

2019 CIFA Water Infrastructure Investment Summit Economic Outlook

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The Economy is Booming

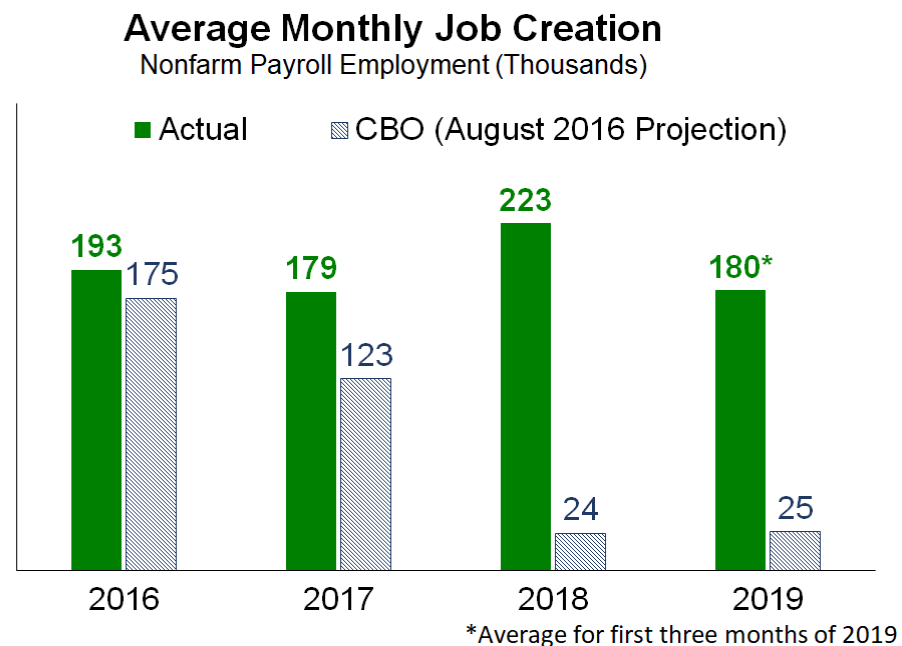
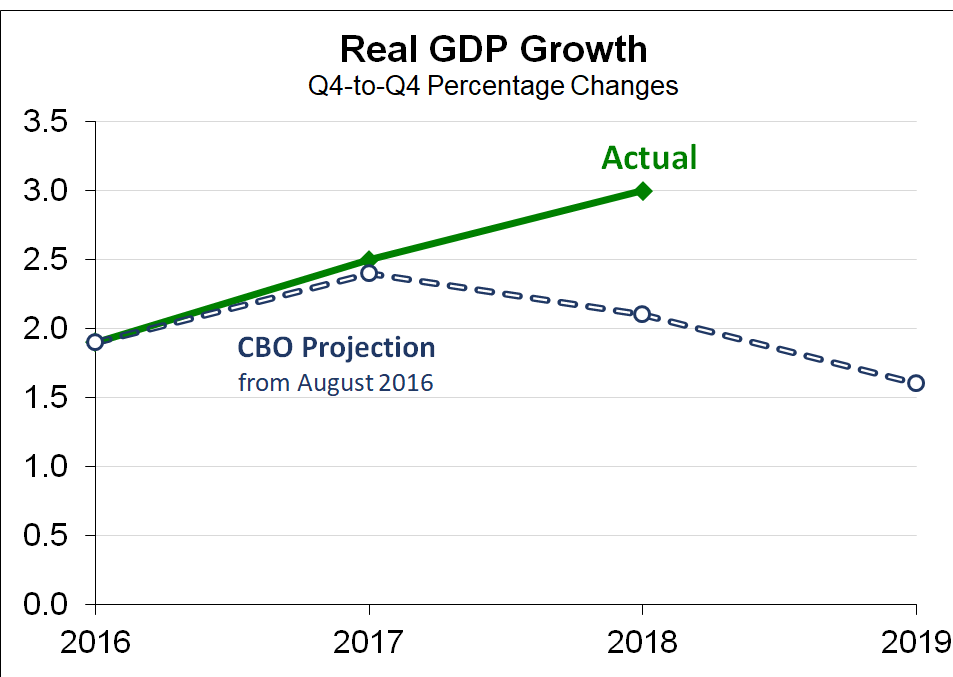
- ▶ The President's Economic Plan is working.
 - Pro-growth tax and regulatory policy have...
 - ...reduced the cost of capital,
 - ...enabling business investment to grow again, which is
 - ...raising labor productivity, leading to
 - ...faster wage growth, which is
 - ...encouraging greater labor force participation, and
 - ...pushing the unemployment rate and jobless claims to 50-year low.
 - There are now more jobs available than people actively seeking employment.
 - Meanwhile, actual inflation and expected inflation remain low.
 - These factors indicate the U.S. economy is growing sustainably.

Stronger Economic Growth and Job Creation:

Real GDP Growth and Average Monthly Payroll Employment Change



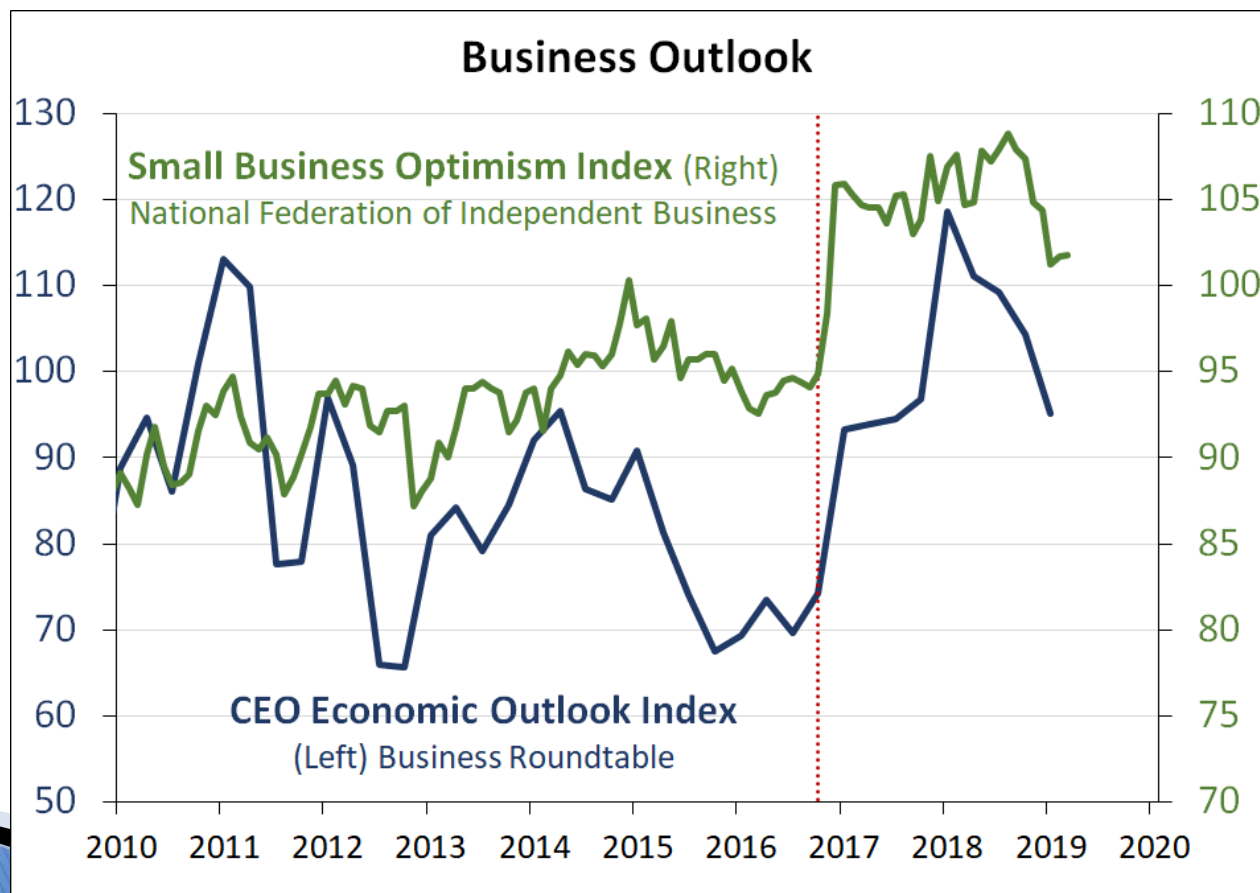
- ▶ As this Administration was taking office, the economic outlook was bleak.
 - CBO projected slowing economic growth and job creation based on the policies then in effect.
- ▶ Pro-growth tax and regulatory reforms have radically transformed the outlook.
 - Growth picked up and robust job creation continues.





