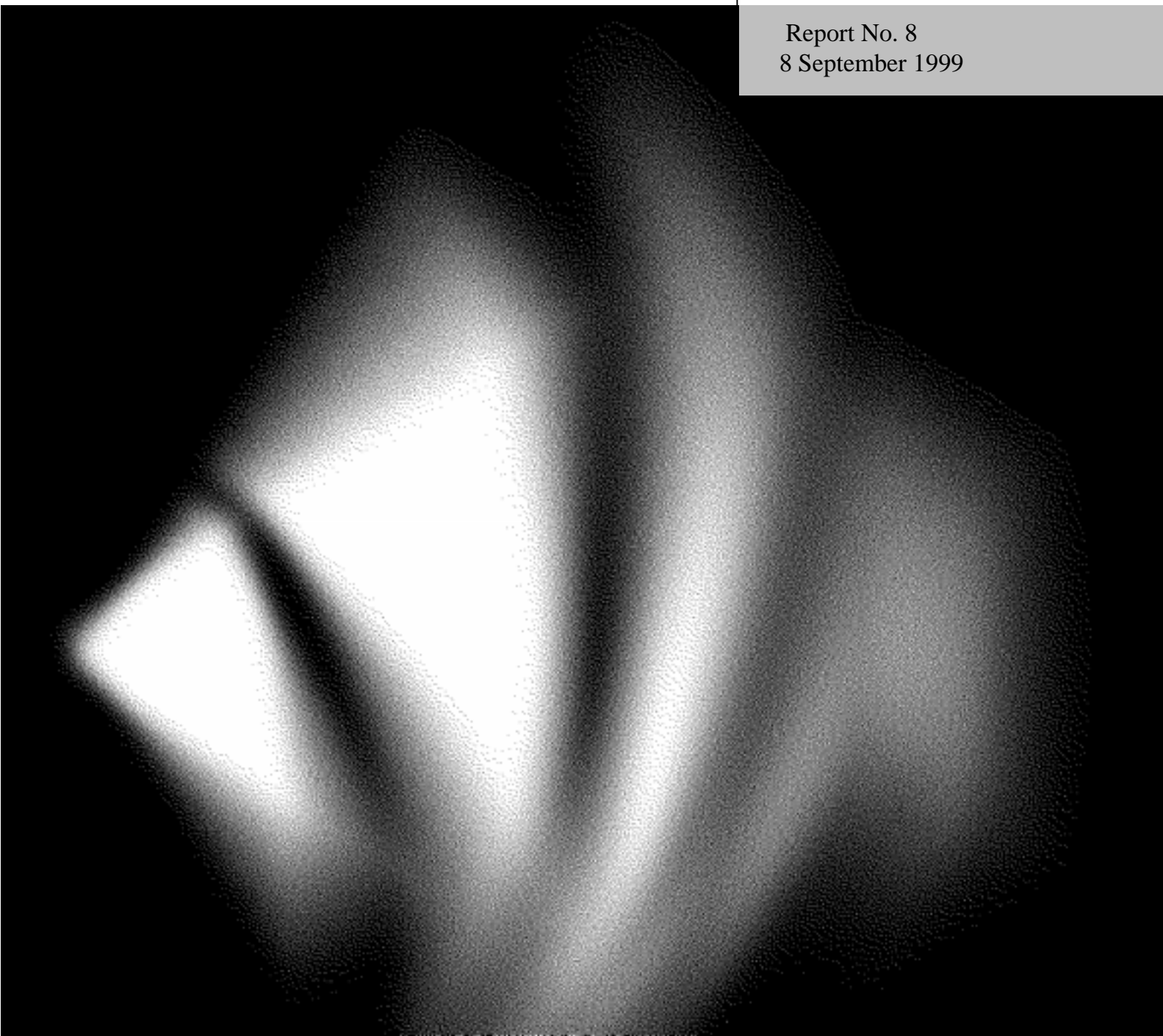




Impact of Competition Policy Reforms on Rural and Regional Australia

Inquiry Report

Report No. 8
8 September 1999



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The Productivity Commission

The Productivity Commission, an independent Commonwealth agency, is the Government's principal review and advisory body on microeconomic policy and regulation. It conducts public inquiries and research into a broad range of economic and social issues affecting the welfare of Australians.

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Terms of reference

PRODUCTIVITY COMMISSION ACT 1998

I, Peter Costello, Treasurer, under Part 3 of the *Productivity Commission Act 1998*, hereby refer the impact of competition policy reforms on rural and regional Australia for inquiry and report within twelve months of receipt of this reference. The Commission is to hold public hearings for the purpose of the inquiry, including in rural and regional Australia.

Background

The Government is proceeding with this inquiry in response to recommendations made by the House of Representatives Committee on Financial Institutions and Public Administration. The Government wishes to ensure that the benefits of increased competition in the economy flow to all Australians, including those living in rural and regional Australia, and that the implementation of competition policy promotes efficiency, economic growth and community welfare. Competition policy also recognises that there can be circumstances in which restrictions on competition may be justified where there are offsetting public benefits.

Scope of inquiry

The Commission's public inquiry should assess the impact (both transitional and ongoing) of the competition policy and related reforms introduced by the Commonwealth, State, Territory and local governments under the three intergovernmental agreements signed in April 1995 — the *Competition Principles Agreement*, the *Conduct Code Agreement* and the *Agreement to Implement the National Competition Policy and Related Reforms*. These agreements followed an Independent Committee of Inquiry into National Competition Policy that reported to Commonwealth, State and Territory Heads of Government in August 1993 (the Hilmer Report).

In undertaking the inquiry the Commission should have regard to the established economic, social, environmental, and regional development objectives of Australian governments. Consideration should be given to other influences on the evolution of markets in regional and rural Australia, including the role of international trade, foreign investment and globalisation generally.

The Commission should specifically report on:

- (a) the impact of competition policy reforms on the structure, competitiveness and regulation of major industries and markets supplying to and supplied by regional and rural Australia;
- (b) the economic and social impacts on regional and rural Australia (including on small businesses and local governments) of the changes to market structure, competitiveness and regulation flowing from the reforms and the effect of these impacts and changes on the wider Australian economy;
- (c) possible differences between regional and metropolitan Australia in the nature and operation of major markets and in the economic and social impacts of the reforms promoted by national competition policy; and
- (d) any measures which should be taken to facilitate the flow of benefits (or to mitigate any transitional costs or negative impacts) arising from competition policy reforms to residents and businesses in regional and rural Australia.

PETER COSTELLO

[Reference received on 31 August 1998]

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Disclosure of interests

The *Productivity Commission Act 1998* specifies that where Commissioners have or acquire interests, pecuniary or otherwise, that could conflict with the proper performance of their functions during an inquiry they must disclose the interests.

Professor Judith Sloan has advised the Commission that she is a director of the following companies:

- Santos Ltd;
- Mayne Nickless Ltd; and
- SGIO Insurance Ltd.

Acknowledgments

In conducting its inquiry, the Commission has benefited greatly from the participation of many people and organisations in rural and regional Australia. The Commission is grateful to all those who provided written submissions or gave freely of their time to discuss issues in various forums.

Commissioners would also like to express their gratitude for the dedicated assistance of the inquiry team on what was a wide-ranging task.

