

False economies

DOING LESS WITH LESS



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This discussion paper is the second in a series looking at the false economies that result from short-term, narrow-minded thinking on Australia's public services. Be part of our ongoing public sector discussion on Twitter [#falseeconomies](#) [#ozpublicservice](#) [#ozbigsociety](#)

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Summary

Cuts to the public sector can end up costing far more than they save, and leaving some jobs to the private sector will result in their being done badly or not at all. While some politicians talk about doing “more with less” this can in reality mean doing less with less. This report sets out six cases where the value provided by public services is greater than their costs, and where the job done by the public sector is, in some or all ways, better than the private sector. The cases provide evidence that reducing government can be wasteful and inefficient. They are a warning that when cuts, privatisation, or outsourcing are considered, there needs to be thorough and sophisticated analysis of the costs and benefits of such actions.

Where cuts to public services cost:

- In 2011 Queensland spent \$120 million maintaining public works skill capacity much higher than that of Victoria. Queensland may have saved nearly three times what it spent, \$350 million, by using that capacity to keep public works costs low.
- Sydney trains save car commuters \$923 million a year by reducing congestion. The congestion reduction also avoids 1 million tons of carbon emissions, and reduces community health costs from air pollution by \$109 million. Even without taking into account less directly observable advantages, the benefits to rail commuters, car commuters, and the wider community are of greater value than rail subsidies.
- The majority of our workforce has vocational or higher education qualifications, meanwhile over 350 thousand low skilled job seekers compete for around 70 thousand jobs. There is need for greater focus on non-school education, as well as schooling and job experience, in national visions for a skilled and productive workforce.

Where the public sector does the best job:

- Without the fiscal stimulus package enacted during the Global Financial Crisis, Australia’s economic growth would have been negative for three consecutive quarters. The effect of the stimulus package was to avoid the waste of our economy being \$7 billion smaller in 2010.
- Detailed analysis by the Productivity Commission comparing public and private hospitals has shown that the efficiency of each is very similar, with both having areas of strength compared to the other. In diagnostics and prosthetics the public sector outperforms the private in terms of efficiency.
- All major political parties (including the traditionally pro-private sector Liberal Party) have accepted the strong case that leadership of the construction of the National Broadband Network (NBN) is a job best done by government.

Introduction

The first paper in the 'False Economies' series, 'Decoding Efficiency',¹ argued that to know whether we are getting public value for public money, we must consider what government does as well as what it costs; we need to look at results as well as resources. This is true both of decisions to cut back on spending or decisions to privatise or outsource public services. The paper outlined how the word 'efficiency' is often misused to mean 'cuts', and how some cuts to public services can end up costing us much more than they save. It also pointed out the problems of assuming the private sector is always more efficient than the public sector, and of being blind to private sector failure.

This report illustrates the points made in 'Decoding Efficiency' with six case studies where the efficiency of Australian public services has been, or could be, negatively affected by cuts or a decision to leave the job to the private sector. In presenting these examples this report is obviously not putting an argument that all public sector cuts will cost more than they save, or that all public services must be delivered directly by the public sector. The intention is simply to make the point that cuts or non-government delivery can be counterproductive. Sometimes public sector cuts will cost more than they save, and some public services should be delivered by the public sector. This means that proposals to cut the public sector, or to have the private sector deliver public services, should be scrutinised carefully to ensure that inefficiencies will not be created.

Ignoring the outputs

A recent survey found that 68% of Australians think the government should spend more on public services.² The same survey also found that the majority of Australians (84.5%) think they pay too much, or about the right amount, of tax. This means that at least 52.5% of the survey participants felt that the government should spend more, but tax them the same or less.

In debates on public services, inputs and outputs are disconnected. Politicians regularly promise that cuts to the public service will not reduce public services, but they are rarely asked to prove that this is true over time. A large part of the reason for this is that in public services, inputs are usually more easily measured than outputs. Inputs such as a budget size or number of staff are usually straight-forward to quantify. The outputs, the positive effects of providing a public service, give a range of benefits and it is often difficult or impossible to determine their exact value.

The following three cases have been selected to illustrate the point that sometimes a reduction of inputs can result in a much greater reduction in outputs. In these situations, cuts mean lower efficiency. These two cases are examples where there is sufficient data to calculate at least some of the benefits provided by public services, and in doing so show how cuts can end up costing more than they save.

