INFRASTRUCTURE AUSTRALIA

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GOOD INFRASTRUCTURE IS AN ASSET, NOT A COST

Extract:

WHY WE MUST BORROW AND BUILD

An explanation of our $250 billion basic infrastructure requirement before 2025, and a positive plan, with numbers, for funding it safely and effectively.

Contact author Ian Spring on (02) 9712 5339 or at ispring@bigpond.net.au

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Why we must borrow and build

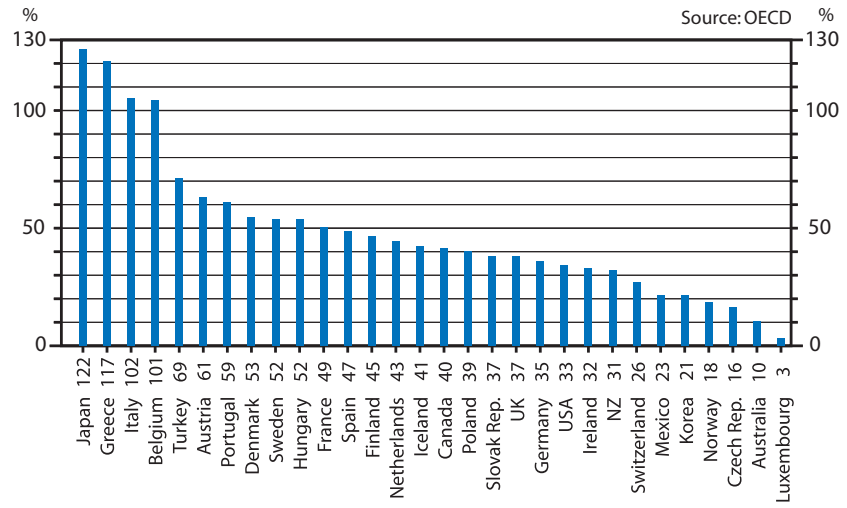
By *Ian Spring*

This article outlines a vision for a 20-year, $250 billion borrowing and building program designed to provide a safe and effective answer to Australia's major infrastructure problems.

Australia's basic infrastructure is grossly inadequate. It is the nation's most serious weakness. Current policies of not borrowing, and therefore having to fund infrastructure from taxation, are failing. Redevelopment of old infrastructure is proceeding at a snail's pace, and if we continue with present policies there will be no possibility of our building the major new systems we will need for the future.

Analysis shows that spending on major infrastructure will have to be doubled if we are to increase productivity enough to cope with our two most serious upcoming problems, countering the effects of population ageing, and maintaining

CENTRAL GOVERNMENT DEBT AS % OF GDP END 2001



NOTE: Since 2001 Australia's debt has declined to under 3%.
This is an extreme position where we are losing all the potential benefits of borrowing.

Ian Spring is an independent economist and retired business manager. This is a shortened and updated version of his paper "Borrow and Build", available at www.borrowandbuild.com.au.

international competitiveness. Such an increase in spending can only be achieved by borrowing.

What follows is an explanation of some of the background and economics of our current infrastructure problem and a positive plan, with numbers, for its solution.

Australia has almost no national debt. We also have awful infrastructure. These two things are connected. While we have followed zero-debt policies, other countries have borrowed and built and have the infrastructure to show for it.

Our national debt is under 3% of GDP - maybe near zero after the last budget. The international norm is between 30% and 50%. Having regard to the economic and social advantages of using debt, Australia is grossly underborrowed or, in financial terms, undergeared (see table on previous page).

There is no economic justification for pursuing such low levels of debt.

There is now a strong body of authoritative material, including material in very recent reports from the Australian Council for Infrastructure Development (AusCID) and the Business Council which makes it clear that prudent borrowing and spending on major infrastructure would yield enormous benefits in employment, productivity, growth, standards of living, social welfare, and international competitiveness. The sooner we start building and start getting these benefits, the better.

As background we need to look at the problems posed by Australia's ageing population. Currently federal budgets are showing strong surpluses, but this situation will not continue. Treasury's 2002/03 Intergenerational Report projects that the ageing of the population will cause surpluses to start to fade after 2007/08, and to dropoff into ever increasing deficits after 2017 (see graph below).

In response to this very serious projected fiscal decline the federal government has identified a need to improve productivity. It has, however, chosen to try to achieve this by labour market reform. With Australians already working some of the longest hours in the world, this can surely have only limited prospects of success. Real productivity payoffs can only come from major investment.

A further effect of population ageing is the tightening of both commonwealth and state budgets, so that even the current low level of tax-based spending on infrastructure would be quite unsustainable into the future.

My estimate is that over the next 20 years Australia will need to spend $250 billion in current dollar terms to bring its infrastructure to the internationally competitive standard needed by 2025 (see table above).

I propose the establishment of a Commonwealth Infrastructure Development Fund, or similar, with a degree of separation from the federal budget, and the development of a practical plan for the use of this fund to enter into a 20-year borrowing and building program.

