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This issue includes data up to 6 November 1997

Economic Overview

This article provides an overview of economic conditions since the 1997-98 Budget.

The June quarter 1997 National Accounts confirmed that a step up in growth occurred in the first half of 1997, following a temporary slowing over the last three quarters of 1996. Gross Domestic Product (GDP) growth in the June quarter 1997 was driven by solid growth in private consumption, dwelling investment and a substantial contribution from non-farm stocks.

At the time of the 1997-98 Budget, faster economic growth was expected to result from stronger growth in private final demand combined with continued modest growth in public demand and a small detraction from growth from net exports. The recent indicators: are consistent with continued solid growth in business investment; point to a continuation of the housing recovery, underpinned by historically high levels of home affordability; and confirm a firming of employment growth, which will support household incomes and consumption. Lower than average rainfall across much of southern and eastern Australia during the winter months raised the risk that farm production may be lower than expected, however this risk appears to have been reduced for the time being with good September rains. Nevertheless, an El Nino event is still being predicted to March 1998, highlighting that uncertainty continues to surround the outlook for next year’s winter crop.

The positive economic fundamentals which underpinned the step up in growth in the first half of 1997 have continued into the second half of the year: inflation at its lowest level since the 1960s; the impact of easier monetary conditions continuing to be felt; and both the household and corporate sectors in structurally sound positions. In particular, the recent interest rate reductions and the depreciation in the exchange rate since the Budget was handed down in May should provide a sizeable stimulus to activity in 1997-98. These influences will help to offset any emerging risk to activity from developments in Asia.

Recent financial market instability in East Asia has increased the degree of uncertainty surrounding the assumption for growth in that region. While it is too early to gauge the impact of recent financial market instability on economic activity in the region, it is likely that economic growth in East Asia will be lower than assumed at budget time. Outside East Asia, economic growth in the United States remains strong and growth continues to pick up in Europe.

Box 1 provides a summary of recent developments in the world economy.

Box 1: Recent Developments in the World Economy

Economic growth in the **United States** has averaged 4¼ per cent (annualised) over the past three quarters, well above the long-term trend. As a result, the unemployment rate has fallen further. At the same time, underlying inflation has continued to fall and there has not been any clear acceleration in labour costs. Recent indicators of activity have been somewhat mixed. Employment growth and consumer spending are expected to moderate and inventory investment to slow. Growth overall is expected to return to a more sustainable level in the year ahead. Should signs of inflationary pressures emerge, any tightening in domestic policy settings is likely to be moderate and any upturn in inflation is likely to be gradual.

The economic outlook for the **East Asian region** has weakened over the past few months with several countries in South East Asia experiencing large currency depreciations and weakening equity markets. Thailand, Indonesia, Malaysia and the Philippines (the ASEAN 4) have been most affected. Together these economies account for around 10 per cent of Australia's merchandise exports and one fifth of the growth in exports over recent years. Our major trading partners in the region are in North Asia — Japan, Korea and Taiwan. A marked slowing in growth in these economies would have a greater impact on Australia. Weaker domestic demand can be expected in the ASEAN 4 in the short term as a result of lower levels of confidence, higher interest rates, exchange rate losses, strains on the financial system, and lower capital inflows. The prospects for these economies over the year ahead will be contingent upon measures to consolidate financial sector liberalisation and to tackle underlying structural problems. The effectiveness of policies to contain the inflationary impact of the currency depreciations will also be critical in the year ahead. Success on this front would help lock in competitiveness gains and underpin a rebound in exports and growth.

The underlying strength of the **Japanese** economy remains difficult to gauge because of the one-off impact of the 1 April increase in the value added tax rate. While growth in the first half of the year was less than expected, domestic demand is expected to rebound in the second half of the year. Policy settings are supportive with interest rates low, the impacts of fiscal consolidation easing and external demand likely to remain a positive force for growth. That said, downside risks remain, highlighting the importance of the domestic structural reform agenda.

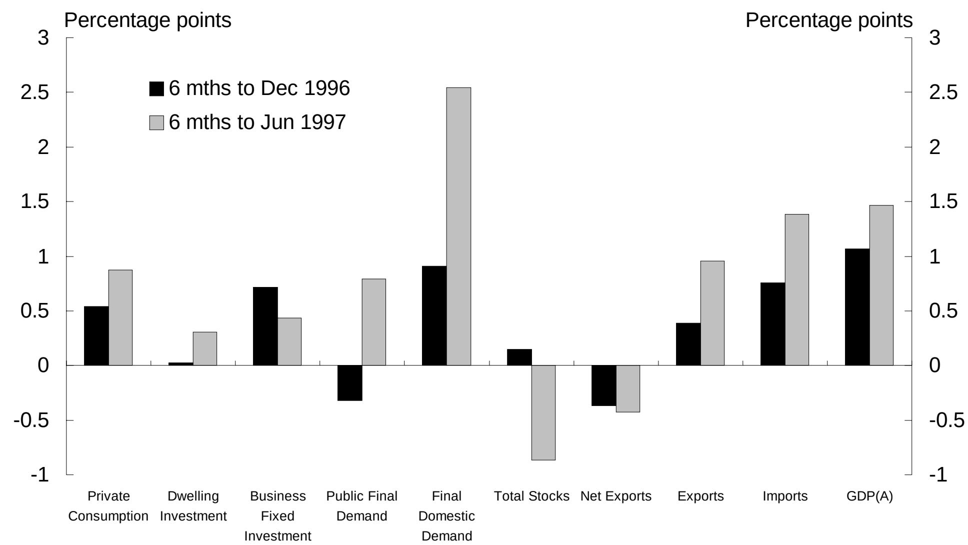
The economic outlook for **Western Europe** is for growth to gain momentum — the solid growth in the United Kingdom and some of the smaller regional economies is expected to broaden to include the larger economies, most importantly Germany. This outlook should be underpinned by a strengthening in domestic demand, supported by still accommodative monetary policy, and a lessening of the impact of fiscal consolidation in many countries. The existence of significant spare capacity across Continental Western Europe suggests that inflationary pressures are likely to remain subdued. In the UK interest rate rises and the appreciation of the exchange rate will work to mitigate against any significant pick-up in inflationary pressures.

DOMESTIC ECONOMIC CONDITIONS

Economic Activity

As evident in Chart 1, a step up in growth occurred in the first half of 1997. This followed a temporary slowing in the economy over the last three quarters of 1996. The pick-up is even more apparent in terms of non-farm activity. The composition of growth in the June quarter was affected significantly by a small number of large one-off transactions, including the sale of gold by the Reserve Bank of Australia (RBA) and the sale of the Loy Yang B power station by the Victorian Government to the private sector. These transactions involved a transfer between components of the expenditure measure of GDP and as such did not have any net impact on aggregate GDP. Abstracting from these transactions, GDP growth in the June quarter 1997 was driven by solid growth in private consumption, dwelling investment and a substantial contribution to growth from non-farm stocks.

Chart 1: Contributions to GDP(A) Growth
(seasonally adjusted, adjusted for one-off transactions)



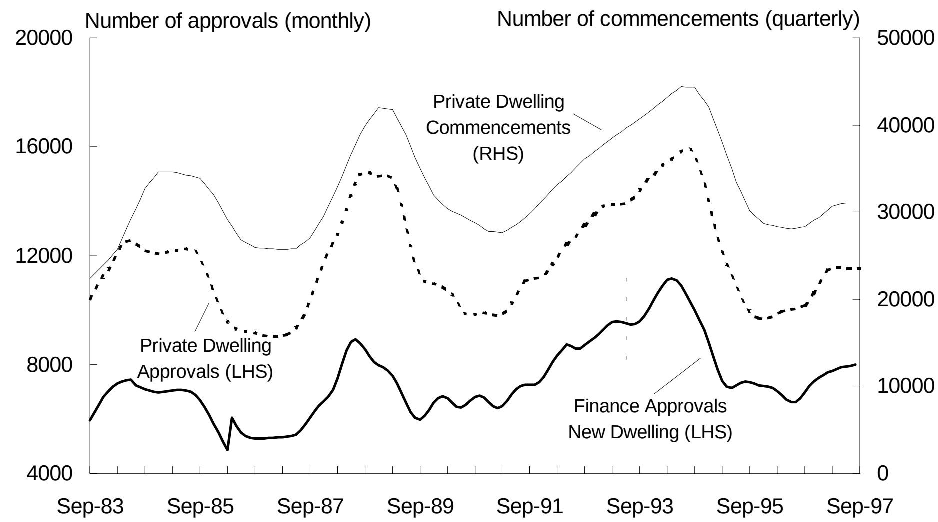
The step up in activity over the first half of 1997 was also evident in the major **business surveys.** These surveys reported an expected slight acceleration in activity over the second half of 1997 with trading conditions, sales and output all expected to improve further, which is also reflected in business confidence being at a relatively high level.

Private Investment

Growth in private investment in the June quarter 1997 was affected by the purchase of the Loy Yang B power station. New private investment, which abstracts from the effect of this purchase, was flat in the quarter. While there were downward revisions to non-dwelling building investment expectations for 1997-98 in the most recent Australian Bureau of Statistics (ABS) Private New Capital Expenditure (CAPEX) survey, these results are at odds with other indicators for investment in the sector. In particular, the value of work yet to be done for non-residential buildings and engineering construction is very high and the value of non-residential building approvals is also high. Recent business surveys also reported an expectation of solid growth in capital expenditure over the next twelve months. In contrast, **equipment investment** intentions were revised up significantly in the CAPEX survey and are consistent with the forecast of moderate growth in constant price investment in 1997-98. Other indicators which also suggest strong growth in equipment investment include: commercial finance commitments and leasing finance for equipment related activities remaining at very high levels in recent months; weak growth in equipment prices; and business credit growth continuing its upward trend. In addition, the positive environment that existed at the time of 1997-98 Budget that was supportive of a continuation in strong growth in business investment remains in place — interest rates are at very low levels, there is a continued absence of price pressures and capacity utilisation and the corporate profit share are at high levels.

The recovery in the dwelling sector has become more apparent since the Budget, with an additional two quarters of solid growth in **dwelling investment.** Dwelling commencements have also continued to trend upwards through 1997 (see Chart 2). While there was some weakness in the sector in the middle of 1997, this appears to have been temporary with more recent building approvals and housing finance data suggesting that the underlying conditions are firm. There remains, nevertheless, monthly volatility in the data. The favourable fundamental influences on the sector remain: the oversupply of housing created in the previous upturn is being eroded rapidly; vacancy rates in some areas are low; and housing affordability is expected to remain very high with low mortgage interest rates (which are at their lowest levels since 1973), rising household income and low house price inflation.

Chart 2: Trend Housing Indicators

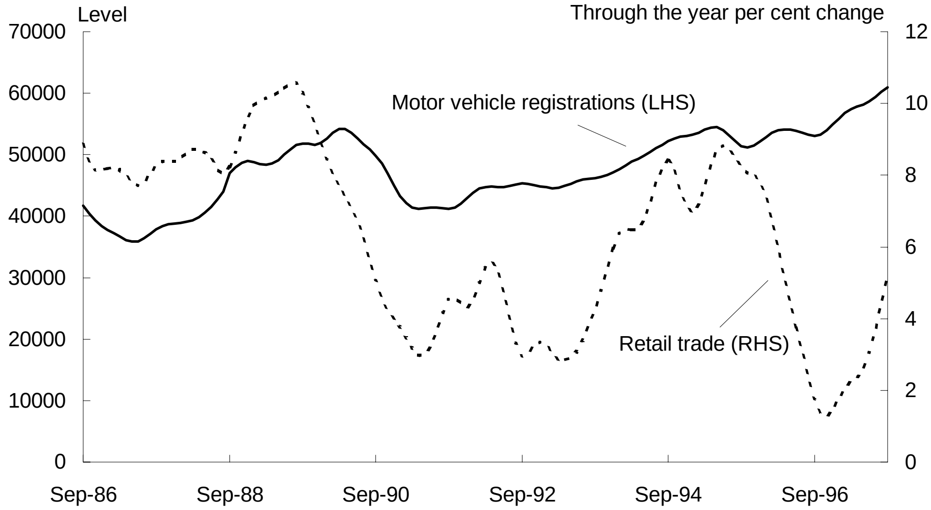


Note: There is a series break in finance approvals for new dwellings in July 1993.

Private Consumption

Consumer spending continues to grow strongly with the recovery in retail spending and strong growth in motor vehicle registrations evident in Chart 3. This is consistent with recent improvements in measures of consumer confidence with the Westpac-Melbourne Institute consumer sentiment index showing rises in each of the past four months. There has also been a pick-up in optimism regarding the future of the labour market with the unemployment expectations index well above the long-term historical average. The strength of the recovery in the labour market will impact on household decisions to continue to spend, both directly in terms of increasing household incomes and indirectly through improved consumer confidence. Businesses are also expecting trading conditions to improve, with the September quarter Australian Business Expectations survey recording a strong rise in expected growth in sales across all industries.

Chart 3: Partial Indicators of Consumption (trend data)



Changes in Stocks

There was a large fall in public authority **stocks** in the June quarter 1997, however this was due to the sale of gold by the RBA and the export of an ANZAC frigate, both of which were fully offset by a corresponding increase in exports. While there was a solid increase in private non-farm stocks, this only slightly exceeded sales growth (adjusted for the impact of the one-off transactions) and, as a result, the stocks-sales ratio was close to the historically low level recorded in the March quarter. The low level of the private non-farm stock-sales ratio suggests that firms are well placed to continue to increase production to match ongoing sales growth. Recent business surveys also indicate an anticipated build-up in private non-farm stocks in line with an outlook for strong sales growth, with the September quarter Australian Business Expectations survey indicating the largest expected increase in stocks over the coming year since that recorded in the June quarter 1994 survey.

Public Final Demand

Growth in public final demand was flat in the June quarter 1997, after abstracting from the sale of the Loy Yang B power station. Public final demand should pick up substantially in 1997-98, partly reflecting the base effects of the Loy Yang B sale in 1996-97 and information in the State Budgets released since May indicating strong growth from the State sector.

Imports and Exports of Goods and Services

Reflecting continuing strength in underlying demand and some increase in prices, the value of **imports** rose solidly in the September quarter. Implied volume outcomes to date appear consistent with budget expectations. **Exports,** excluding the effect of the sale of gold by the RBA and an ANZAC frigate, in the September quarter look to have shown continued modest growth in volume terms, complemented by a rise in prices partly associated with exchange rate movements in the quarter.

In terms of the outlook for rural exports, the widespread rain over much of the grain belt during the month of September helped to alleviate concerns that the lower-than-average rainfall recorded in previous months would continue and cause wheat yields in 1997 to be severely limited. Yields of the harvestable area of wheat in most southern and eastern regions are now expected to be at least around average levels. The Bureau of Meteorology is still forecasting an El Nino event to March 1998 and this is often associated with drier than normal conditions in eastern Australia. This could have some impact on planting conditions for next year’s winter crop — although this is particularly uncertain at this stage.

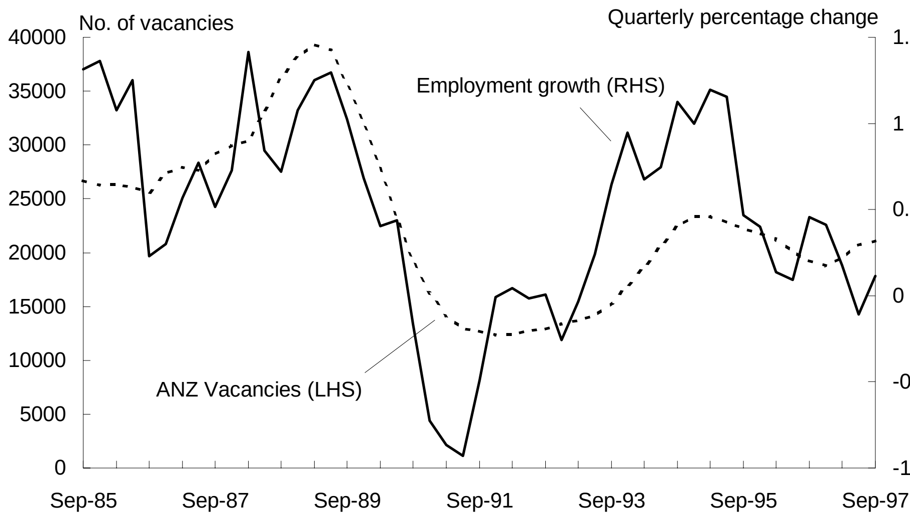
The monthly balance on goods and services has been in surplus for the past six months. The monthly outcomes to date in value terms indicate that strong growth in the volume of imports in the September quarter and a fall in merchandise exports (mainly reflecting the base effects of gold exports in the June quarter) has been offset by growth in service exports which will result in trade in goods and services being roughly in balance. With imports expected to grow more strongly than exports (which will be lower due to the base effect of the gold sales), the **current account deficit** should increase both in dollar terms and as a share of GDP in 1997-98.

Labour Market

Employment has grown solidly on average in 1997-98 to date. While monthly employment outcomes have been volatile recently, employment growth has averaged around 14 400 per month over the last four months.

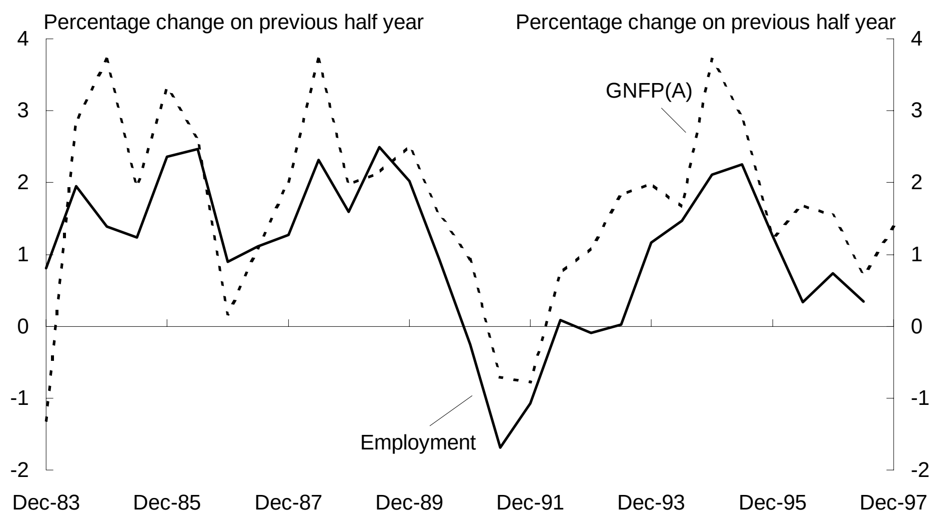
These outcomes appear consistent with the major job vacancy series, which have suggested solid employment growth in recent months. Both the ANZ Bank job advertisements series and DEETYA skilled vacancies index are at high levels. Despite falling slightly in the September quarter, the ABS vacancy series — which is the broadest measure of vacancies — remains at above average levels.

Chart 4: Trend Job Vacancies and Employment Growth



Supporting the outlook for strengthening employment growth is the step up in output growth in the first half of 1997 and the expectation that this momentum will continue through 1997-98.[1] Since most of the impact on employment from changes in activity occur in the three quarters following the change in activity, it would appear that short-term employment prospects remain positive.

Chart 5: Lagged Output Growth and Employment Growth



Note: GNFP(A) growth is brought forward six months, ie June 1997 half year growth appears as December 1997 half year growth, to illustrate the lag between growth in GNFP and employment.

1 The Economic Overview to the Winter 1997 *Economic Roundup* contains a detailed feature on the relationship between employment and output.

Major business surveys are indicating some improvement in employment in the near term. The latest ACCI Westpac survey reported that firms are expecting a strengthening in employment in the December quarter, with expectations at their highest level since June 1995. The National Australia Bank survey also reported a firming in employment expectations for the December quarter. Expectations are now slightly above the levels recorded for the previous two years.

While vacancy data and expectations surveys point to a continuation of solid employment growth over the coming months, overtime and average hours worked — generally considered leading indicators of changes in labour demand — have not showed any discernible pick-up. However, given the expansion of enterprise bargaining leading to employers cashing-out overtime payments and the ongoing volatility of the hours worked series, these series appear to be less reliable indicators of underlying labour market pressures.

The **unemployment** rate is expected to continue to fall over the near term, after falling in September and October. However, the impact on the unemployment rate of faster employment growth is likely to be partly offset by an increase in the participation rate as more people are encouraged to look for a job.

Wages and Prices

The forecast in the 1997-98 Budget was for some further moderation in **wage** pressures, with growth in average earnings on a national accounts basis being 4 per cent in 1997-98. Consistent with this outlook, the June quarter 1997 and preliminary September quarter 1997 data for average weekly ordinary time earnings for full-time adults show average quarterly growth of around 1 per cent. There is the prospect, however, that nominal wage growth may moderate further in line with low inflation and inflation expectations.

Inflationary pressures have continued to remain subdued, with an **underlying inflation** outcome in the September quarter of 1.5 per cent in through the year terms — the lowest outcome recorded since the series began in 1972. This low outcome reflects the favourable movement in nominal unit labour costs, the lagged impact of lower import prices, and ongoing competitive pressures.

The **headline Consumer Price Index (CPI)** fell again in the September quarter, with the annual inflation rate now at its lowest level since 1962. The declines in the headline CPI since the Budget largely reflect the fall in mortgage interest related charges, a decline in the cost of hospital and medical services (related to the introduction of the Government’s Private Health Insurance Incentive Scheme on 1 July 1997) and low underlying inflation.

1996-97: A Review of Economic Developments

This article provides an overview of developments in the Australian economy in 1996-97 and compares the outcome with what was forecast at the time of the 1996-97 Budget and the 1996-97 Mid Year Economic and Fiscal Outlook (MYEFO).

The Australian economy grew in 1996-97 for the sixth year in a row since the recession of the early 1990s. Activity in 1996-97 was supported by favourable international conditions, low inflation and an environment where interest rates were declining and wage pressures moderating. Such conditions were conducive to improvements in the balance sheets of the household and corporate sectors.

However, the preliminary outcome for 1996-97 indicates that growth in activity in 1996-97 was lower than expected at the time of the 1996-97 Budget and also lower than the revised forecasts included in the 1996-97 MYEFO. In terms of the profile of activity over the course of the year, growth eased in the second half of 1996 but was followed by a step up in activity in the first half of 1997. The main reasons for Gross Domestic Product (GDP) growth being lower than expected were lower than forecast contributions from private consumption, public final demand and non-farm stocks. Employment growth was also lower than expected, particularly in the latter half of 1996-97, reflecting the lower GDP growth in the first half of the financial year.[2]

COMPARING ECONOMIC FORECASTS WITH PRELIMINARY OUTCOMES

Prior to considering the performance of the economy in 1996-97 and comparing that with the 1996-97 Budget and MYEFO forecasts, it is worth first noting the assumptions underpinning the forecasts and highlighting that at this stage the Australian Bureau of Statistics (ABS) has produced its first preliminary estimate for growth in 1996-97.

As always, the 1996-97 Budget forecasts were based on key assumptions, historical relations between economic variables and judgements about likely outcomes.[3] One such key assumption is that policy will remain unchanged throughout the forecasting period. Such an assumption facilitates policy analysis

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2 The Economic Overview to the Winter 1997 *Economic Roundup* contains a detailed feature on the causes of the weakness in employment growth in the first half of 1997 and the relationship between employment and output and employment and real wages.

3 A detailed discussion of the purpose and methodology underpinning macroeconomic forecasts is contained in the Autumn 1996 *Economic Roundup*.

and, in particular, the consideration of the appropriateness of current settings. This is one area which distinguishes the official forecasts from those undertaken by the private sector.

The forecasting process also includes several key technical assumptions which may also differ from the approach taken in the private sector. These assumptions include that nominal interest rates and the exchange rate will be unchanged from their levels around the time of the forecasts. The latter reflects the difficulties in accurately forecasting short-run movements in exchange rates.

The June quarter 1997 National Accounts is the initial estimate for 1996-97 and provides the first opportunity to compare forecasts with outcomes. However, the first estimate is very preliminary and will be successively revised over time as the ABS incorporates more comprehensive and complete information into the National Accounts. Such revisions can be made over a number of years. Experience indicates that there is no set pattern to such revisions, although they can be significant. Accordingly, it is premature to make judgements about the relative ‘accuracy’ of forecasts on the basis of first estimates. Taking the budget forecasts from a few years ago to illustrate this point, the budget forecast for GDP growth in 1994-95 was 4½ per cent. In August 1995, the ABS published the first estimate of growth for that year, being 4.8 per cent. In the June quarter 1996 National Accounts, the ABS had revised its estimate for growth in 1994-95 to 4.1 per cent. A year and four National Accounts later (that is, June 1997), the estimate of growth in 1994-95 had been revised to 4.4 per cent. Thus, over time, the budget forecast had both under and over estimated growth, depending on the set of National Accounts used for the basis of assessment.

1996-97 OUTCOME

The August 1996 Budget and January 1997 MYEFO forecasts for GDP growth in 1996-97 of 3½ per cent compares with the preliminary estimate contained in the June quarter National Accounts of 2.5 per cent. Through the year growth to the June quarter 1997 was forecast in the Budget at 3¾ per cent and compares with the preliminary estimate of 3.2 per cent growth. The pattern of growth across the year indicated that activity slowed in the second half of 1996 before picking up in the first half of 1997.

Appropriateness of Forecasting Assumptions

As mentioned previously, the 1996-97 Budget forecasts were prepared on the basis of technical assumptions that nominal interest rates and the nominal exchange rate would be constant during 1996-97. There were four reductions in official **nominal interest rates** totalling 2.0 percentage points during 1996-97. Of these, only one had occurred prior to the Budget being released in August 1996, while three had occurred by the time of the MYEFO in January 1997. A fifth rate cut late in July 1997 brought the cash rate down to 5 per cent. The fall in interest rates reflected continued improvements in Australia's inflation outlook. The improvement in the inflation outlook also saw Australian nominal long-term interest rates fall over the course of the year, from over 8.8 per cent to around 7 per cent. Over the same period real interest rates also declined, though not by as much as the reduction in nominal rates. The profile of the reduction in real rates was also different to that of nominal rates, with most of the reduction in real rates occurring in the latter part of the year. Given the lags involved in the operation of monetary policy, the bulk of the impact of the interest rate reductions during 1996-97 are likely to be felt in 1997-98.

The **Australian dollar**, on a trade weighted (TWI) basis, was slightly higher than that assumed at the time of the 1996 Budget, averaging around 58.75 over 1996-97 (compared with an assumed TWI of 58). It is unlikely that this difference would have had a significant impact on activity during 1996-97, particularly given that the profile of the TWI was such that it was around 58.25 in the first half of the year, then rose on the back of strong commodity prices to a peak of 61.5 in March, before falling back to around 57 by the end of the year.

As expected at the time of the 1996-97 Budget, the **international economy** was supportive of growth in the domestic economy over 1996-97. Real GDP in Australia's major trading partners is estimated to have grown at 4½ per cent in the year (compared with the 4¼ per cent assumed at the time of the 1996-97 Budget). This outcome was driven by continued strong growth in the United States and East Asia and stronger growth in Japan's private sector.

Domestic Activity

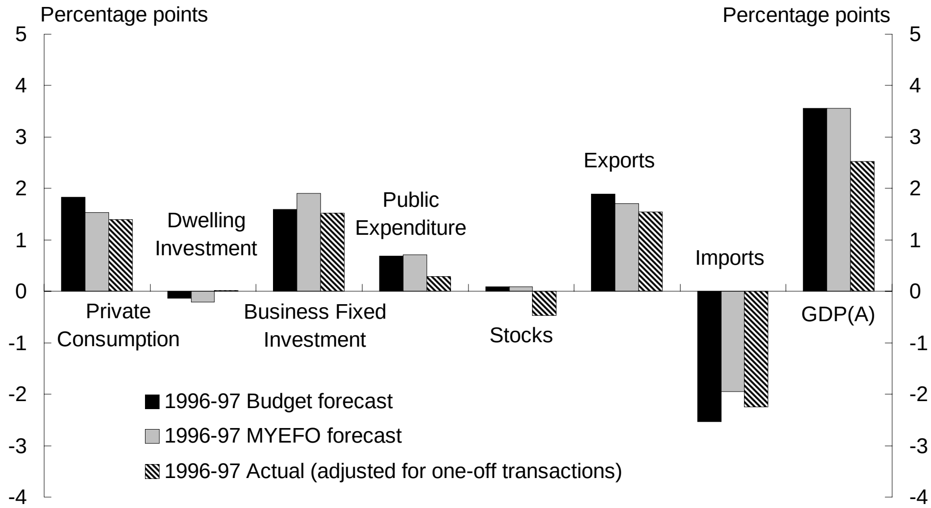
Table 1 compares the August 1996 Budget and January 1997 MYEFO forecasts with the preliminary outcome for 1996-97. The composition of GDP growth in 1996-97 was affected by significant one-off transactions, such as the sale of the Loy Yang B power station by the Victorian Government and the sale of gold by the Reserve Bank of Australia (RBA). These transactions involved a transfer from one component of activity to another component and thus did not have any net impact on aggregate GDP. Abstracting from these, the main reasons for GDP growth being lower than expected were lower than forecast contributions from private consumption (though this was partly offset by stronger activity in the dwelling sector), public final demand (the outcome being less than that budgeted for) and non-farm stocks (see Chart 1).

Table 1: 1996-97 Budget and MYEFO Forecasts and Outcomes

	1996-97 Year Average Budget Forecast	1996-97 Year Average MYEFO Forecast	1996-97 Year Average Outcomes	1996-97 Year Average Outcomes adjusted (a)
Demand and Output				
Private consumption	3	2 1/2	2.3	
Private investment				
Dwellings	-3	-5	0.2	
Total business investment	14	17	15.9	13.5
Non-dwelling construction	15	20	16.9	na
Plant and equipment	14	16	15.5	na
Private final demand	4 1/2	4	4.2	3.9
Public final demand	3 1/4	3 1/4	0	1.4
Total final demand	4 1/4	4	3.3	
Increase in stocks (b)				
Private non-farm	0	0	-0.3	
Farm and public authority	0	0	-0.7	-0.1
GNE	4 1/4	4	2.2	
Exports	8	-	9.5	6.8
Imports	11	-	10.3	
Net exports (b)	- 3/4	- 1/4	-0.1	-0.7
GDP (A)	3 1/2	3 1/2	2.5	
Non-farm product	3 1/2	-	2.1	
Farm product	6	-	14.4	
Other Selected Economic Measures				
Prices and wages				
Consumer Price Index - Headline (c)	2	1	0.3	
Consumer Price Index - Underlying (c)	2 3/4	2	1.7	
Average earnings	5	4 1/2	5	
Non-farm nominal unit labour costs	2 1/2	-	3.3	
Labour market				
Employment (Labour Force Survey)	1 1/2	1 1/2	1.1	
Unemployment rate (per cent) (d)	8 1/4	8 1/2	8.7	
Participation rate (per cent) (d)	63 3/4	63 3/4	63.2	
Household income and saving				
Real household disposable income	2 3/4	-	3.25	
Household saving ratio (per cent)	2 1/2	-	5	
Current account balance ($b)	-20	-20	-16.5	

(a) The adjustments reflect negating the impact of: the sale of the Loy Yang B power station by the Victorian Government to the private sector; the sale of gold by the RBA; and the sale of an ANZAC frigate.
(b) Percentage point contribution to growth in GDP (A).
(c) Through the year to June quarter.
(d) Estimate for the June quarter.

Chart 1: Contributions to GDP(A) Growth(a)



(a) Year-average growth.

Growth in **consumer spending** was lower than both the 1996-97 Budget and MYEFO forecasts for 1996-97, mainly reflecting weakness in the retail sales component of private consumption. Private consumption normally moves very closely with household disposable income, although in 1996-97 the latter grew at a faster rate than forecast. This discrepancy may suggest a weakening of consumer confidence in 1996-97, which led to a more cautious approach to spending. This would appear to be the case, as evident in the measures of consumer confidence and unemployment expectations produced by the Westpac-Melbourne Institute which were at very low levels in the September quarter 1996 — a quarter in which private consumption fell. The fall in consumption in the September quarter was reflected in the downward revision to the forecast for consumption growth for 1996-97 contained in the MYEFO. Given the strength in household disposable income and the weaker consumption growth, there was a larger than expected offsetting increase in the household saving ratio in 1996-97 to 5.0 per cent, which is the highest yearly level since 1990-91.

The recovery in the **housing** sector became apparent from the December quarter 1996 National Accounts (released in March 1997) onwards, with growth in dwelling investment exceeding both the Budget and MYEFO forecasts. This pick-up was driven by a significant improvement in housing affordability, which rose to an historically high level. The rise in housing affordability was due in large part to the reductions in mortgage interest rates flowing from the reduction in official interest rates and increased competition in the home lending mortgage market.

Private **business investment** (abstracting from the Loy Yang B transaction) continued to grow rapidly in 1996-97, though at a slightly lower rate of growth than forecast in both the 1996-97 Budget and MYEFO. While both sets of forecasts were based on around average realisation ratios for private new capital expenditure, in the case of non-residential construction, expectations proved to be significantly stronger than the actual outcomes in 1996-97. Even so, very strong growth was experienced in both the non-residential construction and plant and equipment components of investment. On an industry basis, particularly large increases were experienced in mining, property and business services and the finance and insurance sectors. The strong growth overall was supported by the absence of price pressures throughout 1996-97 and the high levels of capacity utilisation and corporate profit share. While the reduction in real interest rates through 1996-97 would have added to this supportive environment, as noted above, the bulk of the impact of the interest rate reductions is likely to be felt in 1997-98.

Abstracting from the sale of the Loy Yang B power station, growth in **public final demand** in 1996-97 was around 1.7 per cent, compared with a forecast of 3¼ per cent in the 1996-97 Budget and MYEFO.[4] Significant factors that led to this outcome included: commercial decisions made by major public trading enterprises that resulted in lower than expected investment; and differences in the timing between the payment and delivery of military hardware (the transaction being recorded in the National Accounts when ownership passes rather than when payments are made). These factors are consistent with the background noted in the 1996-97 MYEFO that estimates of public final demand tend to be highly volatile from quarter to quarter, which can alter year average estimates significantly.

A large run-down in farm and public authority **stocks,** together with the sharp slow down in the accumulation of private non-farm stocks resulted in a much larger overall detraction by stocks from output growth than that incorporated in the 1996-97 Budget and MYEFO. However, the large fall in public authority stocks was due to the sale of gold by the RBA and the export of an ANZAC frigate, both of which took place in the last quarter of 1996-97 and were fully offset by a corresponding increase in exports. Setting these aside, stocks detracted 0.5 percentage points from GDP growth in 1996-97. This was still a significantly bigger detraction than included in the forecasts and in large part reflects the unexpected large run-down in private non-farm stocks in the first half of 1997, which resulted in the stocks-sales ratio falling to an historically low level. These events contrasted with the experience over the previous three years or so — when the stocks-sales ratio was relatively flat — and suggests that in 1996-97 firms cleared any excess stocks.

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4 The National Accounts concept of public final demand does not cover the bulk of Commonwealth outlays (such as transfer payments) nor does it include the impact of changes in Commonwealth revenue. In addition, the National Accounts concept of public demand includes not only the Commonwealth budget sector, but also the non-budget sector, Commonwealth public trading enterprises and the State and local government sectors — the latter being the largest component of public final demand

As anticipated at the time of the 1996-97 MYEFO, net exports detracted less from GDP growth in 1996-97 than forecast at the time of the 1996-97 Budget. **Imports** of goods and services grew by 10 per cent in 1996-97, broadly in line with the 1996-97 Budget forecast of 11 per cent. Despite slower overall growth in consumption expenditure, imports of consumption goods rose solidly, while strong business investment resulted in an increase of over 14 per cent in the constant price value of capital imports. **Exports** of goods and services rose by around 7 per cent in 1996-97 (abstracting from the one-off sales), compared with the 1996-97 Budget forecast of 8 per cent. The slightly lower outcome for export growth reflected lower than expected exports of elaborately transformed manufactures and some weakness in exports of non-rural commodities, which more than offset the boost to exports from the record wheat crop in 1996-97.

The **current account deficit** was $16.5 billion in 1996-97, around 20 per cent lower than the previous year. This outcome was well below the 1996-97 Budget and MYEFO forecasts of $20 billion, a result largely attributable to the impact of the RBA gold sales, which as noted above took place in the June quarter of 1996-97.

Labour Market

Following solid growth in the first half of 1996-97, **employment** growth was broadly flat in the second half of the year. Employment grew by 1 per cent through the year to the June quarter. Weak employment growth in the first half of 1997 appears to have been largely a lagged response to the moderation in output growth in the second half of 1996, combined with a pick-up in real wages during 1996; the latter primarily due to falling inflation rather than rising nominal wages.[5]

The **unemployment** rate was largely unchanged through most of 1996-97, remaining around 8.7 per cent in the June quarter 1997, higher than the 1996-97 Budget forecast of 8¼ per cent and 1996-97 MYEFO forecast of 8½ per cent. This outcome reflects the lower than forecast employment growth and a fall in the participation rate over the course of 1996-97 (with the slower employment growth likely to have discouraged workers from remaining in the work force).

Wages and Prices

In 1996-97, growth in the National Accounts measure of **average earnings** (AENA) was consistent with the 1996-97 Budget forecast, while growth in average weekly ordinary time earnings (AWOTE) for full-time adults was weaker than expected. AWOTE is an indicator often used to examine wage pressures because it is less affected by changes in the composition of the labour

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5 The Winter 1997 *Economic Roundup* contains a comprehensive analysis of recent labour market conditions.

force between full-time and part-time employees. The weaker than expected growth in AWOTE in 1996-97 reflected a number of factors, including lower than anticipated inflation and a moderation of inflationary expectations, and lower than expected output and employment growth. Non-farm nominal unit labour costs were higher than the Budget forecast largely due to lower than expected total hours worked, which increased average hourly labour costs.

Underlying **inflation** moderated throughout 1996-97, to be 1.7 per cent in the year to the June quarter, below both the 1996-97 Budget forecast of 2¾ per cent and 1996-97 MYEFO forecast of 2 per cent. This low outcome largely reflected the influence of lower import prices, together with an easing in demand pressures, which continued throughout the year.

Headline inflation was 0.3 per cent through the year to the June quarter 1997, considerably lower than the 1996-97 Budget forecast of 2 per cent and 1996-97 MYEFO forecast of 1 per cent. The low headline outcome was mainly due to a lower than expected underlying inflation rate, and reductions in mortgage interest rates during 1996-97 following the Budget.

Trends in Foreign Direct Investment Inflows

This article briefly examines recent trends in foreign direct investment in Australia, both in the context of the longer-term perspective and relative to the experience of other countries. It also discusses the role of foreign direct investment within Australia's overall investment requirements, and outlines characteristics of foreign direct investment in relation to sector and type of asset acquired.

OVERALL INVESTMENT TRENDS

Business investment growth has strengthened since the early 1990s recession, with the result that in constant price terms investment as a share of Gross Domestic Product (GDP) reached a record level in 1996-97. Surveyed business intentions and continuing favourable economic fundamentals point to ongoing strong growth in the period ahead.

As a result, capital stock growth in recent years has recovered to above average rates, and is forecast to continue to strengthen. Coupled with improvements in the efficiency with which the capital stock is used, this strong growth in the capital stock provides the foundation for sustained strong growth in activity and employment.

Australia accesses foreign saving through either borrowing (debt) or greater foreign ownership of Australian activities (equity). Foreign direct investment (FDI) is one form of the latter. For official measurement purposes, FDI is regarded as an equity interest of 10 per cent or more in an enterprise.

A direct comparison of trends in FDI and capital expenditure (investment) is inappropriate. The latter reflects expenditure associated with the creation of new fixed assets (both related to equipment and machinery and to buildings and infrastructure development) or the accumulation of stocks of finished products and work in progress. FDI can be directed towards the acquisition of existing assets as well as to the acquisition of new assets and the resultant expansion of the physical capital stock, and the official data that is available does not distinguish between the two. That said, foreign investment is a relatively small source of funds for investment in Australia. Over the period since the early 1960s, FDI in Australia has been equivalent to around 7 per cent of gross fixed capital expenditure.

