How to plan infrastructure spending for the greatest good

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As Finance Minister Bill Morneau prepares his first federal budget, there is a consensus among economists that, given the current state of the economy, some short-term stimulus is needed, and that infrastructure spending is the most effective tool. There is also a consensus that the best infrastructure spending is for strategic capital projects that are not necessarily "shovel-ready" today, that require more planning before they can be built, but that will increase Canada's productive capacity for the long term.

Mr. Morneau's challenge is to square the circle. He must address a short-term economic imperative, but must also plan to provide the longer-term support needed for large, strategic capital projects. The new government has committed to investing $125-billion in infrastructure over the next 10 years. The minister's fundamental issue is to decide is what types of infrastructure, over how long, how to pay for it and the role of politics in the project decisions.

When Prime Minister Justin Trudeau and big-city mayors met in Ottawa on Feb. 5, the mayors had ideas about both kinds of project – relatively small, shovel-ready projects and larger ones that can transform Canadian cities and contribute to greater economic productivity over the medium and longer term.

Tens of billions of dollars are required for our cities because of many years of inadequate spending on municipal infrastructure. There is a large infrastructure deficit for deferred maintenance – repair and modernization of water and sewage lines, road repairs, modernization of civic buildings, construction of social housing and (given Canadian winters) the filling of potholes. But the larger-scale strategic infrastructure projects – public transit, green infrastructure, electricity grids, ports, critical highways, border infrastructure, science and technology infrastructure and so on – also require massive investment over the next decade.

Shovel-ready projects can begin as soon as financing is provided; longer-term strategic infrastructure requires a lengthier timeline for preparation, approvals, engineering and so on. To create jobs today, at a time of generally slow economic growth, the government's immediate priority, for at least the next fiscal year, should be to focus primarily on the short-term projects, while preparing properly for the longer-term ones. As there is simply no fiscal room for billions

of dollars toward new short-term infrastructure projects, the minister needs either to find new revenue sources, or borrow the money, or both.

Indeed, at current levels, tax revenue is not sufficient for the minister to fund the promised $125-billion over the next 10 years. In the current economic circumstances, there is a compelling argument for some borrowing for short-term infrastructure for the next fiscal year – but not for the next 10 fiscal years. To be fiscally responsible for the long term, Mr. Morneau should set out clearly in his budget the principle that short-term, shovel-ready projects that do not produce long-term economic benefit will not, as a rule, be financed by borrowing. He should consider a new revenue source for such projects.

Ottawa currently transfers 4 cents per litre of the federal gasoline and diesel tax to municipalities, to be used for infrastructure. With the sharp drop in the price of oil, gas prices at the pump have been substantially reduced. This makes it a good time to raise taxes on gasoline and diesel to address municipalities' needs. The minister should announce in his budget an increase of 5 cents a litre, to be transferred to municipalities every year for 10 years. This would more than double the federal infrastructure transfer to municipalities from $2-billion a year to approximately $4.5-billion. This substantial increase in federal funding could also allow for a change to the existing project-funding formula by increasing the percentage of federal funding and reducing the percentage required of cash-strapped municipalities. A gas-tax increase would also have the ancillary environmental benefit of raising the price of fossil-fuel consumption.

Mr. Morneau should establish that significant deficit financing will be reserved for the types of critical strategic infrastructure projects that will bring about long-term economic benefit. The Prime Minister has rightly been clear that these important capital projects should be chosen on their merits and not be subject to political pork-barrelling. There is a simple way to meet this objective.

Canadian universities have been modernized and rebuilt since the creation of the Canada Foundation for Innovation in the budget of 1996. The CFI's funding formula has brought together federal, provincial and private-sector money. Billions of dollars have been extremely well allocated by this arm's-length body over the past 20 years. Its success has been due in large part to the appointment of thoughtful, innovative and creative senior executives from outside government.

Building the modern infrastructure needed for the Canadian economy of tomorrow will require co-operation and substantial investments from federal, provincial and municipal governments, and from large private pension funds. Given Mr. Trudeau's government's commitment to large-scale infrastructure spending over the next decade, Mr. Morneau has a remarkable one-time opportunity to structure it in a manner that sets the country on the right track. He should use the precedent and example of the CFI to create another arm's-length body with a dynamic vision for the future and the mandate to decide, free of political interference, on the large strategic infrastructure projects that will transform our country, increase our productivity and raise our standards of living.