

Dry Down Under: Australia's water woes

AN INTERVIEW WITH ANNA WILSON



Australia is the lucky country. But it is far from fortunate when it comes to water, as a searing drought over the past few years has demonstrated. A fast-growing population and bitter political divisions over climate change have further served to highlight the difficulties Australia faces in managing its scarce supplies water. Anna Wilson, an economist at Frontier in Australia with extensive experience in water markets, looks at the policy reforms the country needs to consider.

What are the central issues concerning water supply in Australia over the coming decades? I suspect climate change is one of them?

Climate change is undoubtedly one of the primary challenges. Projections suggest that, in general, Australia will have a hotter and drier climate in the future. We have already seen the extent to which the water sector is sensitive to changing conditions. During the last decade large swathes of Australia experienced the most extreme drought on record. We called it the Millennium Drought.

Another emerging challenge is the expanding population. Australia's population is expected to grow from around 25 million today to nearly 40 million by 2056 with most of this growth occurring in the major cities.

What do these twin challenges mean for the current regulatory regime?

Adapting to climate change and population growth will require increased capital funding for new infrastructure and to upgrade old infrastructure. It should be expected that water prices will need to go up. However, there is a risk that governments will attempt to limit the rise on grounds of affordability. That might hamper the ability of the industry to operate on a financially sustainable basis. Generally, the economic regulatory regime will need to adapt to help facilitate innovation, efficiency and investment.

In addition, it will be important to make sure wider customer objectives relating to security of supply, health and the environment are more clearly established and specified.

What are the main changes that will be needed to rise to the challenges?

It will be critical to establish efficient regulatory and governance frameworks that are more independent of government. Australian urban water businesses are not privatised and not all of them are subject to independent economic regulation, where regulators can determine or approve prices. Frameworks like this will not guarantee a financially sustainable price path for utilities, so the risk is they will fail to create the certainty needed to encourage long-term planning and investment.

More work also needs to go into resolving the long-term structure of the market to spur greater competition and private involvement. The Australian urban water sector has been very effective in using outsourcing and other contracting models. However, new players want to enter the industry. The problem is that in many states the frameworks are not in place to allow them to do that at the same time as protecting wider customer interests. There's scope for innovative, decentralised mechanisms to be introduced, but the market structures and wider legislative arrangements need to be clear.

Also, it's becoming more important in Australia, as it is in the UK, to make sure there's strong and transparent engagement with customers so there's a better understanding of what people want from their water suppliers. Interestingly, recent research has shown customers are willing to pay a significant amount to avoid water restrictions. It seems Australians are very unhappy when local playing fields - sports ovals, Down Under - can't be used during droughts!

Is there an opportunity to experiment with different approaches, or is it too late?

Right now, with the end of the Millennium Drought, the sector is actually no longer in 'supply crisis' mode. I would argue this is the best time to begin further structural and regulatory reform in the sector. It's definitely not too late.

You spent some time in the UK and in Europe earlier in your career. What are the lessons for us from the work you have been doing more recently in Australia?

I think the lessons that can be drawn from Australia largely relate to how to manage water scarcity. Australia's management of rural water is very progressive. Past reform efforts have focused on pushing through efficient water use, water allocation and management in the Murray-Darling Basin. In this basin, which is larger than France and Germany combined, irrigators can buy and sell water and water rights relatively seamlessly.

Irrigators are not only accepting of these markets, they positively rely on them. Frontier's past work has highlighted how water markets have enabled industries to survive and production to be maintained during the Millennium Drought. So, I think Australia has some important lessons it can share with the UK and Europe in terms of the value of water markets, how to set them up and how to ensure they operate efficiently.

In an urban context, Australia has really been forced to consider the full gamut of water supply and demand management solutions. The use of localised and decentralised supply and of sustainable drainage systems (SUDS) is well accepted. Frontier has been heavily involved in advising on the removal of various barriers - policy, regulatory and business-specific barriers – so these practices can become the norm.

Finally, taking a broader view, how do you think the availability and cost of water ties into the debate about how to boost productivity and growth

I think Australians are acutely aware that water - or a lack of water - is a major constraint on the country's growth, given the importance to the economy of agriculture and mining, both of which are heavy water users.

However, they are less aware of how important well-designed regulatory frameworks and pricing methods are. They can help drive efficient water use in urban areas. They can ensure there is an appropriate level and mix of investment in new supply, demand management and leak reduction. And they can spur innovation and improved productivity within the industry.

Anna is an economist who specialises in network regulatory issues. She heads Frontier's Australian transport practice and has significant experience developing policy reforms and regulatory regimes in the water and transport sectors, in both Australia and Europe. Anna also has worked extensively on the assessment and development of access pricing regimes to enable private sector participation. Before joining Frontier, Anna was an acting director in the Australian Competition and Consumer Commission (ACCC), where she helped develop the rules governing Australia's water markets.