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PUBLIC ENTERPRISES:
A SUCCESS STORY OF MICROECONOMIC REFORM?*

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### Summary

The Evidence on Australian public enterprises is reviewed, and it indicates that performance has been improving markedly, especially since the mid 1980s. In most, though not all cases, total factor productivity growth has been rapid, though in the cases where evidence is available, there is still a considerable gap between productivity levels and those achieved in other countries. There is some evidence of improvements in allocative efficiency, though this is more difficult to systematise. Preliminary analysis suggests that the gains from improved performance are being enjoyed mainly by consumers and that the rates of return of these enterprises have increased by less than might have been expected.

The various types of reform in different enterprises are examined. The most popular reform (and the most amorphous) has been the move to corporatisation - this is continuing. Once off managerial changes and efficiency drives are also common. There are few examples so far of privatisation. There have been some significant moves to open up these enterprises to more competition, though as yet, progress on restructuring the regulatory framework for natural monopoly enterprises has been limited.

Several factors have contributed to the performance improvements. These include structural reforms, such as opening up to competition, monitoring, budgetary factors, external pressures from the private sector, technological change, and macro-economic conditions. The pressure generated by the Microeconomic Reform agenda of governments is important.

While the picture is encouraging, the two main qualifications are, firstly, that productivity growth will need to be high for some time to come for these enterprises to catch up with best practice, and secondly, that a good deal of the performance improvement is due to temporary measures, such as managerial changes, which will not provide continuing pressure for good performance.
1. Introduction

It is becoming evident that economic performance in the public enterprise sector in Australia has been improving markedly. It was generally regarded that there was considerable scope for improvement, but there was no guarantee that this scope would be taken up. Most of the improvement has been in terms of greater productivity, though there have been some changes in other aspects of performance, such as pricing. The performance improvement is quite striking when compared to the productivity performance in the private sector, which in the recent (recession) years has been static or deteriorated. It is also good by international standards, with evidence of greater productivity growth in Australia than elsewhere. The public enterprise sector looks like a success story of Microeconomic Reform.

The interesting aspect of this is that it has been achieved with relatively little change in the institutional structure of the sector. The case for Microeconomic Reform has suggested that structural changes, through increasing competition, through changing ownership (e.g. privatisation) or through altering the relationship between the firm and the government (corporatisation) would be necessary to achieve performance improvements. While there has been some progress in introducing these reforms, it has been slow, and it has been preceded by these performance improvements. This raises the questions of how necessary these structural changes are, and what it is that has induced these performance improvements. It should be recognised that while improvements have been significant, there is still a long way to go.

The Australian experience parallels that of other countries. It has been observed that performance of U.K. public enterprises had been picking up, and that productivity growth had been good compared to the private sector before the institutional structure became subject to much structural change (Molyneux and Thompson, 1987). While much was expected of privatisation as a way of improving productivity, there does not seem to be much correlation between privatisation and improved performance. While privatisation has been
associated with better performance, the firms that were not privatised also improved their performance, in some cases quite spectacularly (Haskett and Kay, 1991). Productivity growth was often rapid before privatisation, as enterprises were prepared for selling off. This is not a complete explanation, however, since enterprises that were not scheduled for privatisation shared the performance improvement. In the British case, these improvements took place against the background of an economy which was generally experiencing a "productivity miracle", and enterprises which remained in the public sector, and those which were privatised, all shared in the "miracle". This suggests that economy-wide determinants were important in explaining the performance of these enterprises. The same types of factors cannot explain what has happened in Australian public enterprises, whose improvements have taken place against a background of a poor productivity growth in most of the rest of the economy.

In this paper, the recent improvements in performance are reviewed first, starting with changes in productive efficiency, and then moving to other aspects such as allocative efficiency. Then the progress on structural changes, such as opening enterprises to competition or changing ownership relations is reviewed. The possible determinants of the performance improvements are examined next. Finally, the current position is reviewed, and the scope for further change is assessed.

2. Assessing Performance in Public Enterprises

Information about public enterprises' performance is improving steadily. The evidence, as of three years ago, is summarised in Forsyth (1989); since then, much has appeared to fill the gaps. The earlier assessments are still valid, but they have been backed up by a good deal more empirical analysis. Some of this has focussed on the actual, past, performance of Australian public enterprises. However, the most important work is that which relates their current performance to that of enterprises elsewhere, and thereby gives some guidance as to what performance levels are likely to be possible. Evidence on this was sketchy a few years back, and while it is far from complete, it has increased significantly.

There has been considerably more interest shown by government bodies on measuring public enterprise performance. Nearly all the studies quoted in Forsyth (1989) assessing performance were by independent academics and consultants - few more by government bodies, such as the Bureau of Transport and Communications Economics. In the period since, many government bodies have turned to performance measurement, notably the Industry Commission (1990, 1991), the Bureau of Industry Economics (1992a,b), the Office of EPAC, the Treasury (1990) and the ABS. A specialist working group, the Steering Committee on National Performance Monitoring of Government Trading Enterprises has been established, and has begun to produce results. Some state governments, such as NSW, have begun to report on performance of their enterprises (NSW Government, 1990).

This interest is having an impact in several areas. One emphasis has been the improvement of accounts and the development of bases for comparisons between enterprises. Another has been the measurement of past financial performance (e.g. BTCE 1990, EPAC, 1990, 1992)Ku, and past productivity performance. There is considerably more available in the way of better measures of productivity, such as total factor productivity, rather than misleading labour productivity measures. There have been several comparative studies between states, and studies which compare Australian enterprises with those overseas. These have usually been on the basis of total factor productivity - there still remain few international cost or production function estimates with Australian observations. This is unfortunate because such studies convey more information about performance than multilateral TFP studies can, as they can allow for factors which differ between observations (e.g. network densities, technology differences) that can influence cost or productivity. There is also very little about where the gains in productivity are going.
The overall picture is one that there are significant gains to be made by improving the efficiency of public enterprises. Some of these gains are currently being achieved, since some of the Australian enterprises are catching up on the best comparable enterprises overseas. In 1989, the (then) IAC made some estimates of what size of impact microeconomic reform, mainly affecting public enterprises, would have on GDP (IAC, 1989). To do this, it needed to make some assumptions about what was possible in individual industries. The research since has confirmed the Commissions' assessments.

The Productivity Performance

Public enterprises have been improving their productivity quite rapidly, compared to other sections of the economy, and enterprises in the same industries overseas. There is some evidence of an increase in the rate of productivity growth over the last few years, though the recession clouds the issue.