Public sector works are cheaper with public sector skills

The Building Education Revolution (BER) program, implemented as part of the Rudd government's stimulus package, was the biggest single program of school building upgrades in Australia's history. Some media outlets vehemently argued that the value for money outcomes of the BER program demonstrated the merits of small government and that governments were not suited to delivering nation-building projects. The reality is the reverse: governments that tried to be too small delivered projects with lower value for money. The evidence for this was set out in the Centre for Policy Development paper by Tim Roxburgh, 'Public works need public sector skills: The lost lessons of the BER program'.³ In summary, one of the findings of this paper was that the states with the lowest levels of public works related skills ended up paying more for the works undertaken. By applying this finding to public works generally, we can see how maintaining public works capacity in government can lead to substantial savings well in excess of the costs.

The final report of the BER Implementation Taskforce, which was set up to examine the value for money of the BER program, gave comprehensive information on the value for money achieved by different states.⁴ To illustrate this we can look at the difference in terms of dollars spent per square meter of works by different states. It is instructive to compare Queensland, which maintained a relatively strong public works skills capacity, and Victoria, which had a very low capacity.⁵ Queensland public schools benefited from a dollar per square metre rate of \$2,753, while Victoria paid \$3,114 per square meter. So, Victoria spent an average of 13% more on each square metre of public works undertaken as part of the BER.

There are a number of potential reasons for this difference. However, looking across the five most populous states, the two states with the highest costs (Victoria and NSW) were those most reliant on external contractors.⁶ The BER Implementation Taskforce concluded that public works capacity was a critical factor, and its reduction represented a 'false economy'.⁷ In other words, this is a claim that the savings made by

having a reduced number of skilled public works employees are less than the costs incurred because more money is spent for the work done.

It is possible to test this claim by calculating an approximation of the savings and costs involved. This can be done by comparing an estimate of the skilled public works staff salary costs of a high capacity state like Queensland, with the estimated salary costs of a low capacity state like Victoria. Calculating how much less Queensland would spend if it had the same staff costs per head of population as Victoria gives an approximation of the potential savings in staff salaries. Looking at the likely additional amount Queensland would have spent on its public works gives an idea of the potential increased costs in contracts.

This gives an inherently very conservative estimation of the extent of the false economy for two reasons: Firstly, the calculations assume that Queensland would have a similar capacity by spending a similar amount per person. Queensland's population is much more geographically dispersed than Victoria's, which adds substantial expenses. It is likely that Queensland would have to spend significantly more per person to achieve the same capacity as Victoria. Secondly, the calculations assume that the only value of increased public works skills capacity is reduced costs in public works contracts. In practice many of the skilled employees will also be using their skills to undertake building work that would otherwise need to be outsourced at similar cost. So the amount of savings from reduced salaries given below is almost certainly an over-estimate.

The costs, as of August 2011, of Queensland maintaining its skills capacity can be estimated as \$175 million from census data on the number and income level of public works related professionals (Carpenters and Joiners, Architects and Landscape Architects, Plumbers and Construction Managers) in state and local governments.⁸ Using the same procedure gives an estimated cost of \$67 million for Victoria. If we assume Queensland would require a smaller workforce proportional to its lower population, then Queensland could furnish itself with a similar level of capacity to that of Victoria by spending around \$54 million. This means that the potential savings to be made by reducing Queensland's greater public works capacity was around \$121 million.

The Australian Bureau of Statistics (ABS) reports that the value of public sector building last year for Queensland was \$2.7 billion.⁹ (This includes all construction of new buildings and alterations and additions to existing buildings, but excludes other construction activities such as roads, bridges, railways, earthworks, etc.) It is difficult to say whether the same level of additional cost reported for the BER would apply to all public building, but if 13% is typical then Queensland would have had \$350 million of additional costs last year if it had had a skills capacity similar to Victoria.

So, Queensland spent around \$121 million on having more public servants with public works skills than Victoria. This increased capacity is generating savings perhaps as high as \$350 million. It should be emphasised that these numbers are broad estimates only. However, since the estimated savings from greater value for money in public works are nearly three times the estimated costs of maintaining public sector skills, it's clear there is substantial value, especially given the conservative nature of the calculation. If it were possible to account for the broader benefits, such as the quality of policy and planning advice derived from those skills, it's likely we'd find that the value is higher still.