FDI has in the past followed a similar trend to total business investment, reflecting the fact that the same basic factors are needed to give good rates of return on foreign and domestic investment — macroeconomic stability, microeconomic policies to improve efficiency and flexibility and a skilled labour market. Consequently, the factors currently creating a favourable environment for strong domestic investment growth are also likely to attract foreign investment.

FDI AND THE SAVING — INVESTMENT BALANCE

The Government’s fiscal consolidation strategy is designed to reduce Australia’s reliance on foreign saving, of which FDI is a component.

Australia has traditionally drawn on foreign saving to fund higher levels of investment than domestic saving alone would allow and to promote faster economic growth and higher living standards. As a result, Australia usually runs a current account deficit (which, over time, equals the excess of national investment over national saving) and this has meant growing net foreign debt and growing foreign ownership of Australian assets as non-residents contributed to capital formation. The widening in the current account deficit in the 1980s resulted in a faster build-up of net foreign debt and ownership. Concern about an ‘excessive’ build-up in foreign liabilities has focussed policy attention on boosting domestic saving to finance more of domestic investment locally.

The Government’s commitment to underlying budget balance over the cycle specifically addresses those concerns, and will see the budget swing into underlying surplus in 1998-99. Reduced public sector borrowing will reduce our net reliance on foreign saving. This is the intended outcome of the Government’s fiscal strategy.

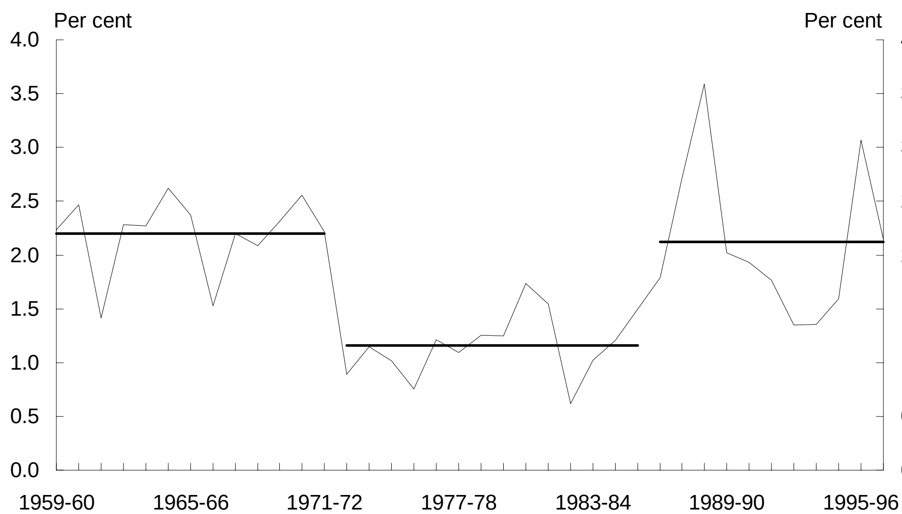
While it is difficult to predict the extent to which different forms of capital inflow will be reduced, it is possible that there will be a reduction in net FDI inflows. If that occurs, it would at least partially reflect our greater ability to fund our own investment, rather than a decline in our attractiveness as a destination for FDI.

TRENDS IN FDI INFLOWS

Over the past decade, FDI inflows as a share of GDP have returned to levels comparable with those of the 1960s (Chart 1) and have been significantly higher than in the 1970s and the first half of the 1980s. In 1996-97, FDI inflow was a little more than 2 per cent of GDP (and amounted to $11 billion).

Annual FDI inflows are highly volatile. Depending on the years chosen, FDI can be argued to have grown rapidly from 0.6 per cent of GDP in 1982-83 to 3.0 per cent in 1995-96, or fallen precipitously from 3.6 per cent of GDP in 1988-89 to 1.6 per cent in 1994-95 (see Chart 1). Neither statement is balanced and the broad conclusion is that there is no evidence of either a declining trend or overall weakness in Australia's FDI inflows in the 1990s compared with the inflows in earlier decades.

Chart 1: FDI Inflows as a Proportion of GDP



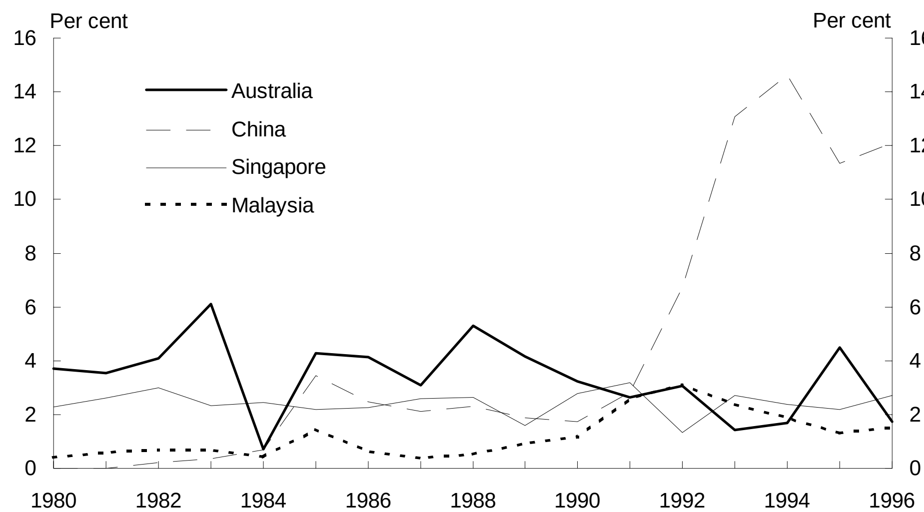
Source: ABS

FDI inflows reached an exceptionally high proportion of GDP in the late 1980s, coinciding with an unsustainable domestic investment boom, and the subsequent decline has to be seen in that context. FDI inflows are also influenced by Australia's business cycle and fell as a share of GDP in the period of weaker economic activity in the early 1990s. Since the mid-1980s, net FDI inflows have on average represented a smaller proportion of net total capital inflows. This reflects increased access to debt financing and increased attractiveness of the Australian share market where net portfolio investment in Australia increased to average 3.6 per cent of GDP since the mid-1980s compared with 1.5 per cent in the period from 1960 to 1985.

Australia's Share of Global FDI Inflows

Australia's share of world FDI inflows in 1996 was lower than it was in 1985 (Chart 2). However, given the sharp volatility of outcomes in the past three years, the extent of the apparent trend decline is unclear. Some decline in Australia's share of global inflows since the mid-1980s would not be unexpected given the rapid growth in China's share in the 1990s (reflecting the effects of the liberalisation of the Chinese economy) and given the rapid growth in GDP and total investment requirements in a number of East Asian economies during this period.

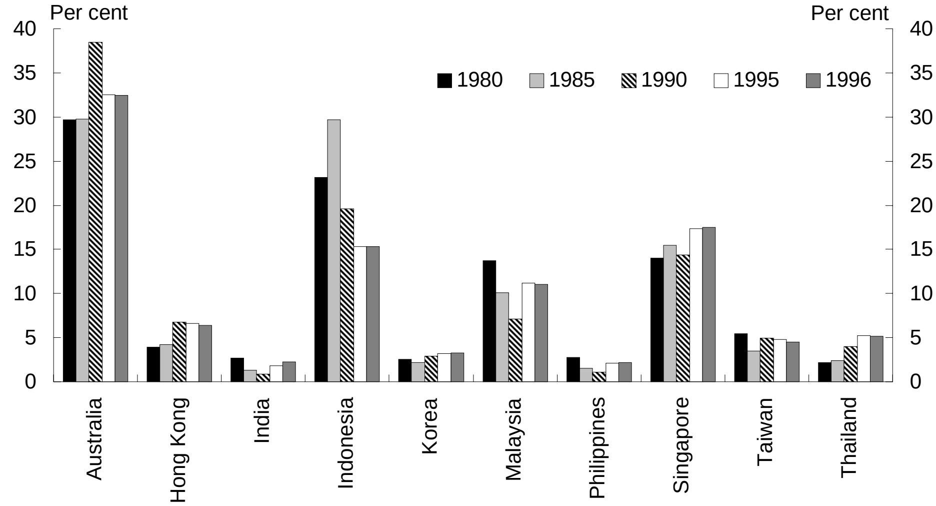
Chart 2: Major FDI Recipients in Asia — Share of Total World FDI Inflows



Source: Department of Foreign Affairs and Trade.

Looking at the stock of FDI reduces the impact of volatility in FDI flows, and hence makes the analysis much less dependent on the particular time period chosen. As illustrated in Chart 3, Australia has the highest share of the FDI stock in East Asia excluding China and it shows no sign of declining over time. Also, while East Asia's FDI stock has increased significantly as a proportion of GDP between 1980 and 1996 (from around 5 per cent to 16 per cent), Australia's stock has risen by a greater proportion (from 8 per cent to 34 per cent), and by much more than the increase for industrial countries (from 5 per cent to 10 per cent).

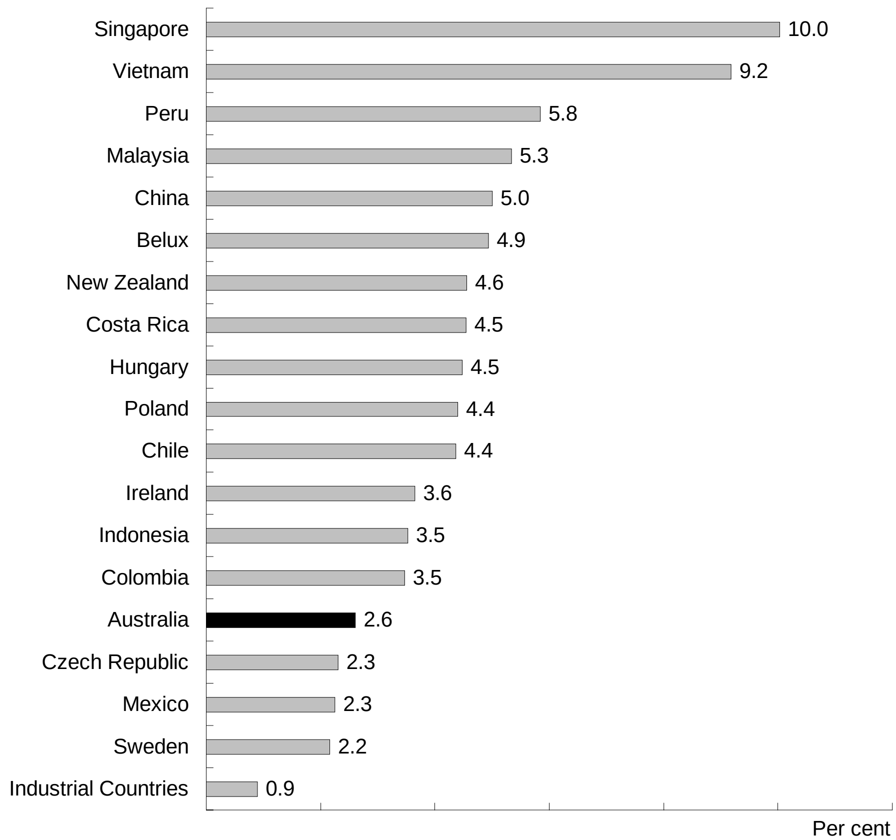
Chart 3: Share of Asian FDI Stock (excluding China)



Source: Department of Foreign Affairs and Trade.

Finally, while Australia ranked among the world's top 20 recipients of FDI relative to GDP in 1996, it is significant that a high level of FDI inflows is not necessarily associated with strong economic performance. With the notable exception of Singapore (and the arguable exception of some others), most of the largest recipients shown in Chart 4 (for example, Vietnam and Peru) are economies in transition or otherwise in need of foreign savings. Many of the highest FDI recipients tend to receive a high proportion of their foreign investment as FDI because (unlike Australia) their relatively underdeveloped financial markets provide limited (if any) alternatives for foreigners to invest in other forms (such as equity or debt securities).

Chart 4: Largest Recipients of Foreign Direct Investment in 1996
(FDI inflow as a proportion of the recipient country's GDP)



Source: Department of Foreign Affairs and Trade (overseas data), ABS (Australian data).

Sectoral Composition of Australia's FDI Inflows

While sectoral data on FDI are limited, they do not suggest that FDI inflows go predominantly to any one sector of the economy. Sectoral Australian Bureau of Statistics data on FDI inflows are available only for the 1980s and 1990s and do not necessarily reflect the final industry destination of the investment. That said, the data show only a relatively small proportion (around 4 per cent) has been directed to mining in the 1990s. The remainder has been fairly equally shared among the manufacturing, finance and other sectors. The share allocated to manufacturing has shown no long-term decline.

Similar observations are drawn from Foreign Investment Review Board data. These relate to foreign investment applications received in the administration of foreign investment policy and their reliability as indicators of actual FDI is therefore subject to significant qualification. Nevertheless, they indicate brisk growth in applications in the manufacturing and service sectors in the last four years, with proposed investment increasing more than three-fold for manufacturing (including electricity, gas and water) and over two and a half times for services (excluding tourism). There was a slight fall in the value of proposed investment in mineral exploration and development over this period, although the number of applications increased for that sector.

Some FDI in the 1990s would have involved the partial or full acquisition of existing businesses, particularly as a result of Commonwealth and State privatisation programmes. A distinction is sometimes made between FDI into existing businesses and that involved in establishing new businesses. However, what is crucial for growth of the capital stock is the overall pool of funds available to fund new investment. If FDI involves the purchase of stakes in existing businesses (whether previously privately or government owned), it still contributes to the pool of savings available for investment.

Some attention is given to the fact that FDI in establishing a new business will include an element of technology transfer. While FDI can be a source of technology transfer, this aspect of FDI is more important for developing economies, which lack the economic infrastructure to import technology by other means, than for a developed economy. FDI is a less important channel for technology transfer for industrial countries like Australia — globalisation of the world economy has meant that new technologies spread quickly between industrialised countries.

There are likely to be other benefits to Australia from FDI, for example those that flow from importing management skills or improving linkages with foreign markets. However, this does not require that FDI be associated with new projects — FDI directed to the purchase of existing businesses can also have these benefits attached.

CONCLUSION

Trends in FDI — which can be used for the acquisition of existing assets as well as for increases in productive capacity — should not be directly compared with trends in capital expenditure. Nevertheless, both FDI and business investment will be responsive to factors influencing rates of return on investment, and broad trends in both since the early 1960s have been similar. Recent and anticipated levels of investment are consistent with growth in the capital stock capable of supporting ongoing growth in output and employment.

Abstracting from volatility, recent FDI inflows as a share of GDP are around the average of outcomes experienced since the early 1960s. Furthermore, Australia's share of the total FDI stock is the highest of any country in the Asian region except China.

FDI in Australia is not concentrated in any particular industry sector, and contributes to the overall pool of saving available for productive investment, even if it is itself directed toward existing assets.

Being Fiscally Responsible in Policy Development

The following is the text of a speech given by Mr Steve French, Assistant Secretary, Budget Policy Branch, Fiscal Policy Division, Treasury to the fifth annual Government Policy Conference, held in Sydney on 4–5 August 1997.

INTRODUCTION

I have been asked to speak about 'Being Fiscally Responsible in Policy Development'. In doing so, I would like to cover three main issues:

- first, what is fiscal responsibility?
  - This includes an outline of the framework adopted by the Commonwealth for fiscal policy determination and the enhanced transparency and accountability mechanisms introduced with the Charter of Budget Honesty;
- second, I would like to cover the fiscal strategy being adopted within that framework, and the benchmarks that are being used to assess fiscal policy; and
- third, I would like to give some brief indications about the implications of greater fiscal responsibility and discipline for the development of policies.

FISCAL RESPONSIBILITY

The meaning of fiscal responsibility is fairly simple and clear, though there are two dimensions to it:

- first, it implies that government budget setting — outlays, revenues, and balances — are determined so that they promote strong, sustainable growth in economic activity and employment. In addition, it implies that government budgets are themselves sustainable, and do not store up problems for future generations, including by racking up high public debts; and
- second, being fiscally responsible implies that government operates efficiently and effectively — in raising revenue and in spending taxpayers' money. This aspect of fiscal responsibility can help to bolster the first.

I'll return to efficiency and effectiveness and the complementarity of policies a little later, but I would like initially to focus on the former set of issues — the macroeconomic aspects of fiscal responsibility.

In the 1990s, the term 'fiscal responsibility' has been associated with the introduction of fiscal responsibility legislation in New Zealand and at the State government level in Australia. In similar vein, the Commonwealth has introduced a Bill for a Charter of Budget Honesty.

Moves towards greater fiscal responsibility are not new. Fiscal responsibility has long been advocated by international organisations, such as the International Monetary Fund (IMF), and national governments themselves.

This has involved the promotion of better budgeting systems — such as the development of budget forward estimates and programme evaluation — and reforms to budget presentation — including the usage of international classifications for government financial estimates, based on economic concepts. In some cases it has also been reflected in attempts to enshrine fiscal rules in legislation or in international agreements, such as those relating to the criteria for European Monetary Union (EMU) eligibility.

These developments have had varying degrees of success — in large part they have been positive developments, though it has to be acknowledged that the implementation of some fiscal rules has not been a success.

In any event, while fiscal responsibility is not 'new', I think that the frameworks now operating and being advanced in Australasia are probably the 'state of the art' amongst developed countries.

Why are these fiscal responsibility frameworks emerging? It is essentially because the fiscal record in many countries is not what it should be. In short, there has been a tendency for governments to spend more than they raise in revenue and to run deficits.

In Australia, the need for improved fiscal outcomes is demonstrated by the persistence of Commonwealth budget deficits over the past twenty years. As Chart 1 shows, there has been a structural deterioration in the Commonwealth's underlying balance since the 1960s, when we were generally running surpluses. The Commonwealth's budget deficits of the past twenty years have been associated with a ratcheting up of Commonwealth general government debt relative to Gross Domestic Product (GDP) over time (as shown in Chart 2).

Chart 1: Underlying Budget Balance

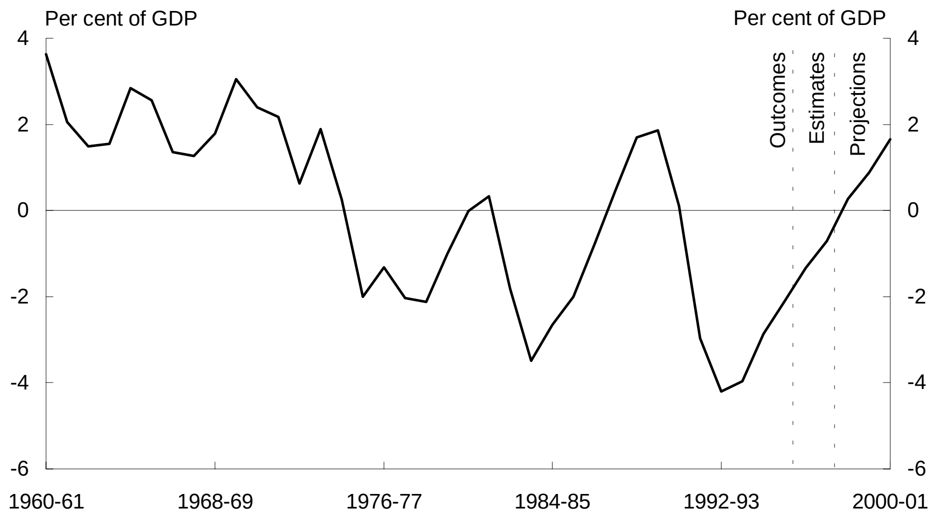
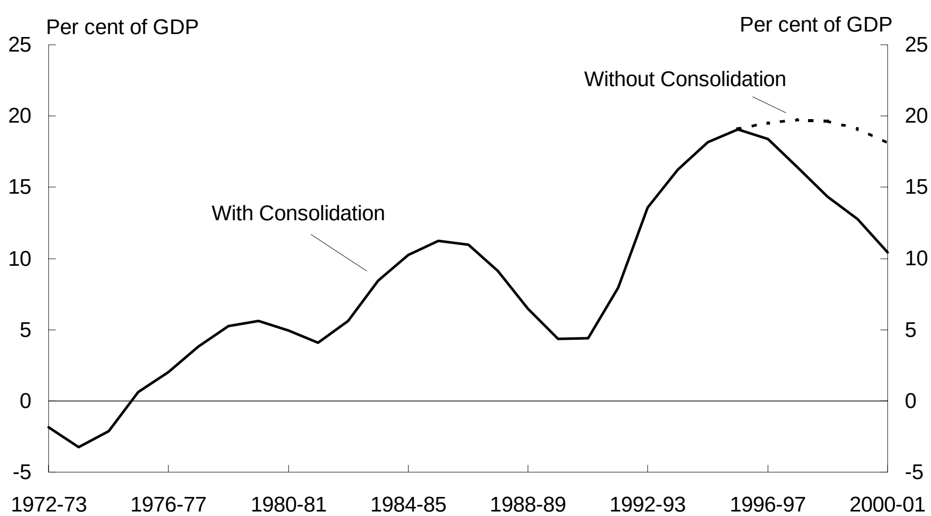


Chart 2: Commonwealth General Government Net Debt



This record is the background against which the Charter of Budget Honesty Bill has been introduced into the Parliament. The philosophy of the Bill is to improve fiscal responsibility and discipline by:

- enhancing the transparency of fiscal policy setting and ensuring that governments explicitly outline their fiscal policy intentions; and
- increasing accountability for fiscal policy outcomes, by ensuring that there is transparency in fiscal policy reporting and that comprehensive information on the fiscal outlook is available.

This enables the public and financial markets to judge governments on their fiscal performance.

The philosophy of the Bill is consistent with international experience which suggests that the greater the level of fiscal transparency the better tends to be the record of fiscal discipline.

The Charter ensures that governments determine and set out their policy in a medium-term framework — and explain how the shorter-term budgetary targets that they set themselves fit within that medium-term framework. The Charter is not about setting down prescriptive fiscal rules or what sort of accounting systems should operate. It recognises that there may be a need for governments to account for changing economic circumstances and to have some flexibility in determining and implementing fiscal strategies. But what it does do is ensure that governments outline their fiscal strategies, objectives and targets — and that they are held publicly responsible for delivering against those objectives and targets.

I think it is worth briefly running through the Charter's key elements:

- the framework for fiscal policy setting; and
- the framework for fiscal reporting.

Fiscal Policy Setting

Under the Charter, governments are required to produce a fiscal strategy statement annually, which must outline:

- the Government's medium-term fiscal strategy;
- key fiscal objectives, targets, and expected outcomes for the budget and three forward years; and
- any actions that are temporary in nature to moderate the cycle, and processes for their reversal.

The Government's fiscal objectives need to be set in accordance with the principles of sound fiscal management. Among other things, that requires governments to:

- contribute to adequate national savings;
- carefully manage financial risks and ensure debt is maintained at prudent levels;

- maintain the integrity of the tax base and stability and predictability in the tax burden; and
- account for the effects of policies on future generations.

Fiscal Reporting

In addition to the annual fiscal strategy statement, there are a number of other elements of the enhanced fiscal reporting framework under the Charter.

First, economic and fiscal outlook reports must be produced both at the time of the budget and mid-year. Apart from information on the fiscal and economic forecasts and projections for the budget and three forward years, the reports need to include:

- a statement of risks to the fiscal outlook, including contingent liabilities facing the Government and a statement on the sensitivity of fiscal estimates to changes in assumptions;
- information on tax expenditures — that is, concessions in the tax system, the budgetary costs of which would not otherwise be clear; and
- estimates on a general government basis (in addition to the budget sector). These general government estimates are not significantly different from the Commonwealth's budget definitions and presentation, but their publication does ensure that information consistent with international standards (and therefore comparable with other government financial statistics) will be continually available in the future.

Second, a report on the final budget outcome must be produced by the end of September each year (with information on both the budget and general government sectors).

Third, an intergenerational report is to be produced every five years. This must outline the effect of maintaining current budgetary policies over a forty year period. The objective is to provide a clear understanding of the longer-term implications of current budgetary settings and an assessment of whether current policies are sustainable in the longer term and consistent with the overall fiscal objectives of the Government.

Finally, the Charter ensures election campaigns are conducted on the basis of up-to-date information on the fiscal outlook, with a pre-election economic and fiscal outlook report to be produced no later than ten days after an election is called. Provision is also made for the costing of election commitments of the caretaker Government and the Opposition during election campaigns by the bureaucracy. The aim of these arrangements is to enhance the chances of a disciplined approach to fiscal policy and to raise accountability for pre-election policy announcements.

Beyond the Charter, I should note that the Commonwealth and State Governments have also agreed to a uniform presentation framework**,** which ensures a common core of information is produced in Commonwealth and State budgets, notably: three year forward estimates are to be produced for the general government sector; and the publication of mid-year reports (by the end of February each year). This helps ensure that there is fiscal transparency and accountability at both major levels of government in Australia, supplementing initiatives of individual States.

FISCAL STRATEGY

So how is this framework for fiscal policy setting and determination being put into effect?

The Charter of Budget Honesty, while not yet passed into legislation, is being complied with and the information required by the Charter has been fully outlined in this year's Budget Papers.

A key is the fiscal strategy statement. There are two important components to the fiscal strategy — with the first relating to the underlying budget balance and the second to public debt.

The central plank of the strategy is to lift the level of national saving by increasing public saving. As a guiding principle, the aim is to maintain the budget in underlying balance, on average, over the course of the economic cycle. That is designed, over time, to ensure that the budget helps to address Australia's national saving-investment imbalance. I think it is worth covering this in a little detail.

Australia's current account deficit is the corollary of the imbalance between its national savings and investment — it represents the extent to which Australia has to call on foreign savings to finance its investment. While current account deficits are not necessarily a problem, countries running them do need to maintain the confidence of financial markets.

There has been a structural deterioration in Australia's current account performance over time — averaging a little over 2 per cent of GDP in the 1960s and 1970s, but over 4 per cent since the early 1980s. This has raised some doubts about the sustainability of the current account and has placed Australia in a situation where we are more vulnerable to economic shocks. It has tended to limit our ability to sustain strong economic growth.

Investment, provided that it is soundly based, is what is needed to sustain strong long-term economic prospects; it is inadequate national savings that has been at the root of the deterioration in the current account position. To an important degree, Australia's poor savings performance has reflected the underlying budget deficits run by the Commonwealth over the past twenty years or so. Correcting this deterioration in the fiscal position should help, over time, to improve our current account position and to create the conditions for stronger sustainable economic growth.

Why do we talk about the underlying budget balance? Traditionally, the main measure of the budget balance has been the simple difference between outlays and revenues — what we call the 'headline balance' today. However, the main focus of the Commonwealth's fiscal strategy has been the 'underlying balance' — which excludes the impact of net advances (that is, net policy loans and purchases and sales of equity assets). This is because this measure approximates net lending in the national accounts, which gives the best indication of the Government's direct impact on national saving. Moreover, as the underlying measure excludes transactions such as asset sales it can give a better indication of the sustainability of fiscal policy. Asset sales in recent years have been quite large, but they cannot be expected to continue forever boosting budget outcomes.

In addition, what do we mean when we talk about balance over the cycle? This is not saying that governments cannot run deficits during an economic downturn. Governments may wish to operate fiscal policy flexibly in a downturn. It may be necessary to allow 'automatic fiscal stabilisers' to operate in order to cushion the negative effects of a downturn — for example, to allow for the 'automatic' higher expenditure on social welfare associated with rising unemployment.

However, there has been a tendency for governments over a long period, not only in Australia, to operate fiscal policy in an asymmetric way — to take discretionary measures to ease fiscal policy in a downturn, but not to reverse them in the upswing. The goal of balance over the cycle addresses that tendency — requiring that if deficits are run in the downturns, surpluses need to be achieved in more favourable economic circumstances. This is bolstered by the requirement I mentioned earlier in the Charter of Budget Honesty, that governments identify the way in which any temporary measures to ease the effects of a downturn will be unwound in the upturn.

The second plank of the fiscal strategy is to achieve and maintain prudent levels of government debt. The extent of accumulated net debt is a key measure in judging the overall strength of a government's fiscal position. High levels of net debt impose a cost on future taxpayers in servicing the debt and meeting the public debt interest burden can limit a government's fiscal flexibility.

By most international standards, Australia's general government net debt is relatively reasonable. At around 25 per cent of GDP, it compares well with the OECD average of 45 per cent of GDP and 60 per cent in OECD Europe. However, it is not clear we should be judging ourselves against those poor benchmarks and, as noted earlier, there has been some tendency for Commonwealth net debt to ratchet up over time. The concern is to address that tendency, so as to ensure the fiscal stance is sustainable in the longer term and to reduce the vulnerability of the fiscal position to economic shocks.

I think the obvious and key point to draw from all of the foregoing is that as we are now more than five years into the economic upturn, it is important that there is now a move into budget surplus and a reduction in our stock of net debt.

That is why the key fiscal targets which have been set down in the recent budget — within the overall medium-term framework — have been to get back into balance by 1998-99 and to maintain surpluses thereafter, while economic growth remains solid.

The fiscal consolidation being implemented to achieve those targets is reflected in the projected outcomes for the underlying balance — with the projected surplus by the turn of the century reaching around 1½ per cent of GDP (see Chart 1) — and Commonwealth general government net debt falling from almost 20 per cent of GDP in 1995-96 to just over 10 per cent by the final outyear.

The underlying budget balance and net debt are two central benchmarks for fiscal policy at the Commonwealth level. Of course there are other measures of fiscal soundness or stance.

For example, the Commonwealth is developing an accruals framework for its budget, so that there will be a clearer understanding of its accumulated assets and liabilities, its operating balance, and the changes in its net assets. That will allow for a better appreciation of the full costs of policies — including those that may be deferred. The implementation of accrual budgeting will not, however, make the need for government to contribute adequately to national saving any less — there will be a continued need for government to focus on its own contribution to net lending.

Moreover, beyond the broad aggregates of budget balances and debt, considerable importance is clearly attached by government to other objectives. In particular, strong efforts are currently being made by the Commonwealth to reassess budget priorities and to enhance the quality of budget policies.

REASSESSING BUDGET PRIORITIES

The quality or the composition of the budget is important. Budget policies affect the economy and the community not just through the broad macroeconomic settings. Saying that does not reduce the importance of getting the overall fiscal settings right — as unless we create the conditions for stronger growth in activity and employment, we cannot improve the lot of ordinary Australians. However, particular taxes and outlays programmes and changes in them can obviously affect people and affect the way they behave. It is necessary to ensure that social goals of programmes can be achieved, while also promoting efficiency in the operation of the economy — for example, by providing adequate support for the unemployed while minimising work disincentives.

If programmes can achieve the right mix — and it is by no means the case that the goals of equity and efficiency need conflict — then that not only promotes better outcomes at the microeconomic level, but can also produce an economy that performs better and achieves better social outcomes overall. If programmes are delivered at least cost, and most efficiently and effectively, that can also contribute to getting the overall fiscal settings right. Therefore, what we need to strive for is policies — both the macro and micro aspects of the budget — that are mutually supportive. I'll give some specific examples a little later.

In addition to the overall fiscal imperative, there are a couple of factors which underline the need to improve the quality of the budget.

First, the Government has a commitment not to introduce new taxes or increase existing tax rates over the term of this Parliament, while ensuring that all taxpayers pay their fair share of tax. The aim — consistent with the principles of sound fiscal management in the Charter of Budget Honesty — is to avoid an undue tax burden on the community, while maintaining the integrity of the tax system.

One consequence of this objective is that there needs to be a focus on reducing budget outlays in order to implement the needed fiscal consolidation. This is reflected in Chart 3, which shows that revenues as a share of GDP are broadly stable through the forward estimates period (between 24 and 25 per cent of GDP), while underlying outlays are falling (reaching around 23 per cent of GDP by the end of the forward estimates period). The discretionary savings measures taken since 1996, equivalent to around 1½ per cent of GDP through the outyears (Chart 4), almost entirely reflect outlays savings.

This focus on outlays is a desirable one, I believe, as international experience suggests that fiscal consolidation efforts which have been based on outlays restraint have been more successful and durable than those based on additional revenue raising.

Chart 3: Underlying Budget Aggregates

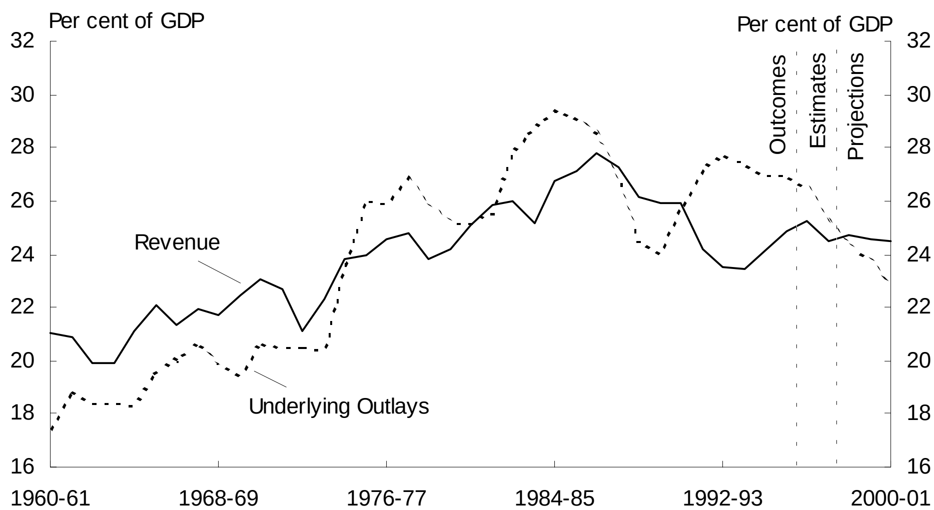
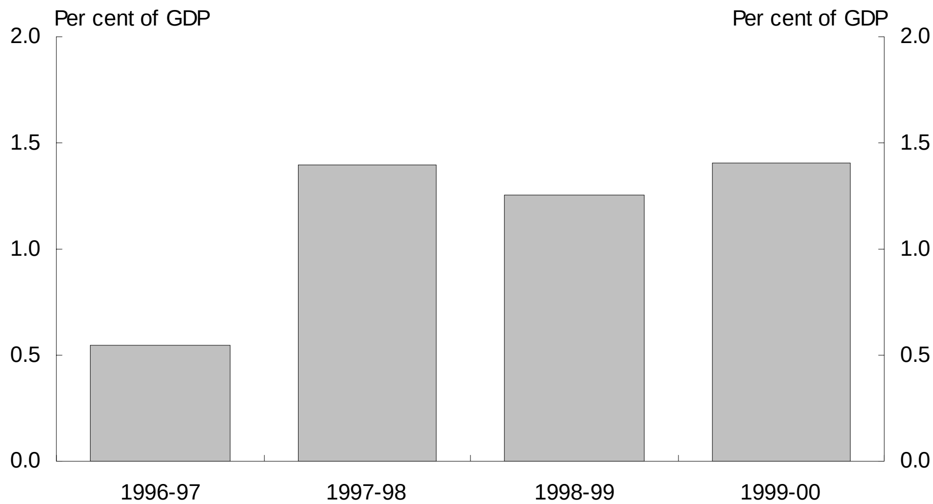


Chart 4: Cumulative Decisions



Second, the Government also made it clear in the recent budget that there were a number of high priority expenditure areas that it wished to enhance or protect. For example, at the commencement of the last budget process, there were clear public statements made to the effect that the social safety net was not at issue in the fiscal tightening being pursued. Given the clear desires and commitments to maintain or develop certain programmes, it is necessary to be better and smarter in achieving reductions in outlays.

There are a number of aspects to this, but it essentially means being concerned with the efficiency and effectiveness of programmes and their delivery. There are systems and reviews for Commonwealth agencies in place to ensure that this happens, encompassing three main elements.

First, there need to be continual reassessments of whether government should have a role in providing some services or whether they would be better discontinued; whether services should be delivered by another level of government; or whether there is not a case for greater user charging for services.

Government clearly has a role in providing services which the private sector cannot provide or under-provides. These are what economists call public goods — street lights are consumed by everyone, but it is difficult to charge for that consumption and they would not be provided unless financed by taxes. Over the years, however, governments have become involved in providing services that could be provided by the private sector — or partially so — or are more properly the responsibility of those that benefit. In the latter case, there may at least be strong justification for user charging.

One example of reassessments of the need for government involvement in services (albeit outside of the budget sector) has been the airline industry, where there has been the withdrawal of government involvement — through sales of government businesses to the private sector — across the world. The historical reasons for government involvement in this sector have long evaporated and such services are now very effectively delivered, and at lower costs to consumers, outside the government sector. Historical reasons for the public provision of other infrastructure services — essentially because of ‘natural’ monopolies in areas such as electricity generation and distribution and communications — are being eroded by the advance of technology and the development of systems that allow for market provision.

Activities that have been thought of as part of the traditional budget sector are also increasingly being examined as areas which need not be delivered by government. An important example is the various Department of Administrative Services’ businesses that have recently been sold to the private sector.

Boundaries between the public and private sectors are not necessarily neat, with activities best falling in one sector or another. For example, while there may be justification for the public provision of higher education services, there is equally an argument that those that primarily benefit — students who subsequently command higher incomes in the workforce — should make a personal contribution to the provision of those services. This is a central rationale for the Higher Education Contribution Scheme (HECS). HECS not only has the effect of ensuring that those undertaking higher education do so with clearer knowledge of both the benefits and the costs, but helps achieve more equitable outcomes. Taxpayers without higher education — and earning less than those who benefit from it — do not contribute to the full cost of providing higher education services. This is a case where the goals of equity, efficiency and fiscal discipline are quite consistent.

Second, there needs to be a focus on the outputs of government programmes, whether they are effective and achieve their objectives, and whether they conflict with other objectives. Historically, there has been considerable emphasis on the inputs to programmes, but not on output and whether programmes achieve their goals.

Assessing whether programmes are effective requires good evaluation. For some while, the Commonwealth has had programme evaluation requirements and no new policy can be agreed without a programme evaluation strategy. There are always difficulties in implementing effective evaluation strategies and some activities or outputs are more amenable to evaluation than others. However, evaluation and the demonstrated success — or otherwise — of programmes can be crucial in deciding whether they should be continued or amended.

The reforms to the delivery of labour market programmes are a case in point, where even early evaluations of some programmes indicated they were not running as planned, and not achieving their goals. The evaluations of the existing programmes were important in influencing the direction of reforms, so that the ineffective programmes — such as public sector make work schemes —

were discontinued and resources were focussed on more promising forms of assistance for unemployed people.

It should also be noted that this sort of evaluation is not only relevant for outlays programmes. For example, the tax system has also been used regularly as a mechanism to provide assistance to certain groups or activities within the community. The National Commission of Audit noted that such assistance has generally been subject to less regular monitoring and evaluation compared with similar assistance provided through government outlays. In response to the Commission's findings, the Government announced in the 1996-97 Budget a comprehensive review of tax expenditures with the aim of clearly understanding their cost, whether their objectives are still relevant, and whether they should continue or might be better delivered through an outlays programme — where the costs and benefits are more transparent both to taxpayers and to those that benefit from the concession.

Third, there needs to be a focus on efficiency in delivering programmes and on whether they are cost effective. In one sense, this is essentially a technical issue. However, there are a number of mechanisms emerging — particularly market based mechanisms — to ensure that programmes are delivered most efficiently, at lowest cost to the taxpayer. Following an Industry Commission review on competitive tendering and contracting, it has been decided that Commonwealth agencies will be required to systematically review their activities and to determine whether some of those mechanisms can be employed. These may not always turn out to be the most cost effective, but it is desirable to examine them before determining the approach adopted.

Again, the reforms to labour market programme delivery provide an example of some of those mechanisms.

A clear separation of purchasing and providing functions has been introduced in the provision of social security services and labour market assistance. This should provide for clearer specifications of the output required, accountability if it is not provided, and more cost efficient delivery.

In the case of labour market assistance, service delivery has been opened up to competition, with the aim of ensuring that service providers strive to deliver the best and most effective output, at least cost to taxpayers. Private providers will be able to tender for government contracts to provide services. Public provision will continue, but this will be done in a way that is consistent with the principles of competitive neutrality — ensuring that neither the public nor private sector deliverers have an unfair competitive advantage over others. Effective competition maximises the chances that taxpayers benefit to the fullest extent possible. Competitive contracting and outsourcing is also being pursued in the area of information technology services for government, with considerable budgetary outlays savings expected to be achieved.