The best measure of overall performance is total factor productivity. This is much to be preferred to the more commonly used indicators, such as labour productivity, because it allows for all inputs and outputs. Where enterprises change their ways of doing things, for example by contracting out, ratios of output to labour directly on the payroll are quite misleading. An increase in total factor productivity usually implies that productive efficiency (output per unit of input) has increased. However, given the way output and input indexes are constructed, it can reflect changes in allocative efficiency, for example when price structures change. Another complication is that TFP changes can reflect scale effects (e.g. lower inputs per unit output because of economies of scale). However, in the context of Australian public enterprises, most of the change in TFP reflects productivity efficiency change.

Another caution is that TFP is surprisingly sensitive to the way the constituent output and input indexes are constructed. Assumptions must be made about price movements (e.g. which deflator to use for which cost categories), how to measure capital, and how to measure output. Different approaches can give very different results. For example, consider Telecom's TFP growth between 1980-81 and 1984-85. According to Telecom, it was 3.8% per year (Telecom, 1991) and according to the Industry Commission (1990, p.32) it was 6.1% per year. Both purport to measure the same thing, yet both the input and output measures differ markedly. In short, TFP measures can be quite sensitive to measurement technique and assumptions. Recent measures of TFP in several public enterprises are summarised in Table 1. One observation is that over the 1980s, most industry groups (like electricity) performed better than the non farm market sector as a whole. This is true also for most individual enterprises. The productivity growth record of Australia in general was quite poor in the 1980s, but that of the public enterprises was good, at around 4% PA (EPAC, 1992).

Another observation is that there is little in the way of an industry by industry pattern. High growth rates were achieved by rail systems (A.N. and Queensland), ports (Brisbane) and Telecom. Poor growth rates were achieved in rail (Victoria) airlines (Qantas) and water. High growth rates are not only achieved by industries characterised by rapid technological change (telecommunications, airlines), but they can be achieved by rail systems and ports (and the airline case exhibited slow growth). This suggests that factors such as the competitive and incentive environment that the enterprises work within, and managerial factors, are important.

A third observation is that there does seem to be evidence of an upsurge in productivity growth. TFP growth overall in public enterprises, and in many individual cases, is higher in the second half of the 1980s. For the group as a whole, the growth between 1979/80 and 1984/85 was 2.8% PA, and between 1984/85 and 1990/91 was 5.2% PA (calculated from data in EPAC, 1992). This is the period during which more attention was given to public enterprise performance, and microeconomic reform was being emphasised. When one looks at individual enterprises, there are many examples of recent spurs in performance. Rapid improvements are not confined to the late 1980s - a few enterprises
Table 1

<table>
<thead>
<tr>
<th>Enterprise</th>
<th>Result</th>
<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rail</td>
<td>1979/80-87/88</td>
<td>5.1% Bunker and Gallagher (1991)</td>
</tr>
<tr>
<td>Australian National</td>
<td>1981/82-85/86</td>
<td>5.8% Industry Commission (1990)</td>
</tr>
<tr>
<td></td>
<td>1985/86-88/89</td>
<td>5.8% Steering Committee (1992)</td>
</tr>
<tr>
<td>SRA-NSW</td>
<td>1980/81-90/91</td>
<td>2.1% Steering Committee (1992)</td>
</tr>
<tr>
<td>Qld</td>
<td>1980/81-88/89</td>
<td>0.7% &quot; &quot;</td>
</tr>
<tr>
<td>Westrail</td>
<td>1980/81-88/89</td>
<td>5.4% &quot; &quot;</td>
</tr>
<tr>
<td>Australian National</td>
<td>1980/81-88/89</td>
<td>4.1% &quot; &quot;</td>
</tr>
<tr>
<td>Electricity</td>
<td>1976-83</td>
<td>6.1% &quot; &quot;</td>
</tr>
<tr>
<td>Australia</td>
<td>1983-90</td>
<td>4.42% &quot; &quot;</td>
</tr>
<tr>
<td>Pacific Power (NSW)</td>
<td>1978/79-90/91</td>
<td>1.1% Steering Committee (1992)</td>
</tr>
<tr>
<td></td>
<td>1985/86-90/91</td>
<td>3.1% &quot; &quot;</td>
</tr>
<tr>
<td>Airlines</td>
<td>1974/75-81/82</td>
<td>4.7% Industry Commission (1990)</td>
</tr>
<tr>
<td>Qantas</td>
<td>1981/82-87/88</td>
<td>1.0% &quot; &quot;</td>
</tr>
<tr>
<td>Communications</td>
<td>1975/76-81/82</td>
<td>7.8% Industry Commission (1990)</td>
</tr>
<tr>
<td>Telecom</td>
<td>1981/82-87/88</td>
<td>5.3% &quot; &quot;</td>
</tr>
<tr>
<td></td>
<td>1980/81-90/91</td>
<td>5.6% Telecom (1991)</td>
</tr>
<tr>
<td></td>
<td>1986/87-90/91</td>
<td>7.9% &quot; &quot;</td>
</tr>
<tr>
<td>Australia Post</td>
<td>1976/77-90/91</td>
<td>1.7% Steering Committee (1992)</td>
</tr>
<tr>
<td></td>
<td>1985/86-90/91</td>
<td>2.3% &quot; &quot;</td>
</tr>
<tr>
<td></td>
<td>1975/76-87/88</td>
<td>2.1% Industry Commission (1990)</td>
</tr>
<tr>
<td>Water</td>
<td>1984/85-90/91</td>
<td>0.9% &quot; &quot;</td>
</tr>
<tr>
<td>Melbourne Water</td>
<td>1981/82-90/9</td>
<td>6.3% Steering Committee (1992)</td>
</tr>
<tr>
<td>Posts</td>
<td>1981/82-90/9</td>
<td>7.0% &quot; &quot;</td>
</tr>
<tr>
<td>Port of Brisbane</td>
<td>1985/86-90/9</td>
<td>6.3% Steering Committee (1992)</td>
</tr>
<tr>
<td>Various</td>
<td>1979/80-90/91</td>
<td>3.6% EPAC (1992)</td>
</tr>
<tr>
<td>Electricity, Gas Water</td>
<td>1984/85-90/91</td>
<td>5.0% &quot; &quot;</td>
</tr>
<tr>
<td>Transport Public Enterprises</td>
<td>1979/80-90/91</td>
<td>0.7% EPAC (1992)</td>
</tr>
<tr>
<td></td>
<td>1984/85-90/91</td>
<td>1.6% &quot; &quot;</td>
</tr>
<tr>
<td>Communications</td>
<td>1984/85-90/91</td>
<td>6.5% &quot; &quot;</td>
</tr>
<tr>
<td>Private Non-Farm</td>
<td>1979/80-90/91</td>
<td>0.2% &quot; &quot;</td>
</tr>
<tr>
<td></td>
<td>1984/85-90/91</td>
<td>-0.3% &quot; &quot;</td>
</tr>
</tbody>
</table>

(e.g. Australian National) had performance spurts early in the 1980s.

