

JOBS – PART IV: THE PROBLEM WITH INFRASTRUCTURE “STYLE” SPENDING – AND OTHER BAD IDEAS!

Stephen L. Bakke  September 29, 2011

Dear Mr. President: In my last note to you I “hinted” that I thought your magical all-purpose combined jobs/energy/environmental program was a bunch of “hooey!” I understand you didn’t like that – Sorry! Then I started thinkin’, and realized you also decided, in your infinite wisdom, to superimpose an “infrastructure evaluation system” on the decision making and underwriting process for green jobs investments! And what resulted? – An accident waiting to happen! Once again, as we Norwegians say: “UFF DA!” – Steve Bakke – September 29, 2011.

The Size of the Governmental Program and the Level of Risk Are Inversely Proportionate to “Smart” Altruism

I fully understand we can’t expect success on all stimulus or jobs programs. Success can’t be certain and sometimes results don’t reflect the most objective expectations. But I see a pattern that indicates the government should stay out of the venture capital business. Bureaucrats and politicians should not be expected to think like venture capitalists – simply by virtue of training and experience. Consider the following two “mind-sets” for evaluating speculative or sizable transactions:

- I understand there is a good chance this may not work, but I think we should do this because it represents a sincere effort to advance an important technology I believe in. This sort of project is just what is needed as a wonderful example of what the future can hold.
- VS
- I understand there is a good chance this may not work, but we have done our homework, tested assumptions, evaluated the technology, and estimated the risk. We have a realistic chance to get my money, and the investors’ money, back – along with a handsome return.

While I can’t read minds, I believe those attitudes are realistic. One is a “best intentions” attitude, while the other is a “best results” attitude. Which do you think represents the attitude most likely to be the wisest with a real feel for the risk/reward relationship? Which do you think is the attitude most often found in private sector venture capitalists?

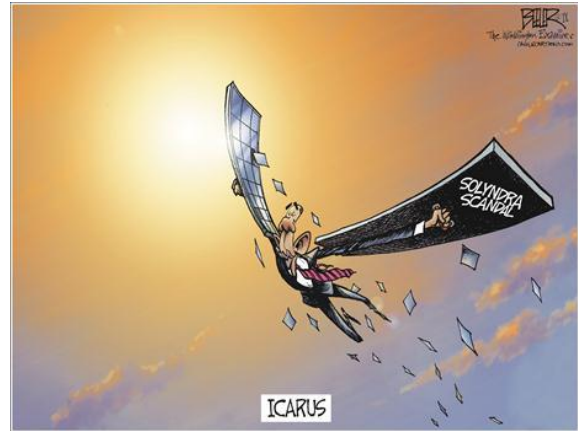
Take One Part Foolish Premise, Add Two Parts Infrastructure Bureaucracy – And What Have You Got? An Incredible Mess! (Spelled S-O-L-Y-N-D-R-A)

The following are important considerations related to infrastructure jobs spending:

- When the government, in a jobs program, substitutes their bureaucratic wisdom for that of the marketplace, I am convinced that they often fund jobs that would have been there anyway, or propping up struggling companies that otherwise shouldn’t survive.
- My sense is very strong that very few firms will, on the margin, survive that wouldn’t have survived on their own with the marketplace dictating results.
- Why don’t many governmental loans guarantees work? Because, like all other subsidies, they divert capital from worthy investment and create a climate of uncertainty in a market weary of government manipulation.

- Why focus on Solyndra? Because it was a huge failure; its financial condition was glaringly apparent before the government made their decision; and it's turning out to be a potential major scandal – deservedly so!

Solyndra is just one example of situations in which the recipients of “green jobs” subsidies may have been better off had they not received government dollars. In the case of Solyndra, I believe it likely that the **government’s foolish and naïve generosity made the situation worse**. Remember that their subsidy was a mortgage loan guarantee for a large, palatial new headquarters.



The bureaucracy apparently didn't/doesn't consider the following:

- My experience with financing struggling and “start-up” companies is that “bricks and mortar” can be a disastrous distraction and waste of funds if done before the company is able to “cash flow” operations.
- Internal emails now indicate the administration was alerted to the true financial condition of Solyndra. And other emails seem to clearly indicate political pressure to speed up the approval. You can check this out if you wish.
- Solyndra received a very negative financial audit report just prior to the initial approval of the government guarantee. PriceWaterhouseCoopers stated that this “raises substantial doubt about its ability to continue as a going concern.”
- Solyndra had not, and could not, internally provide the cash flow necessary to fund normal operations – and then after receiving the loan guarantee for the lavish quarters, they were faced with huge new debt service requirements (aka mortgage payments).
- Solyndra should have used any available dollars (from government or otherwise) for more modest space, leaving more for their normal operations.
- It is now known that as soon as Solyndra defaulted on the loan payments, internal government emails indicate the possibility of “cutting their losses” by preventing any further “draw-downs” on the federal guarantee. The government permitted it anyway. Was the “centerpiece nature” of this project, from a political standpoint, too large to allow to fail?
- Isn't the bottom line obvious? Consider the fact that Solyndra's business model reflects their costs to be about \$4 per watt of power it produced. Consider the fact that Solyndra's business model has been described to be “like planning to sell for \$2 something that costs \$4 to produce.”