IMPLICATIONS FOR POLICY DEVELOPMENT

In conclusion, what does all that imply for the development of programme policies? I think I can be fairly brief as the answers flow from my earlier comments; in some cases, the conclusions are perhaps rather obvious and / or are not novel, particularly to those who are close to the policy development process.

First, in an environment where there is greater focus on fiscal discipline and outlays restraint, programmes need continually to justify their existence — that is, to justify that there is a need for government involvement and that programmes are effective and well targeted in delivering their objectives. If they are not, there is little scope to continue with the ineffective in today's fiscal environment — programmes need to be adjusted and developed to ensure they are achieving their goals or they should be discontinued.

Second, new policies need to jump the same hurdles as those facing existing policies. There has to be a clear and demonstrated need for them. In addition, their adoption by governments is more likely to be successful if they are replacing programmes that are ineffective, so that the budgetary savings from discontinuing these ineffective programmes can create the scope for more effective, higher priority programmes.

Third, policies that can satisfy more than one goal have greater chances of remaining in place, or being implemented. While programmes need not necessarily satisfy multiple goals, if they have regard to both efficiency in the operation of the economy and maximising overall social welfare then they have a higher chance of being adopted or maintained. The budgetary costs of programmes also need to be consistent with the overall macroeconomic goals of fiscal policy — and the programme of fiscal consolidation that is currently underway. That will be all the more likely if some of the new mechanisms for delivering programmes are used, where they are appropriate.

Australian Government Foreign Debt Management

This paper was presented by Mr Andrew Johnson, Director, Portfolio Research Section, International and Investment Division, Treasury to the World Bank Sovereign Foreign Debt Management Forum in Washington on Wednesday, 15 October 1997. The presentation included a history of the Commonwealth's foreign debt management, a description of the Commonwealth's debt management framework and the role played by the Commonwealth's portfolio benchmark in guiding foreign currency debt management.

INTRODUCTION

In Australia, the Treasury Department has responsibility for managing Australian government liabilities in the form of securities and loans. This includes domestic debt instruments such as fixed rate bonds, floating rate notes, inflation indexed bonds and discount notes, as well as foreign currency debt in the form of loans and securities issued in offshore markets.

- It is worth noting that by foreign debt, I mean foreign currency debt raised in offshore markets. Purchases of domestic Australian dollar debt by non-residents, while classified as foreign debt, are not part of the foreign currency debt management strategy.
- I would also note that foreign currency assets, in the form of official reserve assets, are managed independently by the Reserve Bank of Australia.

A BRIEF HISTORY OF AUSTRALIAN FOREIGN CURRENCY DEBT MANAGEMENT

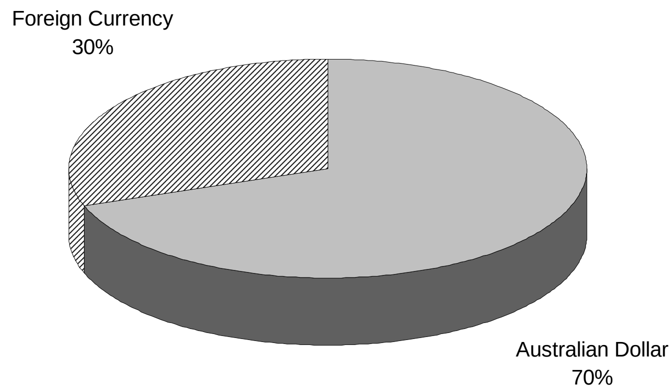
I will start with a brief history of Australia's involvement with foreign currency debt before proceeding to our current strategy.

During the 1950s, 60s, 70s and 80s, the Treasury raised foreign currency debt in a range of currencies and in a range of foreign markets. During this period, foreign currency debt was issued in Sterling (GBP), United States Dollars (USD), Swiss Francs (CHF), Canadian Dollars (CAD), Deutschmarks (DEM), Netherlands Guilders (NLG) and Japanese Yen (JPY). Loans were raised, and securities issued, in various markets including the Bulldog, Yankee and Samurai markets as well as the Euro markets.

During most of this period, Australia was running government budget deficits that required funding. Australia's debt management strategy during this time was largely focussed on what could be called funding risk. Funding risk is the risk associated with ensuring markets have an appetite for the sovereign's debt and that funding needs are achieved. As a result, Australia's debt management strategy was directed to raising funds across a range of markets, in a range of currencies, to spread or diversify funding risk.

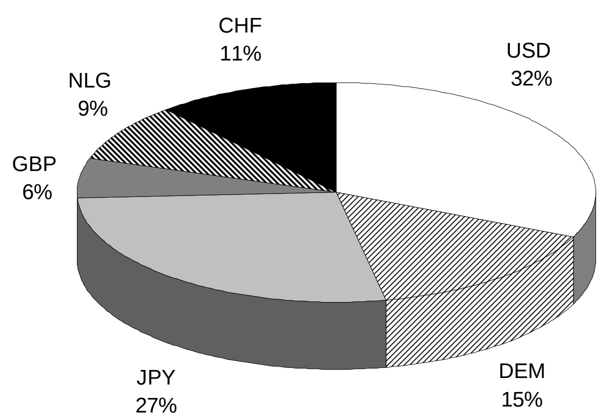
By 30 June 1987, foreign currency debt had grown to constitute around 30 per cent of all debt. The remaining 70 per cent was, of course, Australian dollar (AUD) denominated debt (see Chart 1 below).

Chart 1: Australian Government Debt — June 1987



The composition of this foreign currency debt was 32 per cent in USD, 27 per cent in JPY, 15 per cent in DEM, 11 per cent in CHF, 9 per cent in NLG and 6 per cent in GBP (see Chart 2 below).

Chart 2: Composition of Foreign Currency Debt — June 1987



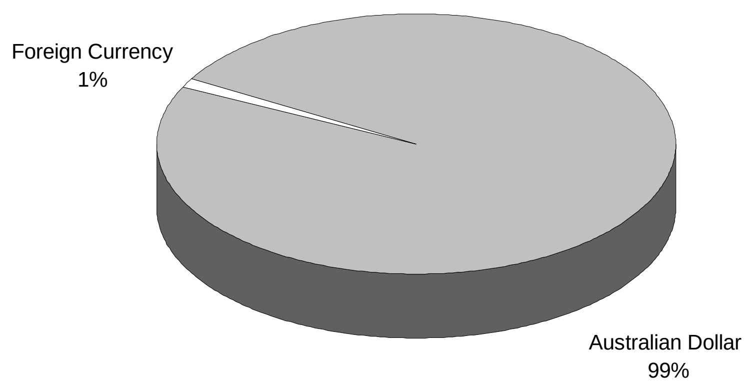
Australian dollar bilateral exchange rates for most of this period were largely fixed under the Bretton Woods system. After its demise, however, the exchange rate became more flexible, initially through a crawling peg exchange rate regime and finally with the floating of the Australian dollar in December 1983. This raised the importance of managing what could be called market risk, and in particular exchange rate risk associated with foreign currency debt. Market risk is the risk that once debt has been issued, movements in financial market prices may lead directly to increased debt service costs, or forgone opportunities to reduce debt service costs.

In the late 1980s and early 1990s, the Australian Government achieved a series of budget surpluses, which were directed to buying back foreign currency debt. In the context of having the capacity to restructure foreign currency debt significantly, and becoming increasingly aware of the importance of managing the market risk associated with the debt portfolio, Australia adopted a portfolio benchmark approach to managing the debt portfolio (including foreign currency debt).

Since the adoption of a portfolio benchmark approach in 1988, there have been some pronounced changes in the composition of foreign currency debt and foreign currency exposure in the Australian government debt portfolio.

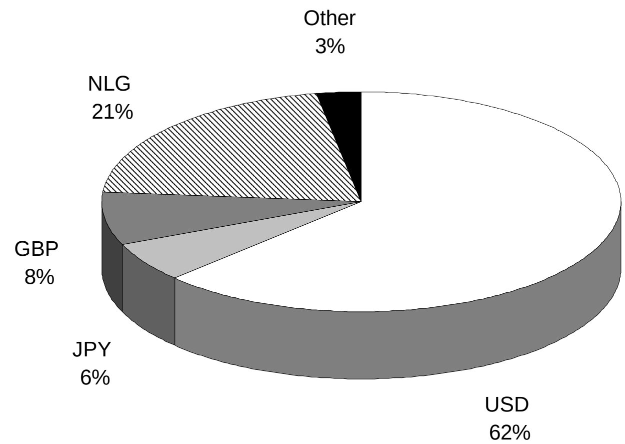
By 30 June 1997, foreign currency debt had been reduced to be only 1 per cent of all debt with the remaining 99 per cent being domestic currency debt (see Chart 3 below).

Chart 3: Australian Government Debt — June 1997



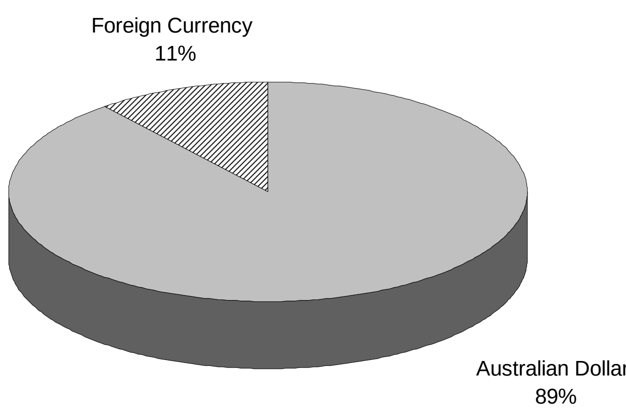
The composition of this minor foreign currency debt component was 62 per cent in USD, 21 per cent in NLG, 8 per cent in GBP, 6 per cent in JPY and 3 per cent in other currencies (see Chart 4 below).

Chart 4: Composition of Foreign Currency Debt — June 1997



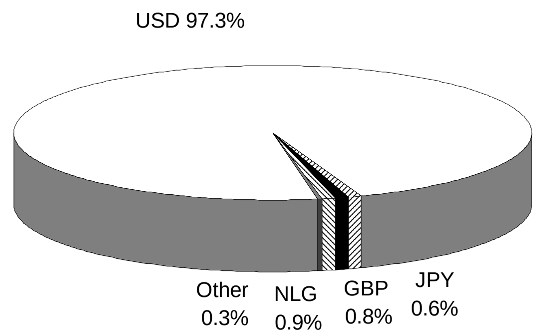
In contrast, by 30 June 1997, although foreign currency exposure in the portfolio had fallen, at 11 per cent it was significantly higher than the 1 per cent attributable to foreign currency debt (see Chart 5 below).

Chart 5: Australian Government Debt after Swaps Currency Exposure June 1997



This foreign currency exposure was primarily in USD (around 97 per cent) with the residual amount in other foreign currencies (see Chart 6 below).

Chart 6: Composition of After Swaps Foreign Currency Exposure June 1997



The difference between foreign currency debt and foreign currency exposure, reflected the use of currency swaps out of non-USD foreign currency debt and AUD debt into USD exposure.

- This difference is an important one: it highlights the difference between having to borrow foreign currency debt (say because of difficulties in raising domestic debt), and deliberately seeking foreign currency exposure (ie, creating foreign currency exposure through either currency swaps or direct foreign currency borrowing).

DEBT MANAGEMENT FRAMEWORK

Before proceeding to a description of Australia's portfolio benchmark approach, I will make some broad comments on Australia's debt management framework. While we have found this framework appropriate for Australia, we recognise that this may not be appropriate to the circumstances of other countries.

All Australian government debt, including foreign currency debt, is managed within a debt management framework that has the goal:

- to raise, manage and retire debt at the lowest possible long-term cost, consistent with an acceptable degree of risk exposure.

It is important to understand the role that foreign currency debt, or more accurately foreign currency exposure, plays in meeting this objective.

Australia is fortunate enough to have a deep, liquid and efficient domestic market for government debt. The Australian Government can fully meet its borrowing requirements through this domestic market. The Australian

Government does not need to issue foreign currency debt to meet any funding need, and indeed has not issued offshore since 1987.

- In fact, the budget balance has recently returned to a substantial headline surplus, and the Government now has a negative net funding requirement (ie, the Government is now reducing debt).

As a consequence, Australia's sole interest in foreign currency debt in recent years has been in the foreign currency exposure it creates. This interest arises primarily from managing market risk rather than managing funding risk. This foreign currency exposure can be obtained either through the direct issuance of foreign currency debt or the issuance of domestic debt coupled with a currency swap.

- This latter approach has been Australia's most cost-effective option for acquiring foreign currency exposure for most of the period since 1987.

For these reasons, Australia is probably better described as managing foreign currency exposure rather than managing foreign currency debt *per se*. A small, long-term, strategic foreign currency exposure has been retained for its impact on the cost and risk of the debt portfolio as a whole — in other words, for its role in managing market risk.

SELECTING A STRATEGIC BENCHMARK

The decision to maintain a small foreign currency exposure in the debt portfolio, well after the majority of foreign currency debt had either matured or been repurchased, was based upon our work on assessing an appropriate structure for the debt portfolio — ie, a portfolio benchmark.

The nature of a portfolio benchmark is coloured by the role it plays in debt management. There are two broad possibilities. The first role is as a target consistent with specified debt management objectives, towards which debt managers attempt to move the debt portfolio. The other is as a yardstick against which the relative performance of the debt portfolio and debt managers can be assessed.

In Australia's case, the benchmark's role is as a target portfolio structure, towards which the debt portfolio is moved, and then held. Used in this role, it becomes critical that the benchmark is consistent with the debt management objectives.

Our benchmark analysis essentially determines what portfolio structure will best meet the debt management objective mentioned earlier:

- to manage debt at the lowest possible long-term cost, consistent with an acceptable degree of risk exposure.

Before one can run this analysis, one needs to define expressions such as cost and risk precisely. For example, cost could refer to the economic or market cost of debt. It could also refer to an accounting or cash outlay debt service cost measure. Risk generally refers to the volatility of cost, but again, the volatility of which cost measure and how is that volatility calculated? The precise definition of cost and risk is important, as it has a strong influence on the nature of the trade-off between that cost and risk and therefore the benchmark adopted.

In constructing our benchmark, it was decided that the long-term economic or market cost of debt was the most appropriate cost concept for Australia's debt management. The advantage of this measure is that the long-term consequences of particular debt management decisions are brought to account immediately. Also, both the realised and opportunity costs of debt management decisions are fully recognised. The risk measure adopted was that of the volatility of accrued debt service costs. This approach makes allowance for the importance of debt service costs in the budget process, where debt management decisions that lead to highly volatile debt servicing costs are undesirable from a medium-term fiscal framework perspective.

Once cost and risk have been defined, an appropriate benchmark for the debt portfolio was determined by simulating future portfolio cost and risk. This involved a series of steps.

- First, it involved modelling the fiscal, economic and structural factors that influence debt management decisions, as well the volatile, uncertain nature of financial markets;
  - this involved modelling the level, volatility and correlation between the different interest rates and exchange rates that affect portfolio cost and risk; and
  - importantly, the analysis did not examine foreign currency exposure in isolation, but fully allowed for its interaction with other components of the debt portfolio.
- Second, the expected cost and risk consequences of a range of possible portfolio structures were analysed. Portfolio structure here is defined in terms of currency and interest rate exposure.
- Third, those portfolio structures which were efficient, in the sense that they have the lowest expected cost for a given level of risk were identified.
- Fourth, one (or a range) of these efficient portfolio structures, that was consistent with an acceptable degree of risk for the sovereign was selected as the portfolio benchmark.
- Finally, extensive testing was performed of the robustness of the selected benchmark to variations in important assumptions underpinning the analysis.

Our benchmark analysis indicates that a small, strategic USD exposure in the debt portfolio has long-term benefit. In the case of Australia, this benefit only comes with USD exposure and no other foreign currency exposure. In particular, it helps to lower the expected long-term cost of the portfolio, without leading to an unacceptable degree of risk. At first glance it may seem counter intuitive that taking on some exchange rate risk through foreign currency exposure does not lead to unacceptable risk levels. The answer lies in the Australian dollar lying within the dollar bloc, and USD exposure offering some currency diversification benefits.

- Our benchmark is a portfolio with 10 to 15 per cent USD exposure, with the remainder being domestic currency exposure. There are also specific targets set for duration in both the domestic currency and USD sectors of the debt portfolio.

Undertaking this benchmark analysis requires some specialist skills and places a number of demands on sovereign debt managers; namely for:

- expertise in portfolio management and, in particular, in financial modelling and portfolio optimisation analysis;
  - in Australia’s case, this involved contracting out for the consultancy services of professionals in this field;
- investment in information technology, in the form of computer database systems to accurately capture the sovereign’s liabilities;
- ready access to on-line information on market prices and yields for various financial markets; and
- sophisticated computer software for portfolio analysis and risk management.

INFLUENCE OF THE BENCHMARK ON DEBT MANAGEMENT OPERATIONS

It is worth outlining how the portfolio benchmark influences debt management decisions and to touch on performance monitoring and assessment issues. As mentioned earlier, the benchmark acts as a target towards which Australia moves its debt portfolio over time. As such, it influences:

- decisions on the composition of the annual government borrowing programme amongst differing debt instruments, formulated as part of the budget process; and
- determines the nature of the currency swap and domestic interest rate swap programmes through the course of the year.

Over the year, there are a variety of factors that affect the structure, duration and currency share of the debt portfolio. These include movement in market interest rates and exchange rates, time decay, and the form, maturity and timing of new debt issuance and swap transactions. The Treasury regularly monitors the debt portfolio's market value and characteristics such as currency share and duration through the course of the year.

Having a benchmark that is a target for debt management policy also influences performance assessment. In particular, Australia does not attempt to out-perform the benchmark through taking currency views. The benchmark represents a foreign currency exposure strategy that is expected to result in the lowest cost over the long term for a tolerable degree of risk. Performance monitoring and assessment is therefore linked to how well the debt portfolio is maintained at the benchmark through time.

BROAD LESSONS FROM AUSTRALIA'S EXPERIENCE WITH FOREIGN DEBT MANAGEMENT

There are perhaps four broad observations that can be drawn from Australia's experience with foreign currency debt management.

- First, having good public sector debt circumstances, that flow from sound fiscal policies over the long term, increases the flexibility to pursue debt management as an objective:
  - in particular, portfolio management objectives can be constrained if the sovereign borrower has to borrow outside its own domestic markets.
- Second, much of our approach is based on the fact that Australia has deep, liquid and efficient capital markets for government debt. This enables Australia to approach foreign debt management without funding risk being a constraint.

- Third, the existence of deep, liquid and efficient derivatives markets, particularly for swaps, has enabled Australia to effectively separate the funding risk and market risk associated with foreign currency debt:
  - indeed, without these derivative markets, Australia would have considerably less flexibility to meet any formulated benchmark; and perhaps
  - there is little point in having a benchmark target without the necessary transactional flexibility to meet its requirements.
- Fourth, adopting a benchmark provides a useful framework to analyse the market risk associated with foreign currency debt, and ensure that this risk is consistent with meeting the management objectives for the debt portfolio as a whole.

The Reform of Occupational Regulation in Australia

This paper was prepared by Messrs David Parker, Blair Comley and Vishal Beri, Structural Policy Division, Treasury and presented by Mr David Parker, Assistant Secretary, Competition Policy Branch, to an Asia-Pacific Economic Cooperation (APEC) Workshop on Competition Policy and Deregulation held in Quebec, Canada in May 1997. It considers the role and design of occupational regulation based upon a set of 'best practice' principles. Regulation is an important part of the legal and institutional fabric of a country. However, governments have become increasingly concerned that inappropriate regulation may lead to adverse growth, efficiency and distributional outcomes. This paper considers possible rationales for occupational regulation and addresses the general question: 'what are the precise objectives of regulation, and how can we design regulations to best achieve these objectives, without producing unintended consequences?'. The paper considers some Australian initiatives in regulatory reform being progressed as part of the National Competition Policy reforms. Finally, the paper concludes with a set of principles to guide the design of quality regulations.

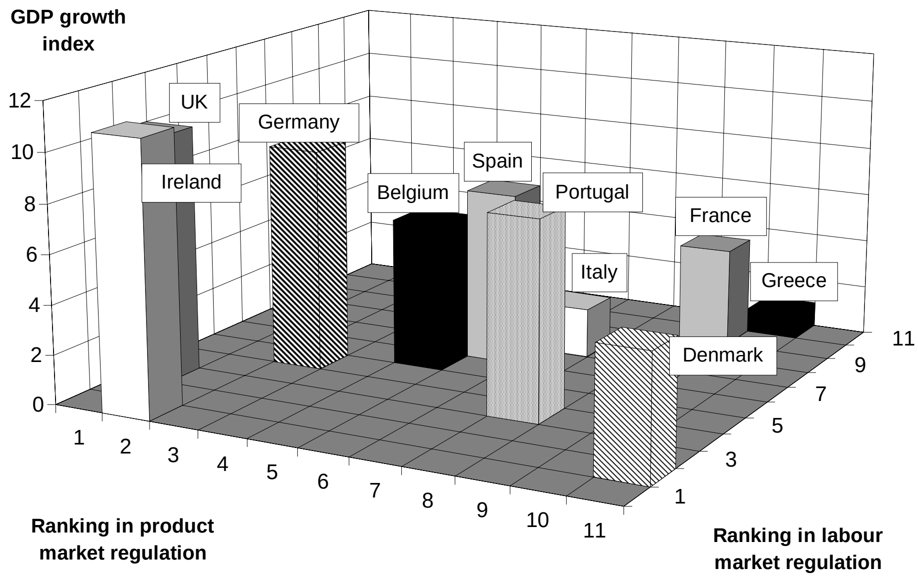
INTRODUCTION

The development of an economy and the regulatory framework in which it operates are interrelated and complementary. Regulation can substantially influence the structure of particular industries and either foster or retard economic development of particular sectors or of the economy generally. Good quality regulation can promote economic growth while not ignoring important social goals.

In recent times there has been an increased awareness of the pitfalls of regulatory capture and a recognition that some legal and institutional arrangements have not evolved to accommodate a changing environment. This has taken place in the context of a growing consensus about the appropriate role of regulation and the adverse effect of poor regulation on economic performance and distributional outcomes. As a result, governments in a number of countries have undertaken reform processes to ensure that regulations are promoting current government priorities and serving to facilitate a competitive and dynamic economic environment.

The view that poor regulation can adversely affect economic performance is not controversial. Nevertheless, it is quite a difficult exercise to make robust quantitative assessments of these adverse consequences, particularly in terms of dynamic costs if the ability of an economy to adapt flexibly to change is impaired. Making such estimates is not the purpose of this paper. It is sufficient to note for our purposes that the effect may be quite significant. An interesting paper by Koedijk and Kremens (1996) analysed the relationship between the degree of regulation (measured by qualitative ranking of product and labour market regulation) and growth rates in eleven European countries over the period 1981 to 1993. The conclusion of their paper (summarised in the following chart derived from their data) is that the more lightly regulated economies tended to experience higher growth rates.

Chart 1: Labour and Product Market Regulation versus GDP Growth, OECD, 1981-1993[(a)]



(a) Low ranking indicates low degree of regulation.
Source: Koedijk and Kremens 1996.

Occupational regulation, which is the focus of this paper, is only part of the overall picture in regulation. However, it is an important part, particularly as many professional services are intermediate inputs to other productive processes. The Industry Commission (IC) (1995) calculated estimates of the benefits of competition policy reforms across a number of sectors. The IC estimated that regulatory reform in a number of professions in Australia (dentists, legal profession, medical profession, optometrists, and pharmacists) would increase the level of Gross Domestic Product (GDP) by around one-third of one per cent. (These professions are, of course, not the entire extent of occupational regulation.)

Regulation is not the only thing that influences industry structure. Obviously, the underlying economics of an industry are very important. So too are other elements of the social fabric, which include cultural values and practices. These influences are quite diverse in the different countries in APEC. Regulations must function within the society in which they apply. What suits one country may not always suit or work in another. These differences need to be borne in mind when thinking about regulatory issues, including in the context of any efforts directed at convergence or mutual recognition.

As economies grow and become more complex there is often pressure for regulatory reform. Similarly, pressures for reform can arise as the intensity of trade with other economies grows. In lightly regulated economies, the traditional roles of culture and practice which govern economic relationships among groups can be put under strain as patterns of economic transactions increasingly shift and widen. In highly regulated economies, regulation can prove to be a barrier to the innovation which is necessary as markets increasingly integrate. Hence, we may see pressures for more regulation in some areas of some economies and pressures for less regulation in other areas of other economies.

Notwithstanding the diversities of different countries, there are some principles of good regulatory practice that are widely applicable and can assist the mutual economic progress to which APEC is directed. This paper is intended to analyse those principles in the context of occupational regulation.

One of the issues that needs to be addressed in reform of occupational regulation (irrespective of whether the direction of reform is for more or less regulation) is the appropriate level of regulation. Formal legal structures which codify, create and limit rights can be general to an economy or they can be specific to particular trade sectors. Occupational regulation is usually sector specific and typically has evolved as a way of codifying previous practices and custom where the pace of change or scope of transactions demands it. The appropriateness of general or specific regulation will depend upon the objective of the regulation and whether the ‘problem’ that is addressed is isolated or systemic.

The regulation applying to an occupation can be a quite complex issue because regulation of any occupation usually involves many layers and different institutional structures. Specifically, there is the general law, industry specific law and general custom and practice. There may be general or industry specific regulators and professional bodies may also undertake self-regulatory functions. There is also the issue of the interrelationship between these different layers and institutions.

The general trend in addressing these issues has been to find new ways to regulate occupations that avoid unjustified restrictions on competition and encourage best practice and innovation. The challenge is to do so in ways that promote important social goals.

THE RATIONALE FOR OCCUPATIONAL REGULATION

This section discusses some rationales for regulation and some desirable properties of regulation.

Law, custom and practice all set the environment in which market transactions take place. Regulation of market activity is necessary where additional sets of rights, or qualifications of rights, are required to assist the market to operate in a manner that is efficient and equitable for participants.

Promoting competition is often useful to encourage both an efficient and equitable operation of a particular market. Competition in the market provides a discipline that balances the interests of sellers and buyers. In so far as equity is concerned, this can be particularly important if one group may otherwise have the ability to capture all the benefits of economic activity through limiting competition. However, unfettered market activity, and unfettered competition, does not always promote the most desirable outcomes.

The regulation of occupations generally arises out of a recognition that there may be a set of circumstances where competition and unconstrained transactions do not produce optimal outcomes. Such constraints include barriers to entry (such as qualification requirements) or regulation of transactions themselves (such as price or other content controls). Three potentially legitimate rationales are often given for regulating individual market transactions in occupational services. These are: information limitations; non-voluntary transactions; and distributional concerns.

Information Limitations

A person who is purchasing goods or services needs to make an assessment of the quality of the goods or services. The consequences of making incorrect judgements (ie, the risk) for a relatively simple good with few characteristics is likely to be small as consumers are likely to be able to form a reasonably accurate estimate of the value of the good. The ability of consumers to form accurate judgements is highest when consumers can assess the quality of the goods after consumption and they undertake repeat purchases.

However, professional services are significantly more difficult for consumers to assess. Five key characteristics of professional services will tend to magnify the information asymmetry and its consequences. First, services are generally not observable before they are purchased as the consumer cannot inspect a service before purchase in the same direct way as can be done with most goods. Second, professional services are by their nature complex and often require considerable skill to deliver and tailor to the consumer's needs. Therefore, it can be difficult for the consumer to assess the quality of the service before it is purchased. Third, the quality of many professional services can be difficult to assess even *after* the service has been purchased. For example, if a person hires a lawyer to undertake litigation, which is ultimately unsuccessful, it can be difficult for the consumer to know whether the legal services were poorly delivered or the case was inherently difficult to win. Fourth, many consumers are very infrequent consumers of professional services. Therefore, they do not have repeat purchases to assess quality. Fifth, the consequences of purchasing poor professional services can be significant. For example, the service may represent a large expenditure for the consumer and a defective service (eg a heart bypass operation) can cause serious and irreversible harm.

These characteristics can be used to justify regulation aimed at quality assurance. Such schemes are intended to provide a guaranteed level of service quality to consumers and therefore reduce risks associated with purchasing professional services. To some extent these schemes substitute search and information gathering by individuals with information gathering and assessment through some regulatory mechanism. These arrangements can reduce the transactions cost for consumers and help the market to function efficiently.

The focus here is on consumer protection, but that does not imply that all professional services should be regulated in the same way. Different services have different complexities and risks. And, in some markets, consumers may be able to form reasonably good assessments of quality and risk through word of mouth reputation or ‘branding’.

Non-Voluntary Transactions

Non-voluntary exchange may not be mutually beneficial. Concern about coercion can be used to justify laws that invalidate contracts that are entered into under duress. Generally societies have laws, customs and practices that limit the ability of individuals to coerce others. In markets for professional services there may be a case for special protection because of greater opportunity for subtle coercion. For example, professionals may have significant opportunities to misrepresent the costs and benefits of taking a particular course of action. There may also be cases where relationships of trust between the professional and the client can be abused.

Distributional Considerations

Distributional considerations are often used to justify regulations which set the terms on which services are provided. These can include price caps which are intended to provide services at lower cost to low income earners.

There is a debate about whether such occupational regulation is appropriate. The key question in that context is whether distributional concerns should be addressed through direct regulation of occupations or whether there may be a better, more direct redistribution mechanism. That may depend on the stage of development of the economy, but generally it is worth noting the following points. First, attempting to redistribute through such regulatory mechanisms is often not transparent. That is, it can be difficult to know whether those who the government intends to assist are actually assisted by the policy. Second, a regulatory approach to redistribution may not be well targeted. The nature of such indirect regulations is such that they cannot differentiate between income groups. Therefore, high income groups will also benefit from the regulations (funded from a cross-subsidy from other consumers). If so, the total redistributive benefit is less than the total cost imposed on other consumers. Third, a more efficient method may be to target the distributive issue directly through the tax/transfer system. Whilst this may well be the best theoretical solution, if the redistribution would otherwise not take place, the redistributional objectives of the government may have to be pursued through some, albeit imperfect, regulatory mechanism.

In summary, economists are generally sceptical about the desirability of using occupational regulation tools to achieve distributional objectives. Such regulations can lead to non-transparent outcomes, can benefit some recipients in unintended ways, and be less efficient than redistributing through the tax/transfer system.

Inappropriate Justifications

Regulations that have the intent of merely increasing returns to groups that are regulated are not generally considered appropriate given the arguments about distributional considerations noted above. Moreover, the redistribution to regulated groups is also likely to involve negative distributional consequences for relatively poor consumers.

It is not unusual that occupational regulation does indeed have that effect. For example, restrictions on entry to a profession can be expected to limit supply of the services of that profession and raise the price of the service and the incomes of those providing the service. The restriction on entry may be justified on the basis of consumer protection and, in one sense, the resulting increase in price represents the cost to the consumer of that protection, that is the consumer pays. This suggests strongly that where restrictions on entry to an occupation are justified on consumer protection grounds, we should be confident that the restrictions are no tighter than necessary to achieve the safety objective and that there is not some better more direct mechanism to achieve the objective. Otherwise, the consumer will be forced to overpay for the protection and the unintended effect of the regulation will be to redistribute wealth from consumers to the regulated profession. Therefore, an important objective of regulatory reform of occupations should be to ensure that regulations which have the effect of increasing the returns to occupations have some legitimate justification.

Sorting appropriate from inappropriate justifications for regulations requires policy analysts to ask the question of what is the perceived problem that is to be addressed and why is it necessary to address it by regulation as opposed to a non-regulatory option. In particular, it is important that the objective of a regulation is thoroughly assessed and that the various ways to achieve that objective and the actual outcome of a regulation are analysed. Assessing all regulations from an economy-wide perspective, as opposed to the perspective of only those being regulated, is very important if these problems are to be avoided.

Using that framework, we can define good quality regulation as regulation which achieves appropriate objectives in the most efficient way. Poor quality regulation can either have inappropriate objectives or achieve appropriate objectives in an inefficient way or with unintended consequences. Compliance costs are also important in this context. Experience in a number of countries has shown that substantial compliance costs can give rise to an increased incidence of non-compliance.

The following sections of the paper examine the various ways that regulation can achieve its objectives and illustrate the types of regulation which are likely to be most efficient.

FORMS OF OCCUPATIONAL REGULATION

The introduction foreshadowed the complex issues of the level at which regulation should be imposed and the structure of regulatory institutions. Before addressing those issues, this part of the paper briefly sets out the various types of sector specific occupational regulations that are commonly imposed by governments. Many occupations have some form of specific regulation in Australia. For the most part this is a responsibility of State Governments, given that the Commonwealth Government generally does not have specific constitutional power to regulate occupations.

Occupational regulations can deal with entry barriers, transactions, and redress mechanisms and can vary in the degree of restrictiveness.

Entry Barriers

Many occupations have barriers to entry. These barriers can take a variety of forms.

Registration requires practitioners to register to be able to provide a particular service. Requirements for registration can include appropriate educational qualifications and/or membership of professional bodies. In addition, candidates for registration may need to pass probity tests or satisfy the criteria to be a ‘fit and proper’ person. Registration schemes can be run by government agencies or by self-regulating industry bodies. In Australia registration schemes apply to regulate entry into a range of occupations such as law, accounting and health services.

Licensing is similar to registration in the sense that the grant of a licence to practise an occupation is often dependent on formal qualifications, approved training periods, or general probity tests. However, licensing can restrict entry into an occupation and place restrictions on the range of activities that an individual can carry out. Licences can be issued by government agencies or by industry licensing boards. In Australia licences to practise have been traditionally associated with many occupations, including construction and manufacturing, engineering trades and agricultural industries as well as lawyers, accountants and other service professionals. For most occupations the licence to practise has been valid only within the jurisdiction in which the licence was granted. An additional licence has been required to practise in another State or Territory.

Negative licensing is an approach where individuals are generally entitled to practise but can be prohibited from practising if they have committed some form of offence deemed serious enough to warrant exclusion from the industry. Negative licensing imposes lower barriers to entry than licensing.

Whilst not strictly restricting market entry, other forms of occupational regulation such as certification and information regulations are also aimed at ensuring that acceptable standards of conduct in practice are maintained.

Certification or accreditation is usually administered by a certification body responsible for keeping a 'list' of those practitioners who have reached a certain level of competency or meet other standards. These schemes are usually non-legislative and fostered by industry bodies. However, whereas certification indicates the achievement of a certain level of expertise or competency, a non-certified practitioner may also be able to provide similar services. For example, certified practising accountants (CPA) are distinguished from those accountants who have not completed the additional study required to become a CPA.

Accreditation operates in a similar way. For example, under an Agricultural and Veterinary Chemicals Accreditation Scheme administered in some jurisdictions, manufacturers, distributors and retailers who are not accredited with necessary training in the appropriate handling and storage of chemicals can be prevented from trading in chemicals.

Transaction Content Regulation

Information regulations are designed to directly address information asymmetries. They may require government warnings, or may require a practitioner to provide specific guidance to a potential consumer. They are generally considered to be the least intrusive form of regulation.

Transaction regulations may also deal with price and other forms of regulation. In this context occupational regulation is part of the broader mosaic of regulation. For example, building codes and legal procedures provide a range of regulations to ensure quality standards.

Performance Based Regulation

It is commonly stated that performance based regulation focussed on outputs is generally to be preferred to prescriptive regulations which control inputs. This is because input controls tend to be more restrictive of innovation and competition. For example, in environmental regulation, it is usually better to specify permissible levels of emissions (a performance target) rather than specify a particular technology (ie, an input) that must be used in the production process. The performance based regulation allows and rewards firms to adopt the most cost-effective means, or invent a better means, to achieve the emissions target. The means found by the firm may or may not be the technology that would have been chosen at a particular point in time by the regulator.

In occupational regulation, entry barriers are more in the nature of input controls than performance based criteria. To the extent that this is justified, it should be because performance based criteria would not provide adequate protection to consumers due to a significant risk that unqualified persons would not be able to systematically provide services that would reach reasonable performance criteria and that the risk associated with a substandard service was very high.

SECTOR SPECIFIC AND GENERAL REGULATION

The justification for specific occupational regulation through Commonwealth, State and Territory legislation is that there may be individual issues that need a tailored solution, or the consequences of inappropriate behaviour are so serious that there needs to be more stringent safeguards than would normally be required. However, the various approaches to regulation are not necessarily mutually exclusive. Rather, the approach adopted is usually a combination of the approaches described above and reliance on general law. Also, some State and Territory legislation provides for some professional associations (generally unincorporated) to set standards for entry into the occupation, to make rules for the conduct of practitioners and set other consumer safeguards. Safeguards usually extend to redress mechanisms should inappropriate behaviour be detected. Aggrieved consumers can then access accelerated dispute settlement procedures in addition to access to general legal processes.

The above discussion illustrates that the overall regulatory structure applying to an occupation is often complex. This complexity can itself pose a challenge for the reform task because analysis of and agreement about the appropriate objectives of the regulation, or the best means to achieve the objectives, may not be straightforward. It has been our experience in some regulatory reform exercises that there has not been agreement among the staff of the relevant regulator as to their objectives.

The decision of whether there should be regulation will depend on the nature of the transaction which is to be regulated (ie, the seriousness of the consequences that would flow from inappropriate behaviour) and the likely effectiveness of different mechanisms. It does not necessarily follow that more serious consequences always imply that a regulatory solution should be adopted. In many cases government action will not be the most effective solution as the government may suffer from a lack of information and capacity to enforce regulations. Dispersed information held by groups and individuals that are closer to the industry may be more reliable and a better basis for action. In these situations it may be more appropriate for standards of practice, for example, to be developed and regulated by the profession rather than prescribed by government. Or, the cultural context and general mores of social behaviour may impose significant sanctions for inappropriate behaviour through loss of face and reputation within the community.

Alternatively, the general legal and institutional structures which apply across the economy may be sufficient to appropriately control behaviour. In an Australian context this includes the Commonwealth's *Trade Practices Act 1974*, individual State and Territory fair trading legislation and common law principles of contract and tort and equity. (An important issue in occupational regulation is the extent to which specific regulation should displace the general law. This is discussed further in the following section.)

The general policy principle, that minimum feasible regulation be targeted directly at the identified objective, offers some guidance on the issue of whether general or sector specific regulation should be adopted to address particular issues. Put simply, if an issue is of general concern, such as the potential for 'misleading conduct', that would be best addressed through legislation that is generally applicable. Addressing the general issue of misleading conduct on a sector by sector basis can invite problems if all sectors are not covered. On the other hand, if there is an issue that is specific to a sector, such as the need for lawyers to observe a higher than normal standard care, then that should be addressed in some form of sector specific regulation. There is a considerable risk that departures from minimum feasible regulation will give rise to unintended consequences.

REGULATORY FAILURE

In practice regulation does not always achieve its objective and there can be undesirable side effects. This section addresses how we should evaluate regulation and desirable properties that should be considered when setting regulations.

Three key questions arise when considering the actual regulations that are in place. First, are the regulations poorly targeted to address the identified problems? Second, do they have unintended consequences? Third, are other policy instruments better equipped to address the same problems? If the answer to any of these questions is 'yes', then it is said that there is 'regulatory failure'. In the broad, the rationale for regulation is to address some form of market failure. Nevertheless, policy makers need to be acutely aware of the possibility of regulatory failure. There is a risk that in addressing a market failure, regulators can substitute a regulatory failure which may have worse consequences than the initial market failure. Ensuring that the process of regulation setting and review follows sound principles reduces the likelihood of regulatory failure. Regulations should address a clearly stated objective, be analysed from an economy-wide perspective, be the minimum feasible regulation, and be periodically reviewed by appropriate bodies.

Even if regulations were appropriately targeted when established, it is possible that the context and application evolve over time such that the regulation no longer addresses the objectives effectively. Two issues that need to be considered are 'regulatory capture' and 'regulatory drift'. Regulatory capture occurs when a regulator takes decisions which are biased in favour of the industry that is being regulated. There is a particular risk that this can occur when professional bodies or associations representing an occupation have an operational responsibility to set standards of entry, in addition to carrying out registration, licensing or even certification functions. Professional bodies may be keen to maintain the incomes of existing practitioners and can do so by restricting the supply of practitioners through high entry standards.

