INFRASTRUCTURE ISSUES THREATEN CANADIAN PROSPERITY

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A shift of financial assets, economic power and corporate investment is presenting municipal governments with a unique opportunity to play a critical role in the prosperity agenda for their cities by developing smart strategies and timely investments to attract the shifting dollars. If they seize the opportunity, cities could build creative clusters that will attract and appeal to the next generation of entrepreneurs, employees and companies. In doing so, these same cities will achieve an enormously important goal: They will develop and sustain the community's vibrancy and productivity, and broaden its tax base.

This article explores the state of infrastructure and the attention given to it in Canadian communities, and discusses the challenges and opportunities for municipalities to build strong, creative cities that can compete in the global economy.

The state of cities

Many factors influence where companies and individuals choose to work and do business. Location, a stable political environment, access to markets, the availability of a skilled workforce, proximity to resources and suppliers, taxation levels, serviced land, transportation corridors, reliable water and electricity and the quality of life are all important.

But there is another rapidly emerging consideration: the state of local infrastructure. Modern, efficient and reliable infrastructure is the foundation of strong local economies. Both hard (roads, sewers, water systems, etc) and tech (hi-speed wiring, broadband, etc) infrastructure are critical to business success. And increasingly, in older North American and European cities, a deteriorating infrastructure and the lack of new, modern infrastructure is a very serious issue. Cities in Canada and the U.S. are falling behind new cities in Asia, India and the Middle East that are attracting the businesses and types of citizens cities need to be socially, economically and culturally vibrant.

In Canada and the U.S., cities are facing infrastructure deficits that are now in the trillions of dollars. Moreover, they don't have the financial resources to fix the problem. (Municipal infrastructure deficits are the difference between the cost to repair/replace the infrastructure of a municipality—roads, sewers, public transit, water systems, bridges, etc—and the financial capacity to pay for the rehabilitation or replacement).

In 2007, the Federation of Canadian Municipalities (FCM) asked McGill University to study the problem. The findings were bleak — the municipal infrastructure deficit was estimated to be $123 billion.

Many experts believe that figure today is too low. Former Prime Minister Paul Martin says bluntly, "The canary in the coal mine is the state of the infrastructure deficit for municipalities. These are huge deficits." Regina Mayor Pat Fiacco, who in September will again host the National Infrastructure Summit, believes the more up-to-date figure approaches $300B.

Those estimates don't include the nearly $300 billion for upgrading the electricity system across the country, or the costs to the federal and provincial governments for making various highway, dam, harbour and other infrastructure investments. It is a crushing reality for government and for business.

In the United States, The American Society of Civil Engineers estimates that the U.S. must spend $2.2 trillion dollars on infrastructure during the next 5 years; $1.2 trillion of this amount has not been budgeted.

The problems with some of Montreal's highways and bridges, and the deadly 2007 Minnesota overpass disaster, are clear proof of the poor state of North American infrastructure. Sinkholes from leaking water mains, ecological problems from sewage overflows, the safety of our food and water, and the annual battle over potholes on our streets are just some of the symbols of our losing battle.

Municipalities simply don't have the monetary resources to fund this infrastructure gap themselves. As Regina Mayor Pat Fiacco told me bluntly, "Regina's ten year capital plan will cost $2.1 billion; of that amount, $1.3 billion is presently unfunded. And I would suggest that is consistent across the country."

Calgary Mayor Naheed Nenshi confirms that. "In Calgary, we have a $6 billion capital infrastructure deficit. I cannot imagine a world in which you could pay for capital using only the property tax."

Canadian cities just have to look at the mess to the south. U.S. cities and states are in an awful financial situation. Arizona sold its legislative buildings; Illinois can't pay its bills; California issued IOUs to suppliers, and New Jersey slashed spending on education.

Several U.S. cities declared bankruptcy last year and several others are teetering or have cut services dramatically. Some investors are concerned about the safety of some normally secure Tax-Free Municipal Bonds that for generations have been a comfortable, secure 'widows and orphans' investment.

At the same time, cities in Asia, India and other countries are investing trillions in new airports, hi-speed rail systems, highways, ports, and technology and innovation districts to create dynamic new financial, business and trade centres. These are attracting international corporations, large investments in the local economy and bright young minds. Creative clusters and new economic opportunities are emerging.