End of 2016: Business Outlook Improves

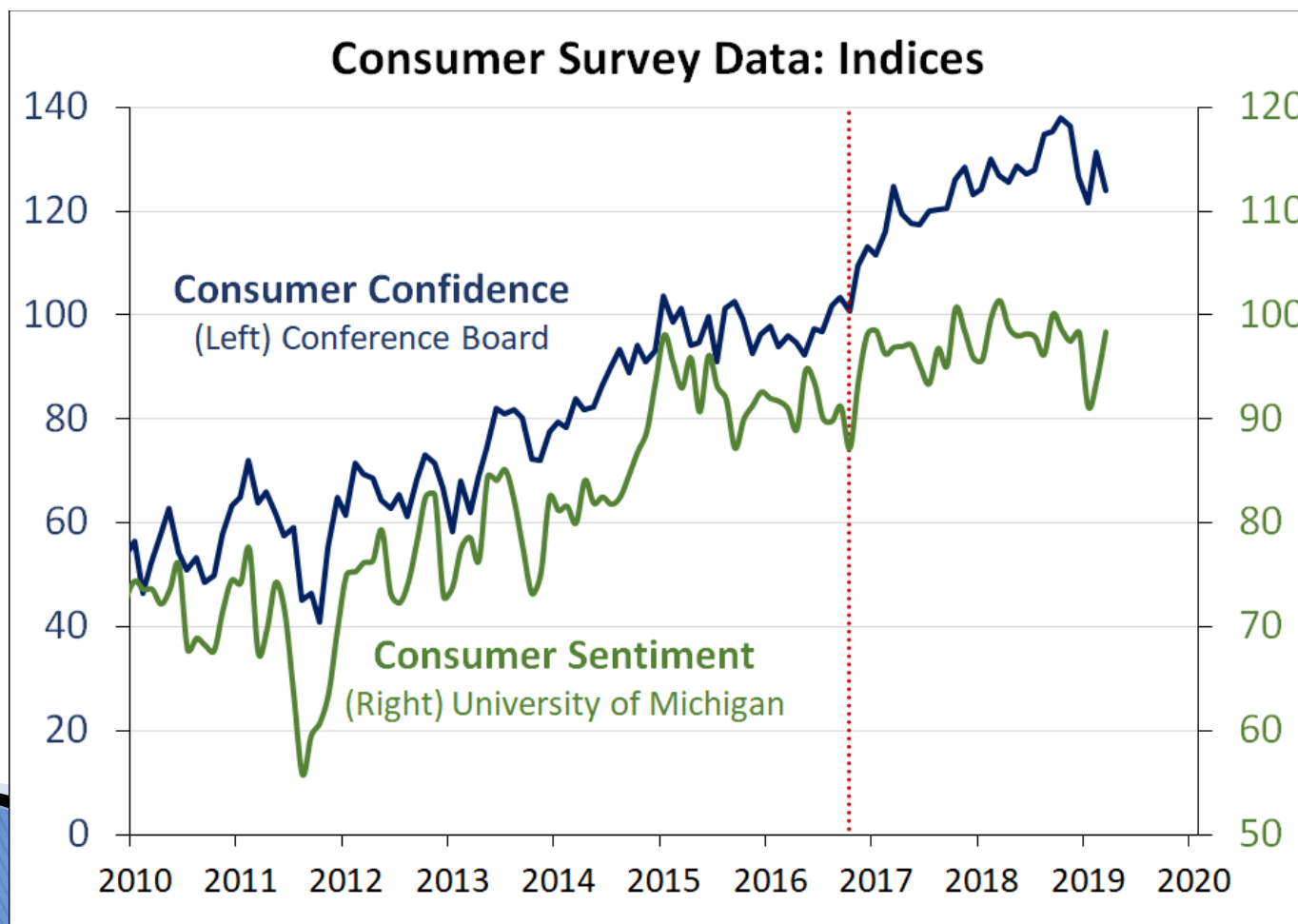
- ▶ The NFIB's Small Business Optimism Index and the Business Roundtable's CEO Economic Outlook Survey have risen markedly.





End of 2016: Consumer Outlook Improves

- ▶ Consumer Confidence—gauges household perceptions of business/job conditions
- ▶ Consumer Sentiment—gauges household and financial situations