For example, the 1994 Baume Report, commissioned by the Commonwealth Government found that the Royal Australasian College of Surgeons and other associations of specialist surgeons exercised an exceedingly high level of control over the supply of qualified general surgeons as well as the number of surgeons in various specialities. It has been suggested that the control of supply by these medical bodies is reflected in the fees and charges surgeons are able to command. A range of other studies have made similar links between the control of supply and high costs in relation to legal and accounting services.

While entry standards may be necessary to ensure consumer protection, capture of the processes of occupational regulation may lift standards above the level which is really necessary. This may create skilled, high cost services to an extent that lower quality, lower priced services are eliminated from the market. If so, consumers who cannot afford high cost services, but may be adequately served by a less qualified practitioner, tend to be marginalised or even excluded from the market. Where this occurs, governments may feel obliged to intervene further in the market to subsidise particular consumers to allow them access to the services. In effect, this is an additional layer of regulation with the objective of counteracting the effect of the regulatory failure. However, a more direct means to address the issue is to address the prime cause of the regulatory failure.

Two factors can ameliorate the potential problems of professional regulation outlined above. First, self-regulatory actions of professional bodies should be subject to competition law or to some other means of control if a competition law is not applicable. Second, consideration should be given to ensuring that the professional governing bodies are not dominated by those that are being regulated. For example, restrictions may be placed on the number of board members who have a pecuniary interest in the regulated industry. Of course, in setting such restrictions due account should be given to the need to have members with specialist expertise.

Another concern is that even if regulations could be said to be appropriate when adopted, they can cease to be appropriate over the passage of time. Such 'regulatory drift' can result from structural change in the economy due to changing technology or consumer preferences. The required level of consumer protection may rise (if services become more complex) or fall (if consumers become more sophisticated). This suggests that it is desirable from time to time to review regulations to ensure that they remain fit for purpose.

REFORM OF OCCUPATIONAL REGULATION

The previous parts of this paper have developed a number of reform principles. In this part, those themes are further developed and illustrated with a number of examples from recent experiences in Australia.

Broadly, there are two distinct elements to regulatory reform — a substantive element and a procedural element.

The reform of substantive regulation applying to a sector is often called 'deregulation'. But that term can be misleading, as reforms of this type are really aimed at better quality regulation. In some circumstances, that can actually imply more regulation. Moreover, such substantive reform can often involve an easing of the prescriptiveness imposed by regulations, rather than a strict reduction in their volume. In general, such reform should aim at maintaining necessary consumer protection mechanisms while increasing flexibility for providers of goods and services. As a first step, this usually involves an assessment of the costs and benefits associated with regulation. Where necessary, it involves the pursuit of more cost-effective forms of regulation. Thus, prescriptive type regulation could be replaced by performance based regulation, where the quality of services provided by an occupation is regulated by standards and performance measures. Governments, industry bodies and consumer groups could participate in the development of standards and performance indicators so that the priorities of each were being met by regulation. This kind of regulatory practice enables all participants in the market to take advantage of changing circumstances and adjust their priorities accordingly, without undermining the purposes of regulation.

Governments can reform their own internal processes for making regulation, with the objective that improved processes will help to ensure that new regulation is of better quality. This could involve a range of management techniques applicable in any particular situation. In Australia this process has involved a number of measures such as; provisions in specific legislation for the periodic review of that particular Act and associated regulations; providing for the review of legislation in general to determine anti-competitive effects and avenues of reform; requiring proposals for new regulations or amendments to existing rules to be accompanied by regulatory impact statements; and sunsetting arrangements. Collectively, these are called 'regulatory quality' mechanisms. Regulatory quality mechanisms can help to avoid and wind back the all too evident problems of the 'regulatory inflation' that many countries have experienced over recent decades.

In Australia, Commonwealth, State and Territory Governments have been applying these measures for some time with respect to occupational and other services that fall within the scope of their respective jurisdictions. However, towards the beginning of the 1990s, Australian Governments increasingly recognised that the reform process may benefit from the development of a national framework that establishes guiding principles to encourage comprehensiveness and greater consistency of reform across jurisdictions. The most obvious benefit of consistent reform practices identified by governments is the facilitation of national markets for goods and services to assist with Australia's international competitiveness.

To facilitate consistency in general structural reform, including changes to occupational regulation, and encourage national markets for goods and services, Australian Governments have developed and are involved in implementing two primary reform models. These are: the National Competition Policy Framework; and procedures for mutual recognition of occupational qualifications between Australian jurisdictions and between Australia and New Zealand.

National Competition Policy

On 11 April 1995, Heads of Government signed three intergovernmental agreements which set out the guiding principles and processes for National Competition Policy (NCP). This includes reforms to the competition law, a range of infrastructure reforms, reforms relating to government commercial activities and a range of general regulatory reforms. In regard to occupational regulation, the primary relevant components of NCP are twofold.

Extension of the Trade Practices Act

All Australian Governments agreed that the competitive conduct rules in the Trade Practices Act would be made to apply to all government business activities and to individuals and unincorporated associations. This is a substantial extension of the application of the competition law which previously had only applied within the limits of the constitutional power of the Commonwealth Government. In broad terms this meant that the law generally applied only to corporations and to some government business activities. The extension of the law was achieved by means of a cooperative legislative scheme whereby all Governments apply the competition law to the full extent of their constitutional competence. Enforcement responsibility is referred by all Governments to a single national competition regulator, the Australian Competition and Consumer Commission (ACCC). This scheme came into effect from 21 July 1996. As a result, the professions and occupations, many of which are not usually incorporated, are now generally subject to the competition law.

The Trade Practices Act specifies the competitive conduct rules for behaviour in the Australian market place and is a key element in the regulation of the general economy. Among other things, the Act specifies that the following behaviour is prohibited:

- agreements, arrangements and understandings which have the purpose or effect, or likely effect of substantially lessening competition;
- agreements, arrangements and understandings between competitors where they refuse to acquire goods or services from or supply goods or services to another person (referred to as a primary boycott);
- agreements which in effect fix or maintain prices;
- actions by persons that have a substantial degree of market power which intentionally eliminate competitors or prevent others from entering any market or engaging in competitive conduct in any market;
- arrangements that make it a condition of supplying goods or services that the buyer must refuse a competitor’s goods or services or accept goods or services from a third person (referred to as exclusive dealing);

- arrangements where a supplier requires the person receiving the goods or services not to sell those goods to another person at less than a price set by the supplier (referred to as resale price maintenance); and
- mergers that lead to a substantial lessening of competition.

These competitive conduct rules limit the ability of persons engaged in occupations from behaving in anti-competitive ways.[6] This includes conduct by professional bodies and any occupational rules (agreements) or regulatory activities made or undertaken by such bodies. For example, if rules established by professional bodies included controls on location of their members' businesses which had the effect of market sharing, these could be regarded as anti-competitive and illegal.

Nevertheless, the law recognises that some agreements which restrict competition may be justified if the restriction yields an overall public benefit. If so they can be authorised through a public process which weighs the anti-competitive detriment against the public benefit.

It is recognised that many self-regulatory activities by professional bodies are desirable. If these rules are anti-competitive they could be subject to authorisation by the ACCC. What will be required under the law is a determination that any anti-competitive effects are not unjustifiably restrictive and have a net public benefit.

An example of an authorisation of this kind comes from the Australian Institute of Valuers and Land Economists which approached the ACCC for an authorisation for its code of ethical and commercial practice. Amongst other features, the code provided for an enforcement process and required registered practitioners to engage in the Institute's continuing professional development programme to qualify for further certification. Although some jurisdictions regulate valuers through registration, the Institute recognised that with the development of mutual recognition arrangements between States, partial registration may be replaced by national deregulation. In this context, the Institute took the view that its national code of practice was essential to maintain and enforce standards with respect to the activities of all registered practitioners. Given the possibility that deregulation would leave the Institute as the sole industry regulator, the ACCC agreed that the code held significant benefit for consumers and authorised its application, subject to conditions minimising its anti-competitive effect.

As a result of the extension of the Trade Practices Act occupational or professional associations now need to consider the anti-competitive effect of their existing and/or proposed activities and rules, and the likelihood of

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6 The law provides a general exemption in respect of contracts for labour. Hence, the collective bargaining activities of unions and their members in respect of conditions of service are not contrary to the law.

authorisations for such practices. Where authorisations are not granted, occupations will need to consider changing their practices or amending their rules. Consideration of these issues will need to be ongoing, evolving in concert with the review and revision of occupational rules by professional bodies and/or government.

The general application of competition law in Australia to limit regulatory capture by professional bodies reflects a policy preference that competition issues of this type should be subject to general prohibitions rather than a sector by sector treatment. That said, if there is no competition law applicable to this type of activity, a sector by sector approach should be considered.

Review of Anti-Competitive Regulation

Government regulation can also bring about anti-competitive outcomes by creating entry barriers or mandating particular conduct. Generally, neither the regulation itself nor the conduct of those complying with the regulation will be contrary to the competition laws.[7] Much occupational regulation is of this type.

All Australian Governments have agreed to review, and where appropriate reform, all anti-competitive legislation (including regulations) by the year 2000. The guiding principle of legislation review specified under NCP is that legislation should not restrict competition unless it can be demonstrated that:

- the benefits of the restriction to the community as a whole outweigh the costs; and
- the objectives of the legislation can only be achieved by restricting competition.

Attachment A contains an extract from the Competition Principles Agreement which sets out further details. More than 1500 separate enactments have been scheduled by all jurisdictions for review under the programme. Legislation that provides for regulation of occupations and is considered to be anti-competitive is subject to the required cost/benefit assessment by the relevant jurisdiction in order to determine whether the Act or regulation should be retained without amendment, amended or repealed. Attachment B provides a matrix of selected occupational regulation that will be subject to review. The reviews will be

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7 It is possible for such regulation/conduct to be inconsistent with the competition laws, say if the regulation permitted price collusion in a particular profession. In this event the competition laws would prevail, unless the regulation were in a transparent form specifically exempting the conduct from the Trade Practices Act. Such exempting regulations are an alternative to the authorisation procedure. Any such exemptions must specifically identify the conduct concerned and reference it as exempt from the Act. As inherently anti-competitive regulations, such exemptions are subject to the regulatory quality mechanisms discussed below. Any exemption enacted by the Commonweatlh Government must be specifically approved by the Treasurer. It is also possible for the Commonwealth Government to override exempting regulations made by a State or Territory Government.

required to address the issues explored in this paper, including identifying the objective of the regulation and considering alternative mechanisms to achieve the objective. In some cases jurisdictions may agree to nationally coordinated reviews. Such reviews may occur where State or Territory legislation complements Commonwealth legislation or where regulated activities are common to a number of jurisdictions. National reviews may be conducted by an independent person(s) appointed by jurisdictions, the newly created National Competition Council (NCC), or perhaps dealt with by the relevant Ministerial Council.

As part of the Competition Principles Agreement the Commonwealth Government agreed to make payments to the States and Territories if they made satisfactory progress with competition policy reforms. The NCC plays a role in enhancing the transparency of the process and assessing the progress of the States and Territories.

The NCP effectively places the onus on the person seeking to retain or introduce a legislative or regulatory restriction on competition to prove that the restriction is justifiable. Importantly, this marks a departure from the common onus of proof which rests with the proponent of change to demonstrate the benefits of moving from the status quo. A broad range of restrictions are captured within the NCP framework. For example, the Queensland Government in its Legislative Review Schedule has classified restrictions against each piece of legislation. The restrictions are: outright prohibition; statutory monopoly; licensing or registration; quantitative entitlements; quality/technical standards; pricing restrictions; business conduct restrictions; preferred supplier/customer arrangements; measures that confer benefit; natural resources permits and licences; and restrictions on out of State parties.

The principle that regulation should only restrict competition if it is necessary to achieve the objective of the regulation recognises that restricting competition can often have unintended consequences and that there will commonly be more direct or less restrictive ways to achieve the desired objective. By way of example, it would be reasonable to argue that strict qualification requirements were necessary to ensure the safety of brain surgery. But it would generally not be reasonable to argue that a numerical limit on the number of taxis was necessary to ensure the safety of taxi travel — a more direct regulatory mechanism would be to prescribe minimum maintenance standards for taxis.

The NCP legislation review principles are also applicable to new regulation as part of the regulatory quality mechanisms. To meet this requirement jurisdictions require proposals for new legislation or amendments to existing legislation to be accompanied by regulatory impact analyses which are designed to indicate whether the proposed regulation imposes restrictions on competition and meets other regulatory best practice principles. Relevant central agencies in jurisdictions are responsible for assessing the comprehensiveness and appropriateness of such statements before the regulatory proposal is considered by Cabinet.

In concert with the ratification of NCP at their meeting in April 1995, Heads of Government also agreed to *Principles and Guidelines for National Standards Setting and Regulatory Action by Ministerial Councils and Standards Setting Bodies*. The guidelines identify the elements of appropriate regulation and propose a number of principles to guide regulatory action by Commonwealth-State Ministerial Councils and other national standard setting bodies. The recommended principles are designed to apply to agreements or decisions which are to be implemented through legislation, regulation, administrative directions or other measures and which would have the effect of encouraging or compelling businesses or individuals to act in ways they would not have otherwise done. Further details are in Attachment C. A number of States have issued guidelines which implement similar principles.

Some Examples

The review of legislation and regulations, development of better regulatory management systems, improvements to the quality of regulation, and deregulation processes able to be applied under the NCP framework are significant tools in the reform of occupational regulation. They bring the regulation of occupational services in line with general structural reforms being applied to the Australian economy and therefore represent a recognition by governments that occupational regulation must reflect changes in practice, law and custom, if it is to foster the most appropriate outcomes for consumers and service providers. The NCP regulation review process is at a relatively early stage. Nevertheless, there have been a number of results in the area of occupational regulation which illustrate potential outcomes.

The New South Wales (NSW) Parliament has recently passed the State Government's *Regulation Reduction Act 1997* which repeals 85 occupational licences in a number of areas including agriculture, construction and manufacturing, entertainment, the environment and pest control. These licences were considered to hinder competition within the respective industries by imposing unnecessary costs on commerce and limitations on the movement of labour, to an extent that outweighed any net public benefit. The review and repeal of these licences is consistent with and an integral part of the NSW Government's legislation review programme under NCP.

The Commonwealth reviewed the patent attorney profession in 1996. The review report addressed the regulatory regime for patent attorneys, as well as for trademark and designs practitioners. The Government has announced reforms to the profession with measures such as:

- allowing any person, including those without qualifications, to prepare and lodge trademark applications;
- a new title, known as Trademark Attorney, will be introduced, requiring a lower level of qualifications than those for patent attorneys. This will be an accreditation mechanism;

- accreditation has been transferred to universities in line with other careers;
- the Patent Attorneys Professional Standards Board will now have members from user groups; and
- allowing more flexible business structures, including mixed partnerships of patent attorneys and lawyers.

However, the Government decided that it would not substantially reduce the entry requirements and reserved work area of patent attorneys. This reflected an assessment of the risk for users of the patent system if entry restrictions were relaxed given that a patent application is a ‘one shot’ process and there are substantial risks of loosing patent protection if a patent application is misspecified.

The Queensland Government has undertaken a review of the health professions in that State. A comprehensive discussion paper with recommendations was released for comment in September 1996. The discussion paper includes the Queensland Government’s preferred position at the time of release. Some of the reforms that are proposed in the paper include:

- ownership restrictions will be removed in most health professions;
- significant reductions in the controls on advertising;
- the number of consumer members on registration boards will be increased; and
- an independent Health Practitioner Tribunal will deal with serious issues of misconduct. This would represent a substantial simplification of present redress mechanisms.

Mutual Recognition

Technological and other developments in a range of service, construction, entertainment, agricultural and other industries mean that a far greater proportion of services are traded across jurisdictional boundaries. This is particularly the case when the physical location of the service provider does not have to be in the same location as the service recipient. If the primary rationale for occupational regulation is consumer protection, then these concerns obviously extend to services provided from another jurisdiction (or provided by the resident of another jurisdiction). Accordingly, if a particular jurisdiction wants to ensure that its consumers are adequately protected, then it generally needs to be convinced that appropriate quality standards are met by all providers.

Traditionally this has been achieved by prescriptive jurisdictionally based standards being imposed. This tended to be the case in Australia where each State jurisdiction had distinct rules, interests and history governing its approach to regulation. For example, in some States lawyers are able to gain admission as solicitors and barristers simultaneously. In other States lawyers must either be registered as a barrister or solicitor, but not both at the same time. Such distinct arrangements may create barriers to entry or other restrictions on practice. Hindering the mobility of labour contributes to the control of supply that many professional or occupational associations enjoy, thereby assisting an environment in which costs of services can be kept high.

Resolution of problems caused by divergence of regulation between jurisdictions can be pursued either through efforts aimed at convergence (as is happening to some extent in Australia in the legal services markets) and / or through mutual recognition arrangements. Mutual recognition arrangements provide for out of jurisdiction practitioners to provide equivalent occupation services within a jurisdiction with minimum constraints. Mutual recognition can be used where jurisdictions agree that it is not necessary to have complete uniformity in occupational regulation across jurisdictions but they nevertheless have sufficient confidence in the regulatory processes of other jurisdictions to rely on the registration decisions of those jurisdictions. Mutual recognition requires agreement between jurisdictions on what constitutes equivalent occupations and can also include cooperative efforts to establish competency standards.

Mutual recognition arrangements with respect to occupational registration and licensing can assist with remedying restrictions on competition within regional markets by increasing the degree of integration with other markets. Importantly, mutual recognition can also reduce the influence of regulatory capture, as those aiming to exclude new entrants would need to capture the regulatory processes in all jurisdictions subject to mutual recognition.

In 1992 Australian Heads of Government signed the *Intergovernmental Agreement on Mutual Recognition*. This agreement is given effect to by the Commonwealth's *Mutual Recognition Act 1992* and complementary State legislation. The mutual recognition scheme has two principles:

- goods sold lawfully in one jurisdiction may be sold in any other, even though the goods may not comply with all the details of the regulatory standards in the second jurisdiction; and
- a person registered in one jurisdiction can be registered to carry out the equivalent occupation in any other jurisdiction, without the need for further assessment or qualifications.

With respect to occupational services the mutual recognition scheme includes registration, licensing, approval and admission requirements, certification, and any other form of authorisation necessary for carrying out an occupation. Simply, the scheme entitles a person registered in one Australian jurisdiction to register in any other Australian jurisdiction. If an occupation is not equivalent between jurisdictions it is possible for some limitations to be placed on the scope of practice of the out of jurisdiction applicant. There are also cooperative mechanisms involving Ministerial Councils to establish competency standards where jurisdictions choose to harmonise standards or where disagreements as to the appropriateness of a standard arise in respect of a particular jurisdiction. Jurisdictions have agreed to be bound by a two-thirds majority of jurisdictions in determining new or modified competency standards. The *Principles and Guidelines for National Standards Setting and Regulatory Action by Ministerial Councils and Standards Setting Bodies* apply in respect of any competency standards developed by relevant Ministerial Councils. It is important to note that these principles require that, where possible, regulatory standards should be consistent with international standards and practice. The scheme does not affect initial registration requirements nor regulations relating to the conduct or practices of occupations in particular jurisdictions.

In June 1996, Heads of Government agreed to extend the current Mutual Recognition scheme to include New Zealand according to a Trans-Tasman Mutual Recognition Arrangement. Legislation to enact the Trans-Tasman Mutual Recognition Agreement is currently before the Commonwealth and New Zealand Parliaments. The Agreement provides for reciprocal treatment between New Zealand, Australia and the Australian States and Territories. A person wishing to practice in the other country need only give notice of their registration to the local registering authority in the other country. Mechanisms are also established to facilitate setting of competency standards as in the Australian Mutual Recognition Agreement. The only exception to mutual recognition of occupations is the medical profession which has been specifically excluded.

Similar initiatives are being discussed at APEC level. The Human Resources Working Group is currently conducting a study into the comparability and disparity of skills testing standards in the Asia-Pacific region, in order to develop a feasible basis for mutual recognition among APEC members.

The major benefit of mutual recognition is to remove barriers to trade between broadly similar systems. Nevertheless, there are some limitations on the effectiveness of mutual recognition schemes. Such schemes work well when the occupation in the jurisdiction where the practitioner is registered and the occupation in the jurisdiction where he/she is applying for registration is substantially the same. Difficulties can arise, for example, in a situation where a practitioner from one jurisdiction which does not require registration seeks to become registered in another jurisdiction. In other words, if the regulatory frameworks are not compatible, mutual recognition may be of little assistance. In these circumstances if jurisdictions wish to bring their markets together on a reciprocal basis, they may need to first consider some form of regulatory convergence. The existence of a mutual recognition scheme does create an incentive for jurisdictions to pursue convergence of national standards for occupational registration and licensing. In Australia, mutual recognition has encouraged the development of national minimum standards for the practice of medicine and the development of registration rules for lawyers that ensure consistency between jurisdictions. The Principles and Guidelines for National Standards Setting discussed above are of course designed to assist this process.

It has proved more difficult to pursue convergence where one or more jurisdictions wishes to maintain non-registration of a particular occupation but this is not regarded as a major difficulty — a person wishing to practise Australia-wide in such partially registered occupations need only satisfy registration requirements in the jurisdiction that has the least restrictive registration requirements.

The last point serves to illustrate that convergence in regulation need not be pursued as an end in itself. There are some benefits in ‘regulatory competition’ between jurisdictions in terms of discovering better ways to regulate particular sectors. Conversely, if all jurisdictions are required to have the same regulation, this can give rise to a regulatory gridlock problem where it is difficult to implement beneficial changes to regulation. Indeed, this can be seen as one of the major benefits of the mutual recognition approach as it allows jurisdictions a degree of flexibility to pursue regulatory reforms without necessarily having to get agreement of all other related jurisdictions once there has already been a substantial degree of regulatory convergence. In that sense, mutual recognition is an important step to ensure that there are no non-tariff barriers to trade.

CONCLUSION AND GENERAL PRINCIPLES

Occupational regulation has a legitimate underlying rationale to protect the consumer due to the complexity of the services in question. However, actual regulations may not be well targeted to address these rationales and may be captured by and confer inappropriate benefits upon those who are regulated. Governments have become more aware of potential problems with regulation and have initiated a range of review processes and ongoing accountability mechanisms to make regulation more effective.

The discussion in this paper has raised a number of questions regarding appropriate policy towards regulation. The following principles attempt to capture the answers to these questions.

- The objective of a regulation should be clearly identified and the need for a regulatory solution should be demonstrated.
- The merits of a regulation should be assessed from an economy-wide perspective.
  - That includes an assessment of the interests of those who the regulation is intended to benefit and those who are regulated, including the compliance costs. Where feasible, this should include consultation with affected parties.

- Minimum feasible regulation which minimises restrictions on competition should be used to ensure that regulations are well targeted and to minimise the likelihood of unintended consequences of regulation.
  - The effects of various options (including non-regulatory options) should be analysed, including direct and secondary effects and implementation issues, to determine the net costs and benefits of the options.
  - Where possible, regulatory standards should be consistent with international standards to minimise barriers to international competition.
- Competition law or some other controls should apply to ‘self-regulatory’ activities of professional organisations to ensure that these do not bring about unjustified restrictions on competition.
- Jurisdictions should ensure that regulatory bodies are comprised of members that strike an appropriate balance between the need to have regulations set and administered by individuals with sufficient expertise, and the need to ensure that representatives of an occupation do not have inappropriate control over entry and conduct in a profession.
- Regulations should be subject to an ongoing review process to ensure that the rationale for their existence remains relevant, and to ensure that the regulation remains the best way of addressing any underlying problem.

ATTACHMENT A — EXTRACT FROM COMPETITION PRINCIPLES AGREEMENT

Legislation Review

1. The guiding principle is that legislation (including Acts, enactments, Ordinances or regulations) should not restrict competition unless it can be demonstrated that:

   a) the benefits of the restriction to the community as a whole outweigh the costs; and

   b) the objectives of the legislation can only be achieved by restricting competition.

2. Subject to subclause (3), each Party is free to determine its own agenda for the reform of legislation that restricts competition.

3. Subject to subclause (4) each Party will develop a timetable by June 1996 for the review, and where appropriate, reform of all existing legislation that restricts competition by the year 2000.

4. Where a State or Territory becomes a Party at a date later than December 1995, that Party will develop its timetable within six months of becoming a Party.

5. Each Party will require proposals for new legislation that restricts competition to be accompanied by evidence that the legislation is consistent with the principle set out in subclause (1).

6. Once a Party has reviewed legislation that restricts competition under the principles set out in subclauses (3) and (5), the Party will systematically review the legislation at least once every ten years.

7. Where a review issue has a national dimension or effect on competition (or both), the Party responsible for the review will consider whether the review should be a national review. If the Party determines a national review is appropriate, before determining the terms of reference for, and the appropriate body to conduct the national review, it will consult Parties that may have an interest in those matters.

8. Where a Party determines a review should be a national review, the Party may request the [National Competition] Council to undertake the review. The Council may undertake the review in accordance with the Council's work programme.

9. Without limiting the terms of reference of a review, a review should:

   a) clarify the objectives of the legislation;

   b) identify the nature of the restriction on competition;

c) analyse the likely effect of the restriction on competition and on the economy generally;

d) assess and balance the costs and benefits of the restriction; and

e) consider alternative means for achieving the same result including non-legislative approaches.

10. Each Party will publish an annual report on its progress towards achieving the objective set out in subclause (3). The Council will publish an annual report consolidating the reports of each Party.

ATTACHMENT B — OCCUPATIONAL REGULATION: SELECTED REVIEWS BY JURISDICTION

Legislation Group	Victoria	New South Wales	Western Australia	Queensland	South Australia	Tasmania	Australian Capital Territory	Northern Territory
Real Estate Agents & Auctioneers	Estate Agents Act 1980 & Regs, Auction Sales Act 1958 1996-97 review		Auction Sales Act 1973 & Regs 1998 review Real Estate & Business Agents Act 1978 2000 review Settlements Agreement Act 1981 & Regs 1997 review	Auctioneers & Agents Act 1971 & Regs 1996-97 review	Land Agents Act 1994 2000 review	Auctioneers & Real Estate Agents Act 1991 national review proposed	Agents Act 1968, Auctioneers Act 1959 1996 review	Agents Licensing Act, Auctioneers Act 1997-99 review
Chiropractors and Osteopaths	Chiropractors and Osteopaths Act 1978 review completed	Chiropractors and Osteopaths Act 1991 1997-98 review	Chiropractors and Osteopaths Act 1964 & Regs 1997 review	Chiropractors and Osteopaths Act 1979 review underway	Chiropractors Act 1991 national review proposed	Chiropractors Registration Act 1982 national review proposed	Chiropractors and Osteopaths Act 1983 timing of review to be announced	Health Practitioners & Allied Professionals Registration Act review by end 1997
Dentists	Dental Act 1972 & Regs, & Dental Technicians Act 1972 1996-97 review	Dentists Act 1989 1995-96 review Dental Technicians Registration Act 1975 1999-2000 review	Dental Act 1939 & Regs, & Health (School Dental Therapists) Regs 1974 1999 review	Dentists Act 1971, Dental Technicians & Prosthesis Act review underway	Dental Act 1984 national review proposed	Dental Act 1982 national review proposed	Dentists Registration Act 1931, Dental Technicians & Prosthesis Registration Act 1988 timing of review to be announced	Dental Act review by June 1997

Legislation Group	Victoria	New South Wales	Western Australia	Queensland	South Australia	Tasmania	Australian Capital Territory	Northern Territory
Lawyers		Legal Professions Act 1987 1996-97 review Conveyancers Licensing Act 1995 1999-2000 review	Legal Practitioners Act 1983 1996 review	Legal Practitioners Act 1995 1998-99 review	Legal Practitioners Act 1981 1997 review Conveyancers Act 1994 2000 review	Legal Practitioners Act 1993 national review proposed	Legal Practitioners Act 1970 timing of review to be announced	
Doctors	Medical Practice Act 1994 1998 review	Medical Practice Act 1993 1995-96 review	Medical Act 1984 1997 review	Medical Act 1939 review underway	Medical Practitioners Act 1983 national review proposed	Medical Practitioners Act 1996 national review proposed	Medical Practitioners Act 1930 1996 review	Medical Act review by June 1997
Nurses	Nurses Act 1993 1998 review	Nurses Act 1991 1997-98 review	Nurses Act 1992 1997 review	Nurses Act 1992 & Nursing By-Law 1993 1998-99 review	Nurses Act 1984 national review proposed	Nurses Act 1995 national review proposed	Nurses Act 1988 timing of review to be announced	Nursing Act review completed
Radiographers	Health Act 1958 (Radiographers) 1998-99 review Health (Radiation Safety) Regs 1994 1998-99 review	Radiation Control Act 1990 review completed Radiation Protection Control Act 1982 1998 review	Radiation Safety Act 1975 & Regs 1999 review		Radiation & Protection Control Act 1982	Radiographers Registration Act 1971 national review proposed	Radiation Act 1983 1997 review	Radiographers Act Review by June 1997
Optometrists	Optometrists Act 1958 & Regs review completed	Optometrists Act 1930 1996-97 review Optical Dispensers Act 1963 1999-2000 review	Optometrists Act 1940 & Regs 1997 review Optical Dispensers Act 1963 1997 review	Optometrists Act 1974 review underway	Optometrists Act 1920 national review proposed	Optometrists Act 1994 national review proposed	Optometrists Act 1956 review completed	Optometrists Act 1997 review

Legislation Group	Victoria	New South Wales	Western Australia	Queensland	South Australia	Tasmania	Australian Capital Territory	Northern Territory
Pharmacists	Pharmacy Act 1974 & Regs 1997-98 review	Pharmacy Act 1964 1997-98 review	Pharmacy Act 1964 & Regs 1997 review	Pharmacy Act 1976 review underway	Pharmacy Act 1991 national review proposed	Pharmacy Act 1908 national review proposed	Pharmacy Act 1931 review completed	Pharmacy Act review completed
Physiotherapists	Physiotherapists Act 1978 & Regs 1997 review	Physiotherapists Registration Act 1945 1997-98 review	Physiotherapists Act 1950 & Regs 1997 review	Physiotherapists Act 1964 & Regs review underway	Physiotherapists Act 1991 national review proposed	Physiotherapists Registration Act 1951 national review proposed	Physiotherapists Act 1977 1996 review	Health Practitioners & Allied Professionals Registration Act review by end 1997
Podiatrists		Podiatrists Act 1989 1996-97 review	Podiatrists Registration Act 1984 & Regs 1997 review	Podiatrists Act 1969 review underway	Chiropodists Act 1950 national review proposed	Podiatrists Registration Act 1974 & 1995 national review proposed	Podiatrists Act 1994 timing of review to be announced	
Psychologists	Psychologists Registration Act 1987 1997 review	Psychologists Act 1989 1996-97 review	Psychologists Registration Act 1976 & Regs 1997 review	Psychologists Act 1977 review underway	Psychological Practices Act 1973 national review proposed	Psychologists Registration Act 1976 national review proposed	Psychologists Registration Act 1994 timing of review to be announced	Health Practitioners & Allied Professionals Registration Act review by end 1997
Ship Pilots	Marine (Navigation & Operation of Vessels) Act 1996-98 review	Marine Pilotage Licensing Act 1971 review completed	Shipping & Pilotage Act 1967 & Regs 1998-99	Transport Operations (Marine Safety Act) 1994 1996-97 review	Harbour & Navigation Act 1993 1997 review			Marine Act Regs review by 30 June 1997
Travel Agents	Travel Agents Act 1986 & Regs 1996-98 review	Travel Agents Act 1986 1997-98 review	Travel Agents Act 1985 & Regs 1998-99 review	Travel Agents Act 1988 & Regs 1997-98 review	Travel Agents Act 1986 national review proposed	Travel Agents Act 1987 national review proposed	Travel Agents Act 1968	

Legislation Group	Victoria	New South Wales	Western Australia	Queensland	South Australia	Tasmania	Australian Capital Territory	Northern Territory
Veterinary Surgeons	Veterinary Surgeons Act 1958 & Regs 1995-96 review	Veterinary Surgeons Act 1986 1996-97 review	Veterinary Surgeons Act 1960 1996-97 review	Veterinary Surgeons Act 1936 1998-99 review	Veterinary Surgeons Act 1992 national review proposed	Veterinary Surgeons Act 1987 national review proposed	Veterinary Surgeons Act 1965 1997 review	Veterinarian Act review by 30 June 1998
Building Occupations - architects - surveyors - engineers - gas fitters - plumbers - drainers	Surveyors Act 1978 1996-97 review Architects Act 1991 1998-99 review Plumbers, Gasfitters & Drainers Registration Act 1981 1998-99 review	Architects Act 1921 review underway Surveyors Act 1929 review underway	Architects Act 1921 & Regs 1997 review Builders Registration Act 1939 & Regs 1999-2000 review Licensed Surveyors Act 1909 & Regs 1998 review Electricity Act 1995 review underway	Architects Act 1985 & Regs 1998-99 review Sewerage & Water Supply Act 1949 1997-99 review Queensland Building Services Authority Act 1991 1997-98 review Electricity Act 1994 1996-97 review Professional Engineers Act 1988 1998-99 review Gas Act 1965 1996-97 review Surveyors Act 1977 & Regs 1996-97 review	Architects Act 1939 national review proposed Plumbers & Gasfitters Act 1995, & Building Work Contractors Act 1995 2000 review	Architects Act 1929 national review proposed	Architects Act 1959, & Plumbers, Drainers & Gasfitters Act 1982 timing of review to be announced Building Act 1972 1997 review Surveyors Act 1967 1997 review	Architects Act, Licensed Surveyors Act, Electrical Contractors Act, Plumbers Drainers Licensing Act reviews to be completed by June 1997
Building and land valuers		Valuers Registration Act 1975 1996-97 review	Land Valuers Licensing Act 1978 & Regs 1999-2000 review	Valuers Registration Act 1992 & Regs 1996-97 review	Land Valuers Act 1994 2000 review	Valuers Registration Act 1974 national review proposed		

ATTACHMENT C — PRINCIPLES OF REGULATION SETTING

In concert with the ratification of NCP at their meeting in April 1995, Heads of Government also agreed to *Principles and Guidelines for National Standards Setting and Regulatory Action by Ministerial Councils and Standards Setting Bodies*. The guidelines identify the elements of appropriate regulation and propose a number of principles to guide regulatory action by Commonwealth-State Ministerial Councils and other national standard setting bodies. The recommended principles are designed to apply to agreements or decisions which are to be implemented through legislation, regulation, administrative directions or other measures and which would have the effect of encouraging or compelling businesses or individuals to act in ways they would not have otherwise done.

The principles themselves are also consistent with the aims of competition policy and are particularly useful for improving the outcomes associated with occupational regulation. The principles of good regulation identified by Heads of Government are that:

- the person seeking regulation must prove that it is necessary;
- the overall aim is effective enforcement of identified objectives with a minimum amount of regulation;
- regulations should have a minimal impact on competition;
- regulatory outcomes should be predictable and clearly identifiable;
- where possible, regulatory standards should be consistent with international standards and practice;
- regulations should not restrict international trade;
- regulation should be subject to periodic review;
- nominated outcomes of standards and regulatory measures should be capable of revision; and
- regulation should attempt to standardise the exercise of bureaucratic discretion.

In order to manage these mechanisms to improve the quality of regulation, Heads of Government recommend that Ministerial Councils proposing regulatory controls, and other standard setting bodies, pursue the following objectives of good regulation:

- legislation should contain the minimum regulation necessary to achieve the identified aims;
- the administrative burden of regulation should be reduced;
- proposed regulation should be subject to the regulatory impact process;

- Ministers should secure full government agreement for regulatory action before such matters are considered at Ministerial Council level;
- compliance strategies should ensure the greatest level of compliance at lowest cost to all the parties;
- regulatory measures must take any secondary effects into account;
- standards should be referenced as current editions in appendices rather than included in the regulatory instrument itself;
- regulatory instruments should be performance based, focussing on outcomes rather than inputs;
- commencement of regulatory measures should be planned so as to assist the business or other cycles of affected parties, and provide for a transition to compliance;
- new regulatory measures should be advertised to inform relevant parties; and
- there should be wide public consultation.

These principles go towards the creation of a nationally consistent assessment process for national standards. To facilitate this, Heads of Government have agreed to a number of processes in relation to the development of national standards. Primarily, Ministerial Councils or standards setting bodies must certify that the regulatory impact statement process has been fulfilled in accordance with the guidelines above. A copy of the regulatory impact statement must be forwarded to the Commonwealth's Office of Regulation Review for information. Any proposed national standard may be reviewed where requested by two or more dissatisfied jurisdictions.

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Assessing Fiscal Policy in an Accrual Environment

This paper was presented by Mr Michael Clark-Lewis, Director, Fiscal Framework and Reporting Section, Fiscal Policy Division, Treasury to the Accrual Budgeting Conference on 18 September 1997. The presentation examines the implications of the Government's adoption of accrual budgeting for assessing the impact of fiscal policy on the economy.

INTRODUCTION

My talk today examines the implications of accrual reporting for assessing government performance at the aggregate level. In particular I wish to focus on the relevance of accrual measures for assessing the impact of fiscal policy on the economy.

Along the way I wish to draw out some of the differences between businesses — the traditional users of accrual reporting — and government and the implications of these differences for measuring aggregate government performance under an accrual framework.

EVALUATING FISCAL MEASURES

In assessing overall government performance two distinct aspects can be identified. One is to assess how a government is managing its own finances: is the government’s fiscal position financially sound and sustainable? The other is to measure how the government is affecting the economy.

It is the second of these themes that is unique to government. Business is not concerned with the effect of their activities on behaviour in Australia as a whole. However, for governments the economic consequences of their actions are important.

This economic focus is evident in the Government’s medium-term fiscal strategy — outlined in the 1997-98 Budget Papers — which is to follow as a guiding principle the objective of maintaining an underlying budget balance on average over the course of the economic cycle. This approach seeks to ensure that over time the Government saves enough to cover its investment needs and so does not make a direct contribution to the national saving-investment imbalance.

The Government’s medium-term fiscal strategy reflects the importance the Government places on raising national saving relative to national investment, thereby reducing the current account deficit and raising longer-term growth prospects.

MEASURING FISCAL POLICY IN A CASH ENVIRONMENT

Budget Deficit

The headline budget deficit measure was for a long time the primary aggregate fiscal measure. It was used to assess both the economic impact of fiscal policy and the soundness of fiscal policy. Few users would stop and think about the nuances of these two perspectives; however, as I will discuss later these differences are important, particularly in an accrual environment.

The budget deficit is of course a cash measure, reflecting the fact that the Commonwealth, in common with virtually all governments in the world, currently reports and budgets on a cash basis. That is to say it records all transactions at the time payments are made.

The budget deficit is defined as government spending (including both capital and current spending as well as net advances) less government revenue. The deficit indicates whether a government is able to finance all its expenditure in any year with the revenue it raises in that same year. That is, it provides an indication of the government’s net financing requirement.

Measuring Economic Activity

In addressing the economic effects of fiscal measures it is appropriate to relate these measures to the national accounts — our primary tool for measuring economic activity. Within the national accounts the concept of **net lending** is the key measure for assessing the direct economic impact of government spending and taxation decisions on economic activity.

Net lending represents the extent to which the government provides or withdraws net resources from other sectors of the economy. Typically the government is a net borrower (ie, has a negative net lending position).

Net lending is the balance between government saving and investment. It represents the direct impact of government spending and taxation policies on domestic demand. The government's net lending position also directly contributes to national net lending (which is the sum of each sector's net lending position). National net lending measures the economy's call on foreign savings which in turn is reflected in the current account deficit.

Net lending is thus a particularly important measure of fiscal policy: it provides information on the direct impact of fiscal policy on domestic demand and national saving.

It is appropriate therefore, when assessing the economic impact of fiscal policy, that we choose a measure that closely approximates the national accounts net lending measure. For this reason, the current Government adopted the **underlying deficit** as the primary measure of fiscal policy in March 1996.

The underlying deficit abstracts from a class of transactions termed net advances that do not typically affect economic production. Net advances comprise equity asset sales / purchases and policy lending.

- Equity asset sales and purchases represent a change of ownership but do not of themselves represent a change in economic activity as no new production takes place.
- Policy lending, such as loans to State Governments, are generally a financing transaction. Such transactions do not directly affect economic activity: this only occurs when the funds are spent by the borrower.

