Committee for Sydney

Parliamentary committee to examine options for financing faster rail

Submission from the Committee for Sydney

December 2019

The Committee for Sydney, herein after referred to as simply 'the Committee', welcomes the opportunity to respond to the Discussion Paper released as part of the *Parliamentary committee to examine options for financing faster rail*, hereafter referred to as 'the Discussion Paper'.

This submission should be taken as the internal views of the Committee for Sydney, and are not necessarily reflective of the views of our member organisations.

About the Committee for Sydney

The Committee for Sydney is an independent think tank and champion for the whole of Sydney, providing thought leadership beyond the electoral cycle. Our aim is the enhancement of the economic, social, cultural and environmental conditions that make Sydney a competitive and liveable global city.

Introduction

The Committee has long been an advocated for faster regional rail, both across Australia and within NSW. We welcome the opportunity to provide this submission and we commend the Morrison Government for undertaking this inquiry.

In 2018, the Committee released a report titled: *The Sandstone Mega-Region, uniting Newcastle, the Central Coast, Sydney, Wollongong*. That report called for the development of a 'mega-region' stretching from Newcastle to Wollongong through Western Sydney and which would act as a global economic powerhouse of 10million people, linked together by fast rail, world-class industries and major trade points.

The report concluded that by introducing a network of one-hour or less heavy rail connections between cities within Sydney's mega-region:

- An additional 40,000 dwellings could be built across NSW by opening up land across rail corridors, delivering over $75 billion of housing affordability improvements for Sydney.

- Businesses would also gain agglomeration benefits from the improved access to Sydney, and that by 2036, there would be an additional 4,725 local jobs in Wollongong, 3,875 in Gosford and 3,225 in Newcastle.

- A moderately fast rail network that reaches speeds of 200 km/h could connect Newcastle, the Central Coast and Wollongong with Sydney in 60 minutes or less.

The Committee accepts that similar benefits would likely be found from comparable investments in the mega-regions around other major capital cities in Australia. Investment in faster rail connections within these mega-regions should be the initial focus for government, with route selection ideally undertaken with a view that such infrastructure could potentially be expanded upon at a future date to deliver a capital-city-linking faster rail network for Australia's eastern coast.

To that end, the Committee welcomes the Australian Government's establishment of the National Faster Rail Agency, which will work with state and territory governments on opportunities to develop rail infrastructure between major cities and key regional centres. We also welcome the *Agency's Faster Rail Plan* as well as the associated funding for business cases on potential links between both Sydney and Newcastle, and Sydney and Wollongong. The Committee acknowledges that the scale of investment required to deliver on these projects is likely to be substantial, and as such, we also commend the NSW Government for continuing to forge ahead with investigations into potential routes for NSW, undertaken by the eminent Andrew McNaughton, former technical director for the UK's HS2 project.

Delivery of such a project is likely to require innovation in both the funding and financing of infrastructure. The Committee acknowledges that this inquiry is primarily focused on the financing side of the equation. Nonetheless, the Committee is of the view that policies which will secure new funding streams from investments in corridor preservation will make securing private investment more achievable, through an associated reduction in risk pricing within each given project's financing. As such, this submission contains recommendations which address both the funding and financing angles of infrastructure delivery.

We would also like to recommend that the terms of reference for future stages of this inquiry beyond this discussion paper be broadened to also capture proposals to address the funding challenge facing the delivery of faster regional rail.

Issue 1: Corridor preservation

Corridor preservation can provide a means of interim revenue prior to construction and will lower the cost of land-acquisition in the long-run.

The Committee notes that Infrastructure Australia (IA) has identified corridor reservation for future investments in an East Coast High Speed Rail Network as one of its top 'High Priority Initiatives' on its 2019 Infrastructure Priority List. IA identified that the cost of protecting and acquiring the corridor in full would be approximately $2.8 billion (2016 prices) using a 7% real discount rate, and that all major corridors could be secured within a 5-year window. IA has already mapped seven corridors as national priorities and has estimated that protection and early acquisition could save taxpayers $10.8 billion in the long run. The Committee accepts that the current tight fiscal environment might make such an investment difficult to deliver, and as such, suggests that a phased corridor of land acquisition may be a more appropriate approach, with capital-city links to large regional towns prioritised for initial acquisition. This would also have the benefit of targeting those areas where the most significant savings can be found in avoided future cost, while avoiding the need for capital intensive investment in the purchase of rural that is unlikely to see much appreciation in land values.

The Committee also notes that the Australian Government views corridor reservation as primarily the domain of the states and we agree that state involvement is critical. Nonetheless, the Committee feels that the federal government should come to the table with joint-funding for targeted corridor preservation, as this would send a powerful signal to potential financiers that the project is supported by incumbent governments at both the state and federal level. This message would be doubly amplified by the existence of bi-partisan support for regional faster rail at both the state and federal level.

