

Mr James Hansen, submission to the Standing Committee on Infrastructure, Transport and Cities

## **Inquiry into options for financing faster rail.**

Within the current professional sphere of infrastructure planning and neo-liberal economic thought, this inquiry will undoubtedly be inundated with recommendations related to “value capture” and assumptions that tax revenue must fund government spending. It is critical this Committee recognises these assumptions are misguided, wrong, and detrimental to the prosperity of our country. Any investment in economic resources of this significance within a large and complex knowledge-intensive economy such as ours has the capacity to generate sufficient levels of economic efficiency to fund such a program without any new taxes or financing mechanism.

### **1. Sovereign currency issuing governments are not fiscally constrained**

Sovereign currency issuing governments, such as the Australian Government, are not fiscally constrained. By the sovereignty of the Australian parliament, laws for the appropriations of funds can instruct the Treasury to issue currency for the conscription of real economic resources for any public purpose deemed appropriate by the parliament. Taxes need only be collected to create demand for that currency and create fiscal space for that spending to not be inflationary.

A “budget deficit” is not only possible, but preferable, as deficit spending by accounting definition adds to the supply of financial reserves for the proper and efficient functioning of the monetary and financial system within a growing economy. There is no financial or legal reason for deficit spending to be financed with any debt instrument, such as a bond or private sector loan, which would provide an unearned interest payment to the private sector for “lending” reserve currency back to the Australian government, the issuer of that currency.

The need to “balance the budget” is a self-imposed political constraint on the proper functioning of the monetary system. Ideological constraints like balancing the receipt of taxes against the spending of the government only acts to constrain economic activity and prosperity for the Australian community. Governments must first spend before they tax. As households and firms have a preference to save and spend using the monetary system, with constrained government spending within a growing economy the demand for finance can only be met by private sector credit. As is currently the case in Australia, private sector credit has reached credit constraints, and the economy is unable to grow and investment in productive resources. Hence our protracted economic decline and inflated asset values that characterises our current economic circumstances.

To address the shortage of money and the over financialisation of our economy, deficit spending must be strongly supported and recommended by this Committee.

### **2. Appropriately managed, deficit spending is not inflationary**

The only constraint to deficit spending is the risk of inflation. Contrary to popular economic belief, the quantity of money itself is not inflationary, but it is the spending of money that is inflationary. Any and all spending can be inflationary, including public and private sector spending (see housing in mining towns or bananas after a tropical cyclone for example).

The highest risk of inflation from spending on fast rail is likely to be in markets for professional consultants, construction workers and construction materials, especially within smaller regional cities. For spending on fast rail infrastructure to not be inflationary, the investment program should consider ways to procure professional services with competitors from foreign markets, and invest in training and skills in regional communities.

Broader risks of inflation are likely to be concentrated in regional cities and nearby towns, as they are no longer by-passed or flown over. Regional towns and cities will be at the epicentre of railway construction, operations and maintenance, potentially generating substantial economic growth. During periods of construction or rapid population growth, there might be a need for temporary housing or other resources to reduce inflationary pressure within these economies.

Larger cities and the broader Australian economy is more likely to experience deflationary price pressures, as faster rail provides competition to the road and aviation transport sectors, and broadly reduces transportation costs throughout the economy.

A well-managed investment program, financed with deficit spending is unlikely to cause any price inflation, while the employment of fast rail technology is more likely to have a broader deflationary effect on prices and improve the cost-of-living and the cost-of-doing-business in Australia.

### **3. Public goods increase the economic pie**

Fast rail technology provides an opportunity for the Australian people to invest in an economic resources that will provide a range of economic, social and environmental benefits. A traditional transport business cases will likely demonstrate the benefits of travel time savings and improved safety and environmental benefits, with the benefits of a well-designed policy option being in excess of the infrastructure costs.

From a funding perspective, it is essential to understand the economic efficiency that results from these avoided costs. As households and firms spend less on transportation, while attaining the same or better outcomes, their income that would otherwise be spent on transport can now be spent on other economic activity, thus growing the size of the economic pie. That economic growth can then in turn pay for the investment in the fast rail infrastructure. That is, the economy is not fiscally constrained, we can supply more money, and is not demand constrained, households and firms can always find something they would like to consume or invest. The economy is resource constrained, and building efficient infrastructure like fast rail will add to the economic resources available to the economy and builds economic prosperity.

### **4. Opportunity cost of not investing in public goods**

Economic evaluation of infrastructure spending is typically framed by neo-liberal ideology as competing for resources with the private sector, which justifies the use of high discount rates and cost-of-capital rates akin to the private sector. This thinking is completely misguided. Public goods do not compete with the private sector, they create it. Public goods create the foundation of economic resources needed by the private sector to exploit for their own productive means. In the short run, the public sector will conscript resources from other private sector employment (or even conscript resources currently unemployment by the private sector), and in the long run that investment will create new economic resources for a more productive and efficient private sector. The private sector doesn't lose from public spending, it participates in it, and in the long run benefits from the new public resource created by it. Investment in new economic resources, like fast rail, is not a zero sum game.

The opportunity cost is therefore not the employment of the resources, but the opportunity cost of not having developing the new economic resource (in this case fast rail technology). To understand if the benefits from the new resource are greater than the costs to develop it, we tally all the costs and benefits and then discount them to a present value for comparison. The discounting of these future value should be based upon a consideration of intergenerational equity, typically at a rate of about 1.5% (as is common practice in most other countries). That is, the community of today will value the costs and benefits more than the community of tomorrow. This intergenerational discount rate is purposefully low, as the community of today should not take near sighted decisions that would harm or hinder the community of tomorrow.

