Committee for
Economic
Development of
Australia

Microeconomic Reform and Business Efficiency

Strategic Issues Forum

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MICROECONOMIC REFORM AND BUSINESS EFFICIENCY

Taking Stock of Microeconomic Reform in the Australian Economy

1. Introduction

The 1980s saw most OECD countries place great emphasis on the structural adjustment of industry markets - on microeconomic reform - as one means of improving efficiency and raising living standards.

During 1991 CEDA, through a special project of its Strategic Issues Forum, conducted a series of discussion meetings to assess policy and implementation aspects of microeconomic reform. This project, culminating in this summary report, has provided an opportunity to take stock of progress in this vital area, and to consider how government, industry, and the community may need to focus their combined efforts during the 1990s to deliver the real and lasting benefits that will justify the inevitable pain associated with this economic re-structuring in the short term.

Is Australia moving too fast or too slowly? Are we getting somewhere? Or are we almost standing still? It is very easy to say, as Prime Minister Bob Hawke said in tabling his 1991 Industry Statement, that:

> *This process of modernisation, of adaptation to the changing world economy, is not something that has some future cut-off point. It must be a continuing process. There is no point at which we can say reform is finished - because there is no point at which the world will stop changing.*[1]

The consequence of this line of argument, however, is that microeconomic re-structuring becomes bedevilled by the same uncertainty principle that Heisenberg propounded in the field of atomic physics:

> *If you know where you are,*
> *then you don't know how fast you are going;*
> *If you know how fast you are going,*
> *then you don't know where you are!*

1 House of Representatives, *Hansard*, 12 March 1991

Short of lapsing into a sort of policy meltdown, there seem to be only two ways for dealing effectively with such uncertainty over micro-economic reform. These are:

- To keep going back to the underlying reform objectives, in order to remind ourselves of just where we want to head;

- To keep checking our progress, by asking what success is going to look like, and what pitfalls we must avoid.

Unless we continue to do this, micro-economic reform will remain an elusive quest for a Holy Grail.

To conduct such a stocktake has been the ambition of this SIF project. By its very nature, such an undertaking is necessarily a preliminary audit of work in progress. What does emerge clearly, however, is the extent of the challenge for Australia in the 1990s. A great many programs for change have been put in place over the past few years; the challenge of the 1990s is to generate a greater sense of urgency about capturing the benefits of these initiatives, whilst accommodating the flexibility needed to respond to new and changing circumstances. The challenge of delivering these results will involve:

- shifting the focus from "enabling processes" to specific objectives;

- defining sustainable outcomes in terms of clear and explicit goals, and commitments to action;

- consolidating the tri-partite commitment of government, industry and unions to real economic development.

The over-riding goal must be to re-structure and re-fit the Australian economy for the 21st century. We need to ensure that industry and business growth is not hamstrung by regulatory precedent and administrative preoccupations that are merely self-serving.

The companion SIF project on national infrastructure issues, and CEDA's major program on "An Australia That Works", being co-ordinated by Fred Argy, will continue this debate that CEDA believes to be so important to Australia's future as a community. This work on shaping a vision for national development will help determine the priorities for structural change, and the pace of change needed to fulfil our national aspirations.

2. Microeconomic Reform.

> *"We talk so much about it that our eyes glaze over at the mere mention of the word."*
>
> *John Prescott, BHP, August 1992*

Despite the amount of attention it has received, there appears to be widespread confusion as to just what microeconomic reform is all about. Microeconomic reform is a buzz-phrase in danger of losing all meaning as a catch cry for action. At the political level, the expansive rhetoric about "re-shaping the economy" either re-reinforces confusion or creates unrealistic expectations. At the other extreme, the "insiders" in the business of packaging economic policy for governments resort to arcane jargon that few people in industry can understand, or are able to relate to the day-to-day imperatives of their business undertakings. What is it all about ? The general objectives for microeconomic reform are typically described as being:

- to ensure that scarce national resources are deployed where they will yield the most benefit to the community;
- to put pressure on the suppliers of factor inputs to minimise costs to users, and to innovate;
- to eliminate the outmoded but entrenched work practices prevalent in these areas;
- to encourage firms and individuals to adjust more quickly and efficiently to changing market signals and opportunities.

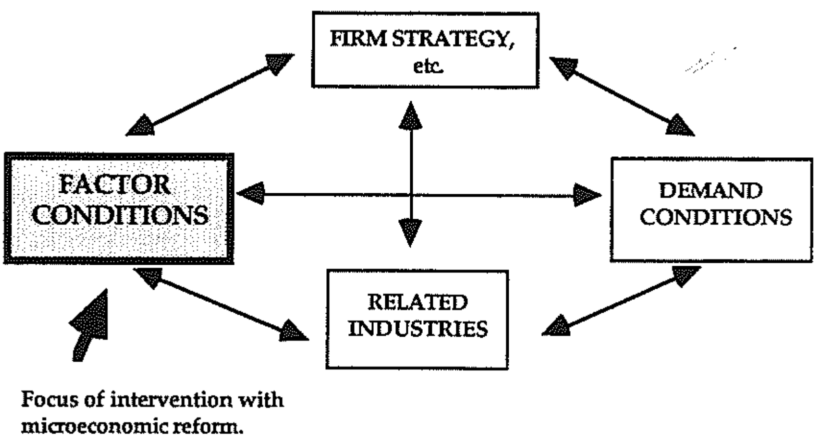
Microeconomic reform, therefore, is mainly concerned with removing structural impediments that discourage or prevent resources being used in the most cost-efficient manner, or which limit the flexibility and responsiveness of workers and enterprises. Removing these impediments generally results in a redefinition of the direct role of government.

