The e-tolling debate: Profit is the root of all evil?

Judging by the reaction and comments on my previous article: [The DA and their roads mess], there are four issues that can be distilled as public perceptions around the topic of e-tolling and tolling in general. The first perception is that any article that seems to support government (or an agency) in any way imaginable is obviously planted and cannot have any merit. Scorn and personal insults are how such articles are dealt with. I would rather not expand on nor explore the political (and deeper) motives that underlie such reaction. The second perception is that due to corruption concerns, any major developments in this country should be halted – irrespective of the economic consequences? That is a point, which I think is worth debating in future. I also find that there is a general lack of understanding around financing of our roads infrastructure and the roles of taxes, the fuel levy and tolling in this. I certainly plan to expand on this in a follow-up. In this article, I want to focus on an argument that often rears its head in political debate around service delivery in general. This argument focuses on the undesirability of the profit motive when it comes to rendering government services to the public.

In my previous article, I expressed the irony that (when it comes to toll roads) the ANC government is pursuing a policy that is in direct conflict with its alliance partners: the Communist Party and Cosatu, whereas the DA is rejecting this policy although it is directly in-line with the general principles of capitalism. This irony seems to have escaped many readers. I say this as many of the comments and expressions made against tolling touched on the issue of profit – and specifically the undesirability of profit. This is an argument that has often been expressed in the ranks of the ANC, is vociferously voiced by Cosatu and lately also by the EFF. The argument goes something like this: *when rendering services to the public, government should not be making a profit – this is especially true in the case of basic services rendered to the poor. Due to the fact that any profit is undesirable this also means that these services cannot/should not be privatised, offered via public private partnerships, or even outsourced to the private sector as that would imply a profit is made*. Judging from the comments to my article last week, this argument is also embraced by many a DA supporter.

But, is it correct to say that in rendering services to the public government should not make a profit? Is profit really such an undesirable element when it comes to infrastructure and rendering services to the public through it? Let us start to analyse this by asking the question: what is profit? Few readers would hesitate to answer that profit is income less expenditure. Thus, an entrepreneur offering a good in the market sets the price for that good and depending on the volume sold and the expenses incurred, either makes a profit or a loss. Simple stuff. The simplicity can easily lead one to believe that setting the price is a rather arbitrary exercise. But it is not and to understand this we can look at profit from a different angle. This angle is called: *pricing for risk*. It is this definition of profit that is highly relevant to government in rendering services to the public.

Let's analyse this further through an example of a typical service rendered by government: our potable water supply. In rendering this service, government takes a number of significant risks. It has to invest extensively in infrastructure to meet the projected demand. But what if the demand is significantly different to its projections? In setting the price, it has to take a view on what its expenses will be. But what happens if some of its expenses rise more rapidly than what was projected? It also has to recover payments directly from the consumers – in this it takes significant credit risk as to each consumer's ability and willingness to pay. The notion of *pricing for risk* dictates that in setting the price, a specific contribution to each of these risks must be included in the price. This means that if any one (or more) of these risks manifests over a period of time, the business will be able to absorb the change to the extent the pricing, in respect of that risk, was correct. This is the basis of sustainability: no business can be operated sustainably without the appropriate *pricing for risk*.

Pricing for risk and its impact on sustainability is a fundamental principle. But, I want to focus on another aspect of *pricing for risk* - it directly implies that the price for a service should not differ depending on who offers that service (i.e. government or the private sector) as the *pricing for risk* must surely be the same. The only factors that could lead to a different price are: (i) if one of the parties gets the *pricing for risk* significantly wrong or (ii) if one party can operate more efficiently than the other. In many instances (not always!) I believe the private sector can do better on both these counts and therefor the general public would end up paying less for the relevant service. I certainly hold this view when it comes to toll roads.

There is one further aspect of *pricing for risk* from the example above that we need to discuss. What happens if none of the risks so priced manifest over a period of time? In that case the business will generate a profit. A suitable profit over a period of time is the ultimate test that the business is operating sustainably. In the private sector, a portion of this profit is paid to shareholders as a reward for carrying the risk over the relevant period of time. The balance of the profit is typically reinvested in the business – often in an attempt to reduce exposure to these very risks. If government renders the service, what does it do with this profit? It also applies a portion of the profit to reward the shareholders (the consumers in this case) as a reward for carrying (and paying for) the risk over the relevant period of time. How does government reward consumers? In a number of ways, ranging from reducing (in real terms) the price of the service, improving the service while keeping the price constant (in real terms) or even reducing taxes. Government will also invest a portion of the profit to reduce exposure to the risks. A good example is subsidies to the poor. Ultimately, government will invest the balance of the profit to render other services that are essential but not always income generating – such as public libraries.

Given all of this, there is an argument around the e-tolling technology that also surfaces on a regular basis (and in last week's comments) that must be busted. This argument is the notion that as the operator of the e-tolling system is now wholly foreign owned, e-tolling is simply a way to enrich these foreigners. What utter nonsense! As long as the price paid to the service provider for the service(s) rendered is based on value for money and performance there should be no issue as to where the shareholders are based and it should not influence the pricing. I wonder where the majority of shareholders in BMW and Daimler Benz that rake in major annual profits from their South African vehicle sales reside? Enough said.

Along the same trend one finds the argument that (minibus) taxis do not constitute public transport as they involve a definite profit motif of the owner and/or driver. Clearly such arguments are incorrect and are simple arguments of convenience.

To conclude: profitability of any operation rendering a service to the public is not the root of all evil. Rather, it is the vital sign of life and survival. If your resistance to tolling (and especially privately operated tolling) of key roads and routes in this country is based on the undesirability of the profit motive, then you need to rethink.