Abbreviations and explanations

Abbreviations

AAA	the Commonwealth Government's Agriculture - Advancing Australia policy
ABARE	Australian Bureau of Agricultural and Resource Economics
ABB	Australian Barley Board
ABC	Australian Broadcasting Corporation
ABS	Australian Bureau of Statistics
ACA	Australian Communications Authority
ACCC	Australian Competition and Consumer Commission
ACSWC	Australian Catholic Social Welfare Commission
ACT	Australian Capital Territory
AFFA	Commonwealth Department of Agriculture, Fisheries and Forestry – Australia
AGA	Australian Gas Association
AIHW	Australian Institute of Health and Welfare
AMPC	Australian Meat Processors Corporation
APIA	Australian Pipeline Industry Association
ARMCANZ	Agricultural and Resource Management Council of Australia and New Zealand
ARWA	Association of Rural Water Authorities
ATC	Australian Transport Council
ATMs	automatic teller machines
AWB	Australian Wheat Board
AWEX	Australian Wool Exchange Limited
BIE	Bureau of Industry Economics
CAN	Customer Access Network

CAP	Common Agricultural Policy
CBD	central business district
CCT	compulsory competitive tendering
CGC	Commonwealth Grants Commission
CIE	Centre for International Economics
CN	competitive neutrality
CoAG	Council of Australian Governments
CPA	Competition Principles Agreement
cpl	cents per litre
CSG	customer service guarantee
CSO	community service obligation
CTC	competitive tendering and contracting
CWA	Country Women's Association
DoLG	Department of Local Government (NSW)
DLWC	Department of Land and Water Conservation (NSW)
DNRE	Department of Natural Resources and Environment (Vic)
EFTPOS	electronic fund transfer point of sale
EPAC	Economic Planning Advisory Council
ESAA	Electricity Supply Association of Australia
EVAO	estimated Value of Agricultural Output
FAG	Financial Assistance Grants
FBT	fringe benefits tax
FDI	foreign direct investment
FIFO	fly-in, fly-out
GATT	General Agreement on Trade and Tariff
GBE	government business enterprise
GDP	gross domestic product
GPWA	Grain Pool of WA
GST	goods and services tax
GTE	government trading enterprise

HFE	horizontal fiscal equity
IAC	Industries Assistance Commission
IC	Industry Commission
IPART	Independent Pricing and Regulatory Tribunal
KWh	kilowatt hours
kt	kilotonne
LGASA	Local Government Association of South Australia
MDBC	Murray–Darling Basin Commission
MFP	multi-factor productivity
MIA	Murrumbidgee Irrigation Area
MIACHA	MIA Council of Horticultural Associations
ML	megalitre
MLA	Meat and Livestock Australia
MLA	Member of the Legislative Assembly
MP	Member of Parliament
Mt	megatonne
mu	metropolitan urban
MWh	megawatt hours
NARGA	National Association of Retail Grocers of Australia
NCC	National Competition Council
NCP	National Competition Policy
NEM	National Electricity Market
NFF	National Farmers’ Federation
NHT	Natural Heritage Trust of Australia
NLP	National Landcare Program
nmu	non-metropolitan urban
NRTC	National Road Transport Commission
NT	Northern Territory
NSW	New South Wales
NVI	National Vegetation Initiative

OECD	Organisation for Economic Co-operation and Development
ORGV	Office of the Regulator General of Victoria
PC	Productivity Commission
PFE	Public Financial Enterprise
PGA	Pastoralists' and Graziers' Association of Western Australia
PIRSA	Primary Industries and Resources South Australia
PTE	Public Trading Enterprise
QDLRC	Queensland Dairy Legislation Review Committee
QAL	Queensland Alumina Limited
Qld	Queensland
QSC	Queensland Sugar Corporation
RAC	Rail Access Corporation
RAS	Rural Adjustment Scheme
RBA	Reserve Bank of Australia
RDO	Regional Development Organisation
RFAs	Regional Forest Agreements
RRMA	Rural, Remote and Metropolitan Area classification
SA	South Australia
SBS	Special Broadcasting Services
SCARM	Standing Committee on Agriculture and Resource Management
SCIs	structural change indexes
SCNPMGTE	Steering Committee on National Performance Monitoring of Government Trading Enterprises
SCT	Specialised Container Transport
SCOT	Standing Committee on Transport
SD	Statistical Division
SIRWP	Sugar Industry Review Working Party
SLAs	statistical local areas
SMA	statutory marketing authority
SRA	The State Rail Authority

SRIDC	Southern Riverina Irrigation Districts' Council
SSDs	Statistical Sub Divisions
STD	subscriber trunk dialling
t	tonne
Tas	Tasmania
TCF	textiles, clothing and footwear
TWh	terawatt hours
TOR	terms of reference
TPA	Trade Practices Act
trans.	transcript
USO	universal service obligation
VET	vocational and educational training
Vic	Victoria
WA	Western Australia
WEA	Wheat Export Authority
WI	Wool International
WTO	World Trade Organisation

Explanations

Bolds	Bolds in the body of the report are highlighted in standard text, as this is.
Findings	<i>Findings in the body of the report are paragraphs highlighted using italics, as this is.</i>
Recommendations	<i>Recommendations in the body of the report are highlighted using bold italics with an outside border, as this is.</i>

Key Messages

- Communities in rural and regional Australia are being affected by a range of beneficial and adverse influences, of which National Competition Policy (NCP) is one.
- Most of these influences are of a long-term nature and largely beyond government control (eg declining terms of trade for agriculture, changes in technology and in consumer tastes).
- Such long-term factors are mainly responsible for the declining share of primary industries in Australia's economy and the associated drift of population away from inland country areas.
- NCP has become a scapegoat for some of the effects of these broader influences.
- Governments should take steps to improve community understanding of NCP, including clarification of how matters of wider public interest, and social considerations in particular, are to be taken into account in its implementation.
- While there are costs associated with implementing NCP, it will bring net benefits to the nation, and to rural and regional Australia as a whole over the medium term. That said, the early effects have favoured metropolitan areas more than rural and regional areas.
- There is likely to be more variation in the incidence of benefits and costs of NCP among country regions than in metropolitan areas.
- Where adjustment pressures develop rapidly and are regionally concentrated, governments may need to consider whether, in addition to generally available assistance measures, specific forms of adjustment assistance are warranted for some people in adversely affected regions.

Overview

During this inquiry, the Commission travelled widely in rural and regional Australia, holding discussions with almost 1000 people from all walks of life. Many of these people, such as local councillors and leaders of industry organisations, conveyed the views of numerous others whom they represent. In addition, the Commission received some 300 submissions and more than 100 participants provided comments on a draft of this report at public hearings. The discussions, hearings and submissions reveal a range of experiences in country areas. Some communities are doing well, but others are finding the going difficult.

Many people in country Australia see National Competition Policy (NCP) as an unprecedented outbreak of ‘economic rationalism’ which ignores important social issues and poses a threat to their way of life — adversely affecting their standard of living and the adequacy of services in country Australia.

NCP is widely perceived as being responsible for the withdrawal of government services, the demise of local businesses, the closure of country bank branches and is regarded by some as a major factor behind the population decline in parts of country Australia. NCP has also been linked to higher rates of crime, drug abuse, suicide and the creation of a demographic ‘hole’ — a shortage of young, motivated people needed to maintain the social fabric of towns through involvement in community,

Some views on National Competition Policy

I believe the Hilmer competition policy ... acts like a giant vacuum cleaner sucking people out of the bush and putting them on the shores in the seaboard. (Senator Ron Boswell, quoted by Gittins, R, ‘The bush vacuum cleaner’, *The Sydney Morning Herald*, 24 June 1998)

... competition policy is perceived to be an agent of community decline in regional and rural Australia. ... Competition policy is not seen as having delivered any major benefits. It is seen as a threat — to businesses, to properties, to livelihoods, to the overall economic base of communities. (National Party of Australia Women’s Federal Council, sub. 130, p. 6)

Manilla Shire Council views economic rationalism as one of the greatest threats to the future security and viability of rural and regional Australia. It also considers that economic rationalism is inextricably linked with implementation of competition policy. Whilst these change drivers may be instrumental in the promotion of efficiency and, perhaps, economic growth Council considers that they are destructive of community welfare. (Manilla Shire Council, sub. 86, p. 1)

sporting and other recreational activities.