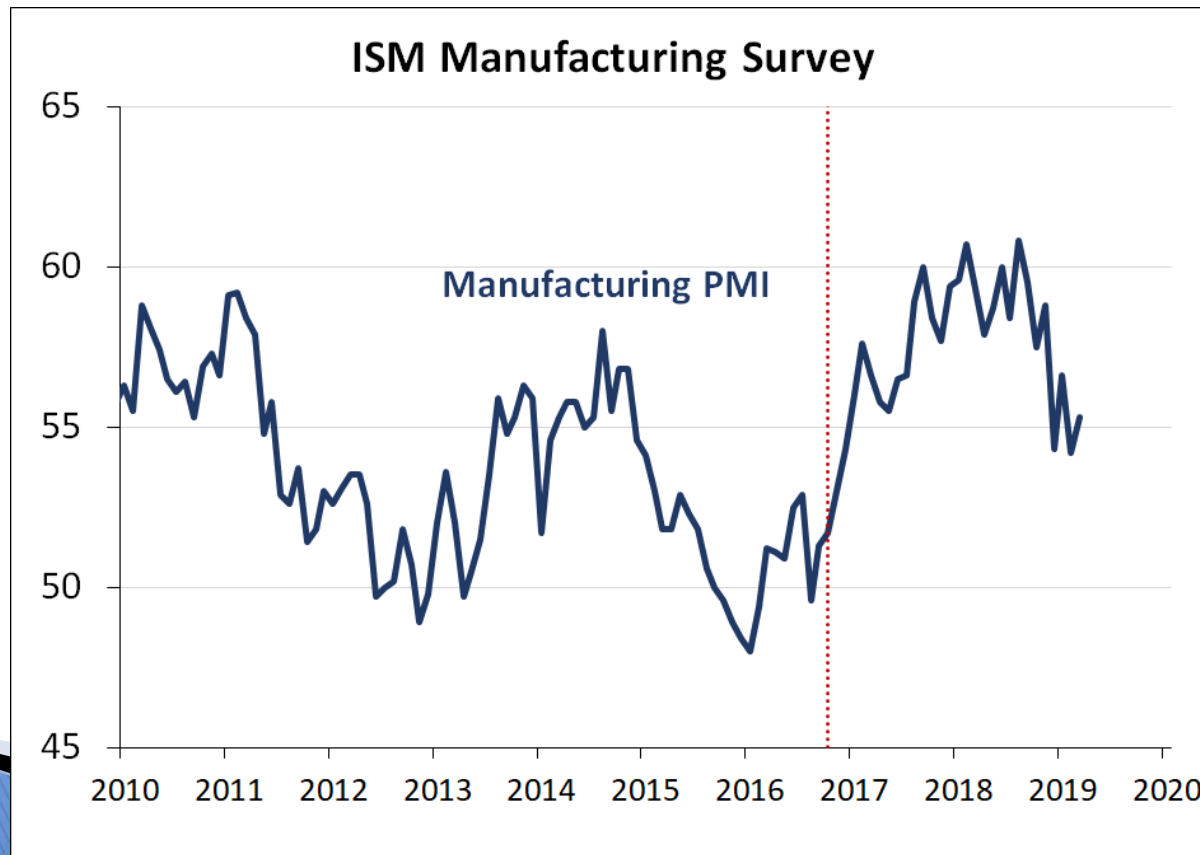


End of 2016: Manufacturing Outlook Improves

The Institute for Supply Management (ISM) Manufacturing Survey



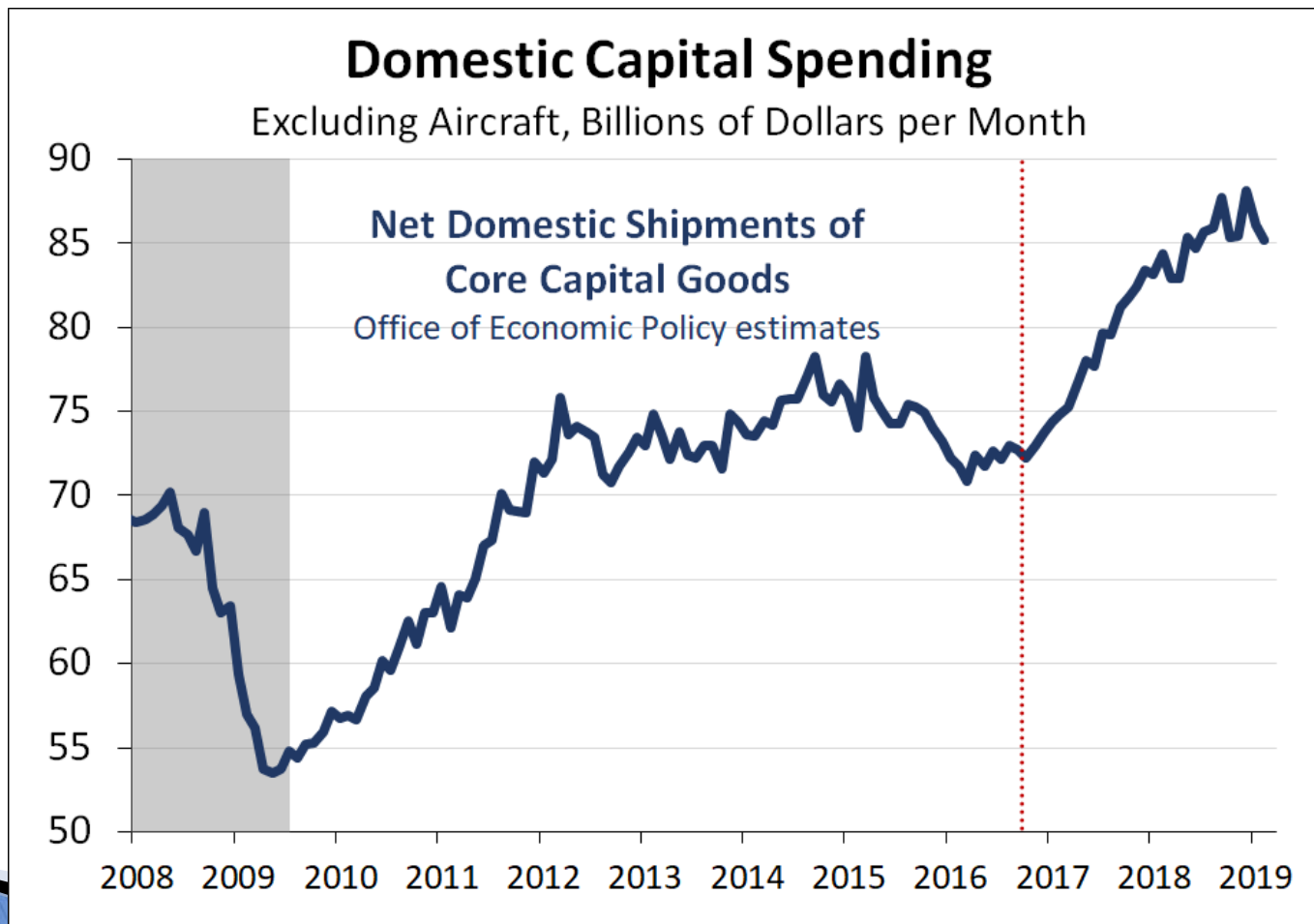
- ▶ ISM's Manufacturing Purchasing Managers Index (PMI) gauges managers' expectations regarding new orders, production, employment, speed of delivery from suppliers, and inventory liquidation.
 - Index values above 50 indicate manufacturing sector is expanding.





Business Capital Investment

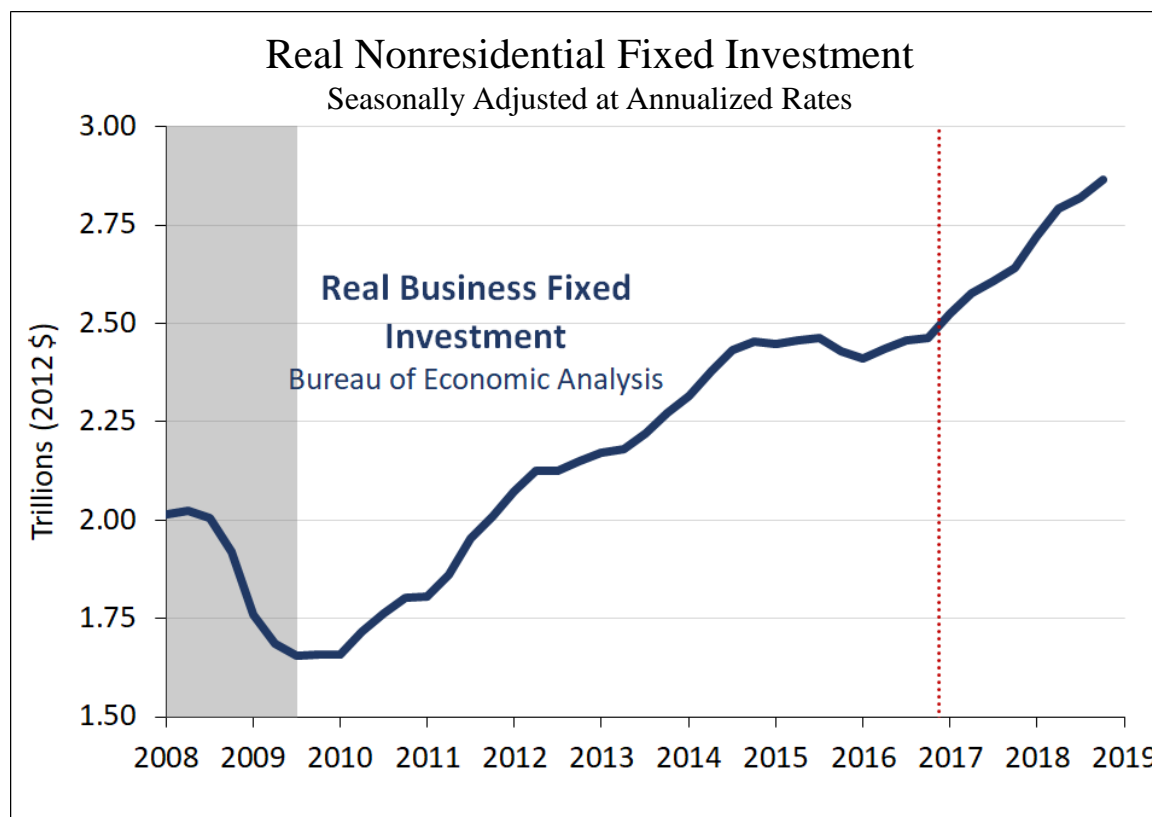
- ▶ Spending on capital has risen dramatically since the end of 2016.