It should be kept in mind that the BER program was funded by the Commonwealth Government. So the false economies of states like Victoria end up wasting federal funds. Given the announcement of significant investments for infrastructure in the recent federal budget, the skills capacity of state public services, and perhaps of the Australian Public Service, should be of high concern to the Commonwealth government.

Removing public transport subsidies can be a waste of time - for car commuters

Governments often ensure the availability of low-cost public transport by providing subsidies that reduce the prices of tickets. So whether the actual vehicles are run by government or a private company, low-cost public transport is a public service ultimately resulting from government funds. It is not generally appreciated that substantial benefits accrue from these subsidised services, benefits not just to the public transport users, but to the wider community, and especially to those who commute by car. This example looks at some of the benefits from Sydney's trains.

In looking at the benefits of Sydney's rail public transport the intention is not to make the argument that the current fare and subsidy levels are necessarily ideal. There is a great deal of sensible discussion on issues such as cost recovery rates, fare increases, finding efficiencies, car use charges, and levels of investment in transport infrastructure. The example given here simply demonstrates that there can be substantial economic benefits from low-cost public transport supported by subsidies.

The subsidies to public transport go towards both a general reduction in ticket prices, and further reductions on tickets for particular groups, such as school student passes and pensioner tickets. It's probably well understood that the further reductions for specific groups are provided for social justice and equity reasons.

What may be less well known is that the general reduction in prices relates strongly to the external benefits of public transport – the benefits to non-public transport users and the wider community obtained from the operation of public transport.

A large part of these benefits go to those who commute by car. The Treasurer, Wayne Swann, observed in his recent budget speech: “Traffic congestion costs commuters time with their families and is estimated to cost our economy up to \$20 billion a year by 2020 if not addressed.”¹⁰ A full bus takes around 30 cars off the road, a train removes its passengers from the road entirely, and this leads to less traffic congestion and so a faster journey with reduced fuel use for those who commute by car. The reduced fuel use also results in significant reductions in emissions that benefit us all.

While the logic of public transport reducing congestion and emissions is straightforward, it is more difficult to determine exactly how much benefit car drivers are deriving and by how much emissions are reduced. However, a report prepared for the Independent Pricing and Regulatory Tribunal (IPART) provides relevant information. This report was written to allow IPART to determine whether the correct level of subsidy was being given to CityRail.¹¹ In its effort to determine optimum subsidies the report used a traffic model to compare traffic congestion under current train use, with hypothetical scenarios including having no CityRail trains.

This procedure assumes that public transport affects traffic congestion because commuters shift to other forms of travel if their current mode of travel is unavailable. This assumption is not uncontroversial. It can be argued that in reality over the long term people adapt to their situation by changing where they live and work, to avoid heavily congested roads or to take advantage of relatively clear routes. However, the extent to which adaption occurs may be limited and occur very slowly, and such adaptations that might occur involve their own costs and benefits. Very few people can change jobs or homes quickly, and many will not go to the effort involved.

By comparing current train use with a hypothetical situation of having no CityRail trains, the annual benefit to car drivers from trains was calculated to be \$923 million. This benefit comes from reduced congestion meaning that car commutes are faster; car drivers and their passengers save time (which was valued at \$13.51 an hour) and use less fuel for their journeys. Having fewer cars on the road also benefits the community generally by \$134 million a year through reducing carbon and other emissions. Around 1 million tons of carbon emissions are avoided annually (valued at \$25/ton). Health costs from other emissions, estimated at \$109 million, are also avoided. These external benefits are in addition to the yearly benefits obtained by the rail commuters themselves, which were calculated to be either \$1,031 million, or \$1,414 million, depending on modelling assumptions.

