Direct Investment in Rail in Africa—A Private Sector Perspective

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AGENDA

- Background on RDC
- Case Study: Nacala Corridor
- Industry Structural Trends
- Conclusions

Background on RDC

- **Pittsburgh-based, privately held railway investment and management company**
- **Focus: Emerging Corridors in Emerging Markets**
- **Financial structure based on <u>Joint Ventures</u>**

Background on RDC (cont.)

Country	Entity	Length Km	(Miles)	Employees	Tons Y. 2009 (in millions)
CURRENT:					
USA	Iowa Interstate	954	(592)	206	11.7
Argentina	ALL Central	5,690	(3,535)	1,200	2.3
Argentina	ALL Mesopotamica	2,704	(1,680)	300	1.0
Guatemala	Ferrovias Guatemala	322	(200)	13	N/A
Peru	Ferrocarril Central Andino	535	(332)	431	1.8
PAST:					**Tons Last Yr of Investment**
Malawi	Central East African Railways	797	(495)	417	0.22 (2008)
Mozambique	Nacala Corridor	873	(542)	404 Rail 209 Port	0.2 Rail (2008) 0.9 Port (2008)
Estonia	Eesti Raudtee	693	(431)	2,345	44.4 (2006)

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The Fundamentals of the World's Freight Railways on One Page

		USA	Europe	Latin America	Africa
REVENUE:	▪ Competition	Other RR	Other RR	Truck	Truck
	▪ Market Share	Mature	Mature	Low	Medium
	▪ Traffic Base	Mature	Mature	Expanding	Reviving
COSTS:	▪ Infrastructure	Good	Excellent	Fair	Fair
	▪ Rolling Stock	Good	Excellent	Poor	Fair
	▪ Staffing	Low	High	High	High
	▪ Railway Capital Markets	Mature	Emerging	Emerging	Minimal

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Case Study: Nacala Corridor

- **First private sector integration of Ports & Railways**

Traffic Base

- Highly diversified — carload freight, LCL freight, passengers
- Main imports — fuel, cooking oil, fertilizer, food
- Main exports — tobacco, food

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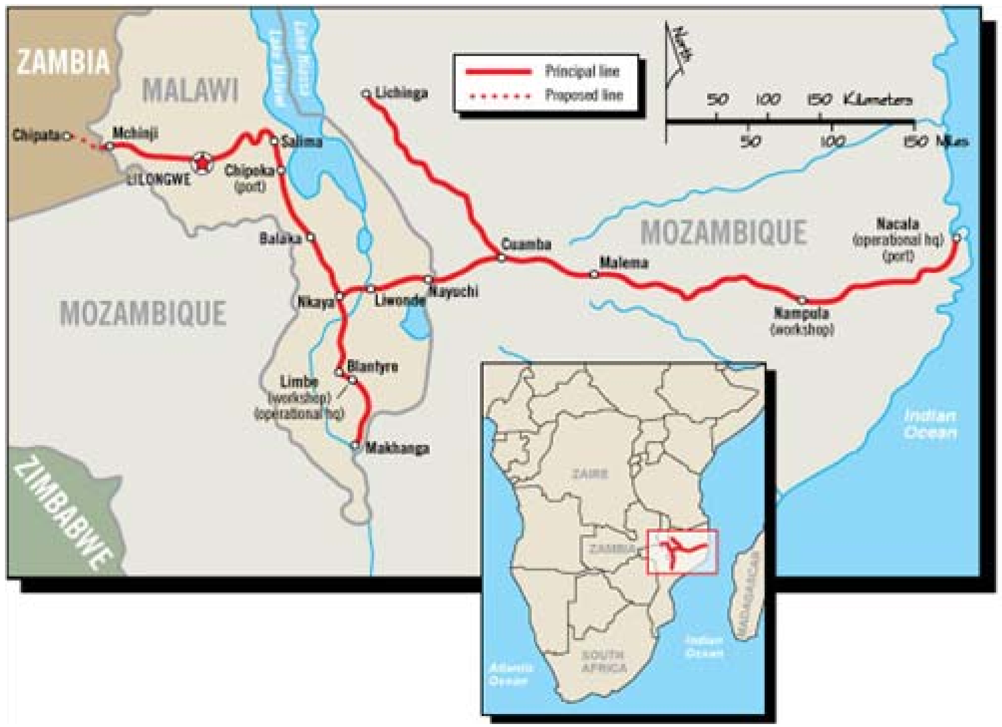
RDC Role: Operator, Investor