Evaluating Potential Performance

While past changes of actual performance are interest, they do not tell us much about how current performance compares with the best possible performance, and thus what the gains from reform could be. There have been a few studies which have considerably clarified the picture here. In particular, international comparisons can be used for this purpose. Another way of measuring potential gains is to undertake a detailed study of a specific enterprise, and compare it with another known to be using best practice.

Evidence on the relative efficiency of Australian public enterprises is presented in Table 2. The first study, by the OECD, is widely quoted, though it must be treated with caution. It suggests that the performance the Australian Electricity, Gas and Water enterprises is very poor - about half as productive as the OECD average, which in turn, would be some way off best practice. The transport sector, which includes many public enterprises, was about equal to the OECD average. The results for electricity, gas and water appear to be worse than what one might expect from other studies. In addition, even if they were accurate, electricity enterprises have been improving productivity quite rapidly since these estimates were made.

The most recent assessment of electricity efficiency is that by Swan Consultants (1991) (See also BIE, 1992a). This compared the Australian enterprises with private US electricity utilities; enterprises that could be expected to approximate best practice. By 1990, the Australian industry was achieving TFP of 72% of the US utilities, with Queensland achieving 80% and Victoria 69%. Over the late 1980s, the Australian industry was recording higher TFP growth than the US utilities, but recently, these have increased their TFP growth.

Another industry which has been subjected to international comparisons is rail (see Industry Commission, 1991 and BIE, 1992b). The Industry Commission compared the TFP of different rail systems within Australia and concluded that there were wide differences -
Table 2

Scope for Productivity Improvements: International Comparisons

<table>
<thead>
<tr>
<th>Industry</th>
<th>Australian Performance Relative to International</th>
<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electricity, Gas, Water</td>
<td>53.8% (Capital Productivity) 42.3 (Labor Productivity)</td>
<td>OECD, 1990</td>
</tr>
<tr>
<td>Transport</td>
<td>115.0% (Capital Productivity) 96.0 (Labour Productivity)</td>
<td>1979-85 Comparisons Relative to OECD Average</td>
</tr>
<tr>
<td>Electricity</td>
<td>72% (Australia-Total) 80% (Queensland) 69% (Victoria)</td>
<td>Swan Consultants (1991) Relative to U.S. Private Utilities 1990</td>
</tr>
<tr>
<td>Rail Freight</td>
<td>74% NSW 66% Vic 78% Queensland 82% W.A.</td>
<td>BIE, (1992b) Relative to Best Practice 1990/91</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>71% Telecom</td>
<td>MONICT (1990) Relative to Comparable US, Swedish Systems</td>
</tr>
</tbody>
</table>

TFP in Victoria was only 35% of that achieved in Queensland. It estimated that if all systems achieved Queensland TFP levels in 1988/89, costs of $2,040m would be saved (relative to operating expenditure of $5551m). Detailed studies of possible efficiency improvements within individual rail systems indicated that costs overall could fall by 30%. The BIE reports on the possible gains from achieving best practice in rail freight (i.e. excluding passengers). Again, there was considerable variation between states, with best practice leading to costs 66% of Victoria's, and 82% of Western Australia's. Three of the four systems examined have also achieved significant TFP growth recently. Across the country, improvements in TFP of around 33% would seem feasible.

An international comparison of costs for Telecommunications (MONICT, 1990) was based on detailed comparisons of Telecom with Swedish and US telecommunications enterprises. It concluded that Telecom's unit costs were about 40% higher than those achieved by these enterprises. Allowance was made for the lower density of the Telecom network, but it was concluded that this could not explain more than one third to one half of the cost difference.

An industry which has not been subjected to detailed international comparison lately is the airline industry. Some of the earliest comparisons between international and Australian performance, using TFP and cost functions, were done for airlines - however, little work has been done lately. These studies (e.g. Findlay and Forsyth, 1984, Kirby, 1984 and Forsyth, Hill and Trengove, 1986) suggested that substantial TFP gains were possible for both Qantas and Australian Airlines. Until the late 1980s, there was little evidence of rapid productivity growth (labour productivity grew quite slowly) and the assessment would remain unaltered. Recently, there have been productivity drives in both airlines, though data are not yet available to evaluate their results. It is worth noting that the new entrant, Compass, was able to achieve significantly lower costs than the other domestic airlines (BTCE, 1991), which suggests that there remains scope for productivity improvement.
The studies covered here cover some important areas, though they are far from comprehensive. There are a number of public enterprises for which evaluations of potential performance, based on international best practice, are not available - some of these are in important industries, like gas and water. With other industry sectors, such as urban buses, there are a number of interstate or public-private comparisons which suggest that there are substantial efficiency gains to be made in some systems. Most of the studies so far have been on the basis of comparisons of TFP, which cannot allow for different conditions, technology and output mixes. It is possible to allow for these through cross-section estimates of cost or production functions; this has been done for airlines, though not for other industries. It is an obvious next step, since the results of cost function studies are more reliable than comparison of TFP as they can allow for more variables. They do require considerable amounts of data; however enough data are available for cost function estimates in some industries, rail for example.

Recent work has confirmed earlier beliefs about the scope for productive efficiency improvements in Australian public enterprises. For those industries which have been studied in detail - electricity, rail, telecommunications and airlines, the potential gains are substantial, being over 25% in all cases. In each of these industries except airlines, there has been good TFP growth in recent years, and so a catch up process is at work. It still has a considerable way to go.

Productivity Growth: Where it comes from, Where it goes.

Most of the attention in monitoring so far has been concentrated on measuring productivity and its change. There has been little in the way of analysis of how it is being achieved, and where the benefits of it are going. There are some interesting patterns emerging, and it worthwhile examining them briefly.

Over the recent period (1984/85 to 1989/90) the output of the Communications and Electricity Gas and Water sectors have been growing more rapidly than the rest of the non-farm market sector. Communications grew by 54.4%, Electricity Gas and Water by 25% and the rest of the Non firm sector by 21.3% (ABS, 1992). Growth in the transport public enterprises was probably about the same as that in the non farm sector on average. This growth was achieved with a small increase in the capital stock; the result was that capital productivity (25.6% for Communications and 19.2% for Electricity Gas and Water, 1984/85-1990/91) grew a little less than output (EPAC, 1992). During this period, labour productivity grew rapidly 59.3% for Communications and 53.0% for Electricity Gas and Water (EPAC, 1992). The result was that there was a slight increase in labour input in Communications, and a significant reduction in Electricity Gas and Water (to 87.2% of 1984/85 levels by 1989/90 - ABS 1992). There was probably a small increase in labour input in the transport enterprises. Overall, recent productivity growth has been achieved with a moderately high increase in output, but some overall reduction in labour.

