

Commentary

B. Delworth Gardner

Leo Eisel and Richard Wheeler (EW) have presented a useful and broad-gauged paper on financing water development projects. Quite appropriately, they have touched on the legal, institutional, and political as well as economic aspects of the developing situation. My consideration of their arguments will be admittedly narrower and unabashedly more partisan, i.e. from a strictly economic point of reference. I have chosen this course, knowing that I will not be quite fair to them, to get many of the more controversial issues squarely before us where they can be debated.

In their opening paragraphs on financing and cost sharing, EW argue that in theory cost sharing and financing are distinct, whereas in practice they are blurred. Then, in the second paragraph, they assert that cost sharing does not rest on an elegant theoretical basis. I have several comments that in general take issue with these assertions.

Yes, there is an important distinction in principle between financing and cost sharing. Financing has to do with who provides the up-front financial resources to get the project built, whereas cost sharing determines who bears the ultimate burden of giving up real resources incorporated in building and managing the project. The reason the distinction becomes blurred is that the federal government often finances the entire project, including, of course, its share of the real resource costs. The share ultimately assumed by the water users and beneficiaries of the project is usually paid at a later time when the government is reimbursed for the share of project costs assigned to the users. It can be argued that this process is economically both efficient and equitable. It is efficient because were it not for

the tremendous financial reserves that are available for project construction to the federal government through taxation and borrowing, projects that meet rigorous benefit-cost tests might never be built. It is equitable, because the project beneficiaries do not reimburse the government until the flow of benefits from the project enhances their income and wealth positions.

It is possible that we accept these arguments without subjecting them to sufficient scrutiny. First, what about the necessity of federal financing? Few, if any, water projects require such enormous up-front financial resources as the Alaskan pipeline, a project financed largely with private sector funds. Many private firms, such as public utilities, finance projects running into the hundreds of millions of dollars. It may not be the size of the projects per se that requires federal financing so much as it is the class of users from whom it may be difficult to collect large sums of up-front money. For example, it could be argued that even if an irrigation project is economically feasible, it may be prohibitively costly—if possible at all—to collect the necessary front-end financial resources from hundreds of farmers, to say nothing of thousands of recreationists or water consumers. Once again, it may be a mistake to jump to this conclusion without some investigation. It is conceivable that lending agencies in the private sector, such as the commercial banks and insurance companies; would be quite willing to lend money on project development that offered potential profits. Projects that are heavily into electric power production obviously could be privately financed if they were economically feasible since so many already are.

My own speculation for why federal financing of water projects exists is quite different from the "size of project" and "capital rationing" issues. There are two basic reasons: (1) many of the proposed projects are not economically feasible and therefore the private market would not generate the funds because losses would ensue and private firms cannot stay in business and make a habit of incurring losses, and (2) some of the outputs from water projects are "collective" goods and thus entrepreneurs in the private market will not have sufficient incentives to invest. I will elaborate

more on this second point below.

It is quite true that the question of economic feasibility is very complex when it is removed from the stratosphere of economic theory and made operational. Quite apart from the collective good issue, there is the question of national goals that EW raise. Their discussion implies that the existence of national interests justifies federal involvement in water development. Is this supposed to mean that private investment does not also further national goals, or that some incompatibility exists between private economic activity and national interests? Does it even suggest that governmental activity is more efficiently directed towards national goals than private activity is? I believe these notions are fundamentally mistaken. We must not forget that the nation is simply the sum of the individuals composing it and that individual interests are the nation's interest. Policies and projects that on balance enhance individual interests are by definition in the national interest. This is really what we mean by economic feasibility of a project—that having it enhances the sum of individual interests and thus the national interest more than not having it.

Perhaps these issues can be more easily analyzed and understood in a different context. What rationale can be given for governmental intervention in financing and bearing the real resource costs of water development? We might begin answering this question by asking another one: if water were expropriable and firm property rights in its use were created so that incentives for private investment in development and use were present, which of North's justifications for federal involvement mentioned by EW would be valid?

I have already indicated why I believe that "national priorities" per se do not justify governmental as opposed to private actions. If the national priority represents a commitment to provide a collective good, however, then a case for governmental action can be made. Collective or public goods are those that are nonrival in consumption (meaning that person A's consumption does not diminish the amount available to person B) and individual consumers are not excludable from the consuming population. A good example is national defense.

