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# 1 Introduction

## 1.1 Background to the inquiry

This report assesses the transitional and ongoing economic and social effects of the National Competition Policy (NCP) on rural and regional Australia. It also assesses the impacts of NCP reforms on people and businesses in rural and regional communities relative to those located in the cities. The inquiry follows a request by a House of Representatives Standing Committee (Hawker Committee 1997a) for a study of the extent to which the benefits of competition are flowing to rural and regional Australia.

The inquiry took place at a time when the economic, social and other circumstances of rural and regional communities were being, and continue to be, affected by the interaction of many factors, including:

- Australia's increasing integration into the global economy and the lowering of international barriers to trade and capital — which have added to pressures for change in some regions and industries, but created opportunities in others;
- downward trends in world commodity prices (eg for some agricultural products and minerals which are major exports for Australia);
- a downturn in the economies of some of Australia's major trading partners (eg Japan and some South-East Asian nations);
- changes in consumer tastes (eg a decline in the demand for wool and increased demand for some horticultural products);
- changes in lifestyle (eg internal migration to coastal areas);
- technological change (eg the 'computer revolution');
- resource discovery and depletion (eg mine development and closures);
- increased attention to environmental and land use requirements; and
- reforms by all governments directed at making Australian industries more internationally competitive and getting better value for money from government programs (eg labour market and microeconomic reforms).

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The net effect of these myriad influences has varied markedly between regions. The associated adjustment pressures have led to changes in the composition of activity within regions, and the movement of resources and people from some (metropolitan, rural or remote) regions to others. Several rural and regional communities have been hit particularly hard — some towns are in decline as their core industries face long term decline, government services are reduced and businesses close or relocate in response to population losses. In contrast, other regions have experienced significant growth (eg those growing cotton, wine grapes and other horticulture products, or benefiting from tourism and mining).

An important task for the inquiry was to disentangle the effects of NCP from, and to examine also, the many other government and non-government factors which influence growth and adjustment in rural and regional Australia.

## **Terms of reference**

The terms of reference for this inquiry are set out at the front of this report. In brief, the Commonwealth Government requested the Commission to inquire into the transitional and ongoing effects on rural and regional Australia of the NCP reform package agreed to in 1995 by the Commonwealth and all State and Territory governments. In particular, the Commission has been asked to report on:

- the effect of competition policy reforms on the structure, competitiveness and regulation of industries and markets supplying, and supplied by, rural and regional Australia;
- the economic and social effects of the reforms on rural and regional Australia and on the wider Australian economy;
- differences between regional and metropolitan Australia in the nature and operation of major markets, and in the effects of competition policy reforms; and
- measures to facilitate the flow of benefits (or to reduce transitional costs or negative impacts) to rural and regional Australia from the reforms.

The Commission also has been asked to consider other influences on rural and regional Australia, including international trade, foreign investment and globalisation. The terms of reference do not require the Commission to consider how best to promote the long-term development of rural and regional Australia. However, because participants have raised this issue, the report also considers government measures which are designed to hold and attract resources to regional areas.

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In conducting this inquiry, the Commission is required to have regard to policy guidelines set out in the *Productivity Commission Act 1998*. These guidelines direct the Commission to take into account the interests of the wider community and also social, environmental and regional objectives that bear on the quality of people's lives. It is also required to consider the need to facilitate adjustment to structural changes in the economy.

## **The inquiry process**

The Commission released an issues paper in late September 1998 inviting written submissions on matters raised by the terms of reference. A draft report was released on 14 May 1999. In total, 303 submissions were received (214 prior to the draft report), primarily from local governments, regional and industry organisations, small and large businesses, farmers and academics. All State and Territory governments were involved in the inquiry in varying degrees.

To gather information about the views and experiences of people living and working in rural and regional communities, the Commission undertook an extensive round of visits in all States and Territories. It visited around 75 rural and regional locations and held informal discussions with around 1000 people representing Commonwealth, State, Territory and local governments, private sector businesses, industry groups (covering mining, manufacturing, agriculture, tourism and other services), regional development organisations, community and environmental groups, academics and others. These discussions provided contact with a wider range of people and localities than would have been possible with the more formal initial public hearings which the Commission usually conducts. Public hearings on the draft report were held in Adelaide, Perth, Tamworth, Albury, Launceston, Bendigo, Toowoomba, Townsville and Canberra in June–July 1999.