The neo-liberal ideology of competing for scarce resources between the public and private sector has institutionalised the use of discount rates that are broadly designed to reflect capital investment hurdle rates. Often using rates between 5% and 10%, these rates reflect a misguided understanding of the essential value of public goods to the private sector, and the intergenerational equity of public goods over an indefinite time horizon. The private sector can't provide these public goods, so there is no private sector equivalent to the employment of these resources. Governments should always invest in the development of public resources where they have a cost benefit ratio greater than 1, where they provide an equitable distribution of benefits across society, and produce a net present value of sufficient size relative to the scale of the investment.

## **5. Landuse efficiency benefits**

A traditional approach to transport infrastructure projects measures the direct benefits of the transport benefits. However it is broadly recognised that transport, especially rail investment, has a far greater economic impact than these direct benefits. Other benefits such as second round effects and 'agglomeration' benefits are often included. This approach seeks to capture the 'wider economic benefits' to knowledge-intensive economic activity of being clustered or better connected, and second or third order benefits from the relocation of firms and households to exploit the new connectivity. The degree to which transport benefits are a more efficient substitute for location benefits (clustering) is not well understood and difficult to measure. The use of wider economic benefits in Cost Benefit Analysis should be limited and used with caution.

However, missing from a typical transport analysis are the benefits of more efficient land-use. That is, high capacity transport networks can facilitate higher-density and more efficient land uses, avoiding the costs of sprawling low density infrastructure. Clustering our towns and cities at slightly higher densities, and using shared transport like fast rail and local transit, communities and governments can avoid the costs of sprawling roads, streets, pipes, wires, cables and land costs for infrastructure like schools and parks. When we build at moderate densities we simply avoid the cost of building and maintaining millions of kilometres and thousands of hectares of infrastructure assets at all levels of government.

For a fast rail program, there is an opportunity to combine faster rail with city-serving light rail, trackless trams or bus-rapid-transit. When these networks are combined, communities can realise the benefits of both cheaper transport and cheaper landuse infrastructure. The combination of these two cost savings has the potential to generate such incredibly large economic efficiencies, that the avoided costs of transportation and sprawl can fund the rail investment at no cost to society. That is, the avoided costs of owning and operating cars, building and maintaining streets, roads, pipes and parks, is far greater than the cost of building the rail assets that enable this pattern of urban settlement.

There is no need to impose new taxes or grow the size of government to fund fast rail. In fact, the financial gains from the avoided cost of sprawling infrastructure can be so vast that governments could reduce tax receipts and/or increase spending on other urban services, such as improving our urban tree canopy with street trees, replace concrete footpaths with stone paving, and build grand civic buildings, from local libraries to international airports. There is simply no need to finance fast rail with new taxes.

## **6. Value capture and tax reform**

This inquiry is likely to hear from a number of industry experts espousing the need for value capture mechanisms and new taxes. Even if you dismiss the sovereignty of the Australian parliament to issue currency to conscript real resources for a public purpose, and believe the monetary system should be constrained and financialised with private sector debt, the government already has a sufficient range of land and property taxes to capture a sufficient share of the value of these investments. We already have GST on new housing and property development, we have capital gains taxes and stamp duty on

property transfers, we have state and local charges and levies on development activity, we have local government rates on unimproved land values, and we have fare-box revenue from the provision of rail services. There is simply no need to collect any new taxes, change the current tax arrangements, or grow the size of government.

The desire by industry experts to change existing tax arrangements are likely motivated by a desire to bypass the sovereignty of the parliament and the democratic budgetary process and delegate taxing and spending powers to technocrats and the bureaucracy. This challenge to the sovereignty of parliament and the elected government should not be supported by this Committee. There should be no new taxes, value capture mechanisms or levies imposed on firms or households, and no tax receipts should be hypothecated to infrastructure spending. Any tax reform should be part of a broader regulatory and economic efficiency reform process, not infrastructure project financing.

### **Concluding remarks**

As I have outlined, there is simply no shortage of financial resources for funding fast rail infrastructure. Any budgetary restrictions are simply self-imposed by a government's subjugation to uninformed credit rating agencies and private sector investment banking ideology. The benefits of employing this technology will far outweigh the costs, and we have all the resources necessary to realise a better future. A sovereign money issuing government has no need to levy any new taxes, charges, or fees to finance investments that generate a positive economic return. There is simply no benefit to leaving fast rail technology unemployed and idle in our economy. This Committee should strongly endorse the use of deficit spending to invest in a comprehensive program of local transit, fast rail, and high-speed-rail across the nation.

The decisions of past governments to not invest in rail technology has hidden an opportunity cost that to date has constrained the prosperity of our country, which has disproportionately affected our regional communities. Burdened by car dependency and sprawling infrastructure, our suburban and regional communities would be a far wealthier and prosperous today had we made decisions to incrementally invest in these technologies and employ these resources in the past. For this Committee, any delay or inaction on the employment of modern rail technology will only further our economic disadvantage while perpetuating the isolation of our regional communities from the global prosperity of our age.

The time to act is now.

### **About the author:**

James is a city planning and infrastructure expert. He has several years of professional experience working with clients in city planning and transport planning, working across a range of public and private sector firms. The statements made in this submission do not reflect the opinions or sentiments of his employer or clients.