The total of the rail commuter, congestion, and emission benefits is then \$2,071 million or \$2,454 million. This can be compared with the government subsidies provided to CityRail, which are \$1,364 million. However, the comparison is not entirely fair since it only accounts for these three benefits, and there are less directly observable benefits that should be taken into account:

- For example, businesses in the CBD benefit from agglomeration, being located in a cluster of other businesses means firms benefit in a range of ways from a concentration of skilled workers.¹²
- There are also significant stress effects of congestion.¹³ This might seem a relatively minor point, but it needs to be kept in mind that in particularly congested US cities it has been enough to occasionally generate literally homicidal road rage.¹⁴
- Given Tony Abbott’s recent comments that urban rail is not in the Commonwealth’s “knitting”, it should be kept in mind that any ‘savings’ made by governments that invest less in public transport infrastructure may be eliminated by the need to spend more on roads. It is unlikely that the voting public will simply accept higher congestion levels. If public transport is not a viable option, voters will probably insist on further road construction, requiring expensive land acquisitions and/or costly underground tunnel construction.

These aspects of the broader economic, social and environmental performance of the city should be taken into account. Considering that even without them the benefits of public transport are greater than the subsidies, it’s clear that the government subsidy of public transport can deliver important advantages.

A skilled workforce needs more than Gonski

Wane Swan’s recent budget speech talked about a ‘skilled workforce’¹⁵ and in Tony Abbott’s budget reply speech he said ‘people who can work should work’.¹⁶ In discussing jobs from their different ideological positions both speeches contain the same glaring false assumption. Swan and Abbott assume that tertiary education and vocational training are not important for employment. Even the most cursory look at employment statistics reveals the inadequacy of their approaches. Any national vision for a skilled workforce must include the higher education and vocational education and training sectors.

The 2011 census data shows that of the 10 million Australians in paid employment, 5.9 million had non-school qualifications (degrees, diplomas, or certificates) as their highest level of education.¹⁷ From this it can be inferred that the majority of the workforce did not rely solely on their school education to obtain a job. This inference is borne out when examining the figures on those looking for work. Of the 600 thousand people who were unemployed and looking for work, only 246 thousand had non-school qualifications. This is a much lower proportion (41%) than amongst the employed (59%), indicating that those with only school education have a harder time finding work.

Wayne Swan talked about 'a highly skilled, educated and productive workforce', but mostly he linked this to the increased school funding that is part of implementing the Gonski reforms.¹⁸ Universities did get a mention, though the cuts being made to their funding did not. TAFEs and the Vocational Education and Training (VET) sector were not spoken of at all. (Of course you could argue that VET is primarily a state responsibility, but this ignores the fact that federal money makes up a quarter of VET funding¹⁹ and that the federal government has substantial influence on the sector.) So, for the majority of the future workforce, Swan's budget only addresses half the story and cuts or ignores the other half.

Tony Abbott's speech spends much less time than Swan's on employment, and presents an even greater lack of understanding about the workforce. His solution relies heavily on work-for-the-dole schemes and increased incentives to work. It's an approach he has advocated for years, and described most succinctly in his 2011 budget reply speech: 'I'm all in favour of training but first things first: the best training is on-the-job'.²⁰ Of course this assumes that it is possible to get a job without training.

The Department of Education, Employment and Workplace Relations (DEEWR) produces monthly reports on the number of job vacancies available.²¹ At around the time the census was conducted (August 2011) there were 227 thousand job vacancies available to the 600 thousand job seekers. DEEWR also produces a skilled vacancies report.²² Subtracting these out gives the number of unskilled job vacancies as 133 thousand. However, this substantially overestimates the amount of unskilled work available since the skilled report only looks at professionals, technicians, and trade workers. This ignores many other jobs that require qualifications. For example, there are 26 thousand managerial positions many of which will either formally require qualifications, or are in practice not going to go to low-skilled applicants. The number vacancies that do not require any non-school qualifications might be more reasonably estimated at 70 thousand.²³

Over 350 thousand low skilled job seekers competing for around 70 thousand jobs means that for every one low skilled worker who can find employment, four will not. And keep in mind that these calculations are for a month where the number of vacancies was high. By comparison, last month's vacancies were 30% lower than the August 2011 figure. Under these conditions many will not be able to avoid long-term unemployment. This makes incentives meaningless, and turns work-for-the-dole simply into government subsidised free labour for the private sector.

