A fail grade for market deregulation

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The older I get, the more cynical I become about government intervention in the economy. That statement might appear to be either a recantation of everything I’ve ever argued, or a sign of the usual tale of left-wingers moving to the right, and right-wingers to the left, as life experience tempers youthful exuberance. It’s neither (well, okay, maybe it’s a bit of the latter), because my developing position reflects the complexities of a mixed economy. The latest real world experience that has pushed me further into cynicism about government is a very personal one: an attempt by the Australian government to increase competition in education via deregulation is the direct cause of the proposal to terminate the economics program at my university. The policy change will actually reduce competition in the education marketplace in Australia: the market was more competitive with the preceding regulations in place.

Is your head spinning yet? Let me clarify the position by explaining why my university (the University of Western Sydney) is proposing to shut down its economics program.

Government regulation used to require universities to set a minimum entry standard to apply for entry to courses based on performance at the final school exam (now known as an “Australian Tertiary Admission Rank” or ATAR). Deregulation of the sector means that this is now optional, and two major universities in my region – the University of NSW and Sydney University – have responded by letting students apply for a course regardless of their anticipated performance at high school. When a minimum ATAR was indicated, many students who thought they wouldn’t get a good enough high school result to qualify at one of the higher ranked universities would hedge their bets by also applying for entry to some of the lower ranked universities – including UWS. That then meant that at the end of one academic year, there was a reasonable spread of
applicants across all universities: the top-ranked universities got the lions’ share, but there were applications too for the lower-ranked universities, from students who also expected to be more lowly ranked.

Now that open slather is permitted, students have responded by applying for courses only at the top-ranked universities. So now, as the current academic year ends, the projected intake into UWS’s economics program is catastrophically low. In previous years we had well over 100 applicants for our first year intake at this point. This year, we have just 19.

UWS management’s reaction to this has been to propose to shut the degree down completely because it is no longer economically viable. As they put it to one of the many ex-students who has complained about the decision: "Whilst we acknowledge the tremendous achievements of our staff and students in raising the profile of economics at UWS and beyond, unfortunately, at the present time just 19 students are forecast to enter the B.Ec course in 2013, which renders the course economically unsustainable. This is largely attributable to the advent of the open market for undergraduate courses which was implemented this year."

Bravo! An attempt to make education more competitive will actually end up reducing competition.

Since all prospective students are applying to the “Sandstones” (as the prestigious universities in Australia are known), prospective enrolments at other universities have plummeted. Managers then face two options: put the courses on regardless and hope actual numbers improve, or shut them down now. The simple reaction is to shut them down – which is what UWS is proposing to do.

You might argue that this is just a knee-jerk reaction by bureaucrats who lack the nous that entrepreneurial managers of private universities might have. The latter could see through the change in policy, and anticipate that numbers will have to improve: the Sandstones don’t have the capacity to take all applicants, so once the actual high school results are known, they’ll fill their lecture theatres to the rafters with high-achieving students, and send rejection letters to the rest.

The rejects will then have to apply to the lower-ranked universities, and the actual numbers at the beginning of the next academic year will be better than the prospective ones right now. From this perspective, the right
response would be to privatise universities and have them run by entrepreneurial capitalists, rather than cautious bureaucrats.

There’s a modicum of truth in that argument, but even if universities were run by far-sighted entrepreneurs rather than cautious bureaucratic bean-counters, this move from a regulated to an unregulated market would still have reduced competition.

Firstly, the Sandstones will increase their share of the market. By squeezing every last available student into their lecture halls, their higher capacity utilisation will reduce the share available to the other universities. Secondly, even a privately run university would be squeezed – especially if its activities were partly debt-financed (as they inevitably would be). Not reacting to a downturn in demand by cutting back on capacity would court bankruptcy.

The best economic model of this conundrum – that a less regulated market can be less competitive and less diverse – was developed by Hotelling.

Imagine a beach with an even distribution of bathers: where is the best spot for an ice-cream shop to set up business? The simple answer is right in the middle of the beach: that maximises the market (the less people have to walk, the more likely they are to buy an ice-cream) and it suits customers too – they have the shortest possible walk to get an ice-cream.

But what if there were two ice-cream vendors? Socially, the best situation would be for one to locate one-third of the way along the beach, and the other two-thirds along it. That way, they each get half the market, and customers only have to walk a maximum of one-sixth of the beach’s length to buy an ice-cream. That’s a great improvement over a maximum walk of half of the beach.

However, if one of the vendors moves closer to the other vendor, he will increase his market share at the other’s expense (if consumers don’t differentiate between them). At the extreme, one vendor can capture 67 per cent of the market by moving right next to the other vendor: he will get 100 per cent of the purchasers from two-thirds of the beach. If left to free competition, both vendors would end up right in the middle of the beach – forcing customers to have to walk up to 50 per cent of the beach to get an ice-cream – and the vendors would still split the customers 50:50.

