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International best practice takes root in Europe

The first privatisation of a former Soviet railway sees the Baltic Rail Services Consortium bringing international experience and best practice to Estonia. Investment and management changes are transforming the outlook for Estonian Railways' transit freight business

BIG-TIME RAILROADING has long been the name of the game in Estonia, but privatisation and competition promise to make it more efficient. On August 31 2001 Baltic Rail Services closed a deal to take over Estonian Railways (Eesti Raudtee, EVR), a tiny part of the former Soviet rail network that once extended over 145 000 route-km. It was a strategic and significant move, for this is the first vertically-integrated privatisation of a national railway in Europe.

In their heyday the railways of the former Soviet Union handled around half the world's rail freight traffic. Despite the economic collapse affecting the region, rail continues to enjoy a market share estimated at around 80%. This means that about 25% of the planet's rail traffic can still be found on the 1 520 mm gauge.

EVR has benefited from its location on an ice-free zone of the Baltic Sea close to major sources of Russian oil.



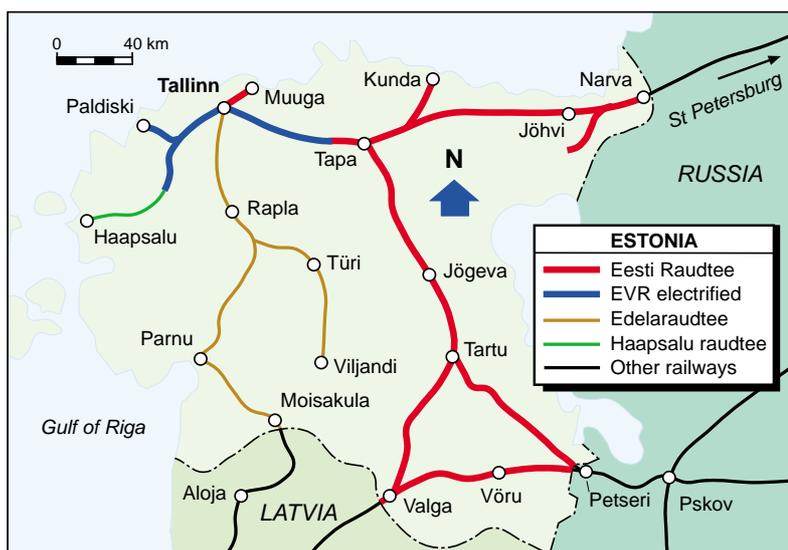
Recent growth in the Russian oil trade has offset the decline of smoke-stack industry, and EVR now enjoys traffic levels almost equivalent to those handled in Soviet times.

Like its railway, Estonia is a small country and one of its main businesses is transit traffic, for the most part moving from Russian origins to the Baltic for movement beyond by sea. Significant investment has been made

in the Tallinn area, especially at the new Muuga port, to handle the transit business. Virtually all of this moves by rail; EVR's main competitors are not lorries, but rival railways moving goods to and from competing ports in Russia, Latvia and Lithuania. The intensely competitive nature of this business, and its importance to the Estonian economy, was a major reason why the government of Estonia decided to privatise EVR.

Two former Soviet diesel locos head a westbound oil train at Tapa

All photos: Railroad Development Corp



The sale process Beginning in 1999, a privatisation structure was put together with the help of international consultants. There were four key characteristics:

- Sale of stock, as opposed to sale or concessioning of the assets;
- A vertically-integrated structure, with no requirement to operate passenger services;
- Government retention of one-third of the stock, with an option to sell it to the buyer of the other two-thirds;
- Open access for passenger and freight operators, at a price allowing EVR to make a profit.

This led to three bids being submitted at the end of 2000.

A US-based group, which claimed to include a succession of North American Class I railways, each, in turn denying involvement, presented the highest bid. This charade constituted a national scandal which continued for around six months.

