

**CONNECTING CONSUMERS AND THE
ECONOMY: THE BIG PICTURE**

**CLOSING ADDRESS TO THE NATIONAL CONSUMER
CONGRESS**

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Good afternoon.

I'm delighted to give the closing address to the National Consumer Congress at such an important time for consumer empowerment. 2007 is a time to be taking a 'big picture' view of connecting consumers to the productive base of the economy. As the Parliamentary Secretary to the Treasurer, Chris Pearce, noted in his opening address yesterday, this year the Productivity Commission will produce the first substantial review of Australia's consumer policy framework since 1984. The inquiry will give us a unique opportunity to take stock of just how effective our consumer frameworks are; and how they could be improved.

The inquiry into consumer policy promises a great deal. It follows a sequence of successful inquiries and reforms that have improved markets and benefited consumers. Consumers have reaped substantial dividends from extensive economic reforms over many years, including widespread deregulation and trade liberalisation. National Competition Policy has facilitated more competitive markets in areas like infrastructure and public monopolies. The Productivity Commission Review of National Competition Policy emphasised its significant contribution to Australia's gross domestic product.

Of course, the consumer benefits of competition reach far beyond what is measured by gross domestic product growth. Consumer welfare and, more generally, improving the wellbeing of the Australian people, goes far beyond growth.

Those of you who have heard me speak on other occasions may recognise the significance of my reference to 'improving the wellbeing of the Australian people'. Those words are the opening line of the Treasury's mission statement.

Far beyond a mere line in our mission statement, the concept of 'wellbeing' has evolved into a framework that drives all of our work. Put simply, it's what we do. The 'Wellbeing Framework' is a grassroots statement of our mission, encompassing market, non-market, material and intangible components.

We see wellbeing as having five core elements — freedom and opportunity; consumption possibilities; distribution; risk; and complexity.

The way in which the wellbeing framework informs our approach to policy issues can be illustrated by developments in telecommunications, which is one part of the National Competition Policy agenda.

Following deregulation and the privatisation of Telstra, Australia's telecommunications sector has emerged as an increasingly competitive market. While infrastructure-based competition is developing, supported by the competition access regime, Australia now has many firms providing telecommunications services.

In telecommunications, the competitive market delivers consumers the freedom and opportunity to make choices. Consumers have been empowered, as evidenced by their movement from the former monopoly provider, to alternative providers. In general, freedom and opportunity is about people having the capability to make life-improving choices.

Competition policy has allowed multiple players to provide telecommunications services. This has cut the cost of telecommunications services and enhanced consumption possibilities. The distributional dimension of wellbeing supports the policy goal that consumers should be able to access telecommunication services, at least of some minimum standard, without being unduly disadvantaged by where they live or their income level.

I imagine that those who have purchased telecommunications services recently will be aware of risk and complexity. In the Treasury, we take the view that wellbeing is enhanced by lowering risk and complexity, other things equal. In telecommunications, the Australian Competition and Consumer Commission plays a significant role in ensuring that consumers and competing service providers are dealt with fairly and that risks are well understood.

Complexity, however, is more problematic. In a technology-driven sector like telecommunications, a considerable level of complexity is probably unavoidable; new technologies tend to bamboozle. But it is probably also the case that the liberalisation of the former monopoly market – which now permits several providers to offer competing packages – adds considerably to the complexity confronting the consumer. The question for policy-makers – especially those charged with responsibility for consumer policy – is whether complexity can be reduced without compromising the achievement of the other things already mentioned: lower prices, better quality, and a much richer set of consumer choices.

I have used issues in telecommunications to illustrate how the wellbeing framework shapes the Treasury's approach to its consumer policy role. I now want to generalise the discussion a little. The wellbeing framework supports four principles that are essential for effective consumer policy:

- First, competitive markets drive consumer welfare and consumers drive competitive markets.
- Second, government intervention in the market should utilise the regulatory or non-regulatory tool best suited to each situation.
- Third, government policy should not impede, but should rather support, the expansion of national markets.
- And fourth, government policy should empower consumers, protecting them when appropriate.

I am not alone in regarding these principles as essential for effective consumer frameworks. The Productivity Commission's recent issues paper highlights the importance of these themes to the consumer policy framework.

Competitive markets drive consumer welfare and consumers drive competitive markets.

The fostering of open and competitive markets, with high levels of consumer participation, lies at the heart of enhancing consumer wellbeing.

Competitive markets and consumer policy are mutually reinforcing. It's crucial to see the links.