We currently spend about $6 billion

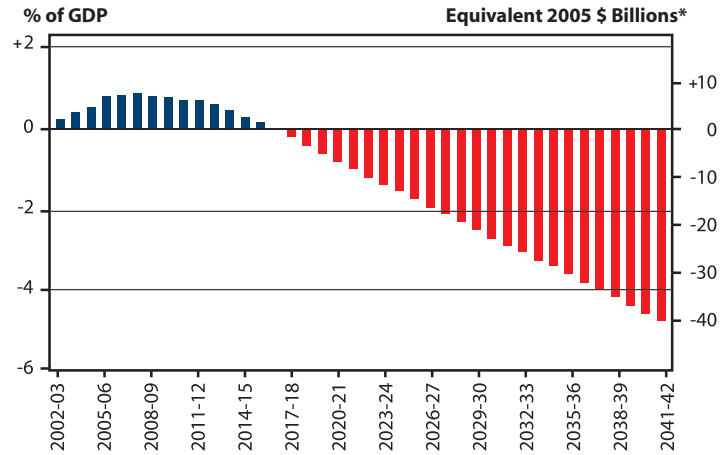
ESTIMATE OF MAJOR PROJECT CAPITAL SPENDING NECESSARY BY 2025

	2005 $
National Highways	20
Non National Highways	20
Urban Expressways	20
Great Western Highway (NSW) Expressway standard	10
Local Government	20
Electricity	30
Urban Rail Renewal (Sydney)	20
New Urban Rail (Sydney)	30
New Urban Rail, Brisbane and Melbourne	5
High-Speed Rail Link Melbourne-Canberra-Sydney-Brisbane. Tilt train standard. Passengers+freight	10
High-Speed Rail Link Wollongong-Sydney-Newcastle	10
New Direct Inland Rail Link Melbourne-Brisbane + other	5
Ports	5
Gas	10
Water and Sewerage	10
Salinity and Rivers	40
Total:	**265**

Say, $250 billion

For sources see: www.borrowandbuild.com.au

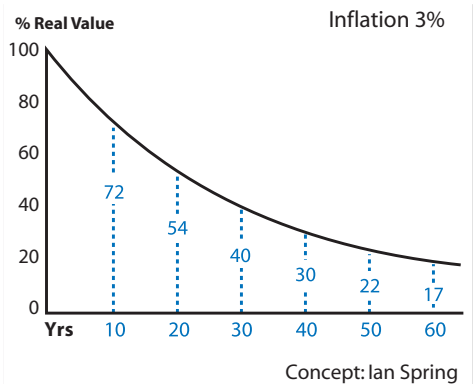
POPULATION AGEING – EFFECT ON FEDERAL BUDGET



Based on Treasury projections. Intergenerational Report 2002-03 Budget Paper No.5

*Addition Ian Spring

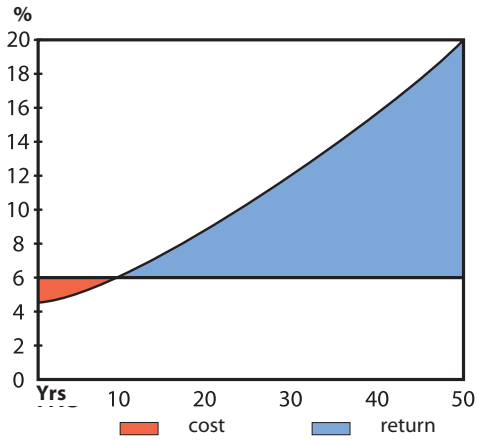
INFLATION SHRINKS REAL VALUE OF DEBT



to $8 billion nationally on major long-term infrastructure. The first step in implementing the plan would be for the development fund to take over responsibility for this money (approximately 1% of GDP). This will free up this amount, virtually straight away, for tax reductions and/or increases in expenditure on health education and other services.

Thereafter the program would build up, over five years or so, to a rate of borrowing of approximately 2% of GDP per annum and extra spending of 1%/a to 1.5%/a. A sensibly managed program of this relatively modest size should not have unduly harmful effects on inflation or interest rates.

INCREASED REVENUE SOON COVERS SERVICING COSTS



Based on long term borrowing at 6%, a 4.5% initial rate of return as extra tax, and inflation at 3%.

Concept: Ian Spring

Careful management of the buildup in expenditure over time, and across regions, would avoid excessive cost increases due to shortages of labour, skills, or equipment. To protect the skills base, the ongoing spending commitment should be continued even through buoyant economic times.

It is neither necessary nor desirable to repay long-term government debt. The debt will write itself off in real terms over time under the effects of inflation. The principle is that individuals repay debt, businesses and governments do not.

Contra-intuitive as it may seem, most of the infrastructure spending will be self-funding within the federal budget from extra taxes flowing from these investments' broadening of the tax base.

The recent Business Council of Australia (BCA) report suggests an $16 billion increase in GDP from a $90 billion increase in investment. This translates to increased tax revenues equivalent to a 4.5% return to the federal budget from infrastructure investment.

The graphs on this page show how the effect of inflation will be to turn this return into a growing "profit" to the budget. Thus infrastructure expenditure on vitally necessary assets is not a burden to the next-generation, it is a benefit.

Another possible objection is that local borrowing may increase foreign debt. This effect is often exaggerated, but it is a fact that the program will almost certainly cause a short- to mid-term lift in foreign debt. Continuing major infrastructure investment is, however, our only way to increase productivity and keep foreign debt down in the long-term. Any short-term problems that appear will have to be managed.

Skills shortages are often cited as an excuse for inaction. Given the long-term nature of the borrowing and building program, there will be plenty of scope for government initiatives in education and elsewhere to overcome this problem; employing Australians.

If borrowing is such a good idea why aren't we doing it already?

History, ideology, mistaken ideas, poor economic theories, and split responsibilities within the federal system have all played a part in shaping what has been widely described as an obsession against government borrowing.

A period of high interest rates until about five or so years ago also discouraged borrowing. When interest rates fell, the federal government should have adopted a new model. It should have stopped repaying debt, used proceeds from the sale of assets for infrastructure, and when these were exhausted, should have started to borrow.

We must abandon the stale old debates on infrastructure. It is not railways versus roadways, it is both, carefully planned to complement each other. It is not public versus private, it is both, with an optimum mix of private efficiency, and cheap public capital. ◻

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