In the end the government terminated discussions and offered the

Left: The first of 74 C36-7 diesel locos previously used in the USA will be shipped to Estonia in April

Drawing: GE Transportation Systems

* Ed Burkhardt (right of photo) is President of Rail World Inc and Chairman of the Supervisory Boards of Eesti Raudtee and Baltic Rail Services. Henry Posner III is Chairman of Railroad Development Corp and Iowa Interstate Railroad and a board member of Estonian Railways



Above and right: An open access Link Oil train arrives at Narva yard in November 2001

Eight-axle tank wagons are used to convey export oil traffic from Russia to Estonian ports and refineries

EVR's principal locomotive maintenance works is located at the key junction of Tapa



transaction to the second highest bidder, Baltic Rail Services. BRS accepted the offer, and the deal was closed on August 31 2001, in cash and at BRS' original offering price of 1 billion kroons (US\$57m) for the two-thirds interest offered, to the relief of all concerned.

BRS' shareholding breaks down along strategic lines and consists of US operators Rail World Inc and Railroad Development Corp, UK infrastructure company Jarvis plc, and Estonian investor group Ganiger Invest. At the end of 2001 the BRS group was expanded to include the AIG Emerging Europe Infrastructure Fund.

EVR today
In terms of its structure, EVR most closely resembles a North American railway. It is a vertically-integrated

freight railway that provides access to suburban passenger operator Elektri-raudtee, inter-city passenger operator Edelaraudtee and international passenger operator EVR Ekspress, which is 49% owned by EVR.

There are also certain European characteristics, such as the presence of a significant open access freight operator, Link Oil, based in St Petersburg. Make no mistake, however – this may be a European railway, but it is a railway that goes to Moscow, not Brussels.

Freight operations bear a strong resemblance to North American practice. Block trains predominate, primarily export oil products, and these make up around 50% of EVR's tonnage, including traffic handled by Link Oil. This is supplemented by export fertiliser and domestic oil shale movements for the power generation industry.

There is also significant wagonload traffic such as timber and cement for export. EVR hauls around 40 million

tonnes a year, which by US standards would rank it at the top of the Class II railways or a small Class I. EVR's 695 km of main lines consist of a mixture of double and single track, some controlled by CTC.



Future prospects

EVR's future prospects and those of Estonia's ports are inextricably linked. The company's first objective is continuous improvement in its already-good safety record, and the second is to protect and expand Estonia's role in the Russian transit business. This is being accomplished through more intensive use of assets and a programme of selective investments in capacity, namely in locomotives and infrastructure.

With regard to locomotives, the similarity between Soviet and North

La pratique internationale s'implante en Europe

La première privatisation d'une partie de l'ancien réseau soviétique a vu le Baltic Rail Services Consortium apporter en Estonie l'expérience et la pratique internationale. Les investissements dans le renouvellement du parc de locomotives ainsi que dans l'amélioration de l'infrastructure sont en voie de transformer la physionomie de l'activité fret en transit de l'Estonie, avec une réaction positive des clients et des marchés financiers. Les Chemins de fer estoniens restent propriétaires de l'infrastructure ferroviaire, mais la concurrence vient d'un opérateur arrivé avec la libéralisation, ainsi que des ports des pays voisins

Internationale Praktiken fassen Fuss in Europa

Die erste Privatisierung eines Teils des früheren sowjetischen Netzes hat zur Folge, dass mit dem Baltic Rail Services-Konsortium internationale Erfahrungen und Praktiken nach Estland kommen. Investitionen in Ersatz von Lokomotiven und Infrastrukturverbesserungen verändern die Aussichten für das estnische Transitgütergeschäft unter dem Wohlwollen von Kunden und Finanzmärkten. Die Estnischen Eisenbahnen verbleiben Besitzer der Bahn-Infrastruktur, aber die Konkurrenz entsteht durch einem Open-Access-Betreiber sowie von den Häfen in den Nachbarländern