- **Begun 1996, with ERL**
- **Malawi concessioned 1999, but with incomplete financing**
- **Cyclone damage in 2003 fixed in 2005 due to incomplete financing**



- **Mozambique operational start-up January 2005**
- **RDC, ERL interests sold to local investors September 2008**

Financing

- Financed between 1999 (Malawi—100% equity)…
- … and 2005 (Mozambique—OPIC debt)
- Equity—25%; debt—75% (plus donor support for famine relief)
- No renegotiation of terms with governments

Financing (cont.)

- **MILLENIUM CHALLENGE**
  - **Project ineligible for financing – “not sponsored by public sector”**
  - ***After*** **sale of RDC shares, Malawi has applied for funding!**
- **WORLD BANK**
  - **Nacala competes with Sena Line, generating conflict with World Bank & CFM (public sector shareholder)**
  - **World Bank funding of Sena Line based on faulty due diligence**
  - **World Bank funding of consultant study to discredit Nacala Corridor**

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Stakeholder Relationships

- Ongoing efforts by public sector to discredit privatization at the local level
  - "Failure to fully staff all stations"
  - "Failure to rehabilitate 77 km"
  - "Failure to provide service on light density lines"
  - "Failure to purchase locomotives with the correct gauge"

“Locomotives with Incorrect Gauge”

Gauge – Convertible U6Bs Loading in Panama for Mozambique

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The Nacala Corridor in Context

	GUATEMALA	NACALA CORRIDOR	ESTONIA
TONS 2004	157,000	300,000 Rail	42,000,000
LINES OF BUSINESS	Atlantic – Containers, Steel, Sugar Pacific – ? Electricity rights-of-way, etc. – ?	Port & Rail	Oil, Fertilizer, Metals
PURCHASE PRICE	$0 + 10% of Revenue	$7 million + $2 million/year + 5% of Revenue	$60 million for 66%
INITIAL FINANCING	RDC Local Capital Markets	SDCN OPIC CFM	Strategic Investors Int'l Capital Markets IFC

The Nacala Corridor in Context (cont.)

Risk vs. Reward

	Anticipated Risk	Actual Risk	Mitigation	Reward
ESTONIA	Traffic	Expropriation	Privatization Agreement	Sale
GUATEMALA	Traffic, Financing	Expropriation	CAFTA	Arbitration
NACALA	Traffic, Financing	Traffic, Financing	Capital Markets	Sale
USA	Traffic	Threat of Expropriation (re-regulation)	Capital Markets	Value Growth

(NOTE: Public Sector = Primary Source of Risk!)

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Industry Structural Trends in Africa

Positive

Revenue:	**African RR's compete with trucks, not other RR's, therefore margins higher.**
	African RR's have growing economies, market share upside.
Costs:	**African RR cost structure presents much room for improvement.**
General:	**African RR's are potentially as profitable as similar railways in USA.**

Industry Structural Trends in Africa (cont.)

Negative

Revenue: Revenue Risk due to lack of meaningful historic trends.

Costs: Lack of local experience for debt financing.

General: Logistical and Cultural gaps make opportunities difficult to identify and pursue.

Competition in Africa is often public sector railways, such as Transnet (South Africa).

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Industry Structural Trends in Africa (cont.)

Aid Programs

CONCLUSIONS
(Macro)

- **Rail is a viable private sector business…as confirmed by value-driven expropriations!**
- **Shareholder Structure is best form of risk mitigation, not Business Plans**
- **Rule of Law is a secondary defense and more important than Privatization Agreements**

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CONCLUSIONS
(<u>Specific to Africa</u>)

- **Public sector aid programs in past competed with private sector potential**

- **Today's competition is primarily between public sector investors & private sector investors (but aid programs still represent competition)**

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A Luta Continua!

- Vision, experience and commitment are not enough.
- Financial capacity is NOT the constraint.
- The public sector and multi-laterals need to be Part of the Solution, not the Problem.

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