SAKELIGA

SELFSTANDIGE SAKEGEMEENSKAP

31 July 2020

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TO: **Portfolio Committee on Transport**

ATTENTION: **Valerie Carelse (Committee Secretary)**

DELIVERED: **By email: vcarelse@parliament.gov.za**

BRIEF COMMENT: ECONOMIC REGULATION OF TRANSPORT BILL

The following comment provides Sakeliga's perspective on the Economic Regulation of Transport Bill. The objects of the bill outline the core reason for the Bill, which is to establish a Transport Economic Regulator (TER) and the Transport Economic Council (the "Council").

Sakeliga represents more than 12 000 members across various industries in South Africa. Transport is a vital economic activity and core input to value creation. Our perspective on the Bill is mostly concerned with economic regulation in principle, given the current realities of the transport sector. Obviously, a bill such as this one includes many legal intricacies, on which we will not comment at this point. It is more the principle that underlies the bill that concerns us.

While we more than agree with a central contention of the bill, which is that the Transport sector requires change due to the sizable involvement of large and monopolistic state-owned enterprises, we are unconvinced that economic regulation as put forward will solve the core problematic issues in the sector.

Broad perspective on the bill

In essence, we do not believe that economic regulation (with punitive price controls) will automatically solve the underlying institutional problems and dysfunction at large dysfunctional state-owned enterprises in the transport sector, which seems to be the main point of contention. Note, however, that, to the extent the bill paves the way for greater private-sector participation in the Transport sector, we welcome it.

Note also: We reserve our rights to consult with our legal representatives and to challenge the bill at a later stage if we determine that the bill infringes on the rights and/or interests of our members.

In the following section, we briefly outline some of our main concerns:

- The memorandum of the bill rightly determines that, "*the South African institutional framework of transportation is dominated by large state-owned companies, who have a very high degree of market power over either the infrastructure or services, which they operate.*"
- Unfortunately, the bill seeks to address such problems of institutional arrangement and intra-enterprise inefficiencies mainly by means of expanded, more centralised economic regulation and

an expanded even punitive price control regime. Obviously, a bill such as this one includes many legal intricacies, on which we will not go into at this point. It is more the principle that concerns us.

- Rather, we agree with economics subject matter experts, such as Prof Mike Muller's and Dr Sean Muller's claims and concerns[1] that similar regulatory models, e.g. Nersa with Eskom, has not worked as envisioned South Africa. In other sectors, the performance of regulators, such as ICASA and water regulators, on face value, is also not producing the value that was hoped for.
- Even the National Development Plan's documents by the National Planning Commission[2] have attested to the shortcomings of economic regulators*: "**Although regulators have succeeded in issuing licences, developing pricing methods and establishing technical and service standards, they have not achieved the positive outcomes initially envisaged**. Based on the performance of the ICT, electricity and port sectors, South Africa is slipping down international benchmark rankings. The reliability of electricity supply has deteriorated and prices that were previously below economically viable levels are now climbing at rates that consumers are unable to absorb. Communications quality, speed and cost are significantly worse in South Africa than in comparable nations, with a similar situation in rail and port performance." [Emphasis added in bold].*
- Of special concern to us is clause 4 of the bill, which allows the minister to apply economic regulation to public as well as to private enterprises under certain conditions. Are constitutional concerns involved? To what extent would this deprive the commercial and other rights of private enterprises? On this point, we may decide to seek further legal opinion.
- Stated simply, if economic regulation, on appearance, failed so abysmally in other sectors, why should the public assume it to work on an even larger scale in an even larger and highly complex sector of the economy?
- If the problem really is the "domination" of large public-owned entities in transport, why should price controls or similar interventions solve the problem? Consider, by way of example, that a punitive price control on Eskom, in our estimation, is unlikely to solve institutional problems within Eskom. The most likely consequences, in our view, include unhealthy distortions of prices in the market, likely losses of revenue for Eskom, and eventually, because Eskom cannot be really out-competed for poor behaviour by market competitors, further demands on the taxpayer for bailouts. Equally then, we wonder, why should we assume a different outcome in the transport market which is "dominated by large state-owned companies"?
- The possibility of irrational resource allocation should also be considered. Price controls affect consumer behaviour. Consumers do respond to prices changes even if those prices are not rational market prices. Likely effects of relative resource over-consumption or unnecessary consumer shortages should be guarded against. Yet, it is unclear how a regulator would precisely determine possible trade-offs in the competing uses of rivalrous economic resources and tax monies.
- Price controls and similar interventions, in our estimation, do not in and of themselves foster a market-based or "economic" allocation of resources, especially in markets greatly distorted by government ownership and regulatory barriers that prevent entry to competitive players. Price control, in this instance, will take into account final consumer prices, but may fail to consider cost distortions and other dysfunctions of public entities that do not suffer market consequences, such as a true risk of liquidation (given among other things the possibility of bailouts).

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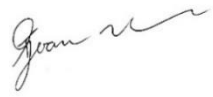
[1] Cf. Muller, S.M. and Muller, M. (2019). *Against the expansion of a failed economic regulation model in South Africa.* Draft paper presented to 5th Annual Competition and Economic Development (ACER) Conference.
[2] Cited in IBID.

- Meaningful prices are the outcome of the market process, which is an interaction between various suppliers and demanders in open markets with few government-imposed restrictions. Without a market to give valuable price information, the regulator, such as NERSA or the proposed TER, will, in our estimation, be groping in the dark.
- Even worse, the regulator itself may be susceptible to undue political influence or "regulatory capture" by special interests. This is not even to ascribe malevolence to the action of regulators, but merely the realities of incomplete information (in markets substantially influenced by state ownership) and powerful political incentives, e.g. pressure to ensure below (or above) market prices for extended periods, despite the unavoidable economic realities of resource scarcity and resource trade-offs.
- Moreover, within the void of the absence of true prices, the regulator may set prices or standards that are too high (or too low), in terms of the reality of current resource constraints and trade-offs. This would lead to opportunity costs and broader harms to overall economic efficiency. As an extreme example, the regulator could mandate that all public taxis should be to the standard of Rolls Royce vehicles, but clearly, that is an inappropriate and overly expensive allocation of scarce social resources. Yet, where should the regulator draw the line in terms of service standards?
- Granted, the current situation is untenable and requires change. On this we agree. Sakeliga, unfortunately, is unconvinced that greater centralisation and bureaucratisation of the transport sector by means of economic regulation and an overarching transport council will achieve the ends hoped for.
- We also share further concerns with Prof Mike Muller and Dr Seán Muller[3] who are of opinion that a new transport regulator may inadvertently take away valuable resources from other economic ends and furthermore, that a new regulator may not solve the actual structural issues rampant in the transport sector.
- These structural issues, we think, are best solved at the level of the State's SOE policy and by means of SOE reforms, the liberalisation of the sector and privatisation within market-centred legislative reform.

Yours faithfully,



Gerhard van Onselen

Senior Analyst: Sakeliga

[3] IBID.