The focus is on "input factors" to production

It is important to recognise that the primary focus of microeconomic reform revolves around the "input factors" influencing industrial performance, and how gains in factor productivity can be passed directly to end-users. It is, therefore, mainly concerned with the infrastructure costs and performance associated with transport, construction, power and energy, and communications, as well as with the organisation of labour markets, education, and taxation regimes. The focus, therefore, is on the supply side of the economy, and in particular those areas not traditionally trade exposed.

As such, the focus of microeconomic reform can be seen to correspond closely to the "factor conditions" category in Michael Porter's now well-known schematic of the primary determinants of industry competitiveness[2]. In economic jargon, factors of production represent "the inputs necessary to compete in any industry, such as labor, arable land, natural resources, capital and infrastructure".[3]

FIGURE 1: THE DETERMINANTS OF NATIONAL ADVANTAGE



Source: Michael Porter (1990)

It is helpful to locate the main thrusts of microeconomic reform within such a model, as it serves to remind us of all the things that microeconomic reform does not, and can not, address in itself. What we are talking about here, therefore, are changes relating to factor conditions which are absolutely necessary to the international competitiveness of our industries, but changes that will not generally be sufficient in themselves.

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2 Michael Porter, *The Competitive Advantage of Nations*, 1990, p72
3 *Ibid.*, p73

The context for change

The public sector has traditionally been responsible for most of the key infrastructure inputs to industry and business in the areas of energy and power, water, communications and transport. Government, at both Federal and State level, has thus directly controlled some of the key factor conditions affecting the competitiveness of Australian industry. The restructuring of these infrastructure markets through the introduction of competition, and the corporatisation and privatisation of government enterprises, are fundamental to the microeconomic reform agenda.

As a consequence, effective structural adjustment to improve productive efficiency requires action across a number of different fronts. Some of the elements involved include controls on market access, the regulation of market operations, direct intervention in the structures of enterprise ownership, or rules governing company operations. Figure 2 attempts to locate these various elements within the overall framework of national policy.

This framework reminds us that broad strategies for structural adjustment can only be formulated within the context of government policy settings, the functions and mechanics of regulatory administration, and the ownership and operating structures of enterprises.

This simple model is particularly useful in positioning the various elements of restructuring in relation to each other. It serves to remind us that:

- Government intervention to implement policy objectives can take many forms, with action needed at both State and Federal level;

- the rationale for particular market and enterprise controls should be able to linked back to national policy settings;

- multiplying layers of regulatory intervention is likely to increase the probability of unintended consequences and efficiency "bottlenecks".

Figure 2, therefore, highlights the essential interdependence between the different elements involved in a process of structural change. Both Federal and State governments need to be involved. Achieving efficient and beneficial industry outcomes will depend upon the extent to which policy changes are devised and implemented in a coherent and consistent manner. As the following example indicates, this is especially important in the key area of structural reform in industries traditionally dominated by monopoly public utilities.

Telecommunications as a case study

From the early 1980s the institutional restructuring and market liberalisation of infrastructure services have been shaped by an OECD policy formula for the explicit separation of - and distinction between - national policy functions, regulatory administration, and the market operations of enterprises. The telecommunications sector provides a good example of the application of these principles in implementing microeconomic reform in the provision of electronic infrastructure.

The government's main policy focus in telecommunications has been the use of competition policy to promote industry efficiency and improved customer service. In large measure this has been driven by perceptions of gross over-staffing in Telecom Australia, and of the lack of customer focus that frequently bedevils monopoly markets.