A key issue for this inquiry has been to ascertain whether these views are well founded.

Many of the problems identified are indeed affecting some communities in country Australia, but the sources of these problems are less clear. The NCP reforms, agreed to by all Australian governments in 1995, interact with a range of other government policies and the diverse economic and social changes which shape Australia's growth and development more generally.

The Commission's primary task has been to investigate and report on the effects of NCP on people, businesses and communities, especially in country Australia. The Commission has looked at the effects to date and likely long-run effects on country Australia and the nation as a whole. It has sought to disentangle the effects of NCP from other sources of change. In doing so, it has considered the following questions:

- what does NCP entail and what are its effects?
- how significant is NCP relative to other factors?
- is country Australia affected more or less than metropolitan areas by NCP reforms?
- are there particular problems caused by NCP which need to be addressed?
- is there a need to supplement existing policies which help country communities to cope with any such problems?

To address these questions, it is necessary to examine the economic and social circumstances of country Australia and to consider what is driving them.

How is country Australia faring?

A common perception is that Australia is an increasingly urbanised society, with country areas continuing to lose population. Australia's emergence as a highly urbanised society is not, however, a recent phenomenon. At the time of Federation, around two-thirds of the population lived outside the capital cities. From that point, people began drifting into the capital cities. By 1971, the proportion of people living outside capital cities had fallen to just over one-third. Subsequently, that proportion has been relatively stable.

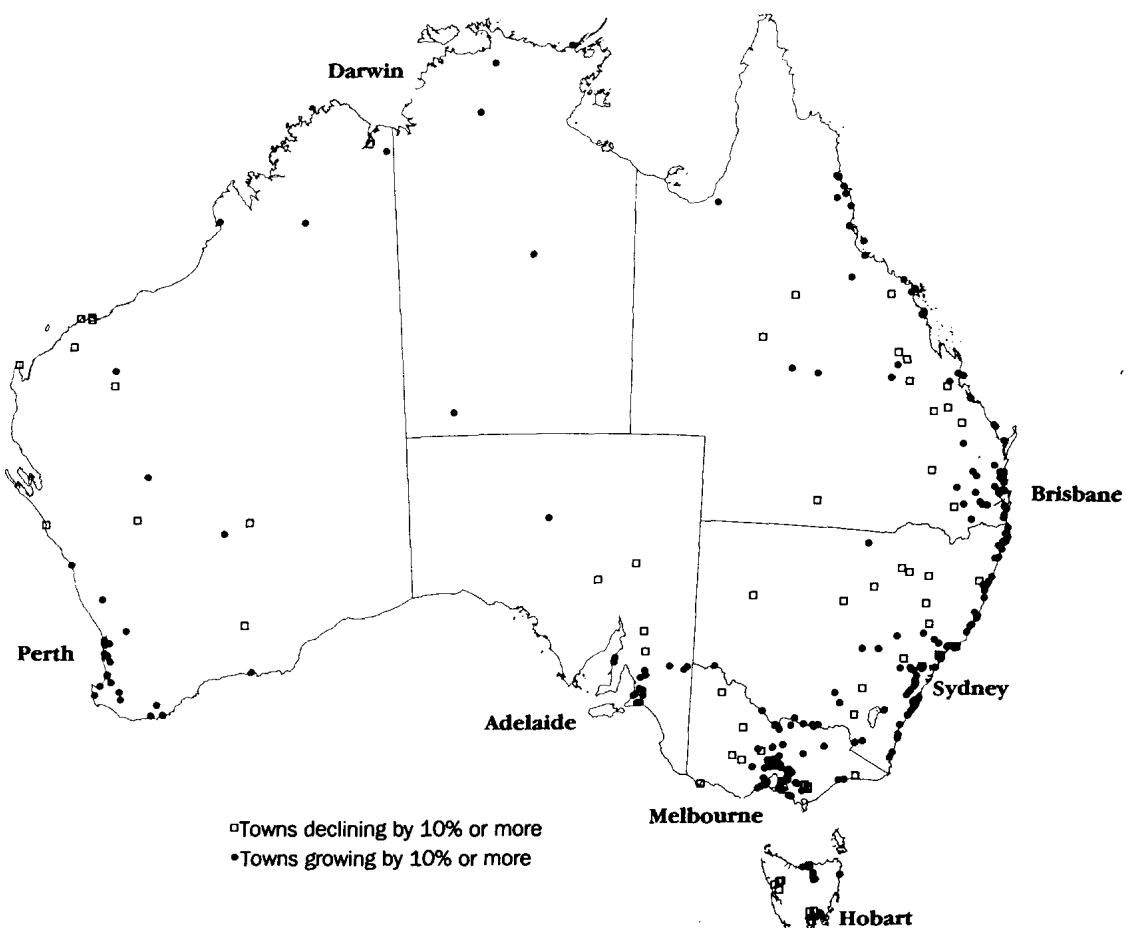
Population growth is concentrated now in or near coastal zones, most notably in Queensland and New South Wales and in the south-west of Western Australia, where horticulture, tourism and other service activities are expanding.

Many inland provincial cities have also grown, but often at the expense of nearby smaller towns. This 'sponge city' phenomenon, whereby people from small outlying communities are drawn to larger regional centres, has been facilitated by improved transport links, more reliable vehicles and the availability of a wider range of, and cheaper, goods and services in larger centres.

There is also a common perception that, across the nation, small towns are withering. Yet, of the 578 towns with a population between 1000 and 20 000 in 1986, almost half grew by more than 10 per cent in the decade to 1996. Most of this growth was in coastal towns, fed in part by changing lifestyle preferences, such as the movement of retirees. The small towns which are in decline are located predominantly in inland Australia.

Economic and social indicators point to the different circumstances of people living in the cities and country regions. People in country Australia tend to have, on average, lower levels of household income, but higher levels of home ownership

Population changes in small towns, 1986–1996



and cheaper rent and mortgage payments. They also have lower levels of tertiary education but higher levels of vocational training. Country regions typically have higher mortality and suicide rates. Nevertheless, country lifestyles continue to appeal to many people.

The experiences of regions in country Australia coping with change are mixed, with some regions doing better than others. High rates of structural change do not necessarily involve employment loss. Similarly, low rates of structural change are not always associated with high employment growth. In country Australia, as well as in metropolitan areas, services have been the main source of jobs growth.