Both of these approaches ignore the pressing need to encourage as many Australians as possible to undertake tertiary or vocational education. This is a significant issue since the census data shows that the number of job seekers with only school qualifications is around a fifth the size of the total number of higher education and VET students. So a substantial increase in capacity is required. However, this year Universities are facing a cut of \$900 million at the federal level, working against Labor's sensible trend of increasing funding to higher education.²⁴ And the VET sector is suffering large cuts at the state level (a total of over \$600 million in Victoria, NSW, and Queensland).²⁵

The potential benefits of a more skilled, more employable, population are difficult to quantify in total, but are no doubt large. The benefit to individuals involves increased income obviously, but perhaps more importantly the increased self-confidence that comes with employment has a range of positive psychological and health influences.²⁶ For the economy, skill shortages are alleviated, allowing greater productivity. And a higher skilled economy is generally more productive and delivers higher wages.²⁷ This means the Government has the benefit of reduced welfare costs and increased tax take, allowing more money to be invested in infrastructure or other nation-building projects. And as a society we benefit from a more informed and engaged population making for stronger communities and a healthier democracy.

Tony Abbot's glib dismissal of education and training is woefully inadequate to deal with the realities we face and runs the risk of missing out on substantial benefits. Wayne Swan was right to make skills a major theme of his budget speech, but he has only considered part of the picture. High quality schooling and work experience are clearly critically important, but for the majority they are not sufficient. Swan argues that 'we'll only win the economic race in the Asian Century if we win the education race'. You won't win any races if you only run part of them. Higher education and VET cannot be left out of our plans for skilled workforce.

Some jobs are best done by government

The 'Decoding efficiency' paper critically examined two misuses of the word 'efficiency' that can lead to false economies in public services. The first misuse, that 'efficiency' means 'cuts', has been shown false by the above three cases. The following three cases show that the second misuse 'the private sector is always more efficient' can result in greater costs than savings.

Those who subscribe to a neo-liberal perspective can often forget that there are some tasks that governments are better suited to than the private sector. This can lead to attempts to 'shrink' government even in the face of both public opinion and evidence. A blind faith in the market can result in decisions to withdraw government from the jobs it should be doing. This can be through selling government assets, outsourcing services previously provided by the public sector, or simply withdrawing government from the area in the expectation that the private sector will fill the gap. Privatisations, government outsourcing, or simple cuts, are pursued on the mistaken assumption that the private sector is always more efficient than the public sector, and therefore the costs to government, or the economy as a whole, will be lower. This can be a false economy, with the private sector doing so much less in critical areas, that any potential savings are overwhelmed by the costs of doing too little. The following cases are just three of many examples that show that government may do a better job than the private sector.

It's not just the size of your stimulus package, it's the way you use it

While there are a complex range of different actions governments can take in poor economic circumstances, debate around responses to the Global Financial Crisis (GFC) has focussed on two broad approaches: austerity and stimulus. The stimulus approach envisions that government can play a critical role in helping the economy. Austerity instead involves government cutting back on its activities, and therefore by default leaving economic recovery to the private sector.

There is growing international evidence that austerity doesn't work, or at least, doesn't work as well as its advocates have claimed. The IMF Chief Economist published a paper early this year indicating that government spending cuts do not, as was forecast, reduce economic activity by only 50c for every government dollar not spent. Instead it may reduce economic activity by \$1.50 for every dollar cut.²⁸ Then just last month a spreadsheet error in the research for an influential article has been discovered, and the case to say that high levels of debt are associated with lower growth is not as strong as it would appear.²⁹

Australia was one of only three advanced economies that avoided recession during the GFC. International acclaim has been consistently directed at the Commonwealth Government's fiscal stimulus package as a response to the GFC. "One of the best designed Keynesian stimulus packages of any country" opined former World Bank Chief Economist, Clinton administration economic advisor and Professor of Economics Joseph Stiglitz. Stiglitz is not alone in the economics profession in heaping high praise on the Rudd Government's fiscal injections in an attempt to stave off recession. An open letter was circulated in 2010 signed by more than fifty professors and lecturers from Australia's leading universities praising the government's actions in stimulating the economy and preventing a recession and mass unemployment.³⁰ The IMF also commended the 'quick implementation of targeted and temporary fiscal stimulus'.³¹ And it was considered to be 'among the most effective in the OECD'.³²

Turning to the calls of waste and inefficiency that have been a hallmark of some media coverage pertaining to the stimulus package, Joseph Stiglitz again offers a cogent argument for the approach the government undertook and the efficiency with which its agencies undertook the delivery of the program.