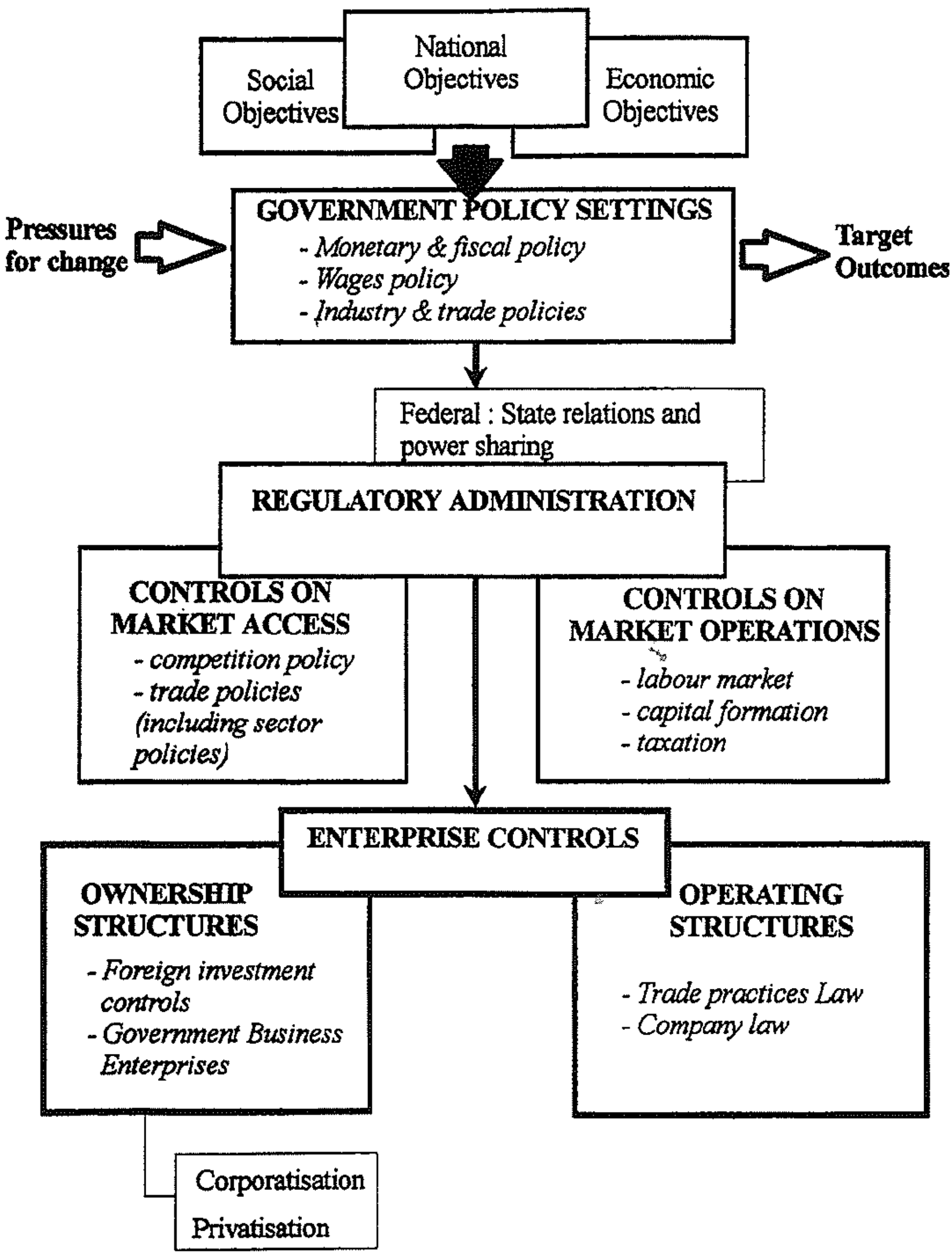
Traditionally most monolithic public utilities exercised regulatory and public policy powers as an adjunct to their charter for service provision. Significant market liberalisation in telecommunications has therefore required the parallel establishment, in 1989, of a separate industry regulatory agency, AUSTEL, and the privatisation or corporatisation of the incumbent public utilities. Hence the sale of Aussat as part of the licensing of a second network competitor, and the restructuring of the incumbent carrier as a public company, albeit government owned, with a wholly commercial charter. The government itself has resumed the policy responsibility for the subsidisation of the non-commercial activities needed to support universal service, and for industry development.

In this instance, direct and extensive government intervention has been exercised to bring about the desired scale of market restructuring:

> *Overseas experience has revealed clearly that when dealing with an environment where there is an entrenched, monopolistic market structure, it is not sufficient to simply privatise or de-regulate to produce competition and community benefits. We are therefore adopting a careful approach to overcome the structural barriers to competition which have developed, quite naturally, under the former monopoly arrangements.*[4]

4 Vanessa Fanning, Department of Transport and Communications, Speech to CEDA's Strategic Issues Forum, 1 February 1991.

FIGURE 2: THE POLICY CONTEXT OF MICROECONOMIC REFORM



Source: T.A.Cutler

In such a context it is easy for everyone to become preoccupied with competitive structures and the contestability of markets, at the expense of sufficient attention to whether these new market structures - whether duopoly or open, and regulated extensively or lightly - actually deliver different and better results for end users and consumers.

The underlying rationale for microeconomic reform in this industry example has been the achievement of greater efficiency through introducing greater "transparency" between national policy objectives, industry regulation, and market operations. Similar issues have been raised in quite different areas, such as business taxation. Here CEDA members have expressed concern about a lack of clarity in the role of the Tax Office. Through the process of rulings and audits the Tax Office operates, by default, as a policy setter on tax imposts. This activity, however, complicates its relationships with business in its role as the revenue collection arm of the government.

The limits to microeconomic reform

This attempt to clarify the main objectives of microeconomic reform - a concern to address the causes of inefficiency at the level of "factor inputs" - has highlighted the wider ramifications of such an undertaking. Nonetheless, it is important to reiterate that microeconomic reform will not, by itself, resolve all the problems with industrial competitiveness nor Australia's fundamental economic problems. In particular, it will do little to alter such things as the imbalance between savings and investment. If, however, microeconomic reform is linked to appropriate macroeconomic policies for monetary, fiscal, and wages outcomes on the one hand, and to changes in enterprise culture and investment on the other, it will support the effectiveness of new initiatives in both these areas.

The potential gains

The overriding benefit being sought is the creation of more competitive and efficient industry structures.

