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## Swan budget signals choice under threat

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Variety in a free market is the key to efficiency, so why is Labor eroding it, asks **Henry Ergas**

IF there is one lesson that emerges from experience with economic reform in Australia and internationally, it is that choice is the key to efficiency. At the end of the day, it is consumers who are best placed to evaluate the services offered to them by suppliers. And it is the threat of that choice being exercised that disciplines suppliers and ensures that they innovate, invest and provide consumers with enduring value.

This is no less true of the services traditionally provided by state governments, including education and health, than it is of those goods and services supplied by the private sector. It is for this reason that the expansion of choice that has occurred in the past decade -- with the growth of non-government schools and private hospitals -- is so important. The reality is that significant numbers of consumers have voted with their feet and, in doing so, have placed great pressure on public-sector suppliers.

That choice might never have occurred had the state governments and the unions that represent public-sector suppliers had their way. It happened because the commonwealth was willing to put in place arrangements under which subsidies followed consumers rather than being rusted on to public-sector suppliers.

This is exemplified by health. In the 2005-06 financial year, the federal government provided more than 90 per cent of the funding to private hospitals. This area of expenditure had grown eight-fold since 1995-96, from \$381 million to \$2.7 billion, with government expenditure on private hospitals rising from less than 3 per cent of the total hospital funding budget to just less than 11 per cent.

When account is taken of that shift, the commonwealth share of direct hospital funding, far from declining, remained remarkably stable during the period: in 1995-96, the commonwealth accounted for 50.3 per cent of total (federal plus state and territory) expenditure on hospitals; for 2005-06, the commonwealth's share of total hospital funding was 49.98 per cent. But what did change is the extent of the federal funding that goes to the private sector, reflecting consumers' growing use of private hospital services.

Labor came to office committed to maintaining choice, and rightly so. But this makes the messages in Labor's first budget mixed, if not somewhat concerning.

The changes to private health insurance, for example, send a signal that, as opposed to the former Howard government, Rudd Labor is much less keen on the idea of people making provision for their health care through private insurance. Although the ultimate outcomes are as yet unclear, it is telling that the budget

papers anticipate a significant fall in the number of Australians taking out private health insurance.

Weakening private health insurance could affect the growth of the private hospital sector, making consumers more dependent on a public hospital system that has found it difficult to meet the community's expectations. It may be that this is merely the consequence of rushed decision-making and a failure to think through the longer-term effects of what is being done.

But it could also reflect an instinctive and unthinking centralism that views choice as incidental rather than being at the core of good policy.

Nothing better highlights the issues this raises than the budget's quite proper concerns about how the windfall we are securing from the minerals boom can be best used. The fear Wayne Swan has expressed is that the windfall may be squandered. It is for this reason, we are told, that the windfall must be sequestered into funds that will be available for future spending. But if that is the rationale that underpins those funds, then the announcements made in the budget are not reassuring.

At its simplest, this is because so little has been said about how those funds -- which are individually large and collectively enormous -- will be governed. For instance, in the case of the Building Australia Fund, will we have full disclosure of the cost-benefit analyses that should underpin every project? If not, how can we be assured that decisions will be taken to the high standards required to ensure good use of the funds being set aside?

This is especially important because history shows that no one is better at squandering resources than governments. Surely consideration should therefore have been given to ways of returning the windfall to taxpayers in avenues that nonetheless quarantined it from immediate domestic spending. For example, accounts could have been opened for each child, depositing an amount that could be spent only in future years for health and education. Equally, supplementary superannuation funds could have been provided to low-income households, which have every incentive to treat carefully any additional savings they obtain.

In short, now is the time for Labor to show that it really is committed to choice. If it isn't, all the future funds in the world will not provide Australia with the economic future we can properly hope for.

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