This pattern can be expected to continue. Labour productivity in the electricity industry in the US is much higher than in Australia (Swan Consultants, 1991) and moves to achieve US TFP levels would imply large reductions in labour input per unit of output. To an extent this would be achieved through contracting out, and thus the impact on the labour market would not be as severe as it seems. In rail, labour productivity is low in the Australian systems as compared to the US systems, suggesting that cost reductions will need to be achieved through reductions in the labour force (BIE 1992). This reduction in labour force seems to be generally accepted (Rail Industry Council, 1990). Even in rapidly growing areas like telecommunications, output increases are being achieved in spite of labour force reductions (Telecom, 1991). If anything, the pace of labour shedding is likely to increase in the early 1990s, especially if GDP growth is weak.

This pattern may have an influence on where the gains from productivity growth are going. They do not appear to be going to the labour force. Those who lose their jobs are usually worse off, but there is no evidence of those remaining gaining much. Over the
period 1984/85 to 1989/90, hourly earnings rose 39.1% in the rest of the non-farm market sector, but only 35.9% in Electricity Gas and Water and 37.1% in Communications (the price deflator for the non-farm market sector rose 38.5%) (ABS, 1992). Averages may mask larger changes in relativities if those who keep their jobs were more skilled, the relative decline in earnings would have been greater. In short, there has been a slight decline in relative, and real wages, in these two sectors, dominated by public enterprises experiencing good productivity growth.

Most of the recent gains in productivity have been applied to price reductions and improvements in the rate of return for the enterprises. Again looking at the Electricity Gas and Water and Communications sectors, over the period 1984/85 to 1989/90, output prices relative to those of the total non-farm market sector fell to 86.9% and 80.3% (ABS, 1992). (See Table 3). The gross rate of return rose from 4% to 4.5% for the (highly capital intensive) Electricity Gas and Water sector and from 8.1% to 9.6% in Communications (ABS, 1992). If output prices had been held constant relative to those of the non-farm market sector, and labour costs had been as actually recorded, these rates of return would have increased to 5.5% and 14.3% respectively (Table 3). This suggests that of the TFP growth, approximately 25-33% was applied to increasing the rate of return, and the remainder was applied to output price reductions.

This is an interesting result, given the emphasis being put on improving the financial results of public enterprises. There have been phases in enterprises where the bulk of productivity gains have been applied to increasing the rate of return - for an example, in Telecom between 1981-82 and 1987-88 (Industry Commission, 1990, pp.33-34). Within individual enterprises there will be limits to this - when rates of return become quite good, it may be politically difficult to increase them more, and so productivity increases need to be passed on in price reductions (OTC being the exception here). Consistent, and long, series of rates of return are not easy to come by. Data collected by EPAC (1990, 1992) suggest a

<table>
<thead>
<tr>
<th></th>
<th>Communications</th>
<th>Electricity, Gas, Water</th>
<th>Res of Non-Farm Market Sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>Implied Average Hourly Earnings, 1989/90</td>
<td>137.1</td>
<td>135.9</td>
<td>139.1</td>
</tr>
<tr>
<td>Implicit Price Deflator for Gross Product 1989/90, 1984/85 = 100</td>
<td>109.4</td>
<td>118.3</td>
<td>138.5</td>
</tr>
<tr>
<td>Gross Operating Surplus/Capital Stock, 1989/90</td>
<td>4.5</td>
<td>9.6</td>
<td></td>
</tr>
<tr>
<td>Potential Gross Operating Surplus/Capital Stock, 1989/90</td>
<td>5.5</td>
<td>14.3</td>
<td></td>
</tr>
</tbody>
</table>

gradual improvement in rates of return in aggregate. However, when individual sectors are examined, results can be surprising; in spite of achieving high productivity growth recently, the electricity industry rates of return have not been increasing significantly, even though they are quite low. Studies of specific industries, such as rail (BTCE, 1990, LC, 1991) indicate a gradual improvement in rates of return, though not for all systems. A further qualification is that some enterprises, notably the water authorities, have levied other charges, such as "environmental levies", which do not get counted as price increases, yet which add to cash flow (see Walker, 1992). These levies can be quite substantial, and it may be that normal price increases have been moderated to lessen the impact on consumers. Normal accounts may thus understate the actual financial rates of return. In addition, depreciation practices may result in returns being understated (Walker, 1992).

Overall, given the emphasis on achieving "commercial" results and cost recovery, the movements in profitability and rates of return in public enterprises has been slower than would have been anticipated. Even where rates of return are low, there have been examples of moderate to high productivity growth which have been applied to output price reductions rather than to increasing the rate of return. Productivity improvements in recent years have been sufficient to have facilitated a much greater increase in rates of return than have been achieved. This highlights just how unsatisfactory rates of return are as a measure of performance.

Allocative Efficiency: Improvements and Potential

In recent discussion and assessment of public enterprises, by far the most attention has been focussed on productive efficiency aspects, and to a limited extent, financial aspects. There has been quite little discussion of allocative efficiency, including the efficiency of price structures and levels, and investment policy. A number of the reports which have examined the case for reform have given some attention to allocative efficiency aspects. For example, the MONICT report (1990) on Telecommunications, confirmed earlier views that the Telecom price structure was deficient. It also argued that Telecom was somewhat behind other systems in the introduction of new technology; it is possible that this has been because Telecom's investment program has been constrained, as Telecom has argued. Pricing and investment is important in the Electricity industry, and indicators reported (BIE 1992b) suggests that more efficient patterns of investment and pricing are possible. The Australian systems have fairly low capacity factors, high reserve plant margins, moderate availability factors and not very high reliability. These indicate excess investment in capacity, and not very effective use of existing capacity. It may take some time to correct these, as they are partly the result of the excessive investment in the early 1980s. These can be corrected with better pricing and investment criteria; it is too early to tell whether better investment criteria are being used, but there is clear room for improved price structures. Possible improvements in allocative efficiency in Rail were outlined by the Industry Commission (1991).

In a number of industries there have been improvements in pricing. A simple, yet effective, example arises with the peak surcharge being imposed at Sydney airport. Pricing structures for ports are being revised. Competition in the domestic airline industry has induced Australian Airlines to adopt a more demand responsive price structure, and to pay more attention to the leisure market. Competition in telecommunications is inducing Telecom to alter its price structure, and when Optus is an effective competitor, the prices of long distance calls, currently well above costs, can be expected to fall. Water authorities are gradually moving towards charging for water, rather than relying on water rates to cover their costs.