While the adoption of the underlying deficit was primarily motivated by a desire to better match the measure of fiscal policy with the Government's macroeconomic policy objective, it also has advantages in assessing the soundness of the government's fiscal position. This is because the two transactions excluded — policy lending and asset sales — do not affect the government's balance sheet and so do not affect the government's overall financial position.

In summary, the underlying deficit improves on the headline deficit for measuring both fiscal sustainability and the economic impact of fiscal policy.

MEASURING FISCAL POLICY IN AN ACCRUAL ENVIRONMENT

Accrual Measures and Economic Impact

Having adopted the underlying deficit measure, an important question is how the introduction of accrual accounting may change the measurement of fiscal policy.

The main difference between cash and accrual accounting is the time when transactions are recorded. The accrual framework attempts to measure all flows at the time economic value is created, transformed, exchanged, transferred or extinguished. The cash framework measures flows when payment is made.

The national accounts framework recommends measuring all transactions on an accrual basis. However, government transactions in the national accounts are not fully on an accrual basis, reflecting data limitations due to the use of cash accounting by Commonwealth and State Governments.

The adoption of accrual budgeting and reporting by Commonwealth and State Governments will affect both the national accounts[8] and budget presentation of government transactions. In making this change the appropriateness of available fiscal measures needs to be reassessed.

Before turning to those issues, it is pertinent to examine why the national accounts favour the accrual basis of recording transactions. There are two reasons:

- it ensures consistency of timing between transactions. An advantage of the accrual framework is that economic flows such as the profitability of productive activities can be measured without distorting leads and lags in actual cash payments; and
- it allows for the measurement of non-monetary flows which can affect economic well being and behaviour.

The accrual measurement of transactions can more accurately reflect when productive activity is taking place, avoiding distortions that can arise from leads and lags in actual cash payments. However, an accrual transaction basis is not unequivocally superior in measuring the direct economic impact of transactions. An example is the treatment of accruing superannuation entitlements (accumulated by eligible employees over their working life). Under the accrual framework accruing superannuation entitlements are treated in the same way as other income. The accrual approach recognises that accruing entitlements will influence personal spending and saving behaviour. However, it

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8 The principal change will be the inclusion of accruing superannuation entitlements as a government expense instead of the cash expenditure on superannuation. Further changes will also occur due to the implementation of the international *System of National Accounts 1993*, which updates the United Nation's 1968 *A System of National Accounts.*

is not clear that an extra dollar received in superannuation entitlements will have the same impact on consumer spending as an extra dollar in cash even though the accruals framework treats them exactly the same. In this case an extra dollar of cash income may have a more direct effect on an individual's spending and saving behaviour and hence a more immediate impact on economic activity.

The Government's adoption of accrual accounting will allow the national accounts to more fully record government transactions on an accruals basis. Nonetheless, the national accounts will continue to use the net lending concept discussed earlier for measuring the budget's economic impact. At issue is whether standard accrual accounting measures, such as the operating balance and the change in net assets (also termed change in net equity or change in net worth) will enable us to approximate the national accounts measure of government net lending when it changes to an accruals basis.

A key feature of net lending is that it takes account of the acquisition of capital, whereas standard accrual measures only take account of the consumption of capital. This reflects the different perspective of the national accounts, which is to measure production, compared to the standard accrual presentation which focuses on resource use. These two perspectives are illustrated when we compare the effects of the government operating a motor vehicle for a year and purchasing a new motor vehicle.

- If the government runs a motor vehicle for a year then it will have consumed part of the life of that motor vehicle. The standard accrual presentation records that consumption of resources in the form of depreciation.
- However, the direct economic consequences of running a motor vehicle for a year are minimal compared to the consequences of purchasing a new motor vehicle. When the government purchases a new motor vehicle it is directly contributing to the employment of labour and capital used in producing that motor vehicle.

The national accounts records both the consumption of capital and new investment in capital. For example, saving in the national accounts takes account of the consumption of capital. However, in deriving net lending the acquisition of capital (equivalent to the change in the stock of new capital assets on the government's balance sheet) is included and the consumption of capital excluded. In this way, the national accounts net lending measure adopts the accrual timing of transactions but also takes account of the acquisition of capital to more accurately measure the government's direct impact on economic activity.

It follows from my discussion that the underlying deficit may no longer be an accurate approximation of net lending once the national accounts begin to reflect the additional information that the Government's adoption of accrual reporting will provide. In addition, because of the different treatment of capital in the national accounts, standard accrual measures (such as the operating balance and change in net assets) will not be appropriate for measuring the economic impact of fiscal policy.

However, the Government will be able to continue to include measures in government finance statistics that closely estimate net lending as measured in the national accounts. Moreover, the potential exists for net lending in the national accounts and government finance statistics to be calculated in exactly the same way. However, at this stage it is unclear whether this will be fully achieved. This reflects a number of differences that exist between the accounting and national accounts frameworks in the treatment of certain transactions. These issues are still being worked out. Nonetheless, the adoption of accrual accounting by the Government will bring government financial accounting closer to the approach recommended in the national accounts.

Accrual Measures and Financial Sustainability

My preceding comments do not in any way imply that standard accrual measures are inadequate for assessing the financial sustainability of government. Indeed, the focus of standard accrual measures on current transactions, while a drawback for assessing economic impact, is an advantage for assessing financial sustainability.

This is evident when considering the features of the two most common accrual measures: the operating balance and change in net assets.

The **operating balance,** defined as revenues less expenses, provides a measure of government saving. A valuable feature of the operating balance measure is that all costs involved in providing government services are included, such as depreciation and employee superannuation, not just cash costs. Hence if revenues are set to match expenses, then the government will be able to maintain the current level of services over time. In contrast, cash measures do not encompass all transactions, so that accruing superannuation and depreciation expenses may create the need for future fiscal adjustments even when the budget is in balance on a cash basis.

The operating balance is a useful measure of fiscal sustainability because it directly addresses the ability of governments to sustain existing services.

Another aggregate accrual measure is the **change in net assets**, which is equal to the operating balance plus any revaluation of assets and liabilities. The inclusion of balance sheet revaluations can provide additional information in assessing the sustainability of the government's position. In particular, if the government's assets rise in value then this improves the government's financial position by increasing the asset base on which the government can draw.

However, it should be kept in mind that the factors affecting asset valuations are generally outside government control and that increasing asset values could potentially obscure otherwise unsustainable government policies. Therefore, while this measure is useful it should always be considered in the context of the operating balance.

It should also be recognised that it is difficult to value many government assets as they are not normally traded. This can affect the interpretation of changes in the value of government assets.

Asset and liability revaluations may also create a degree of volatility in the change in net assets measure without necessarily changing the ability of governments to pursue their objectives. Further, increasing values for depreciable assets will have the second round effect of increasing expenses in the future as the cost of replacing those assets will have risen.

STOCK MEASURES

So far I have focused on the flow measures within the cash and accrual frameworks. However, a range of stock measures is also available for assessing the government's fiscal performance. These measures are primarily used to assess the sustainability of the government's fiscal stance rather than for assessing the economic consequences of policy.

Under the current framework, net debt is the primary stock measure. Net debt is defined as the difference between selected financial liabilities and assets and shows the cumulative amount of net borrowing that the government has undertaken over time to finance its expenditure. High levels of net debt impose a call on future revenue to finance interest payments and reduce the flexibility governments have to adjust outlays. Therefore, high debt levels typically raise questions about the sustainability of a government's financial position.

The accrual net asset measure extends net debt to report on the total net asset position, by bringing physical assets into account as well as additional financial assets (such as equity) and liabilities. The key advantage of the net asset measure is that it recognises the value of capital assets which may be financed by borrowing.

This is an important distinction, since it is widely accepted that borrowing to finance capital assets can be readily justified as these assets provide a flow of services over time that can offset the stream of borrowing expenses. In contrast borrowing for sustained periods to finance current spending will lead to an accumulation of liabilities with no offsetting assets.

The inclusion of non-financial assets allows a more complete assessment of the strength of the government's fiscal position. However, as noted earlier, it is difficult to value some government assets and not all will necessarily be saleable (for example, it is impractical to sell most city roads). It is important therefore not to presume reported government assets can readily be sold in order to repay debts.

APPLYING ACCRUAL MEASURES TO GOVERNMENT

The foregoing covers the main issues that need to be considered in selecting aggregate fiscal measures. My following comments highlight the need for users to ensure they fully understand the available measures and their relevance to government.

Objectives

It is important to recognise that just because the Government is to adopt the accrual framework currently used by business the resultant measures cannot necessarily be interpreted in the same way as for businesses.

First, as I have outlined, governments have different objectives to business, such as managing economic conditions. For this reason a measure that approximates national accounts net lending needs to be applied. This is not a criticism of standard accrual measures, rather a recognition of the need to assess the relevance to government of measures designed for business.

Second, governments have unique powers, such as the capacity to tax, that business do not possess. Thus whereas a business with a negative net asset position is unlikely to be able to raise additional funds for investment and would be regarded as insolvent, for government this is not the case. Governments may be able to sustain a negative net asset position for a considerable period of time, and indeed this may be an appropriate course of action, because of its capacity to raise taxes in the future. This capacity to tax suggests that standard accrual measures do not fully measure the financial strength of governments since the capacity to raise revenue through taxes is not included.

Coverage

Another reason why caution should be exercised in interpreting accrual measures relates to their scope and coverage.

As with all measures, the accrual framework generates some grey areas in terms of classifying transactions. Sophisticated users of statistics need to be aware of these issues and take them into account in interpreting the measures. This is no different to the adjustments we discussed earlier in deriving the underlying deficit to better measure the economic impact of fiscal policy.

An example is the respective treatment of employee superannuation and pensions. As we have discussed, under the accrual framework superannuation expenses are recorded as they accrue. However, pension entitlements are not considered to accrue over time but rather become payable when the eligibility criteria are met. Therefore, accrual measures will not include any information on future pension outlays. There is a sound justification for this treatment; however, it cannot be denied that governments have implicit commitments to pay pensions in the future. Moreover, taxpayers will be interested in information on the likelihood of these commitments being met: a question standard accrual measures cannot answer. The lesson here is that users must be aware of what transactions are included in the accrual measures before drawing conclusions.

CONCLUSION

In concluding, there are three main issues I wish to highlight. First, in determining which accrual measures are most relevant to government it is important to consider the economic focus that is unique to government. This focus is central to the operations of government — as embodied in the Government's medium-term fiscal objective.

Second, accrual measures can provide a good indication of both the economic impact and the sustainability of fiscal policy.

- As discussed, the standard accrual measures — operating balance, change in net assets and net assets — can assist in assessing the sustainability of fiscal policy. In addition, the national accounts net lending measure is particularly suited to assessing economic impact.

Finally, the adoption of accrual budgeting will introduce a suite of new fiscal measures and we need to understand the features of these measures and to take particular care to ensure the different features of government compared to business are taken into account when interpreting the results.

Liberalisation of Foreign Investment in the Australian Financial Sector

The following article is an edited version of a paper presented at the 26th Conference of Economists by Adam Boyton, International Structural Issues Section, International and Investment Division, Treasury.

EXECUTIVE SUMMARY

This paper provides a case study of Australia's experiences with the liberalisation of foreign investment as part of broader deregulation of the financial sector.

The paper finds that the liberalisation of Australia's foreign investment regime was an important driving force in providing a competitive stimulus to the financial sector, enhancing technical, allocative and dynamic efficiency.

There were also some transitional problems as participants in the financial sector learnt to adapt to the new deregulated and competitive environment. In particular, a sharp rise in non-performing loans and write-downs during the recession of the early 1990s, which were related in part to deregulation, resulted in some exits from the sector and the re-capitalisation of other institutions — although the overall stability of the financial sector was not called into question.

Overall, the benefits of foreign investment continue to be recognised by the Australian Government. Indeed, the Government recently announced it would further relax its foreign investment policy to consider a foreign takeover of one of the four major banks.

HISTORICAL REGULATION OF FOREIGN INVESTMENT IN THE FINANCIAL SECTOR

Between 1945 and the early 1980s new foreign banking businesses and foreign takeovers of existing banks were not permitted. Three foreign banking groups operating in Australia prior to 1945, owned by the Governments of China, New Zealand and France, were permitted to continue — although the Bank of China, which had established a branch operation in Sydney in 1942, ceased operations in 1972. These banks had limited branch representation and a relatively small share of Australian banking business.

Other foreign banks, while excluded from a formal banking presence, nonetheless participated in the Australian financial sector in various ways, including through correspondent relationships with Australian banks and through local representative offices, which facilitated activities such as their offshore lending to Australian borrowers. They also provided letters of credit to support borrowings on Australian money markets and had interests in Australian merchant banks[9] and other non-bank financial institutions (NBFIs) (Committee of Inquiry into the Australian Financial System 1981 and Edey and Gray 1996).

NBFIs were not subject to the same level of regulation as banks. Prior to the 1970s, there were no general restrictions on foreign investment in these institutions.[10]

In particular, foreign investors were able to invest in finance companies, which provided consumer credit for the purchase of household goods and motor vehicles, and finance to the business sector through leasing and commercial loans (although the finance company sector had become dominated by subsidiaries of the major banks).

In 1975 the *Foreign Takeovers Act 1975* was passed. The Act, and the broader provisions of policy, provided for approval of proposals by foreign investors for

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9 Merchant banks are unlicensed and may not call themselves banks. They may accept, but not solicit, deposits directly from the household sector, nor may they issue cheques. However, apart from their money market activities, they undertake a wide range of corporate finance and corporate lending activities. Merchant banks were not subject to the restrictions on interest rates which formerly applied to banks, nor to other banking regulations (including prudential regulations) and hence had a competitive advantage over banks in some areas.

10 However, in 1968 the Government prevented a foreign takeover of one of Australia's largest life insurance offices.

investment in the Australian economy, including for the establishment of new NBFIs, or acquisitions of existing ones, where substantial net economic benefits to Australia were demonstrated; or, if the net economic benefits were small, where there was an effective partnership in ownership and control between Australian interests and the foreign investor.

GENERAL FINANCIAL SECTOR REGULATION

Banks, in particular, were subject to a high degree of regulation, stemming from a desire on the part of authorities to use the banking sector as the conduit for monetary policy. By influencing the volume of bank lending, authorities sought to affect overall financial activity. To this end direct controls were applied, the most significant being controls on the interest rates banks could offer on their deposits and charge on their loans; limits on the maturity of term deposits; requirements that they hold a certain percentage of their assets in government securities; quantitative and qualitative lending restrictions; and requirements to hold special reserves on deposit with the central bank (Harper 1991).

NBFIs were less regulated than banks and operated with a higher degree of flexibility, enabling them to steadily increase market share as a result of the regulatory advantages they enjoyed. Building societies, in particular, benefited from the provision that savings banks hold more assets in the form of government securities than housing advances (Grenville 1991). Finance companies also grew in importance, satisfying the demand for the hire purchase of household durables. In an effort to share in this growth, by the 1960s, each of the major trading banks had acquired an interest in a specialist finance company (Financial System Inquiry 1997).

DEREGULATION OF THE FINANCIAL SECTOR AND THE LIBERALISATION OF FOREIGN INVESTMENT

In the early 1980s, inquiries into the Australian financial system recommended deregulatory measures to promote competition between existing banks and increase the efficiency of the financial system.

The Campbell Committee (1981)[11] doubted that the level of competition in banking was adequate to ensure maximum efficiency and maximum benefits for all consumers of banking services. It considered that Australian banks conducted relatively high cost operations (by international standards) and that some of those costs had emanated from the complex set of financial system controls.

11 The Committee of Inquiry into the Australian Financial System (the Campbell Committee) was established by the Government on 18 January 1979. Its final report, *Australian Financial System Inquiry Final Report* was received by the Government on 29 September 1981. The Campbell Committee also produced an interim report in 1980.

To help promote increased competition in the financial sector, the Campbell Committee recommended a liberalisation of foreign investment policy in the financial sector, arguing that domestic institutions would be unable to provide as much competitive stimulus in the short term as the introduction of foreign banks. The Committee noted that:

- the number of licensed banks was small and declining;
- domestic institutions had traditional management attitudes; and
- the size and cost advantages of existing banks represented barriers to entry.

In contrast, the Committee considered that foreign banks could provide an effective competitive stimulus (particularly in the short term) as they:

- already had the resources and banking experience (especially in international trading and foreign exchange dealing) necessary to establish wide-ranging banking businesses in Australia;
- were often operating non-bank financial intermediaries in Australia, and thus, like many large non-bank financiers, faced lower economic barriers to entry than some other domestic entrants who were not currently in the financial sector;
- had internationally recognised standing as banks and should readily command the confidence of the Australian community; and
- were less likely to be deterred by risks and uncertainties, and possibly less than average profit levels, associated with early establishment years.

The Committee also felt that the entry of foreign banks would quicken the pace of integration between Australian and overseas capital markets; and that the introduction of foreign banks and the move toward a more competitive environment should present only minimal disruptions to banking operations, provided the rate of entry was carefully controlled. However, it considered that unrestricted entry of foreign banks could be disruptive as it might result in undue fragmentation of the financial system; over-aggressive competition; and a socially unacceptable loss of resident ownership and control.

The Martin Committee (1984)[12] broadly supported the proposals of the Campbell Committee regarding the entry of foreign banks. It considered that 'additional foreign participation in banking, albeit subject to specific limits, would be beneficial to the Australian community'.

The Government responded to these calls for increased liberalisation of foreign investment regime in the financial sector by inviting applications from domestic or foreign interests for a limited number of banking authorities in September 1984; and subsequently authorising fifteen foreign banks to commence operations in February 1985.

12 The new Government commissioned a report on the Australian financial system on 29 May 1983. This report was to have regard to the Committee of Inquiry into the Australian Financial System (the Campbell Committee), the Government's economic and social objectives and the need to improve the efficiency of the financial system. The Government received the report, *Report of the Australian Financial System Review Group* (the Martin Report) on 21 December 1983.

Foreign investment policy governing the financial sector has been further liberalised since 1985:

- in 1986, the Government announced that investment in non-bank financial intermediaries would be approved unless considered to be contrary to the national interest (Foreign Investment Review Board 1996);
- in 1992, the Government stated that it would permit the issue of new banking authorities to foreign owned banks to operate branches in Australia, subject to certain conditions. These conditions included some restrictions on the acceptance of retail deposits by foreign bank branches; that the Reserve Bank was satisfied the bank and its home supervisor were of sufficient standing; and that the bank agreed to comply with certain Reserve Bank prudential supervision arrangements. Limits on the number of new banks that could be established were also removed in the same year, as was the restriction precluding foreign banks from bidding for the smaller Australian banks (that is, with the exception of the four major domestic banks) (Foreign Investment Review Board 1996); and
- in April 1997, the Government announced, in its initial response to the Final Report of the Financial System Inquiry (1997),[13] that it had decided to remove the blanket prohibition on a foreign takeover of the four major banks. Any proposed foreign takeovers or acquisitions would be assessed on a case by case basis on its merits in accordance with the Foreign Acquisitions and Takeovers Act. However, the Government also indicated that it would continue to apply the principle that any large scale transfer of Australian ownership of the financial system to foreign hands would be contrary to the national interest (Costello 1997a).

The Current Stance of Foreign Investment Policy

Australia has been an attractive destination for foreign investment reflecting, *inter alia:* a stable political environment; sound macroeconomic management; a well-qualified labour force; and a stable regulatory and policy framework.

> 'The Government's foreign investment policy is framed and administered with a view to encouraging foreign investment in Australia and ensuring that such investment is consistent with the needs of the community. The Government recognises the substantial contribution foreign investment makes to the development of Australia's industries and resources. Capital from other countries supplements domestic savings and provides scope

13 The Financial System Inquiry (the Wallis Inquiry) was established by the Government in 1996 to review developments in the Australian financial system since deregulation, to consider the factors likely to drive further change, and to make recommendations for possible further improvements to the regulatory arrangements. The Inquiry presented it final report to the Government on 18 March 1997. The Inquiry also released a discussion paper in November 1996.

> for higher rates of economic activity and employment. Foreign direct investment also provides access to new technology, management skills and overseas markets.' (Foreign Investment Review Board 1996).

Except for investment in specific sectors[14] the Government raises no objections to foreign investment proposals unless they are contrary to the national interest.

Foreign investment in the banking sector needs to be consistent with the *Banking Act 1959*, the *Banks (Shareholdings) Act 1972* and banking policy, including prudential requirements (Foreign Investment Review Board 1996). That is, foreign owned banks are subject to the same regulatory requirements as Australian owned institutions.

The Government permits the issue of new banking authorities to foreign owned banks, subject to prudential and competition considerations. These include that: the Reserve Bank is satisfied the bank and its home supervisor are of sufficient standing; the bank agrees to comply with the appropriate Reserve Bank prudential requirements; and the foreign bank expects to make a worthwhile contribution to banking services in Australia, and not merely add to the number of banks in the country.

Since 1986, foreign investment proposals relating to NBFIs have been approved unless considered contrary to the national interest.

Broader Financial Sector Deregulation

Along with liberalising foreign investment, broader deregulatory initiatives were also undertaken to improve the efficiency and competitiveness of the financial sector and to make Australian capital markets more internationally integrated and competitive.

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14 These specific sectors include real estate; civil aviation; shipping; the media (including broadcasting, newspapers and telecommunications) and banking.

THE EXTENT OF FOREIGN INVESTMENT IN THE FINANCIAL SECTOR

Following the liberalisation of Australia's foreign investment regime, the level of foreign investment in the financial sector has risen, as Table 1 shows.

Table 1: Level of Foreign Investment in the Financial Sector (end-June 1978 and end-June 1996)

Category of Institution	Total sector assets		Assets controlled by foreign owned institutions		Share of assets controlled by foreign owned institutions	
	$ billion		$ billion		per cent	
	1978	1996	1978	1996	1978	1996
Banks	44	483	3	70	7	15
Building Societies and Credit Unions	10	28	0	0	0	0
Merchant Banks	4	59	2	56	62	94
Authorised Dealers	2	4	0	4	22	100
Finance Companies	17	49	6	18	34	37
Other NBFIs	2	20	0	3	0	16
Life Companies	12	127	2	45	13	36
Non-Life Superannuation	9	154	0	42	0	27
Managers for Public Unit Trusts	-	55	-	23	-	42
General Insurance	6	58	2	18	33	31
Friendly Societies and Common Funds	-	13	-	0	-	0
Total Financial Sector Assets controlled by Foreign Institutions (per cent)					14	27

- data not available.

Sources: *Financial System Inquiry Final Report* (1997); *Australian Financial System Inquiry Interim Report* (1980) and Reserve Bank of Australia.

Foreign investment is greatest in the banking and merchant banking sectors, with substantial foreign investment also in life offices and non-life superannuation.

Merchant banking continues to have a high degree of foreign ownership of assets, reflecting, *inter alia*, a history of foreign control given the limited regulation of the merchant banking industry compared with the rest of the financial sector.

The share of banking assets under foreign control remains fairly low. This reflects the dominance of the 'big four majors' that, until recently, foreign investors have been precluded from acquiring. The 'big four majors' represented almost 80 per cent of banking sector assets at 30 June 1996. In addition, rationalisation among regional banks may have tended to limit the scope for significant levels of foreign investment in that part of the banking sector; although, in 1995 the Bank of Scotland purchased a 51 per cent stake in the Bank of Western Australia.

Table 2 shows the number of authorised foreign banks in Australia. It indicates that the 1985 and 1992 regulatory changes facilitated a significant expansion in the number of these institutions.

Table 2: Authorised Foreign Banks in Australia

	1984	1986	1988	1990	1992	1994	1996
Branches	2	3	3	3	3	8	17
Subsidaries	0	15	15	15	14	13	13
Total	2	18	18	18	17	21	30

Source: Reserve Bank of Australia.

THE PERFORMANCE OF THE FINANCIAL SECTOR SINCE DEREGULATION

Increased competition in the financial sector since deregulation, (including through the introduction of foreign institutions) has provided an impetus for domestic institutions to increase:

- technical efficiency (that is, outputs being produced at the lowest possible cost, using the minimum amount of inputs);
- allocative efficiency, or the extent to which prices reflect costs and funds are allocated to their best uses across the economy; and
- dynamic efficiency (representing the extent of innovation in the financial sector).

Technical Efficiency

There is evidence that the technical efficiency of the Australian financial sector has improved since deregulation, although international benchmarks suggest that there remains scope for further improvements.[15]

In addressing the question of improved efficiency in the financial sector since deregulation, the Financial System Inquiry (1996) noted that, notwithstanding the rise in financial assets as a share of Gross Domestic Product (GDP), the contribution of the financial sector to GDP has been declining (see Chart 1).

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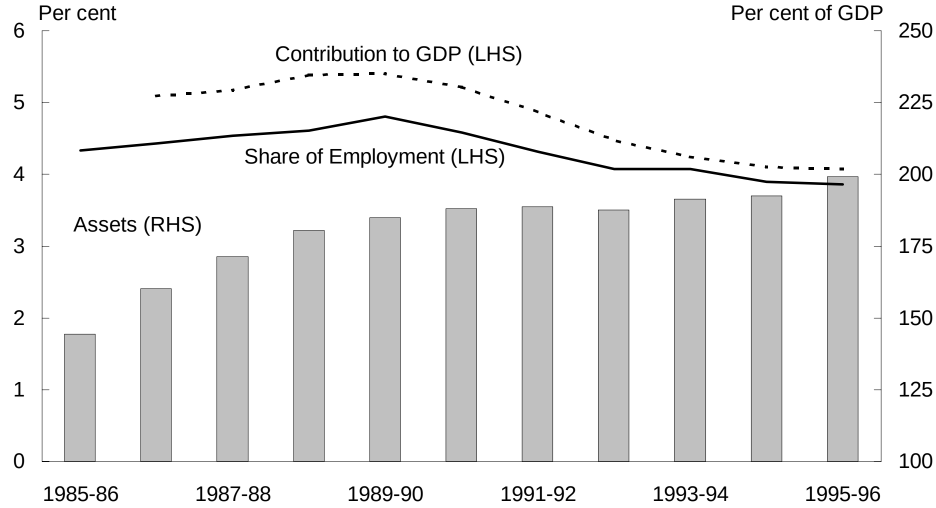
15 Data prepared for the Financial System Inquiry (1997) by the Reserve Bank covering the banking sector show that on international comparisons of price competitiveness, Australian interest margins are relatively high, while non-interest income is relatively low. In aggregate, overall banking sector revenue is at the 'high end of middle', while profitability is similar to comparable banks overseas. This conclusion does not; however, mean that the efficiency of the financial sector has not improved since deregulation, just that further improvements may still be possible.

Chart 1: Employment and the Contribution of the Financial Sector to GDP



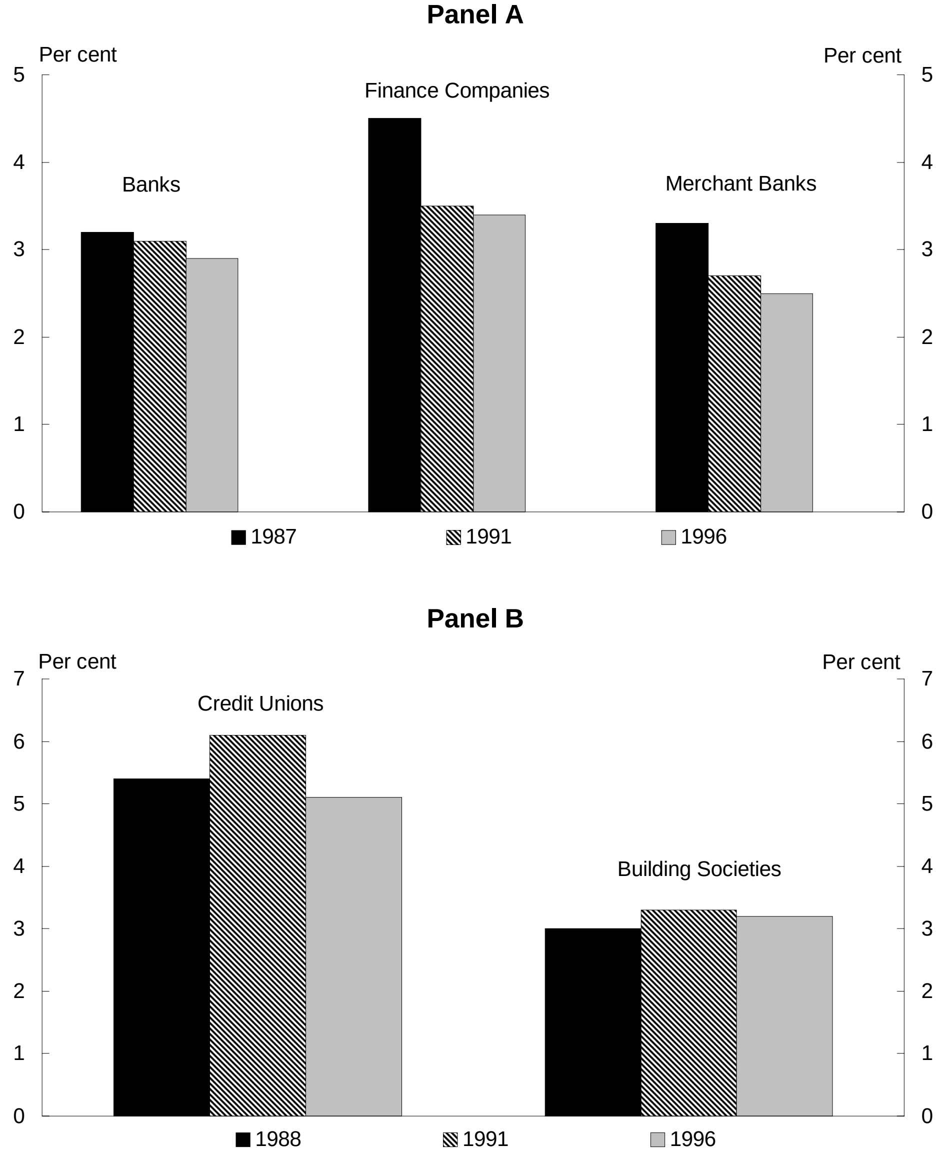
Sources: *Reserve Bank of Australia Bulletin*; ABS Cat. Nos. 5206.0 and 6248.0.

That is, the financial sector has been managing a greater amount of assets with fewer resources. The Inquiry found that these declining costs are primarily due to lower employment in the financial sector, driven by technological restructuring and enhanced efficiency.

Increased competition in the financial sector (including through the introduction of foreign banks) has provided an impetus for domestic institutions to become more technically efficient, by reducing their costs of production.

Data from the KPMG survey on financial institutions performance (see Chart 2), show that over the period 1987 to 1996, the ratio of operating expenses to assets has fallen for banks, finance companies and merchant banks. The ratio of operating expenses to assets for credit unions also fell over the period 1988 to 1996, while the ratio for building societies increased — although the exit of many of the larger, more efficient institutions to become banks may have distorted the survey results (Financial System Inquiry 1997).

Chart 2: Ratio of Operating Expenses to Assets



Source: KPMG (1997).

Allocative Efficiency

Allocative efficiency can be enhanced by costs to consumers (that is, fees and charges imposed by financial institutions) reflecting the underlying costs of providing services (for example, through reducing the extent of cross-subsidies). By more closely equating prices and marginal costs, resource allocation can be improved.

One of the expected outcomes of financial deregulation was that there would be a reduction in banks' internal cross-subsidies that allowed some customers to access goods and services for less than their marginal cost, while others subsidised that consumption. Since deregulation, it is fairly clear that pressure on banks to relate their fees and charges more closely to the true costs of providing services has increased (Harper 1991). The increasing prevalence of fees and charges on retail banking accounts has reduced the extent of cross-subsidisation (and hence an inefficient allocation of resources) — although there is still some way to go, as less than 15 per cent of the costs of providing retail transaction accounts is offset through the collection of fees and charges (Prices Surveillance Authority 1995). Outside the retail banking sector, the Financial System Inquiry (1997) found that stockbroking commissions and bid and ask spreads (that is, the difference between buying and selling prices, in effect, a dealer's commission) in the money market and foreign exchange markets have fallen.

There is also evidence of improved allocative efficiency in the life insurance industry due to:

- a reduction in the ability of the larger players to cross-subsidise across products by the entry of niche insurers into the most profitable product markets;
- price competition coming from other parts of the financial sector that offer competing investment products;
- increased disclosure of fees and commission; and
- the trend towards unbundling of the risk and investment components of life insurance products making the returns on the investment component more comparable and transparent (Department of the Treasury 1996).

However, overall reductions in cross-subsidies have been fairly limited, although their incidence has fallen in recent years as larger institutions respond to niche competitors (such as mortgage originators — specialist institutions that only offer mortgages, raising funds on wholesale markets rather than through deposit taking).

Dynamic Efficiency

Dynamic efficiency refers to the extent of innovation and the speed at which new developments are adopted by firms. While much of the evidence in this area is anecdotal, some of the product development and innovation in the financial sector since deregulation is highlighted in Table 3. There had been some degree of innovation prior to deregulation; however, the extent to which institutions, particularly banks, could innovate with respect to pricing, for example, was limited.

Table 3: Product Innovations since Deregulation

1980-85	1985-90	1990-96
Card-access savings accounts	EFTPOS	Mortgage originators
PIN for debit and credit cards	ATM network linkages	giroPost
ATMs became widely available	Telephone banking	Financial EDI
Variable repayment home loans	Cash management accounts	Mortgage offset accounts
Monthly income term deposits	Housing bonds	Smart card trials
First cash management trusts	Equity and fixed rate mortgage loans	Mobile lending
Compounding term deposits	Home/personal computer banking	Mobile EFTPOS (taxis)
Daily interest cheque account	Payroll system	Equity participation in SMEs
VISA and MasterCard	Increasing derivatives trading	International ATM linkages
Automatic sweep facilities		

Source: Financial System Inquiry (1997).

The impact of foreign banks in promoting product innovation and development has been significant in a number of areas.

In retail banking, examples include the payment of interest on current accounts and improvements to credit card facilities by the foreign banking sector which were quickly taken up by Australian banks (Edey and Gray 1996). Foreign banks were often leaders in introducing electronic banking, providing more flexibility in business accounts and introducing revolving lines of credit secured against mortgages.

The main impact of foreign banks has been in the wholesale market, including merchant banking activities. In aggregate, the relative contributions of foreign banks to the foreign exchange market, the derivatives market and funds management are much greater than their share of assets (Fraser 1994). Foreign banks account for just over half the turnover in Australian foreign exchange markets and in the markets for interest rate derivatives. Foreign banks are also market leaders in various financial markets — they have pioneered new products (for example, binary options) and are the only significant suppliers of some specific financial services (for example, spot foreign exchange markets for currencies such as the Malaysian Ringgit and the Thai Baht).

Foreign bank entry has also resulted in improved access to international capital markets (Fraser 1994). The local operations of foreign banks have stimulated and facilitated the provision of funds from associated financial institutions overseas to companies and governments in Australia. Moreover, having important global financial institutions operating in Australia makes it easier for Australian companies and governments to issue securities on international capital markets and to use swaps.

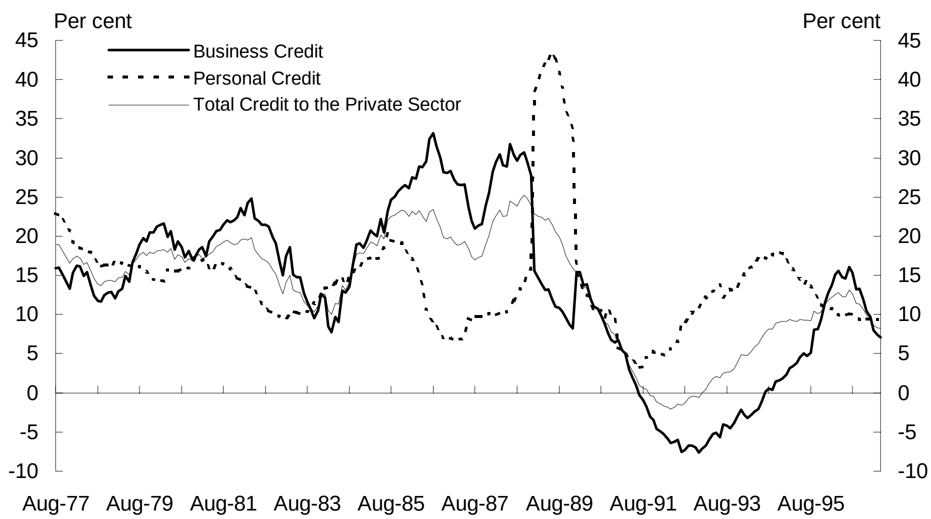
PRUDENTIAL ISSUES

While the Australian financial sector has a good track record for stability and reliability, deregulation of the financial system was associated with transitional problems that developed as financial intermediaries, consumers and businesses learned to operate in the new environment.

Growth in Credit

Although it had been hoped that deregulation would increase the availability of credit and enable banks to take on more risk, the very strong growth in credit extended to the business sector that followed deregulation (see Chart 3) was unexpected (Macfarlane 1991).

Chart 3: Growth in Credit Extended to the Private Sector by Financial Intermediaries



Source: *Reserve Bank of Australia Bulletin.*

Underlying this rapid expansion in credit were a number of demand and supply side factors.

Supply Side Factors

On the supply side, the resources available in the financial sector increased significantly over the period 1983 to 1988, with the amount of capital in the sector rising from $4.5 billion in 1983 to $20 billion in 1988. Over the same period, the number of banking groups operating in Australia rose from 15 to 34, while the number of merchant banks increased from 48 to 111 (Macfarlane 1991).

The introduction of new institutions (including foreign banks) and the significant increase in financial sector resources explains some of the rapid growth in credit over the 1980s. It could also raise the question of whether too many new banking licences were issued.

Demand Side Factors

In Australia, along with much of the rest of the world, the level of corporate gearing increased significantly over the 1980s (Table 4). Underlying this trend in Australia was a rise in the number of highly leveraged corporate takeovers over 1984–87, while credit growth post 1987 was driven, *inter alia*, by the property boom. Contrary to popular perceptions, the increase in gearing was not just confined to more aggressive entrepreneurial companies, but was widespread (Macfarlane 1991).

Table 4: Credit by Sector (per cent of GDP)

		Business	Housing	Personal	Total
Australia	1980	26	18	10	54
	1990	58	20	12	90
United States	1980	52	40	14	106
	1990	64	54	15	133
United Kingdom	1980	18	20	3	40
	1990	42	48	8	97

Source: Stevens (1991) cited in Macfarlane (1991).

Declining Credit Standards

The combination of demand and supply side factors contributed to a general decline in credit standards. Other factors behind the decline in credit standards included inadequate risk assessment and monitoring of borrowers' financial situations (Reserve Bank of Australia 1990). Some of these deficiencies could be traced back to the former quantitative credit restrictions, under which banks did not have to judge credit risk to the same extent as they did under the new regime (in the regulated environment where the amount of credit they could extend was fixed, banks only lent to their safest customers).

As interest rates rose over the late 1980s, the fall in credit standards began to manifest itself in significantly higher levels of non-performing loans and write-downs, resulting in the re-capitalisation or takeover of some State based banks, and the closure of some NBFIs.

- The State Bank of Victoria was acquired by the Commonwealth Bank in 1991 following significant losses by its merchant banking subsidiary; while the Government of South Australia had to provide its State Bank with a substantial equity injection.

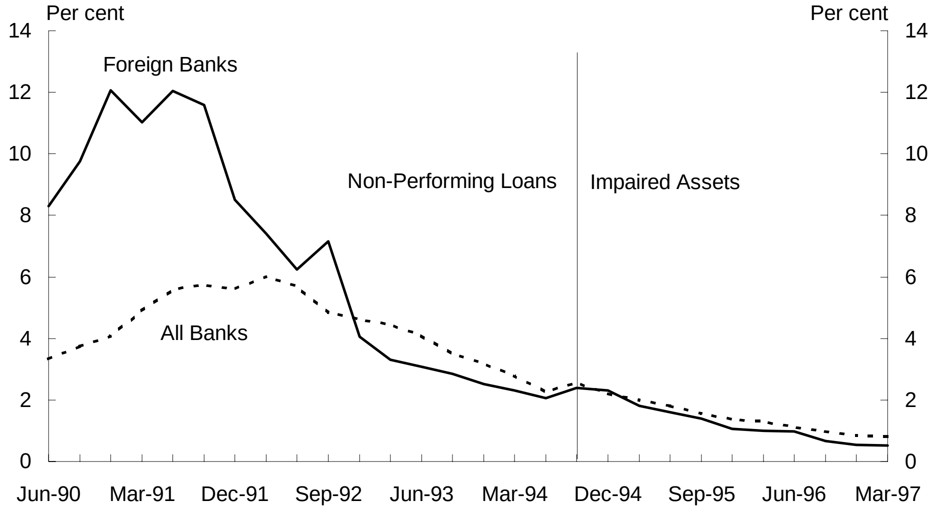
- Among the NBFIs, a Victorian based building society (Pyramid), a friendly society (OST) and a fund manager (Estate Mortgage) either collapsed or went into liquidation.

