

Ridgway Capital Projects Commentary

19 November 2010

Earthquakes, Funding Challenges and Suggestions

Last week I was asked to speak at a function organised by Christchurch public relations firm Carter Price Rennie.

While Christchurch will remain fairly fragile for some time yet, there is a general sense that there is a silver lining to the earthquake. I spoke about how that silver lining might be financed and concluded that there will be much pressure on councils in the region to come up with answers in this regard.

A council is effectively a large infrastructure management business after all. In Christchurch, for example, the council has around \$7 billion worth of assets, half of which are classified as infrastructure, mostly in the form of transport, water and waste assets. What is interesting is that 95% of those assets are financed with ratepayer equity, which I argued in my talk can be seen as free money by councils but to ratepayers have a significant opportunity cost.

A good proxy for measuring ratepayer opportunity cost is to consider the pre-tax cost of a mortgage. If a householder is paying 6.5% per annum, then the tax adjusted cost of mortgage is around 10% per annum. Councils, therefore, are in economic terms financing themselves with expensive money that they see as being of no cost in financial terms. This needs to be addressed, by having a hard look at capital structure and employing more intergenerational debt.

Debt, however, will only go so far to close the significant funding challenges Christchurch faces. Changing the way we manage infrastructure is also important and, for arguments sake, I singled out our water and wastewater system for discussion. The true costs of the services need to be understood better through transparency and corporatising the business. We must then pay for our water based on volume consumed. Next, a series of performance benchmarks need to be applied so that the service can be delivered more cost-effectively. Finally, different contracting models like a management contract possibly bundled with other municipalities, need to be considered. All this can be achieved without any transfer of ownership and we will use our resource more wisely.

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