Inherently flawed are the “pipe dreams” that keep fantasies in business. Other green energy projects continue to indicate that they can't exist WITH OR WITHOUT government subsidies. The government should have known these things! If the decision makers aren't aware of this, they have

no business being in the venture capital business. And was “politics” a factor? The administration and those doing their bidding are obviously not worthy venture capitalists. It seems quite clear, they are mainly in the business of politics and elections.

Other Infrastructure or Green Jobs Programs

Without passing judgment on their merits, here are some other unsuccessful stories:

- Evergreen Solar in Massachusetts – filed for bankruptcy in August.
- SpectraWatt – filed for bankruptcy in August.
- My research turned up a number of other examples of recent “green jobs” bankruptcies.
- In one federal funds set-aside (the one that gave us Solyndra), the original \$38.6 billion budget still has approximately \$19 billion unspent. The stated intent for this program was to advance “green technology” and create an original estimate of 65,000 jobs. So far, a total of approximately 3,500 jobs have been generated. That’s about \$5 million per job created!
- BrightSource Energy – received a 1.6 billion loan guarantee from the government – lots of temporary construction jobs (700) – but only 86 permanent jobs.
- Yuma Desalting Plant in Arizona – built by the federal Bureau of Reclamation at a taxpayer cost of \$245 million. Whoops – in 1993 it was decided it wasn’t needed. It’s been idle for two decades at a \$6 million annual taxpayer cost.
- Johnson Controls – the current administration advanced \$300 million taxpayer dollars as part of a stimulus grant so the company could make high-tech batteries. Only 150 jobs have been created so far.
- Weatherization Assistance Program in Texas – the current administration gave \$327 million in stimulus money to the program and only approximately 1,000 jobs were created and saved – that’s actually better than many examples.
- Weatherization program in Seattle - \$20 million cost – 14 jobs.

My point is that these are consistently sold as a solution to all ills – energy, environment and jobs. They just aren’t successful for creating jobs, no matter how hard you may wish otherwise!

Is Anything in the Works? Lots!

The program which gave us Solyndra is not yet fully spent and the administration is rushing to get the dollars “out the door” before the program expires at the end of September. For example, just this week, the Energy Department approved two loan guarantees worth more than \$1 billion for solar energy projects in Nevada and Arizona in order to beat the deadline. Check them out – the companies are for Tonopah Solar Energy and Mesquite Solar 1 in Tonopah, Nevada and Phoenix, Arizona. I have no idea as to their viability, but interestingly, the smaller of the two projects is scheduled to receive over twice as much as the larger project. HMMMMMMMM? Risk/reward?

I have a list of the larger DOE green energy guarantee projects under consideration. These appear to include mostly solar related, with some wind power, and one biomass power example. In the interest of not putting you to sleep, permit me to just summarize some statistics:

- 9 proposals totaling approximately \$6.5 billion in cost.
- 3,650 temporary construction jobs will be involved.
- 283 permanent jobs will be added.
- if all temporary and permanent jobs are considered, this would represent an expenditure of \$1,652,174 per job – that’s high.

- **If we look at just the permanent jobs, the total expenditure per job becomes almost \$23 million – you just can't make this stuff up!**

And Guess What! A Czar for This and a Czar for That!

And now, the Obama administration is working on creating another “government corporation” – don't forget the success of “Fannie and Freddie.” This is to be the “American Infrastructure Financing Authority” (AIFA) to “provide direct loans and loan guarantees to facilitate investment in economically viable infrastructure projects of regional or national significance.” This would require a new bureaucracy including a “Chief Lending Officer” in charge of “all functions of AIFA relating to the development of project pipeline, financial structuring of projects, selection of infrastructure projects.....the creation and management of a Center for Excellence to provide technical assistance to public sector borrowers in the development and financing of infrastructure projects.....an Office of Rural Assistance to provide technical assistance in the development and financing of rural infrastructure projects.” Billions and billions and billions.....and billions!

Also, a new “czar” is being created to oversee the above functions as well as existing federal infrastructure funding. What happened to cabinet officers? Obama avoids accountability once again.

This ol' Norwegian just says **UFF DA!**