Losses flowing from non-performing loans and write-downs were not just restricted to State banks and NBFIs. As Chart 4 shows, foreign banks, along with domestic banks, were also carrying a significant level of non-performing loans during the recession of the early 1990s. The share of non-performing loans to total assets reached 12 per cent for the foreign bank sector in 1990-91, three times the average for the system as a whole (Fraser 1994).

The higher proportion of non-performing loans in the foreign bank sector, notwithstanding the experience of their parent institutions, suggests that the actions of the domestic banks in protecting market share might have contributed to foreign banks taking on riskier business. The domestic banks began reacting to the possibility of competition from foreign banks well before deregulation and foreign investment liberalisation, through mergers and acquisitions in the early 1980s. Domestic banks also sought to protect their position by competing vigorously for market share (Grenville 1991 and Fraser 1994). However, with the benefit of hindsight, this may have been an over-reaction. The significant advantage of large customer franchises and extensive branch networks enabled the domestic banks to maintain their retail businesses following the entry of foreign banks (Edey and Gray 1996), resulting in the new institutions competing almost exclusively in the business lending and wholesale sectors.

The nature of the supply side factors might also raise issues relating to how foreign investment liberalisation and financial sector deregulation were managed. It could be argued that staging or limiting the introduction of foreign banks might have proved more effective, through both limiting the resources available to the financial sector and reducing the extent of domestic banks' reaction to the competition posed by foreign institutions.

Chart 4: Non-Performing Loans/Impaired Assets as a Percentage of Total Assets



Source: Reserve Bank of Australia.

Nevertheless, the problems of the early 1990s did not threaten the broader stability of the financial system. They did, however, serve to reinforce the need for appropriate prudential standards and the importance of vigilance on the part of regulators and institutions themselves. Recent years have seen a return to more sustainable levels of credit growth and a significant decline in the extent of impaired assets.

OBSERVATIONS

While the introduction of foreign banks and the liberalisation of foreign investment policy has, on balance, been a positive experience, some transitional issues did arise.

The removal of quantitative restrictions on the provision of credit by banks, coupled with the fact that foreign banks tended to concentrate on business lending, did lead to lax credit standards in the provision of business credit.

The effects of this became fully apparent in the recession of the early 1990s as write-downs flowing from lax credit standards during the 1980s increased significantly, requiring the re-capitalisation of some institutions and the exit of others. Nonetheless, the overall stability of the financial system was not threatened — although the experience did serve to reinforce the objectives underpinning the changes in prudential standards implemented in the late 1980s. The appropriate prudential regime for the financial sector has also been an important element of the recent Wallis Inquiry.

There is little doubt that the entry of foreign banks provided a spur to competition. The threat of competition was sufficient to stir the domestic banks to considerable activity (in particular, mergers and acquisitions in the early 1980s), even before the foreign banks arrived (Grenville 1991 and Fraser 1994). However, the important advantage of large customer franchises and extensive branch networks enabled the major Australian banks to maintain their retail businesses against foreign banks (Edey and Gray 1996).

While the outcomes might not have been exactly what was predicted, this is not the benchmark by which the policy changes should be measured. Rather, the focus should be on how the system has developed and how it compares to that that existed in the pre-deregulation period. Given that focus, the evidence suggests that the Australian financial sector has become more efficient, more dynamic and more internationally integrated.

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Treasury Submission to the Inquiry into the Treatment of Census Forms

On 7 May 1997 the Treasurer, the Hon. Peter Costello, M.P., referred for consideration by the House of Representatives Standing Committee on Legal and Constitutional Affairs the current practice of destroying name-identified forms collected in population censuses. The Treasury's submission to the Committee sketches some of the uses made of census data by the Treasury and other major users, and notes the importance of maintaining the integrity of information collected in the census.

INTRODUCTION

This submission has been prepared in response to the Inquiry by the House of Representatives Standing Committee on Legal and Constitutional Affairs into the Treatment of Census Forms. Its main purposes are:

- to note the importance of the Census of Population and Housing to the provision of the statistical information central to monitoring and understanding trends in the Australian economy and society, and to a wide range of public and private decision-making;
- to indicate the range of data used by the Treasury which are dependent on information derived from the census, and the uses to which the data are put; and
- to state the importance of maintaining the quality of data obtained from censuses.

SOME USES OF DATA FROM THE CENSUS

The census is fundamental to the Australian social statistics system in providing socio-economic and demographic data which are important for the development and implementation of a range of policies at all levels of government, and for business planning and investment decisions. The census questionnaire is compiled after consultation with major users of statistics, community groups and the public at large, and with a view to its relationship to other statistical series compiled by the Australian Bureau of Statistics (ABS). Because the census covers the Australian population as a whole it avoids sampling error, and for many purposes it provides more reliable information than that derived from sample surveys. Also, obtaining data from the census may be the only practicable means of providing reliable information in respect of matters affecting only a small proportion of the population, or in cases where 'small area data' are needed for the country as a whole — for example, figures for each local government area, or smaller. Compilation of statistics for small areas and small population groups is thus a major function of the census, and as such statistics are relatively volatile, timely, high-quality data are particularly important for effective decision-making.

It is important also to recognise that the accuracy of a wide range of intercensal household surveys conducted by the ABS on such matters as health, housing and crime, as well as basic economic information, depends on census data. For example, the design and allocation of the samples used by the ABS for household surveys is based on population data from the census, and the census also enables 'benchmarking' of surveys — such as the Labour Force Survey — which are conducted regularly on sample populations. The 'benchmarking' involves comparison of results of the survey sample with independent estimates of the whole population based on the census (adjusted for births, deaths and migration between the time of the census and the survey). Such comparisons help to ensure the reliability and comparability of the regular sample surveys. Accurate census data thus underpin the reliability of many other important statistical series compiled from sample population surveys.

The information collected in the census reflects needs of governments and other users. A major purpose is to establish the populations of the States, Territories and local government areas. Australia's population growth has been much faster than that of most developed countries, and it has had high rates of immigration and of internal (eg interstate) migration. One important reason for obtaining regular and accurate census information on population is the constitutional requirement that the number of members of the House of Representatives chosen in the several States be in proportion to the respective numbers of their people.

Other major uses of census data are related to the transfer of revenue from the Commonwealth to the States (and Territories), and to local government, in the context of the high degree of vertical fiscal imbalance between the various levels of government in Australia. For example, Financial Assistance Grants (which account for the bulk of general revenue assistance from the Commonwealth to the States) for 1997-98 will amount to around $16 billion, and their allocation among the States is based on the States' populations and their per capita relativities, as assessed by the Commonwealth Grants Commission for the purpose of promoting horizontal fiscal equalisation. Census data are necessary for accurately determining the populations of the States, as well as for examining demographic, geographic and economic factors which enter into the determination of their per capita relativities. The Treasury portfolio is responsible for making general purpose payments to the States and Territories flowing from decisions of the annual Premiers' Conference and Grants Commission Relativities. Specific purpose payments to the States and local government are also very substantial, and census data are important for determining their allocation in such important fields as education and hospitals.

More generally, census data underpin a range of significant decisions by different levels of government and by the private sector. Census data can be used to establish the needs of the community and enable services and any necessary infrastructure or other investment to be targeted appropriately. A few examples are:

- by enabling cross-matching of factors such as age, income, ethnicity, type and ownership of housing and residential location, the census data help to identify social and economic trends and problems, and where to target action to address community needs: for example, the census yields data on internal migration patterns which assist planning for aged care services;
- the emphasis on questions relating to housing reflects the census's importance in the analysis of financial and other aspects of home-buying and renting in relation to specific categories of people;
- a particular application concerns services for minorities, such as Aboriginal and Torres Strait Islander people. The census provides information on where these people are, and on aspects of their housing, educational attainment, family size, income and labour force experience. Such information enables the estimation of current needs and the projection of future needs, and where service delivery should be concentrated. It thus facilitates the development and implementation of measures to improve the access of Aboriginal and Torres Strait Islander people to adequate housing, workforce training, education more generally and a wide range of other services (such as health care);
- similarly, the census facilitates measures to direct settlement assistance to migrants, the planning of multilingual information programmes, provision of interpreters and translation services, and other migrant welfare services;
- the census data assist analysis of urban planning issues involving transport and land use, through the information they provide on car ownership, modes and routes of journeys to work, and areas where residential or commercial/industrial demand for land is growing. This helps determine when and where land should be made available for

development and where extra transport capacity will be required, enabling forecasts of public transport patronage and planning of new transport routes. It also helps in planning parking facilities and provision of amenities and services for the working population near their places of work; and

- census data on education, occupation, labour market participation and place of work are vital for the analysis of a range of important labour market issues, including the demand and supply of skills; trends towards part-time work; estimating child care needs; providing the required level of labour market services, and matching them to specific areas; monitoring the employment experience of minorities. A particular application has been the analysis of the demographic and labour force characteristics of employees in industries and in locations facing structural change.

Census-related data are thus integral to the formulation of a broad range of government policy, the allocation of resources between different tiers of government, and the efficient implementation of government policy. Reliable census data are necessary to meet a range of community needs, including the promotion of equity objectives through the identification of special needs of particular groups in specific locations, which may require government policy measures, and to ensure the efficient use of the very substantial resources employed by all levels of government, and by the private sector, to meet those needs.

Census-related data are also important inputs to decision-making by businesses in the transport, land development and housing construction sectors, which have an obvious interest in the data indicating where there will be increased demand for their services. Equally, such data can assist businesses in locating close to potential customers — even to customers with particular characteristics, such as income or age — or to potential employees; moreover, businesses operating beyond the regional scale can be helped in gauging the potential national market for their products or services, and in projecting feasible rates of growth. Census-related data facilitate increased efficiency in a range of significant private sector investment decisions.

USE OF CENSUS-RELATED DATA BY THE TREASURY

Because of the Treasurer's broad responsibilities, including resource allocation and the formulation of the Commonwealth Budget, many of the above applications are of interest to Treasury. The following examples, however, relate to the use of census-related data in the areas for which Treasury has prime responsibility. The information used includes both data derived directly from the census, and data from ABS household surveys which use census data for construction of samples and for benchmarking.

Retirement Incomes

The census is a primary source of data in respect of the distributional analysis undertaken in relation to retirement incomes.

Models have been developed by the Retirement Income Modelling Task Force (RIM) — now part of the Financial Institutions Division of Treasury — to project the comparative adequacy, equity, costs and benefits of alternative retirement income policies. These policy impacts are modelled at the individual, couple and population level and include the effects of policy on taxation revenue, on social security outlays, on retirement income, on private saving and on national saving. Apart from the importance of these issues in terms of Commonwealth Government policy, the models' projections of superannuation are used by many private sector analysts.

The operation of RIM depends on detailed statistical information from ABS household surveys, including the income and housing survey, the Household Expenditure Survey (HES), the Labour Force Survey and its supplementary surveys (superannuation, retirement intentions, labour force experience). In this analysis, the most important applications of the census are the updating of the household survey sampling framework and the provision of information on persons in non-private dwellings.

- The reweighting, or dynamic ageing, of ABS data is undertaken to provide current estimates of various distributions. Parameters from the census — such as age, sex, family status, labour force status and location — are used in the reweighting of ABS sample survey datasets.
- ABS household surveys generally exclude persons in non-private dwellings (such as nursing homes and retirement villages). At any given point in time, a significant proportion of the aged are in such dwellings. Census information (non-private dwelling type cross-classified by age and sex) is the source used most frequently to reconcile estimates of these sample surveys with population estimates.

Taxation

Another use of ABS household survey data in the analysis of the effects of alternative revenue and expenditure measures is in relation to taxation. For example, using HES data, Treasury's Price, Revenue, Incidence, Simulation Model (PRISMOD) is able to estimate the impact on differing household types of changes in commodity prices (including through indirect tax changes), income tax and government transfer payments. Although valuable information on income and other variables is available to the Australian Taxation Office (ATO) from analysis of taxpayers' tax returns, the ATO information is organised in relation to the taxpaying unit — for individuals, the individual taxpayer — rather than to households (which may include more than one taxpayer).

Analysis of the effects on households gives a fuller picture of the impact of tax policy alternatives.

Macroeconomic Forecasts and Policy Advice

Accurate economic statistics are central to the conduct of macroeconomic policy. It is clearly important to measure accurately the economic variables which are of concern to the community, and which form the objectives of macroeconomic policy, including economic activity, inflation and unemployment. The successful conduct of policy also relies on a sound understanding of the relationships between many economic variables as these relationships form the basis of economic forecasts and assist in assessing the impact of changes in policy. While many factors affect these judgements, the task is made easier if the underlying economic statistics are sound.

Treasury therefore relies heavily on the accuracy of ABS statistics in formulating its advice on macroeconomic conditions and the conduct of macroeconomic policy. For example, projections and forecasts for economic variables such as inflation, economic activity and employment growth form a key input into calculating the budget forward estimates, and hence are of critical importance to the Department's advice to the Treasurer on fiscal policy. While the use of census data for macroeconomic analysis is generally indirect, there are many data sources important to Treasury that are linked to the census.

Economic Activity

The quarterly National Accounts data provide key information about current economic conditions, and are the foundation for forecasting developments in the year ahead. Important areas where the National Accounts figures depend on census data for benchmarking include:

- private consumption expenditure on rent — this accounts for almost 20 per cent of private consumption expenditure and 12 per cent of Gross Domestic Product (GDP);
- estimates of the value of total wages, salaries and supplements — this accounts for around 50 per cent of the income based measure of GDP (GDP(I)), which in turn has a weighting of a third in the ABS's recommended measure of GDP (GDP(A) — the average of the income, expenditure and production based GDP measures); and
- estimates of GDP per employee / head.

In addition, the estimates of government consumption expenditure (such as expenditure on the provision of education or health services) by State in the State Accounts make use of census population data.

Developments in the dwelling sector have a significant impact on total economic activity in Australia. Census data on factors that determine future levels of dwelling construction (including household formation, estimates of the housing stock, structure of dwellings) are inputs to the forecasting processes for this sector. Although a relatively small proportion of GDP, dwelling construction tends to be particularly volatile and can make a significant contribution to changes in GDP.

Labour Market

Reducing unemployment is a prime Government objective, and a principal aim of economic policy. The level of unemployment also has consequences for government expenditure, just as the level of employment has consequences for government revenue. Reliable data on levels of unemployment and employment, and other aspects of the labour market, are central to macroeconomic analysis, forward estimates of revenue and expenditure, and policy development in the Treasury portfolio, as well as to specific labour market policy issues in other relevant departments.

Census data provide benchmarks for the Labour Force Survey in a number of areas which are important for Treasury in monitoring, explaining and forecasting labour market developments. These include:

- gross flows data — that is, data on flows between various labour market categories — are integral to monitoring developments in the labour market;
- disaggregated data by industry and occupation which show the relative strength of employment in different industries, sectors and occupations; and
- statistics showing unemployment by educational attainment which provide an indication of the degree of mismatch of skills in the economy. The extent to which there is mismatch between the demand and supply of labour is important in analysing both macroeconomic conditions and structural factors.

Inflation

The Consumer Price Index (CPI) is an important measure of price change in the economy and is used directly to adjust a range of Commonwealth payments, including payments to the States and personal benefits. The CPI is also used to derive the underlying measure of inflation which is targeted by the Reserve Bank when setting monetary policy. The CPI is reweighted every five years to ensure that it continues to reflect household spending patterns and hence remains an accurate measure of price change. CPI weights are based on the HES. The next reweighting of the CPI will be for the March 1998 quarter, to be published in April 1998, based on the 1993-94 HES survey.

DATA QUALITY AND THE DESTRUCTION OF CENSUS FORMS

The issues to be considered by the Committee include the costs and benefits of changing from the current system of destroying census forms — so as to remove links between the information recorded on the forms for statistical purposes and the names and addresses of the individuals who provided the information — to retaining census forms. The benefits which we have seen claimed in respect of retention of the forms are of little direct relevance to Treasury's functions, and we do not propose to comment on them: we could add nothing to the discussion in the ABS's annual report for 1995-96.

There are at least three possible costs from retention of census forms:

- monetary costs of storage (or of microfilming and storage of the microfilms) and of subsequently providing access to researchers. The ABS (in its 1995-96 annual report) has quoted an estimate made in 1988 for storage costs, of between $2 million to $9.4 million, in 1988 prices;
- possible conflict with the objectives of policy relating to individual privacy;
- possible adverse public reaction to perceived privacy problems, leading to reduced cooperation with ABS and the consequences that may have for census and other statistical data.

The range of costs given for storage would in themselves put the onus on proponents of retention to substantiate claims as to the value of retention. The costs of storage are considerably less than the cost of planning and undertaking the census and processing and making available the results, but the cost of the census is amply justified by the manifold important applications of census data.

While consistency of policy on privacy matters is an important issue, it is not in itself an area on which Treasury has particular expertise. Treasury nevertheless notes that a survey carried out in 1996 on behalf of the ABS found that a high proportion of the community would have strong concerns about privacy if it were decided that census forms would be retained. Furthermore, a substantial proportion of interviewees indicated that perceived threats to privacy, and in particular, retention of census forms with names and addresses of respondents, would make them less likely to provide full and accurate information when participating in the census.

Treasury's main interest is in the possible impact that a decision to retain census forms may have on the quality of ABS statistics. The particular value of statistical information from the census derives in large measure from the completeness in its coverage, and even relatively small reductions in the level of cooperation could have a substantial adverse effect on the quality of the census data, which could not be fully remedied by post-evaluation surveys. Any reduction in cooperation would not be randomly distributed and could introduce significant bias in data derived from some census questions.

A high quality statistical database is necessary for efficient and effective decision-making by both the government and private sectors. Any reduction in the quality of census data would affect the sample basis for a range of other surveys, as well as detracting from the ability to check and adjust series based on samples through benchmarking against census data. The importance of census-related data to a wide range of government and private activities has been noted above. Another consideration is that if people's perceptions of the ABS are adversely affected in relation to the census, their level of cooperation in other surveys conducted by the ABS is also likely to decline.

As regards Treasury's functions, a reduction in the quality of census data and sample survey data used by Treasury could increase the difficulty of modelling and developing retirement income policies, assessing economic conditions and processes, and economic forecasting. This has the potential ultimately to reduce the effectiveness of a range of economic policies in achieving their objectives.

Because good decisions require good information, Treasury would be concerned by any reduction in cooperation by the public with the ABS in the conduct of the census, and would envisage that consideration of the impact of retention of census forms on public cooperation with the ABS would be central to the Committee's investigations and deliberations.

SUMMARY AND CONCLUSIONS

The objective of this submission has been to emphasise the role of the census in maintaining the integrity of data collected by the ABS. ABS data underpin decision-making by all levels of government and the private sector. Treasury is a heavy user of data for policy purposes.

Although we are not in a position to assess the extent to which retention of census forms would impair the integrity of ABS data, the risk of a material reduction of data quality appears to be a very real one.

Treasury Submission to the National Competition Council Review of the Australian Postal Corporation Act

The National Competition Council (NCC) is currently reviewing the remaining mail services reserved to Australia Post. The review forms part of the Commonwealth's legislation review commitments under the Competition Principles Agreement. An interim report was publicly released by the NCC in *early October 1997, with the final report scheduled to be presented to the Government in February 1998.*

The main objective of Treasury's submission to the NCC's review is to promote the case for increased competition in the postal services market, given its national significance and importance as an input to other businesses.

EXECUTIVE SUMMARY

The *Australian Postal Corporation Act 1989* (the APC Act) was amended in November 1994 to allow competition in a number of postal services which had previously been reserved to Australia Post. The corporation has subsequently recorded a very strong performance, measured in terms of productivity, revenue growth, profitability and dividend payments to Government.

This strong performance has been achieved against a backdrop of significant technological change whereby postal services are facing increasing competition from other communication modes and losing market share as a result. However, new technology can provide opportunities for Australia Post to improve its standards and speed of service in traditional areas of business, as well as open up new areas of business.

Section 27 of the APC Act embodies a set of social obligations concerning the provision of a comprehensive letter service to all people in Australia. An important feature of Section 27 is that Australia Post has the discretion to determine what is 'reasonable access' to and a 'reasonable standard' of postal service. Australia Post has exercised its discretion by varying the standard of its delivery services to different categories of consumers based on the cost of delivering a postal service.

A key issue for the current review is to examine the way Australia Post's universal service obligation (USO) is currently defined and costed and then assess whether it can be preserved in the face of competition, either through Australia Post competing effectively (including through improving efficiencies) or by some funding arrangement (eg a universal service fund) which 'insulates' the USO from competition.

Treasury recognises that Australia Post would be faced with the need to make a number of adjustments, possibly significant, to its operations in order to continue delivering a universal service at a uniform price in a completely deregulated postal market (or a market where the current level of reserved services is significantly reduced). However, the difficulties Australia Post is likely to face in such a market can be exaggerated and the threat of competition, potential or real, from other suppliers would place pressure on Australia Post to contain its costs and improve the quality of its service.

If the postal services market were to be deregulated, Australia Post would have a number of advantages over potential new entrants who are likely to face significant difficulties establishing competing mail networks. In addition, Australia Post appears to have built up strong customer loyalty and has an established 'brand name'. This would likely be an important competitive advantage in a deregulated postal services market.

Whilst Australia Post's customers appear to have benefited from the nominal price freeze on standard postage articles since January 1992, they may not have shared fully in Australia Post's achieved productivity gains to the extent that might have been possible if a more restrictive price capping arrangement had been in place over the period. To avoid a continuation of this situation, a reduction in prices for Australia Post's reserved services could be investigated. The imposition of a more restrictive price cap for the next three to five years could also be considered.

Finally, there are doubts as to whether Australia Post's existing interconnection arrangements for bulk pre-sorted mail have met the pro-competitive intent of the 1994 legislative amendments and there appears scope for the development of a more desegregated schedule of interconnection discounts for this type of mail.

INTRODUCTION

Australia's National Competition Policy Framework

Competition is a key driver of economic efficiency and innovation in the economy which ultimately delivers benefits to consumers through reductions in prices, increased levels of service quality and choice. Over recent years, Australia has developed a legislative framework which facilitates the competitive process while providing remedies for unacceptable market conduct, and which also allows desirable social policy objectives to be met.

The NCC's review of the APC Act forms part of the Commonwealth's commitment to review by the year 2000 its legislation that restricts competition or imposes costs on business. The guiding principle of the legislation review process is that legislation should not restrict competition or impose costs on business unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs and that the objectives of the legislation can only be achieved by restricting competition. The legislation review process, in turn, is a key element of the Commonwealth's broad commitments under the Competition Principles Agreement signed by all Australian Governments in April 1995.

Industry Commission's Mail, Courier and Parcel Services Report

The last major review of the Australian postal services market was undertaken by the Industry Commission (IC). In its October 1992 report, *Mail, Courier and Parcel Services*, the IC recommended, amongst other things, several options to increase competition in the delivery of postal services.

In November 1994, legislation was passed amending the APC Act to allow competition in a number of postal services which had previously been reserved to Australia Post (AP). The key changes were that:

- the price threshold for competition was reduced from ten times to four times the standard letter rate ($4.50 to $1.80), and the weight threshold for competition was reduced from 500 grams to 250 grams;
- the movement of letters within document exchange networks was exempted from AP's reserved services;
- the carriage of mail into and out of Australia was deregulated (but the delivery of international mail within Australia continued to be reserved to AP); and
- a framework for bulk mail interconnection to AP's network at designated mail centres was established.

NCC’s Review

The review of the APC Act by the NCC reflects the national significance of postal services. In broad terms, the NCC is to examine the need for a statutory protection to AP of the exclusive right to carry letters, and the implications of a reduction or removal of that reservation in the context of the Government’s commitment to the provision of a standard letter service to all Australians at a uniform price. In undertaking its review, the NCC is to have regard to the findings of the IC’s 1992 report, as well as the reform outcomes arising from the 1994 legislative amendments.

Australia Post’s Network

The largest part of AP’s postal service involves the transportation of physical mail (letters and parcels). The chief functions of its network are the collection, sorting, transportation and delivery of mail. The nodes of this service can be classified into: collection points (post boxes, post offices), sorting points (mail exchanges) and delivery points (private letter boxes). In that regard, **traditional mail is very much a transportation service rather than a communications service, although over time there has been increased bypass of transportation networks through the use of telecommunications networks** (see discussion of technological change below). The variable costs involved in physically transporting mail can be classified into six broad areas:

- costs of establishing and maintaining collection points;
- cost of transportation from collection points to mail exchanges;
- sorting costs;
- cost of transportation between mail exchanges;
- re-sorting costs; and
- cost of transportation to delivery points.

In addition, there are the fixed infrastructure costs of land and buildings for mail exchanges and post offices. A larger proportion of AP’s costs appear, however, to be variable rather than fixed. For example, AP’s largest cost is labour, reflecting the labour intensive nature of postal operations, accounting for around 60 per cent of its costs. This mix of variable and fixed costs raises the issue of whether there are economies of scale and scope in AP’s operations (economies of scale exist where average costs for each unit of output produced falls as output is increased, whilst economies of scope exist when one firm can provide a range of services more cheaply than a number of firms providing each service separately). This issue is closely related to that of whether the postal service is a natural monopoly (ie, a single firm can produce the entire industry output at a lower total production cost than two or more firms).

In its 1992 report, the IC found that economies of scale in collection, transportation between mail exchanges, sorting and delivery were already likely to be exhausted in Australian cities. This was reflected in the fact that other operators (eg couriers, mailing houses) were already performing some of these functions. In contrast, in rural areas, where mail volumes are smaller, the IC considered that it was likely to be more efficient for one firm to provide a letter service. According to the IC, economies of scope were likely to be greater where mail volumes were low.

Treasury concurs with the IC's views and notes that to the extent that economies of scale have been exhausted, there would be net benefits from introducing more competition into the Australian postal market. Nonetheless, a related key issue is the extent to which the standard letter service at a uniform price would be sustainable in the face of greater competition. This will depend on the extent to which AP's economies of scale and scope interact with the varying costs of different mail paths. This issue is discussed in the section 'Australia Post's Ability to Provide its USO in the Face of Increased Competition' below.

Over time, a number of technological changes have occurred which have influenced the nature of the postal service, as well as the breaking of traditional boundaries between different parts of the communications sector.

- **Sorting of mail has become more mechanised and centralised within larger mail exchanges, rather than manually within individual post offices. In that regard, the mail transportation service has become increasingly separable from the post office 'shop front'.**
- **Bulk mailers have also incorporated technology to pre-sort mail, allowing them the option of avoiding the first three of the six broad costs identified above.**
- **Telecommunications has enabled mail prepared in one central facility to be electronically transmitted to a point near the final destination, where letters are printed, enveloped and sorted before delivery to a mail exchange near the end point. While not avoiding the cost of transportation to the delivery point, this avoids most of the other costs.**

Moreover, electronic mail and fax can be used to bypass the whole postal network, provided the receiver has access to the required telecommunications facilities. As this type of bypass becomes more common, the role of the standard letter service will become less significant. Future movements in the relative price of letters to telephone calls could be an important determinant of the speed of this trend.

It is apparent then, that the rapid pace of technological change in the communications sector provides a double edged sword for AP. On the one hand, postal services are facing increasing competition from other communication modes such as fax and electronic mail, and losing market share as a result (although it should be noted that mail volumes are growing at around 4 per cent a year, which AP expects to be maintained into the next decade). On the other hand, new technology can provide opportunities for AP in terms of improving its standard and speed of service in traditional areas of business, as well as expanding into non-traditional areas of business. For example, AP already provides an electronic-to-physical mail service (EDIPost) which has exhibited recent strong growth in volumes.

Australia Post's Recent Performance

The reform of Commonwealth government business enterprises (GBEs) in the late 1980s produced significant gains, in terms of lower costs and better service, to business and the wider community. AP's performance showed marked improvement following its corporatisation in 1989. There are, however, limitations to the degree of efficiency improvement which can arise from GBE reform alone.

Experience in the telecommunications sector has demonstrated that competition is the ultimate engine for efficiency improvement. Fostering more competitive markets and seeking efficiency gains in infrastructure industries such as telecommunications and postal services is particularly important given that they represent a basic cost to business that influences the ability of business to compete in international and domestic markets.

Since its exposure to greater competition as a result of the 1994 legislative amendments, AP has recorded a very strong performance, measured in terms of productivity growth, revenue growth, profitability and dividend payments to Government, notwithstanding a freeze on the standard letter price (of 45 cents) since January 1992. (The freeze has been extended until June 1998.) The standard letter is the most significant product in AP's reserved services, the reserved services accounting for around 56 per cent of total revenues. Moreover, AP has recorded strong growth in its non-reserved services over this period — that is, those services which, in principle, are open to competition. The turnaround in AP's performance since the late 1980s is such that it is now regarded amongst the best performing postal operators internationally.

Notwithstanding AP's high international standing and its recent good performance, it is arguable that there remains scope for AP to improve the efficiency of its postal operations. The experience of the 1994 legislative amendments indicates that a further reduction in the level of reserved protection is likely to be the best means of facilitating this efficiency improvement.

Funding the Delivery of the Postal Universal Service Obligation

This strong financial performance over recent years raises the issue of the funding of AP's universal / community service obligations (USO / CSOs). AP has traditionally emphasised the link between its USO / CSO obligations — broadly, the provision of a reasonably accessible universal letter service at a uniform price — and its reserved services. In other words, AP has suggested that should the reserved services protection be reduced or removed completely, then 'cream skimming' would arise on its most profitable routes. As a consequence, its revenues, profits and employment would all fall and ultimately AP would be unable to meet its USO / CSO obligations. A recent report by the House of Representatives Standing Committee on Communications, Transport and Microeconomic Reform, *Keeping Rural Australia Posted*, which focussed on AP's CSOs, recommended, amongst other things, that the CSOs of AP should continue to be funded through cross-subsidies. Nonetheless, the Committee considered that AP's reserved services could be reduced without disadvantaging rural and remote communities.

Recent Changes to Commonwealth GBE Accountability Framework

The Government has recently decided on a number of refinements to its GBE governance arrangements aimed at strengthening the existing accountability framework. These include differentiating between CSOs and USOs and the funding of these respective obligations. A full discussion of the implications of the Government's decision for AP is in the section 'What are Australia Post's USO / CSOs?' below.

Future Reform of Postal Services

In light of AP's performance since the 1994 legislative amendments, and the range of developments outlined above which will be impacting on the Australian postal services market in the future, the current review of AP is timely. **Treasury considers that the threshold issue for future reform of the postal services market is the extent to which those services currently reserved to AP should be further opened up to competition and the extent to which any potential loss of revenue will impact on AP's ability to continue delivering a universal letter service.**

AP'S STATUTORY UNIVERSAL SERVICE OBLIGATION

Postal policy in Australia and internationally has traditionally been based on the premise that an unregulated postal market would not provide a universal letter service. Consequently, a universal service obligation is imposed on the (typically) public postal operator which is given monopoly protection to enable it to generate sufficient revenues to cover the costs of supplying the universal service. The most significant policy issue in this case becomes the determination of the scope of the monopoly (ie, the range of postal services 'reserved' to the monopolist) rather than whether there are alternatives to the monopoly provider model. Nonetheless, some countries (eg Sweden, Finland) have recently rejected this postal policy paradigm and completely deregulated their postal markets while maintaining USOs on their public postal operators.

Treasury sees strong merit in this alternative approach and considers that a key issue for the NCC review to examine is the way AP's USO is currently defined and costed and then assess whether it can be preserved in the face of competition, either through AP competing effectively (including through improving efficiencies) or by some funding arrangement (eg a universal service fund) which 'insulates' the USO from competition.

What are Australia Post's USO/CSOs?

Section 26 of the APC Act obliges AP to, as far as practicable, perform its functions in 'a manner consistent with sound commercial practice'. Within this broad framework, AP appears to perform a number of USO/CSOs, both of a statutory and non-statutory nature.

AP's key USO is specified in Section 27 of the APC Act and obliges AP to provide:

- reasonable access to a letter service regardless of location;
- a standard letter service at a uniform charge;
  - for letters that are 'standard postal articles' as defined in the APC Act;
- a reasonable standard of letter service; and
- a letter service between Australia and the world.

Section 27 essentially embodies a set of social obligations concerning the provision of a comprehensive letter service to all people in Australia; however, it is important to recognise that the actual USO is only that part of the letter service that AP would not provide if it were acting commercially. There is a potential principal/agent problem here in that the Government does not have access to full information concerning the nature of the alternative, strictly commercial, decisions that would otherwise be made by AP. Hence, a risk arises that the Government may be induced to fund some loss making activities that AP would have undertaken anyway, as it may not necessarily be in AP’s commercial interest to discontinue all loss making services.

In a recent decision concerning its GBE governance arrangements, the Government drew a distinction between a USO and a CSO. The Government determined that a CSO arises when a Commonwealth GBE is required to carry out specified activities which:

- the GBE would not elect to do on a commercial basis (or which it would only do commercially at higher prices); and
- the Government does not, or would not, require other organisations in the public or private sectors to undertake or fund.

In addition, the Government decided that, in-principle, all CSOs would be budget funded.

In contrast, a USO exists where the first condition above holds, but not the second; that is, the Government does, or would, require other organisations in the public or private sectors to undertake or fund the specified activities. The funding of USOs will depend on a range of factors including the nature of the service, the existing and future delivery alternatives and budget considerations. For example, with respect to telecommunications, the Government has decided to impose a USO obligation on the industry as a whole by means of a universal levy. A similar issue could arise if AP’s existing reserved services were to be significantly opened up to competition.

More generally, there is a need to clarify exactly the activities that AP is currently engaged in that are considered to be CSOs (ie, not part of the delivery of the universal letter service) and decide whether the provision of these CSOs should continue by means of budget funding.

Finally, **it is also apparent that with the exception of the requirement that it provide a standard letter service at a ‘uniform charge’, the obligations on AP with respect to the letter service are not tightly defined and so there is a degree of discretion, tempered by public expectations, available to AP on the delivery of the USO. In practice, the use of this discretion has been reflected in consumers facing different quality of service standards depending on the cost of providing that service.**

Australia Post’s Discretion in USO Delivery

With respect to AP’s statutory USO, an important feature of Section 27 is that AP has the discretion to determine what is ‘reasonable access’ to a service and a ‘reasonable standard’ of service. AP has exercised its discretion by varying the standard of its delivery services to different categories of consumers based on the cost of delivering a postal service (using its ‘urban base rate’ formula).

Hence, AP provides five street mail deliveries a week to residences and business addresses where all of the costs of the delivery can be met from the revenues generated by the delivery, and provided the mail receptacle is reasonably accessible from the footpath of a public road. Where delivery costs are much higher than the average costs of delivery, AP reduces the frequency of delivery progressively, with small decreases in frequency being made in response to large increases in cost, and with some locations not receiving any mail deliveries. Delivery services in rural areas are also contracted out to local transport operators.

Similarly, AP aims to locate street post boxes and other lodgement facilities in places where customer demand is sufficient to warrant the cost of establishing, clearing and maintaining such facilities. Street post boxes are sometimes installed in locations which would not be justified on commercial criteria, for example, to meet the needs of the aged or disabled near hospitals or nursing homes. However, while AP maintains street post boxes for uneconomic reasons, it generally only does this while they achieve a minimum lodgement of 25 articles per day.

Because they relate to the delivery of mail along mail paths, these measures also have a direct effect on the cost of meeting the non-discretionary commitment to ‘a standard letter service at a uniform charge’. It is important to bear this in mind when considering the possible deregulation of the postal services market and the delivery of a universal letter service.

It can be seen that, by using its discretion as far as access and reasonable standards of service are concerned, AP is directly affecting the cost of delivering a universal letter service. In other words, AP is already differentiating access conditions (and quality of service) to minimise the cost differences of mail flows within and between metropolitan and non-metropolitan areas. Moreover, as part of this cost minimisation approach, AP has contracted out parts of the delivery of the universal letter service (see below).

If the reserved protection were to be reduced or removed, AP would need explicit guidance from the Government as to the comprehensiveness of the postal service it would be expected to provide. Under Section 28C of the APC Act, regulations may prescribe performance standards in relation to the frequency, speed or accuracy of delivery or in relation to availability and access of services supplied by AP. This would be an important mechanism by which the Government could provide comfort to consumers that postal service standards would be maintained at an appropriate level. Indeed, the Government has already made a commitment to develop a Charter of Responsibilities for AP. It is intended that the Charter will be based on minimum performance standards established under Section 28C.

AP also differentiates between the type of retail outlets in metropolitan and non-metropolitan areas as far as the range of services supplied is concerned. Hence, in metropolitan areas, there are ‘post shops’ and traditional post offices, both of which offer a full range of postal and financial services (in addition, there are specialised ‘business centres’ for business users). In contrast, in rural areas there are post offices run in conjunction with other business, such as chemists, convenience stores and dry cleaners, and community postal agencies, both offering a smaller range of postal services.

Indeed, the extensive licensing of retail outlets means that AP is essentially providing ‘reasonable access’ to and a ‘reasonable standard’ of letter service in partnership with others. For example, as noted above there are already a number of post offices being run (by licensees) in conjunction with other businesses, while delivery services in rural areas are generally contracted out. This is an important issue when considering deregulation of the postal services market and the delivery of a universal letter service.

Standard Letter Service at a Uniform Charge

It is generally accepted that uniform charging implies the use of a cross-subsidy whereby revenues from parts of the network which exceed costs are used to fund the costs of servicing other users where revenues are insufficient. Under the current arrangements, there are no mechanisms in place to ensure that cross-subsidisation is limited to services reserved to AP and is not used to support services open to competition.

It is not clear that in a deregulated environment, a requirement on AP to continue providing a letter service at a uniform charge would necessarily be onerous. The introduction of differential tariffs (for instance reflecting geographical cost differences) would impose transaction costs which may not be liked by consumers or postal operators. These may arise from the difficulties of determining marginal costs for individual mail routes and operating a schedule of prices for different routes, for example, charging different prices for intra or interstate mail. As noted above, AP has already taken steps to reduce geographical cost differentiation and this assists uniform pricing. There may be scope to take this process further. In the US, private couriers appear to have adopted uniform quoted rates for delivery anywhere within the 48 adjoining states, including to rural areas some distance away from the airports used by courier firms. Competition occurs on service and price (eg negotiated volume discounts), however, rates are set such that a profit is not made on every delivery. Finally, it should be noted that larger AP customers already receive a selective discount for bulk mail. This issue is discussed in more detail in the section ‘Interconnection Arrangements’ below.

Australia Post’s Reserved Services

Section 29 of the APC Act provides AP with an exclusive right to: carry letters within Australia, collect and deliver letters; and issue postage stamps. The APC Act defines a ‘letter’ as any form of written communication directed to a particular person or address.

Section 30 of the APC Act provides a reasonably large number of exceptions to those reserved services, the most well known being the carriage of letters greater than 250 grams (subject to certain conditions) and the carriage of a letter within Australia at a rate at least four times the uniform charge ($1.80) for standard postal articles.

Notwithstanding these legislative exceptions, in practice it will always be difficult to perfectly delineate a reserved service from a non-reserved service. Consequently, 'grey' areas will likely develop at the boundary of a particular legislative exception where potential competitors see an opportunity to provide a service in competition with AP, despite AP considering that the service is reserved. There is no doubt that when faced with artificial constraints on competition, a company may seek to 'push the boundaries' if it can see a profitable business opportunity.

