Australian drought policy: Notes on collateral damage and other issues

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Introduction

Drought is a familiar topic to Australian agricultural and resource economists. So much so, it is almost impossible to say anything original about the subject. And I am about to confirm that is still the case.

There is a yawning gulf between professional opinion about drought and what passes for official policymaking and journalistic commentary. The response to the widespread drought in eastern Australia in 2018 has been low rent with little regard for the facts of Australian agricultural geography, especially that Australia has vast semi-arid areas where agricultural and pastoral activities are always vulnerable for weather and non weather-related reasons. So trivial was the coverage of the recent drought that prudent management of drought risks practised year-in-year-out by most farmers was described by the ABC as 'defying the drought'. There is a similar gulf between informed and lay opinion for other topics of interest to this audience: for example, the economics of irrigation, and agricultural development in northern Australia. It turns out that these two topics have been influenced directly by community attitudes and political responses to drought. The link between the deeply flawed Murray-Darling Basin Plan (MDBP) and the Millennium Drought is a recent and important example. This observation suggested the major theme of this note – collateral damage from drought.

In preparing for this meeting, I reread the Proceedings of a 1967 Bankers' Conference on Drought that was organised by the Reserve Bank of Australia. The approach of twenty or so papers in the Proceedings is rational and empirical. Underlying economic issues surrounding drought were then much the same, although prevailing economic circumstances were different. Agriculture was still an important part of the economy, and the wool industry was dominant within agriculture. The major difference was the then highly regulated financial market. Market-oriented economists like Keith Campbell and Jack Lewis pointed out ways that application of financial regulations handicapped commercial farming operations, especially in the Pastoral Zone.

The politics of drought was different. In an era with different information and communications technology, stark images of the effects of drought were not on daily display. Drought was dealt with in a less excited way.[1]

[1] An interesting account of how farmers coped with drought in the past is given by the historian Rebecca Jones (2017) in *Slow Catastrophes: Living with Drought in Australia.* The book is based on diaries kept by farming families. Conservative strategies for managing drought risks were appreciated from earliest times.

The difference between sophisticated and unsophisticated views on drought is more or less defined by the extent to which drought is regarded as a normal risk of Australian farming and, for that reason, mainly a private responsibility, or a contingency so difficult to manage that risk management should be a responsibility for government. Casual observation suggests the balance has swung towards the latter view, and to the Commonwealth Government at that.

Putting the above remarks slightly differently, the political economy of drought is influenced by the economic perspective taken with respect to risk management in general, and empirical judgements about the functioning of rural credit markets and the social security system. Also at play are well-known controversies concerning the role of ad hoc policymaking vis-à-vis government commitment to a pre-determined strategy applied to policy problems, economic and otherwise. While a case can be made for discretion rather than rules in situations of great uncertainty, discretion easily descends into rent seeking and opportunism in policy making.

Like genuinely interesting questions in a mixed economy, there are a few twists and turns in the public economics of drought. Notably, the systemic occurrence of drought due to the 'El Nino Southern Oscillation' (ENSO) phenomenon, which limits the scope of private drought insurance because large numbers of farmers find themselves in similar circumstances (Stoneham et al. 2004). Furthermore, the temporal and spatial features of drought raise difficult questions like definition and declaration of drought, eligibility criteria for assistance, and the meaning of 'exceptional circumstances'. A complication for drought policy is that intervention to support farmers can be counter-productive by discouraging self-insurance, exacerbating the environmental and animal welfare consequences of drought. The latter are now more relevant with further urbanisation and a decline in agriculture's share of the economy.

Stoneham et al. (2004, table 2.2, p.12) report interesting comparisons between farmers given drought support and non-recipients. Drought assistance was more likely given to those who did not prepare for drought, farmers with higher net asset values and farmers who were less cautious in farm and financial management. This sort of research should be continually updated.

