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US: Obstacles to progress

By Anna Fifield

Construction workers reinforce the hillside during the Interstate 405 widening project near the Mulholland Bridge. The US needs to spend $20bn more a year just to keep current transport infrastructure out of decline, civil engineers say

When Rusiko Jibladze stepped off her flight to Dulles airport, gateway to the capital city of the richest country in the world, she was taken aback. The 48-year-old from formerly Soviet Georgia, this year making her first visit to the US, could scarcely believe what she saw.

"It was the airport that shocked me first – everything seemed to be so old and falling apart – and then the roads. I expected everything to be shiny and new, and instead it was grey and worn out," Mrs Jibladze recalls. "All my life I heard how amazing America is, so I thought I'd find myself in a fairy tale. Instead it was so grim."

Barack Obama understands Mrs Jibladze's reaction all too well. Aware that crumbling infrastructure is holding back economic growth, the president has been talking about the urgent need to invest since before he took office. "America, it is time to focus on nation-building here at home," he said in June, contrasting that task with efforts in Afghanistan.

Certainly, Mr Obama has tried to think big, portraying a vision of an America with the fast trains of France, the smooth highways of Germany and the internet connectivity of South Korea. Just as Abraham Lincoln had transcontinental railroads, Franklin Delano Roosevelt had the New Deal public works programme and Dwight Eisenhower oversaw the creation of the interstate highway system, Mr Obama saw scope for a post-recession infrastructure boom.

But increasingly partisan politics and a stubbornly weak economy have conspired to force him to act small. The impact of the $787bn Recovery Act, the package of tax cuts and "shovel-ready" infrastructure projects Mr Obama introduced when he took office, is petering out; and the wrangle over raising the federal borrowing limit has made any talk of spending almost impossible. "It's a different time in Washington right now," Robert Puentes, an infrastructure expert at the Washington-based Brookings Institution, says of the way deficit cuts dominate discussion. "Today everything is on the back burner."

The president, who last year set an ambitious goal of doubling exports within five years, has signalled he will refocus once the debt ceiling debacle is over. "If we have a plan to get that done, then the next step is looking at bolder plans like infrastructure," he said in a television interview last month. "Putting people to work, rebuilding. Not just our roads and bridges, but also broadband lines, high-speed rail – putting all those construction workers that used to be in housing to work."

A senior administration official says the president will settle for incremental progress. "If we can't do all of these things at one time, let's do the things that we can get done, and over time they add up," he says.

Such progress cannot come soon enough for business leaders such as Scott Davis, chief executive of **UPS**, the package delivery company for which a delay of five minutes a day per truck costs $100m a year. "The US is not going to be competitive with the rest of the world if we don't have the proper infrastructure. It's frustrating," Mr Davis says, describing how moving goods by truck is eight times more efficient than by air, and rail is four times more efficient than trucking. Ships are the most efficient of all but ports are congested, he adds.

It is imperative to tackle the problem, he says. "The way we're going to have jobs is by growing and exporting. We need to be able to compete with the developing world but we can't unless we have the infrastructure."

Indeed, the US spends only 2.4 per cent of gross domestic product on infrastructure – less than half the average of 5 per cent that prevails in European countries – and half the level of 1960, according to the Treasury. In its latest infrastructure report card, the American Society of Civil Engineers awarded America a D. One in every five bridges is classified as "structurally deficient", requiring significant maintenance, repair or replacement. This was the classification held by the I-35W bridge in Minneapolis before it collapsed in 2007, killing 13 and injuring 145.

The number of miles travelled by cars and trucks has doubled in the past 25 years, but highway lane miles have increased by only 4.4 per cent. Demand for electricity has increased by about one-quarter but the construction of new transmission facilities has decreased by 30 per cent. The US now ranks 23rd for overall infrastructure quality, according to a World Economic Forum study.

Deteriorating surface transport infrastructure will cost the economy more than 870,000 jobs by 2020 and suppress GDP by $3,100bn, says the ASCE. If investments in surface transport are not made within the next decade, businesses will pay an added $430bn in costs and exports will fall by $28bn.

To bring surface transport infrastructure up from deficient to sufficient would require an additional $94bn investment in highways and transit systems, the report concluded. "If we continue to fail to make these investments, it will affect families, businesses and our place in the world economy," says Kathy Caldwell, president of ASCE.