Business Capital Investment

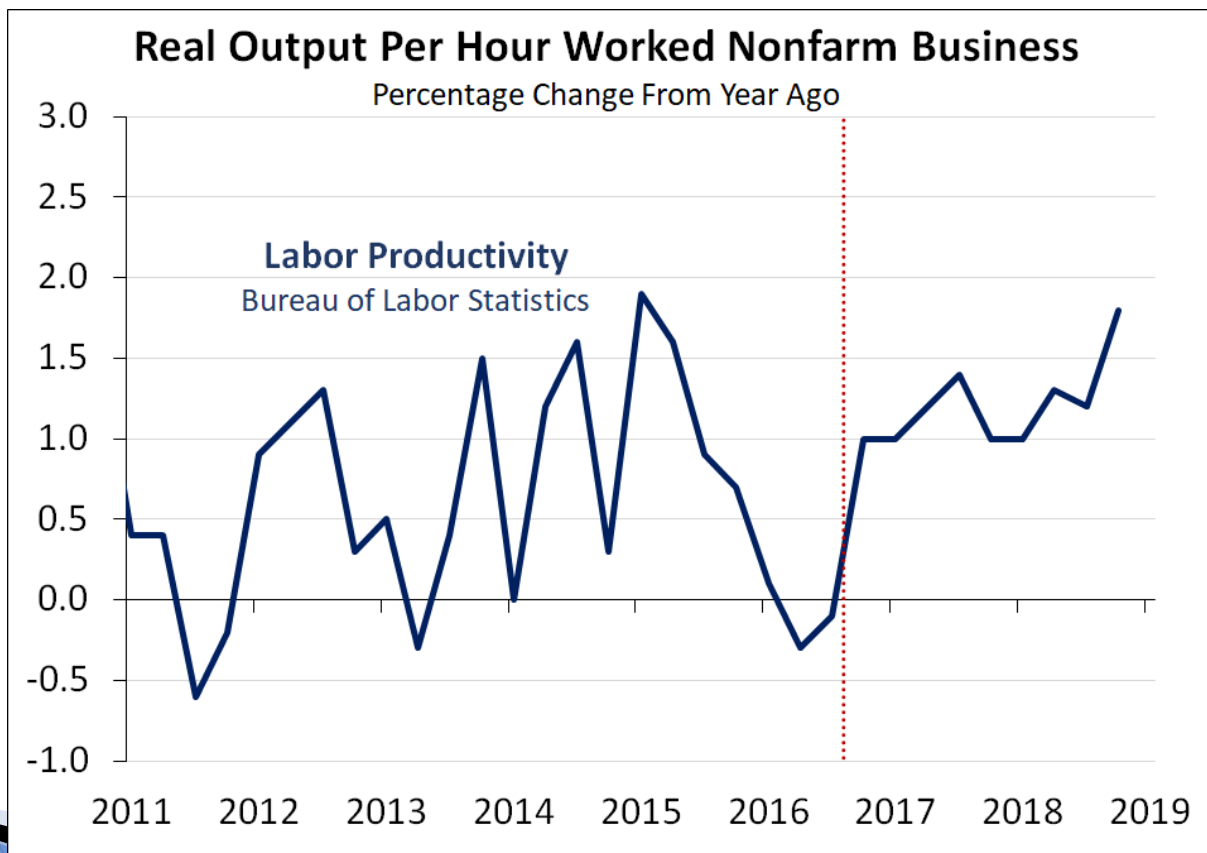
- ▶ More broadly, inflation-adjusted business fixed investment started rising again after stagnating in 2015 and 2016.





Nonfarm Labor Productivity Growth Picks Up

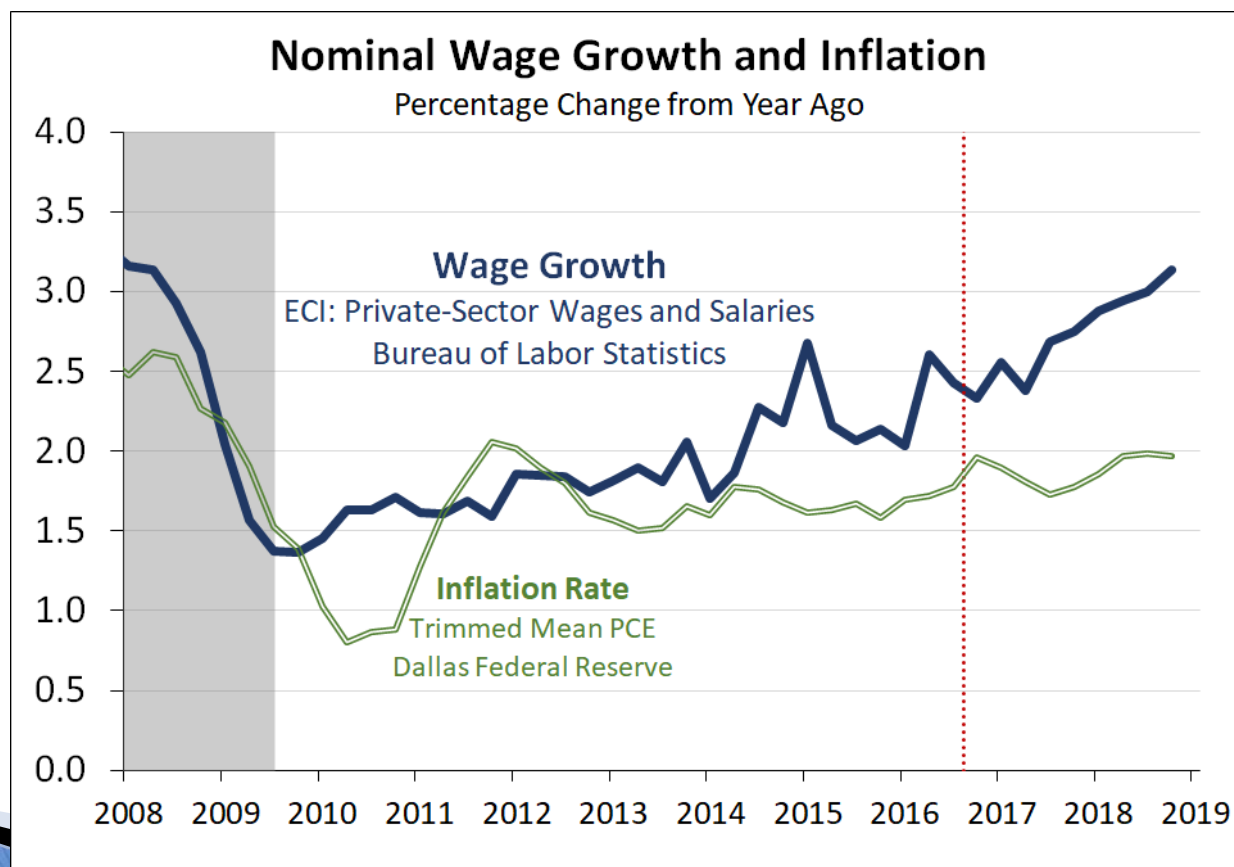
- ▶ Additional capital (tools, equipment, etc. that can be used to produce goods and services) enables workers to be more productive.
- ▶ After an erratic performance, labor productivity now registers sustained growth.





