



AgEcon SEARCH
RESEARCH IN AGRICULTURAL & APPLIED ECONOMICS

The World's Largest Open Access Agricultural & Applied Economics Digital Library

This document is discoverable and free to researchers across the globe due to the work of AgEcon Search.

Help ensure our sustainability.

Give to AgEcon Search

AgEcon Search
<http://ageconsearch.umn.edu>
aesearch@umn.edu

*Papers downloaded from **AgEcon Search** may be used for non-commercial purposes and personal study only. No other use, including posting to another Internet site, is permitted without permission from the copyright owner (not AgEcon Search), or as allowed under the provisions of Fair Use, U.S. Copyright Act, Title 17 U.S.C.*



Financing Urban Highways and Transit



**Clifford Winston
Brookings Institution**

Public Sector Problem, Private Sector Perspective

- Discussions of financing arise for the public sector
- More precisely, the discussion is concerned with how to fund public deficits—for example, introduce a new tax or find another source of funds
- Private sector firms finance their operations from revenues from the sale of products and services and from capital markets

Efficient Financing

- Private firms efficiently finance their operations or they fail. Efficiency encompasses:
 - Pricing
 - Production
 - Maintenance
 - Investment
- How has the public sector performed?
- Is privatization the answer?

Pricing

- Public enterprises are justified on the basis of social desirability: compare consumer surplus with deficits
- Value considerations: the service should provide sufficient value so that users' willingness to pay generates sufficient surplus and revenues so the service is socially desirable
- Prices should cover enough of the relevant costs so that the service is socially desirable

Pricing in Practice

- Highway and transit prices are far below private and social costs
- Highways provide sufficient value such that prices could be raised to reduce deficits and the social costs of congestion and road damage. This may not be true for transit.
- Raising prices faces political obstacles
- Cost reduction is thus critical to improve financing.

Cost Reduction in Practice

- Costs can be reduced by reducing production, maintenance, and investment costs but, in practice, this has proved difficult
- Production costs are inflated by regulations (e.g., buy-American provisions, Davis Bacon Act)
- Maintenance costs are also inflated (capital subsidies in transit, suboptimal highway design)

Cost Reduction (continued)

- Investments are not based on cost-benefit analysis. Costs are often underestimated and benefits overestimated.
- Some investments are earmarked expenditures that elected officials provide to constituents—“bridges to nowhere.”
- In sum, US urban bus and rail transit systems run large deficits and highways are now running a deficit.

Public Sector Solutions

- Public sector solutions call for more funding for transit and highways—alternatives include VMT taxes, an infrastructure bank, and public-private partnerships.
- But those approaches ignore the inefficiencies in pricing and production, maintenance, and investment—inefficiencies that won't be addressed.

Privatization

- Privatization of urban highways and transit may provide incentives to improve pricing to respond to users' preferences and to improve the efficiency of operations and investments.
- Privatization may also lead to innovations and more technological advance
- Experiments are essential to see how privatization would perform in practice.