The Industries Commission has estimated that real gains of up to $16 billion, or 5 per cent of Gross Domestic Product, could be achieved over a period of ten years through a continuing program of reform in the areas of transport and communications, electricity supply, and the structure of assistance to agriculture and manufacturing. Estimates from the Bureau of Industry Economics suggest greater returns from more sweeping reforms. These gains would not be once-off, but continue to accrue year after year.

Although the overall benefits from microeconomic reform are substantial, the distribution of benefits and their impact at the firm and consumer level is of crucial importance. For example, the success of financial deregulation needs to be tested against whether it has provided small businesses with better and more efficient access to finance, or has ended the rationing and arbitrary discrimination that characterised past credit policies. It is clear that lower personal tax rates and the introduction of company dividend tax imputation have significantly assisted small businesses to achieve more robust levels of equity financing.

One of the difficulties is that there is often no direct relationship between the aim of increasing overall efficiency, and distribution of the resulting benefits. In some areas, such as public utilities with embedded cross-subsidies, the first impact of market restructuring can well be price rises for households and individual users. The hope is that overall benefits should accrue as firms are able to pass on the savings from more efficient factor inputs.

The costs of structural adjustment

The pain associated with structural adjustment tends to be more obvious and more immediate than the expected gains.

This is partly because the costs tend to be borne by relatively small and often cohesive groups, whether workers and employers in a particular industry, the users of particular services, specific categories of professionals, or a regional community. The benefits of reform, on the other hand, tend to be more widely dispersed across the community as a whole.

In addition, the costs are often up-front, while the gains accumulate more gradually over time. Some types of reform initiative, such as award restructuring, can offer quick pay-offs. Others, such as tax changes to alter incentive structures, are generally slow to produce results, although in the long run the benefits generally far outweigh the costs of the initial impact of change.

The short term costs can increase, or the future benefits can be discounted, if groups disadvantaged by reform are well organised and thus able to extract disproportionate compensation for the pain of adjustment.

In implementing reform, the challenge is to find ways to minimise the shortterm costs and to increase the community acceptance of the need for change. This raises three key issues.

First, reform demands sensitivity, consultation, information, and public education. Here the objective is to develop a commitment to "win-win" outcomes. Often both the substance of reform proposals and the level of community acceptance of the need for change is compromised by reformist zeal and an initial failure to put all the facts on the table. The extended debate over telecommunications reform during 1990 provides a good example. Despite daily media coverage of the politics of the debate, opinion polls revealed that the community at large had simply no idea at all what all the fuss was about. We can be almost certain that comparable polls on shipping or rail transport would tell the same story.

The need for effective public education cannot be stressed too much. The problem is how to do it. While there has recently been a lot of focus on the importance of good internal communications within firms, as a key element in promoting and implementing change, this has not been matched by effective communication processes and dialogue at an industry or community level. Industry associations, unions, and business groups like CEDA should accept greater responsibility for public education programs at this broader level. An initial step might simply be to publicise more widely the specific commitments of individual firms.

Second, the likelihood of achieving community support can be enhanced if the reform program is broadlybased. This helps to ensure that reforms in various areas will re-reinforce each other, and increases the chances that the costs for any one group in the community will be offset, at least in part, by gains in other areas. For example, it will be easier for manufacturing industries to adjust to tariff cuts if these form part of an overall sectoral program with demonstrable net benefits. (It is, of course quite a different matter if no demonstrable net benefits can be established).

Third, the question of whether, and how, to compensate the losers from reform must be confronted openly and effectively. The aim here must be to facilitate acceptance of change, without siphoning off the benefits in the form of "greenmail" to special interest groups.

Reform as a package

All these considerations reinforce the desirability of pursuing an overall program of reform as a package, and not promoting individual initiatives in isolation on a stand-alone basis. The debate over tariff levels and taxation provide good examples of reform initiatives that have neither been conceived nor implemented as part of a coherent program for restructuring and industry development. Generally speaking, reform in one area, such as lowering the levels of subsidisation in product markets, can increase pressure for reform in other areas, such as the achievement of greater flexibility in labour markets. What cannot be assumed is that related adjustments or necessary complementary measures will be implemented in a systematic way, without positive action to bring this about.

3. The 1980s : Creating an Agenda for Reform.

The 1980s saw Australia move quickly towards fuller integration into the global economy as, at the broadest level, more and more aspects of economic governance became exposed to, and tested against, the realities of international competition. In the early 1980s the focus of attention was very much on government monetary policy and the restructuring of financial regulation. In the second half of the decade attention then shifted to microeconomic reform.

Microeconomic reform became the primary focus of the Hawke government's third term agenda in 1987. A "Structural Adjustment Committee" (SAC) of the Cabinet was established to set priorities and to oversee a reform program.

The initial sectors targeted included areas like shipping and telecommunications. At the same time, considerable attention was directed at the government trading enterprises that dominated so many of the infrastructure functions crucial as "factor conditions" across the Australian economy.

At the national level, the corporatisation of large government employers like Telecom Australia and Australia Post focused attention on whether or not these utilities should still be considered natural monopolies. Through sanctions offered by the Loans Council and tied grants, the Commonwealth has been able to help maintain pressure for change in the State utilities responsible for power, energy and water supply. NSW is the one State to have implemented a concerted program of corporatisation and privatisation; most of the other States have been slow to follow the lead given by the Federal and NSW governments. A consistent theme at CEDA meetings has been the lack of sufficient attention to substantive reform at the State level, particularly in Victoria.