If American and Canadian cities fail to provide the infrastructure, educational opportunities and quality of life needed for progressive industries and CRINK (CReative, INnovative, Knowledge-based) economy jobs, then our economic prosperity is threatened.

We need to invest in human capital if we are going to compete globally, but we also need to invest in physical infrastructure.

Where's the money going to come from?

The problem, of course, is funding these initiatives. The 2012 Canadian federal budget had little good news for infrastructure spending. After the Drummond Commission Report was issued in Ontario, there appears to be little appetite for investing significant provincial dollars in Ontario infrastructure.

Unlike in North America, infrastructure investments in other parts of the world have been enormous. Cities in China, South Korea, India, the Middle East and other regions are seeing an explosion of capital spending.

For example, New Songdo is a city built on reclaimed land off the coast of South Korea near Incheon. It didn't exist ten years ago. Today it is a thriving, hi-tech, green and fully wired city of 75,000 residents and 300,000 workers. It is becoming an international financial and business centre, and is just 200 minutes by air from one-third of the world's population. It features a Jack Nicklaus-designed championship golf course, a lovely central park, water features, a convention and performing arts centre and other civic amenities. The $35-40B project was funded primarily by the private sector.

Masdar City is the zero-carbon eco-city being built in Abu Dhabi. It is becoming a global hub for renewable energy and clean technologies. The design-of the city is leading edge, and it is attracting international investors, businesses and talent. Phase One, to be completed in 2015, will have 7,000 residents and 15,000 commuters, and more phases will be built in the future.

In China, investments and the speed of changes are truly breathtaking by Western standards. The Mag-Lev train in Shanghai travels 431 kms/hour. Elsewhere, high-speed trains bracket the country, gleaming new airports are beautiful and functional, commercial, residential and financial towers continue to spring up, and the manufacturing and design centres in southern China buzz with optimism.

Investments in these regions are generally driven by a strong central government commitment to innovation and economic development. Canada does not seem to have the same sense of political will or urgency for improving and renewing our infrastructure.

China is now in the midst of what experts say is the greatest human migration ever—an estimated 150 million people have moved from rural to urban communities in the past two decades, and another 300 million are expected to move in the next 30 years. Cities that don’t exist today will have to be developed.

The implications for everything from food production to urban design, from schools to health care, and from government investments to private sector business opportunities, are staggering. Not the least of which, of course, are where the immigrants will live and work – soon-to-be built cities.

Moving rural residents off the land is a profound trend in several Asian and South-east Asian countries. The impact on urban destinations will be huge. And the implications for business and industry are equally intense.

The McKinsey Global Institute is well respected for its analysis of economic and social trends. Its conclusions are quite clear—there is a population and economic impact shift towards eastern (i.e., Asian and SE Asian) cities:

“Today, major urban areas in developed regions are, without doubt, economic giants. Half of global GDP in 2007 came from 380 cities in developed-regions, with more than 20 percent of global GDP coming from 190 North American cities alone. The 220 largest cities in developing-regions contributed another 10 percent. But by 2025, one-third of these developed-market cities will no longer make the top 600; and one out of every 20 cities in emerging-markets is likely to see its rank drop out of the top 600. By 2025, 136 new cities are expected to enter the top 600, all of them from the developing world and overwhelmingly—100 new cities—from China.” {McKinsey Global Institute, 2011}

The McKinsey & Company quarterly report in 2011 went on to identify some significant changes it believes are coming for large cities around the world. It predicts that by 2025, there will be a dramatic shift in the economic clout of some of the world’s top cities:

2025 Newcomers	2025 Dropouts
Bangkok	Athens
Beijing	Barcelona
Chendu	Denver
Chongqing	Detroit
Delhi	Hamburg
Doha	Lille
Foshan	Melbourne

Guangzhou
Hangzhou
Mumbai
Nanjing
Shenyang
Shenzhen
Tanjin
Wuhan
Xi’an
Minneapolis-St. Paul
Munich
Nagoya
Oslo
Rhein-Main
Rio de Janeiro
Stuttgart
Taipei
Vienna

The implications are clear and staggering for investors and elected officials. A dramatic dislocation is occurring across the global economy. Few governments, and even fewer North American municipalities, are recognizing and responding to this global tectonic shift of people and resources.

