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Dearie me, oh dearie, dearie, me, do we have to have fools running the country? [1]

Written by Tim Worstall [2] | Thursday 18 July 2013

Sigh [3]:

Backing a report by CentreForum, the think tank, Sir Ian said that ?many companies, especially the private equity infrastructure funds, have paid out excessive dividends to their owners?. He advocated the introduction of ?some form of dividend control?, whereby ?payments of dividends above those assumed by the regulator when setting price limits, would be accompanied by reductions in the tariffs paid by customers?.

No, absolutely not. Sir Ian has clearly forgotten what happens when you place those sorts of detailed restrictions upon regulated companies. They'll inflate their capital base, play around with loan interest, pay the management more: whenever you try to micromanage like this you'll find people gaming your micromanagement.

What we actually want to happen is how we did this regulating of prices immediately after privatisation. We set a target for prices (RPI plus or minus something, depending upon the industry) and then let everyone rip with capitalist glee as they slashed and burned through their overstuffed workforces. Or as I suppose I should put it, increased productivity to the benefit of all. They did indeed make vast profits in doing so. Now if we had just left them alone for all time this would not have been a good solution: but we didn't. We told them that their pricing regulatory structure would be reviewed after some years. And then, that's where we got them. Because we revised the regulated prices to take account of the productivity improvements they'd already made. And quite deliberately made sure that in the next period they lost those excessive profits they'd made in the first.

There's good reason to manage affairs this way as well. Sir lan doesn't know what an "excessive dividend" is, nor do I. Nor do either of us have a clue as to how to increase the productivity in these companies and thus their profits. So, what we do is set prices (they are natural monopolies after all, we're not going to leave them alone entirely), then let them make as much money as they can for, perhaps, 7 years. They know how to increase their own productivity and so they do and they increase their profits. But we don't let them keep those for all time: we now reset after 7 years and see if they can do it again.

We're giving them the incentive to become more efficient and profitable: but the regulation of how much more grossly, fatcatterly, profitable they become lies in the reset of the regulated prices, not fiddling with dividends and rates of return inside the regulator period. For that fiddling removes the incentive for them to become more efficient, y'see?

We did in fact get the price regulatory process correct the first time around. We didn't set the right numbers, no, not at all: but we did get the process right. Go make as much money as you can for the next regulatory period. And the more you make the tighter the next set of regulations will be. This is the correct mixture of the necessary regulation over monopolists and the drive for greater efficiency.

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