Structural change: characteristics of Australian regions

<i>High change and low employment growth</i>	<i>High change and high employment growth</i>
<ul style="list-style-type: none"> • above-average reliance on mining; • weak representation in service sector; and • employment reductions in manufacturing and mining industries. <p>(eg Lyell in Tasmania and Whyalla and Flinders Ranges/Pirie in South Australia)</p>	<ul style="list-style-type: none"> • diverse industry structures; and • sectoral employment shares close to the national average. <p>(eg Gascoyne/Carnegie and Lefroy in Western Australia and Cairns in Queensland)</p>
<i>Low change and low employment growth</i>	<i>Low change and high employment growth</i>
<ul style="list-style-type: none"> • strong orientation towards agriculture; • little change in reliance on agriculture; and • smallest shares of employment in the service sector. <p>(eg Mildura–Mallee in Victoria)</p>	<ul style="list-style-type: none"> • employment base heavily oriented towards service industries; and • less reliance on agricultural and mining-based activities. <p>(eg urbanised areas and coastal New South Wales and Queensland)</p>

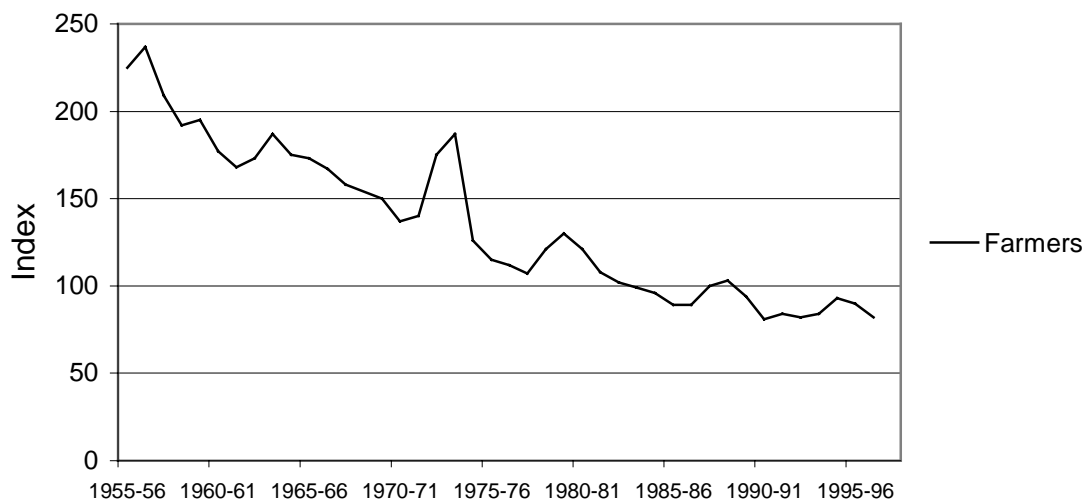
‘Drivers’ of change

Trade and foreign investment have always been important to country Australia. More recently, the increased scale and pace of globalisation have intensified adjustment pressures in some regions and created growth opportunities in others. Forces affecting the fortunes of country Australia include:

- technological advances, such as improved transport and telecommunications, increased mechanisation of farming, agronomic developments and adoption of new mining techniques;
- a downward trend in the world prices for agricultural commodities, which has been reflected in a decline in producers’ terms of trade;

- changes in consumer tastes, such as the decline in the demand for wool and increased expenditure on tourism, which have had markedly different regional effects;
- changes in lifestyle, such as an increase in internal migration to coastal areas; and
- government policy changes, such as lowering trade barriers, deregulating the financial system and increased regulation to protect the environment.

Declining terms of trade for farmers^a



^a Ratio of index of prices received, in Australian dollars, to index of input prices paid.

These forces have contributed to significant changes in the composition of Australia's economic activity, with differing regional implications across country Australia. Notwithstanding the continued growth of agriculture and mining, their combined share of Australia's gross domestic product has declined from 24 per cent in 1948-49 to around 8 per cent today. This decline reflects the rapid expansion of service activities.

In response to these longer-term forces, increases in agricultural productivity have resulted in fewer, but larger, farms. In mining, adoption of new technologies has resulted in significant new investment and the discovery and development of mineral, coal, oil and gas deposits.

The current circumstances of country Australia have been influenced strongly by these broad long-term economic forces. NCP appears to have become a scapegoat for the adverse economic and social effects of these mostly unrelated forces. Indeed,

some governments submitted to this inquiry that it is not possible for NCP to have created the havoc attributed to it because most NCP initiatives are relatively recent.

It is against this backdrop that the impact of NCP needs to be assessed.

What is NCP all about?

NCP extends competition into areas of the economy which have been dominated by government monopolies, typically in the provision of infrastructure, or where competition has been restricted by legislation (eg by statutory marketing arrangements). It also extends and strengthens the coverage of trade practices legislation governing anti-competitive conduct. NCP represents the joint desire of Australian governments to deliver the benefits of competition through a national approach to competition reform. It aims not only to facilitate effective competition to promote economic efficiency and the social benefits which flow from that, but also to accommodate situations where competition conflicts with social objectives.

In practical terms, NCP consists of three agreements between the Commonwealth and all State and Territory governments.

NCP agreements

The *Competition Principles Agreement* sets out principles for reforming government monopolies, prices oversight of government businesses, reviews of legislation, access to 'essential' infrastructure facilities and placing government businesses on a competitively neutral footing with each other and private businesses.

The *Conduct Code Agreement* extends Australia's competitive conduct rules to all businesses — unincorporated businesses were previously exempt.

The *Implementation Agreement* recommits governments to earlier reforms in gas, electricity, water and road transport. It specified a program of \$16 billion in financial grants to State and Territory governments, contingent on implementation of reforms.

Improvements in the performance of government business enterprises and in the provision of infrastructure are important objectives of NCP. Past studies of government businesses identified clearly that:

- they typically suffered from poor management, excessive or inadequate capital investment and over-manning which added considerably to costs;
- the range and quality of goods and services produced often did not meet the needs of users; and
- prices frequently did not reflect the cost of supply.

These enterprises are significant suppliers of inputs, such as energy and transport services, used by the rest of the economy, country and city alike. Poor performance by them imposes a ‘tax’ on users and the economy generally.

NCP reforms to improve the performance of government businesses build on previous reforms and, in broad terms, involve structural separation of:

- competitive elements from ‘natural monopoly’ elements, to promote competition and improve regulation of natural monopolies; and
- the regulatory functions of government from the commercial operations of government businesses.

Other important measures which form part of NCP include the extension of competition rules to all businesses, regimes for access to essential infrastructure and competitive neutrality reforms. There is also an extensive program of review of legislation at all levels of government to remove anti-competitive restrictions which cannot be demonstrated to be in the ‘public interest’.

The ‘public interest’ test provides for non-economic matters (eg social welfare, regional development and environmental concerns) to be taken into account in reviews of legislation which restricts competition, in reforms of government business enterprises and in the introduction of competitive neutrality. The purpose of this test has not always been properly understood or applied. Properly conducted reviews, including careful analysis of public interest matters, can inform policy decisions and help to avoid unnecessary adjustment costs.

Some of the concerns raised with the Commission by people in country Australia about NCP reflect unease at the prospect of a loss of industry assistance or other benefits associated with anti-competitive regulation. But many concerns stem from policies which are not a requirement of NCP, even though they have similar objectives and may lead to the discretionary adoption of policies such as contracting-out and privatisation.

What NCP does not require

- | | |
|-------------------------------------|---|
| • asset sales and privatisation; | • cutting the size of the public sector; |
| • compulsory competitive tendering; | • local government amalgamations; |
| • contracting out; | • reductions in welfare and social services; or |
| • financial market deregulation; | • removing community service obligations. |
| • industrial relations reforms; | |

These misunderstandings are not surprising — the aims and mechanisms of NCP, and its relationship to other policies, have generally not been well communicated to the people most likely to be affected by them. The fact that, in some areas of NCP (eg water reform, competitive neutrality and reviews of statutory marketing arrangements), implementation has proceeded slowly, at differing speeds and with variations in guidelines in different jurisdictions, has compounded this problem.