Those who made submissions, and the groups and locations which the Commission visited to hold informal discussions, are listed in appendix A.

## **1.2 Defining rural and regional Australia**

The terms of reference focus on rural and regional Australia — a term for which there is no precise definition.

Rural and regional Australia can be defined by physical and social characteristics (eg geography and cultural boundaries) and perceptions. For example, in many respects, the South Australian and Tasmanian Governments regard their entire States as regions, and some consider the Northern Territory as part of the South-East

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Asian region. Within Australia, regional administrative arrangements can transcend State boundaries (eg the Murray–Darling Basin Commission).

The definition of regions is governed often by the availability of data and the purpose for which those data are collected. Some examples are cited below.

- The Australian Bureau of Statistics (ABS) compiles data for States and Territories, statistical divisions (66), sub-divisions (194) and local areas (1336). It also produces some social trends analyses based on just three categories — rural areas, towns and cities.
- The National Office of Local Government classifies the 729 local governments which receive financial assistance grants into 22 discrete categories from ‘Urban Capital City’ through to ‘Remote Extra Small’.
- The Commonwealth Department of Employment, Workplace Relations and Small Business has adopted a classification of 450 ‘local labour markets’.
- Regional economic models usually adopt contiguous geographic zones — for example, the MONASH model, a derivative of which used for this draft report accommodates 57 regional areas.

Construction of a standard statistical definition of rural and regional Australia, which would have the benefit of simplicity, has not been feasible. It would require all relevant data series to be reconfigured to fit that definition, which is not practical because of the wide-ranging nature of this inquiry. Moreover, different classifications of regional data can be useful for different analytical purposes. Thus, in this report, the Commission has used data from a range of sources which adopt different interpretations of terms such as ‘metropolitan’, ‘remote’ and ‘rural’. In chapter 2, for example, it has aggregated the 1336 ABS local areas to create four categories — ‘capital cities’, ‘coastal’, ‘inland’ and ‘remote’. In other chapters, data are presented in the manner in which they have been collected.

Although statistical and jurisdictional boundaries are important, the Commission has not sought to constrain the reference by adopting a narrow view of what constitutes ‘rural and regional Australia’. Rather, in an attempt to capture the essence of the reference — which in colloquial terms is about the ‘city’ and the ‘bush’ — it has taken a broad view.

The Commission has interpreted ‘rural and regional Australia’ to include farms and rural towns (eg Ouyen in Victoria and Narrogin in Western Australia), important regional centres (eg Tamworth and Whyalla) and mining towns (eg Mount Isa and Kalgoorlie). It considers that the terms of reference were not generally intended to include capital cities or major urban–coastal agglomerations such as Geelong, Wollongong and Newcastle. Nonetheless, a broad definition allows the particular

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circumstances of small and remote capitals (eg Hobart and Darwin) and larger, but remote, cities (eg Cairns) to be taken into consideration where particular circumstances or issues warrant their inclusion.

The Balanced State Development Working Group (BSDWG) considered the Commission's definition of rural and regional Australia to be too broad. It said:

... to redefine the reference so that it covers all parts of Australia other than metropolitan areas and to call that country Australia is a much broader view of the parts of Australia which are in the reference than we think is appropriate (trans., pp. 1042–3)

In its submission, the BSDWG (sub. 205) considered that the terms of reference for the inquiry should not cover large 'self-contained' communities such as Broken Hill, Cairns, Kalgoorlie and Whyalla. However, such definitional rigidity would rule out towns which clearly are remote. This would not accord with the generally accepted notion that the inquiry should cover the 'three Rs' — rural, regional and remote communities.