The public economics of drought involves decisions concerning the 'whom', as well as the 'when', 'what' and 'how much' of government intervention. Sometimes disarming (shameless) in their frankness, state governments have almost given up defending their traditional responsibilities for land management, in the face of increasing Commonwealth financial power. Queensland Minister for Natural Resources, Dr Anthony Lynham, said recently in relation to a dodgy irrigation proposal emanating from Canberra "If you want to build infrastructure for the benefit of Queensland, I'll take your money" (ABC News 2018)[2].

[2] The same news item refers to $230 million extracted by Kennedy MP Bob Katter for irrigation projects in return for supporting the Morrison Government.

Collateral damage from drought

It is now a commonplace for agricultural specialists that the enthusiasm for irrigation in south-eastern Australia starting in the late nineteenth century was a consequence of misguided appreciation of the economic opportunities confronting Australian agriculture. Professional scepticism about the role of irrigation in Australia is well based. It depends on application of classical principles of production economics and comparative advantage together with accounting for the extreme variability of Australian rainfall and runoff for the capital costs of irrigation, on-farm and off-farm (Davidson 1969, 1981; Randall 1981; Watson and Rose 1980; Watson 2007). Market prospects for irrigated commodities are part of the equation. Concern with the environmental consequences of irrigation came later.

Just as well known from the writings of Bruce Davidson and others is that early adventures with irrigation were encouraged by nebulous plans for drought proofing Australia; an aspiration that went by the board when enthusiasm for irrigation confronted the large number of uneconomic farms that followed closer settlement.

Similar vague sentiments and romanticism inform renewed enthusiasm for building dams to support government sponsored irrigation development in northern Australia, the inherent difficulties of which are also well known (Davidson 1965). If anything, the case for government sponsored northern agricultural development is weaker than in Davidson's day because modern earth moving machinery and pumping technology allow large properties to invest in small-scale irrigation on their own account, enhancing the profitability of the cattle industry.

The most recent expression of the nexus between drought and reckless investment in irrigation is the MDBP that was cobbled together in response to the Millennium Drought, and the 2007 Federal election. The MDBP is defective conceptually (at more than one level), extraordinarily costly, ineffective in achieving its objective of environmental remediation, and damaging to the workings of the Australian Federation.[3]

Sadly, the worst results of the MDBP could have been predicted, and avoided.[4] Among the faults of the MDBP is the over-simplified approach to the notion of 'environment', as if a multi-faceted concept could be expressed in a single word, and over emphasis on investment in off-farm and on-farm infrastructure rather than (gradual) buyback of irrigation licences alongside careful selection and implementation of environmental projects. Another unsatisfactory aspect of the MDBP was the failure from the beginning

[3] With so much evidence of bipartisan hydraulic folly, 2007 was a bad year for aficionados of water policy, and taxpayers. Drought-induced panic and ignoring professional knowledge and advice played a big part in the expensive and unsound Bracks-Brumby-Thwaites Victorian water plan.

[4] The MDBP is an example of the Abilene Paradox. After all that effort, no one is satisfied. The initial mistake of relying on planning rather than patient administration has been followed by years of confusion and escalating costs, with no end in sight.

to face squarely the difference between the environmental issues of the Murray mouth and Lower Lakes and those upstream. In essence, this is the point at which the contested science, economics and politics of the MDBP converge.

The Productivity Commission and a South Australian Royal Commission undertook separate and concurrent investigations of the MDBP in 2018. Without having read these voluminous reports in full, it appears that neither inquiry asked the fundamental question. Was the idea of a (prescriptive) MDBP ever justified? The always problematic Water Act (Cwlth) of 2007 was treated as a given in both inquiries. Hardly surprisingly, there are differences between the approach of the PC that with its predecessors has conducted several investigations of irrigation and irrigated industries in the MDB, and a one-off Royal Commission exercising legal reasoning and investigative procedures. Both inquiries produced useful results. Consistent with its earlier Inquiries and its established approach to the case for government assistance, the PC restated the failings of infrastructure investment. The PC has also drawn attention to the inability of the MDBP to satisfy its deadlines and objectives. The South Australian Royal Commission highlighted administrative problems in the development of the MDBP.