As you would know, markets have both a supply and a demand side. Competition policy usually seeks to nurture healthy competition among suppliers of goods and services. Consumer policy, on the other hand, facilitates functioning markets by empowering consumers to exercise their preferences, to make informed choices, and to signal to suppliers what it is that they, the consumers, want.

Governments that subsidise inefficient farming practices around the world might want to pretend otherwise, but the fact is that production is pointless without consumption; the whole role of an economic system is to satisfy consumers' demands for the goods and services they want. Obviously, we need suppliers to produce the goods and services sold in the marketplace; but not necessarily the goods and services that happen to interest the suppliers. Consumers must be able to provide market signals to ensure that the right goods are produced, with the right characteristics, in the right quantities and at the right prices.

It is well understood that markets will deliver sub-optimal outcomes for consumers if firms form a cartel, for example. It is perhaps not so well understood that markets will fail if consumers don't have enough knowledge to make sound choices or don't trust suppliers sufficiently to participate fully in the market. Critically, consumer policy supports market participation.

The link between consumer welfare and competition law is more obvious when market failures on the demand side – due to information asymmetries, for example – lead to failures on the supply side. Consider the greengrocer selling genuine organic produce, competing with a greengrocer who sells low cost, ordinary produce labelled as 'organic'.

While we need consumer policy to protect consumers from deceptive trading — as in the case of a shonky greengrocer — consumer policy also ensures the continued viability of the legitimate market operator, underpinning a more competitive market. Likewise, competitive markets support consumer interests. When markets are unduly concentrated and little competition exists, consumers may be forced to consume high priced or low quality products, even in the presence of consumer protection regulation.

Interventions should consider all options and maximise net benefits

My second principle is that government intervention in the market should reflect the extent of market failure and use the best fit-for-purpose approach to ensure that any market regulation produces the highest possible net benefit for consumers. We talk about the 'net benefits' of regulation because regulation has costs for consumers, in the same way that market failures cost consumers.

Often we hear calls for more 'black letter' regulatory intervention to deal with the potential abuse of consumers. However, while regulation can form an important part of the protective armoury for consumers, regulatory intervention is not always the solution.

Today, the ACCC, together with policymakers and industry, leads the world in market-based consumer policy. Charters, guidelines, standards, internal dispute resolution mechanisms and codes of conduct form an integral part of the regulatory landscape and the regulator's toolbox. While much of this policy is commonly described as self-regulation, it may best be described as 'co-regulation' because the mechanism often works by leveraging the synergy of stakeholder and regulator interests. And today's consumer policy mechanisms include

consumers. In fact, consumers often drive the process, and they don't need access to a court or tribunal to do so.

It is a practical reality that some markets are more competitive and function better than others. It often may be unnecessary to create blunt regulatory interventions to assist consumers in relatively competitive markets, generally free from market failures. In such markets, non-binding co-regulation may be the best approach to supplement the general provisions of the Trade Practices Act. For example, a non-binding code of conduct may be all the competitive stimulus market participants need to focus their efforts on consumer interests. In less competitive markets, suffering more severe market failures, more binding co-regulatory or mandated mechanisms may be required.

Selecting the right tool to address market failure, to prevent harm to consumers, requires a careful balancing act since the cost of market intervention is usually also borne, ultimately, by consumers.

Government policy should not hinder the expansion of national markets

My third principle is that regulation and policies generally should not hinder the development of national markets. This may seem a curious theme to introduce at a consumer congress. But consumers do have a lot to gain from national markets.

Over the past few decades, market reforms like trade liberalisation, coupled with technological advances, have changed the face of the traditional marketplace.

Consumers stand to gain significantly if firms are able to operate nationally. Firms operating in national markets may have greater capacity to keep costs down by achieving economies of scale, and national firms can exert a competitive discipline on local firms. With effective competition policy, those cost gains will be passed onto consumers. Moreover, national markets usually produce an efficiency dividend in terms of better quality goods at lower prices. They mean more consumer choice, greater accountability for firms, and more niche operators. They are more dynamic, more competitive and, although you will often hear argument to the contrary, more reliable than regional markets.

The Government continues to encourage the expansion of national markets through a variety of initiatives. The Council of Australian Governments, COAG, is progressing reforms across the policy spectrum to benefit consumers in this way. In particular, COAG continues to develop and implement the competition stream of the National Reform Agenda that

incorporates reforms designed to boost Australia's productivity by facilitating competition and the efficient functioning of national markets. This includes harmonising regulations which, to date, have operated to segment markets.