Improvement in investment practices are slow to have an impact, and even then, they need not be obvious from the performance data. The greater emphasis on cost recovering profits targets and corporatisation may be leading to more rigorous assessment of
investments. Administrative changes, like the formation of the Rail Freight Corporation, may lead to better investment criteria. Nevertheless, governments still do exercise considerable control over investment, as the promises of the ‘One Nation’ statement indicate, and the federal governments making availability of rail investment funds conditional on industrial relations reforms indicates.

3. Structural Reform of Public Enterprises

Suppose that the key objective of reform of public enterprises is to increase economic (i.e. productive and allocative) efficiency. There are several ways in which this can be done, but they can be categorised. Two broad approaches are as follows.

(a) Directly measuring efficiency, or proxies for it, and rewarding good performance according to these measures.

(b) Measuring profit, and rewarding good performance according to it, but constraining the use of market power by the use of competition or regulation.

The first of these ways has been frequently discussed, though it is rarely, if ever, implemented, except in the trivial case where, under perfect competition, profit can be used as a measure of welfare. The objective behind these measures (Scott 1978, Loeb and Magat 1979, Finsinger and Vogelsang, 1982, Gravelle, 1982; Sappington and Sibley, 1988) is to develop an indicator of overall economic (producer’s and consumer’s) surplus, or the change in it, which could be used as a basis on which to reward managers. Managers would then seek to maximise efficiency; and would refrain from exploiting the firm’s market power. In principle, some of these measures should be simple to quantify (for an application to Qantas, see Forsyth 1992a), but they have not found favour. Perhaps this is because it is always easier to focus on something which is directly measurable (profit) and construct control systems for public enterprise around them than to rely on non-measurable concepts, such as overall surplus.

Most of the practical attempts to improve performance are examples of the second method. There are several ways of getting a firm to maximise profits - one is to privatise it, and another is to corporatised it, setting profit as the sole objective, and rewarding management performance according to profit. Where competition is strong, no further regulation need be present, however where there is market power, some system of regulation, such as price caps, would be called for. (For a discussion, see Forsyth, 1992b). Additional objectives can be allowed for by contracting with the enterprise to address them - for example, it can be induced to perform community service obligations by payment of subsidies.

Most of the mechanisms in place in Australia to encourage better performance by public enterprises are close or distant approximations to this structure. There are few, if any examples of public enterprises which are encouraged to maximise profits, however, some are set profits targets, and others are explicitly directed to give considerable weight to their rate of return. Several are being corporatised and are being instructed to be more commercially oriented. A few are being partially privatised. Competition is being permitted for some public enterprises, though sometimes competition is only permitted for part of their product range or operations. A few enterprises are now subject to general regulatory bodies, such as the Trade Practices Commission. In some cases, natural monopoly problems are being addressed by direct regulation of price behaviour. All of these devices represent the implementation of structural reforms, which may be thorough going, or superficial. Apart from this, enterprises are being subjected to ad hoc, non structural influences such as management changes and efficiency drives.

In evaluating how substantial or otherwise reforms have been, there are two central questions that must be answered. The first is - how strong and explicit is the pressure on management to achieve the stated objectives? The second is how effectively is the use of market power constrained? The answer to the first question tells how hard the management
will be induced to seek cost minimisation and efficient price structures, whereas the second tells how effectively price levels will be kept at efficient levels.

**Patterns of Reform.**

In Table 4, reforms that have been taking place in a range of industries where public enterprises are significant are identified. For specific industry case studies, see Dick, 1992 forthcoming (Shipping and Ports) Forsyth 1992 forthcoming, (Land Transport) and Maddock, 1992 forthcoming (Telecommunications). Several reforms are considered one of these, privatisation, is not strictly a "public enterprise" reform since it involves a shift of an enterprise out of the public sector. Nevertheless, it is included for completeness, and because it can be a response to a public enterprise performance problem. At the other end of the scale, a managerial change or an efficiency drive is not a structural reform in the sense that it permanently affects the environment in which the enterprise operates.

In a single table it is not possible to capture all that is going on at Federal and State levels. In some cases, the policies being adopted by one State differ markedly from those by other states. The list of industries includes most of those for which public enterprises are significant players. An indication of the significance or extensiveness of reform is given. This is based on judgement. A small change could encompass a major change in part of a system (e.g. privatisation of some electricity generation stations in some States) or a limited change across the board (allowing competition for some telecommunications services across Australia). In some cases, changes such as privatisation have been foreshadowed (e.g. airlines) and are likely to take place these are noted.

**The Reforms in Detail**

**Privatisation**

Australian governments have generally been reluctant to privatise core public enterprises (Domberger, 1992 forthcoming). They have privatised industrial enterprises (such as factories or dockyards) and real estate, though there have been few examples of
privatisation of core public enterprises. Indeed, the enterprises which have been, or are planned to be, privatised are generally those which operate in fairly competitive markets, such as airlines and shipping lines or are secondary producers, such as Ausgrid. Governments have also been willing to privatise in parts of systems where competition is feasible - for example, Queensland has recently sold the Gladstone electricity generating station. The downside of privatisation (excessive use of market power) is of least concern with these. The motivation for privatisation has partly been one of generating a quick cash flow, though efficiency objectives have played a role (through privatisation the government can gain the benefits of expected efficiency improvements quickly, as a capital sum).

Partial Privatisation

This may be done either for cash or incentive reasons. In the case of Victoria’s Loy Yang B power station, it seems as if cash has been an important motive, though the new private shareholders have promised efficiency improvements. In the case of banks and financial institutions, at least part of the motivation for privatisation has been to gain strategic private sector shareholdings that might contribute to the running of the firm. This does not appear to be the case with the Commonwealth Bank partial privatisation, which was directed towards small shareholders, and was used as a way of financing the purchase of the State Bank of Victoria.

Corporatisation

It is certainly true that the most popular reform, especially with State governments, in corporatisation. Most States have adopted corporatisation as a goal, produced reports on how they intend to achieve it, and in a few cases, they have moved towards instituting it. The main issue with corporatisation is what it is intended to imply. At one level it can involve converting a public enterprise into a firm which is as similar in terms of objectives, incentives and sanctions to a private firm as is feasible. This is the intention in NSW. (NSW Steering Committee 1988) At another level, it can simply mean giving the enterprise a corporate form, telling it to be more commercial, and paying the senior management more. This appears to be the intention in Victoria. NSW was at the forefront of moves to corporatise, but after the 1988 Steering Group Report, progress has been slow.

