

**Senate Standing Committee on Economics**

**ANSWERS TO QUESTIONS ON NOTICE**

**Treasury Portfolio**

Supplementary Budget Estimates

17 October – 18 October 2012

**Question:** SBT 2

**Topic:** Vocational Education and Training System

**Hansard Page:** pg 110, Wednesday 17 October 2012

**Senator CAMERON asked:**

**Senator CAMERON:** ...While the textbook conditions of perfect competition are rarely met, what percentage of the Australian economy would you describe as competitive and what percentage do you think is dominated by firms with significant market power? What should governments do about firms with that market power? You did a study into the vocational education and training system. Liberal-National governments in Victoria, Queensland and Western Australia have undertaken what I describe as a form of economic vandalism with an assault on productivity through cuts to the TAFE system and social advancement for people. Do you think that the reduction of hundreds of millions of dollars of public funding to the TAFE system will allow the TAFE system to continue to contribute to increased productivity in the nation?

**Mr Banks:** That sounds like a slightly loaded question, but we can probably respond to it in the context of the work we did on looking at the gains from VET reform more recently, including the education—

**Senator CAMERON:** That is why I am asking. I have had a look at that report and you do indicate the importance of the VET system to productivity, social cohesion and a range of other issues. If hundreds of millions of dollars have been pulled out of that system, I would like to know what the Productivity Commission thinks that will do to productivity and social cohesion.

**Mr Woods:** I can certainly confirm the first bit, because it is one of my inquiries, but we have not studied the consequence of the actions of the state governments. We will get back to you.

**Senator CAMERON:** Thanks.

**Answer:**

A number of factors suggest that significant and unchecked market power is not widespread in Australia. Due to the microeconomic reforms that have been implemented over the past few decades, including the reduction of trade barriers in the 1970s and 1980s and the implementation of National Competition Policy, markets characterised by significant barriers to entry are much less common today. (Indicators such as domestic market share and concentration can be misleading as they do not capture the scope for import competition and market entry.) Where significant barriers to entry do exist, it is largely in markets that are natural monopolies. Markets of this type normally are regulated to limit firms' capacity to set prices well above long-run cost.

This is not to say that policy makers need not be concerned about market power. The Commission has identified a number of areas of the economy in which improved regulatory settings and/or the promotion of greater competition could raise national welfare.

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Victoria, Queensland and Western Australia have announced reduced spending on vocational education and training (VET) in their respective 2012-13 budgets.<sup>1</sup> It is understood that all VET providers in these states, both TAFE and non-TAFE, will be affected. Potential impacts of the funding changes on productivity and social inclusion will depend on consequent changes in the quantity and quality of training across the VET system. In answering this question, the focus is therefore on the VET system as a whole, not TAFEs alone.

For a number of reasons, the potential effects of the reductions in spending on productivity and social inclusion are difficult to predict.

While expenditure in 2012-13 is budgeted to be lower than in 2011-12, actual expenditure could differ from budgeted amounts. For example, in Victoria, total spending on the VET system in 2011-12 was about 12 per cent higher than anticipated.

Efficiency gains could mean that levels of training activity do not fall in line with reduced expenditure. Performance targets presented in each of the Victorian, Queensland and Western Australian budgets suggest that the quantity of training delivered is expected to be unaffected by the spending changes. Further efficiency gains would be consistent with recent trends around the country — government real recurrent expenditure per hour of training delivered fell between 2008 and 2010 in many states (SCRGSP 2012).

In Victoria, co-contributions from students and industry are likely to increase, offsetting to some degree the decline in government subsidies.<sup>2</sup> The impact of the resulting increase in price on the quantity of training demanded will depend on how prospective students respond.

In general, a reduction in a subsidy will result in higher consumer prices and lead to a reduction in the quantity demanded, but some consumers will be prepared to pay higher prices. Higher prices for some courses would also likely lead to substitution towards cheaper courses. Some prospective students would choose not to enrol at all. The sign of the effects on productivity of course substitution is uncertain, but more straightforward where people choose not to enrol in further training — all else equal, it will be negative.

As Victoria's recent experience illustrates, it is difficult to estimate future expenditure in a demand-driven, fully contestable system in which eligible students are entitled to a government-subsidised place. Changes in the structure of training subsidies in Victoria, with reduced funding for some courses and increases for others, also make it difficult to predict the effect of overall budget changes in that state.

Overall, because it is difficult to conclude with any certainty the effect that changes in funding will have on the quantity and quality of VET training, the effect on productivity and social cohesion is uncertain. That said, to the extent that quantity or quality decline (other things equal), productivity and national welfare are likely to decline as a result (PC 2012, *Impacts of COAG Reforms: Business Regulation and VET*, Research Report, Volume 3 — VET, Canberra.).

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<sup>1</sup> The Question on Notice refers specifically to these three states. New South Wales also announced expenditure reductions in its 2012-13 budget, and again in September.

<sup>2</sup> Among recent changes to the Victorian VET system, providers are now free to set the prices that they charge students for training (DEECD 2012a, *Refocusing Vocational Training in Victoria*, <http://www.education.vic.gov.au/Documents/about/department/refocusingvetstatement.pdf> (accessed 16 November 2012)).