If you hadn't spent the money, there would have been waste. The waste would have been the fact that the economy would have been weak, there would have been a gap between what the economy could have produced and what it actually produced - that's waste. You would have had high unemployment, you would have had capital assets not fully utilised - that's waste. So your choice was one form of waste verses another form of waste. And so it's a judgment of what is the way to minimise the waste. No perfection here. And what your government did was exactly right.³³

The calculations of Treasury support Stiglitz's analysis. Fiscal stimulus estimates indicate that growth would have been negative for three consecutive quarters without fiscal stimulus. Originally the fiscal stimulus was forecast to increase GDP growth by 2 percentage points in 2009 and to detract around 1 percentage point from growth in 2010; the estimates have changed only slightly since then.³⁴ This means that the effect of the stimulus package was to avoid the waste of our economy being \$7 billion smaller.³⁵

It is interesting to note that although Australia's stimulus package was one of the largest as a percentage of GDP, a number of nations with large stimulus packages did not perform very well subsequently. The OECD has concluded that the effectiveness of the stimulus was due to both the size of the measures and the speed

with which it was introduced. The targeting of the stimulus to households (particularly those on modest incomes) and to school building (which can be undertaken rapidly) also contributed to the speed of its effect.³⁶ So, it seems that the design of the stimulus is critical, and this requires sufficient public service capacity to plan, cost, establish, and monitor large projects, perhaps against very tight timeframes.

It should also be noted that a number of other explanations have been suggested for Australia's performance during the GFC. Some of these alternative explanations also point to the critical role of a high-quality public service, e.g.:

- **Banking regulation:** None of our major banks failed, and we were one of only two advanced G20 nations that did not need to make a government injection of funds to the banking system (though, as in many countries, the government did issue guarantees for bond issuance and deposits). OECD analysis shows that our regulations were not stricter, but they were well implemented. Our banking system 'benefited from years of rigid supervision by "better than world-class" financial regulators'.³⁷
- **The Reserve Bank:** Appropriate actions by the Reserve Bank, and supporting government monetary policy helped to maintain the stability of the financial system during the GFC, and was no doubt a key factor (though indications are that the full effect of monetary policy is delayed and was muted by the nature of the financial shock).³⁸

Other explanations for Australia's success have been offered which imply less of a role for government, such as population growth, structure of the economy, and demand from our major trading partners, especially China. Indeed China's demand is the main reason usually given as an alternative explanation for why we did so well. However, it's worth noting the example of Canada, which also has large mineral resources, but did not fare as well as we did. Also worth noting is the argument of economist Steve Keen, that if our current economic position had been the result of China's strong economy (itself boosted by a substantial stimulus program) then export industries would have experienced employment growth first, followed by the rest of the economy. Instead the growth was driven by industries benefiting most from the stimulus.³⁹

The likelihood is that all these factors played complimentary roles, with the non-government aspects being fed by, and feeding into, the effectiveness of government actions. And it should be kept in mind that the "non-government" aspects may have involved a significant government role in the long-term, for example, immigration policy affecting population growth, and international trading relations facilitated by diplomacy.

Whilst free market ideologues continue to offer commentary that dismisses the efficacy of the government's action during the GFC and talks of the endless waste of big government, the economic reality is that Australia avoided recession, prevented mass unemployment and today has an economy that is the envy of the developed world partly because of timely government intervention in a slowing global economy.

Strengths in different areas - public and private hospitals

It might seem that Australia's hospitals would provide an opportunity for a relatively clear-cut assessment of the claims of 'private sector primacy', the belief that the private sector is always more efficient than the public sector. Here we have both sectors operating similar institutions in the same industry. It should be straightforward to compare the two sectors' performance. In 2009 the Productivity Commission produced a detailed and comprehensive report comparing Australia's public and private hospitals.⁴⁰ A significant challenge for this report was factoring in the differences between private and public hospitals. Although the two sectors operate in the same industry, there are number of differences between the sectors and the jobs they do:

- **Size:** There are far more very big (201 bed or more) and very small (0-50 beds) public hospitals, the 51-200 range is roughly evenly split between public and private.
- **Location:** There are slightly more private hospitals in the major cities, outside these public hospitals dominate and there are no private hospitals in Remote or Very Remote areas.
- **Activities:**
 - Public and private hospitals focus on different kinds of care (so for example, private hospitals on average do more rehabilitation, while public hospitals engage in more palliative care).
 - Public hospitals tend to do more teaching.
 - Public hospitals do the vast majority of accident and emergency work.
- **Demographics:** Children and young people comprise a larger share of the case load of public hospitals, in private hospitals the age group with the highest proportion of patients admitted is 50 to 64 years.

