

Infrastructure: what is right?

Most of the current debates on infrastructure financing focus on two very different aspects: the enormous size of infrastructure investment demand, and the critical need to invest in what is considered the 'right type of infrastructure'. There are multiple ways of looking at demand for infrastructure and so depending on the underlying assumptions and models, it is quite natural that there will be multiple estimates. It is hard to get a consensus on a single number. But once the numbers are in trillions, why waste time arguing about methodological purities? Whatever the differences, these would be well within a reasonable margin of error in any case.

And so this entry is about a long list of attributes that are currently used to illustrate the 'right way to invest in infrastructure'. Local money for local infrastructure - which means no bailouts by Washington - is considered right. Emphasis on asset maintenance gets high marks. Partnerships with the private sector are essential elements of the right strategy. Mass-transit to reduce urban congestion costs and modernization of transport system are integral parts of right infrastructure investments. Information infrastructure, especially creating high-speed broadband is supposed to benefit innovation and so must be right. Green energy, clean technology, smart grid and other tools that modernize the energy sector are encouraged too. Reduced logistic cost, efficient and intelligent transport, including freight modernization, would benefit local industries and so are usually considered right. And for developing countries the right kind of infrastructure is, among others, inclusive, market expansive, regionally integrative, and sustainable.

So what is wrong with labeling everything 'right'? Nothing, except that all these statements allude more to a religious discourse driven by faith and belief rather than professional substance. And this gives very little guidance to policy makers about the underlying trade-offs that need to be evaluated before making the 'right' choice. For China, which is spending heavily on infrastructure, the fear is the possible overheating of the economy - which is energized by infrastructure investment, but is in reality paid for by the enormous value generated by labor arbitrage.

And the Indian infrastructure investment model may end up paying a much, much higher fiscal cost of going the PPP route which, once embarked on, may be very difficult to regulate in the future, at least in the medium term. Rent seeking and corruption will proliferate because it is difficult to design the 'right' types of incentives for infrastructure. Is this a story of any one country in particular? Not really. PPPs bring additional resources for infrastructure investments, but often, elaborate financing structures divert policy makers from the fundamental issue of how new services are going to be paid for today and in the longer term.

Unfortunately, there are very large gaps in the analytics surrounding the current choices countries make. There is a fundamental asymmetry of skills, information, and incentives between the two deal-negotiating parties, at least in developing countries: the private sector use all three to ensure that they maximize value for themselves in any investment proposal; government representatives, on the other hand, often lack all three but do have the exclusive right to grant market access. And as elaborated earlier (infra101), market access alone has high potential for super normal profits. This, coupled with the high transaction costs of closing a single deal, is nothing short of a perfect recipe for rent seeking.

So, if you go back to the basics, 'right' infrastructure means remembering that there are only two possible ways to fund infrastructure: either by the service users, or by citizens at large through tax and other indirect payments. The third way, (i.e., paying for infrastructure with vast tracks of land and thereby allowing the private sector to create value from idle resources) is an option unlikely to be available in many countries today given the extreme pressures on land resources. Investing right is thus not a mantra, but instead detailed and often dangerous work for policy makers, who must examine counterfactuals and choose projects that generate maximum value for infrastructure consumers. So it's not about faith or beliefs, you can't simply wish a project 'right'. It's all about hard facts and figures.