But such large numbers are a hard sell in Washington. Though some deficit-cutting proposals included plans to increase infrastructure spending, none came close to the level needed even to maintain roads, bridges and airports in their current condition.

There is little doubt infrastructure projects are a winner when it comes to creating jobs, even if only in the short term. "For every dollar spent, we get more out of infrastructure investment than anything else," says Donna Cooper of the liberal Center for American Progress think-tank, a former deputy mayor of Philadelphia. "If you give $1bn in tax breaks, you're not sure if it creates any jobs. But spend $1bn on bridges and you know it creates 18,000 jobs."

However, efforts to promote infrastructure spending are bogged down in Washington over concerns about who receives credit for creating jobs, Ms Cooper says. "This is not because of the financial or the budget crisis – this is politics. It's all caught up in the fight for the next presidential election," she says.

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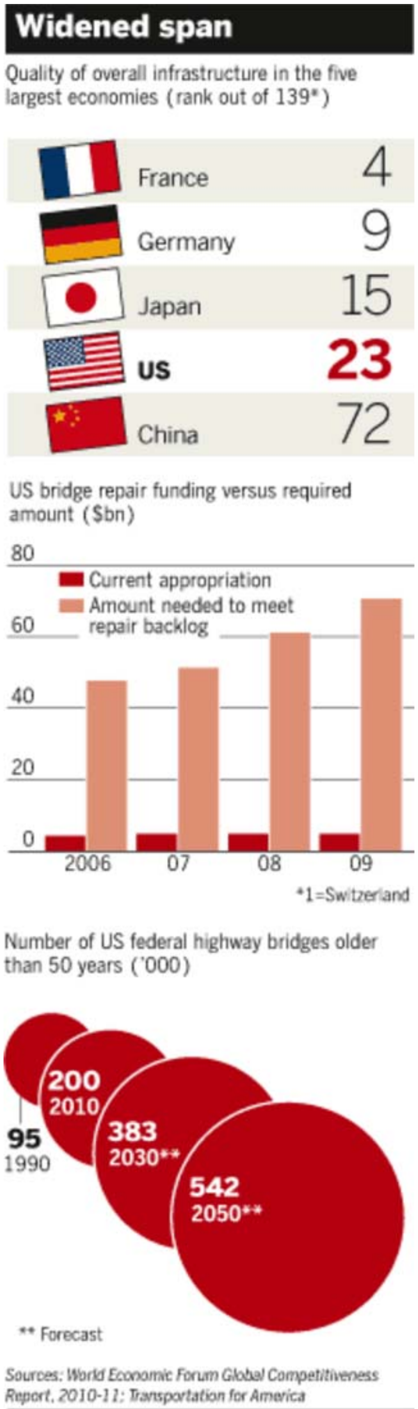
Numerous proposals have stagnated on Capitol Hill. The previous five-year authorisation for highway spending, worth $285bn, expired in 2009 and Congress has failed to pass a new one, instead using a hodge-podge of extensions. With the latest due to expire on September 30, John Mica, Republican chairman of the House of Representatives transport and infrastructure committee, last month unveiled a six-year bill that would cut spending by about 35 per cent.

The Senate's environment and public works committee responded with a two-year, $109bn bill that would keep spending at current levels plus inflation rather than cutting it. Though some Democrats are unhappy at maintaining the status quo rather than boosting spending, this proposal is more likely than Mr Mica's to win bipartisan support. House Republicans "would vote down a Mother's day resolution if it had extra spending", he said, referring to the Tea Party caucus that generally objects to any increased spending.

Infrastructure should be a promising area for bipartisan compromise, says Ryan McConaghy of the Third Way, a left-leaning think-tank. "For the left it's a job creator with immediate effects, like FDR's New Deal or Eisenhower's highway system. And the business community supports it because it makes investment decisions more attractive."



Both the labour unions and the Chamber of Commerce, seldom on the same side of an issue, support greater infrastructure spending. The chamber has criticised Mr Mica's $230bn bill for being too small.

The problem is not about the rationale but the revenue. American infrastructure investment has historically followed a user-pays model. Money for roads, for example, comes from the Highway Trust Fund, by way of a fuel tax of 18.4 cents a gallon and 24.4 cents per gallon on diesel. But revenue from petrol and diesel taxes has shrunk, particularly as high pump prices cause drivers to economise, while the cost of building and maintaining roads has risen. The fund will run dry in 2013 if left unaddressed.

