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Some Realism, Please!

Times are tough, let's not make them tougher by dwelling in fairy land.

This week, a study into the financial sustainability of the top 100 NSW councils was released showing that 37 were unsustainable and would need to increase their revenues by 80% to 300% over the next ten years to meet their financial obligations and manage their infrastructure. A further 17 were considered to be 'on the verge' of being unsustainable.

This is not a problem that is confined to New South Wales. It is part of a continuing, and worsening, picture that has been revealed in previous studies in Victoria (SAM 3) and South Australia

According to the new report's author, Professor Percy Allan,
"Residents and ratepayers of such councils are facing mounting bills to rectify their finances and infrastructure **unless other tiers of government come to the rescue**"

But can we realistically expect to be rescued?

*Editor: Dr Penny Burns, AMQ International
PO Box 75 Salisbury South Australia 5108
Telephone 61 (0) 8 8359 0559
Email: amqi@amqi.com Website www.amqi.com*

Where is that gold at the End of the (Government) Rainbow ?



If we find ourselves in financial strife we can always rely on someone else to bail us out, right? But who?

The States?

But the states are finding that *their* sources of income are declining and are seeking ways to cut back on the expenses that they are responsible for.

More money for councils means less money for state infrastructure and for the maintenance and operations of schools, hospitals, main roads, police, etc.

Federal Government?

Sorry. The price to be paid for our current record levels of debt incurred for purposes of economic stimulation will be record levels of interest to service that debt. This increased cost will need to be met from declining revenues because in an economic recession, everybody's incomes decline, people and companies earn less and so pay less in taxes.

Moreover, in recessionary times, more of the Federal Government's income is diverted into social support for those not able to manage by themselves.

And more money for councils means less money for federal infrastructure, defence, and less to support the unemployed, service the debt, and manage the country.

Private Sector?

The Private Sector has done much to provide new infrastructure and, in some cases, to manage and maintain infrastructure. But they are also finding it difficult to get long term finance in the current climate.

Borrow Overseas?

Us and everyone else! Demand for credit is exceeding international supply.

It's time to face facts, there is no pot of gold to sustain local government infrastructure.



So Can Ratepayers Fund?

Rate revenues in unsustainable councils need to rise by from 80% to 300% over the next ten years to meet council's financial requirements according to the Allan report. Many will not be able to afford such increases for the number of aged pensioners is increasing and the economic recession will mean loss of jobs, or reduction in incomes.

Because of this, it could be that the burden of sustaining our future infrastructure will fall on a smaller and smaller subset of the population and, for them, it will represent an even higher percentage.

If Ratepayers are to pay more money for council infrastructure, it means less money for mortgages and rent, household expenses, children and general living. They may be able to do it - but it means that the time has come to ask ourselves the question we have been steadfastly avoiding.

The Elephant in the Room

Is it worth giving up more scarce dollars to sustain all of our current infrastructure at the level we are currently paying for - or do we have more infrastructure, at a higher standard, than we can afford?

There I have said it!

It is all well and good arguing that infrastructure is a 'good thing' and that we can never have too much of a good thing - as long as someone else pays.

But if, when all the arguing, and pleading, and bullying, and shouting is done - it is WE who have to pay, do we really think that we are getting value for money?

Or could we manage things better?

Could we rethink the services we are currently receiving in the light of the cost of getting those services? Could we examine the savings to be made by

- changing the service?
- changing the asset?
- changing the costs required?

These are all STRATEGIC ASSET MANAGEMENT questions - and when we run out of the easy options of getting more money,

Strategic Asset Management is all that we are left with!

“It is folly for a man to pray to the gods for that which he has the power to obtain by himself.”

Epicurus (341-270BC)

The sooner that we recognise that a ‘solution’ to our current financial problems will not come from petitioning the gods (i.e. government) but rather from ourselves, the sooner we will arrive at a sustainable position.

Here is a story that illustrates this. It was first published in my very first newsletter, back in March 1994.

Residents of Litchfield Shire Council, in the Northern Territory like most other municipal areas, had a desire for sealed roads adjacent to their properties to lessen the dust problems, to enable all weather access and enhance property values, but with over 300 km of unsealed roads in the council area and little spare cash, they were concerned that they may have to wait a long time before the Council was able to seal their particular road.

This was 1990. The Northern Territory had been granted self government in 1978 and since that time, councils had been petitioning the Territory Government and the Federal Government for money for road sealing. Their pleas fell on deaf ears. With a population of less than 200,000 and an area the size of ..., vehicles per day traffic counts fell far short of needs in other parts of the country. Still, for 12 years, they had been petitioning one government after another to pay for their roads, completely ignoring an even more serious problem - namely, that in the Northern Territory it is either too hot, too wet, or too hot and wet to actually build roads much of the year. In fact there was something like a 4 month window in which road building could take place.

Then Peter Visentin was appointed Shire Manager. Peter had some radical ideas about running remote councils. For one, he opened the council offices on Saturday morning only. He figured this is when people would want to come as they would be working on other days. For another he made a road offer. He calculated how much it would cost to seal the road in front of a typical property (excluding the road forming costs that would be borne out of taxpayer rates) and told the residents that if they wanted their road sealed, they could pay that sum. The first person who turned up with his cheque was told he was now ‘Road Captain’ and as soon as he could convince the other residents in the street to be part of the road building, they would get their road. People self managed. Those who were prepared to put the effort in got their roads done first. By 1994-95, 109 blocks had nominated and provided money towards new roads.

Had they only had this idea sooner - they could have had their roads sooner and saved themselves 12+ years of fruitless petitioning!



Three important things to know about infrastructure:

Infrastructure does not make money

Infrastructure does not generate demand

Infrastructure does not provide service

Not directly. Infrastructure is a facilitator. It supports growth, it supports income development, it supports service provision - but the impetus to growth, income and service have to be there first.