There are inherent difficulties with corporatisation, especially of natural monopolies. In its purest form, it involves insisting that firms which have had a multiplicity of vague and conflicting objectives become aggressive profit maximisers. It is difficult for governments to tell their firms to become grasping monopolists, to indulge in anti-competitive practices if they are profitable and to disregard any other objectives they may have been pursuing for over a century. In particular, it is difficult for governments to commit themselves to such simple objectives, and to commit themselves to enforcing incentives and sanctions. Enterprise managements will find it difficult to believe that the government will not ultimately bail them out. Thus far, governments have not developed ways of monitoring performance, and in particular, developing ways of evaluating the contributions of managerial performance and external factors (such as recessions) in determining the results of the enterprise, in ways that the private sector has been able to.

So far, corporatisation has stopped well short of mimicking the private firm. Typically enterprises are given several conflicting objectives, and they are not given any guidance as to the relative weights to be put on them. This is a step forward - at least objectives are being stated clearly. The rewards structures are not very closely related to performance, and the sanctions are very general. (It is difficult for a government to promise to sack managers under specified circumstances). Most corporatisation blueprints are distinctly vague about the critical rewards/sanctions issue (an exception being the NSW one). Nevertheless, corporatisation as foreshadowed, and being implemented, has advantages over the public enterprise model. It can lead to greater management flexibility. It is being accompanied by more explicit objectives, and closer attention to the monitoring of performance. It is also being accompanied by greater competitive neutrality in input and
output markets.

While not necessarily part of corporatisation as such, the setting of profits or rate of return targets can put pressure on the enterprise to perform. How much pressure depends on how the targets are set, what information is available about possible performance, and whether there is competitive pressure or regulation at the product market level. If tightly set, profit targets and price controls can act as a dual constraint system to force better performance out of the enterprise. The difficulty is that the principal/agent problem, whereby the principal knows less than the agent about what is possible, is not solved. The constraints may be set too slack, leading to poor performance, or too tight, leading to inconsistencies and the breakdown of the system. (Forsyth, 1992a) Nevertheless, the system may be workable though imperfect, and it has been applied with a measure of success to Telecom (now AOTC).

Overall, corporatisation can mean many different things, and there are differences in its substantiveness in different jurisdictions in Australia. It tends to be associated with useful clarifications, and somewhat, though ill defined, greater emphasis on profit. As proposed and practised, it does not come to grips with the rewards/sanctions issue, which is at the core of the performance problem.

Managerial Changes and Efficiency Drives

These are not structural changes, but they have been commonly used, especially in the past when the performance of an enterprise has been seen to be poor. They have been used in natural monopoly areas, such as water, electricity and rail, where privatisation and profit oriented corporatisation is seen as too extreme. They can be quite effective, and measured performance often shows a clear improvement for a time after they have been employed. However, there are problems with such methods. One is that the effects are short lived - performance improves and then stagnates. There is no continued pressure for good performance. A second is possibly more serious. When managers are set tasks to improve certain specified aspects of performance in a short time, they tend to be myopic. They have no incentive to look to the long term, and will conduct a 'slash and burn' campaign, which produces results which look good for a time, but which give rise to long term problems. For example, training and investment will be neglected. Nevertheless, they are commonly used devices for improving public enterprise performance. Ideally, they should be followed up with structural reforms which lock in the gains.

Increasing Competition

Many public enterprises are protected by statutory restrictions on competition. One way of increasing the pressure on them to not use any market power they have, and to produce efficiently, is to open them up to more competition. This is one of the simplest and most straightforward ways of improving performance. There have been some significant examples of governments increasing competitive pressure on their enterprises. A good example was domestic airline deregulation, which has removed most of the restrictions from competition with Australian Airlines. In the telecommunications area, the government has opened up some areas (customer premises, resale) up to extensive competition, and in others (trunk services, mobile networks) it has allowed one or two additional competitors. In other areas, changes have been less extensive - for example, with international air services, some scope for additional Australian airlines is to be allowed. In areas such as posts, railways, urban transport and electricity the scope for competition at the fringes has been increased. It is possible that further liberalisation in these areas will come about. While there has been considerable opening up to competition, there is still scope for very much more.

The Federal government appears much more relaxed about allowing competition than its state counterparts. One might be for tax reasons - when a private firm replaces a state owned enterprise, though privatisation or competition in the market place, profits are taxable by the Federal government. Thus privatisation has posed problems, and private firms have been at a disadvantage compared to their State owned competitors. This should not be of
too much concern to State governments, though it can slow the development of competition. An aspect which may be of more concern is that State monopolies can constitute a source of revenue to states which are limited in their taxing powers. They may be unwilling to see this monopoly power eroded, as this will be at the expense of their revenue. The Federal government, with a wider range of tax instruments, may be less worried about the revenue consequences of additional competition.

Exposure to Competition Regulation

As markets become more open, but strong elements of market power remain, the issue of the application of competition policy becomes more important. Where a firm faces no competition, it need not indulge in predatory behaviour, nor prevent competitors from using essential facilities. Even the most thorough deregulation of markets is going to leave significant cases of market power. Up to now, most public enterprises have been exempted from the application of Trade Practices legislation. As they begin to compete with private firms, it would seem appropriate that they face the same environment, and face the same regulations on mergers, predation and access to essential facilities.

There have been some examples of exposing public enterprises to competition regulation. The best example is that of Australian Airlines - domestic airlines are now subject to Trade Practices legislation. In some areas, Telecom (AOTC) has been made subject to it, though it is also regulated by a specialist body, AUSTEL. The most important examples of scope for anti-competitive practices are likely to occur in areas where natural monopoly is important (electricity, rail, gas), though where competition is feasible for some parts of the system. These tend to be dominated by the States. However the States have been unwilling to expose their enterprises to competition regulation, probably for the same reasons that they have been unwilling to allow competition in the first place.

Specialist Regulators

When enterprises with market power are privatised or corporatised (and given a profit objective), regulation may be needed to restrict the emergence of this market power. In Britain, privatisation of national monopolies (telecommunications, gas, electricity and water) was accompanied by the establishment of specialist regulatory bodies, like OFTEL. These regulate prices, usually with price cap, or CPI-X, regulation, and monitor quality. The same issue has arisen in Australia in telecommunications - as Telecom has been induced to be more commercially oriented, and been set profits targets, it has been subjected to price caps administered by AUSTEL. Most of the natural monopoly areas lie within the jurisdiction of the States, and in spite of their interest in corporatisation, few of these have given much consideration to the regulatory problem (this may be because corporatisation is intended to be formal rather than substantive). NSW has established a Pricing Tribunal, which can oversee the pricing behaviour of its monopolies, though the mechanisms and approaches it adopts are yet to be determined.