In 1989, the Federal government initiated a new round of regulatory review in land transport, aviation, and telecommunications. This was followed in 1990 by a major focus on the restructuring of Federal-State relations, and long overdue attention to the regulatory overburden represented by Australia's multiple tiers of government and administration. This has created opportunities for rationalisation in areas like the operation of national rail and road systems, and the mutual recognition of standards or codes relating to the sale of goods and the provision of services. Steps are finally being taken towards more streamlined "one stop shopping" for government approvals associated with major national development projects.

4. Progress so far: Different perspectives.

The government's Economic Planning Advisory Council (EPAC) has put the view that substantial progress has been made in implementing reforms at the microeconomic level in Australia. EPAC points to OECD studies which indicate that Australia has performed well in a number of areas, including the liberalisation of trade in both manufactures and agricultural products, financial deregulation, simplification of the taxation system and programs to introduce commercial principles into the corporate sector[5].

On the negative side, the OECD points to areas where it considers further reform to be needed. These include the taxation system (particularly the current regime of indirect taxes), the labour market, and existing systems of education and training.

Prime Minister Paul Keating's recent *One Nation* statement itemises an extensive and impressive record of reform initiatives across a broad front[6]. Quite apart from its primary purpose of promulgating the government's political agenda, *One Nation* is a major document of record which summarises the major steps in microeconomic reform taken thus far. This checklist includes:

- aviation, with the abandonment of the two-airline policy and the deregulation of domestic aviation;
- telecommunications, with the establishment of a pro-competitive industry regulatory body, AUSTEL, and the introduction of a network competitor to the merged Telecom and OTC;
- shipping, with moves to lower crew levels and re-structure work practices;
- the waterfront, with programs to reduce over-manning under new enterprise agreements on work and management practices;
- restructuring the public sector through the corporatisation of government trading enterprises and selective privatisation, resulting in considerable growth in labour productivity;

5 EPAC, *Microeconomic Reform*, Council Paper 42, May 1990
6 P J Keating, *One Nation*, Canberra, 1992

- the initiation of a program of benchmarking the performance of business input services;

- business regulation, with new, unified, corporation laws, an increased focus on trade practices supervision, changes to government purchasing arrangements, rural marketing, import and export controls, and customs procedures.

Lack of comprehensiveness is not one of the charges that can be laid against the government's reform agenda. To the contrary some would argue for a greater concentration of effort on a few of the more key areas: those with the greatest potential to deliver broadly based benefits to industry. For example, faster change on the waterfront or with transport, or the "unbundling" of the traditional electricity monopolies to separate the markets for power generation and for distribution, would seem to offer greater overall returns than the painful restructuring of the textile, clothing and footwear industries which have little cross-sectoral impacts on overall efficiency.

What is contested is the pace of change, with both business users and the Federal Liberal and National Coalition arguing strongly for quickening the pace of business restructuring. Industry groups, particularly in the manufacturing sector, complain vigorously that the slowness of microeconomic reform initiatives fatally undermines any prospect for manufacturers being able to confront the challenge of import competitiveness imposed by tariff cuts.

Tariff schedules can be changed at the stroke of a pen; changes to the efficiency of factor inputs to industry cannot. Unless these reforms are managed and delivered as part of an integrated - and synchronised - package, the real prospects for national advantage are put gravely at risk. The Metal Trades Industry Association has concluded that:

> *...the drive for reform which has ensured that tariff reductions will continue relentlessly, has broadly stalled when it comes to implementing essential microeconomic reforms so that tangible effective cost reductions are actually delivered to manufacturers as an integral part of this tariff reduction program.*
>
> *No one should be in any doubt that the only way Australian industry can possibly cope with these tariff reductions is if there is a firm nexus between the tariff reductions and achieved,*

> *tangible microeconomic reforms and appropriate microeconomic settings.*[7]

This general statement of the problem translates directly into a balance sheet dilemma for individual companies; a point summarised succinctly by Bill Bytheway of Mayne Nickless at one of the CEDA discussions:

> *Manufacturers have direct control over a mere 25% of their total costs. Therefore, for the nation to be truly competitive, we must also reform the other 75% of the cost burden.*[8]

In some areas like labour market reform the Federal government has it within its own power, as by far the largest direct employer of unionised labour, to take the lead in the establishment of decentralised enterprise agreements and new standards of industrial relations practice. Indeed, given the growing dominance of public sector unions within the labour movement generally, it is hard to see how any significant labour market restructuring can occur at all without government, at both Federal and State level, exercising the direct leverage of its own managerial control.

As already noted, progress has been least apparent at State level, with the exception of NSW. Hopefully, the increased attention being paid to the reform of Federal-State regulation will begin to expose the States to greater critical scrutiny. Recent initiatives to create mechanisms for "guaranteeing free trade in goods and services " across the States within the Australian market, with particular attention to mutual recognition of standards and the abolition of non-tariff barriers, has been an area of progress insufficiently recognised:

> *For Australia to be an integrated and more internationally competitive national economy, it is essential to overcome the inefficiencies caused by regulatory differences among Australian States and Territories.*[9]

The restructuring of taxation, and the proper position of tariff reforms within the context of the taxation regimes of which they form part, is a major area where business and industry continues to be disappointed at the lack of political courage and the absence of "fact-based" public discussion.