One area that has generated a number of these boundary problems, and which was identified by the IC in its 1992 report, is addressed advertising mail. The IC identified companies which had run into problems with AP when attempting to deliver addressed advertising mail. Hence, under the APC Act, an advertising catalogue with a one page insert addressed 'Dear valued customer' or 'Dear cardholder' could be interpreted by AP as being a letter and hence a reserved service. While the 1994 legislative amendments partially addressed this problem by removing some forms of addressed advertising material from the reserved services, Treasury understands that boundary problems remain as far as 'personalised' advertising mail is concerned. Moreover, the delivery of such mail has little relevance to the provision of a universal letter service.

There is little doubt that there are a number of companies that could immediately expand their presence in this market segment. Consequently, the grounds for some forms of addressed advertising mail continuing to be reserved to AP are not compelling. Treasury acknowledges that AP will likely lose some mail volumes as a result. However, there would seem little real likelihood that even a significant loss of business in this area would pose any risk to AP's ability to continue delivering a universal letter service. Moreover, the extent of the loss of volume will be dependent on AP's willingness to compete and be innovative in the face of new entrants to the market.

AP has a larger network than its competitors which provides a competitive advantage. On the other hand, smaller private sector operators may be able to provide a lower cost, more innovative service than AP.

More broadly, **Treasury supports the NCC closely examining the current definition of a 'letter' and other exceptions to the reserved services to see whether similar boundary problems to those in advertising mail are occurring.**

Australia Post's Ability to Provide its USO in the Face of Increased Competition

AP claims that should its reserved services be reduced or completely removed, it would lose significant market share and the resulting economies of scale and scope that a significant market share delivers. In combination with 'cream skimming' on its most profitable routes, AP believes that it would be unable to continue delivering a universal letter service at a uniform price.

Treasury recognises that AP would be faced with the need to make a number of adjustments, possibly significant, to its operations in order to continue delivering a universal service at a uniform price in a completely deregulated postal market (or a market where the current level of reserved services is significantly reduced). However, the difficulties AP is likely to face in such a market can be exaggerated.

As has been noted in the above section on 'Australia Post's Discretion in USO Delivery', AP has already taken a number of steps to reduce the geographical cost differences between mail paths, including contracting out and reducing the frequency of delivery in rural and remote areas, as well as licensing retail postal outlets that are run in conjunction with other businesses in these areas.

In considering AP's ability to compete with potential new entrants, it is important to make a broad distinction between mail lodged in AP's network that is charged at the uniform price and mail that attracts bulk discounts. AP currently provides discounts for bulk pre-sorted mail reflecting costs saved in processing and handling. In effect, the uniform letter price becomes a 'list' price off which AP offers discounts for its largest customers. Bulk pre-sorted mail accounts for around 30 per cent of the total letter mail posted.

In a deregulated environment, AP would continue to be able to offer differentiated bulk mail rates to compete with new operators in this market segment. These discounts may have a geographic dimension. Clearly, AP would still remain susceptible to a new operator entering the market and undercutting its discounted prices, however, AP would have some degree of flexibility in pricing in a key segment of its postal business. In contrast, for 'single piece' items (letters posted in small quantities), the legislative requirement to provide a 'standard letter service at a uniform price' would bind AP so it would not be able to compete with lower cost operators on price. AP would, nonetheless, still have some non-price competitive advantages which are discussed below.

In analysing the potential extent of 'cream skimming', the key feature of the economics of postal operations is the interaction between the economies of scale and scope of the postal network (to the extent they exist) and the varying costs of different mail paths. There is no direct connection between the size of the losses incurred on those (low density) mail runs where costs exceed the uniform price (the cost of the USO) and the size of the revenues on those (high density) mail runs where marginal costs are below the uniform price (the profitable routes used to cross-subsidise the USO). AP's high density runs are those most susceptible to competition, while its lowest density mail runs are those which it would be required to continue providing as part of its USO. Competitors, on the other hand, would choose not to operate on these latter routes.

AP may be vulnerable to competition on the lowest cost runs, despite the presence of economies of scale and scope, depending on the number of individual mail runs which are viable on a stand alone basis. If the cost to AP of any loss of market share is greater than the benefit to all consumers, then competition will lead to a static welfare loss. However, this potential loss needs to be set against the likely dynamic gains, through increased consumer choice, innovation and pressure to reduce costs. This is conceptually no different to the introduction of competition to Telstra. Moreover, there are credible alternative means of funding the USO apart from cross-subsidies (see below)**.**

In assessing how AP would cope in a deregulated environment, it should be recognised that it has a number of advantages over potential new entrants who are likely to face significant difficulties establishing competing mail networks. AP's current network allows it to connect all households and businesses across the country. Customers know that the one postal service is capable of delivering a piece of mail from its origin to final destination. In contrast, a mail network which does not provide a universal service faces a major problem of having to assess whether it can actually deliver the mail prior to acceptance. For example, such a network may need to rely on interconnection with AP's network or other smaller networks in order to deliver interstate items — a piece of mail could conceivably have to flow though two or more postal networks to reach its final destination.

Interconnection between different providers is difficult in the supply of postal services given the physical transfer of large volumes of mail that it entails. Difficulties include the fact that there are multiple points in the network where interconnection can take place and there is a significant task in coordinating the transport and delivery functions of different networks. These problems can be compared with the relative ease of interconnection in telecommunications. There may also be particular problems negotiating competitive interconnection fees with other network operators (see the section 'Interconnection Arrangements' below).

In addition to operating the only universal network, AP has built up what appears to be strong customer loyalty as a result of the provision of a reliable service over many years, and has an established 'brand name'. In contrast, it might take time for new operators to establish a similar reputation, particularly with household users.

AP generally downplays the commercial value generated by its provision of a universal postal service and the presence in the market that provision of such a service gives it. For example, it is possible that AP's very strong performance in recent years in the non-reserved services sector of the postal market has been assisted by its provision of a universal service. In addition, AP’s extensive coverage of retail outlets has enabled it to provide a wide range of non-postal services, including financial facilities such as bill paying and banking, which are showing strong volume and revenue growth.

Overall, it seems quite plausible that if the postal market were significantly deregulated, the extent to which competing networks would set up in competition with AP is likely to be limited. One possibility would be local services in high density areas, such as central business districts, with links to similar areas in other States/Territories, as currently occurs with document exchanges. Nonetheless, a deregulated market would provide scope for other suppliers to develop new services or provide the same services as AP at lower cost. This threat, potential or real, would in turn place pressure on AP to contain its costs and improve the quality of its service.

Finally, it should be recognised that any discussion of the likely effects of reducing AP’s reserved protection on the provision of the USO is hindered by a lack of meaningful data. Notwithstanding the complexity of deriving a value for the USO, AP’s annual point estimate of the total cost of providing the USO does not contribute significantly to the debate on the best means of funding and delivering its USO, and particularly the sustainability of the USO if the postal services market were further deregulated. For example, there does not appear to have been any attempt to estimate the net cost of the USO by major traffic volumes (eg city-city, city-country, country-country, international) since the IC’s estimates in 1992.

The Australian community potentially pays a high price for this lack of transparency, as a result of the maintenance of a level of reserved service protection for AP that may not be necessary for delivering the postal USO. However, without adequate information which can be subjected to independent scrutiny, this remains only a suspicion rather than a fact. This information asymmetry clearly places AP in a powerful position in arguing for maintenance of the status quo, although its strong financial performance in recent years suggests that its ability to continue delivering the USO in the face of deregulation should not be underestimated.

This information asymmetry is exacerbated by the standard reliance internationally on the monopoly provider model as the best means of delivering a universal letter service and a general unwillingness to look at alterative ways of delivering that service. This can be contrasted with the telecommunications sector both in Australia and internationally, where greater reliance on competition, in combination with a more extensive use of universal service funds, has proven to be a credible alternative to the monopoly provider model. As already noted, the Government recently decided that Telstra’s requirement to provide access to pay phones and the adoption of a standard local call tariff was a USO and should be funded by all industry participants in proportion to their respective market shares.

Similarly, **AP's requirement to provide a universal letter service, as specified in Section 27 of the APC Act, could be funded by a levy on new entrants if the postal services market were to be deregulated. A more tightly defined postal USO could also be developed as part of this process. AP would continue to be required to provide the USO, however, it could choose to subcontract some parts of the supply of the universal service.** As noted in the above section on 'Australia Post's Discretion in USO Delivery', AP has already taken steps down this path, including contracting out roadside delivery in rural and remote areas.

An alternative means of injecting greater competition into the postal services market while allowing AP to continue funding the cost of the USO would be to set a price floor to limit the extent of 'cream skimming' on AP's most profitable (lowest cost) routes. For example, in a completely deregulated postal market, competitors could charge below the current 45 cents uniform price for a standard letter but not below 40 cents. In principle, the price floor would be set at a level sufficient to protect enough of AP's lowest cost routes to enable it to generate sufficient revenues to continue cross-subsidising the cost of the USO.

In practice, there would be features of such a price floor which would make it an unattractive option compared to a universal service levy. It would likely be a difficult regulatory task to set the floor at a level which promoted greater competition while not excessively protecting AP's lowest cost routes. The regulator would need to acquire detailed information on the nature of AP's average and marginal costs in order to meet this objective. While opening up some mail runs to greater competition, a price floor could protect AP from competitive pressure on its lowest cost runs which could dull its incentive to improve efficiencies. Alternatively, a floor price could lead to inefficient non-price competition in terms of the quality of delivery service offered. The result could still be 'cream skimming' on some routes unless the regulator was able to regulate quality of service as well as the floor price.

Competition at Different Price Thresholds

International experience suggests that it is not until the level of protection of standard postal articles is reduced to around two times or less the standard letter rate (in AP's case 90 cents per letter or less) that true competition is likely to take place. For example, the level of protection provided for NZ Post was phased down in three steps from $NZ1.25 to $NZ0.80 between October 1989 and October 1991 (the standard letter price in NZ is $NZ0.40). Full deregulation is foreshadowed in 1998.

There appears to be some support for this in an Australian context, where industry observers have estimated that a reduction in AP's protection to 90 cents would only expose to competition around $300 million of its business. AP has claimed that the previous reduction in protection to $1.80 only exposed to competition around $250 million in revenue. In the absence of full data, there will always be a degree of uncertainty about the extent of competitive pressure at different price thresholds. Nonetheless, as the reserved service generates revenues of around $1.5 billion, it is quite possible that reducing the level of protection to 90 cents would only expose around 20 per cent of the reserved service to competition. Consequently, reducing the level of protection to significantly below 90 cents would appear to be required to allow effective competition over the bulk of the reserved service.

Australia Post's Non-Statutory CSOs

In addition to its Section 27 obligations, there appear to be a number of services that, over time, AP has chosen to undertake, or has been required to undertake by successive governments, which could be classified as CSOs. Community expectations also may have built up around the provision of certain services by AP. AP has argued that in costing its USO / CSOs, special allowance should be made to include recognition of the additional costs of government ownership. For example, AP argues that the annual costs of around $30 million to operate and maintain post offices which are also heritage properties should be included in the cost of the CSO. Other activities that could potentially be categorised as CSOs include the provision of medical and educational materials in rural areas.

With respect to heritage properties, it is possible that AP's responsibilities are greater than those faced by the private sector. This might be occurring as a result of the higher proportion of heritage buildings it owns, and community expectations that AP should continue to operate out of such buildings, notwithstanding that these buildings are likely to be more expensive to maintain and / or may be inappropriate for modern postal operations. However, the issue of AP operating out of heritage buildings needs to be separated from the provision of a universal letter service at a uniform price. The provision of a universal letter service at a uniform price does not depend on AP operating out of heritage buildings. It is inappropriate then for any additional costs this imposes to be reflected in a higher uniform price or an excessively high level of reserved services.

More generally, **consideration may need to be given to defining more precisely what is expected of AP by way of CSOs, so that these CSOs can be more accurately costed and, preferably budget funded, in line with the Government's recent decision on GBE accountability arrangements** (see above section on 'What are Australia Post's USO / CSOs?').

Resale Price Maintenance (RPM) of Standard Postage Stamps

RPM is *per se* prohibited under the *Trade Practices Act 1974* (ie, it is not subject to the substantial lessening of competition test). However, RPM can be authorised by the Australian Competition and Consumer Commission (ACCC) subject to a public interest test, if it is judged that a particular RPM arrangement results in a benefit to the public that outweighs any anti-competitive effect.

Section 33A of the APC Act prohibits, amongst other things, the sale of postage stamps for less than their usual retail price. This legislated RPM is intended to support the uniform pricing policy for standard letters. Effectively, AP supplies stamps to retailers at a particular ‘wholesale’ price and the margin or commission received by those retailers is fixed. A retailer has no discretion to lower the final price and take a lower commission. For each stamp sold outside the retail chain, AP only receives the ‘wholesale price’ and, by losing the difference between the retail and ‘wholesale’ price, it arguably diminishes its ability to fund the USO. It has been further argued that if retailers were allowed to undercut the retail price this would exacerbate the loss of revenue.

Treasury considers that this argument should be tested by the ACCC and that authorisation under the Trade Practices Act would be preferable to an industry specific exemption.

INFORMAL ‘FREEZE’ ON THE STANDARD POSTAGE STAMP PRICE

Prices Oversight of Australia Post

Under Section 33 of the APC Act, postage charges for standard articles are subject to Ministerial review. In exercising the powers under Section 33, the Minister is required to have regard to changes in the Consumer Price Index (CPI). In practical terms, this could be expected to impose some form of cap on any increases in the price of standard postal articles. AP’s reserved services are also declared under the *Prices Surveillance Act 1983* (the PS Act). Under the provisions of the PS Act, AP is required to notify the ACCC before increasing the price of its reserved services.

AP has held the price for delivery of a standard postal article constant at 45 cents since 1 January 1992 and has indicated its intention to maintain the freeze until June 1998. In other words, AP will have held the nominal price of delivering a standard postal article constant over this period, while real prices have fallen. The Steering Committee on National Performance Monitoring of Government Trading Enterprises has estimated that the real price of a standard letter has declined by 7.5 per cent since 1991-92; however, most of this gain has been concentrated in the last two years (real prices increased by around 2.5 per cent between 1990-91 and 1992-93, reflecting an increase in the standard postage stamp price from 41 cents to 45 cents between September 1990 and January 1992). The nominal price freeze was originally agreed between AP and the former Government, consequently the appropriateness of the freeze vis-a-vis alternatives such as a nominal price fall under a formal price cap, has never been subject to independent scrutiny by the ACCC.

The principal aim of a price cap is to prevent a firm with monopoly power exercising that power through restricting output or charging higher prices than would occur in a competitive market. A CPI-X price capping arrangement places a limit on the growth in the monopolist's prices equivalent to the rate of CPI growth minus the rate of productivity growth it would be likely to achieve relative to economy-wide productivity growth (the 'X'). It can be seen that AP's nominal price freeze has been equivalent to a price cap of CPI=X (in other words, CPI-X = 0 therefore CPI = X). To the extent that AP's productivity growth has outstripped inflation over this period, then the company will have made significant gains in revenue, notwithstanding the nominal freeze in the standard letter price.

Australia Post's Performance under the Nominal Price Freeze

Since AP instituted the price freeze, it has recorded a very strong financial performance. AP's return on assets has increased each year since 1992-93, reaching 17.6 per cent during 1995-96, reflecting strong increases in its earnings. Between 1991-92 and 1995-96, AP's earnings before interest and tax increased by 62 per cent compared with growth in average total assets of 7 per cent. AP's operating sales margin has increased steadily since 1992-93 reaching 12.5 per cent in 1995-96. Over this period, AP's annual average labour productivity growth has been around 5 per cent, compared to annual CPI growth of 2½ per cent (labour accounts for around 60 per cent of AP's total costs).

Reserved services account for around 55 per cent of AP's business, with the standard letter service being the major reserved product. It would also appear that the prices of other reserved services have been held broadly constant since 1992. The balance of AP's business activities are non-reserved services which, in principle, are subject to competitive pressures. Hence, it would be fair to say that the performance of AP's reserved services has been an important contributor to its overall strong financial performance.

Distribution of Productivity Gains

AP's strong productivity growth in recent years in combination with its strong recorded financial performance raises the issue of the distribution of those productivity gains. In a competitive market, increases in productivity would tend to be shared amongst all stakeholders, with consumers gaining through lower prices, as costs fell and rivals fought for market share. In contrast, if competition is lacking, prices may not fall in response to productivity gains.

Furthermore, in the absence of a sufficiently strong competitive environment, there may not be a sufficient inducement for AP to explore all avenues to increase productivity.

While at face value AP's customers appear to have benefited from the nominal price freeze (ie, as a result of the real price fall), they may not have shared fully in AP's achieved productivity gains to the extent that might have been possible if a CPI-X price capping arrangement with X > CPI had been in place over the period. To avoid a continuation of this situation, a reduction in prices for AP's reserved services could be investigated. This could be achieved by reviewing the 1994–97 period to see whether a price reduction could have been feasible and, if so, whether an immediate price reduction is warranted. The imposition of a CPI-X price cap for the next three to five years, which could be administered by the ACCC under the provisions of the PS Act, could also be considered.

The setting of the price cap would require information on AP's cumulative productivity and cost performance during the period of the freeze, as well as AP's expectations of future trends in these variables. It would be possible, in broad terms, to establish a cap which provides an incentive for AP to seek efficiency gains while ensuring that productivity gains are shared with consumers in the form of lower prices.

Clearly, the need for a cap to be applied to the price of standard postal articles supplied by AP is linked directly to the level of competition it faces in their delivery. Hence, if AP was exposed to greater competition in the delivery of standard postal articles, the pricing discipline this could be expected to impose would lessen the need for a cap. However, a reduction in reserved services protection may not result in strong competition developing in the short term. Consequently, a price cap regime may still be required as a transitional mechanism while sufficiently robust competition to ensure price restraint developed. This would be a similar situation to Telstra which is still subject to price caps on a range of services in markets where competition is weak or non-existent.

INTERCONNECTION ARRANGEMENTS

Legislative Framework

Interconnection is a potentially important means of facilitating greater innovation and efficiency in the delivery of postal services. In practical terms, interconnection allows competitors of AP to carry bulk quantities of letters which would otherwise be reserved to AP some part of the distance towards their destination, and to then lodge the letters with AP for final delivery to the addressee. By interconnecting in this way, AP's competitors receive some level of discount reflecting the costs avoided by AP.

The establishment of a legislative framework for bulk mail interconnection to AP's network was an element of the former Government's 1994 postal reforms. Under Section 32A of the APC Act, AP must provide interconnection on the basis of a rate reduction which reflects its estimate of the average transport costs per letter avoided in respect of the letters lodged for delivery. Nonetheless, the provision allows AP to take a broader interpretation of the interconnection terms and conditions than avoided transport costs. It is open to AP to negotiate individual terms and conditions of a service with customers.

Section 32B of the APC Act allows for regulations to be made to enable the ACCC to inquire into a dispute arising from the operation of a bulk interconnection service provided by AP under Section 32. The ACCC is not the final arbiter in disputes but rather makes recommendations to the Minister for Communications, the Information Economy and the Arts.

Australia Post's Interconnection Arrangements

Under the interconnection arrangement, AP has chosen to average all interstate line haul costs for a specific type of mail to arrive at a single discount of around one cent per letter for regular delivery (and a single discount for off-peak delivery). **In other words, as well as being relatively small, the discount is constant for letters regardless of their origin and distance carried to the mail centre of lodgement.** There are separate schedules for different sized letters and the discount for avoided transport costs is additional to pre-sort discount arrangements. AP notified the former Prices Surveillance Authority (PSA) of its proposed charges for bulk mail, including the interconnect discount, in July 1994. The PSA did not object to the notification.

As a consequence of bulk mailers getting the same interconnection discount regardless of the distance they have line hauled their mail, in practice they might be expected to bypass AP mainly on short haul segments rather than longer haul segments. This is because the averaging of all interstate line haul costs to arrive at the single interconnection discount makes it extremely difficult for third parties to successfully compete with Australia Post on line hauling mail when transport costs for longer routes are greater than those for shorter routes.

Moreover, while AP may be able to negotiate relatively favourable rates for its air transport contracts compared to potential competitors because of its very high mail volumes, the current interconnection discount does not recognise that part of the transportation function can be bypassed through electronic distribution. However, a bulk mailer utilising this option would still only receive a one cent per letter discount for AP's avoided costs.

It is questionable then whether the averaging of costs underlying the interconnection discount truly reflects AP's avoided costs. The overall effect of the arrangement has been to introduce a further level of cross-subsidisation in mail services. In addition, Section 32A is open to interpretation as to the

extent to which bulk mailers can actually negotiate with AP on interconnection terms and conditions.

Overall, there are doubts as to whether the existing interconnection arrangements have met the pro-competitive intent of the 1994 legislative amendments and there appears scope for a more desegregated schedule of interconnection discounts for bulk pre-sorted mail to be developed.

Part IIIA Access Provisions of the Trade Practices Act

Since the 1994 amendments to the APC Act, a national access regime under Part IIIA of the Trade Practices Act has been introduced as part of the competition policy reforms agreed with the States and Territories in April 1995. It effectively establishes a right for persons to negotiate with owners for access to a 'declared service' provided by a nationally significant infrastructure facility. Where these negotiations fail, the ACCC can arbitrate the terms and conditions of access. Applications for the declaration for a service are made to the NCC. The NCC is required to make a recommendation to the 'designated Minister' (in the Commonwealth sphere, the Treasurer) and that Minister must then decide for or against a declaration and publish his or her decision. Currently, AP's services are exempt from declaration under Part IIIA.

The primary role of the access regime is to prevent a vertically integrated firm from misusing market power that arises from one of the markets in which it operates. Where structural separation has not occurred, the access regime could be used to inject competition into upstream or downstream markets.

An issue arises whether the Part IIIA access provisions potentially provide a better means of promoting competition in the postal services market than the legislative framework under Section 32A of the APC Act. It is not clear whether AP's postal services network would meet all of the statutory criteria necessary for an access declaration to be successful, although clearly this would have to be tested in practice. Nonetheless, **there is no apparent reason why AP's reserved services should continue to be exempt from Part IIIA. Finally, while the issue of interconnection is an important one, the need for interconnection arrangements for AP is lessened or removed if the level of reserved letter protection is reduced or removed.**

Statistical Appendix

LIST OF CHARTS AND TABLES

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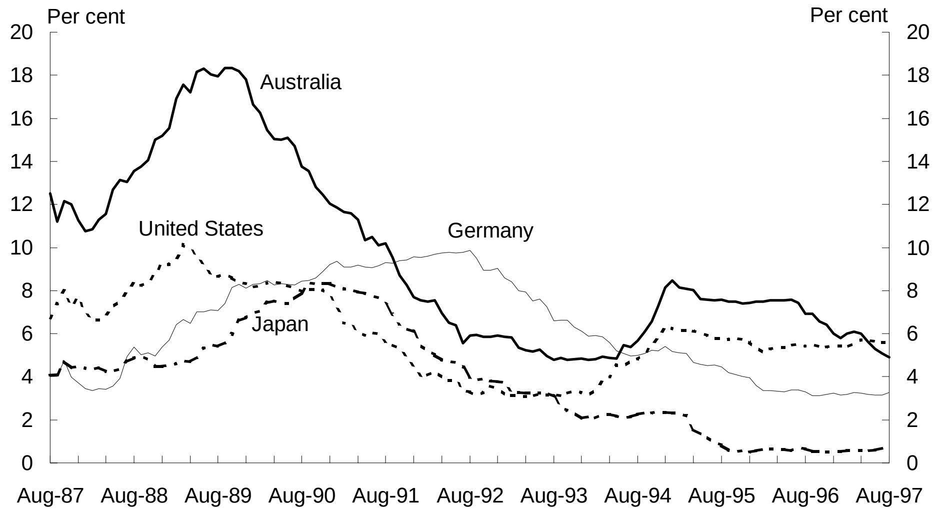
Key to Tables

n.a.	not available
n.y.a.	not yet available
..	change less than 0.05%

Chart 1: Selected International Indicators

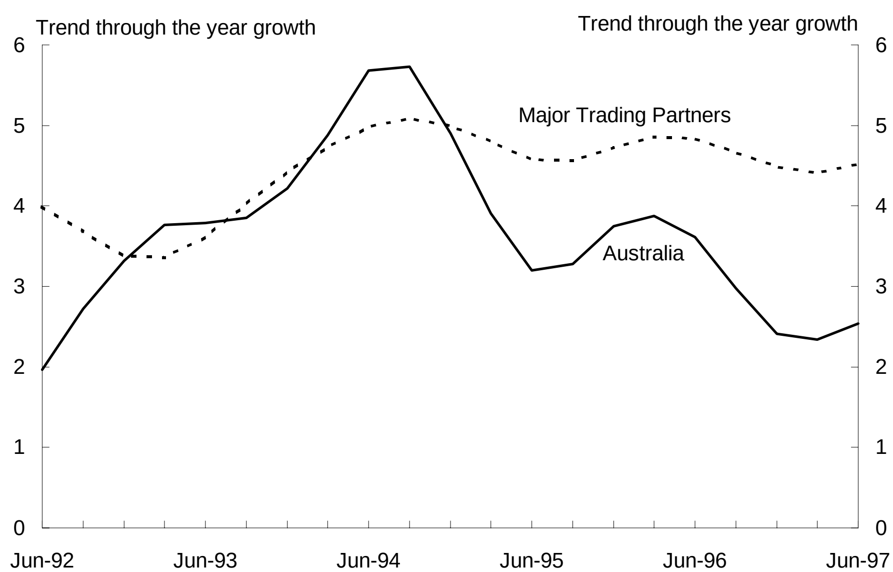
Panel A: Short-term Interest Rates(a)



Source: OECD Main Economic Indicators.

(a) Average monthly rates; USA — certificates of deposits, Japan — 3 month certificates of deposit, Australia — 90 day bank accepted bills and Germany — 3 month FIBOR.

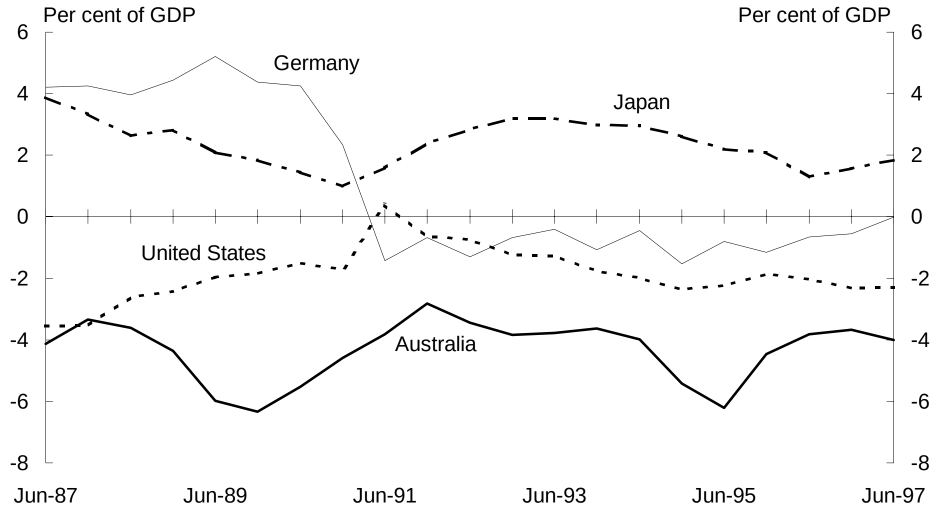
Panel B: Real Output(a)



(a) Constant price seasonally adjusted GDP growth for each major trading partner is weighted by their respective shares of total Australian merchandise exports from 1993-94 to 1995-96. In this chart, major trading partners comprise OECD and Asian major trading partners. OECD major trading partners comprise the G7 (Japan, USA, UK, Germany, France, Italy and Canada) and New Zealand. Asian major trading partners comprise South Korea, Taiwan, Hong Kong, Singapore, China, Malaysia, Indonesia, Thailand and the Philippines.

Chart 1: Selected International Indicators

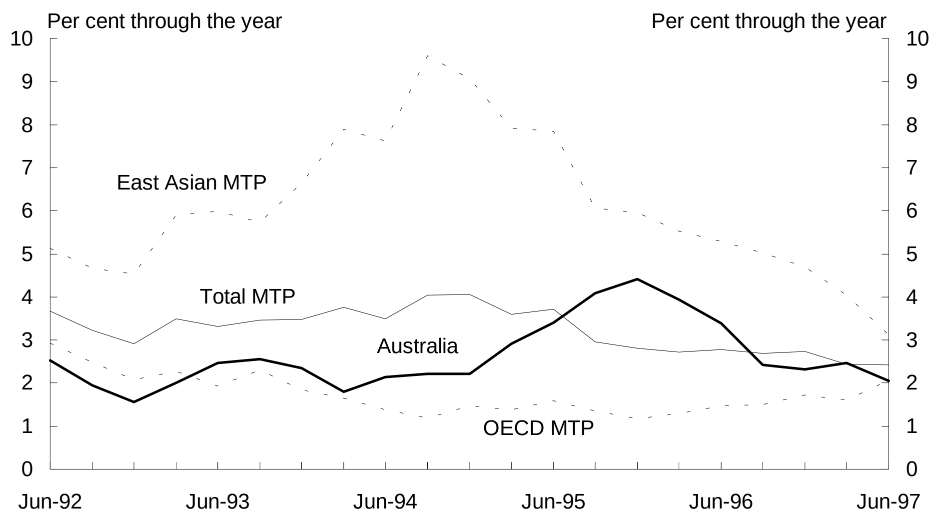
Panel C: Current Account Balances(a)



Source: OECD Economic Outlook.

(a) Seasonally adjusted estimates. Germany refers to Western Germany only until June 1990, and unified Germany thereafter.

Panel D: Consumer Price Inflation(a)



(a) In this chart the major trading partners (MTP) series is comprised of the ABS All Groups (excluding housing) CPI measure for the countries for which it is available (US, Japan, Germany, UK, New Zealand, Canada, South Korea, Singapore, Indonesia, Taiwan and Hong Kong) and the respective national government All Groups CPI series for the remainder of Australia's MTP (France, Italy, China, Malaysia, Thailand and the Philippines). None of the countries for which the All Groups CPI measure has been used includes the mortgage interest rate effect in the calculation of their All Groups CPI series.

The aggregate inflation rates are derived as the weighted average of the individual trading partner inflation rates, where the weights are the respective shares of Australian total merchandise trade from 1993-94 to 1995-96.

Chart 2: Contributions to Trend Quarterly GDP(A) Growth

(Average 1989-90 Prices)

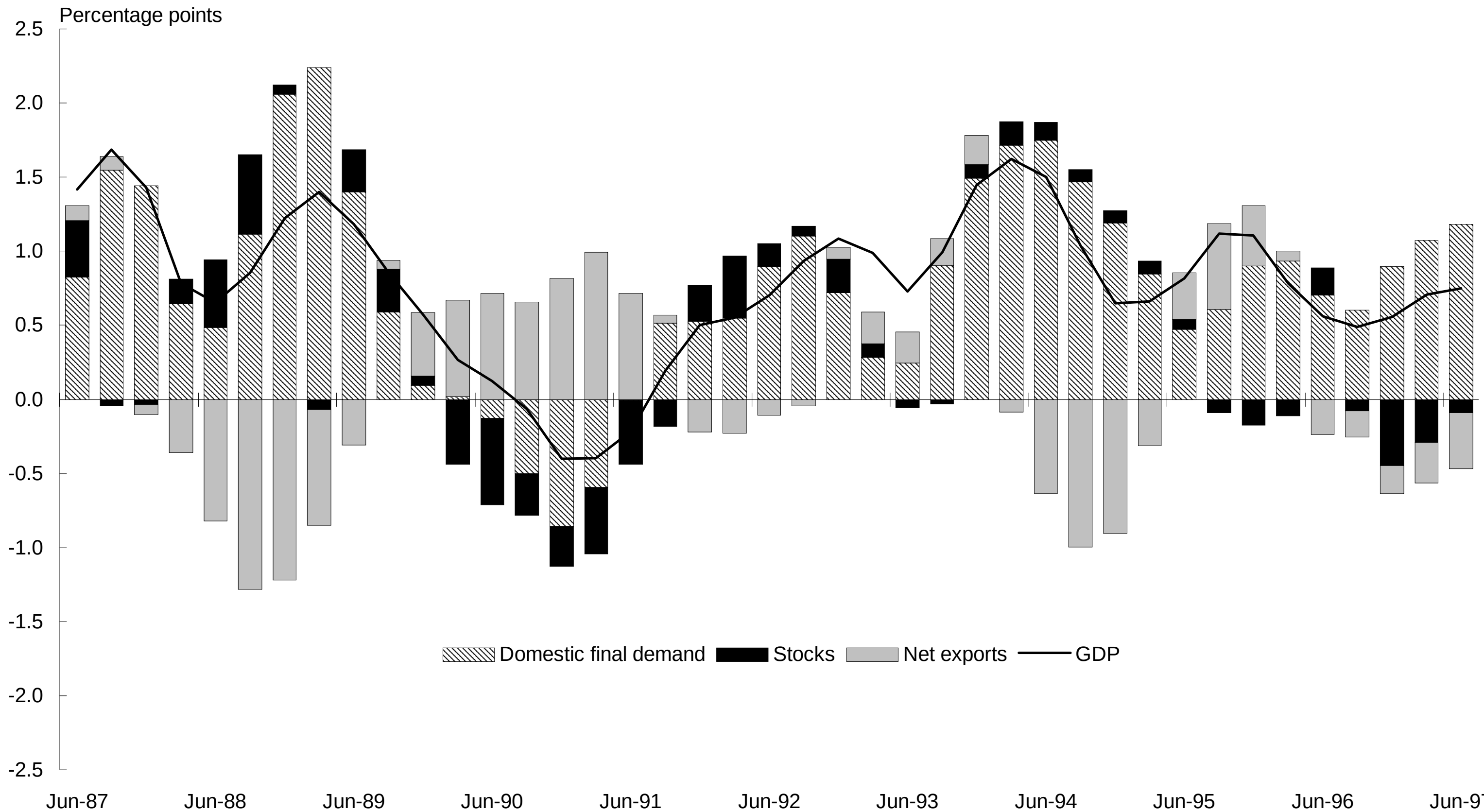


Table 1: Components of Gross Domestic Product (average 1989-90 prices)

	Final domestic demand												
	Private consumption	Private investment in dwellings	Private business fixed investment	Private final demand	Public final demand	Total final demand	Exports	Imports	Farm product (a)	Non-farm product (a)	GDP(A)(b)	GDP(I)	GDP(I) adjusted for terms of trade
Year -													
1994-95	4.9	3.8	15.5	6.0	5.5	5.9	3.8	17.7	-21.6	5.9	4.4	4.8	5.7
1995-96	3.9	-13.0	10.7	3.4	1.2	2.9	10.2	5.4	25.2	3.0	3.8	3.6	4.4
1996-97	2.3	0.2	15.9	4.2	0.0	3.3	9.5	10.3	14.4	2.4	2.5	2.8	3.7
Quarter -	(Percentage change on preceding quarter - Trend)												
1996 Jun	0.6	-1.5	4.8	1.1	-0.6	0.7	1.4	2.5	1.9	0.6	0.6	0.7	1.0
Sep	0.5	0.8	3.2	0.9	-0.3	0.6	1.0	1.8	4.7	0.5	0.5	0.7	0.9
Dec	0.6	2.3	1.3	0.8	1.3	0.9	1.5	2.4	4.1	0.5	0.6	0.6	0.8
1997 Mar	0.7	3.1	0.7	0.9	1.9	1.1	2.0	3.2	2.5	0.6	0.7	0.6	1.0
Jun	0.7	3.6	2.5	1.2	1.1	1.2	1.6	3.2	0.7	0.6	0.8	0.6	1.0
Quarter -	(Percentage change on preceding quarter - Seasonally Adjusted)												
1996 Jun	1.1	2.4	2.6	1.5	-2.4	0.6	-0.8	1.5	-3.7	0.3	0.0	0.2	0.6
Sep	-0.1	-2.1	5.0	0.5	-2.1	-0.1	1.3	0.0	12.0	0.7	0.9	1.1	1.2
Dec	0.9	3.0	-0.6	0.8	3.6	1.4	1.6	5.3	1.2	0.5	0.3	0.5	0.7
1997 Mar	0.6	3.5	2.0	1.1	2.5	1.4	2.6	0.3	3.9	0.2	0.7	0.4	0.5
Jun	0.8	4.0	12.2	2.9	-6.0	1.0	11.3	6.3	-1.2	1.3	1.2	1.2	1.8
Quarter -	(Percentage change on a year earlier - Trend)												
1996 Jun	3.3	-13.3	15.7	3.9	0.9	3.2	11.4	7.5	25.8	2.8	3.6	3.5	4.3
Sep	2.7	-8.3	17.3	4.1	0.1	3.2	9.3	9.3	17.8	2.7	3.0	3.1	4.1
Dec	2.4	-1.7	15.0	4.0	0.5	3.2	6.9	9.7	14.0	2.3	2.4	2.7	3.8
1997 Mar	2.3	4.7	10.3	3.7	2.2	3.4	6.0	10.3	13.9	2.2	2.3	2.6	3.7
Jun	2.4	10.2	7.9	3.8	4.0	3.8	6.3	11.1	12.5	2.2	2.5	2.6	3.7

(a) Income measure.

(b) GDP(A) is the average of the income (GDP(I)), expenditure (GDP(E)) and production (GDP(P)) based estimates of GDP.

Source: ABS Cat. No. 5206.0

Table 2: Contributions to Change in Gross Domestic Product (Average) (average 1989-90 prices)[(a)]

	Final domestic demand						Change in stocks			
	Private consumption	Private investment in dwellings	Private business fixed investment	Private final demand	Public final demand	Total final demand	Private non-farm	Farm & public authority	Net exports	GDP(A)
Year -	(Contribution to change in GDP(A))									
1994-95	3.0	0.2	1.5	4.6	1.2	5.8	0.4	-0.1	-2.6	4.4
1995-96	2.4	-0.7	1.1	2.7	0.3	2.9	-0.2	0.2	1.0	3.8
1996-97	1.4	0.0	1.8	3.3	0.0	3.3	-0.3	-0.7	-0.1	2.5
Quarter -	(Contribution to change in GDP(A) - Trend)									
1996 Jun	0.3	-0.1	0.5	0.8	-0.1	0.7	0.2	0.0	-0.2	0.6
Sep	0.3	0.0	0.4	0.7	-0.1	0.6	-0.1	0.1	-0.2	0.5
Dec	0.4	0.1	0.2	0.6	0.3	0.9	-0.4	-0.1	-0.2	0.6
1997 Mar	0.4	0.1	0.1	0.7	0.4	1.1	-0.2	-0.1	-0.3	0.7
Jun	0.4	0.2	0.3	1.0	0.2	1.2	0.0	-0.1	-0.4	0.8
Quarter -	(Contribution to change in GDP(A) - Seasonally Adjusted)									
1996 Jun	0.6	0.1	0.3	1.1	-0.5	0.6	0.2	0.2	-0.5	0.0
Sep	-0.1	-0.1	0.6	0.4	-0.4	-0.1	0.1	0.2	0.3	0.9
Dec	0.5	0.1	-0.1	0.6	0.7	1.3	-0.5	-0.3	-0.8	0.3
1997 Mar	0.4	0.2	0.2	0.8	0.5	1.4	-1.1	-0.1	0.5	0.7
Jun	0.5	0.2	1.5	2.3	-1.3	1.0	1.3	-2.3	1.2	1.2

(a) The sum of the contribution of the expenditure components do not precisely sum to the change in GDP(A) due to the statistical discrepancy between GDP(E) and the average of GDP(E), GDP(I) and GDP(P).