An Assessment of Reforms

In the public enterprise sector, there have been a number of structural reforms instituted, and several of these are quite significant. However, they do not constitute a thorough going reform of the system. There have been a few examples of privatisation, mainly in moderately competitive industries. There is considerably more scope in many industries for allowing more competition. There has been little progress in changing the conditions under which the natural monopoly enterprises operate. While there has been much talk of corporatisation, implementation has been limited, and when it has been achieved, it has concentrated on changing corporate forms rather than altering incentives and sanctions. It has proven difficult for governments to convert these enterprises into aggressive profit maximisers. At the same time, they have been slow to address problems at the product market end, in terms of pricing and quality, that more profit oriented objectives will produce. They have not encouraged competition where it is feasible and developed regulatory structures for where it is not. Perhaps the best example of a significant structural
reform is that for Telecommunications, though even this has not resolved the question of objectives and incentives for AOTC. Where significant improvements in performance have been sought by governments, it has usually been achieved by ad hoc measures such as managerial changes and efficiency drives.

4. Explaining Performance Improvements

Granted that performance in recent years has been improving, some explanations for this need to be sought. The most natural explanation would be in terms of structural reforms, such as discussed in the previous section. The objective of reform is to foster improved performance by increasing the pressures on the enterprises. The problem is that structural reforms have been relatively modest, and several industries which have put in strong performance improvements have not been subject to much structural reform (e.g. the State Rail Authority of NSW recently). Various managerial changes and efficiency drives can be the proximate explanations of performance improvements, but it is necessary to look at broader forces to explain the changes. Some of these are considered - it is worthwhile noting the impact of structural reforms first.

Structural Reforms

There have been some structural reforms which affect a few public enterprises. Possibly the most significant of these were domestic airline deregulation, and partial deregulation of telecommunications. Productivity growth for Telecom has been good in recent years, and this has occurred as it has faced competition in more of its markets, and prepares to face more competition. It is not possible, using available data, to assess Australian Airlines performance, but it seems very likely that it will be recording significant productivity increases (BTCE, 1991). Competition has not only affected productivity - it has resulted in improved price structures in both airlines and telecommunications.

Most cases of privatisation are recent, and it is not possible to assess the impact on performance. Various forms of corporatisation have been taking place, though most enterprises are yet to be affected. It could be that the more informal changes to owner/manager relationships which have been taking place, such as the setting of profits targets, is having an impact - however, these need not represent long term, structural changes. In short, there is a lot of recent experience that cannot be attributed to structural reform.

Monitoring

Over the 1980s, public enterprises were subjected to much more monitoring. This began with an interest in improved accounting and measurement of rates of return (especially in the early 1980s in Victoria). Then attention turned to the measurement of productivity, and the interest in this continues to grow. More recently, there has been greater interest in comparisons of productivity, between enterprises in different States, and between Australian and overseas enterprises. At different stages over the decade, there have been specific internal studies of particular enterprises. Development of comparable accounts and estimations of performance measures is given considerable weight in the Federalism reform process.

Monitoring, of itself, may spur on better performance (see Hensher, 1989). To an extent, it may come about because there is concern about the level of performance. When monitoring produces evidence about performance, especially on relative performance of comparable enterprises, it also provides evidence of the possible gains from improved performance. Whether it results in structural or ad hoc reforms, the information on possible gains puts pressure on governments to act, and informs interest groups on what they are missing out on.

Budgetary Factors

At both the State and Federal level, budgets have been tight in the 1980s. The Federal government has been seeking to move its budget into surplus, and its grants to the States have become less generous, leading them to be more constrained. This would lead
them to demand greater financial returns from their public enterprises. It could also induce them to privatise their enterprises, to gain extra cash from sale, and to avoid the costs of financing their expansion in the future. Budgetary factors have been relevant in several of the privatisation decisions, such as those affecting Qantas and Victoria's Loy Yang B power station.

The experience of increasing rates of return over the public enterprise sector is consistent with the budgetary pressure interpretation of performance improvements. Governments have insisted upon, and received, greater financial returns from their enterprises. In markets where the enterprises face strong competition, this can only be achieved through greater productivity, though where market power exists, it can be achieved via higher productivity or higher prices. The significant fact is that even in those areas, like electricity, gas, water and communications, where considerable market power exists, the gain in the rate of return has not been at the expense of price increases. Rather, the greater part of the productivity gain has been passed on in the way of lower output prices. This is somewhat surprising, granted the attention given to budgetary factors. It is also interesting given that the rate of return on gross and net assets is still quite low, for the public enterprise sector, compared to the rates of return in the private sector.

The overall rates of return mask sharp differences in rates achieved in different industries. Rates of return for the monopoly areas (except water) tend to be comparable to, or close to, those in the private sector, but there are some very poor performers, especially rail, which pull the average down. Several, though not all, of these poor performers are enterprises which have not achieved rapid productivity growth. The pattern is thus one of some industries (electricity, communications) achieving high productivity growth, achieving improved rates of return, and passing on productivity gains as price reductions, and of other industries (rail, urban public transport) achieving slow productivity growth, where progress to increase rates of return has been slow. Very high rates of return for some enterprises (e.g. Telecom) might be politically awkward, so governments are constrained in their ability to convert productivity increase into higher revenues for themselves.

**External Pressure**

It is difficult to measure external pressure, but it is probably true that governments have been coming under increased pressure to reduce prices for the outputs of public enterprises. This pressure has come especially from the private enterprise sector, which has been finding it difficult to compete, and which has focussed on public enterprise prices as factors making its inputs more expensive. Governments, as always, are subject to pressure from consumer/voters to keep down prices of services their enterprises produce. Public transport fares are particularly sensitive. However, even with increased interest by the private sector, it is difficult to see that increased pressure from outside has been all that effective as a factor encouraging better performance.

**Potential Structural Reform**

The threat of structural reform, or the existence of plans for it, may be a potent means of securing efficiency improvements. If an enterprise believes, or knows, that it will be facing more competition in the future, it will try to prepare for it - especially if its costs are too high. This factor was probably quite relevant in the case of Telecom, which has expected to face increasing competition, and has been preparing for it. If costs are too high when competition eventuates, the enterprise may find it difficult to maintain its market size, and may even struggle to survive.