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7 Metal Trades Industry Association, *Ledger Report No 2 on Tariff Reductions and Microeconomic Reform*, 24 January 1992, p2

8 Bill Bytheway, Mayne Nickless Ltd, "Land Transport in Australia - An Operator's Perspective", CEDA, September 1991

9 Conference of Premiers and Chief Ministers, *Report of the Committee on Regulatory Reform to Heads of Government*, Adelaide, November 1991

Finally, even though the direction of change in many areas is not contested, there is considerable and understandable nervousness about whether reform objectives will be maintained once it comes to implementation. Fears about structural change being watered down through pragmatic concessions to special interest groups are not unfounded, especially when government enterprises are involved. The view from business is that the reform agenda is not being driven fast enough. Clearer objectives need to be set, and firm accountabilities for meeting them accepted. All parties need to be prepared to make definite commitments to action and to outcomes, and to be held to them.

5. Impediments to growth : A framework for evaluation.

Much of the debate over microeconomic reform can be seen as a contest between the different stakeholders over the priorities and strategies for change, and over the distribution of the expected efficiency gains. At its starkest, the debate is about who gets the benefit: is reform a milch cow for government as an excuse for new charges and taxes, and do service providers pass on the cost savings to users, or retain them to boost their own profitability?

Figure 3 represents the general battlefield on which these debates about the distribution of efficiency gains will occur. The contestants are government, suppliers, and the end customers. Senator Bob Collins, as Minister for Shipping and Aviation, commented during 1991 that "the principal aim of reform is to ensure that the benefits of reform are passed onto users by way of reduced costs and improved service". It is crucial that all reform efforts are assessed on this basis.

CEDA's SIF members overwhelmingly endorse this focus, but speaker after speaker at CEDA forums have reiterated the point made by Phillip Petersen from APM with respect, in this instance, to the waterfront:

> *...not one dollar benefit have we seen, not one hour of reduction in time despite the extraordinary amount of time and money involved. If the government had applied one tenth of the heat to all players that was used during the pilots' strike the increases could have been interesting.*[10]

Figure 3 identifies the two generic points at which efficiency "bottlenecks" can be expected, and at which arguments about the distribution of efficiency gains will occur.

10 Philip Petersen, APM, Speech to CEDA's Strategic Issues Forum, 20 September 1991

This analytical model suggests that regulatory impediments or "bottlenecks" to economic productivity may arise at two levels. The first potential source of regulatory distortion lies in the area of the government policy framework for the delivery of infrastructure or factor inputs to business enterprises and industry.

What industry seeks from government policy in this area is clarity of purpose, and certainty about the regulatory administration of policy settings. Some of the areas of regulatory impediment and policy bottleneck that have been raised include:

- the level and extent of cross-subsidisation in infrastructure provision;
- the structural consequences of public ownership;
- the government policy influences on capital formation;
- the investment environment (including the availability of, and access to, markets, skills, resources, and technology).

Critical attention has been given by business and government to re-evaluating many of the embedded assumptions underlying entrenched industry structures and which have provided the rationale for particular forms of regulatory control and intervention. The efficacy of government initiatives in this areas needs to be subjected to the test of policy benchmarks against other countries; that is, a relative test for how well Australia's government is performing in delivering policy settings that are designed to enhance productivity and innovation in the production of infrastructure requirements.

The second area of potential bottleneck is in the extent to which the actual requirements of the end users of factor inputs to the economy are met in practice. During this SIF project, many of the end users, the purported beneficiaries of microeconomic reform, complained at the slowness with which the benefits of structural change flowed on to them. This raises the crucial question of the distribution of efficiency gains, and the role of government taxation policies and of trade practices regulation in increasing the transparency of distributive trade-offs. The Business Council drew attention, in 1991, to what appeared to be happening in practice:

> *Industry seems to be caught between governments pumping up road freight costs, with the extra revenue going into their own pockets, and rail charges going up to reduce their deficits. There seems to be more effort on raising charges than on the major structural and labor reforms that would lift efficiency and reduce costs.*[11]