The Productivity Commission report attempts to take into account these differences in its comparison. As part of this a multivariate statistical analysis was run which allowed a weighted score, based on the in-hospital mortality rate, to be assigned to each hospital.⁴¹ The averages of these scores are then calculated for various sizes of public and private hospitals. Comparing these scores shows no significant difference for large

hospitals, but it seems that small private hospitals do slightly better than small public hospitals. Interestingly much of this difference comes from the small private hospitals run by not-for-profit entities. A calculation of total technical efficiency shows similar results for public and private efficiency.

The report also contains a calculation of costs of each episode of care for an admitted patient. These costs are weighted based on case-mix to give comparable figures. The results are mixed with public hospitals keeping costs down on diagnostics and prosthetics, and private hospitals achieving lower costs on pharmaceuticals and general hospital charges.

The overall picture of this comparison of public and private hospitals is that the efficiency of each is very similar, with both having areas of strength compared to the other. The advantage of this situation is that both sectors can perhaps learn from each other to improve efficiency. This is a good example of the benefits of having both public and private sector participation in an industry. The example shows that it is unsupportable to insist that the private sector is always superior in efficiency.

A clear need for government leadership - the National Broadband Network

Unlike the cases above the National Broadband Network (NBN) is a work in progress. So the outcomes described here are predictions. However these predictions are based on a well-known pattern; that the private sector is not well-suited to leading the construction of big networks. The best way to build a national network, regardless of whether it's communication, transport, or something else, is through the leadership of a national government. That doesn't mean that there can't be substantial private involvement, and a great deal of the work of rolling out the NBN is being done by private contractors. But for a number of reasons, three of which are outlined here, government needs to be the organisation that provides national leadership on key objectives and standards of delivery.

The most significant problem for private sector leadership in constructing an NBN is the uncertainty of the timing of economic returns. The value of a network doesn't increase in a predictable fashion. The first private telephones were a novelty, but not very useful. A hundred phones across an entire country are unlikely to connect you to many people you know. Perhaps even a thousand phones won't be useful, but at some point the network is of enough value that everyone wants to be part of it and the way we communicate is changed forever. At that point the network becomes economic to run, but the timing of that point is impossible to predict. This is a high risk for private sector investors who generally cannot bear this timing uncertainty.

Another problem is with consistency and reliability. It would be extremely difficult to find a private company big enough to take on the entire task of rolling out an NBN (and even if possible would create a monopoly and remove any possible benefits of private sector competition). If a network is built by a variety of organisations there will be differences in the kind of network installed and the way it is set up in different areas. This will constrain the way in which the network can be used. For example, an organisation may wish to invest in high quality video conferencing because of the savings that can be made by having employees telecommute. However, if it is uncertain that all employees will be able to successfully use the system from home depending on where they live, then the investment will likely not be made. The consistency involves a number of factors, not just the speed, but aspects such as its 'jitter' (tendency to have slow periods and bursts of speed) and 'latency' (delay in transmission). Inconsistencies in these aspects can make communication much less intelligible, and can cause data losses. A government driven national roll-out with a guarantee of certain minimum standards gives a consistency that broadens the potential applications of the network.

Inconsistency and reliability are of particular relevance for rural communities, since it is in these smaller markets where reduced incentives for private investment make these problems more likely. This is a disincentive for businesses to operate in rural areas. If a level of consistency is guaranteed, not only do rural areas benefit, but arguably strain on capital cities is reduced.