This lack of adequate information has fuelled serious concerns about many reform measures in country Australia and allowed NCP to be misrepresented. For example, a government may cite NCP as the basis for a decision to contract work in a way which precludes local community participation. Such a decision, however, is a discretionary policy choice by the government concerned, not a requirement of NCP.

The Commission sees a need for a significantly improved community understanding of NCP.

RECOMMENDATION 1

All governments should take steps to ensure that the information they provide about their National Competition Policy undertakings is:

- *accurate in terms of both its content and relationship to other policies; and*
- *publicly available in a readily accessible form and is provided to those implementing, and those most likely to be affected by, National Competition Policy reforms.*

RECOMMENDATION 2

All governments should publish and publicise guidelines which:

- *outline the purpose and scope of the ‘public interest’ provisions of the Competition Principles Agreement; and*
- *provide guidance on how the provisions should be interpreted and applied.*

The common set of basic principles for application of the ‘public interest’ test which is intended to be developed jointly by governments also should be published and disseminated widely.

(Chapter 11, pp. 321, 328)

Consistent with the need for a better understanding of NCP, fears could be allayed if panels conducting reviews of major legislation were given clearer operational guidelines. Furthermore, major reviews of anti-competitive legislation in a

particular State should have regard to possible effects on Australians as a whole, not merely those on people of the State in question.

RECOMMENDATION 3

Governments should require major legislation reviews to go further than simply determining compliance or otherwise with National Competition Policy principles. Reviews should be based on genuine public input, be conducted in a transparent manner, outline the likely distribution of costs and benefits, and inform interested parties why and how reform, or maintenance of the status quo, will lead to superior outcomes and performance than the alternatives.

RECOMMENDATION 4

In the case of reviews of anti-competitive legislation which may have significant impacts extending across jurisdictions, the benefits and costs should be weighed in terms of the interests of Australians as a whole.

(Chapter 11, pp. 322, 330)

There is provision under NCP for the National Competition Council (NCC) to conduct reviews of Commonwealth or nationally significant State legislation. A possible conflict of interest for the NCC may arise here because the NCC is also responsible for monitoring each jurisdiction's compliance with their NCP commitments and for making recommendations to the Commonwealth Treasurer on competition payments. It would be more appropriate for reviews of Commonwealth legislation (and nationally significant legislation reviews) to be conducted by bodies which are seen to be at arm's length from NCP assessment processes.

RECOMMENDATION 5

The National Competition Council should no longer be asked to conduct legislation reviews.

(Chapter 11, p. 341)

Some participants, including some governments, argued that certain NCP reforms are being implemented too quickly.

Control of NCP rests with governments and they have used fora and processes to consider and, where necessary, modify specific implementation schedules. The evidence suggests that these procedures are working. The review of NCP by the Council of Australian Governments, which is to take place at some time after April 2000, could consider such issues.

RECOMMENDATION 6

At this juncture, there should be no across-the-board extension of the National Competition Policy target dates.

(Chapter 11, p. 335)

Structural reform of public monopolies, particularly in infrastructure areas where market power is an issue, has been accompanied by the creation of new regulatory agencies, and a widening role for existing regulatory agencies under NCP. In view of the importance of these agencies in achieving benefits from NCP, the Commission considers it appropriate that they be monitored and reviewed periodically.

RECOMMENDATION 7

All jurisdictions should ensure that their regulatory agencies responsible for the oversight of National Competition Policy-related reforms are subject to periodic independent review to ensure that they are performing appropriately.

(Chapter 11, p. 339)

Country and metropolitan effects of NCP

There are a number of intractable problems in assessing, in any comprehensive way, the benefits and costs of NCP. In large measure, this reflects the problems involved in isolating the influence of a specific, but wide-ranging, set of policy reforms from the array of other factors which affect economic and social conditions.

Notwithstanding these difficulties and the limited progress in some reform areas, it is possible to observe some significant impacts of NCP in specific sectors, such as those stemming from infrastructure reforms. While some broad trends are evident, there is considerable variation between reforms and between jurisdictions. For some reforms, there appear to be different effects in country and metropolitan areas.

Costs and prices

Costs and prices are affected by many factors unrelated to NCP, including technological changes and shifts in consumer preferences. Even so, there is

evidence of improved productivity from NCP reforms, leading to reductions in costs and prices across most infrastructure services which have been subject to competition reforms. These include electricity, gas, rail, ports and telecommunications, all of which are important inputs to other industries throughout the economy, including those in country areas. At the same time, prices of some services have risen to reflect more closely the costs of their provision.

To date, many of these reforms have produced greater cost reductions for large rather than small businesses, and for business users rather than residential customers in both metropolitan and country areas. Benefits are expected to spread to smaller users over time, although prices for some users will remain dependent upon the maintenance of community service obligations. Furthermore, the improved competitiveness of businesses which supply smaller regional firms and consumers is likely to be of indirect benefit to country communities. Costs and prices are likely to be reduced in those communities, and output and employment increased.

Customers in most States have had substantial reductions in electricity prices in real terms during the 1990s. Since the establishment of the national electricity market, prices have fallen further, although some question the sustainability of such low prices. In the case of gas, country Australia has benefited from the extension of the gas network and associated opportunities for existing and new business, as well as

Illustrative cost and price changes

<i>Reform area</i>	<i>Cost/price change</i>	<i>Period/date</i>	<i>Markets affected</i>
	%		
Electricity	↓16	1991-92–1997-98	Australia — real (inflation adjusted) average prices all customers
	↓22	1991-92–1997-98	Australia — real average prices all commercial/ industrial users
	↓3	1991-92–1997-98	Australia — real average prices all residential users
Gas	↓43	1992–1997	Six major distributors — real controllable costs
	↑7	1991-92–1996-97	Vic — real prices for residential customers
	↓22	1994–1998	Australian gas prices — industrial and residential
Water	↓30	1991-92–1996-97	NSW — real prices for metropolitan customers
	↓10	1991-92–1996-97	Vic — real prices for metropolitan customers
	↑8	1991-92–1996-97	Tas — real prices for metropolitan customers
Rail	↓40	1991-92–1996-97	Freight rates on the Melbourne to Perth rail route
	↓16	1991-92–1996-97	National rail freight rates (in real terms)
Ports	↓23	1991-92–1996-97	Port authority charges
Telephone	↓25	1991-92–1996-97	Subscriber trunk dialling calls
Postal	↓9	1991-92–1996-97	Australia Post — real price of posting a standard letter

for households.

Water reforms are a more complicated area. Because water is relatively scarce in some regions of Australia, and given the widespread incidence of cross-subsidies between different users, some price rises have occurred. There is no clear picture yet on costs and prices of rural irrigation services. In some regions, the introduction of tradable water entitlements is allowing water to be allocated to higher value uses, with significant benefits for sellers and purchasers. In others, this element of reform is proving difficult.

Fears exist that the agreed reform principles for investment in new rural water supply schemes and extensions to existing schemes could limit worthwhile regional development. Given the large expenditure involved, it is important that properly conducted benefit–cost studies of such schemes be published, and that the nature and magnitude of any social and environmental benefits and costs be clearly identified.

One issue which may arise from this process relates to the financing of these investments. NCP requires that the total costs of new water infrastructure be fully recouped over the economic life of the project. However, NCP recognises that early users of such infrastructure should not be expected to bear all of the large initial capital costs. Moreover, operating losses will be usual in the early years as development is undertaken, and do not in themselves invalidate the possible long-term net benefits.