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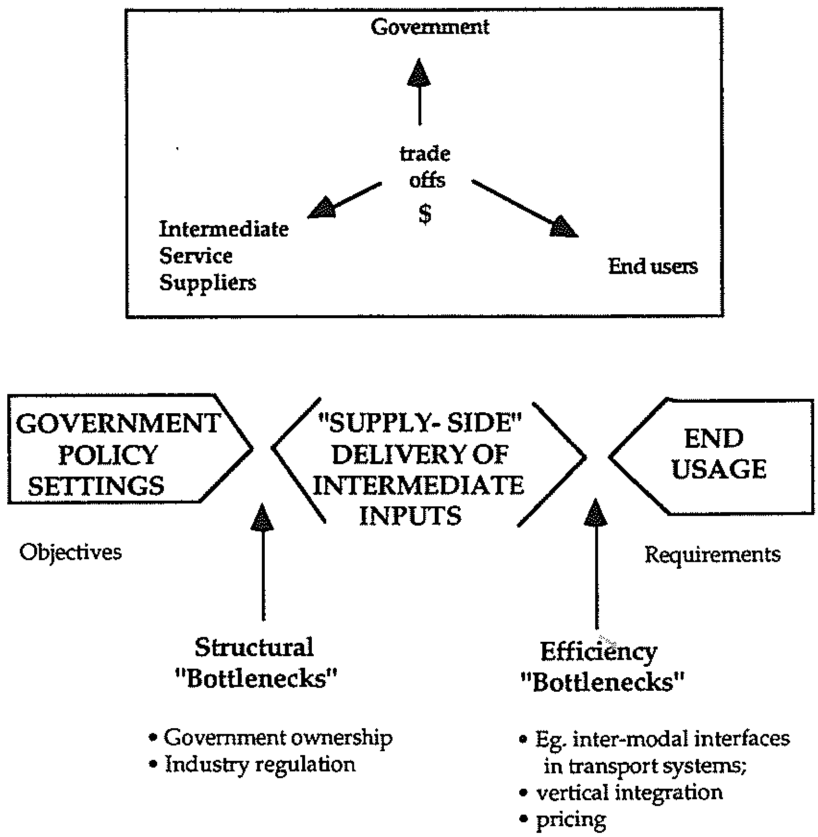
11 "Micro Reform to Cost More", Business Review Weekly, 1 November 1992, p36

FIGURE 3: A FRAMEWORK FOR EVALUATION

Distribution of efficiency gains



Subsequently, the Prices Surveillance Authority has criticised shipping companies for their apparent failure to pass on reform savings to users: Professor Alan Fels has commented that:

> *I feel very strongly that the fact that these benefits of waterfront reform are not being passed on, together with the cartel arrangements these shipping lines are allowed to have, is of great concern.*[12]

12 *The Age*, 3 September 1992

Other issues raised at this interface point in Figure 3 include the question of cross-modal and cross-sector alignment. Examples of this raised during the project included the bottlenecks between port and land transport systems, or the impact of conventional trading hour restrictions on logistics and distribution costs.

6. Measuring up : The role of benchmarking.

The conventional test of the rate of progress with reforms in all these areas is in terms of enterprise or sector benchmarking against "international best practice". Much has recently been made of the usefulness of measures of international best practice as a means of setting specific improvement targets for Australian industry.

At the level of facilitating practical change, the operations of multi-national corporations provide a real spur for "best practice" in the sectors in which they operate. The internal benchmarking of performance across different company sites provides a powerful intra-company imperative for change which, in the right conditions, can create the opportunity for significant flow-on effects for a country's industry sector as a whole. During the current SIF series, Exxon Chemicals provided a useful casestudy of this intra-company benchmarking of industrial relations practices.

The benchmarking of industry sectors at large has tended to be more controversial, particularly in the case of monopoly utilities like power or telecommunications, where the use of international comparisons has been advanced as a surrogate for market competition. As the debate over telecommunications demonstrated, international comparisons can generate a lot of heat without providing much help in implementing new policy approaches.

In many areas, such as transport, it is arguable whether benchmarking in itself can ever lead to the right industry targets. The reason is that, because of its distance from its trading markets, Australian industry has an in-built structural disadvantage due to the disproportionate burden of distribution costs compared with trading competitors. This suggests that the challenge in many areas, if sustainable competitive advantage is ever to be achieved, is to "get ahead" of the rest of the world, not merely to catch up.

FIGURE 4: BENCHMARKING

COUNTRY COMPETITIVENESS	COMPANY COMPETITIVENESS
Aspects of Government Policy Competitiveness:	**Aspects of Industry and Enterprise Competitiveness:**
. Infrastructure quality and efficiency . Country economic management: - *inflation* - *interest rates* - *national debt.* . Elements of sovereign risk. . Trade policies: - *trade barriers* - *international market across* . Foreign investment policies.	. Trade parity versus strategic advantage . Cost/availability of primary and intermediate inputs . Extent of both regulatory and market "bottlenecks" [within a dynamic, not a static model]

Figure 4 highlights the limits of looking at measures of industry or enterprise competitiveness in isolation of some of the wider questions of country competitiveness : questions which call for measures of the comparative efficacy of a government's policy responses to the challenges of economic development.

In the final analysis, however, the effectiveness of structural adjustment must be tested against the extent to which we can see discernible changes in the economics of the business systems represented by Australia's trading enterprises. The issues raised by the businesses represented at the CEDA discussions related to the extent to which concrete evidence of change was evident in their operating experience.

This is not a bad "bottom-line" test. That it has proved hard to discuss properly is probably a function of the fact that, so far, the main reform objectives have generally not been spelt out in terms of any specific endtargets or milestones, let alone in terms of targets that might be meaningful at an enterprise level. What this would involve is a vertically-integrated summation of the impacts of changes on a sector basis. At government level, the nervousness about being seen to espouse anything resembling sectoral industries policies has made it exceedingly difficult to close this loop.

7. "Permanent white water" : The challenges for the 1990s.