Wages Grow Faster; Inflation Holds Steady

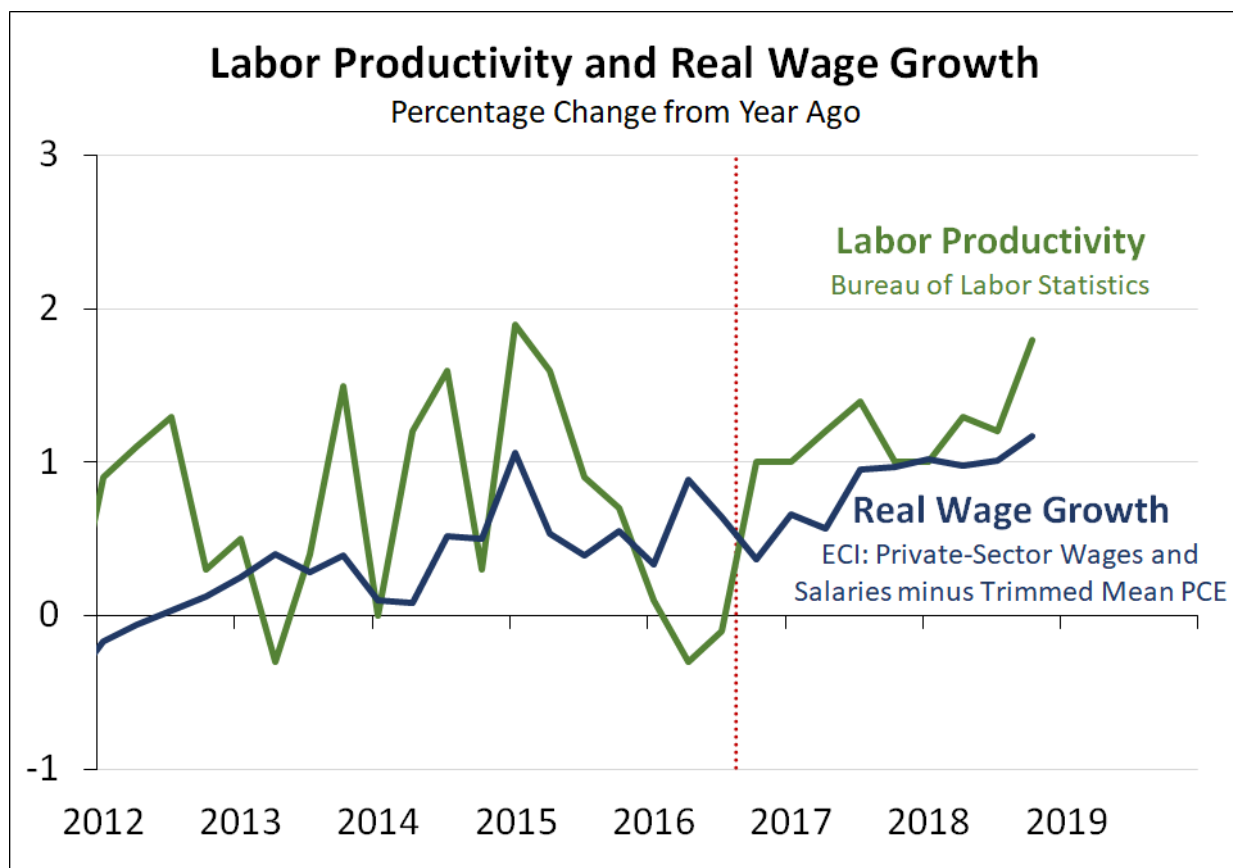
- ▶ Worker wage gains ultimately are driven by labor productivity gains.
- ▶ Inflation has remained stable, while wage growth has accelerated to the highest rate in a decade.





Productivity and Real Wage Growth

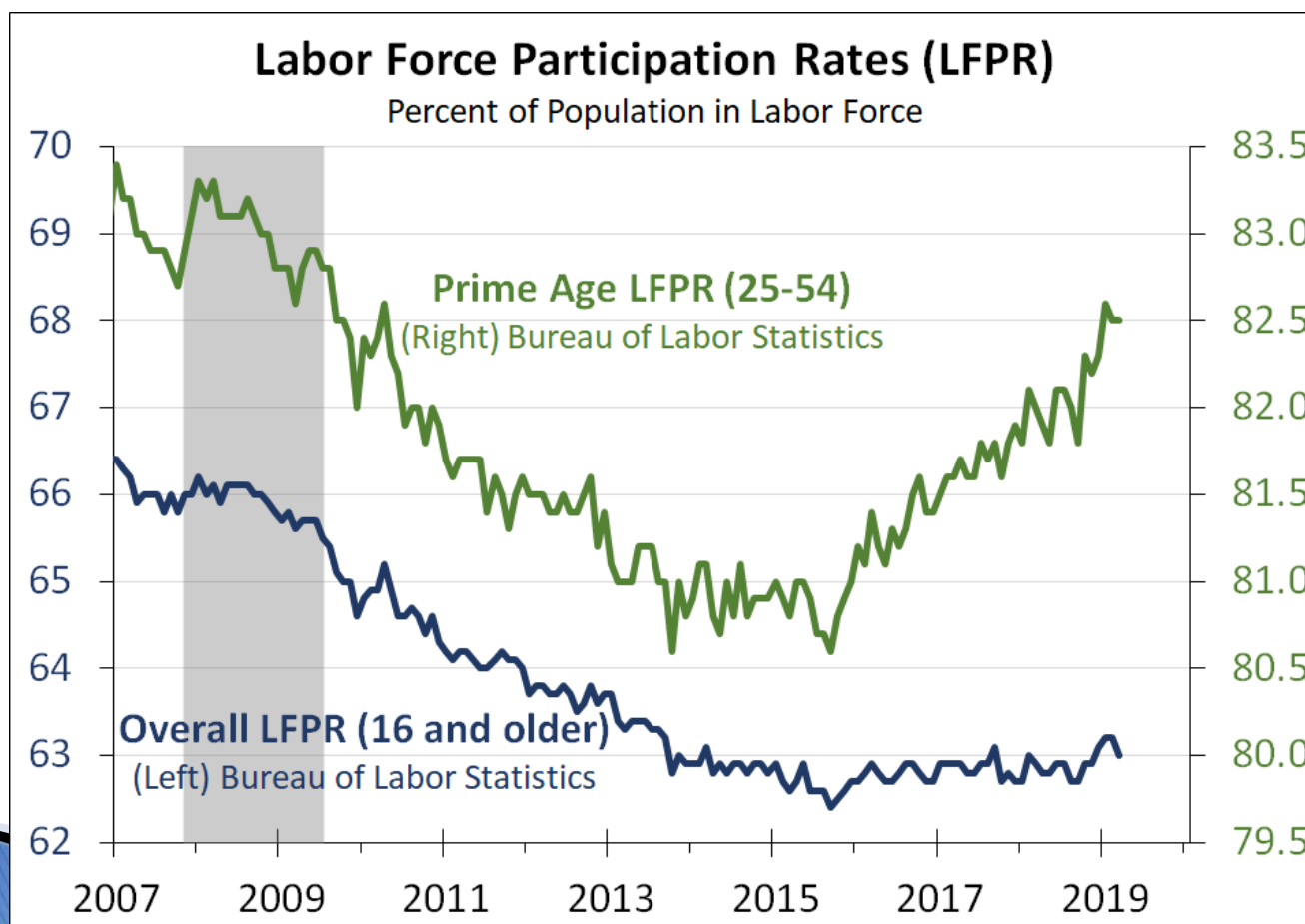
- ▶ The difference between nominal wage growth and inflation is the real wage, which appears to be rising with labor productivity as economic theory predicts.





Labor Force Participation Rates

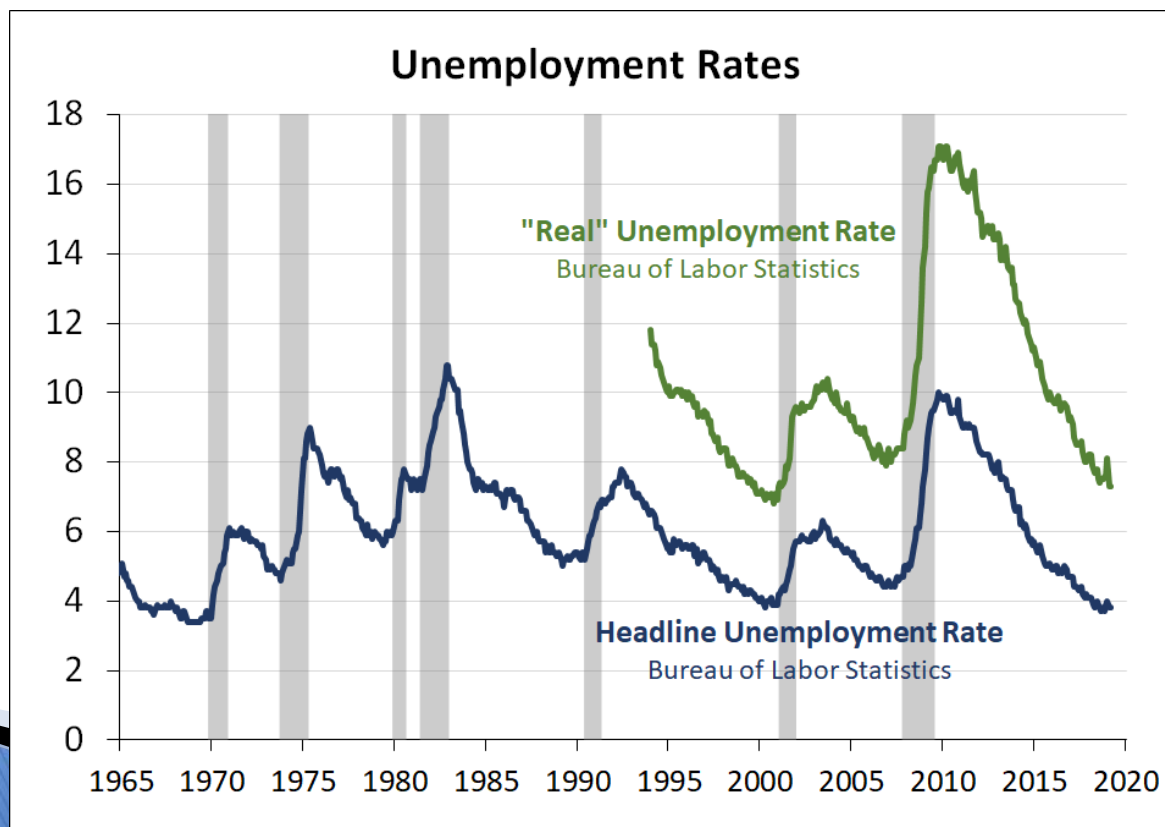
- ▶ It is widely anticipated that an aging U.S. workforce would continue to drag down overall labor force participation rates down; however, prime working-age individuals continue to reenter the labor force.