RECOMMENDATION 8

All benefit–cost studies of major new water infrastructure investments should be publicly available and clearly identify the nature and magnitude of any social and environmental benefits and costs.

(Chapter 5, p. 145)

It is difficult to determine cost and price effects of changes to statutory marketing arrangements because many reviews have not yet been completed. As the arrangements typically were designed to assist some rural producers, review outcomes which lead to the dismantling of such arrangements will disadvantage some, though not all, producers.

In some instances, the impact on producers may be large and regionally concentrated, and could pose adjustment difficulties for affected communities. At the same time, users and consumers in country and metropolitan areas are likely to gain.

In the case of local government, it is too early for the effects of NCP reforms to have emerged fully. As a result of the requirement that councils review their operations to comply with competitive neutrality principles, many have developed better information systems and achieved cost savings from improved management of business activities. This pattern applies in country areas as well as in the cities. For some smaller rural shires, however, the up-front transitional costs could outweigh any potential long-term benefit. Efforts by State governments to inform councils of how to comply with these requirements should help to avoid such outcomes.

NCP does not prohibit the provision of subsidised services for country or metropolitan communities. It seeks to have them identified, costed and provided in a transparent manner so that they can be evaluated against other social priorities.

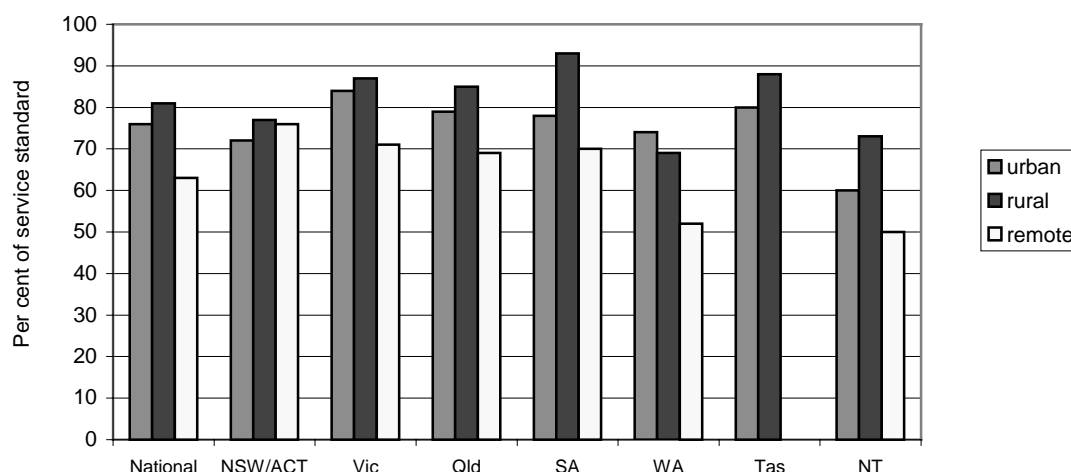
This increased transparency clearly involves the risk that subsidies will be reduced or discontinued. Indeed, as a result of the identification of such services under legislative reviews, some governments have moved away from cross-subsidies to more 'cost-reflective' pricing and direct subsidies to selected groups. This is a matter for political resolution in the jurisdiction concerned. NCP should not be used as an excuse by governments to abrogate their responsibilities for the provision of adequate services to country communities.

Service quality

The available evidence on the quality of service provision suggests different outcomes in different areas:

- Telstra's connection service for new country customers has improved to a level above that for metropolitan business customers, but is still below that for metropolitan residential customers;
- since the introduction in January 1998 of minimum service standards which vary by geographic area, the fault repair service provided to Telstra's customers in remote areas has been relatively poor, but rural customers have generally fared better than urban customers;
- indicators of Australia Post's service standards and quality, including the number of retail outlets, remained high over the period 1991-92 to 1996-97;
- in New South Wales and Victoria, for instance, loss of electricity supply and average duration of outage have generally been reduced for urban customers, but the trend for country Australia is unclear; and

Telstra's fault repair service, 1998



-
- in some States, urban water reforms have resulted in generally improved levels of service and improvements in the quality of water delivered. There is also evidence of reduced waste and increased attention to environmental allocations.

Jobs in country Australia

Between 1981 and 1996, employment in country Australia increased by 22 per cent to 2.32 million — a similar proportional increase to that which occurred in metropolitan areas.

That said, the early direct effects of NCP reforms on employment appear to have been adverse. To some extent, this reflects the removal of overmanning which had developed while government business enterprises enjoyed monopoly status or faced weak incentives to perform efficiently. As the broader effects of the reforms work to expand the nation's economy, the employment picture is likely to improve, but regional outcomes will differ. The early direct effects include:

- between 1992 and 1997, employment in regional and urban electricity supply was reduced by around 23 000 employees, or 38 per cent. Some of this fall was offset by increased employment of contractors;
- between 1992 and 1997, six major gas distributors reduced employment by 3400 jobs, some 42 per cent of their workforce. The majority of those losses were in metropolitan areas. Some have been offset by the increased contracting-out of services and work associated with the expansion of gas networks into country Australia;

-
- the closure of railway workshops in country areas led to a substantial loss of local employment in communities such as Port Augusta. In the decade to 1998, rail employment in capital cities was reduced by 44 per cent. In other areas, it was reduced by 73 per cent; and
 - labour shedding in telecommunications has also been occurring for some time — reflecting the uptake of new technology as well as reduction of overmanning. In the decade to 1997, Telecom/Telstra employment declined by 18 per cent. Part of this has been offset by employment creation in new service providers. There is no evidence that labour shedding has been proportionately higher in country areas than in metropolitan centres.

Among local governments in country Australia, there is a widely held view that the introduction of competitive neutrality will mean a loss of local jobs to private businesses outside the area, thereby compounding the loss of activity in vulnerable communities. Most concerns relate to local councils' losing bids for State contracts (especially roadworks) — but this is primarily a contracting-out, rather than NCP, issue. Some rural councils have used the 'public interest' provisions of NCP to retain certain services in-house in order to preserve local employment. In these circumstances, job losses resulting from contracting-out would need to be balanced against the benefits of having council work performed at lower cost, which can lead to lower rates and/or expanded services.

Three other issues affecting the economic and social conditions of country Australia, though essentially not part of NCP, were of concern to participants — the growth in market share of major supermarkets, bank branch closures and the possible effects of deregulation in the petroleum industry.

Evidence available to the Commission suggests that major supermarket chains have been responding more effectively than smaller retail stores to customers' preferences. They have provided more convenient access to a wider range of goods and services, often at lower prices, as trading hours have expanded. This has been at the expense of business opportunities for some traditional small retailers. At the same time, new opportunities have arisen for efficient suppliers of fresh foods and for other retailers.

Bank branch closures have been part of the decline of some small country towns. The spread of newer bank technologies and the deregulation of the financial system have reduced the demand for and supply of traditional banking services and seen the emergence of new financial services and new ways of providing traditional services. While benefiting many, it has disadvantaged some, particularly people reliant on traditional banking services in those small rural communities where all branches have been closed and only of limited range of replacement services have emerged.

The deregulation of the petroleum industry, which is currently being implemented, is intended to increase competition and benefit motorists. This has happened already in some areas, with the advent of independent petrol retailers such as Woolworths bringing about reductions in petrol prices in country and metropolitan areas. As in the case of bank branch closures, some small country communities will be adversely affected, in terms of local employment and convenience, by the closure of service stations.

