that assistance would be available from governments in times of difficulty. (McColl et al. 1997, p. 12)

Improved risk management strategies can enhance the capability of farm businesses to withstand adverse shocks, thereby increasing self-reliance.

Expenditure review principles

The terms of reference require the Commission to take into consideration the Commonwealth Government's Expenditure Review Principles. There is no public enunciation of those principles.

Policy interfaces

Several participants in this inquiry have raised concerns about the multiple and sometimes uncoordinated impacts of government policy 'silos'. Irrigators, in particular, stressed the need to be cognisant of the interactions and potential tensions between water policy and drought policy.

There are several policy areas that interact with drought policy, including:

- water reform — for example, rules governing water allocation and trading, or investment in infrastructure improvement
- climate change — for example, adaptation and mitigation (such as the proposed carbon pollution reduction scheme)
- natural resource management — for example, land clearing, soil erosion, salinity, native vegetation and feral pest control
- taxation — for example, fuel excise, income tax averaging, and managed investment schemes
- innovation — for example, the provision of public funding for research and development and extension services
- animal welfare — for example, the condition of livestock when water and feed are scarce and during transport
- social policies — for example, the provision of mental health resources
- regional development — for example, population distribution, horizontal fiscal equalisation and the provision of services in regional areas.

Many of these policy interfaces are raised throughout this report, but it would be inappropriate to attempt to redefine any of the above policies solely on the findings of this review.

1.4 The draft report process

The Commission released its draft report into Government Drought Support (PC 2008a) for public comment on 30 October 2008. To prepare the draft report, the Commission consulted widely with government departments, agricultural producer

organisations, individual farmers, regional councils, agribusinesses, small business owners, and social and community groups (appendix A). Roundtables were held throughout rural Australia and visits and consultations covered cropping, sheep, beef, dairy, pork, horticulture, viticulture and mixed farming operations spanning reliable and marginal regions (rainfall dependent and irrigated) operating on both freehold and leasehold land. The scale of operations ranges from vast pastoral properties to extensive broadacre operations in the Western Australian wheatbelt and down to smaller scale ‘blockies’ in the Riverland. In all, the Commission held meetings in 31 towns and cities around Australia and received 107 submissions prior to releasing the draft report.

In the draft report, the Commission found that, when measured against policy objectives relating to self-reliance, preparedness and climate change management, current government-funded drought support programs have many shortcomings. To address these shortcomings, the Commission made many proposals. The two key directions proposed were that:

- governments should refocus their farm business support programs to help farmers through research, development, extension, professional advice and business management training, all of which can help build self-reliance and preparedness
- all farm families facing hardship, not just those in EC areas, should have access to temporary income support through a scheme designed for farming circumstances.

Responses to the draft report

Ministers with responsibility for primary industries met in Canberra on 12 November 2008 to discuss options for improving drought policy. They considered the BoM-CSIRO climate outlook, the Expert Panel’s report on the social impacts of drought and the Commission’s draft report.

The Ministers noted that all three assessments indicated that governments need to refocus drought programs to support early investment in preparing for the social, environmental and economic impacts of drought and climate change. Accordingly, the Ministers agreed to the following principles for the further development of drought reforms:

- There should no longer be Exceptional Circumstances (EC) declarations or ‘lines on maps’. Instead, governments should focus on addressing the specific needs of farming families, farming businesses and farming communities.
- Future farm family welfare assistance should require a level of mutual responsibility.

-
- Government farm business support should assist farming businesses plan and prepare for the future. Farm business support will be based on a willingness by those businesses to prepare for the impacts of drought and climate change.
 - For access to the income support system, farming families should have a temporary period of exemption from the normal assets tests for farm assets but otherwise receive the same access rights as the wider community.
 - Government policies and programs should support farming communities to prepare for drought and enhance their long term sustainability and resilience.
 - Acknowledgement that drought is just one of a number of hardships that can adversely impact farmers.
 - Recognition of the important role of farmers as the nation's food producers. (PIMF 2008b)

At that meeting, Ministers also reaffirmed that the EC rules will not change for those producers currently receiving assistance in existing EC-declared areas.

The Commission sought public input on all aspects of its draft report. To this end, it conducted an extensive range of regional roundtables and public hearings to directly elicit individual and organisational responses to its draft proposals (appendix A). In addition to the 107 submissions received prior releasing the draft report, a further 81 submissions responded to the draft report (appendix A).

All of the evidence taken at the public hearings and regional roundtables, together with the submissions, have been taken into account in the preparation of this final report.

1.5 Outline of the report

This report comprises three parts: the background (chapters 1–3); the Commission's analysis of current drought support programs (chapters 4–6); and the future policy direction (chapters 7–11).

Background

To evaluate drought support measures, it is necessary to understand drought policy against the backdrop of longer term influences impacting on rural and regional Australia. Changes to the agricultural sector, the composition of rural and regional Australia and non-policy related influences on farmers' self-reliance and preparedness are discussed in chapter 2. What constitutes drought is addressed in chapter 3, which explores how the economic and social implications of drought are

manifested. Environmental aspects of drought and the implications of the prognosis for climate change are also considered.

Analysis of current drought support policies and programs

The evolution of drought policy and the respective roles of the Commonwealth and state and territory governments is described in chapter 4. The chapter also outlines the suite of assistance measures — from EC-triggered programs to Farm Management Deposits and other government programs. Chapter 5 analyses EC declarations, considering issues such as the inequities that arise from placing ‘lines on maps’ and process matters — criteria, timeliness and costs. Chapter 6 evaluates current drought support measures individually, as well as addressing many cross-program issues.

Self-reliance and preparedness

How the current system can be improved is explored in chapter 7. Chapter 8 focuses on a policy framework for encouraging farmers’ and farm businesses’ capacity to prepare for and manage drought. The role of government in providing a social safety net for all Australian households, including farm households in hardship, is then discussed in chapter 9. That chapter explores appropriate income support measures and their implications for ongoing rural adjustment. Chapter 10 discusses policy areas related to drought, such as water, natural resource management and climate policy, and considers the influence of these policies on drought-related outcomes. The final chapter addresses transitional and implementation issues (chapter 11). It concludes with the outlook for agriculture and rural communities under the Commission’s recommendations.