Despite the initial upfront capital costs, targeted corridor preservation can also be delivered in such a way that it delivers a new revenue stream for government. Infrastructure Australia already operates under an assumption that when corridor reservation takes place, 50% of unimproved properties will be rented out for some interim use; for example, as a carpark or an extension of a private garden. The Committee agrees with Infrastructure Australia that significant rental revenue possibilities exist with the earlier purchase of corridors, particular in those urban areas and major regional areas which would be targeted through a phased corridor acquisition program.

While modelling for such proposals is beyond the scope of this submission, the Committee would like to recommend that the next stage of this inquiry specifically calls for submissions that propose new methods for generating revenue in preserved corridors. The Committee notes that once corridor routes have been identified and infrastructure delivery funding has been announced, the value of land will undergo a notable increase in value, which will also provide opportunities for government to capture some of that value increase through dedicated value capture mechanisms. This presents some opportunity to commoditise the revenue from anticipated future gains from value capture as port of the infrastructure financing process.

Response to Issue # 1:

1. **Recommendation 1:** That the Australian Government collaborate with state governments to jointly fund a 5-year program of land corridor preservation, which will initially target the corridors connecting capital cities to nearby major regional hubs.

2. **Recommendation 2:** That the next stage of this inquiry calls for submissions around the generation of new revenue opportunities from the acquisition of land corridors, including but not limited to, land leasing and value capture mechanisms.

Issue 2: Discount rates

The current discount rate disincentivises long-term, country-shaping rail projects, while a lower rate would be more supportive of regional faster-rail

The Australian Parliament's standing committee on infrastructure has already recommended that the discount rate be reduced from 7% to 4%. Similarly, the Grattan Institute has identified that a lower discount rate would remove the current disincentive for prioritising rail projects, which are made proportionally less attractive by the current rate.

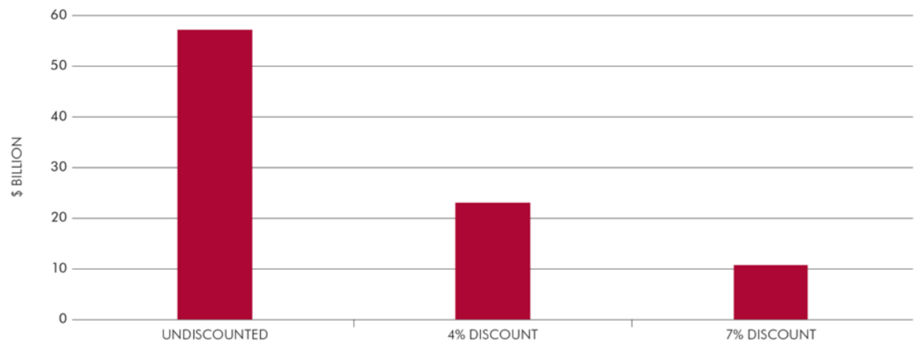
The Committee also acknowledges that Infrastructure Australia has typically evaluated investment in East Coast High Speed rail using a 7% real discount rate. However, the *High Speed Rail Study Phase 2* Report published by the Australian Government in 2013 used a 4% real discount rate, noting that:

> *"A four per cent discount rate has been assessed as more suitable for large scale and long-life infrastructure projects such as HSR, and has therefore been adopted as the discount rate applied for the primary evaluation of HSR"*

That report concluded that a High-Speed Rail network connecting Sydney to Melbourne would have economic benefit cost ratio of 2.5-to-1, making it a worthwhile project overall.

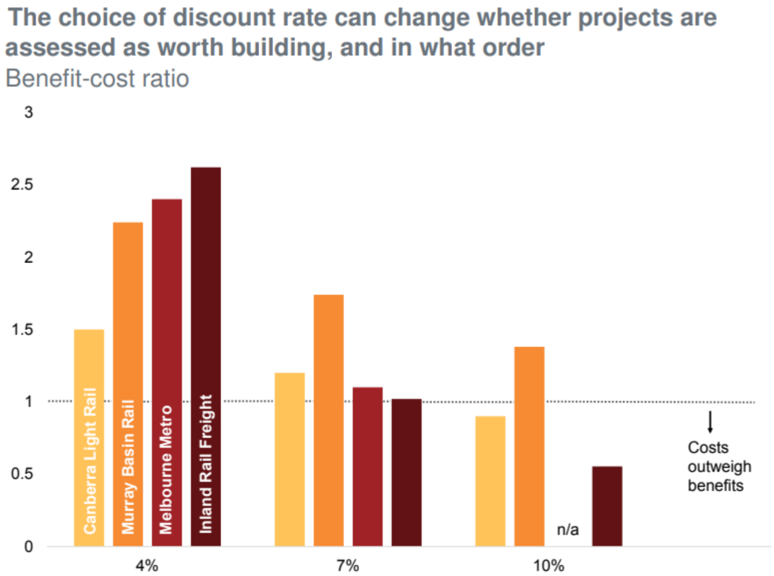
Infrastructure Australia has also evaluated the impact of a lower discount rate on the estimated savings from corridor preservation for an East Coast High-Speed Rail network.