Assessing longer-term effects

In addition to the identifiable direct initial impacts, NCP reforms will have enduring economy-wide effects on output, incomes and employment. Using the MONASH regional economic model, the Commission has sought to illustrate these effects, and also the possible long-term implications for metropolitan and country regions of the NCP reforms. Such models cannot depict with precision the actual effects on small regions of policy changes as broad-ranging and complex as the NCP. Nonetheless, modelling can provide some insights about possible results, especially flow-on or indirect effects.

The model estimates that, in the long-term, NCP is likely to mean that national output will be in the order of 2.5 per cent higher than otherwise — an amount equivalent to almost one year of economic growth. This is less than was estimated by the Industry Commission in the lead-up to the 1995 NCP agreement, largely because NCP reforms are less extensive than the list of possible reforms modelled at that time.

The model does not capture the dynamic efficiency gains which are expected to flow from NCP reforms (eg changes in business behaviour which result in sustained improvement in productivity growth). Furthermore, the model assumes no change in the unemployment rate. If this conservative assumption was varied to allow some aggregate employment growth as a consequence of the output growth, the long-run gains would be higher.

The estimates of the long-term effects from the model indicate considerable variability across regions as a result of the NCP reforms. Individual reforms are estimated to produce different effects, which also differ across regions. Overall, a wider dispersion is estimated among country regions than in metropolitan areas in terms of output, employment and average income per person employed. Metropolitan areas are estimated to experience increases in output close to the national average, better than average employment outcomes and below average increases in incomes per person employed. By each measure, some country regions

Estimated regional effects of NCP from model

Overall:

- only one of the 57 regions modelled is estimated not to benefit from NCP in terms of output;
- all regions are estimated to benefit in terms of average income per person employed; and

with no change in aggregate employment assumed:

- in the majority of regions, the estimated effect of NCP is either to increase employment or to reduce it by an amount which would be absorbed by less than one year of recent employment growth;
- in five of the 57 regions, five or more years of recent (relatively slow) growth would be needed to offset job losses from NCP;
- there are nine regions which lost jobs over the decade to the mid-1990s and which are estimated to experience further declines in employment as a result of job relocation associated with NCP reforms; and
- collectively, these 14 regions account for 25 per cent of Australia's land area, but only 6 per cent of national employment.

are estimated to gain more, and some less, from NCP reforms than metropolitan areas.

Estimated effects of NCP derived from modelling are only broadly indicative. Nonetheless, together with other available evidence, including costs associated with implementing some reforms, they support the Commission's assessment that there will be net benefits for Australia as a whole from NCP. Country Australia as a whole is likely to benefit from NCP, although there is likely to be more variation in the incidence of benefits and costs among regions. The Commission notes that, to date, the reforms implemented have provided greater benefits to large businesses in all areas and to people in metropolitan areas.

The effects of NCP reforms on most, but not all, regions are likely to be less significant than those resulting from the broad economic forces continually reshaping economic and social conditions in Australia. Failure to continue to implement NCP reforms will not stop the operation of these forces, but would deny the community the benefits of the reforms.

In country Australia, the benefits of NCP reforms are facilitated, and costs mitigated, by certain measures which are in place to meet the economic and social needs of rural and regional communities. These include measures to limit anti-competitive behaviour in the generally 'thinner' markets, such as provisions of the

Trade Practices Act, measures which provide State and Territory governments with the financial capacity to provide ‘average’ standards of services to their citizens, and explicit community service obligations which provide access to, and delivery of, infrastructure services at prices below the cost of supply.

More recently, in part in response to the adverse effects on country people of rationalisation of some government services, including that arising from NCP, the Commonwealth Government has acted to improve access to services. Measures taken include the establishment of rural transactions centres and increased incentives for doctors to set up practices in country areas, as well as better access to modern telecommunications technology.

The Commission sees a greater role for governments in helping to overcome information gaps about prospects for investment and employment, facilitating self-help initiatives, removing impediments to development and improving policy coordination.

Adjustment issues in country Australia

The conclusion that NCP reforms are producing benefits overall for metropolitan and country areas does not mean that adverse effects of some reforms on some country communities should be ignored. Governments have at their disposal policy instruments to mitigate such effects.

Coping with change

While NCP can be viewed as an overlay on an environment of continual change, it is also a *source* of change. In some instances, it may exacerbate negative economic and social consequences of other factors affecting particular regions.

If adjustment pressures develop rapidly and are regionally concentrated, generally available assistance programs may prove to be deficient. Governments may need to consider whether, on a case-by-case basis, additional specific forms of adjustment assistance are warranted to help people in communities adversely affected by change, including by NCP reforms.

In considering adjustment assistance, governments should ensure that there is effective coordination between agencies in dealing with adjustment problems, effective consultation and community involvement to ensure informed local input, and appropriate monitoring of outcomes to ensure that lessons are learnt from experience.

The extent of any adjustment problems arising from NCP reforms which could warrant such additional adjustment assistance is difficult to gauge in advance. Some of the adjustment, at least in terms of job losses from (pre-NCP) reforms of government businesses, has already occurred. However, some job losses associated with infrastructure reforms may have adverse social effects in country communities where job opportunities are limited. Reform of some statutory marketing arrangements could also create concentrated adjustment problems for certain communities.

Implementation of major NCP reforms should have regard to whether additional measures to facilitate adjustment are required to address large regionally concentrated costs. In doing so, the difficulties of identifying those in genuine need and of delivering assistance to them effectively need to be recognised.

Often, generally available measures, such as social welfare payments, job placement services and general support for (re)training will be sufficient to manage the adjustment burden. This approach has certain advantages in that it:

- treats individuals in similar circumstances equally;
- addresses the *net* effect of reforms and concentrates on those in genuine need; and
- supports families and individuals rather than a particular industry or activity.

Of course, this assumes that current assistance programs are effective in targeting basic needs across regions. It is important to ensure that such programs are performing appropriately in this respect.

RECOMMENDATION 9

Governments should rely principally on generally available assistance measures to help people adversely affected by National Competition Policy reforms. The effectiveness of these measures should be kept under review.

RECOMMENDATION 10

Where governments decide that specific adjustment assistance is warranted to address any large, regionally concentrated costs, such assistance should:

- ***facilitate, rather than hinder, the necessary change;***
- ***be targeted to those groups where adjustment pressures are most acutely felt;***
- ***be transparent, simple to administer and of limited duration; and***
- ***be compatible with general ‘safety net’ arrangements.***

(Chapter 13, pp. 377, 395)

Findings

Part A Developments in country Australia

1. A large proportion of the fastest-growing large country municipalities and smaller towns are located along the coast. Those experiencing falling population are predominantly in the interior or have economies dominated by a declining industry. While there are many inland towns and cities whose population is increasing, population growth in most small inland towns is below the national average. *(chapter 2, p. 26)*
2. Many wheat and sheep farming districts often have a growing provincial centre or 'sponge city'. In part, the growth of the provincial centre is the result of the relocation of population from farms and smaller towns in the surrounding districts. *(chapter 2, p. 28)*
3. Population growth in coastal regions is closely linked with growth in employment in the service industries and in the number of older and unemployed persons. Other areas of country Australia, on average, are experiencing slower population growth, in part linked to slow growth or contraction in employment in agriculture and services. *(chapter 2, p. 31)*
4. By some measures, people in country Australia have lower incomes relative to those in the cities, and the difference appears to be increasing. Educational attainment is lower, although there is a higher proportion of people with vocational training. On average, the unemployment rate is also higher in country Australia. The picture is a diverse one, with some regions doing much better than others. *(chapter 2, p. 39)*
5. Since the early 1970s, changes in the overall structure of the Australian economy have followed the broad pattern of development of most developed economies. Notwithstanding the absolute growth in output of agriculture, mining and manufacturing, their shares of gross domestic product have declined, while that of the services sector has risen. *(chapter 3, p. 51)*
6. Since the early 1980s, both the level and the variability of structural change has been greater in country Australia than the cities. *(chapter 3, p. 60)*