The tax is low by international standards, and has not risen since 1993. But every elected official in Washington knows that messing with it is political suicide. "So the question is, how do you pay?" says Mr McConaghy of Third Way. "Banks get you only part of the way, bonds get you only part of the way, but ultimately you need a new revenue stream."

As an example of good governance, Ron Utt of the conservative Heritage Foundation holds up Bob McDonnell, the Republican governor of Virginia. Mr McDonnell campaigned for office in 2010 with a proposal to fund improvements to the state's roads without raising taxes. "He found $1bn in [public] money sitting around or being wasted, which he has used on a huge and ambitious building programme, resurfacing roads and building new bridges," Mr Utt says.

Chris Edwards, who runs downsizinggovernment.org for the libertarian Cato Institute, says the government should hand infrastructure to the private sector. "Other countries – in Europe, and Canada and Australia – have privatised their air traffic control, airports and roads," he says. "We don't have the money for infrastructure that we had in the 1950s."

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The incentive to do more with less is adding new impetus to decades-old plans to establish a national infrastructure bank, an idea supported by Mr Obama. In his budget in February, the president requested that Congress put $5bn a year for six years into establishing such a bank.

Several blueprints are in circulation, including one from Democrat John Kerry and Republican Kay Bailey Hutchison that would create a lender based on the federal Export-Import Bank, which Mr Kerry says could turn $10bn into as much as $640bn in 10 years. Others want to model it on the European Investment Bank, which holds about $300bn in capital from European Union member states. "The whole point is to leverage private capital so it won't just be on the government's dime," the administration official says.

Critics warn that, if the infrastructure bank issued its own bonds, it could run into trouble like Fannie Mae and Freddie Mac, the government-sponsored mortgage lenders whose debt Washington was forced to guarantee in 2008. But in an area where cost overruns are rampant, a greater involvement of private capital could help assuage concerns.

The bank also offers something sorely missing from US transport policy, which has not been updated since the 1960s: a national strategy. It would have an independent board of directors that would give projects the green light based on need, rather than pork-barrel politics. Lawmakers have used "earmarks" to win funding for developments in their district, regardless of whether they made regional or national sense. The most notorious was the $398m Alaska bridge connecting the island to a town of 50 people, which was scrapped in 2007 after a public outcry.

"I don't think the American public needs any convincing that we need infrastructure investment," says Ms Cooper. "I think they need convincing that the government can do it right, and that they won't waste their money on bridges to nowhere."

Local funding: Slower muni sales point to a mood of austerity and a fear of defaults

Municipal bond issuance, which finances a big chunk of the roads, bridges, tunnels, sewer systems and schools built across the US, has plunged to its lowest in more than a decade. The drop follows a retreat by investors, who fear rising local defaults following the recession, as well as austerity among politicians shying away from big projects and debt sales, **writes Nicole Bullock**.

"In the current political environment, some people, not only elected officials, are claiming that there is no distinction between 'spending' and 'investing'," says Emil Frankel of the Bipartisan Policy Center, a think-tank.

States and local governments typically do not build reserves for these investments. For its part, the federal government provides tax breaks for local individual investors to buy "munis", allowing states and city governments to pay relatively low interest rates on their borrowings.

So far this year, about $140bn in muni bonds have been issued, the slowest annual pace since 2000, according to Thomson Reuters. Analysts' estimates are for $250bn-$275bn for the full year, compared with an annual average of $360bn over the past decade.

Direct infrastructure investment by the private sector could fill some of the gap, but such deals are less common in the US than in Europe and Asia – partly because munis have provided cheap funding. Such projects have faced resistance from those who fear rising costs if assets are run for profit.

But interest in public-private partnerships is growing, especially for transport projects and the management of vehicles used for public services, says Christopher Mier at Loop Capital, a broker and investment bank.

The decline in muni issuance will not shutter existing projects, since they are typically planned and financed far in advance. Last year was a record for the muni market, with $430bn in bonds sold. A federal programme, called Build America bonds, which provided incentives for infrastructure bonds, fuelled issuance and some states accelerated their financing plans to take advantage of the federal aid, which expired at the end of 2010.

“The impact [of this year’s decline in muni issuance] will be felt next year,” says Matt Fabian, managing director of Municipal Market Advisors, a research group. “Diminished ability or interest in borrowing, which may persist, means fewer projects being done in the medium term and ultimately the need for other sources of funding to develop.”