Overall, the Commission's broad approach to defining rural and regional Australia was generally supported by participants. For instance, Tasmania's West North West Councils considered that:

... rural and regional Australia knows who it is — and the community will define itself around the issue, as opposed to setting boundaries and lines around the area ... there is strong support for the approach outlined by the Commission in its issues paper, which sees rural and regional Australia including all areas other than the large metropolitan centres. (sub. 5, p. 2)

**For the sake of succinctness, the Commission has adopted the term 'country Australia' when referring to rural and regional Australia.**

### **1.3 What is National Competition Policy?**

NCP is defined in the terms of reference for this inquiry as the set of reforms agreed to by the Commonwealth, State and Territory governments under intergovernmental agreements signed in April 1995. These reforms, which are discussed in detail in chapter 4, cover:

- prices oversight of certain government businesses;
- competitive neutrality between significant government businesses and private sector competitors;
- reform of the structure of Commonwealth and State public utility monopolies;
- reviews of legislation which restrict competition;

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- provision for allowing businesses to gain access to certain infrastructure facilities;
  - extension of the competitive conduct rules of the *Trade Practices Act 1974* to all businesses and professions in Australia, whether private or government; and
  - continuation of earlier reform commitments for gas, electricity, water and road transport agreed to by the Council of Australian Governments (CoAG).

In recognition of the economic benefits expected to flow from the reforms, and that the Commonwealth stands to gain increased tax revenue, NCP specifies a program of financial grants by the Commonwealth to State and Territory governments contingent on implementation of the agreed reforms.

In sum, NCP refers to a package of measures which, broadly speaking, aim to encourage competition. The underlying notion is that greater competition will usually create incentives for improved economic performance. To the extent that this can be achieved, incomes, employment and living standards are likely to rise. However, as it is not sensible to promote competition in some markets, NCP permits restrictions on competition where such arrangements can be shown to be in the ‘public interest’.

While NCP can be defined fairly precisely, its boundaries can appear arbitrary because many other microeconomic reform initiatives which also are intended to improve competition, such as general reductions in tariff assistance and deregulation of financial markets, lie outside NCP. Similarly, the ‘four pillars’ policy, which prohibits key retail banking mergers, and the recent deregulation of the petroleum industry, are also examples of competition policies which lie outside NCP. Of course, many reform initiatives have elements in common with NCP principles. For example, commercialisation of government businesses is consistent with NCP.

To put NCP into context, some examples of government policies potentially affecting metropolitan and country communities are presented in box 1.1. It is apparent from the box that NCP is only one part of a broad policy agenda.

Too strict an interpretation of NCP could lead to many of the concerns expressed by people in country communities being ignored. Consequently, the Commission has looked at the broader context in which concerns about NCP have been raised. The terms of reference, the Commission’s guidelines and its open public inquiry processes encourage such an interpretation.

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**Box 1.1      Examples of government policies potentially affecting country Australia****Microeconomic reforms**

- reductions in trade barriers (eg tariffs and quotas)
- reductions in other assistance programs (eg production bounties)
- easing of labour market regulation (eg wages agreements at the enterprise level)
- competitive tendering and contracting (eg outsourcing of information technology services)
- commercialisation, corporatisation and privatisation of government utilities and services (eg formation of business units within government departments)
- deregulation (eg petrol industry, financial markets)
- consumer protection and pro-competitive legislation (eg Trade Practices Act) and
- national competition policy

**Other government policies**

- macroeconomic policies (eg fiscal, monetary and exchange rate policies)
- public provision of social services and infrastructure (eg schools and hospitals)
- public provision of 'economic' infrastructure (eg roads and airports)
- foreign investment restrictions (eg Foreign Investment Review Board)
- regional policies (eg Rural Telecommunications Infrastructure Fund)
- environmental policies (eg regional forest agreements)
- Aboriginal reconciliation (eg native title legislation)
- social 'safety net' and adjustment (eg general social welfare schemes, regional adjustment schemes and phased reform measures)

## **1.4      Themes from country Australia**

The experiences of regions in country Australia are mixed. The Commission met people in regions that are growing (eg Katherine in the Northern Territory), others that are contracting (eg Whyalla in South Australia) and some that are seeking to diversify their economic bases (eg Atherton in Queensland where some producers are switching from tobacco growing to horticulture). For illustrative purposes, country Australia can be split into three broad categories according to their growth experience:

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- *Growing*: Some regional areas are performing strongly and recording growth rates well in excess of the national average. These areas often have a diversified economic base, and may be prospering from growth in particular activities such as tourism and certain resource-based and agricultural activities (eg cotton and grape growing or export-oriented food processing). In some cases, towns that are faring well are benefiting from the regional consolidation of economic activity at the expense of smaller nearby communities — regional service centres (eg Dubbo in New South Wales) can attract and hold banking services, large retailers and government service centres and thereby draw trade and income from neighbouring areas.
  - *Static*: Large parts of country Australia are experiencing ‘business as usual’ overall. These areas typically have sufficient population to hold basic services. Towns in these regions tend to have some degree of diversification in economic activity. However, the composition of that activity may be changing in response to shifts in the fortunes of various products (eg wool relative to wheat).
  - *Declining*: The population of some areas in country Australia is in decline. These areas often lack a diversified economic base — for example, a mining town (eg Moura in Queensland) can find it difficult to adjust to a mine closure. Towns in these regions are often adversely affected by the ongoing decline in the number of farms (and hence rural population) throughout Australia. Scale is important and very small communities are vulnerable to self-reinforcing decline.

The Commission visited regions performing strongly as a result of new opportunities. It also encountered regions responding positively to challenges beyond their control — such as reduced demand and/or prices for their agricultural or mining products. People in many regions are seeking to assert greater control over their future by harnessing community resources in a variety of ways, including:

- promoting a region’s inherent advantages for investment (eg lower cost housing, better quality of life, a dedicated and stable labour force, excess infrastructure capacity and industrial sites);
- assembling incentive packages to attract people to relocate into the region (eg concessional land and rates holidays);
- diversifying into other activities (eg eco-tourism or niche horticultural products);
- seeking to retain certain services through community participation (eg community banking facilities); and
- improving sporting, social and recreational facilities and opportunities (eg festivals and competitions).



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Regional experiences across Australia involve a mixture of progress and setbacks. Agricultural production and exports are increasing — although the product mix is changing from, for example, the traditional beef and wool sectors to increased production of cotton, wine, canola and horticulture products. However, the Commission received relatively little input from people in such growth sectors, or from those managing the top third of farms which account for around 70 per cent of broadacre agricultural production.

On the contrary, this inquiry has provided an outlet mainly for expressions of unease — as the Hon. Russell Cooper, MLA (the Queensland Opposition spokesman on primary industries) noted in relation to benefits flowing from NCP reforms:

There may have been. Often the good news doesn't come through, it's all bad. (trans., p. 624).

This view was noted also by the Senate Select Committee on the Socio-Economic Consequences of the National Competition Policy, which said:

... when negative impacts arise, NCP is held up as the culprit — guilty or not (it is rarely given credit for any benefits which arise). (Quirke 1999, p. 61)

Many people raised concerns about reform initiatives that are demonstrably linked to NCP. Some see NCP as another component of ongoing 'economic rationalism' which they regard as inimical to their wellbeing. It is also viewed by some as a bureaucratic drive led by State governments in pursuit of competition payments.

Many participants were more worried about government policies which do not form part of NCP (eg privatisation). In addition, during regional visits and in submissions, most people raised concerns about developments which are essentially beyond the control of governments (eg changes in consumer spending patterns and falling commodity prices).

The rest of this chapter attempts to convey the general tenor of views expressed to the Commission during meetings with, and in submissions from, people in country Australia. It does not attempt to categorise regional impacts according to whether they derive from the actions of governments or from factors beyond their control, or to assess the validity of the views advanced — that task is addressed in the body of this report.

### *Centralisation and falling service standards*

Loss of local provision of services was a common theme throughout country regions — for example, *bank closures* and a reduction in government employees such as Telstra, rail, public works and community service personnel. Withdrawal of services

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has deprived some communities of facilities (eg the capacity to bank shop takings) and can induce further population decline which threatens thresholds necessary to sustain important *social infrastructures* (eg schools, medical facilities and police stations). These developments were said to be typical of a more damaging overall trend — the *centralisation of management functions* to regional centres and capital cities.