Canadian cities at a cross-road

Canada has a national government that has no strong urban agenda, and provincial governments that tend to offer a traditional, paternalistic approach to the municipalities for which they are responsible, rather than engage in useful discussions to improve the situation. Canada remains woefully behind in things like a national transportation policy.

Montreal Mayor Gerald Tremblay is candid about the challenges facing our cities. “Canada is the only G8 country without a Transportation Plan [that addresses gridlock]. In Montreal the gridlock costs the local economy $1.4B, in Toronto $2.5B.”

Canada’s towns and cities are facing greater challenges than ever, and they seem to have few allies. Generally speaking, the national media has failed to understand or report on the plight of cities and their importance to Canada’s prosperity. There has been little debate during federal or provincial election campaigns on this major topic. However, it is also a reality that municipalities and their lobbying organizations have failed to intrigue or inspire citizens to address these larger questions facing municipalities about their future.

Several critical steps should be considered to improve Canada's infrastructure deficit, and our municipalities' ability to finance them:

1. A crucial new round of discussions involving municipalities, business and industry leaders has just begun, prior to the expiry in 2014 of the $2B Building Canada Plan. In the 2012 budget, the federal government committed to having a new, long-term infrastructure program in place in the next couple of years.
2. It is time to change the tax system in Canada. Canadian municipalities are funded primarily by property taxes. Yet out of the total tax dollar that Canadians pay, municipalities receive only 8 cents. That situation is not sustainable for building dynamic towns and cities.
3. The most obvious alternative is to allocate some of the consumption-based taxes (such as GST/HST) to municipalities and infrastructure renewal. This kind of broader funding base is common in many other countries around the world. Also common is greater core funding from the federal government for major infrastructure.
4. We need to eliminate the duplication and over-regulation of business. Tax dollars should go to the order of government that can most efficiently and effectively deliver a particular service or function.
5. Municipalities need to look more at private sector partners for infrastructure investments. PPPs have had a decidedly mixed response in many cities, but the new reality is that taxpayers simply cannot fund all of the community's renewal requirements.
6. Some municipalities are seeing their debt levels rise as they face increased costs, sometimes downgraded credit ratings, and a higher share of their operating budgets going to service debt. That in turn limits the amount they can invest in infrastructure renewal or other operating costs. The downward spiral is very worrying.

7. Cities need to get smarter. They need to better use technology to help them identify, predict and sustain their core operations, such as infrastructure management, crime patterns, anticipate traffic congestion and the likes. Many communities have done a poor job of managing their physical assets.
8. Many local politicians have not had the courage to invest in needed repairs and upgrades. This is especially so for the water and sewer systems, which are underground and never given a thought by homeowners—until the day comes when they can't flush. It takes courage as an elected official to raise the rates for utilities, particularly when the benefit won't be realized until years into the future.
9. The provincial and federal governments need to do a better job of managing and renewing their own infrastructure. From the Trans-Canada highway to rail, from dams to border crossings, there are badly needed investments and improvements that must be made.
10. We need to embrace innovation when designing and building infrastructure — from using membrane technology to expanding sewer capacity to the materials we use to pave our roads. These can cut costs and increase the life of the project.

Playing on the international stage

Recognizing the changing international investment climate takes courage from Canadian politicians. For too long there has been sparring and disagreement on broad national policies to move the country forward. In this new era of dramatic growth in other countries and a period of slow growth in many North American cities, it is past time to develop new strategies and policies.

Ottawa Mayor Jim Watson was clear when he spoke at an FCM Municipal Infrastructure Forum in 2012: "Repairing and maintaining infrastructure is vital to ensuring we have strong communities and a strong economy. Municipalities will continue to lead on the front-lines, but this is a long term commitment that requires a team effort by all orders of government.”

Mayor Watson is absolutely correct. Canadian municipalities are responsible for more than 50 percent of Canada’s infrastructure. That’s why the seeming inability of the three main orders of government to work together and make prudent, regular infrastructure investments is a serious issue.