A further problem is the likelihood that competing networks may be built alongside each other. An example of this is the needless duplication involved in having separate Optus and Telstra mobile phone tower networks. This leads to many areas having two towers when only one would be required for the number of mobile phones in the area. Not only is building duplicate networks a waste of resources, the costs of which are largely passed on to consumers through higher charges, but it can cause numerous other inefficiencies. For example, both Telstra and Optus offer "cable internet" connections which operate through a hybrid fibre-coaxial cable (HFC) network. Because Telstra and Optus each have their own HFC network it is not possible to change providers remotely. Instead it involves a technician visiting the premises in order to run a second cable and install a second socket in the wall.

The case for federal government leadership in providing an NBN is so strong it has more-or-less been accepted by all major political parties. Most of the media debate on NBN policies has focused on the potential false economies⁴² of the Coalition's current alternative NBN plan of rolling out fibre-optic cable to 'nodes' for most streets and connecting to the existing copper network from there, rather than connecting fibre directly

to almost every house as in Labor's plan. Less commonly discussed is the Coalition's rapid transition from commitments to "dismantle the NBN" to their current alternative.⁴³ The Coalition has accepted, not only that Australia should have an NBN, but that the primary responsibility for providing it must lie with government.

Although the Coalition has said that it will remove the regulations that currently prevent competing networks from being built, there is no estimate given of the extent to which the private sector is likely to take up this opportunity. The Coalition's plan for the NBN states that:

We will issue a revised statement of expectations directing NBN Co to provide broadband services with a minimum download data rate of 25 megabits per second by the end of 2016 in all areas of Australia, and 50 megabits per second by the end of 2019 in 90 per cent of the fixed line footprint.⁴⁴

And Tony Abbott, in his recent budget reply speech, said:

let a competitive market deliver the speeds that people need at an affordable price with government improving infrastructure in the areas where market competition won't deliver it.

The Liberal Party, despite its 'private sector primacy' ideology, has accepted that responsibility for provision of the NBN should lie with the government created NBN Co. So there is broad agreement that leadership of the construction of Australia's next significant network is a job best done by government.

Conclusion

The above six cases show that actions to cut public services or have them provided by the private sector can be inefficient. While such actions do not always lead to waste, the clear evidence that it can occur demonstrates the need for careful assessment. It is also hoped that the difficulty of such assessment is apparent. These six cases were 'low-hanging fruit', areas where there were rich data sources and the outputs relatively quantifiable. Even so, many of the figures are rough estimates, and the full range of effects is not incorporated. The assessments to be undertaken will be complex, but necessary if we wish to improve our public services efficiency, rather than simply doing less with less.

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- ⁴² There is a potential false economy in the Coalition's current NBN policy, though it is more like the first three cases studies in that it is a cut to Labor's roll-out plan that could end up costing more than it saves. The Coalition policy may at first glance seem like a reasonable compromise. Fibre-optic cable will be rolled out to 'nodes' for each street and connect to the existing copper network from there, rather than directly to every house. This is claimed to cost a little over half the predicted price for Labour's plan and deliver up to a quarter of the speed, a speed which is sufficient for most current uses (at least the download speed, the upload speed which is much lower is arguably already a significant constrain on normal use). The problem with this caution is the risk that we will later need fibre direct to every house. The copper network is reaching the physical limits of what it can deliver, whereas fibre can deliver speeds of over a hundred times what is being currently promised. Whether we will need these speeds is not certain, but the likelihood is very high. There has been a long trend of increasing access rates (see: P Gerrand, 'The Coalition's NBN policy is a triumph of short-termism over long-term vision', *The Conversation*, 10 April 2013, <http://theconversation.com/the-coalitions-nbn-policy-is-a-triumph-of-short-termism-over-long-term-vision-13333>). Of course not all trends continue indefinitely, but there's no good reason to bet against this one in the near future. A range of different potential uses for the increased bandwidth have been put forward. Just one example is high definition video conferences, which will give a greater ability to work from home, avoid business travel for meetings, and allow

people to see a doctor remotely. So, if the trend continues it may cost as much to upgrade to a higher bandwidth system as it would have done to do it in the first place. Meanwhile our technological development lags that of other countries while we upgrade. And people who require the larger bandwidth immediately (e.g. those in industries that become reliant on it) will opt out of the NBN for more expensive private systems. This potentially leads to the problems of consistency and competing networks mentioned above. None of this is certain, but it doesn't make any sense to plan as though a long-running trend will soon stop, when there are no indications that it will.

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