Las prácticas internacionales echan raíces en Europa

La primera privatización de parte de la antigua red ferroviaria soviética ha visto como el Baltic Rail Services Consortium ha aportado las experiencias y las prácticas internacionales a Estonia. Las inversiones en nuevas locomotoras y la modernización de las infraestructuras ferroviarias están transformando las perspectivas del transporte de cargas en tránsito por Estonia, y los clientes y mercados financieros están respondiendo favorablemente. Los ferrocarriles estonios siguen siendo los propietarios de las infraestructuras ferroviarias, pero la competencia se consigue con la presencia de un operador de libre acceso y gracias a los puertos de los países vecinos



American practice allows the introduction of used locomotives from North America. We have chosen a fleet of GE-built C36-7s that are being re-gauged and equipped with Russian-style couplers and cab signalling. The aim is to replace completely EVR's existing Russian and Ukrainian-built locomotive fleet with C36-7s. The first of 74 units will reach Estonia in April, and deliveries will continue through the rest of the year.

This also represents a significant initiative for GE, as successful introduction of its locos in Estonia is expected to open doors in other countries in the former Soviet region.

Upgrading the infrastructure Infrastructure investment is focused on improving capacity, particularly on single-track segments reaching the Russian border. Passing loops will be lengthened on the principal main line between the connection to the October Railway at Narva and the start of double track at Tapa. At a later stage, improvements will also be made to the Tapa - Petseri route. Extensive resignalling will be required across the network, with replacement of obsolete Russian equipment and widespread installation of CTC planned.

Equally critical to the investment programme are changes in operating practices that will make better use of assets and create additional capacity without additional investment. These range from the operation of longer trains to the reduction of intermediate shunting between arrival at the border and delivery at the port. Use of hump yards is being reviewed with an eye towards streamlining marshalling processes. At the same time we aim to develop additional wagonload traffic that will justify continued use of some of the yards.

To permit operation of the heavier US locomotives, EVR is raising its maximum axleload from 23 to 31 tonnes. Bridges and rail conditions have been carefully evaluated, and only minor work will be required to

accommodate this change. Were the railway not vertically integrated, it is doubtful if the axleload issue would have been dealt with successfully.

Management plans include the establishment of a single customer service centre and the concurrent elimination of many manned stations in the field. EVR has worked with the trade unions and government to establish an enhanced redundancy plan to cushion the effect on the labour force. Around 4 200 people were employed at privatisation, and this total is projected to decrease steadily as the effects of capital investment and management initiatives work through.

The partners in BRS intend to operate EVR as a stand-alone Estonian business with its own management. However, the investors will provide active oversight as the company's operations are restructured in accordance with international best practice.

Edward A Burkhardt of Rail World Inc is Chairman of the Supervisory Boards of both BRS and EVR, and Guido Sammelselg, the leader of the

Estonian investor group, is Deputy Chairman. Burkhardt was the founder of Wisconsin Central Transportation Co in the USA, and served as the first Chairman & CEO of English Welsh & Scottish Railway in the UK. Board member Henry Posner also has extensive experience in managing international railway operations, serving as Chairman of both Iowa Interstate Railroad and Ferrovías Guatemala. Jarvis, the integrated services provider, is represented on the board by Andrew Smith.

Currently, a search is underway to fill the position of Managing Director. In the meantime, Earl J Currie and Mark A Rosner of Rail World Inc have been appointed acting Managing Director and Deputy Managing Director respectively, and Jarvis manager David Douglas is Infrastructure Director.

We are gratified by the initial market response, both from freight customers and the financial markets, and we look forward to the steady evolutionary change planned for the company and the region. ■

Left: A domestic inter-city passenger train run by Edelaraudtee stands at Varga

Above: An EVR Ekspress international train arrives at Tallinn, where commuter trains are operated by Elektriraudtee



Above: Kopli yard serves the port of Tallinn. Left: CTC dispatcher at Tallinn. Right: Retarder operator at Muuga yard. BRS envisages that EVR will be able to harness the expertise of its local staff