As Mayor Tremblay noted in our interview, the provincial and federal governments need to understand that their situation is not better than municipalities. “We cannot continue to accelerate the development of our cities if our only source of revenue is property taxes.”

President Barack Obama addressed the American infrastructure deficit issue in his 2012 State of the Union address. He called for a fifty-fifty split of the savings resulting from the end of the Iraq war, with half the money going to debt repayment and the other half to infrastructure investments.

In Canada, we seem unable or unwilling to even have this discussion, let alone come to a national consensus on the importance and value of such investments. It is hurting our cities, our economy and increasingly will impact our international competitiveness and appeal.

If we won’t fund these investments ourselves, what are the options? The China Investment Corp. (the Chinese sovereign fund) has recently taken significant positions in two large infrastructure projects in the United Kingdom. The first was in railway reconstruction and the second in building a water treatment facility.

Many Canadians are uncomfortable with foreign ownership of local municipal assets. In fact, attempts by some communities to sell even a portion of their locally owned utilities (hydro, water…) have often ended in rancorous public opposition.

Yet as our economy becomes more global, as our brightest graduates become more international in their movement and thinking, as business crosses borders more easily and as trade barriers fall, it is still the local community in which people choose to live, work, raise their families and enjoy a vibrant lifestyle.

A city is not just about bricks and buildings, cops and kids, pipes and playgrounds. Great cities have an identity, sometimes even a global brand, that provides a powerful belief around which locals rally.

As well as Canada has done, there still remains one question: Can we do better. And what of the future?

The recently released 2011 census data showed clear winners and losers amongst Canadian cities and provinces, and how they are growing and prospering. There is a growing split between prosperous Canadian cities (generally in Western Canada) and cities facing uncertain economies and slow growth (generally in Ontario and eastern Canada). This has potentially dramatic implications for further population shifts, economic activity and the development of dynamic urban communities.

Can we compete with the best and the brightest around the world? As Surrey, BC Mayor Dianne Watts questions, "Will our next generation be the leaders of the world, or the labourers of the world?" In other words, will our economy be more than just the traditional supplier of natural resources? Can we innovate and excite in the global marketplace? When our graduates are deciding where to live, work, play and raise their families, will they be attracted to Canadian cities or to more vibrant international centres?

This is the market and the marketplace that has arrived. Building creative, dynamic cities is paramount to attracting the talent and the investments our economy needs to develop and prosper. Offering a high quality of life is more important than ever before. Borders don't mean much to the brightest minds and the global flow of investments.

Smart infrastructure investments are needed across Canada now, and a secure, sustainable plan to design and finance them is long overdue.

Calgary Mayor Nenshi described property taxes to me as "Regressive, feudal, medieval." He continues, "If you were designing the worst possible form of taxation, you may come up with something that looked like the property tax…It is a very, very difficult way for cities to manage themselves."

Ideas to change the system include allocating one percent of the HST (or GST) for municipalities, or one percent of the income taxes paid in the local community. It seems unlikely that with their own financial problems either the federal or provincial governments will vacate income tax revenue. In an important first step, however, Saskatchewan has just begun sharing one percent of its PST with its municipalities.

Former Prime Minister Paul Martin implemented the federal Gas Tax program that now results in municipalities receiving a share of $2B annually, much of which is now used for public transit. In our interview, he raised the critical question: "Do municipal politicians want more money from a senior order of government, or do they want the power of new taxation to raise more money and be held accountable?"

Mayors may have to swallow hard and take the responsibility for arguing for a one percent increase in the HST, for example, with that money flowing to our towns and cities for infrastructure renewal.

Canada's municipal leaders understand the issues and limitations facing their cities. They also understand that the senior orders of government and the private sector have to be players, just as they are in thriving economies in cities and countries around the world.

Strong, vibrant, prosperous and internationally respected cities are vital to our economic prosperity as a nation. Canadian cities are in an international battle for critical resources—talent, business investment, immigration, infrastructure improvements, downtowns that are fun and socially active, and communities offering a great quality of life.

In this global economy, nobody cares about cities that are crumbling and falling behind.