Source: ABS Cat. No. 5206.0

Table 3: Gross Product by Industry (average 1989-90 prices)

	Agri-culture, forestry & fishing	Mining	Manu-fact-uring	Electri-icity, gas & water	Cons-truct-ion	Whole-sale trade	Retail trade	Accomm-odation, cafes & restaurants	Trans-port & storage	Communi-cation services	Finance & insur-ance services	Property & busi-ness services	Gov. ad-minist-ration & defence	Edu-cation	Health & comm-unity services	Cultural & recre-ational services	Personal & other services
Year-								(Percentage change on preceding year)									
1994-95	-19.9	4.2	3.9	2.9	6.2	12.2	5.2	9.0	8.2	12.6	2.3	6.6	4.1	2.2	2.1	6.5	6.4
1995-96	22.5	5.0	1.1	0.2	1.1	5.1	3.2	3.8	3.5	13.6	4.6	0.8	4.0	1.4	6.1	3.3	7.5
1996-97	13.0	2.4	1.4	1.5	2.4	2.0	0.9	-1.5	2.0	10.7	7.5	4.2	0.0	-1.9	0.5	3.0	4.0
Quarter -								(Change on previous quarter - Trend)									
1996 Jun	1.7	1.6	0.0	0.1	0.8	0.1	0.2	-1.1	0.5	2.9	1.7	-0.1	-0.7	-1.1	-1.2	1.2	1.3
Sep	4.3	0.4	-0.1	0.1	1.6	-0.4	0.0	-1.4	0.3	2.7	2.0	1.0	-1.2	-0.5	-0.9	0.6	0.5
Dec	3.8	-0.5	0.3	0.7	0.7	0.6	0.3	-0.1	0.3	2.3	2.0	2.3	0.1	0.1	0.9	0.3	0.5
1997 Mar	2.3	-0.1	0.6	1.1	-0.6	1.3	0.6	1.2	0.6	2.2	1.6	2.5	1.0	0.3	1.7	0.3	0.8
Jun	0.6	0.2	0.6	1.2	-1.2	1.1	0.6	1.8	0.5	2.0	1.3	2.5	1.5	0.0	1.6	0.3	0.9
Quarter -								(Change on previous quarter - Seasonally Adjusted)									
1996 Jun	-3.5	1.9	-2.2	-0.2	1.7	-3.0	-0.4	-0.3	-0.8	2.8	1.2	1.6	-0.7	-2.2	-2.7	0.7	0.8
Sep	11.1	-1.9	2.2	-0.7	3.7	0.1	0.0	-2.5	0.1	2.1	3.2	0.1	-1.6	-1.3	-0.5	0.7	0.7
Dec	1.0	2.7	-0.9	0.9	-1.2	1.2	0.1	-1.1	1.6	3.4	1.5	2.4	-0.2	1.5	0.3	0.6	-0.2
1997 Mar	3.7	-3.7	0.0	1.9	0.3	1.4	1.1	2.8	-0.9	1.3	1.2	3.2	1.2	0.8	3.5	-0.4	1.5
Jun	-1.2	3.2	2.4	0.6	-2.3	0.9	0.4	2.1	1.7	2.5	2.1	2.1	2.5	-1.7	0.3	1.2	1.0
Quarter -								(Change on year earlier - Trend)									
1996 Jun	23.2	6.9	2.6	0.5	1.2	4.3	2.1	1.0	3.8	12.6	6.0	-0.2	4.2	-2.3	4.4	4.1	6.9
Sep	16.0	6.2	1.6	0.8	2.3	2.4	1.2	-1.8	3.0	12.0	6.7	0.5	0.8	-2.9	0.5	4.3	5.8
Dec	12.7	3.5	0.7	1.1	3.0	1.3	0.9	-2.6	2.0	11.2	7.3	2.9	-1.1	-2.3	-1.0	3.6	4.3
1997 Mar	12.6	1.4	0.7	2.0	2.4	1.5	1.0	-1.5	1.7	10.5	7.5	5.8	-0.8	-1.2	0.4	2.4	3.1
Jun	11.4	0.0	1.4	3.1	0.4	2.6	1.4	1.4	1.7	9.5	7.0	8.5	1.4	-0.1	3.3	1.6	2.7

Source: ABS Cat. No. 5206.0

Table 4: Household Income (Constant price, seasonally adjusted estimates)[a]

	Non-farm wage and salary earners	Non-farm average earnings	Non-farm wages, salaries and supplements	Income of unincorporated enterprises, etc: Farm	Income of unincorporated enterprises, etc: Other (b)	Real household income	Real household disposable income
Year -			(Percentage change on preceding year)				
1994-95	4.6	0.5	5.2	-48.0	12.1	5.8	5.5
1995-96	2.7	1.4	4.1	171.9	2.3	4.9	4.2
1996-97	1.7	3.2	4.9	-6.3	2.2	3.8	3.1
Six months to -			(Annualised percentage change)				
1995 Jun	0.2	2.6	2.8	-25.0	9.4	4.6	4.0
Dec	1.7	3.2	4.9	-32.7	6.3	4.2	4.4
Jun	3.5	4.5	8.1	-0.8	-3.1	4.0	3.2
1996 Dec	2.3	3.4	5.8	34.6	-3.1	3.6	2.3
Jun	-0.3	2.3	2.0	20.7	6.0	3.7	2.3
Quarter -			(Percentage change on preceding quarter)				
1996 Jun	0.4	0.8	1.1	-23.1	2.4	1.3	1.5
Sep	1.2	1.5	2.7	12.0	-1.8	0.7	0.6
Dec	0.7	0.7	1.4	4.5	-1.9	1.2	0.5
1997 Mar	-0.3	0.4	0.1	10.1	2.4	0.4	0.6
Jun	-0.4	0.7	0.3	-4.8	2.9	1.6	0.5
Quarter -			(Quarterly percentage change on year earlier)				
1996 Jun	1.0	2.4	3.4	352.6	5.2	5.3	5.0
Sep	1.7	3.9	5.6	-18.5	3.8	4.4	3.7
Dec	2.0	3.2	5.2	-8.8	2.0	4.2	3.5
1997 Mar	2.0	3.4	5.4	-0.9	1.0	3.7	3.3
Jun	1.2	3.3	4.5	22.7	1.5	4.0	2.2

(a) Deflated by the implicit price deflator for private final consumption expenditure.

(b) Includes income of non-farm unincorporated enterprises, income from interest and dividends and imputed income from dwellings.

Source: ABS Cat. No. 5206.0

Table 5: Wages, Labour Costs and Company Income (seasonally adjusted)

	Average weekly earnings (Survey basis)		Average earnings (National accounts basis)		Unit labour costs Non-farm			Factor Shares Non-farm			
	Full-time adult ordinary time earnings	All persons total earnings	Nominal	Real (b)	Nominal (c)	Real (d)	Private corporate sector Real (e)	Wages share (f)	Private Corporate GOS share (g) (j)	Corporate GOS share (h) (j)	GOS share less net tax and net interest (i) (j)
Year (a) -	(Percentage change on preceding year)					(Index)	(Index)	(per cent)	(per cent)	(per cent)	(per cent)
1994-95	4.1	3.4	1.8	0.5	0.4	97.0	98.0	57.0	33.5	17.7	21.2
1995-96	4.5	2.5	4.1	1.4	3.6	97.9	98.2	57.7	33.4	18.2	20.0
1996-97	3.9	3.0	4.7	3.2	3.3	98.8	100.3	58.6	31.9	17.6	n.y.a
Quarter -	(Percentage change on preceding quarter)										
1996 Sep	1.1	0.7	1.9	1.5	2.1	98.9		58.6		17.6	
Dec	1.1	0.4	1.1	0.7	1.4	99.5		58.9		17.8	
1997 Mar	1.0	1.3	0.7	0.4	-0.2	99.2		58.9		17.1	
Jun	0.3	0.0	1.0	0.7	-0.8	98.0		58.1		17.9	
Sep	1.6	0.8	n.y.a	n.y.a	n.y.a	n.y.a		n.y.a		n.y.a	
Quarter -	(Percentage change on year earlier)										
1996 Sep	3.8	3.5	5.5	3.9	4.1						
Dec	3.9	2.8	4.9	3.2	3.9						
1997 Mar	4.3	3.4	4.9	3.4	3.7						
Jun	3.5	2.4	4.7	3.3	2.6						
Sep	4.1	2.4	n.y.a	n.y.a	n.y.a						

(a) Annual data are original data.
(b) Deflated by the implicit price deflator for private final consumption expenditure.
(c) Ratio of nominal hourly labour costs (non-farm wages, salaries and supplements, plus payroll tax and fringe benefits tax less employment subsidies, per hour worked by non-farm wage and salary earners) to average hourly productivity (real gross non-farm product per hour worked by all employed persons).
(d) Nominal unit labour costs as defined in footnote (c) deflated by the derived implicit price deflator for gross non-farm product. (Base for index: 1966-67 to 1972-73 = 100.0)
(e) Ratio of wages, salaries and supplements, payroll tax (less employment subsidies) and fringe benefits tax paid by the private non-farm corporate sector to private non-farm corporate sector gross product at factor cost, plus payroll tax (less employment subsidies) and fringe benefits tax. (Base for index: 1966-67 to 1972-73 = 100.0)
(f) The ratio of non-farm wages, salaries and supplements to gross non-farm product at factor cost.
(g) Ratio of the gross operating surplus (GOS) of the private non-farm corporate sector to the gross product at factor cost of the private non-farm corporate sector.
(h) The ratio of the gross operating surplus of non-farm corporate trading enterprise companies to gross non-farm product at factor cost.
(i) The annual non-farm gross operating surplus share defined in footnote (g) less net tax and net interest paid by private non-farm corporate trading enterprises.
(j) Excludes private financial trading enterprises.

Sources: ABS Cat. Nos. 5204.0, 5206.0, 5222.0, 6301.0 and 6302.0

Table 6: Prices

	Consumer price index (a)			Implicit price deflators (d)	
	All groups	All groups excl. mortgage interest & consumer credit charges (b)	Underlying rate (c)	Gross non-farm product (e)	Private final consumption expenditure
Year -	(Percentage change on preceding year)				
1993-94	1.8	2.5	2.1	1.0	1.5
1994-95	3.2	2.7	2.1	1.0	1.3
1995-96	4.2	3.6	3.2	2.9	2.7
1996-97	1.3	2.3	2.1	2.3	1.5
Quarter -	(Percentage change on preceding quarter)				
1995 Dec	0.8	0.8	0.7	0.3	0.3
1996 Mar	0.4	0.3	0.4	0.7	0.5
Jun	0.7	0.7	0.8	0.7	0.3
Sep	0.3	0.4	0.5	0.4	0.4
Dec	0.2	0.7	0.4	0.9	0.3
1997 Mar	0.2	0.7	0.4	0.3	0.3
Jun	-0.2	0.2	0.3	0.6	0.3
Sep	-0.4	-0.2	0.3	na	na
Quarter -	(Percentage change on a year earlier)				
1995 Dec	5.1	4.1	3.2	3.2	2.9
1996 Mar	3.7	3.5	3.3	2.9	2.6
Jun	3.1	3.2	3.1	2.5	2.2
Sep	2.1	2.3	2.4	2.1	1.6
Dec	1.5	2.2	2.1	2.8	1.6
1997 Mar	1.3	2.6	2.1	2.4	1.5
Jun	0.3	2.1	1.7	2.3	1.4
Sep	-0.3	1.5	1.5	na	na

(a) Based on the eight capital cities consumer price index.

(b) See article in the January 1989 *Economic Roundup* regarding the use of this series for economic analysis.

(c) ABS estimate based on Treasury methodology. An article on the construction of this estimate appeared in the Summer 1995 *Economic Roundup.*

(d) Quarterly and through the year figures are derived from seasonally adjusted data. The year-average data are original.

(e) Gross non-farm GDP(E).

Sources: ABS Cat. Nos. 6401.0 and 5206.0

Table 7: Labour Market

	ANZ Bank job advertisements series	Employed persons			Unemployment		Participation rate
		Full-time	Part-time	Total	Rate	Persons	
	(Percentage change on preceding year)					(Levels)	
Year -					(per cent)	('000)	(per cent)
1994-95	29.1	3.2	6.6	4.0	9.0	794.5	63.3
1995-96	-7.0	2.3	3.3	2.6	8.5	766.7	63.7
1996-97	-8.5	0.3	3.4	1.1	8.7	796.5	63.5
Quarter -		(Percentage change on preceding quarter - seasonally adjusted)					
1996 Sep	-4.3	0.5	0.5	0.5	8.7	795.6	63.7
Dec	-2.2	0.0	1.5	0.4	8.6	791.6	63.6
Mar	2.4	-0.3	1.9	0.2	8.7	801.6	63.6
1997 Jun	10.5	-0.3	0.5	-0.1	8.7	796.6	63.2
Sep	-1.2	0.4	-0.5	0.2	8.7	797.1	63.1
Quarter -		(Percentage change on a year earlier - seasonally adjusted)					
1996 Sep	-14.2	0.7	2.4	1.1			
Dec	-12.8	0.6	2.4	1.0			
Mar	-11.2	0.1	4.5	1.2			
1997 Jun	5.9	-0.1	4.4	1.0			
Sep	9.3	-0.2	3.3	0.6			
Month -		(Percentage change on preceding month - seasonally adjusted)					
1997 May	-7.3	-0.4	-0.8	-0.5	8.8	809.8	63.2
Jun	0.8	-0.3	1.4	0.1	8.5	777.8	63.0
Jul	-2.9	0.8	-1.5	0.3	8.7	801.2	63.2
Aug	4.3	-0.6	0.0	-0.5	8.7	798.7	62.9
Sep	2.8	0.9	0.9	0.9	8.6	791.5	63.3
Oct	-0.3	-0.2	0.5	0.0	8.4	772.7	63.0

Sources: ANZ Bank and ABS Cat. No. 6202.0

Table 8: Balance of Payments (seasonally adjusted)

	Balance on merchandise trade	Balance on goods & services	Net income balance	Net unrequited transfers	Current Account Balance		Net Income Balance		Volume of		
						Percentage of GDP	Percentage of current account balance	Percentage of GDP	Exports of goods & services	Imports of goods & services	Terms of Trade (a)
Year (b) -		($ million)			($ million)	(per cent)	(per cent)	(per cent)	($ million)		
1994-95	-8269	-8589	-18506	393	-26702	5.8	69	4.0	89060	-89789	91.7
1995-96	-1878	-766	-20613	1043	-20336	4.2	101	4.2	98146	-94608	95.6
1996-97	1364	2818	-20561	1205	-16538	3.2	124	4.0	107467	-104358	99.8
Quarter -											
1996 Jun	-389	-38	-4647	303	-4382	3.5	106	3.8	25125	-24629	97.9
Sep	-43	410	-5370	326	-4634	3.7	116	4.3	25452	-24623	98.4
Dec	-612	-275	-5353	315	-5313	4.2	101	4.2	25854	-25920	99.2
1997 Mar	127	449	-4668	247	-3972	3.1	118	3.6	26521	-25985	99.7
Jun	2028	2411	-5179	322	-2446	1.9	212	4.0	29528	-27615	102.1
Month -											
1996 Nov	-378	-224									
Dec	82	210									
1997 Jan	-166	-3									
Feb	67	234									
Mar	-265	-182									
Apr	47	273									
May	787	904									
Jun	1857	1929									
July	-102	181									
Aug	203	318									
Sep	326	408									

(a) The ratio of the implicit price deflator for exports of goods and services to the implicit price deflator for imports of goods and services, 1989-90 = 100.
(b) Annual data are original data.
Sources: ABS Cat. Nos. 5368.0 and 5302.0

Table 9: Australia's External Liabilities

	Public sector gross debt	Private sector gross debt	Total gross debt	Net debt	Net external liabilities
			(Levels of Australian Foreign Liabilities)		
As at end -			($A million)		
1995 Jun	100117	123564	223681	181477	261186
1996 Jun	97918	138094	236012	187535	286130
1997 Jun	96479	158208	254687	202024	307460
1996 Jun	97918	138094	236012	187535	286130
Sep	94573	147222	241795	195386	289124
Dec	100616	146742	247358	199074	299376
1997 Mar	98618	149201	247819	197673	297748
Jun	96479	158208	254687	202024	307460
As at end -			(Percentage of GDP)		
1995 Jun	21.9	27.0	48.9	39.7	57.1
1996 Jun	20.1	28.3	48.4	38.5	58.7
1997 Jun	18.9	31.0	50.0	39.6	60.3
1996 Jun	20.1	28.3	48.4	38.5	58.7
Sep	19.2	29.9	49.1	39.6	58.7
Dec	20.1	29.4	49.5	39.9	59.9
1997 Mar	19.6	29.6	49.2	39.2	59.1
Jun	18.9	31.0	50.0	39.6	60.3

Source: ABS Cat. No. 5306.0

Table 10: Australia's Income Flows

	Public sector gross debt	Private sector gross debt	Total gross debt	Net debt	Net external liabilities
	(Gross and Net Interest Payable, and Net Investment Income) ($A million)				
Year ended -					
1995 Jun	5571	5994	11565	9802	17314
1996 Jun	5789	7070	12859	11019	19388
1997 Jun	5462	7373	12835	11074	19286
Quarter ended -					
1996 Jun	1228	1771	2999	2597	4249
Sep	1628	1783	3411	2907	5238
Dec	1253	1912	3165	2693	4913
1997 Mar	1347	1828	3175	2798	4362
Jun	1233	1851	3084	2676	4773
Year ended -	(Percentage of Exports of Goods and Services)				
1995 Jun	6.4	6.9	13.3	11.3	19.9
1996 Jun	5.9	7.2	13.1	11.2	19.8
1997 Jun	5.2	7.1	12.3	10.6	18.5
Year ended -					
1996 Jun	5.9	7.2	13.1	11.2	19.8
Sep	6.0	7.3	13.2	11.3	20.3
Dec	5.8	7.3	13.0	11.2	19.3
1997 Mar	5.4	7.3	12.7	11.0	18.7
Jun	5.2	7.1	12.3	10.6	18.5

Source: ABS Cat. No. 5306.0

Table 11: Selected Economic Indicators

			Indices of unit labour costs & prices adjusted for exchange rate changes (b)(c) (19			
			Price based		Unit labour cost based (f	
						Components o labour cost in
	Private non-farm stocks to sales (a)	Imports to sales (a)	CPI based (d)	GDP deflator based (e)		Nominal unit cost index
Year -						
1994-95	0.931	0.258	80.3	77.5	78.4	96.3
1995-96	0.932	0.252	87.1	83.2	84.9	98.1
1996-97	0.918	0.248	93.3	90.0	94.0	100.6
Quarter (h) -						
1996 Jun	0.932	0.249	93.0	88.9	91.2	98.9
Sep	0.941	0.245	92.6	88.6	92.5	100.3
Dec	0.933	0.251	93.9	90.2	94.7	101.1
1997 Mar	0.905	0.246	94.5	91.1	95.4	100.9
Jun	0.885	0.247	92.3	90.3	93.6	100.0

(a) ABS National Accounts measure.

(b) A discussion of these indices and detailed figures covering the period from the September quarter 1970 to the March quarter 1983 may be found in a supplement to the July 1983 Roundup of Economic Statistics titled 'International Comparisons of Relative Price and Cost Levels'.

(c) The weights used are based on a 3 year moving average of Australia's imports from the US, Japan, UK and Germany. The four countries are the source of about 60 per cent of Australia's imports. Observations are quarterly averages. A rise (fall) implies a deterioration (improvement) in Australian costs and prices relative to the four countries above after adjusting for exchange rate changes.

(d) The CPI based index is the ratio of the Australian Consumer Price Index to the weighted geometric average of the exchange rate adjusted consumer price indices of Australia's four major import sources.

(e) The GDP deflator based index is the ratio of the GDP deflator for Australia to the weighted geometric average of the exchange rate adjusted GDP deflator of Australia's four major import sources.

(f) The unit labour cost based index is the ratio of unit labour costs in the non-farm sector of the Australian economy to the weighted geometric average of the exchange rate adjusted unit labour costs in the business sector for Australia's four major import sources.

(g) Ratio of household saving to household disposable income.

(h) Quarterly data are seasonally adjusted except for the trade weighted index and the nominal exchange rate.

(i) Period Average, May 1970 = 100.

Sources: ABS Cat. Nos. 5206.0 and 5302.0

INDEX OF ARTICLES AND OTHER MAJOR TREASURY PUBLICATIONS

Articles in the Economic Roundup

Details of articles published in the past two editions of the Economic Roundup are listed below:

	Treasury Submission to the Senate Heritage Access Inquiry
	Treasury Submission to the Inquiry into Fair Trading
Winter 1997	Overview of Economic Developments
	World Economic Outlook
	The OECD Jobs Study
	Commonwealth Government's 1997-98 Budget Financing Program and Debt Management Strategy
	Australia's Experience with Indexed Bonds

Copies of these articles are available from the Treasury. Written requests should be sent to The Director, Current Economic Conditions Section, The Treasury, Parkes Place, Parkes, ACT, 2600. Telephone requests should be directed to Antonietta Caggiano on (02) 6263 2932.

Treasury Economic Papers

Titles and publication dates of Treasury Economic Papers (TEP) issued in recent years are listed below:

TEP 14	Financial Monitoring of Government Business Enterprises: An Economic Framework (1990)
TEP 15	Competition Policy — Submission to the Cooney Committee Inquiry into Mergers, Monopolies and Acquisitions and the Lee Committee Inquiry into the Print Media (1991)
TEP 16	Treasury Submission to the National Competition Policy Review (1993)
TEP 17	Research and Development Policy: A Framework for Analysis (1994), Treasury Submission to the Industry Commission Inquiry into Research and Development in Australia

Copies of these papers can be purchased from your local Government InfoShop (formerly the Commonwealth Government Bookshops) — **for InfoShop locations and further information phone toll free on 132 447.**

Treasury Research Papers

Titles and publication dates of Treasury Research Papers (TRP) issued in recent years are listed below.

	Title	Author	Date
TRP1	Asset Price Inflation	Tony Urbanski	December 1990
TRP2	The Redistributive Effects of Inflation	Brian Cassidy	March 1991
TRP3	Inflation and Uncertainty	Martin Parkinson	September 1991
TRP4	Economic Infrastructure in Australia	Alison Smith	September 1992
TRP5	Australia's Medium-Term Economic Growth: A Policy Perspective	Bart Dowling	November 1992
TRP6	National Saving and External Balance	Glenys Byrne	July 1993
TRP7	Aggregate Saving in Australia: Measurement and Trends	Brendan Flynn	October 1993
TRP8	Extended Measures of Investment and Saving	Peter Depta, Frank Ravalli & Don Harding	February 1994
TRP9	Climate Change: Interpreting and Measuring Emission Targets	Rob Sturgiss	April 1995
TRP10	What Future for Payroll Taxes in Australia?	Matthew Ryan	September 1995
TRP11	Derivatives, Financial Innovation and Taxation	Richard Wood	December 1996

Copies of these papers can be purchased from your local Government InfoShop (formerly the Commonwealth Government Bookshops) — **for InfoShop locations and further information phone toll free on 132 447.**

1995-96 Tax Expenditures Statement

The *1995-96 Tax Expenditures Statement* was released in January 1997 and provides comprehensive information on the extent and cost to revenue of tax expenditures for the years 1992–93 to 1999–2000. Tax Expenditures Statements are prepared annually in conjunction with the Australian Taxation Office.

Copies may be downloaded from the Treasury web site (http://www.treasury.gov.au).

Copies can be purchased from your local Government InfoShop (formerly the Commonwealth Government Bookshops) — **for InfoShop locations and further information phone toll free on 132 447.**

Treasury Annual Reports

Annual reports are published separately for the Treasury and the Royal Australian Mint.

Copies of Treasury Annual Reports and those of other Treasury Portfolio Agencies can be purchased from your local Government InfoShop (formerly the Commonwealth Government Bookshops) — **for InfoShop locations and further information phone toll free on 132 447.**

Treasury Conference Papers

1. Douglas, J & Bartley, S. 1996, *Risk Premia in Australian Interest Rates*, paper presented to the 25th Conference of Economists, Economic Society of Australia, Australian National University, Canberra, 23-25 September.

2. Ferry, N. 1996, *Australia's Current Account Performance and Microeconomic Reform,* paper presented to the 25th Conference of Economists, Economic Society of Australia, Australian National University, Canberra, 23-25 September.

3. Lucich, M. 1997, *A Comparison of the Labour Supply Decisions and Wages of Migrant and Australian Born Married Women*, paper presented to the 26th Conference of Economists, Economic Society of Australia, University of Tasmania, Hobart, 30 September to 1 October.

4. Boyton, A. 1997, *Liberalisation of Foreign Investment in the Australian Financial Sector*, paper presented to the 26th Conference of Economists, Economic Society of Australia, University of Tasmania, Hobart, 30 September to 1 October.

Copies of these articles are available from the Treasury. Written requests should be sent to The Office Manager, Economic Division, The Treasury, Parkes Place, Parkes, ACT, 2600. Telephone requests should be directed to Antonietta Caggiano on (02) 6263 2932.

A Summary of Australia's Foreign Investment Policy

A general summary of policy and a summary specifically related to real estate are available from the Executive Member, Foreign Investment Review Board, The Treasury, Canberra, ACT, 2600 (Phone (02) 6263 3795; Fax (02) 6263 2940).

These policy summaries are also available on the Internet. Copies may be downloaded from the Treasury web site (http://www.treasury.gov.au).

Pre-Budget Submissions 1997-98

The *Pre-Budget Submissions 1997-98: Individuals and Business, Community and Labour Organisations* was published in April 1997. The publication contains an overview and summaries of Pre-Budget submissions received by Treasury for the 1997-98 Budget.

Copies may be downloaded from the Treasury web site (http://www.treasury.gov.au).

Copies can be purchased from your local Government InfoShop (formerly the Commonwealth Government Bookshops) — **for InfoShop locations and further information phone toll free on 132 447.**

Publications by the Business Law Division

1. *Section 52 Trade Practices Act and Dealings in Securities* was published in March 1997. This report deals with the application of Section 52 of the *Trade Practices Act* to prospectuses and other aspects of dealing in securities.

2. *Corporate Law Economic Reform Program* was published in March 1997. This document outlines the strategies to be employed to improve the content and implementation of Australia's Corporate Law to promote business and economic development.

3. *Corporations Law Amendment (ASX) Bill 1997* was published in August 1997. This booklet lists proposed amendments to the Corporations Law for the regulation of stock markets consequential on the proposed change of company type of Australian Stock Exchange Limited.

4. *Review of the Regulation of Corporate Insolvency Practitioners — Report by the Working Party* was published in June 1997. This report examines matters of key importance to corporate insolvency practitioners including regulatory structure, criteria for registration, appointment and remuneration and complaint procedures and remedies. The key findings and recommendations made by the working party include proposed measures to increase competition, remove barriers to entry, reduce administration costs and streamline reporting requirements.

5. *Review of Requirements for the Registration and Regulation of Company Auditors — Report of a Working Party of the Ministerial Council for Corporations (MINCO)* was published in July 1997. This publication reports the findings of the working party which reviewed the regulation of company auditors with a view to ensuring that an appropriate legal framework is in place for the registration, appointment, supervision and disciplining of company auditors in relation to their functions under the Corporations Law and to ensure their independence.

6. *Accounting Standards, Corporate Law Economic Reform — Program Proposals for Reform Paper No. 1* was published in September 1997. This document contains proposals for the reform of the accounting standard setting framework in Australia to give greater recognition to the impact of Australian accounting standards on the economic efficiency and competitiveness of Australian firms.

7. *Fund Raising, Corporate Law Economic Reform Program — Proposals for Reform Paper No. 2* was published in October 1997. This document sets out proposals for reforms designed to significantly reduce the cost of fundraising by Australian companies while maintaining an appropriate investor protection.

8. *Directors' Duties and Corporate Governance, Corporate Law Economic Reform — Program Proposals for Reform Paper No. 3* was published in October 1997. This document sets out proposals for reforms designed to facilitate the management of corporations through clarifying the role of directors and improving management's responsiveness to shareholders.

9. *Corporations Agreement* was published in October 1997. This Agreement, between the Commonwealth and the States and Northern Territory, underpins the national scheme for the regulation of companies and securities in Australia.

Copies may be downloaded from the Treasury web site (http://www.treasury.gov.au).

Copies of these publications can be purchased from your local Government InfoShop (formerly the Commonwealth Government Bookshops) — **for InfoShop locations and further information phone toll free on 132 447.**

Treasury Macroeconomic (TRYM) Model — Public Release

Licensed access to the Treasury macroeconomic (TRYM) model on computer disk is available for purchase — either on a single issue basis or on subscription which involves quarterly updates.

There are two versions of the TRYM model: a TSP version, and a stand-alone Windows version. The TRYM data base is also available as a separate product.

The **stand-alone version** has the model (equation, parameter and data base files) incorporated in computer software to run the model. The software simulates the model and presents results in Windows format. It allows the concurrent use of time series data bases and multiple data views and graphs, facilitating comparison of different model scenarios. Graphs and data derived from TRYM data bases and simulations can also be pasted into other Windows applications, such as spreadsheets and word processing documents.

The **TSP version** has the model in a format compatible with the Time Series Processor econometric package, a copy of which will be needed to run the model. Although running simulations with the TSP version demands more expertise than does the stand-alone version, the TSP version allows access to TRYM equations and parameters. It therefore provides flexibility for research into individual equations and model sectors, as well as experimentation with model specifications, assumptions and solutions.

Each version comes with a user's guide specific to that version, documentation of the data base and two other manuals:

- a new version of the TRYM documentation which provides a detailed description of the model, incorporating the specification and diagnostics of individual equations (including those added, changed or updated since the 1993 conference); and
- *The Macroeconomics of the TRYM Model of the Australian Economy*, which describes the theoretical macroeconomic mechanisms and interrelationships underlying TRYM and discusses how TRYM relates to some macroeconomic issues of interest.

The latter two manuals are available for separate purchase from the Treasury. Telephone requests can be directed to Lea Buckton on (02) 6263 3273.

Requests for information on the public release of TRYM in computer-accessible form should be directed to:

TRYM Contact Officer
Analytical Services Section
Australian Bureau of Statistics
PO Box 10
BELCONNEN ACT 2616
Phone: (02) 6252 6122
Fax: (02) 6253 1033

TRYM Related Papers

1. Antioch, L. & Taplin, B. 1993, *Savings, Dwelling Investment and the Labour Market: Decisions by Households*, TRYM Paper No. 5, Commonwealth Treasury, Canberra.

2. Ryder, B., Johnson, A., Taplin, B. & Jilek, P. 1993, *Australia's Trade Linkages with the World*, TRYM Paper No. 6, Commonwealth Treasury, Canberra.

3. Taplin, B. & Parameswaran, P. 1993, *Employment, Investment, Inflation and Productivity: Decisions by the Firm*, TRYM Paper No. 3, Commonwealth Treasury, Canberra.

4. Jilek, P., Johnson, A. & Taplin, B. 1993, *Exports, Imports and the Trade Balance*, TRYM Paper No. 4, Commonwealth Treasury, Canberra.

5. Downes, P., Louis, C. & Lay, C. 1994, *Influences on the Australian Business Cycle*, paper presented to the 23rd Annual Conference of Economists, Economic Society of Australia, Gold Coast 25-28 September.

6. Johnson, A. & Downes, P. 1994, *The Impact of a Lower NAIRU on the Australian Macroeconomy — Responses in the Treasury Macroeconomic (TRYM) Model*, paper presented to the 23rd Annual Conference of Economists, Economic Society of Australia, Gold Coast, 25-28 September.

7. Johnson, A. & Louis, C. 1994, *An Analysis of the Macroeconomic Effects of Higher Productivity Using the TRYM Model*, in EPAC 1994, *A Comparison of Economy-Wide Models of Australia*, Office of the Economic Planning Advisory Council, Commission Paper No. 2, AGPS, Canberra.

8. Downes, P. 1995, *An Introduction to the TRYM Model: Applications and Limitations*, paper presented to the International Federation of Automatic Control (IFAC) Symposium, ‘Modelling and Control of National and Regional Economies’, Gold Coast, 2-5 July.

9. Edge, R. 1995, *Modelling Import Prices in the Treasury Macroeconomic (TRYM) Model*, paper presented at the Econometrics Conference, Monash University, 13-14 July.

10. Gardner, R. 1995, *Consumption and Saving in the TRYM Model*, paper presented to the 24th Annual Conference of Economists, Economic Society of Australia, Adelaide, 24-27 September.

11. Lay, C. & Johnson, A. 1995, *The Relative Price Block in the Treasury Macroeconomic (TRYM) Model*, paper presented at the Econometrics Conference, Monash University, 13-14 July.

12. Louis, C. 1995, *Control Applications of the TRYM Model*, paper presented to the International Federation of Automatic Control (IFAC) Symposium, ‘Modelling and Control of National and Regional Economies’, Gold Coast, 2-5 July.

13. Stacey, G. & Downes, P. 1995, *Wage Determination and the Labour Market in the Treasury Macroeconomic (TRYM) Model*, paper presented to the 24th Annual Conference of Economists, Economic Society of Australia, Adelaide, 24-27 September.

14. Louis, C. 1996, *A Rational Expectations Solution Method for the TRYM Model*, paper presented at the Econometric Society Australasian Meeting, University of Western Australia, 10-12 July.

15. Downes, P. & Stacey, G. 1996, *The NAIRU in the Treasury Macroeconomic (TRYM) Model of the Australian Economy: Definition, Measurement and Policy Implications*, note prepared for input into the OECD Economic Policy Committee Working Party 1, Programme of Work, Autumn 1996, Topic A.2, NAIRU: Concepts, Measurement and Policy Implications, Commonwealth Treasury, Canberra.

16. Downes, P. & Louis, C. 1996, *Monetary Policy in the TRYM Model: Uncertainty, Expectations and Policy Credibility*, paper presented to the Economic Modelling Bureau of Australia (EMBA), Model Comparison Conference, 'Monetary Policy: Price Level and Inflation Targeting', Canberra, 23 May.

17. Douglas, J., Thompson, H. & Downes, P. 1997 *Modelling the Exchange Rate and Commodity Prices in the Treasury Macroeconomic (TRYM) Model*, paper presented to the 26th Annual Conference of Economists, Economic Society of Australia, Hobart, 29 September to 1 October.

18. Jovanoski, S., Stoney, N. & Downes, P. 1997 *Modelling the Dwelling Cycle in the Treasury Macroeconomic (TRYM) Model*, paper presented to the 26th Annual Conference of Economists, Economic Society of Australia, Hobart, 29 September to 1 October.

19. Downes, P. 1997, *The Treasury Model and the Business Cycle*, paper presented to the Melbourne Institute of Applied Economic and Social Research Conference, 'Business Cycles: Policy and Analysis', Melbourne, 5 September.

Copies may be downloaded from the Treasury web site (http://www.treasury.gov.au/Publications/TRYM).

Copies of TRYM related papers can be obtained from the Treasury. Written requests should be sent to The Director, Modelling Section, The Treasury, Parkes Place, Parkes, ACT, 2600. Telephone requests should be directed to Antonietta Caggiano on (02) 6263 2932.

Publications by the Retirement Income Modelling Task Force

The views expressed in these papers are those of the authors and do not necessarily reflect the views of the Departments financing the RIM Task Force or of their Ministers or advisers.

Technical Papers

1. Bacon, B. 1994, *RIM Population and Demographic Modelling*, Working Paper No. 2.
2. Osborne, S. 1994, *The RIP Model: System Documentation*, Working Paper No. 3.
3. Rothman, G. 1994, *The RIP Model: Parameter Documentation*, Working Paper No. 4.
4. Rothman, G. 1994, *The RIP Model: User Manual*, Working Paper No. 5.
5. Brown, C. & McDiarmid, A. 1995, *Legislative References & Assumptions for RIMHYPO*, Technical Paper No. 1.
6. Brown, C. & McDiarmid, A. 1995, *RIMHYPO: An Outline of the Code*, Technical Paper No. 2.
7. 1995, *INDMOD VERSION 3.2: Operating Instructions*, Working Paper No. 2.
8. Rothman, G. 1995, *Estimating Superannuation Parameters for the Self Employed*, Working Paper No. 4.
9. Bacon, B. 1996, *Pensioner's Share of Wealth: An Income Distribution Survey Analysis*, Working Paper No. 1.

Conference and Other Papers

1. Brown, C. 1993, *Tax Expenditures & Measuring the Long Term Costs & Benefits of Retirement Incomes Policy,* Conference Paper No. 1.
2. Gallagher, P., Rothman, G. & Brown, C. 1993, *Saving for Retirement: The Benefits of Superannuation for Individuals and the Nation*, Conference Paper No. 2.
3. Gallagher, P. & Dr Preston, A. 1993, *Retirement Income Modelling & Policy Development in Australia*, Conference Paper No. 3.
4. 1994, *Response to the Senate Elect Committee on Superannuation for Analysis of the Effects of Allowing Withdrawals from Superannuation Funds for Housing Deposits*, Retirement Income Modelling, Paper No. 1.
5. McDiarmid, A. 1994, *Taxation of Superannuation and Disposable Income in Retirement*, Women & Superannuation Seminar, Conference Paper No. 1.
6. Brown, C. 1994, *The Distribution of Private Sector Superannuation Assets by Gender, Age and Salary of Members*, Conference Paper No. 2.
7. Rothman, G. & Bacon B. 1994, *The Impact of Population & Labour Force Scenarios on Superannuation, Tax Expenditures & Pension Costs*, Colloquium of Superannuation Researchers 1994, Melbourne, Conference Paper No. 3.
8. Gallagher, P. 1994, *Submissions to the Strategic Review of the Pensions' Income & Assets Test*, Retirement Income Modelling Paper No. 2.
9. Brown, C. 1995, *Measuring the Adequacy of Retirement Incomes*, Colloquium of

Superannuation Researchers, University of Melbourne, July 1995, Conference Paper No. 1.

10. Rothman, G. 1995, *The Distribution of Superannuation by Sector, Account Type and Personal Characteristics*, Colloquium of Superannuation Researchers, University of Melbourne, July 1995, Conference Paper No. 2.

11. Gallagher, P. 1995, *The Policy Use of the Products of the Retirement Income Modelling Task Force*, Colloquium of Superannuation Researchers, University of Melbourne, July 1995, Conference Paper No. 3.

12. Bacon, B. 1995, *Projecting Labour Force, Earnings, Assets and Retirement Behaviour*, Conference Paper No. 4.

13. Bacon, B. 1995, *Labour Force Status, Earnings, Asset Accumulation, Retirement Behaviour and Long-Run Projections*, Conference of Economists, Adelaide 24 September 1995, Conference Paper No. 5.

14. Bacon, B. & Gallagher, P. 1995, *Early Retirees — Trends and Their Use of Superannuation Benefits and Social Security Payments*, Retirement Income Modelling Task Force, DSS Seminar on Early Retirement, 14 December 1995, Conference Paper No. 6.

15. Gallagher, P. 1995, *The Impact of the New Superannuation Scheme on Long-Term Personal Savings*, Retirement Income Modelling Task Force, 8 November 1995, Conference Paper No. 7.

16. Bacon, B. 1996, *Retirement in Australia: A model of retirement — 'RETMOD'* Retirement Income Modelling Task Force, Fourth Annual Colloquium of Superannuation Researchers, University of Melbourne, 11-12 July 1996, Conference Paper No. 1.

17. Brown, C. 1996, *Sources of income and the assets of older Australians*, Retirement Income Modelling Task Force 1996, Fourth Colloquium of Superannuation Researchers, University of Melbourne 11-12 July 1996, Conference Paper No. 2.

18. Rothman, G. 1996, *Aggregate and Distributional Analysis of Australian Superannuation Using the RIMGROUP Model*, Retirement Income Modelling Task Force, Fourth Colloquium of Superannuation Researchers, University of Melbourne, July 1996, Conference Paper No. 3.

19. Bacon, B. 1996, *An Ageing Society: A Working Life/Retirement Perspective*, The Eighth National Conference of the Australian Population Association, 3-6 December 1996, Conference Paper No. 4.

20. Brown, C., 1997, *Preservation and the Effectiveness of Retirement Incomes Policy — Some Results of Individual Modelling*, Retirement Income Modelling Task Force, Fifth Colloquium of Superannuation Researchers, University of Melbourne, 11-12 July 1997, Conference Paper No. 1.

21. Rothman, G. P., 1997, *Aggregate Analyses of Policies for Accessing Superannuation Accumulations*, Retirement Income Modelling Task Force, Fifth Colloquium of Superannuation Researchers, University of Melbourne, June 1997, Conference Paper No. 2

22. Gallagher, P., 1997, *Assessing the National Saving Effects of the Government's Superannuation Policies Some Examples of the New RIMGROUP National Saving Methodology*, Retirement Income Modelling Task Force, Paper No. 3

Copies of these articles are available from the Treasury. Written requests should be sent to The Director, Retirement Income Modelling Task Force, The Treasury, Parkes Place, Parkes, ACT, 2600. Telephone requests should be directed to Kay Hutchins on (02) 6263 3934.