Many regions in country Australia have minimal or no access to *mobile phone networks* and limited television coverage. While basic telephone services are available to virtually all households, in country areas the quality is often insufficient to enable *Internet access* or basic data transmission services such as facsimile. A frequently expressed concern of people in country Australia is a feeling of impotence associated with the replacement of local services with *call centres* that can be thousands of kilometres distant. The closure of local Telstra depots is widely considered to have led to poorer local *service standards* (eg long delays for telephone connections). However, most people in country communities recognised that the introduction of competition in telecommunications has led to cheaper long distance phone calls.

### *The social consequences of population decline*

Many people in country Australia expressed concern about the loss of population to provincial centres and capital cities. Of particular concern is the *demographic imbalance* in many regional areas — in particular, a ‘shortage’ of people aged from between 15–35. This is said to arise from a lack of *employment and educational opportunities* and from closures of local bank branches and government offices and workshops.

Incidental effects of this demographic imbalance include the loss of motivated individuals who often are important for maintaining the social fabric of a small community through, for example, involvement in sporting clubs. This trend is said to have had a detrimental effect on the extent of *community leadership and voluntarism*. In some areas, the Commission was told that the ongoing *withdrawal of public and private services* (eg schools and banks) has reduced the flow of female employees into towns and created a shortage of women of marriageable age.

These concerns form part of a broader perception of a *deteriorating social amenity* in parts of country Australia. The lack of diversionary opportunities is considered to contribute to frustration and social dislocation. Rural counsellors told the Commission that the social costs of structural change are often reflected in drug abuse, alcoholism, escalating crime rates and youth suicide.

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## Government policies inducing decline in country Australia

A significant proportion of country people feel that they have been abandoned by governments. Many hold the view that the Commonwealth Government has no commitment to country Australia and that State and Territory governments are catering to the interests of the major urban populations. For example, some participants noted that country areas find it difficult to gain *basic services*, whereas millions of dollars are spent propping up urban public transport systems and city sports and arts facilities.

Some government policies are viewed as undermining the viability of regions. The *contracting-out* of roadworks, previously performed by regionally-based public works personnel, but now sometimes performed by contractors from elsewhere, is a common concern. In several States, people argued that the scale of tenders being let by State governments rules out work opportunities for locals and small contractors. Moreover, it was often said that *sub-standard infrastructures* are being built by outside contractors, reflecting their poor understanding of local conditions and/or mis-specification of tenders by city-based bureaucrats.

*Compulsory competitive tendering* in Victoria was seen by several local councils in regional areas as an unnecessarily onerous process. More generally, local governments in several jurisdictions complained of prescriptive requirements placed upon them by policy makers in capital cities — these include *tendering procedures* for markets too small to sustain more than one service provider. Many councils complained of *rigid guidelines* which reduce flexibility and force quality to be sacrificed in favour of lower costs. More generally, many people questioned the appropriateness of contracting-out and centralising *social services*. That said, many local councils indicated that *competitive neutrality* has delivered significant benefits in the form of improved costing information that enables them to make better use of rate payers' funds.

In rural regions, the issue of declining international *commodity prices* and the actions of other countries in *subsidising* agricultural products on world markets is a concern. Others (eg tobacco producers) complained of the impact of *tariff cuts* and the withdrawal of assistance. Of course, some producers who use certain rural products as inputs into their own production (eg feedstocks) favour further reform of those arrangements which raise the prices of inputs.

In remote regions, it was commonly stated that the Commonwealth Government has proven to be unreceptive to the damage inflicted on communities by the *fringe benefits tax* on employer-provided housing. This is claimed to increase costs significantly and frustrate attempts by regions to offer greater housing choices to employees in order to counter the impact of *fly-in, fly-out* operations.

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Some participants indicated that the problems confronting country Australia are, in part, a legacy of earlier *government policies* — for example, State government policies which force mining companies to establish remote towns are said to have planted the seeds of future adjustment problems when the resource was depleted. Similar comments were made about well-intentioned *soldier settlement* policies following the world wars. More recent examples include practices such as putting disadvantaged people in *public housing* in regions with limited employment opportunities.