The SA RC relied in part on evidence given in public hearings by disaffected participants in the preparation of the MDBP. While there is no doubt that corners were cut in grappling with the obligation to produce an acceptable version of the MDBP on time, a pertinent question is whether these short cuts were inevitable. There can be no argument that there has been internal disagreement in the operations of the Murray-Darling Basin Authority as it attempted to meet the requirements of the Water Act to produce a prescriptive plan. The political class finds it difficult to understand that some things are not just unknown, they are unknowable. Too often in the water debate, it is forgotten that a political solution is required to a political problem. Several environmental attributes have to be reconciled. The idea that there is something called 'best available science' is nonsense. The idea of applying 'best available economics' to complicated policy problems would be laughed out of court, and rightly so.

A contributing factor to the muddle surrounding both the MDBP and drought policy is the willingness of economists and other specialists to focus on the esoteric rather than the obvious. The ambiguity of water saving from infrastructure investment and the difficulties surrounding interpretation and measurement of return flows is a second order issue compared with the costs and illogical reasoning used to justify subsidised investment in irrigation infrastructure.

Worse than ambiguous, just wrong, is the analogy drawn between HECS-type schemes and drought finance (Botterill and Chapman 2002). On both sides of the transaction, capital markets have little information on which to base student loans. The same does not apply to drought-affected farmers and their lenders. Now that social security provisions are extended to farmers during droughts, the dubious case for concessional finance is weakened enough already without creating more boondoggles. Instead, the generous eligibility conditions afforded farmers compared with other groups should be seriously questioned.

Concluding comments

Past hopes of developing a credible rule-based National Drought Strategy treating drought as a commercial risk, jointly with a disciplined approach to welfare provision, have evaporated due to lack of commitment by governments (political backsliding). Public sentiment is too easily influenced by the visible consequences of drought. The evolving pattern of increased support from the Commonwealth and state governments has undermined serious attempts to develop consistent drought policies. Today's programmes of drought relief are ad hoc and generous.

In a few respects, this is counter-intuitive. Some economic dimensions of drought favour a 'private responsibility' view of managing drought risk. Changes in technology, superior access to information and improved transport infrastructure have made droughts more manageable. At the farm level, modern machinery has made fodder conservation and handling much cheaper than previously for livestock farms. The current (or recent) drought has been characterised by high wool and red meat prices. In previous droughts, livestock were often sold at distressed prices.

What has not changed is the variation in the attitudes of individual farmers to risk.[5] And the fact that there is no single drought strategy that is applicable at an industry level. Farmers decide their own drought strategies according to their expectations and financial position. Whether agriculture in aggregate is more vulnerable financially to drought is vexed. Often, role of market/government questions hinge on judgments about the flexibility or rigidity of economic systems. These should be decided as far as possible on the basis of empirical investigation not whim.

Is agriculture more risky now than it was in the past? Modern production systems use more purchased inputs that have to be financed. Are the hard luck stories of farmers' treatment by the banks revealed in the Banking Royal Commission sufficient evidence to require major changes to the rural credit system? Careful evaluation of arrangements for agricultural finance in past panics, drought and otherwise, have shown that not to be the case. What of corporate farming and the increasing specialisation of large family farms for dealing with drought risks.[6]

These issues are worth thinking through because the prospect of climate change changes the reference point for drought. If climate change is the harbinger of the unfavourable weather patterns traditionally associated with drought occurring more frequently, drought ceases to be what was previously understood. What was once judged out of the ordinary has become the norm.

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[5] Recent developments have vindicated an earlier remark of Ross Parish. An effective drought strategy for individual farmers is to 'do nothing, then scream'.

[6] The challenging observations of Charles Massy (2017) are of some interest even for critics of his approach. Without much doubt the aesthetics of large-scale cropping systems in much of Australia are less appealing than the mixed farming systems of yore.

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