At its February 2006 meeting, COAG also committed to reducing the regulatory burden across all three levels of government. COAG has, for example, identified harmonising product safety regulation as a consumer policy priority for all Australian governments. The Productivity Commission review into product safety concluded that a single national system of product safety could make a significant contribution to the development of truly national product markets.

In an increasingly national, indeed global, market for goods, different product safety regimes in each Australian state and territory place a significant compliance burden on many firms. If industry were required to comply with a single, national product safety regime, the potential cost savings could flow to consumers in the form of better quality goods at lower prices, and it is likely that consumer safety would be more readily assured.

More generally, consumer protection goals would be enhanced considerably by all Australian governments working together to formulate policy which supports national markets.

Consumer empowerment is the priority

My fourth principle is that government policy should empower consumers and protect them where required.

While competition laws are directed to making markets work efficiently, consumers also need policy protection to ensure they can exercise effective choice. Such interventions empower consumers to drive the market and activate competition.

A consumer who is informed about price, quality, range and availability is an empowered consumer. Of course, that doesn't always mean that he or she will make rational choices. Indeed, contemporary insights from behavioural economics describe systematic departures from rational consumer decision making.

The central insight of behavioural economics is that people form judgements intuitively, not rationally. Intuition is not precisely the same thing as perception, but it has strong links to the essentially automatic processes of perception. Thus, judgements tend to be made quickly, effortlessly, automatically and emotionally. And they are affected strongly by current

stimulation. As Nobel Laureate Daniel Kahneman puts it, ‘the central characteristic of agents is not that they reason poorly but that they often act intuitively. And the behaviour of these agents is not guided by what they are able to compute, but by what they happen to see at a given moment’.¹

Consumer policy should be designed to empower consumers, in the sense of making it much more likely that they take decisions in a rational manner. The many laws requiring product information disclosure are designed to empower consumers in precisely this sense; as are laws prohibiting misleading and deceptive conduct.

A good example of how the Treasury is working to empower consumers is through the work of the Financial Literacy Foundation.

Modern financial markets are complex, and recent policies have enabled individuals to take more responsibility for their financial decisions, particularly in relation to retirement savings. But consumers need to be confident and well-informed if they are to take advantage of the opportunities and choices available to them.

The Financial Literacy Foundation is playing a key role here by working to raise awareness of the benefits of developing good money management skills and by creating opportunities for all Australians to learn more about money.

Education may not always be the answer – or, at least, not all of the answer. When it comes to government intervention, one size definitely doesn’t fit all. The best policy tool depends on the problem at hand.

Another example of consumer empowerment is product disclosure documents in the financial services sector. It appears that while assisting many consumers, product disclosure does not empower all consumers. While the law requires clear, concise and effective disclosure, financial advisors are expanding the documents in an effort to limit potential liability. Instead of being empowered by information provided in the product disclosure documents, some consumers may be overwhelmed by detail - disempowered by complexity. The task is to find more effective means of empowering the consumer.

¹ Daniel Kahneman, ‘Maps of Bounded Rationality: Psychology for Behavioural Economics’, *American Economic Review*, Vol. 93 No. 5, December 2003, pp. 1449-1475, at p. 1469.

Sound consumer policymaking also demands that we protect consumers in various circumstances. We do not rush to employ consumer protection tools, because these often lessen consumer autonomy and power, and that would obviously run counter to our broader goal of consumer empowerment.

But consumer protection mechanisms will sometimes be appropriate, and can be very powerful. Consider product safety regulation. The law prescribes minimum safety requirements for various products, effectively preventing consumers from exercising choices would that involve buying an unsafe product. This is at the Draconian end of policy intervention. Yet there are many examples where the net benefits to consumers easily justify such an apparently heavy-handed approach.

Conclusion

Consumer policy will always present challenges.

These challenges will be met best by bearing in mind four key principles: (1) competitive markets drive consumer welfare and consumers drive competitive markets; (2) government intervention in the market should utilise the regulatory or non-regulatory tool best suited to each situation; (3) government policy should not impede, but should rather support, the expansion of national markets; and (4) government policy should empower consumers, protecting them when appropriate.

The high level goal must be consumer empowerment, recognising that in some cases a consumer protection mechanism may be justified.

The four principles I have outlined will be highlighted in the Productivity Commission inquiry into consumer policy. That inquiry holds great promise. It will, I am sure, give us a strong foundation to meet the challenges of today — and position us well for the consumer policy challenges of the future.