### *Commercialisation of government businesses*

The identification and costing of community service obligations associated with the *commercialisation and corporatisation* of government businesses was an issue raised during discussions in many country areas. There is widespread concern that the process will lead to removal of *cross-subsidies* used to support lower prices for goods and services provided by government businesses to many users in country Australia. As the Commission was told, ‘in the past if we wanted better services we could lobby the local member, but now there is no way that a competitive business will supply a service at a loss’.

Many areas have seen reductions in uneconomic services (eg some *rail routes* are no longer serviced) and an increase in charges (eg requirements to contribute to water *headworks charges*). As well as affecting people living in the region, full cost recovery can deter new development. Some participants considered that full cost attribution and the *user pays* principle make sense, but drew the line at governments also seeking a *rate of return* on publicly funded infrastructure. This issue often emerged with respect to the construction and operation of water infrastructure and is seen as a threat to agricultural development.

Several participants sought the retention of government ownership of utilities. There is a widespread fear that the long history of *subsidised power and water* — so-called ‘postage stamp’ pricing — to regional areas is under threat. There are also concerns that uneconomic public infrastructure will fall into disrepair. In contrast, regions that are ‘losing’ from uniform pricing policies — for example, users on main rail lines who cross-subsidise users on spur lines tend to favour more *cost-reflective pricing*.

### *Competition in regional markets*

Most *regional markets* have fewer suppliers and buyers than those in the cities — some country towns may be able to sustain only one supermarket or processor. This

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has raised concerns that changes following the *legislation review* process will leave small producers at the mercy of regional monopolies (eg processors) and powerful retailing interests. Many rural producers felt that decisions taken following legislation reviews of longstanding *statutory marketing arrangements* for commodities such as grains, dairy products, eggs and potatoes could have adverse effects. It is commonly held that reform of such arrangements will be at the expense of rural producers and their communities, of doubtful benefit to consumers, and a windfall for retailers and/or processors.

Many participants also considered that regional consumers are increasingly likely to face higher prices because of the influence of *powerful retailers*. Indeed, a perceived *lack of competition* is a cause for concern in many smaller regional markets.

Similarly, the prospect of the removal of regulations curtailing trading hours and of regulations protecting groups such as *newsagents*, *service stations* and *pharmacies*, is considered likely to damage small communities. Unrestricted competition is seen by some as favouring large retailers and large service providers (eg road freight companies) by enabling them to expand and diversify at the expense of small local operators. However, some people in communities which had never (or had previously) experienced regulated trading hours consider that such restrictions would have little impact other than to inconvenience consumers.

Although not associated with any recent policy change, the Commission encountered disgruntlement with the significant differences in *petrol prices* between metropolitan and country areas. In some cases, independent petrol retailers such as Gull and Woolworths have introduced keen price competition which has reduced regional petrol prices. This development is usually welcome but, in some cases, people complain that it threatens the viability of local service station businesses.

### *A lack of vision for country Australia*

A common plea by people in country Australia is for governments to have a vision for Australia into the next century. Many consider that the end result of current trends — whether driven by *globalisation* or government policy — will be a nation with massive population centres on the coast and a sparsely populated interior servicing fly-in, fly-out mining operations and large scale agriculture. Some people argue that reliance on economic criteria, rather than a *nation-building* vision, would have resulted in projects such as the Kalgoorlie pipeline and the Snowy River hydro-electricity scheme never getting off the ground. In this context, many people in country Australia are calling for integrated *regional development policies*.

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In later chapters, these concerns are addressed with a view to ascertaining their significance across country Australia generally.

## **1.5 Structure of the report**

To address the concerns of participants within the context of the terms of reference, the report is divided into three parts.

- Part A provides a brief overview of demographic and economic change, and the main sources of change, with an emphasis on changes affecting country Australia;
- Part B assesses the impacts of the NCP reforms, particularly on communities in country Australia; and
- Part C describes common misconceptions about NCP and proposes measures which could be taken to improve its implementation and operation. It also describes government policies which can facilitate the flow of benefits, or mitigate the costs, of the NCP reforms. These include policies which aim to maintain or attract resources to, and provide adequate levels of service in, country Australia. Finally, a number of adjustment issues are considered.