The challenge of the 1990s is that, whatever changes we initiate in Australia and whatever progress we achieve, the rest of the world is not going to stand still. In this environment of "permanent white water", the challenge is to do better than simply catch up with the rest of the world in those areas where we are significantly behind. As David Murphy of Ford Australia put it at this SIF forum:

> *If we assume the Japanese are improving productivity at around 5% per annum, then with the 2.5% per annum reduction in tariffs, we have to improve at 7.5% per annum just to stand still. But standing still means that we will be uncompetitive.*

One of the greatest challenges in the 1990s, therefore, will be for government, business, and the labour movement to generate a greater community sense of urgency about the need to implement change. The present grudging acceptance that things are not working is simply not enough to ensure that new initiatives will be implemented effectively, or in time. In many of the discussions around the country a sort of "excuse mentality" crops up all too often: that what is possible is fatally constrained by Australia's small domestic market, or by relatively high wage levels.

Since the mid-1980s there have been no shortage of initiatives in the area of microeconomic reform and structural adjustment. No one can damn government or industry for any lack of comprehensiveness in these programs. That said, this paper has suggested that there is plenty of scope for better effort, including:

- a much greater sense of urgency about what must be achieved, particularly at the State level where progress has been slowest;
- a less piecemeal approach, with much greater attention to managing the balance between international trade exposure on the demand side, and increased supply competitiveness through microeconomic reform;
- better efforts to set firm targets and timetables, with governments, industry, and individual enterprises making public and specific commitments to action;

- a stronger focus on delivering results to the end-users as the driving force of reform, with close monitoring of the progress of restructuring by the Industries Commission, the Trade Practices Commission and the Prices Surveillance Authority to ensure that the benefits of reform for customers are not siphoned off by governments or service providers;

- greater attention to industry and public education and communication about the imperatives of change and the challenges associated with national economic renewal: we need to parallel, at an industry and community level, what the best firms are now doing in terms of internal communication and education within their enterprises;

- developing an industry and community culture of "permanent white water": a culture of continual improvement to "get ahead of the game" and to get off the dizzy merry-go-round of always being in a "catch up" situation.

What follows is a working checklist of some of the key challenges and imperatives for Australia during the 1990s:

1. Real change is hard work, and there are not many "quick fixes". The advocates of "fast-tracking" schemes are often really about side-stepping structural impediments to efficiency. Unfortunately, our political and market systems are still not good at tackling issues where change involves long time-frames.

2. Being as good as the rest of the world is not good enough. Almost by definition, the benchmark of world parity will never serve to identify the possible sources of competitive advantage. Benchmarking is, however, a powerful reminder of the imperative for change.

3. Progress to date shows insufficient attention to end-users - particularly medium and small business. Business needs to be far more active in communicating the facts about how much industry innovation and prices are determined by the cost and quality of infrastructure inputs and the environment of business regulation.

4. Priorities and timetables for structural change should be more clearly determined, to ensure that the energy of government and industry is not diffused across too broad a front.

5. Government efficiency and policy efficacy needs to be benchmarked as much as that of industry and enterprises; a global economy needs competitive government.

6. While GBE's have been corporatised and even privatised, new QANGOs, especially Reform Authorities, have multiplied apace, with little public debate. In delegating the executive tasks of implementation to new statutory authorities, care needs to be exercised to ensure that these bodies do not degenerate into the sort of institutional selfserving behaviour that characterised the public bodies they have been set up to change.

7. The focus at present is overwhelmingly on traditional, embedded problems. This is necessary, but not sufficient. Equal attention must be given to ensuring efficient and efficacious responses to new and emerging regulatory pressures and demands. For example, in areas like trade and the environment, international regulation is beginning to constrain sovereign controls; Australia must act to ensure that such developments do not unduly prejudice our competitiveness as a country.

8. We need to make sure we do not repeat the mistakes of the past and create new regulatory impediments to business efficiency at the same time as we are painfully dismantling others. There is a danger, for example, that the proliferation of new regulatory agencies in areas as diverse as telecommunications, environmental protection and resource development will develop an institutional life of their own.

9. Market restructuring and the creation of new markets in the 1990s will require thinking outside traditional corporate and regulatory pigeon-holes. In this context, it can be argued that there has been too little attention to cross-sectoral impediments to growth. A good example of this need is in the re-structuring of inter-modal interfaces in transport systems. On another front, the reassessment of the role of the traditional public utilities in areas such as power and energy creates the opportunity for significant new investment and growth possibilities.

10. Finally, there is the ever present danger that regulatory change will not keep pace with industry convergence and restructuring brought about by technological and market change. The best current example of this is in the area of telecommunications and broadcasting, where future industry growth will be fatally constrained if traditional regulatory approaches are retained. The problem is that regulatory practice can never effectively guide market developments; it will always lag. A key

challenge, therefore, is to ensure that the regulatory solutions of today do not pre-empt future opportunities.

In the continuing challenge of economic development and the search for greater business efficiency, it is wise to remain sceptical about the efficacy of regulatory solutions. This is not to deny the need for regulatory intervention, but to emphasise the importance of ensuring that regulatory intervention serves the economic objectives and industry outcomes that we seek to achieve.

Unless kept in such a perspective, our regulators will end up with a dismal epitaph:

> *"They cost too much; they got in the way when we didn't need them; and we couldn't find them when they were needed."*