

## **Council for the National Interest**

### **Productivity Commission - Draft Report**

**Hearing 20 Dec 2004**

This report is essentially two things. It is a progress report, and it is a plea for its continuing existence.

The Commission's case is weak and unproven. It has achieved many good things, but its time has come. It should pack up and go home.

The writing is on the wall. The Prime Minister has taken the productivity incentive payments for the next two years away for another purpose. CoAG will not change this.

The great contribution of the Commission is the very big change of attitude of governments and the community towards National Competition Policy and its benefits.

The great harm done by the Commission stems from its nature. The Commission is driven by economic fundamentalists. Like religious and other fundamentalists their virtue is in reminding us of higher ideals. Their crippling defect is their remoteness from reality and their slavish adherence to dogma.

The consequential detriment to the community of the Commission's competition policy is not understood or appreciated by the Commission. **'Nothing must stand in the way of Competition. This is the Holy Grail.'** seems to be the mantra, regardless of the consequences.

The Commission's zealous insistence upon competition above all else with sometimes scant regard for the impact and consequences of their actions is classic fundamentalist behaviour. Many people think this is dangerous.

Some observers might say that the rationalisation of the dairy industry is a classic example of the extremism of the Commission. There is no doubt that the archaic pricing practices in NSW had to be changed but the total hurt to communities across Australia was not warranted. Has the retail price of milk to the consumer been significantly lowered and staying low? The answer to the question is NO.

#### **Electricity Supply**

Of far more significance is the electricity supply industry.

To quote from p 162 of the Report. "Reliable, affordable and sustainable energy services are critical to Australia's economic and social wellbeing. They are an important input for most businesses and are essential for supporting basic quality of life."

As a direct result of following the Commission's fanciful and ridiculous fetishes about fragmentation and competition the electricity supply situation across Australia is now an imminent disaster.

Threats of shutdowns, brownouts and power failure are common and universal. How the communities will suffer in this coming summer remains to be seen. What is fundamentally clear is that there is a gross shortage of generating capacity and the situation is going to get worse before it gets better, due to the long lead times necessary to increase generating capacity.

This shortfall has occurred because there has been an enormous reluctance by the players to spend funds on capital works and ongoing maintenance. Competition and profits have been the drivers. This massive underspend on capital works will take years to correct and who in the fragmented industry will pay for it?

There has also been a huge underspend of capital on the critical transmission and distribution networks.

The following extracts from industry submissions are very revealing.

Electricity Users Association, Sub123

*However our view is that since 2000-01 large business users have experienced increases in electricity prices across all States, to the extent that most of the benefits derived early on have been dissipated. -----is likely to lead to price increases of up to 35% for some large end users over the next five years in NSW.*

*Overall by 2012, electricity prices could be over 60% above levels at the beginning of deregulation reforms in 1998.*

*While tariffs in Qld and NSW have continued to remain moderate, those in Victoria and especially South Australia have risen strongly. With 45% increases in industrial/commercial tariffs applicable in South Australia from mid-2001 and 30-35% increases in domestic tariffs expected from the start of 2003, and with further pressure to come on Victorian retail tariffs,----*

*---base load capacity--- there is the real risk for end users that appropriate generation investment will not occur or will be delayed. This will leave end users to foot the bill of higher than necessary prices and/or lower levels of supply. We understand that a Delta/NEMMCO forthcoming paper suggest concerns about the ability of the NEM to deliver timely base load capacity.*

Energy Supply Assoc. Sub 94.

*In terms of new investment, the energy sector has significant hurdles ahead.*

*--- almost \$ 40 billion of new investment will be required in meeting our stationary energy supply requirements over the next ten years*

*Ultimately retail prices that are set below the cost of supply will have a dampening effect on investment. ---over time investors will have little incentive to invest in new assets, raising the possibility of supply shortages.*

### Comment

It is too easy to nod at the figure of \$40 billion and to move on, without appreciating the magnitude of what it means. Other industry sources estimate that 80Bn\$ - 90Bn\$ needs to be spent on capital infrastructure electricity projects in the next 5 years. Both these figures are quite extraordinary.

Note that in 2003 total expenditure in Australia, on all resource industries – minerals, processing and energy, was \$20 billion.

Even allowing for growth in demand these figures clearly show the huge backlog in capital expenditure.

There is a lack of confidence in the industry. Perhaps the appointment and sacking in rapid succession of the CEO in WA and the tragic death of the CEO in Qld are symptomatic of this condition.

The people of Australia are going to suffer from a shortage of a basic necessity of life as a direct consequence of the short sighted and simplistic policies of the Commission.

### **Conclusion**

The nation has benefited from the initial work of the Commission. But it is now doing more harm than good. The economic fundamentalists have shown us the dangers of narrow outlooks pursued by zealots. It is now time for the Commission to close down.

It will take many years for the electricity supply industry to recover from the damage caused by the policies of the Commission. The focus on competition has prevented the necessary capital expenditure on generating capacity, transmission and distribution networks. The required spending on capital works is enormous.

It will be interesting to see how long it takes for there to be a guaranteed supply of a basic necessity of life.

## **Supplementary Submission**

### **Council for the National Interest**

#### **Productivity Commission - Draft Report**

At the Perth Hearing on 20 Dec there was possibly some confusion about whether my submission was about the National Competition Council or the Productivity Commission.

Let there be no doubt that my submission was about the Commission; not the Council.

My concerns are about the Commission; its nature and its performance. The Draft Report shows the very narrow approach and attitude of the Commission. The Commission can rightly claim that it is not the executive and therefore the blame lies elsewhere. True, but it is the Commission that makes the bullets for the executive to fire.

I believe there are grave weaknesses in both the competition policy and its implementation.

State governments, the Federal government, and the National Competition Council must also share the responsibility for the terrible situation we are now in.

Probably the biggest culprits are the State governments who have a very short term outlook and who have consistently stripped cash out of the public utilities for short term political gain.

**Something must be done to protect the capital works investment funds of the utilities.**

A possible way is to limit, by law, the maximum percentage of 'profit' that a government may take each year. Annual variations to this, if any, must then be approved by Parliament. There are many examples of the consequences of not protecting the capital works funds, the London Underground is one that comes quickly to mind.

Public utilities, who provide what are now regarded as essentials of life, must be shielded from obsessive short term outlooks. We must find a way to ensure their strategic needs are satisfied.

Dec 04

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On a matter of detail. At page 64 of the review there is Figure 4.2 **Electricity supply reliability. I have some difficulties with this graph.** The graph shows that for the year 00/01 there was a fall of some 50% in the outage frequency (number of occurrences). Statistically this is highly unlikely, you simply do not get changes of that magnitude when dealing with very large numbers. I suspect that either the data base has been changed or the method of measurement has changed. Further I am curious to know how the figures look for the following year. The graph should not stop at June 2002. I suggest the Figure be removed from the Draft Report.