BIPARTISAN POLICY CENTER

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"Drivers of Job Creation"
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Thank you, Mr. Chairman, Senator Heller and Member of this Senate Banking, Housing, and Urban Affairs Subcommittee on Economic Policy for the opportunity to address on the important issue of the economic returns and job growth benefits of investment in infrastructure. This has been a matter that has dominated our work on transportation and infrastructure policy at the Bipartisan Policy Center (BPC), where I am currently a Visiting Scholar. I directed BPC's National Transportation Policy Project (NTPP) that issued a series of reports and white papers between 2009 and 2012, which, among other matters, addressed the inter-relationship between transportation and infrastructure investment and benefits to the broader economy.

Most relevant, in January 2011 NTPP issued a white paper, entitled "Strengthening Connections Between Transportation Investments and Economic Growth," co-authored by two members of NTPP, Douglas Holtz-Eakin, a distinguished economist and former Director of the Congressional Budget Office (CBO), and Martin Wachs, one of America's leading scholars of transportation and urban planning during a long career at the University of California, Berkeley, UCLA, and RAND Corporation. I will refer to this white paper during my testimony this morning.

Increasingly, over the past 25 years, as a state and federal transportation official, a consultant, teacher, and policy contributor on transportation and infrastructure issues, I have come to appreciate the role that these investments play in building economic growth and prosperity. Throughout American history, even before the birth of the Republic, investments in roads and canals (the so-called "internal improvements" that Henry Clay and Abraham Lincoln and their Whig colleagues espoused), railroads and ports, highways and aviation have characterized public policy and have influenced – perhaps, more than any other single thing – where cities are located and

whether they grow or decline. From Albert Gallatin, Thomas Jefferson's Treasury Secretary, to Dwight Eisenhower, America's leaders have spoken of the economic and political significance of wise infrastructure investments. In the words of Gallatin, "Good roads and canals will shorten distances, facilitate commercial and personal intercourse, and unite, by a still more intimate community of interests, the most remote quarters of the United States. No other single operation, within the power of Government, can more effectually tend to strengthen and perpetuate that Union which secures external independence, domestic peace, and internal liberty."

In my own teaching I have made extensive use of a book by a distinguished economist, Peter Bernstein, *Wedding of the Waters*. It's about the construction of the Erie Canal in the early years of the 19th Century. Its development was, of course, a marvel of surveying, engineering, and construction at the time, but what Bernstein is most interested in is the extraordinary impact that this infrastructure investment had on the economy of the state, the region, and the nation. The Erie Canal connected the newly settled areas of the Mid-West and Great Lakes regions to the original states, and allowed the agricultural products and natural resources to reach Eastern and world markets, and for industrial products to reach what was then America's frontier. New cities were born, like Buffalo and Syracuse, and older cities took on new and prosperous economic functions, like Albany and, of course, New York City. The Erie Canal reinforced New York City's pre-eminent position, as America's center of finance, commerce, and international trade, a position that it has held for over 200 years. In a word, the Erie Canal created what we have known as the American economy.

Similarly, as William Cronan, distinguished University of Wisconsin historian, demonstrated in his monumental *Nature's Metropolis*, the coming of the railroads to Chicago fundamentally changed the economies and the natural and built environments of that great city and of the Plains and other western regions of America, by making it possible for the products of America's "Great West" to reach national and regional markets.

In a March 2012 report of President Obama's Treasury Department with the Council of Economic Advisors (CEA), it was noted that the United States has a rich history of investing in infrastructure and reaping the long-term benefits. Those benefits include both the short-term effects of stimulating the maintenance and creation of construction and construction-related jobs and long-term economic growth. It seems that every surface transportation authorization bill, at least since ISTEA in 1991 (and probably before), has been justified on the basis of stimulating construction employment, the so-called "jobs' multiplier" effect. Elected and appointed officials are fond of

talking about 20,000 or 30,000 or 50,000 new jobs' being created by the enactment of such legislation. I have done so, myself.

While infrastructure investments play an important role, in stimulating construction jobs, quantifying the so-called multiplier effect is, perhaps, more difficult than it sometime appears. Certainly, infrastructure projects can be important, in stimulating new construction and construction-related positions, particularly, in times of severe unemployment in construction, as was the case during the "Great Recession," which America has recently endured. However, there are substantial uncertainties, in predicting such job growth, and therefore it should not be the sole basis for justifying public investment in infrastructure.

As Holtz-Eakin and Wachs noted in the BPC white paper, to which I have referred, "Spending on transportation is often justified on the basis of jobs impacts, but estimated multiplier effects carry substantial uncertainty. Generally, they are not purely data-driven; rather they rely on judgments and assumptions, may not take into account aspects of the structure or timing of an investment that would have an impact on its actual multiplier effects, and may miss qualities of the specific economic environment in which an investment is being made. These uncertain estimates about how many jobs will be created by a given increment of transportation spending too often obscure meaningful comparative assessment of different investment opportunities."

