Infrastructure Funding Confusion Muddies Debate: Friedlander

DALLAS - The effort to determine how to pay for the restoration of America's crumbling roads and bridges is being hindered by the failure of policymakers to distinguish between the funding and the financing of infrastructure projects, according to veteran municipal market strategist George Friedlander.

"Access to financing is clearly not the problem, while access to funding is a severe and — if anything — accelerating problem that even a $1 trillion federal program over 10 years is unlikely to ameliorate," Friedlander wrote in a paper presented Monday at a closed-door infrastructure roundtable sponsored by the Municipal Securities Rulemaking Board.

The availability of investable capital for a project — the financing — is vast but what state and local governments need is help with paying for a project or reducing the cost of the debt issued for the project, wrote Friedlander, a managing partner at Court Street Group Research. He joined the group in late 2015 after some 40 years with Citigroup. He currently serves as chairman of the Municipal Bonds for America Coalition's technical advisory committee.

"Sources of capital, no matter how vast, simply do not provide funding," he wrote in the paper. "They provide financing."

Recent statements by Transportation Secretary Elaine Chao that the main cause of delays in infrastructure projects is overbearing regulations rather than a lack of private capital is "scary wrong," wrote Friedlander.

"It confuses the availability of investable funds — financing — with the availability of resources to pay for a project or to repay debt issued to finance a project — funding," he pointed out.

The first step toward renewal should be to reinforce and support those programs that have been effective in funding infrastructure, such as the Highway Trust Fund, he wrote.

"To be sure, more spending is needed, and in some cases, achieving this goal will require significant additional federal financial support," he wrote. "However, that support needs to be incremental over successful existing structures, not a replacement for them."

Any new strategy to boost spending in President Donald Trump's infrastructure program would not have the sort of project sorting and selection mechanism provided by the taxexempt bond market, Friedlander noted.

The $137 billion of federal tax credits in the Trump infrastructure plan are unlikely to stimulate $1 trillion of private investments in revenue-producing projects as proposed, he wrote.

The revenues needed to repay private investors in a P3 project are the same ones that would be used to pay bond debt service and operating expenses, he noted.

“There are vast numbers of projects that are simply not supportable by user fees,” Friedlander wrote.

“The efficiency of the tax-exemption as a way of disbursing financial support for projects remains vastly greater than certain critics would suggest.”

Alternative financing mechanisms such as public-private partnerships and bank loans have their place but smaller issuers are at a distinct disadvantage to larger municipalities in accessing these, he wrote in the paper.

“While there may be ways to strengthen and sharpen the operations of the municipal market through the incorporation of alternative sources of financing, the simple fact is there is no viable substitute to municipal bonds,” he wrote.

A new program similar to the Obama administration’s stimulus-era Build America Bonds would be a useful taxable complement to tax-exempt bonds in funding infrastructure, according to Friedlander.

“More than $150 billion of BABs were issued and the taxable nature of the bonds opened-up the market to nontraditional investors, such as pension funds and insurance companies as well as foreign investors,” he noted.

If the Trump administration and Congress are serious about increased spending on infrastructure, they must figure out how to make state and local governments more enthusiastic about participating in the funding, Friedlander wrote.

New-money issuance by states and local governments, when adjusted for inflation, has virtually collapsed, he noted.

“On a net basis, state and local governments haven’t borrowed a nickel since the beginning of 2010, while borrowing in other non-financial sectors of the U.S. economy has continued to pile up,” Friedlander wrote.

The need to cover rapidly growing pension liabilities will quickly diminish the capacity of many states and cities to fund infrastructure, according to Friedlander.

Trump said in an address on Tuesday in Kenosha, Wis., that an infrastructure bill would be ready soon that could be linked to tax reform efforts but provided no details.

“Infrastructure. Big infrastructure bill,” Trump said. “Probably use it with something else that’s a little bit harder to get approved in order to get that approved. But infrastructure is coming, and it’s coming fast.”

Congressional Democrats will be reluctant to go along with any tax reform measures until Trump releases his income tax returns, warned Senate Minority Leader Charles Schumer, D-N.Y.

“Everyone is going to jump to conclusions that he is benefiting and maybe that’s the reason he is doing it,” Schumer said.

The Transportation Department said Tuesday it would create a new infrastructure advisory post to oversee implementation of Trump’s priorities. Secretary Chao is expected to name James Ray, a principal at KPMG, as senior adviser on infrastructure.

The Bond Buyer

By Jim Watts

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