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7. High rates of structural change in country Australia do not necessarily involve employment losses. Similarly, low rates of structural change are not always associated with high employment growth. *(chapter 3, p. 60)*
 8. Broad long-term economic forces which are beyond the control or influence of governments have been key drivers of the economic and social changes of particular relevance to country Australia. These include: changing technology and increasing productivity; rising incomes and changing lifestyles; and declining world agricultural and mineral commodity prices. *(chapter 3, p. 78)*

Part B The National Competition Policy Reforms

9. In regional Australia, large users of electricity have enjoyed significant reductions in usage charges. As access to the contestable market (ie ability to choose supplier and negotiate price) is extended, direct price benefits for other businesses and households should also occur. Employment in the sector has fallen in both urban and regional areas. *(chapter 5, p. 118)*
10. The main impact of NCP gas reforms in urban areas has been a rebalancing of usage tariffs between businesses and households, which has seen large price falls for business users and more modest falls for households in all States except Victoria, in which there have been modest increases. For country Australia, the main benefit has been the stimulus provided by the extension of the gas network and the associated opportunities this has created for existing and new businesses. *(chapter 5, p. 131)*
11. NCP water reforms have resulted in significant increases in charges for many users, particularly irrigators. Notwithstanding improvements in the efficiency of service delivery, these increases are likely to continue. At the same time, the reforms are providing benefits to the environment through, for instance, greater incentives to reduce wastage, thereby leading to more efficient investment in water infrastructure. However, more progress on reforms intended to improve water property rights and their tradability is necessary in order to enhance the prospects of achieving a net increase in the value of agricultural output. *(chapter 5, p. 159)*
12. The modest progress in road transport reform has meant that the projected benefits have yet to be fully realised in both country and city areas. Nonetheless, country areas have derived some benefit to date from the reductions in regulatory overlaps and inconsistencies between jurisdictions. Also, better road access for newer technology, such as B-doubles, and increased competition have seen productivity increase and freight rates fall. *(chapter 5, p. 168)*

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13. Rail reforms have produced significant benefits for the economy in general and particularly for users in country Australia. This has involved job losses. Full-time employment in the rail industry has declined more rapidly in country Australia than in the capital cities, with adverse effects on certain rural communities. *(chapter 6, p. 175)*
 14. Competition in telecommunications has seen prices fall for both country and metropolitan customers. However, service quality outcomes in all areas have been mixed. *(chapter 6, p. 182)*
 15. The process of reviewing statutory marketing arrangements is well under way, but, to date, relatively few of these reviews have been completed or reforms implemented. Consequently, it is too soon to assess the effects of these reforms. *(chapter 7, p. 201)*
 16. The range of conflicting views on the validity and effectiveness of statutory marketing arrangements reinforces the importance of NCP in requiring the review of such arrangements in order to assess whether they benefit the community as a whole. *(chapter 7, p. 213)*
 17. Misperceptions about the scope and implementation of competitive neutrality, and in particular the application of the ‘public interest’ test, suggest that early efforts by governments to inform those affected by competitive neutrality were inadequate. Additional efforts by governments have gone some way to counter these lingering misperceptions in the public and private sectors, but continuing measures are still necessary. *(chapter 8, p. 238)*
 18. Changing social patterns (such as more flexible working hours, the increase of women in the workforce and single parent households) have contributed to decisions by governments to make shopping hours more flexible. These more flexible retail trading hours have weakened the competitiveness of some retailers. At the same time, they have been of net benefit to consumers and appear to have increased employment, including in country Australia. *(chapter 9, p. 260)*
 19. The potential for legislation reviews to introduce important changes affecting people’s lives and livelihoods highlights the need for integrity in the review process, including the operation of the ‘public interest’ test provisions of NCP. *(chapter 9, p. 266)*
 20. As the reviews of legislation governing professions in most jurisdictions have yet to be undertaken, NCP has had little impact overall to date on the provision of professional services in country Australia. *(chapter 9, p. 268)*

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21. There are a number of reasons why petrol prices are always likely to be higher in the country than in the cities. These include less competitive markets, the cost of transporting petrol from refineries and the more limited scope to sell large volumes of petrol at smaller profit margins. *(chapter 9, p. 277)*
 22. Infrastructure services represent significant costs for industries based in country Australia. NCP reforms affecting the provision of these services are producing productivity gains which, although leading to some employment losses, have helped to make user industries more competitive and benefited consumers. *(chapter 10, p. 293)*
 23. There would appear to be significant gains for the Australian community, and for country Australia as a whole, from implementing NCP reforms. The reforms are likely to have a more varied effect in country regions than in metropolitan areas, with implementation costs of some reforms being more evident in the former. *(chapter 10, p. 306)*
 24. The effects on most, but not all, regions of the NCP reforms are likely to be less significant than those resulting from the broad economic forces which are continually reshaping economic and social conditions in Australia. *(chapter 10, p. 308)*

Part C Improving National Competition Policy and achieving better outcomes for country Australia

25. Many people have a poor understanding of NCP and its effects. As a consequence, it has been blamed for adverse social and economic impacts resulting from a range of sources. This state of poor knowledge involves a risk that worthwhile reforms may be forgone and actions to overcome problems may be misdirected and ineffective. *(chapter 11, p. 315)*
26. Without a clear delineation of responsibility for reform initiatives, there is scope for jurisdictions not to take responsibility for potentially unpopular discretionary actions, but rather to imply (explicitly or implicitly) that they are required to do so under NCP. *(chapter 11, p. 321)*
27. The manner by which restrictions on competition may be considered under NCP is not well understood by many people. This is consistent with a wider lack of effective communication about, and hence appreciation of, what constitutes NCP and how it is implemented. *(chapter 11, p. 324)*

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28. Control of NCP rests with governments which have used forums and processes to consider and, where necessary, modify NCP implementation schedules. The evidence suggests that these processes are working.
(chapter 11, p. 335)
29. NCP does not mean that the provision of community service obligations to country Australia must be curtailed. However, it will enable the wider community to assess, in a transparent manner, the costs and benefits of providing these services.
(chapter 12, p. 354)
30. The provision of community service obligations reflects political judgements about the equitable provision of services to people throughout Australia. The Commission's recommendations relating to better provision of information about NCP should help to ensure that governments do not abrogate their responsibilities to provide an 'adequate' level of services to communities in country Australia by claiming that cost-cutting measures are dictated by NCP.
(chapter 12, p. 354)
31. There may be a case for specific adjustment assistance packages where a concentrated adjustment shock occurs rapidly and is large relative to the size of a community. The decision to proceed with assistance will be influenced by the (direct and indirect) costs and benefits of an adjustment package tailored to a particular regional change relative to the costs and benefits of relying on general measures.
(chapter 13, p. 383)
32. There is significant scope to improve the management of the reform process in country Australia through:
- genuine and effective community consultation;
 - governments co-ordinating their responses to adjustment difficulties; and
 - monitoring of outcomes.
- (chapter 13, p. 391)*