As the BPC white paper further noted, "Short-term job creation, while vitally important, must be viewed within the context provided by a long-term view. Over the long-term, higher productivity . . . is the key to higher labor earnings and improved standards of living." It is the long-term economic benefits, in terms of productivity, efficiency, access to markets, and labor force flexibility, which should be the goals and purposes of public investment in transportation and other infrastructure projects and programs. The March 2012 Treasury-CEA report noted that investments in infrastructure allow goods and services to be transported more quickly and at lower costs, resulting in both lower prices for consumers and increased profitability for firms. This report also concluded that infrastructure investment created middle-class jobs. It reached this conclusion, based on an analysis that 80 percent of the jobs created by investing in infrastructure would be in the construction, manufacturing, and retail sectors and that, by distribution of wages in these three sectors, 90 percent of these jobs would be defined as middle-class jobs, that is, between the 25th and 75th percentiles in the national distribution of wages.

However, selecting and supporting those infrastructure investments that promise the greatest short- and long-term economic benefits in a time of persistent budget deficits and stagnant public spending is a difficult challenge to public policy leaders. Public investment capital is constrained, not least by a political environment that often views "investment," as just another category of spending, and by a political process that seems incapable of establishing sustainable revenue streams for such investments.

Surface transportation funding at the federal level has been stagnant for several years, and the motor fuels taxes, on which such funding depends, have not been increased in over 20 years. As BPC's transportation policy project noted in its June 2011 report, "The reality is that federal transportation spending is likely to be under enormous pressure for some time to come, despite compelling evidence that we have been falling consistently short of making the infrastructure investments needed to sustain an efficient, safe, environmentally sustainable, and well-functioning transportation network." The same may be said about all other areas and categories of infrastructure.

The premium, then, needs to be on making "wise" infrastructure investments, that is, those that promise the greatest economic benefits, in terms of increased productivity, efficiency, and job creation. Unfortunately, although there are exceptions, America does not have in place an analytical, planning, and capital programming framework that allows such investment decision-making to occur. We need to be able to develop comprehensive strategic capital programs, in which investments are synergistic and prioritized, and, pursuant to which, scarce resources are directed to the most promising projects.

For many years, Edward Gramlich, a distinguished economist and former Federal Reserve Governor, argued that the greatest returns could be found with investments in existing assets. This view was consistent with the analytical approach of a report several years ago to the United Kingdom's Treasury and Department for Transport (DfT) by Sir Rod Eddington, former CEO of British Airways (the Eddington Report). The Eddington Report concluded that, generally, the most positive benefits, in relation to costs occurred with incremental improvements to existing facilities and networks, rather than from large "build-it-and-they-will-come" projects.

Most important, and relevant, about the Eddington Report, however, was its application of benefit-cost analyses to competing projects and its reliance on economic factors, in making choices about the investment of constrained public resources. For example, it found that, given the tremendously important role of the London metropolitan region to the national economy

and of the movement of goods and services to, from, and through a national system deeply dependent upon global trade and finance, investments in the assets and networks critical to these elements of the British economy were, by far, the most beneficial.

Similarly, the decision about an enormous public infrastructure investment – about $20 billion (US) for the development and construction of an entirely new subway line across metropolitan London – in a time of severe austerity was justified on the basis of a strong business case that completion of the new Crossrail line would serve to enhance mobility and access in London and benefit the agglomeration of financial and related services, on which the British economy has come to depend for economic growth and prosperity.

Of course, neither the Eddington Report nor the business case for Crossrail has perfect application to the decisions that America's public leaders have to make about infrastructure investments, but the analytical and decision-making processes that have been used in those cases do seem relevant to the United States. We need to be able to make better and "wiser" infrastructure decisions in the context of scarce public investment resources, stagnant federal infrastructure funding, and the unwillingness of Congress to provide for sustainable revenue sources to support such investments.

Of course, these circumstances stimulate other significant federal policy changes, in order to respond to the need for greater infrastructure investment. For one thing, as federal infrastructure funding stagnates, the investment burden is falling more heavily on states and localities. Limited federal funds have to be used more effectively to leverage greater public and private investment at those levels. My BPC colleague, Aaron Klein (a distinguished alumnus of this committee staff) and I argued in an OP/ED a few months ago that the federal role in infrastructure was, increasingly, moving from funding to financing. This calls for the expansion of existing federal loan and credit enhancement vehicles, like TIFIA, as well as consideration of new ones, such as infrastructure banks and financing authorities. But expanded federal financing requires the establishment of appropriate revenue streams at the state and local level to support federal credit and provide returns to private investors. To that end, federal barriers to state and local innovations to establish such sustainable revenue sources should be eliminated, and such state and local innovations should be incentivized by federal policy.

None of these policy initiatives, however, remove the need to make better and wiser choices. Public capital resources at all levels will remain scarce for the indefinite future, so investments must be made in those infrastructure projects and programs that promise the greatest economic returns, both in

the short-term and the long-term. Analytical and decision-making tools are available to us, in order to select the right infrastructure investments. It is critical that America's public officials use those tools on a consistent basis.