Infrastructure does not make money

We often think of infrastructure under the headings of social, environmental and economic infrastructure - and we have come to think of the last of these, 'economic infrastructure' as making money, even if we know that the others don't, but instead contribute to our quality of life now and into the future.

But if we think this way we are wrong. Take the economic infrastructure we are most familiar with - roads, water and electricity. By itself the road does not make money. Trucks using the road may make money. Toll roads may be able to capture some of this by the pricing structure used. But building more toll roads itself is no guarantee of more income - hence the secret contracts and deals that toll road providers enter into with governments! More water and electricity infrastructure need someone to use it - some factory or consumer. *Without increased demand, more infrastructure is just concrete and steel.*

Infrastructure does not generate demand

There is much media and government hype that give the impression that if you build infrastructure, the private sector will come forth with matching investment to make use of it. Not so. Private entrepreneurs invest when they can see the opportunity to get a return on their investment. Without consumer or business demand they will not invest, no matter how much infrastructure is provided. Why should they? Confusing the issue have been a number of economic studies showing a correlation between government spending on infrastructure and private investment. But that is just what it is - a correlation, not a causal correlation. Sometimes (oftentimes) the two occur

together, not because infrastructure is causing the private investment to occur, but rather because both the infrastructure building and the private investment are spurred by the same incentive - usually population expansion, but sometimes by the existence of a bottleneck that has been holding back effective demand. Other economic studies have shown that *when there is no 'third factor' influencing demand for both infrastructure and private investment, there is no correlation. Infrastructure spending works best when there is pent up demand to meet.*

Infrastructure does not provide service

Infrastructure is often thought of in terms of the services it delivers, but it actually delivers none! That is, of itself, it delivers none. All infrastructure, from roads to water and waste water, to hospitals and schools, requires - at a minimum - that they be managed and maintained. Without this year-in, year-out attention there is simply no service. A school without teachers, or a hospital without medical staff, is just a building. Medical and educational services only come when the building is maintained, managed, staffed, cleaned, lighted, heated, cooled, and secured. While it may not be quite so obvious, water and wastewater pipes are just underground conduits until the flows are managed. And without regular maintenance, cleaning, water treatment, etc., they are not only lacking in service but actually present a hazard. Roads that are maintained and managed well (traffic control, lighting, maintenance, etc.) provide a useful service, but roads with potholes, slippery surfaces, undulating pavements, etc. are not only not useful but downright dangerous. *So unless we can afford to pay for these ongoing costs, we do ourselves a disservice by having more infrastructure.*

Yes, infrastructure is 'good' - but it is possible to have too much of a good thing!

The current situation is a wake up call.



Choose it or Lose it!



If you have more infrastructure than you can afford to properly maintain, you have **two options**

1. **You can spend a little on each, but not enough to do a proper job on anything.**

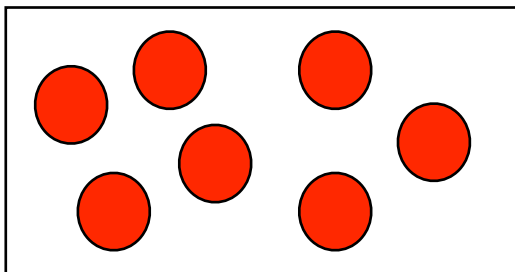
or

2. **You can prioritise, give what is needed by way of maintenance to your most important assets, and as a matter of deliberate choice, less to the others.**

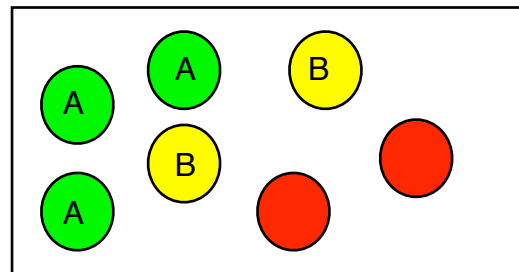
Option 1 in the past has been universally the most popular because it is easiest. It avoids the pain of having to make a strategic asset management decision - and achieves the pleasure of presenting the resulting arrears as a case for extra funding for 'backlog maintenance'

Option 2 is the strategic asset management option - less popular because it is hard and requires you to know far more about your assets, the benefits that they are providing for the community, and what other options exist.

However, continued application of Option 1 will mean that ALL of your assets will eventually move from a good condition to a poor one and you will lose them. Option 2 gives you the opportunity to save those that are most valuable - but at the cost of making decisions on the least valuable.



Option 1 All eventually under-maintained and lost



A : Selected as important and maintained properly; B: Selected as useful but not as important and service levels and cost reduced; Rest : Selected as disposable in the cause of the greater good!

At a minimum, don't make things worse!

If you are presently unsustainable with your current infrastructure portfolio, think very carefully before you add to it.

If grant money is available consider:

- A. Where is any matching funds that you need to provide coming from? You don't want to lose something that you have planned for as being of importance to your community for something that someone else has planned for that is of less importance.
- B. How much it will cost to maintain, operate and sustain that asset. You do your community no favours if you saddle them with debt.
- C. What are you going to do without! What other costs can you reduce so that you can afford the ongoing costs of the grant funded asset?

Avoid the necessary maintenance for the new item detracting from the funds available for your existing portfolio. If you haven't got enough for all (and if you are unsustainable, you don't) then you need to make some strategic choices (See previous page "Choose it, or Lose it".)

Be fair to your community - don't saddle them with debts they cannot pay!

**Remember there is no pot of gold at the end of the government rainbow,
if you incur the debt, you will have to pay for it!**

Coming next issue: The importance of Strategic Asset Management and the techniques available.

Note: Our promised Case Study has been deferred and will be published later.