Comparison of total savings from corridor protection on an undiscounted and real discounted basis ($2016)



While it remains the view of Infrastructure Australia that a 7% discount rate remains appropriate for an East Coast High-Speed Rail network, it needs to be acknowledged that this recommendation is specifically for the delivery of land acquisition across the entire network, and as such, cannot be interpreted as an endorsement for a higher discount rate on land acquisition for shorter rail connections, including faster rail link connecting Sydney to Newcastle. The Committee notes that the risk profile for the East Coast High Speed Rail Network, which could realistically only be delivered over multiple decades, is substantially different to the risk profile for a faster rail connection between Sydney and Newcastle. The capacity to more immediately generate revenue from corridor reservation or through value capture in rural areas is also less than is the case for urban and regional areas, as is the potential to avoid higher land purchase costs through early acquisition. As such, the potential benefits identified from corridor reservation on shorter and less rurally intensive legs would be higher and more certain than was identified for the entire East Coast High Speed Rail network. Given this, the Committee has formed the view that while a 7% discount rate may have been an appropriate for corridor reservation pertaining to the East Coast High Speed Rail network, a lower discount rate could be more appropriate for application with regards to both the corridor reservation and project delivery of shorter, faster-rail journeys, including connections between Sydney and Newcastle, Sydney and Wollongong, and to a lesser extent, Sydney to Canberra.

The Grattan Institute has also identified that a lower discount rate would remove the current disincentive for delivering rail projects, which are currently penalized by the 7% rate devaluing the agglomerative economic benefits which typically result from major rail investment.



However, not all rail projects are the same. Urban rail projects are distinct from faster regional rail projects, and short-distance faster regional rail projects are distinct from city-linking high-speed rail projects. The Grattan Institute has recommended that standard discount rates be varied based on risk characteristic, with urban passenger rail given a lower rate than regional freight rail for example. The Committee views this as one possible option for consideration when considering whether to reform Australia's infrastructure appraisal processes. However, setting different discount rates for different asset classes does introduce a level of subjectivity to the appraisals process, and could end up disproportionally increasing the risk associated with some taxpayer investments. A more solution might be to maintain consistency in discount rates across asset classes, while varying the threshold for benefit cost ratios (BCRs) on different classes of projects. Urban road projects with limited long-term agglomerating benefits for example could be required to meet a higher BCR threshold for approval than a nation-shaping high-speed rail network, which will have compounding benefits for generations to come. Such decisions would also require a degree of subjectivity from politicians, but the trade-offs between lower short-term returns and larger long-term returns would be far easier to explain to the average voter than would be the case were you to introduce a complex system of varying discount rates.

The Committee supports the Grattan Institute's recommendation that the Parliamentary Budget Office undertake a review of Australia's system of setting discount rates, as is already done on an annual basis in New Zealand. Such a review could also be undertaken by the Treasury. Regardless of which body undertakes this review, the Committee also recommends that the review considers whether it may be appropriate to set different thresholds for BCRs for different projects. Opening up the possibility of higher BCR thresholds on some projects would also offset the risk that a lower-discount rate system would introduce a higher level of risk for government as an investor.

Response to Issue # 2:

1. **Recommendation 3:** That either the Parliamentary Budget Office or the Australian Treasury review the current system of setting discount rates to determine whether the current rate is too high, and whether a more flexible system is required which differentiates BCR analysis by infrastructure investment typologies.

Issue 3: Prioritisation of shorter trips over major inter-city connections

Shorter connections for higher speed rail are likely to provide more immediate economic and social benefit for capital cities in the long run than longer inter-city connection

The Committee agrees with the Australian Government's decision to prioritise business cases for regional rail projects which will connect capital cities to their surrounding regional areas ahead of investments in projects which connect between the capital cities themselves. Such capital-city connections should absolutely occur in the future, however, as has been identified by Arup's Australasia Transport Developments Leader David Harding, the economic case for regional connections is stronger in the short-term. Given this, land corridor reservation should focus on those connections within the next 5 years, with intercity connections potentially made the focus of purchases in the 5-to-10-year window. The one possible exception to this rule could be a faster rail connection between Sydney and Canberra. The geographic proximity between these two cities is small enough in scale that that a faster-rail connection between these two hours could help bring Canberra into the broader Sandstone Mega-Region. The economic agglomeration potential in Canberra is also stronger, with the city well placed to absorb significant population growth, providing value capture opportunities and helping to lock-in the benefits of economic agglomeration.

Response to Issue # 3:

1. **Recommendation 4:** That corridors be targeted in line with the prioritisation of projects identified by Infrastructure Australia, with all land purchased for regional connections within five years, and land for inter-city connections purchased within ten years.