Unemployment Rates Reach Record Lows

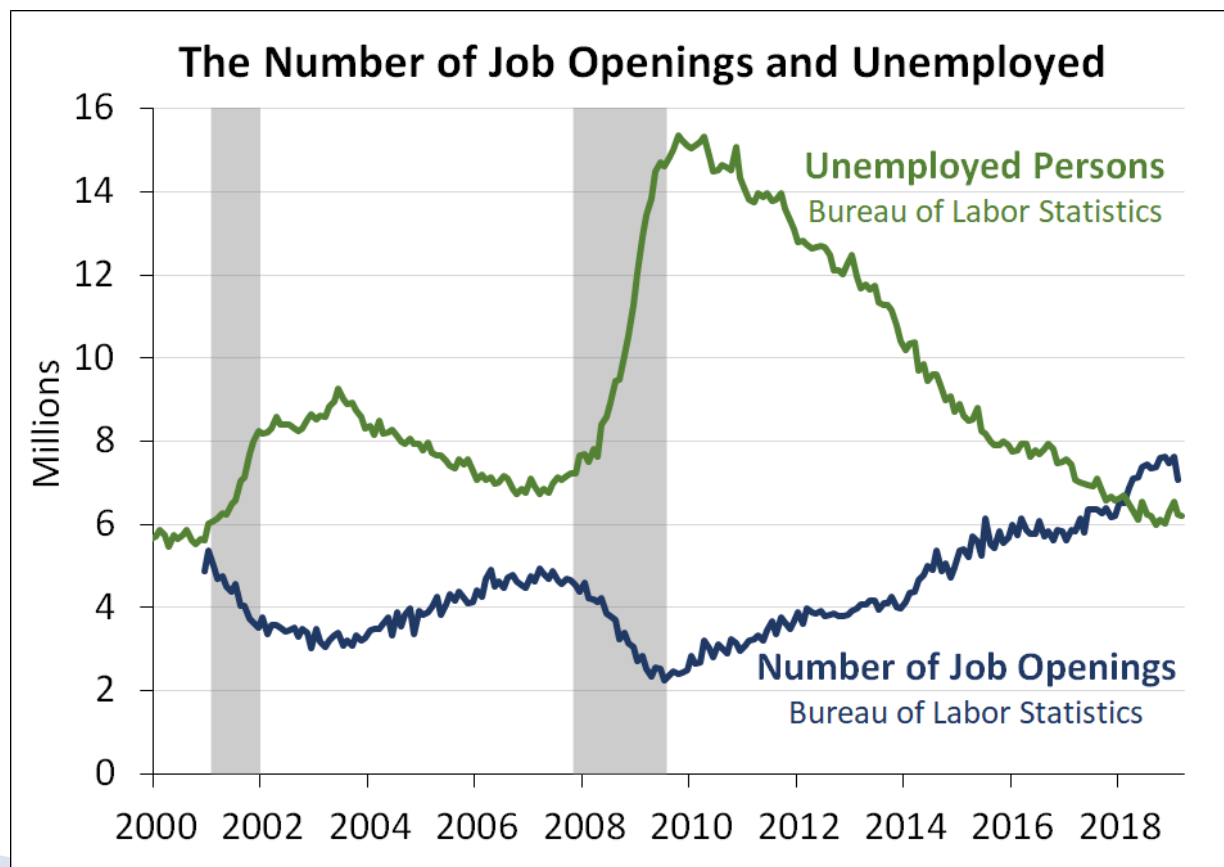
- ▶ In 2018, the “headline” unemployment rate fell to a low last seen in 1969.
 - The headline rate only counts those who searched for work in the last four weeks as unemployed.
- ▶ The so-called “real” unemployment rate is now the lowest since March 2001.
 - This measure includes those accounted for in the headline rate as well as those who searched for work in the past 12 months and those who want full-time work but can only find part-time work.





Job Openings Exceed the Number of Unemployed

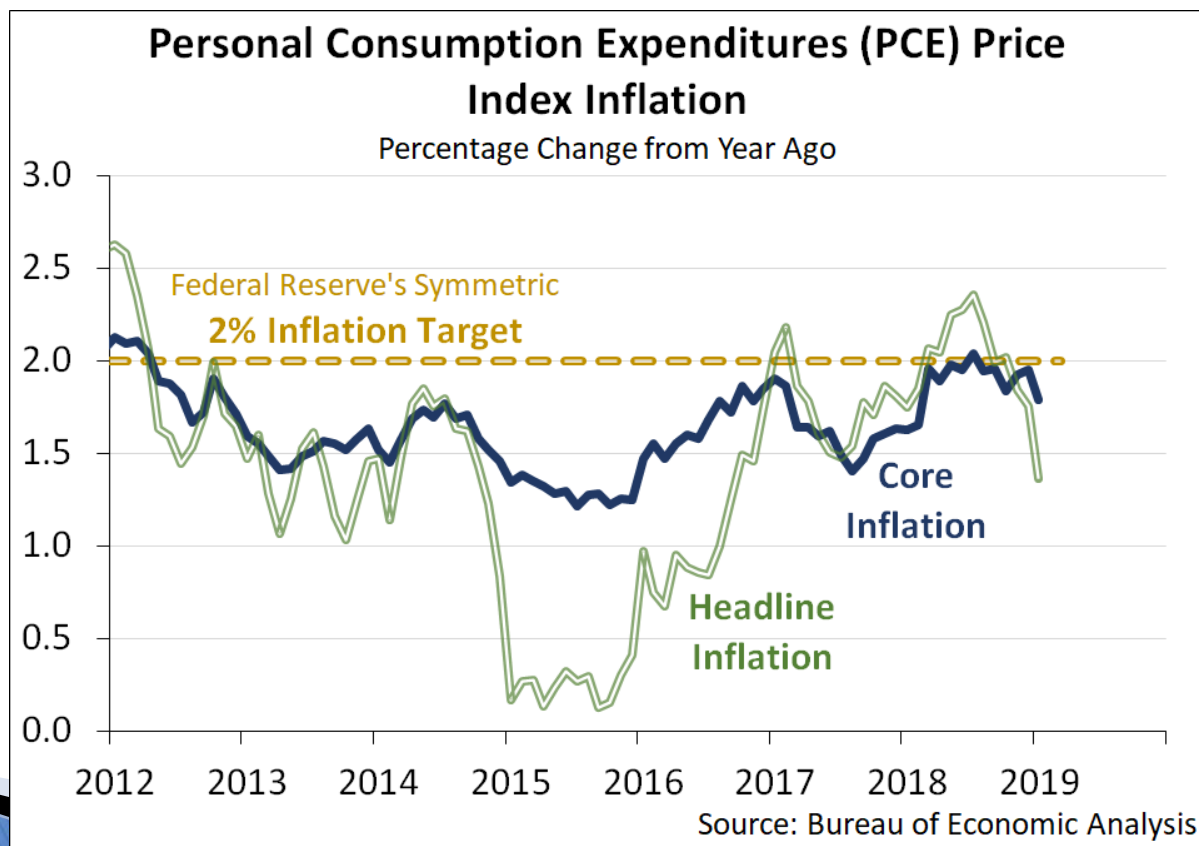
- ▶ There are over 7 million job openings compared to about 6 million who are unemployed.





