THE FUTURE OF LOCAL GOVERNMENT COUNCILLORS AND THE INTERNET CREATING A COMMUNITY HUB
The case for issuing bonds to fund council infrastructure renewal

The creation of a local government bonds market has been touted as a potential reform that could help the nation’s councils address their massive infrastructure renewal backlog. Professor BRIAN DOLLERY details why such a market should be established.

That local government across Australia faces a massive infrastructure renewal problem is well known. The depth of this problem has been estimated by PriceWaterhouseCoopers to be as high as $15.3 billion nationally, yet state and federal governments have refused to seriously entertain solutions based on councils borrowing or the establishment of a national infrastructure renewal fund. The problem finds its way into the “too hard basket” with the greatest of ease.

An alternative method (occasionally mooted but never fully explored) of addressing the problem in a cost-effective and sustainable manner lies in the issuance of bonds based on the assets of local government utilities.

We ought not be concerned that any move in this direction is “privatisation by stealth” or exposing valuable municipal assets to the fickle winds of global financial markets.

Issuing municipal asset-backed securities would involve a number of participants. In the United States, for example, local governments sell a debt instrument to an underwriter (a role typically fulfilled by an investment bank) which then re-sells the security to investors.

In order to keep the securities discrete from other bank business, the assets are issued by a Special Purpose Vehicle (SPV). Investors receive both coupon payments on the bonds and the price of the bond on maturation, with the SPV also collecting revenue from utilities to service these payments.

The SPV can also package a range of asset-backed securities to appeal to investors.

While not a totally risk-free asset, an asset-backed by revenue streams from LWUs would compare very favourably with NSW Treasury Corporation and Commonwealth Government securities.

The Centre for Local Government recently estimated that a yield of around 7% could be offered. Including the cost of paying the bond on maturity, the cost of debt for the LWUs over 10 years can be calculated to be 7.27%.

An issue of 955,000 bonds with a par value of $1000 per bond neatly covers the LWUs’ infrastructure backlog. Crucially, LWUs had enough operating surplus to service the coupons.

According to DEUS in 2006, the aggregate turnover of LWUs for 2005/06 was $850 million, excluding grants received for capital works.

Calculating operating, maintenance and administration costs (OMA) at $418.7 million for the same time period, this left $431.3 million - ample monies to park in the SPV.

But would anybody buy a now much-maligned asset-backed security? Isn’t talk of government bonds harking back to last century?

On the contrary. Not only can municipal securities be made attractive through a range of measures (of which tax minimising legislation is just one) a number of fund managers are already “on this page”.

In April 2007, Macquarie Bank issued the Macquarie Global Water Index, and the Australian fund manager MFS Group launched the ‘MFS Water Fund’. According to its website, the MFS Fund is intended to provide investors with exposure to “a broad and diverse range of water-related businesses including utilities, infrastructure and technology companies and the owners of water assets and water rights”.

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Councillors should lead the way on carbon reduction

Dear Editor

The recent and ongoing debate around the carbon pollution reduction scheme has led to some interesting observations and reflections on the implications for the local government sector.

Typically, the largest implication for most local governments will be increased energy prices – a significant issue as they use energy to deliver their many services to the community.

Small councils or those with extremely tight budgets will need to take this into account now.

I think it is fair to say that the local government sector has been working on energy efficiency for many years and is in reasonable shape to take up this challenge: after all, they have saved over 13 million tonnes of CO2e in the past decade through the Cities for Climate Protection campaign.

The community.

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Besides water, many other goods and services provided by councils enjoy similar income inelasticity (we all use them), and are decidedly unexciting when compared to the SPVs at the centre of the credit market crisis.

In a cautious investment environment, where companies look to reduce their exposure to risk through portfolio diversification, municipal infrastructure bonds could look particularly attractive.

By themselves, asset-backed securities do not offer a quick fix to the infrastructure backlog problem.

They are nevertheless a financial instrument that combines the best of a market-based approach to publicly owned assets.

And it’s an old-fashioned idea – that’s precisely why we should like it.

Brian Dollery is Professor of Economics and Director of the Centre for Local Government at the University of New England.

The above article is an extract from Financing the Australian Local Government Infrastructure Backlog through a Bond Issue on the Capital Market, one of many papers available on the Centre for Local Government’s website www.lge.edu.au/clg.


We are unclear at this stage about the end detail of the role of waste management, off-sets and requirements to complete inventories.

Again, in all of these areas, councils have made major steps over the past decade.

So I am essentially optimistic.

But I think that we also need to remember that even after we have priced carbon and set up a mechanism to reduce it through the reduction scheme, we will still need to train our communities, develop technical expertise, maintain political commitment and build cross-sectoral partnerships to achieve the sort of targets that our government is discussing.

It is a fallacy to think that all of this will magically happen once the scheme is up and running.

Indeed, we may face some of the push-back that is happening in New Zealand as the reality of such an approach hits home: and it won’t just be in the pages of The Australian!

I therefore urge us all to ensure that real community building – the essence of what is called “complementary programs” in the Green Paper – continues and indeed grows.

In our democracy, the role of practical work on the ground to explain and develop climate solutions is critical.

Along with the price signals of the new scheme, each of us has a role in doing what we can where we are.

Wayne Wescott
CEO, ICLEI-Oceania

Inquiry must address needs of coastal communities

Dear Editor,

The local government sector welcomed the Federal Government’s announcement in May this year of a Parliamentary Inquiry into a New Regional Development Funding Program.

The announcement indicated the inquiry is “to provide advice on future funding of regional programs in order to invest in genuine and accountable community infrastructure projects”.

The inquiry therefore appeared to be of particular relevance to councils in the nation’s high-growth coastal areas.

As local councils are aware, non-metro coastal areas have experienced considerable growth over the past decade.

From 1997 to 2007 the population in these areas increased by 1.27 million people.

These coastal communities now represent more than 80% of Australia’s regional population.

Yet while the population continues to migrate to the coast, resources are not flowing with them.

As a result, a growing number of people in these areas are isolated from key services with reduced access to health and aged care, public transport, education, family support and youth services.

The Rudd Government’s inquiry into a new regional development funding program offered a ray of hope to these communities.

There was a feeling that although their needs had been largely ignored in the past, they were now going to be more adequately addressed through a “genuine and accountable” regional and local community infrastructure program.

To some extent those hopes have diminished following the recent series of roundtables and public forums held by the Infrastructure and Transport Committee as part of its inquiry.

From our observations the focus of these hearings has been on the application and assessment processes to be followed under the new program rather than on the needs and priorities of regional communities in genuine need of support and assistance.

We can only hope that in formulating its recommendations to the Minister that the House Standing Committee, in its preoccupation with achieving the most effective process for administering grants, does not lose sight of the purpose of the program, which is to help meet the real and pressing needs of working families in regional Australia.

Barry Sammels
Chair, National Sea Change Taskforce and Mayor of the City of Rockingham