

7 March 2001

Mr Neil Byron  
Presiding Commissioner  
Productivity Commission  
Locked Bag 2  
Collins Street East  
MELBOURNE VIC 8003

**RE: Review of the Prices Surveillance Act 1983**

Dear Mr Byron

CSR's Managing Director, Mr Peter Kirby, has asked me to respond to your letter of 15 January 2001 which attached a copy of the Productivity Commission's Interim Report on the review of the *Prices Surveillance Act 1983*.

Specifically the Commission has asked for information on the cost impact, in CSR's experience, from the implementation of the Act.

As you would know, CSR has had two of its products directly affected by prices surveillance control under the Act: concrete tiles from 1985 to 1995 and pre-mixed concrete from 1986 to 1991. We have also had one product indirectly affected, this being Portland cement through our 50% owned subsidiary, Australian Cement Holdings, from 1986 to 1994.

Overall it is CSR's strong view that there is no need for such monitoring and control of prices in a competitive market, that is where goods and services are subject to normal market forces exercised by consumers and producers.

We do however recognise, as identified in your interim report, that the Act now primarily deals with pricing by companies with significant market power (usually arising from a natural monopoly), in substantial markets or during a transition from a legislative monopoly to a competitive market.

As a general comment the interim report canvasses in good detail the issues CSR faced in addressing prices surveillance and we agree with all four interim findings contained in the report notwithstanding our primary view on prices surveillance.

In response to your specific request on cost information, you will no doubt understand that our last activities with the Prices Surveillance Authority were in the mid-1990s and information and corporate knowledge of our experience is not widely held.

We can however make the following limited observations for your inquiry on concrete tiles and pre-mixed concrete.

**Concrete tiles**

In 1989 CSR with Redland PLC (49%) of the United Kingdom formed Monier PGH Ltd (50% CSR) which included the Monier concrete tile business as well as the PGH clay brick, paver and pipe business. In 1995 CSR purchased Redland's 49% share of the company.

The Prices Surveillance Authority (PSA) inquiry (Report No 62, 1995) covered many issues which showed concrete tiles to be a competitive and open market, including the ease of substitution in roofing and low barriers to entry on most fronts (technology and access to raw materials).

A review of the few remaining CSR files on this case shows that CSR did delay investment in this business, principally in Victoria, during the period of the prices surveillance activities on concrete tiles (Monier was the only concrete tile producer under surveillance during the period of 1985 to 1995).

Specifically:

- Monier delayed the development of a public and trade selection centre in Victoria due to poor returns from a low regulated price. About a \$3 million investment was required for the facility. A regional sales centre was subsequently built after a successful submission under the Act per 'profit recovery' provisions for "investment and employment" purposes. At the time the two other main competitors in the Victoria market had six such centres and Monier was suffering loss of market share because of the lack of such centres and package deals offered at such centres. The prices surveillance regime in this case effectively delayed an investment decision which in the normal course of events would have occurred earlier to meet consumer purchasing preferences.

During this time Monier typically invested between \$1-\$2 million annually and directly into the concrete tile business for the purposes of staying in business.

- In a similar example, improving profits were necessary before Monier could justify expending about \$50 million to build a facility to manufacture clay bricks and pavers in Victoria. Profits from sales in Victoria as regulated by the PSA were such that this investment could not be seriously considered and ultimately was not pursued.

Another relevant issue is that the PSA focused on unit cost increases over a set period as a basis for regulating prices. During the early 1990s when the construction industry in general was in decline, conditions were such that full unit cost increases could not be passed onto the market and had to be absorbed by Monier. **The lack of a longer term view by the PSA of the cyclical nature of the industry impacted on the company's ability to sustain profits across the business cycle.** This in turn impacted the scope of investment decisions and, importantly, affected the company's general competitiveness and ability to prepare for returning customer demand.

#### Pre-mixed Concrete

CSR entered the quarrying and pre-mixed concrete business in 1965 with the acquisition of 50% of Ready Mix Concrete Ltd.

The pre-mixed concrete business differs from the concrete tile business in that investment in concrete batching plants is justified on the grounds that it broadens the avenues available to sell additional volumes of quarry products.

Like the concrete tile business, the barriers to entry are low, with low capital costs and common technologies. Under these conditions the ability to differentiate the product is limited and strong price competition exists between suppliers.

**The main characteristic of prices surveillance in the concrete business was however that prices realised in the market were generally always lower than the average prices endorsed by the PSA<sup>1</sup>.**

Another feature, as noted by the PSA<sup>1</sup>, was the continued investment in the industry in the face of declining and relatively poor rates of return.

*These outcomes were a feature of the vertical integration between the manufacture of quarry products and concrete batching which characterises all major participants in the market. Costs and income from both operations are often averaged across the businesses, a factor well recognised by the PSA<sup>1</sup>.*

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<sup>1</sup> Ahmed Rushdi (1991) Prices Surveillance in Vertically Integrated Multi-Grade Firms: A Case Study of Australian Pre-mixed Concrete Industry. A paper presented to the 20<sup>th</sup> Economists Conference, Hobart 1991.

Generally, in terms of impacts on CSR's 'costs', prices surveillance did not unduly affect investment, however direct compliance costs were considered onerous, estimated at five weeks per submission for an individual State. This was primarily because of the wide variety of products available to customers and the high number of individual sites. This was a direct response to customer needs and a reflection of competition in the market place.

In the case of pre-mixed concrete, the activities of the PSA, as indicated by higher regulated prices than actual prices, were at odds with the reality of the market place and the nature of the concrete business as a closely linked value adding process to the quarry business.

### **Other comments**

As a general comment there only appears to be limited specific evidence available of the cost impact of the Act on CSR's activities. This is because the Act influenced business decisions almost on a day to day basis. The overall pervasiveness of a regulated and legally binding price was top of mind and was a 'given' - the impact of which did not need to be documented or necessarily assessed. This observation is based on the anecdotal views of CSR management involved with the Act at the time.

As another general comment, in CSR's experience the implementation of the Act rarely appeared able to fully appreciate the characteristics of the market which it was trying to regulate. This was mainly a result of the complexity of the particular market (i.e. range of products, variable size of customers, State differences, cyclical nature).

This led to frustration in supplying information to the satisfaction of the PSA, but also meant that the regulation was based on a partial and at times artificial assessment of the real market and its linkages. Because companies like CSR had no option but to follow the ruling from the PSA, this meant investment and other commercial decisions were equally made with imperfect and some times artificial information.

CSR trusts this assists with the Commission's deliberations on its interim findings and thanks the Commission for the opportunity to make this submission. As outlined earlier, CSR is of the view that there is no need for such monitoring and control of prices in a competitive market.

If you have any enquires please contact me on 02 9235 8040.

Yours sincerely,

Debra Stirling  
*General Manager Corporate Affairs & Investor Relations*