Inflation Remains in Check

- ▶ Meanwhile, inflation remains at or below the Federal Reserve's symmetric 2% inflation target.
 - “Symmetric” means that 2% is not a ceiling, but an average to be maintained over time.
- ▶ This indicates that faster economic growth is sustainable.





Economic Outlook Summary

- ▶ The U.S. economic outlook has improved dramatically since 2016
 - Real GDP growth is higher
 - Job creation continues to be robust and wage growth has picked up
 - Business investment continues to be elevated

- ▶ Inflation
 - Inflation remains at or below the Fed's 2% target
 - Inflation expectations remain anchored

- ▶ Cumulatively
 - These factors suggest that faster U.S. economic growth is sustainable
 - Compared to CBO's 2016 projections for real GDP growth to slow to 1.6% in 2019, this is poised to be another strong year for the U.S. economy

Infrastructure

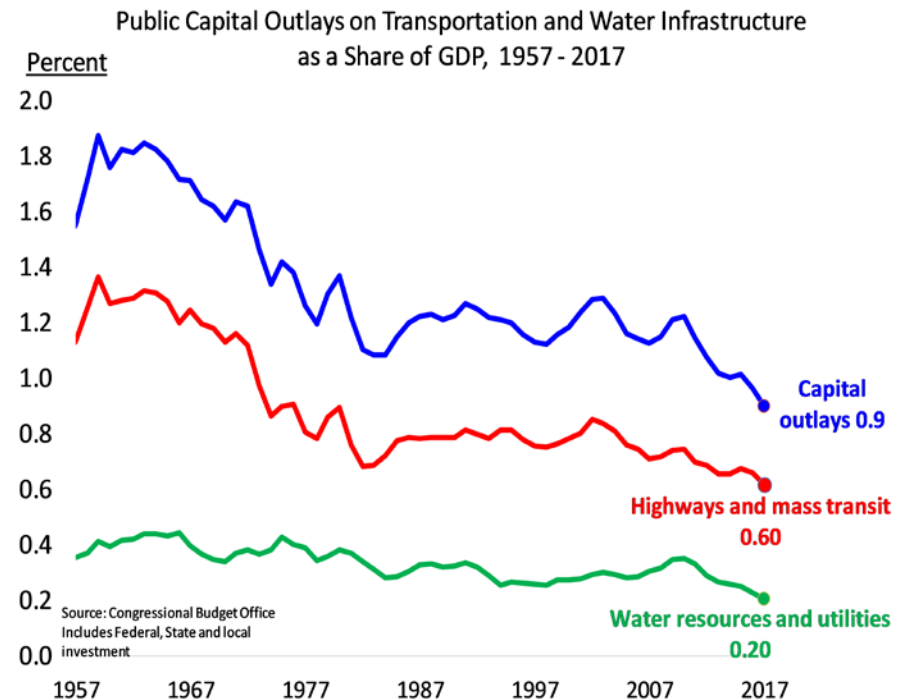


High quality and reliable infrastructure is critical to our continued economic success



Capital outlays for transportation and water infrastructure have fallen as a share of GDP

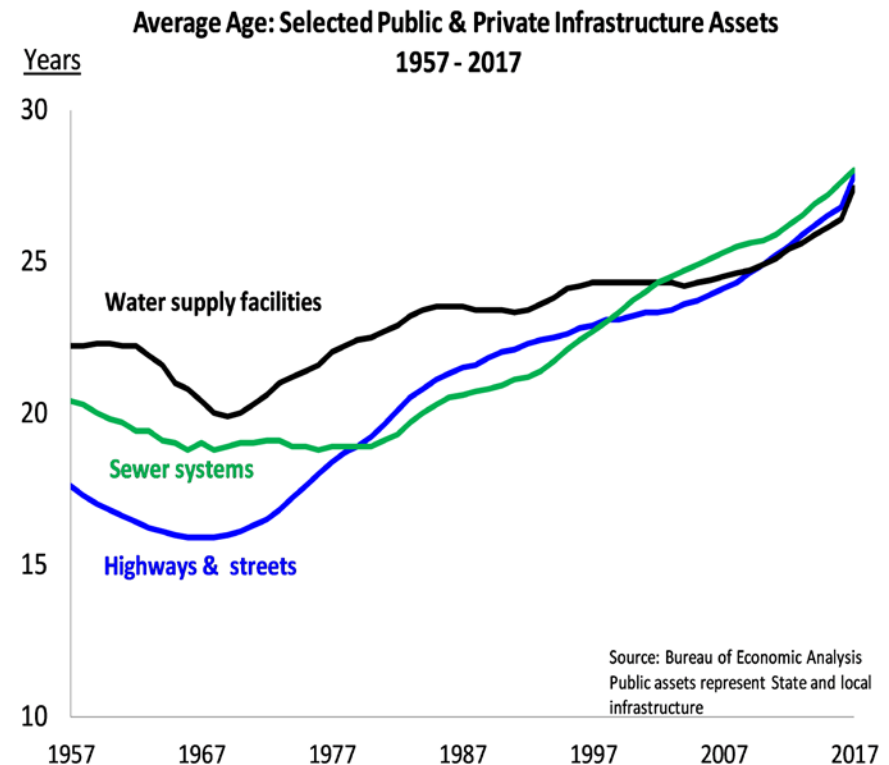
- ▶ U.S. infrastructure assets are **predominantly publicly-owned** in:
 - Surface transportation (roads and transit)
 - Water (drinking water and waste water)



Infrastructure capital stocks continue to age



- ▶ *Chronic underinvestment has imposed significant costs on the U.S. economy*
- ▶ **Surface transportation:** 6.9B hours in traffic, costing \$160B in additional fuel and time
- ▶ **Water:** 240,000 water main breaks annually, property damage and service interruptions
- ▶ **Electricity:** Low resilience to weather-related outages costs \$18B-\$33B annually



Channels through which infrastructure increases productivity in the long run



- ▶ Improved transportation infrastructure lowers the cost to firms of obtaining labor, capital and energy inputs for goods and services they produce and delivering output to customers.
- ▶ Improved transportation and communications infrastructure enhances the transmission of cost reductions and knowledge spillovers from frontier to lagging firms.
- ▶ Improved transport reduces congestion and commuting times, improving labor market efficiency.
- ▶ Clean drinking water and adequate sanitation improve public health and can lead to more productive workers; replacing old pipes reduces leakage and major disruptions.

The President's Goal: At Least \$1 trillion in Infrastructure Investment



The Administration has committed to working with Congress to significantly improve our Nation's infrastructure by:

- ▶ **Seeking a long-term surface transportation bill:** the Administration looks forward to working with Congress to reauthorize the current surface transportation bill, which expires at the end of 2020.
- ▶ **Providing \$200 billion for other infrastructure priorities:** the Administration believes it is important to provide additional investments in infrastructure, across a range of sectors, including water infrastructure.
- ▶ **Make targeted Federal investments:** the President's 2020 Budget also includes increases for important infrastructure grant programs, including \$3 billion for DOT's INFRA and BUILD programs.

