

# MEDIA RELEASE

**EMBARGO: Sunday June 4<sup>th</sup>, 9.00 pm.**

## **Revamp drought policy to focus more on preparedness, less on emergency help**

Future Australian drought policy should be focused more on encouraging farmers to prepare for the next drought, and less on providing assistance once a drought occurs.

This is the consensus among six experts who have contributed papers on drought policy to the latest edition of the *Farm Policy Journal*, released today by the Australian Farm Institute.

There was general agreement amongst the authors on a number of broad principles.

Most agreed that the Exceptional Circumstances Relief Payments – equivalent to the Newstart Allowance – should continue to be available as welfare assistance for eligible low-income farm families in drought areas.

Most authors also agreed that stronger incentives are needed to encourage farmers to better prepare for the next drought. These could include tax concessions associated with expenditure on fodder and water storages, or incentives to develop comprehensive drought management plans.

There was also strong support for improved government provision of training and information for farmers, so that climate risks are better understood and can be monitored more effectively.

There was less agreement, however, on the current Commonwealth farm business support assistance, which takes the form of interest rate subsidies for eligible farmers. Most argued that this assistance is only available to a small number of farmers, and sends the wrong signal by rewarding farmers who are less well prepared for drought. Some also argued that it may be impeding the development of commercial risk management tools such as insurance or weather-linked derivatives. The majority view was that the assistance in its current form should not be available as part of future drought policy.

A number of authors proposed modifications to farm business support. They suggested it should only be available as a loan or under a contract arrangement where farmers are required to demonstrate they have undertaken adequate drought preparation, and are carefully managing the natural resources on their farm.

A notable feature of most of the discussion was a recommendation that governments need to take a long-term perspective when developing drought policy. Most authors warned of the dangers of knee-jerk responses within a drought, and the need to signal future changes well in advance so that farmers have a clear understanding of the risk-management strategies they need to undertake, and time to implement them.

**Further information: Mick Keogh BH (02) 9690 1388 AH 0418 256 066**

**(Abstracts of Journal Papers Follow)**

### **Taking National Drought Policy Forward**

**Peter Arkle**, Policy Manager – Rural Affairs, National Farmers' Federation

The agreement of governments on the National Drought Policy (NDP) in 1992 marked an evolution in how drought is viewed in Australia. From the time of agreement, drought was cast as a business risk and farm managers were expected to prepare for and manage all but the most extreme droughts. Now 14 years on, the true success of the NDP must be assessed in terms of the practical contribution the policy has made in assisting farmers to prepare for and manage a drought event. The severe 2002–05 drought has provided an opportunity to reflect on this contribution. Encouragingly, Australian farmers were better prepared than in previous droughts, and there is evidence to indicate that the NDP has played a major role in providing farmers with improved risk information, enhanced farm risk management skills and, to a lesser extent, assistance in building financial and physical risk reserves. This enhanced preparedness also appears to have reduced relative demand for exceptional circumstances assistance, suggesting that Australian farmers are making strong progress towards self-reliance. That said, many farm managers do acknowledge that more could have been done to prepare for the drought, and Ministers, by agreeing to the 2005 NDP objectives, have recognised the need for a greater policy focus on improving drought preparedness.

### **Drought and Structural Adjustment**

**Jim McColl**, Research Fellow CSIRO Land & Water

**Mike Young**, Chief Research Scientist, CSIRO Land & Water

Australian history is rich with stories of the adverse effects of attempting to shore up existing businesses experiencing financial difficulties rather than allowing new businesses the opportunity to enter and other existing businesses to adjust and expand. For drought policy, this observation presents a dilemma – does one help those in need or does one bite the bullet and let change occur? Nearly all recent reviews have made the observation that communities and also long-term productivity will be best served in terms of equity and efficiency if drought policy restricts itself to the delivery of programs that expedite change and, where necessary, provide welfare assistance to families using a separate policy processes. This approach makes it possible to allow the best businesses to prosper whilst simultaneously providing welfare assistance to families in need.

### **Dry Enough For You? Farming, Drought and Policy in a Dry Country**

**Bill Malcolm**, School of Agriculture and Food Systems, University of Melbourne

Drought is inevitable in farming in Australia. Current government policy for dealing with the consequences of drought wastes resources and worsens public wellbeing. Drought policy perversely penalises farmers who run their businesses in ways to cope with drought. Instead, it encourages farmers and those with whom they deal with to take more risk. Farmers and people in their markets for inputs and outputs can do many things together to manage farm risk, including drought. Farm businesses with good prospects for profit and growth would be better off if drought risk was no longer subsidised and, instead, if these farmers increasingly worked through markets to manage the risks of their farm businesses, including drought. Nearly everyone else would be better off too.

### **Drought Policy – Impact on Farmer Decision-making**

**Rob Brown**, Adviser, Peppin Planners

Income and interest support during drought events defined as exceptional circumstances are rarely if ever incorporated in farmer decision-making pre-drought. They are also inappropriately targeted to a minority group of eligible farmers and are either poorly or negatively related to drought policy objectives. Current drought objectives should be extended to include the need to support people with the psychological pressure of prolonged drought and in recognition of political pressure to 'support farmers'. A loan type framework is proposed to provide broader, simpler and more equitable access at lower cost. Savings in crisis measures would be better directed toward six key areas: improving research and development targeting better productivity and environmental outcomes between and during drought; improving information availability for farmers; improving availability of regionalised drought risk measures including mandating 'drought risk health warnings' on finance and land/water transactions; cohesive and consistent measures supporting on farm improvements and rewarding on farm environmental benefits; and, finally, removing disincentives and supporting intergenerational transfer.

### **Incentives, Information and Drought Policy**

**Arthur Ha**, Principal Economist, Economics and Policy Research Branch, Victorian Dept of Primary Industries (DPI)

**Bill Fisher**, Manager Economic Services, Victorian DPI

**Jane Harris**, Senior Policy Adviser, Consumer Affairs Victoria

**Gary Stoneham**, Chief Economist, Victorian Department of Sustainability and Environment

**Loris Strappazzon**, Lead Economist, Victorian DPI

It is very difficult if not impossible to design an efficient and fair drought policy that relies on retrospective revelation of information, as attempted by the current National Drought Policy. Better policy must take account of: hidden information (adverse selection); hidden actions (moral hazard); lack of 'persistence' in government responses; and how drought policy interacts with other policy instruments such as tax concessions for the agricultural sector. The private insurance sector faces similar problems, and deals with these by providing incentives for truthful revelation of type, rather than 'one size fits all', by offering a 'menu' of contracts. This approach could be applied to drought policy.

### **Income-contingent Loans for Drought Relief**

**Bruce Chapman**, The Australian National University

**Linda Botterill**, University of New South Wales

**Michael Egan**, RMS Accountants

There is arguably a consensus that the current approach to drought relief is in need of reform and possibly replacement with an improved government financial assistance mechanism. This paper outlines the potential advantages and challenges associated with the implementation of income-contingent loan arrangements for drought relief as a possible alternative to the existing interest rate subsidy scheme. The conceptual basis of income-contingent loans is explained, and reference is made to the application of policies of this type in other areas of government financial intervention. The paper addresses the administrative challenges associated with such a policy reform, with reference to the idiosyncrasies of agricultural financing. An illustrative example is offered of what an income-contingent loan applied to drought assistance might mean for the time stream of both revenue for the Commonwealth budget and repayment obligations for farms of differing economic size.