

Potty PFI?

Kelvin Hopkins MP casts a critical eye over the private finance initiative as both an irrational nonsense and taxpayer's burden...

The Private Finance Initiative (PFI) is one of a ragbag of privatisation schemes that simply puts large sums of public money into private pockets and to no good purpose. It is based on a central myth, a mantra chanted repeatedly that is simply untrue. It is a misleading yet plausible lie, which even otherwise committed socialists seem sometimes to lack the confidence to challenge.

That myth, that lie, is that the level of government debt, of public borrowing, must be kept low, be held down or dire consequences will follow. This is a nonsense, but it is astonishing how many – even on the left – have fallen for it and have failed to challenge the privatisers on their central premise when their whole rationale is baseless and illusory.

As with all debt, provided that it can be funded, there is no problem, and public borrowing can be more easily funded than private finance because it is cheaper. It is time to reverse the drive to privatise and to begin to roll back the ravages of Thatcherism, of which PFI is a bastard offspring.

A problem with politics is sometimes that a simple rational argument has to be repeated several times before it is conceded by those in power. Fashion, prejudice, being 'on message', keeping in step with leaders often seem to be more potent influences in the consciousness of those in politics than reason and logic. This has rarely been more true than today, but some may perhaps be forgiven when every twist of spin in the media and volumes of misleading propaganda are used daily to buttress misguided neo-liberal dogma, of which privatisation is a central tenet.

Counter-arguments to PFI have been made but given very little coverage. The left has the right arguments, but the anti-PFI case needs to be made more confidently and more often.

So what is that case, and how do we put the arguments?

Government borrowing has two components, one of which is cyclical. When the economy slows down, unemployment rises, tax revenues fall and benefits payments increase. Government expenditure increases and income falls so the Government borrows to cover the shortfall until the economy revives. When unemployment falls again, tax revenues rise, the cost of benefits payments fall and government's cyclical borrowing falls. Gordon Brown's

golden rule that borrowing levels across the cycle should be neutral is not unsensible, but this says nothing about the absolute level of gross public borrowing, which could and should be higher – and much higher too.

This is because the other component of government borrowing – the non-cyclical element – that which is committed to investment, has been partially constrained and replaced by private investment, which is much more expensive. Governments can borrow cheaply at very low rates of interest because there is no risk in such lending to the Government. The Government does not go bankrupt so the money markets are very happy to lend cheaply to government because such lending is absolutely secure. There is no logic, therefore, in using private finance for investment in the public sector.

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Neither is government seeking to make profits from public investment, although, of course, if a surplus arises from a public enterprise, this accrues to the public purse and can be spent elsewhere in the public services, assisting the poor or supporting further investment in useful public projects.

Long-term interest rates are now very low, so long-term borrowing is especially cheap and large sums are easily accessible to government from the markets. Substituting private investment for public investment, in PFI projects, for example, costs government, and therefore the taxpayer,

billions over the years, simply because private borrowing is so much more expensive. PFI has a risk premium built-in and profits taken on top of that. The vastly higher revenue payments for such private borrowing still come from the Exchequer and thus from our taxes.

Even then, PFI projects have a high risk of failure, as has been seen already. PFI companies – notably Jarvis – have been in financial difficulties. Indeed, in 2004, Jarvis’ shares slumped and the company was teetering on the brink of bankruptcy putting scores of PFI schemes at risk of collapse. This is why I asked the Prime Minister at Question Time why the Government did not simply let Jarvis go bankrupt, buy-out the PFI contracts from the Receiver at a knock-down price and operate them subsequently in the public sector, saving millions and even billions of pounds of taxpayers’ money in the long term. Funding failed PFI schemes in the public sector would not only be much cheaper but guarantee their future security too.

Using PFI to hold down public borrowing, keeping investment in the public sector off the Government’s balance sheet, is analogous to a home owner seeking to reduce the size of their building society mortgage by buying out a proportion of it with much more expensive borrowing from elsewhere. The end result may look as if one has a smaller mortgage but the total monthly repayments on house purchase borrowings would be higher. Why would anyone do anything so irrational? But that is precisely what government has done by replacing cheap public investment with expensive PFI schemes.

But PFI is even more irrational than that because the resulting capital asset doesn’t even belong to the public sector, so government is paying much more and not even owning the asset. This is rather like our householder choosing not to increase their mortgage to build an extension, but instead to ask a private developer to build and own the extension and then rent it back to the householder at a higher monthly cost than the alternative extended mortgage. Irrational is perhaps understated – potty is more like it.

The Chancellor has made much of the substantial reduction in public borrowing levels since he became Chancellor. Part of this is simply because unemployment has fallen, which we all applaud. The previous Conservative Government had effectively engineered a deep recession in the early 1990s by putting Sterling into the ERM and trying to sustain that policy with massive hikes in interest rates. The ultimate ‘Golden Wednesday’ collapse of the ERM destroyed the credibility of the Conservatives and led directly to Labour’s massive victory in 1997. Economic recovery was well under way by then, driven by the substantial cuts in interest rates after 1992, and the consequent and very large depreciation of Sterling.

However, using this Conservative legacy of high public borrowing arising from the revenue fall-out from ERM to constrain public investment was illogical and damaging. Public investment was desperately needed in health and education in particular after the savage squeeze on public investment during the Thatcher/Major years. PFI – invented by the Tories – was then adopted by New Labour to keep

public investment off the Government’s balance sheet, an irrational obsession for which we are now paying, and which will continue to burden the public purse and future generations of taxpayers for decades.

The truth is that all schemes of privatisation designed to replace public borrowing and investment with private investment are irrational. If proof of this were ever needed, it is surely the privatised railways that now receive several times the subsidy from government that BR received under public ownership. Subsidy per passenger journey has apparently reached some five times what it was in public ownership just over a decade ago, and the cost of laying new railway track has quadrupled. The industry is quite simply corrupt, with the privatisers filling their pockets from government coffers.

The railways are in fragmented chaos, in contrast with the integrated State run systems on the Continent of Europe. The creation of Network Rail and the bringing in-house of railway maintenance were open acknowledgements that privatisation has failed. It is time to bring the whole industry back into public ownership, re-integrate its operations, and finance its investment in the public sector to produce a better and more accountable railway at a fraction of the cost to the public purse and fare paying passengers.

But the heart of the problem remains government’s determination to keep public borrowing for investment needlessly low, and even to squeeze public borrowing for investment to compensate for rising debt on the revenue side – an imbalance between current public spending and tax receipts. Britain’s government gross debt is very low by historic and international standards.

Indeed, government current spending would be lower if government borrowing for public investment had been increased and PFI had never been invented because of the lower returns needed to fund public borrowing. Britain is in serious need of more public investment – especially in infrastructure – and public borrowing is the sensible way, not PFI or any of its privatising ugly sisters.

Across the whole public sector, privatisation, including PFI, costs the Exchequer and therefore all of us billions of pounds each year. The Chancellor wishes to secure his reputation for prudence. To achieve this, he would do well to reverse the process of privatisation, abandon PFI and expand public borrowing for investment once again.

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