The role of competition policy in structural adjustment

An overview of recent Australian structural reforms

Joe Dimasi

Executive General Manager – Regulatory Affairs Division

Australian Competition and Consumer Commission

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Introduction

- Australia undertook major reform in National Competition Policy (NCP) in early 1990s
- Was a response to concerns about Australia's poor economic productivity performance
  - GDP per capita and GDP per hour were ranked 16th out of OECD member countries
- NCP followed an independent review (Hilmer review)
- Focus of reforms was competition: competition was recognised as a means of enhancing community welfare by promoting a more efficient use of resources

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Overview of the reforms

- Reforms included:
  - The creation of an economy wide competition law
  - Competitive neutrality between government and private enterprises
  - Removal of regulatory restrictions to competition
  - Structural reform of public monopolies
  - Access to essential facilities
  - Prices oversight to constrain monopoly pricing

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Economy wide competition law

- In Australia, anti-competitive conduct rules (e.g. prohibitions on anti-competitive agreements, misuse of market power and certain mergers) are embodied in the *Trade Practices Act*
- The reforms gave these laws economy-wide application: due to constitutional law issues, these laws did not previously apply to state owned business enterprises or unincorporated associations
- Economy-wide application enables a consistent and uniform application of competition law
- Process in place to authorise anti-competitive conduct where competition benefits may not be sufficient to offset other social costs

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Competitive neutrality

- Despite competitive neutrality at law, governments could still confer financial advantages upon their own businesses
- When operating in markets where private operators are present, governments agreed to a set of competitive neutrality principles, including:
  - Charging cost reflective prices, adopting corporate models, paying or making allowances for government taxes and commercial borrowing rates, and complying with the same regulations as private businesses
- These principles expressly did not apply to non-business, non-profit activities of government businesses
- Important as governments increasingly contracting with private operators to provide services

Removal of regulatory restrictions

- Despite economy-wide application of the *TPA*, regulatory barriers may impede emergence of competition in certain markets
  - E.g. legislated monopolies for public utilities, statutory marketing schemes and professional licensing arrangements
- Governments agreed to a systematic review of existing legislation
  - Restrictions on competition to be removed unless the benefits as a whole outweigh the costs and restricting competition was the only way to achieve those benefits
- Establishment of institution (National Competition Council) to monitor progress

Structural reform of public monopolies

- An economy wide competition law can protect competition but it cannot create competition in industries that lack a competitive market structure
  - E.g. gas and electricity industries were traditionally vertically integrated and mostly state owned monopolies
- Governments agreed to structural reform of public monopolies to separate the contestable and non-contestable elements
- The policy did not require governments to privatise their activities, but did require a transparent process to identify functions or activities that should stay with government, if the business was privatised or corporatised

Access to essential facilities

- Competition may still not be possible in markets with ‘natural monopoly characteristics’
  - Problem common to a lot of network infrastructure
- To compete in related markets, new entrants need access to existing infrastructure
- Governments agreed to a national third party access regime for facilities that could not be economically duplicated and were of national significance
- Purpose was to create competition in industries dependent upon that infrastructure, not competition within the infrastructure industry itself

Prices oversight to constrain monopoly pricing

- In markets that are not contestable, businesses may have the ability to charge prices above competitive market prices for extended periods of time
  - Problem common to a lot of 'natural monopolies'
- Governments recognised that competition law will not constrain 'monopoly pricing' and introduced regulation to constrain pricing in a number of industries
- Purpose was not to create price competition in the infrastructure industry, but rather to preclude monopoly pricing from restricting the emergence of competition and more efficient outcomes in dependent industries

Industry specific reforms

- Economy wide reforms were accompanied by a number of sector specific reform initiatives
- Sector specific structural reform and access regulation were introduced into a number of industries as part of the reform of public monopolies
- Comment on four major sectors:
  - Electricity
  - Gas
  - Telecommunications
  - Rail

Electricity reforms

- Historically state based and publicly owned with each state largely self-sufficient in terms of generation
- Infrastructure for generating, transporting and retailing electricity was vertically integrated
- Governments agreed to:
  - Place utilities on a commercial footing
  - Vertical separation of infrastructure
  - Allowing for customer choice of supplier
  - Implementing a system of third party access to transmission and distribution infrastructure
  - Establishing a wholesale electricity trading market

Electricity reforms – Cont.

- Outcomes
  - Electricity wholesale prices have fallen (by around 50% in NSW and Victoria)
  - Retail prices have fallen for larger customers
  - Price differentials for summer peak: better investment signals
  - Greater interconnection
- Investment in regulated transmission sector is at a historically high level

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Gas reforms

- Historically state based with supply to demand centres typically met by a single basin through a single set of pipeline infrastructure
- Infrastructure for transporting gas to demand centres was largely publicly owned and vertically integrated (across transmission, distribution and retail)
- Governments agreed to:
  - Remove legislative restriction upon interstate trade of gas
  - Place utilities on a commercial footing
  - Vertical separation of infrastructure
  - Allowing for customer choice of supplier
  - Implementing a system of third party access to transmission and distribution infrastructure

Gas reforms – Cont.

- Outcomes:
  - Some emerging competition between basins
  - Greater security of supply through improved interconnection
  - Higher level of investment in the regulated transmission sector

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Telecommunications reforms

- Historically dominated by single government owned national carrier with a legislative monopoly
- Duopoly in fixed line telephony and triopoly in mobiles introduced in 1991
- Full competition and revisions to the regulatory framework in 1997

Telecommunications reforms

- Introduction of an access regime has been particularly significant as structural reform of the horizontally and vertically integrated national carrier has been limited
- Outcomes
  - Prices have fallen significantly – between 1977/8 to 2001/2 average basket of telecommunication service fell around 20%
  - Investment has been high
  - Quantitative estimates put growth to economy at $10b as a result of the reforms

Rail reforms

- Historically, the interstate track network was state based, with differences between states in the operation of networks restricting competition across the entire network
  - E.g. track widths varied between states
- Governments introduced reforms:
  - Vertical separation of rail ownership from above rail businesses of some government entities
  - Corporatisation and privatisation of some government entities
  - Establish a single corporation responsible for the management and operation of Australia's interstate rail network

Rail reforms – Cont

- Co-regulation of safety across states and mutual recognition of accreditation
- Improving uniformity of technical standards and operating practices
- Implementing systems of third party access to various track networks

• Outcomes
  - Improved volumes
  - Increased train lengths
  - Gross mass per train has improved

Outcomes of Reforms

- While a causal link is inherently difficult to establish, NCP and related reforms have coincided with the most consistent and sustained period of economic growth in Australia's history
  - GDP per person has grown by 2.5 per cent a year since 1990 compared with the OECD average of 1.7 per cent
  - Australia's OECD ranking has risen from the low of 16th in 1990 to eighth in 2002
  - Australia's Productivity Commission estimates that household income is $7,000 per annum better off as a result