The threat, or imminence, of privatisation can also be a spur to improved performance. While the enterprise may survive in the new environment, the management may not. The management is forced to ensure good performance, because it operates in a competitive market, even if the firm does not. Furthermore, performance of the enterprise may be improved, as a matter of policy, before privatisation. If there is doubt concerning just how much more efficient and profitable the firm might be before privatisation, a
government may be able to maximise sale proceeds by undertaking an efficiency drive in preparation for privatisation.

**Technological Change**

Technological change is one factor which can influence the productivity growth of enterprises. Technology sets a maximum to productivity, and technological change sets a maximum to the rate at which productivity can grow. Some industries, like telecommunications and airlines are ones in which technological growth is quite rapid, and even inefficient firms in these industries can achieve high rates of productivity growth even though they do not catch up on the more productive enterprises in the industry. Technological factors are of some relevance in explaining the high productivity growth rates in some industries. However, they are not all, or even the major part of the story. A lot of what is happening in the enterprises that have recorded high productivity growth recently (telecommunications, electricity) has been catch-up. It is this catch-up, or improvement in actual performance by making it closer to potential performance, that we are primarily interested in. Technological factors are important in explaining between industry differences in productivity growth - for example, a 3% productivity growth in the postal system may be a more impressive result than 3½% in telecommunications. The underlying technological change must be taken into account when comparing achieved productivity growth in different industries.

**Macro-Economic Conditions**

These are important in two ways. Firstly, they can affect measured productivity growth directly. Secondly, they can affect policy towards public enterprises, and thus the productivity growth they achieve. The first way is straightforward. If there is a downturn in the economy, demand for the output of an enterprise may fall absolutely, or fall below forecast levels. It will rarely be possible to adjust all inputs in proportion. The most difficult to adjust may be capital goods capacity; this tends to be fixed. It can be that an investment program is under way, and it is costly to reduce the growth in capacity. It is usually not possible to reduce the labour force in proportion either, though labour is a more variable factor. Inputs tend to be constant, or rise, in a recession, whereas output falls; the result is that productivity falls. This is no indication of lower efficiency. When the economy recovers, and demand increases, inputs increase less than proportionally, and measured productivity increase.

The second way relies on the response of the government to the macro-economic conditions. If unemployment is high, the government may be unwilling to induce its enterprises to shed labour. One of the most important ways of achieving efficiency improvements has been reducing labour input. Such factors may be relevant in explaining why some governments, especially that of Victoria, have been slow and restrained in their pursuit of reform.

**The Micro-Economic Reform Agenda**

There has been considerable emphasis over the last five or so years on Micro-economic reform, as a means of resolving Australia's economic problems. It is seen (correctly) as enabling higher real incomes and (incorrectly) as increasing competitiveness and reducing the current account. One of the sectors that governments can most directly influence is that which consists of their own enterprises. Efficiency improvements in these are valuable in their own right, but they will also lead to cost reductions for other industries, which use the public enterprises' outputs as their own inputs.

Governments have become more committed to reform, and one might expect to see some speeding up of productivity growth. There is some evidence of this (see Section 2) though this evidence is not comprehensive. While there have been only limited structural reforms (see Section 3), it is possible that governments have been keen to get results, and have implemented ad hoc, short term reforms. This could be because these are usually easier to achieve in the short term, and it could be that structural reforms are more thorough and impose costs on more groups, and are thus more difficult to achieve. Labour
shedding, especially if accompanied by generous redundancy agreements, is relatively easy to achieve, and produces quick results. The efficiency gains can be substantial and valuable, even though they may not be long-lasting unless backed up by structural measures. The relatively good performance of public enterprises recently may be due in part to governments perceiving the gains, and taking, in the main, short term measures to achieve them.

5. Conclusion

The public enterprise sector has been, over the 1980s one of the better performing sectors, at least in terms of its productivity growth. While total factor productivity growth in the rest of the economy has been poor, at less than 1% P.A., that in the public enterprise sector has been around 4% p.a. There also seems to have been an upturn in productivity growth in the latter part of the 1980s, and early 1990s. In spite of the recession, productivity growth continues. Part of the explanation for this is that the productivity level at the beginning of the decade was low.

In spite of this, there is still a significant gap between Australian productivity levels and those being achieved elsewhere. Evidence on this question is not available for all industries, but for important industries such as rail, electricity and telecommunications, most Australian enterprises are achieving only 75% or less of levels being achieved elsewhere. They are catching up, but gradually.

This can best be illustrated with an example. Suppose that Australian public enterprise productivity levels are 75% of what is being achieved elsewhere. Suppose that TFP growth of Australian enterprises continues at around 4% P.A. Suppose overseas enterprise's TFP grows at only 1% P.A. If so, it will take the Australian enterprises 9.8 years to catch up. If the overseas enterprises TFP grows at 2% P.A, it will take Australian enterprises 14.8 years to catch up. This is a long time to wait.

Structural reforms of public enterprises have been slow in coming, though there have been some significant examples. There is still much scope for opening them up further to competition. On the ownership side, there has been privatisation, but most attention is being given to corporatisation. So far, this has not involved substantial change to the incentives faced by the enterprise's management, though it has resulted in some clarification of objectives and a more commercial approach. It remains to be seen whether corporatisation results in a real change in incentives, or is primarily a formal change.

In the light of this, recent performance improvements need to be explained in terms of several factors. In some cases, structural changes, and the threat of further changes, have been important in improving performance. This would be the case for Telecom (AOTC), which realises it is facing a more competitive environment, and is preparing for this. Another possible explanation of change is the budgetary situation of most Australian governments. One might expect them to be more insistent on improved financial performance from their enterprises. There has been some improvement, but it has been slow in coming, and it is less extensive than might have been expected. While enterprises have become more productive, much of the gain has been passed on in lower prices. Governments may have become convinced of the gains from microeconomic reform, and may have put pressure on their enterprises to achieve them, even if they have not been the primary recipient.

One question for the present is whether the current reliance on ad hoc efficiency drives, and administrative restructuring is going to be sufficient. There must be doubts as to how long the gains achieved will last, and whether the present approach will be enough to speed up the rate of performance improvement so that the potential benefits do not take decades to be achieved. The problem with ad hoc measures such as efficiency drives is that they do not put continued pressure on for good and improved performance; in fact, performance sometimes actually slips back. While the gains they reap may be useful, they need to be locked in by ensuring that the pressure is on the enterprise to keep improving performance. Structural reforms, when designed properly, do this automatically.

Public enterprises can be regarded as a partial success story of Microeconomic
Reform so far. Pressure on them has increased, and their performance has improved. But both the competitive and ownership/incentive environments within which they operate have been changed much less than is possible. To maintain performance, and to speed up its improvement so that Australian enterprises can catch up with overseas performance standards, the more permanent and thorough structural reforms need to be tackled.

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