You’d get a socially and economically better outcome if vendors were regulated, and required to set up some minimum distance apart from each
other: people would have to walk less, and ice-cream sales would rise because of the shorter walk to get an ice-cream.

What is happening now to higher education in Australia – and to my department at UWS in particular – is a classic example of this phenomenon. And therein lies a conundrum. I’ve spent a fair part of my life watching government meddle in education in ways that were ostensibly designed to improve it, but in practice diminished it. Instances range from the abolition of the three-tier system we used to have – of universities teaching intellectually-oriented disciplines and professions, CAEs (Colleges of Advanced Education) teaching skill-oriented occupations and TAFEs (Technical and Further Education) teaching industrial and skilled labour occupations – to the two-tier system today, to the introduction of HECS (the “Higher Education Contribution Scheme”) – which was supposed to make students contribute to the cost of their education, and has instead resulted in a student body more focused on earning money to pay fees than studying and learning (there: I’ve now earned my grumpy old man badge).

The moral in part is that old classic, “if it ain’t broke, don’t fix it”. Governments have “fixed” higher education so many times now that it’s well and truly broken. Rather than attempting to improve complex systems that they clearly don’t understand, politicians and bureaucrats should respect what has evolved over time, and stop devising simple solutions – such as “let’s introduce competition into education” – to complex systems.
Do the maths on education funding

The rapid rollout over the past year of massive open online university courses, or MOOCs, illustrates how university education is becoming a global commodity. While Australian universities face pressure to launch online courses, the Gillard government is aiming to increase the quality of university teaching and research. One of the goals listed in the Asian Century white paper released in late October was that 10 of our universities would be in the world's top 100 and our school system would be in the world's top five by 2025.

But universities are struggling to accommodate the surge in student numbers since the government relaxed restrictions on place numbers in 2010 as a result of the Bradley review in 2008. The Gillard government argues that funding for universities has increased. An Ernst & Young report released in July showed funding per student was $2000 higher in 2013 than in 2008. But the government will not loosen the antiquated regulations on fees that universities can charge students. Instead the talk is about extra government spending on education, such as the $6.5 billion in extra funding that the Gonski report recommended for schools.

Former head of the Commonwealth public service Mike Keating has raised the provocative idea that rather than increasing schools funding, we should cut it. Mr Keating's belief that we are wasting money on schools and should divert the funds to vocational training has some support. Labor MP and former ANU economics professor Andrew Leigh and ANU researcher Chris Ryan showed in a 2009 study that despite a 10 per cent increase in real per-child school expenditure between 1975 and 1998, which paid for smaller class sizes, literacy and numeracy performance declined.

As the gap between tax revenue and spending widens, it's time to re-examine such ideas, because finding extra funds to deliver on the education goals in the Asian Century white paper will be difficult indeed. In July, Fred Hilmer, the University of NSW's vice-chancellor and chairman of the group of eight universities, said if his university could charge students in better paid professional courses such as law and medicine 25 per cent more, the university would raise $30 million a year.

If the government is serious about creating elite universities and high quality schools, it should change the present system of capping university fees and give them more market flexibility.
Totally off-key

No matter how much spin Peter Tregear (Letters, November 8) puts on it, he can’t alter the fact that the ANU has sacked or made redundant many of Australia’s top-performing musicians. Apart from those trying to finish their altered degrees, students who graduate after 2013 will be academics, work in the music industry or be teachers, not performers.

Telling the Canberra community we should basically stop grumbling and support the new-look School of Music is a bit much considering we tried hard to support and retain what was already there – a topnotch, world-class performance facility. If, as he seems to think, performance standards won’t slide, who are these new staff members who will outshine those who lost their jobs? Students wanting to be performers won’t be coming here any more. Who will be performing?

Lis Hoorweg, Campbell

It’s a bit rich for Peter Tregear, head of the ANU School of Music, to claim the future success or failure of the school rests in the hands of the Canberra community (Letters, November 8). Whatever is now the fate of the school, it remains the full responsibility of the ANU Vice-Chancellor, Ian Young, and the ANU Council who forced enormous budget cuts on the school despite overwhelming opposition. These cuts have sparked the mass redundancy of internationally renowned music educators seen over the past two months, presided over by the new head of school. The school has been left with a handful of staff, minimal capacity to offer programs in 2013 and the absence of the very teaching academics who would draw new students and encourage existing ones to stay on.

No amount of pre-emptive blame shifting will disguise the fact that the brutal cuts to the School of Music budget were inevitably going to have drastic consequences for the maintenance of high-quality music education at the ANU. The ANU vice-chancellor must recognise this form of cold and indifferent economic rationalism is ultimately destructive and is a wholly inappropriate imposition on the fine educational work of Australia’s national university.

Stephen Darwin, ACT division secretary, National Tertiary Education Union