Executive Order 13868: Promoting Energy Infrastructure and Economic Growth



- ▶ Promote efficient permitting processes that employ a single point of accountability, avoid duplicative and redundant studies and reviews, and establish clear and reasonable timetables
- ▶ Rulemaking to examine applicability of existing safety regulations for modern LNG facilities that are much different than smaller facilities prevalent when regulations were drafted 40 years ago

Federal Capital Revolving Fund (FCRF): Agencies underinvest in Federal capital assets



- ▶ Currently, before an agency can purchase real property it must receive an appropriation for the *full* purchase price
 - The appropriation scores in that year against the agency's discretionary caps and the maximum funding that the Appropriations Subcommittee can provide
- ▶ It is difficult to make large and irregular acquisitions that contend with operating and programmatic expenses for limited resources
 - As a result, agencies will resort to short-term consecutive operating leases to meet longer-term requirements

FCRF Mechanics



- ▶ FCRF is capitalized initially by a \$10 billion mandatory appropriation; total annual capital purchases are limited to the lower of \$2.5 billion or the balance in the FCRF
- ▶ OMB first reviews the project, and it must be designated in advance in an appropriations Act, including an appropriation for the first repayment
- ▶ An eligible project is a Federal facility acquired by an agency for its use
- ▶ Capital asset purchases would be scored as direct spending, while agencies would use discretionary appropriations to fund annual repayments
 - Repayments to the fund would be made from future appropriations over 15 years, and used to replenish the fund for future purchases

Innovative financing strategies: Public-private partnerships (P3s)



- ▶ Well-designed P3 projects can deliver benefits that are greater when:
 - Bundling exists across phases
 - Private sector expertise and innovation
 - Competition

- ▶ Private financing is not a substitute for public funding but it is a tool for state and local governments

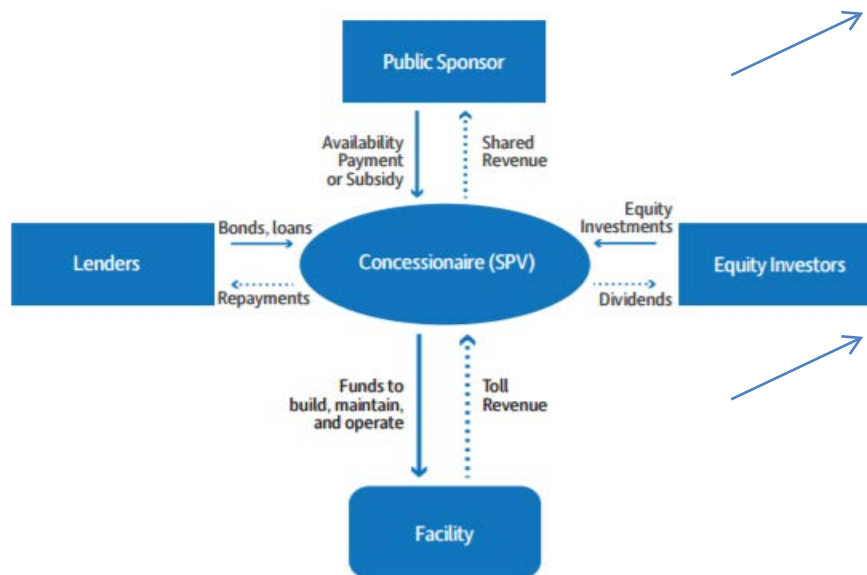
- ▶ Governments must evaluate whether a P3 can deliver a project at lower cost over the project's lifecycle than conventional procurement

Mechanics of a P3



Traditional Public Sector Procurement:

- The government sponsor owns the asset but contracts with *separate* private firms to complete each phase of the project, e.g. designing, constructing, operating and maintaining the asset
- Each private firm makes decisions for the part of the project it is responsible for, without considering the whole project
- Government sponsor finances the project through municipal bond market and/or other government financing sources and subsidies



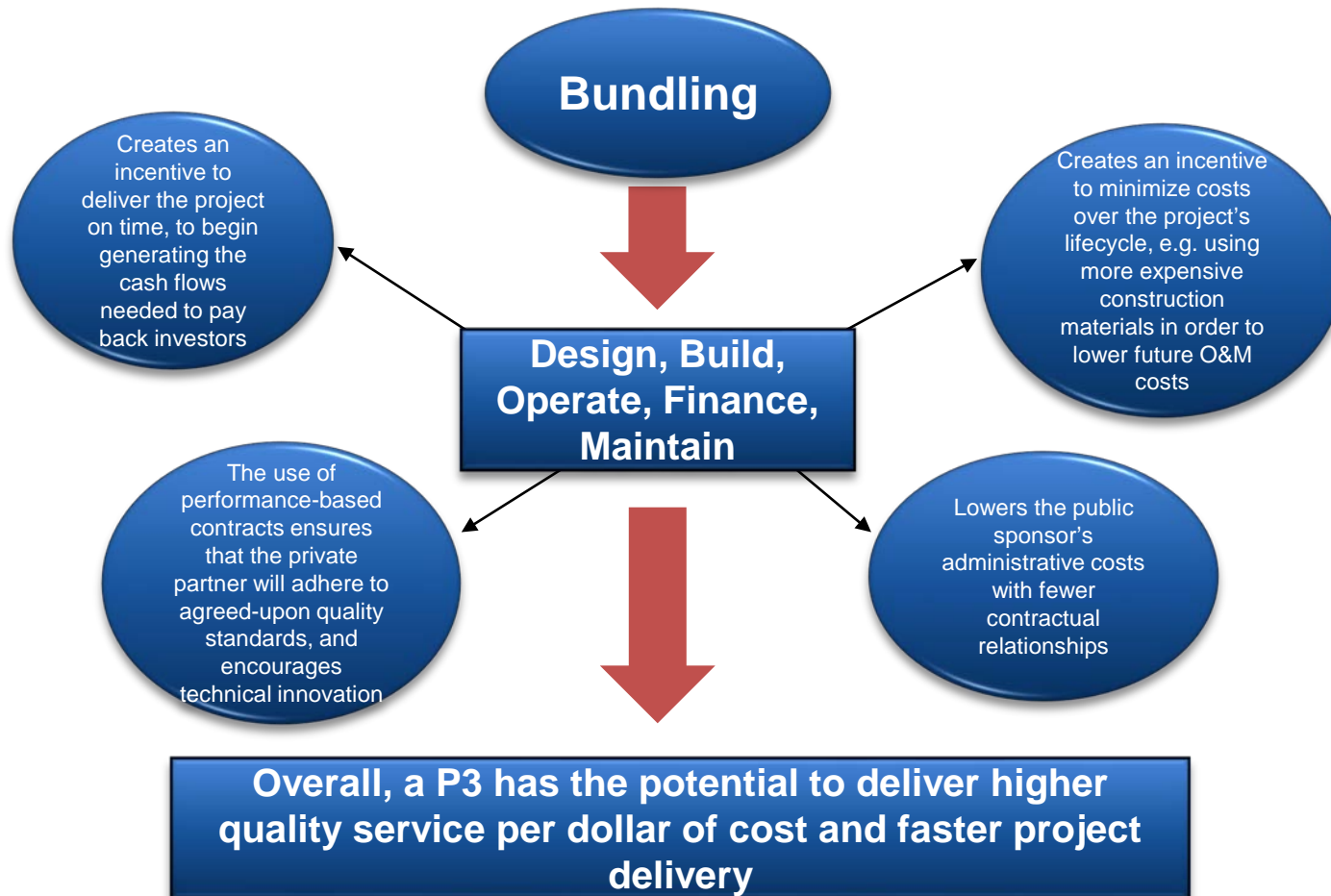
Innovative P3 Procurement

- Under a P3, the government sponsor retains ownership of an asset but contracts with a *single* private entity to do some combination of the design, build, operate and maintain project phases (Bundling!)
- Typically, a legal entity called a project company or special purpose vehicle is established to manage the combination of the phases. The project's capital structure has equity from the project company owners, which could include private equity funds, pension and other institutional investors.
- Capital outlay and operating expenses are financed through bank loans and/or bond issuance.
- Federal, state or local financing and/or credit assistance is utilized where available.

Note, a P3 requires a dedicated revenue stream, or funding source, to be viable through users fees or availability payments from the public sponsor



Benefits of P3s to the Taxpayer, Compared to Conventional Methods



Why is the U.S. behind other countries in the use of P3s?



- ▶ Public sponsors focus on the low cost of municipal bond financing versus private debt, instead of the cost savings that a P3 brings
- ▶ State & local governments often lack necessary project finance or technical expertise to manage a P3
- ▶ Tax law limitations
- ▶ A patchwork of P3-enabling legislation across states
 - It is difficult to navigate the U.S. Federalist system where infrastructure decision-making authority is widely dispersed among Federal, state and local jurisdictions
 - Lack of standardized legal documents and credit enhancement products
 - Unpredictable timing for project approvals and permitting

Conclusion



- ▶ The President's economic plan is working
 - Three percent GDP growth
 - Faster real wage growth
 - Near record low unemployment
 - Low inflation

- ▶ Infrastructure is an important part of that plan
 - Our aging infrastructure is holding us back
 - Federal dollars as a multiplier
 - Streamline permitting