ATF2015

AfDB TRANSPORT FORUM

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PPP and Risk Mitigation:
Lessons Learnt from RVR

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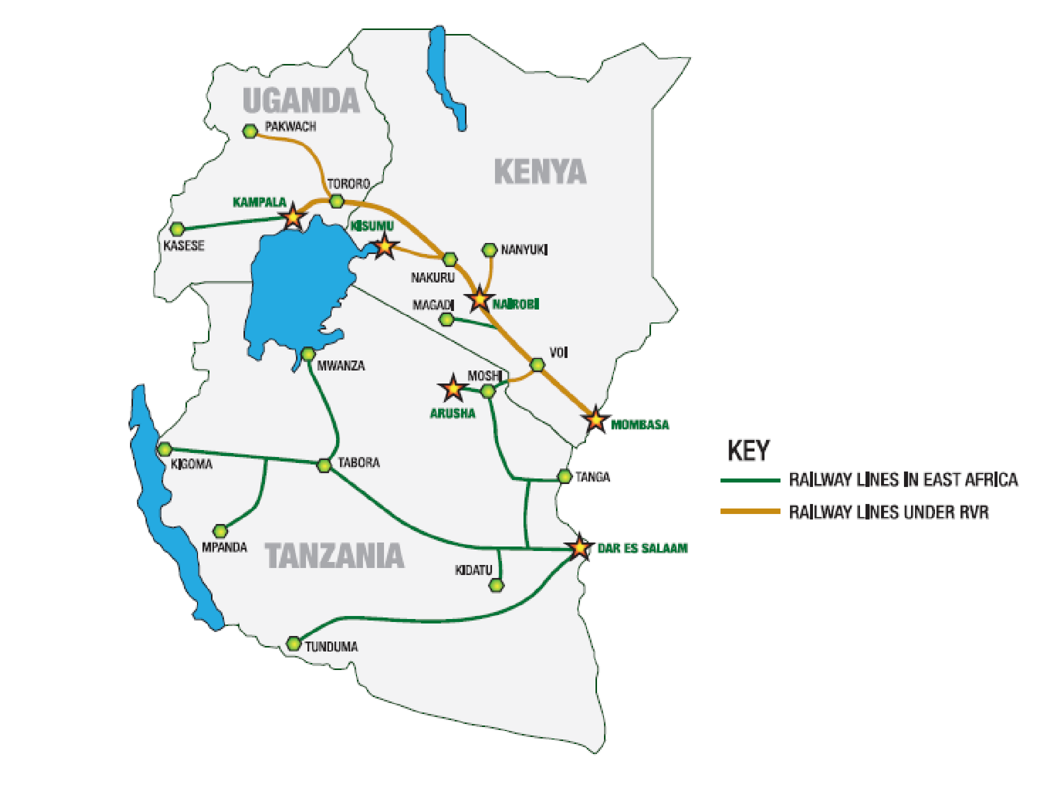
TABLE OF CONTENT

KRC & URC Railway Systems



- **Total length of network:**
  - ✓ Kenya: 2,210 km
  - ✓ Uganda: 1,241 km
  - ✓ Total: 3,451 km
- **Total length of concessioned network:**
  - ✓ Kenya: 1,920 km
  - ✓ Uganda: 431 km
  - ✓ Total: 2,351 km
- **Opening of Financial Proposals: 2005**
- **Preferred bidder: Sheltam Railway Company Ltd.**
- **Concessions signed in January 2006 – effective in April 2006 (Commercial Close)**
- **Financial Close reached on 31 October 2006**

Pre-Concession Performance

	Kenya Railways Corporation (KRC)	Uganda Railways Corporation (URC)
Total length of network (km)	2,210	1,241
Total freight volume (million tonnes/yr)	2.3	0.9
Main commodities	Containers, soda ash & wheat	Containers, wheat & fuel.
Revenues (US$ million/yr)	53	19.5
Number of wagons	6,000	1,433
Number of locomotives	175	44
% wagon in operation	41	89
% of locomotive in operation	20	73

PPP Project Identification & Selection

- Kenya
  - ✓ Concessioning of KRC undertaken as part of the Public Enterprises Reform Programme.
  - ✓ In 2000, the Government approved concessioning of KRC
  - ✓ In 2002 IFC Advisory Services engaged as TA.
- Uganda
  - ✓ In 1999 URC identified as a candidate for privatisation
  - ✓ Management contract followed by a concession (20 – 30 years)
  - ✓ Cabinet approved direct concessioning in 2001
  - ✓ In 2002 Canarail engaged as TA
  - ✓ Key challenge: entirely dependent on Kenya rail network
- MoU for Joint Concession in 2004
  - ✓ To avoid Malawi/Mozambique experience

Key Objectives

- Enhancing the role of the private sector in the economy.
- Reducing the demand of the Public Enterprises on the Exchequer so as to improve the use of scarce resources.
- Reduce the role and rationalise the operations of public enterprises.
- Improve the regulatory environment.
- Broaden the base of ownership and enhance the development of capital markets.

PPP Feasibility Analysis

- Need for new long-term investment - $300 million
- Double freight traffic in the first 5 years to 6 million tonnes/yr.
- Reduce railway transport costs by US$20 – 30 million/yr.
- Concessionaire's revenue to increase to US$200 million/yr. in Yr. 5 with a project of US$250 million/yr. in Yr. 25.
- Reduce deterioration of roads and reduce road maintenance by US$10 – 20 million/yr.
- Other benefits: reduced congestion and pollution, improved safety and lower energy consumption.

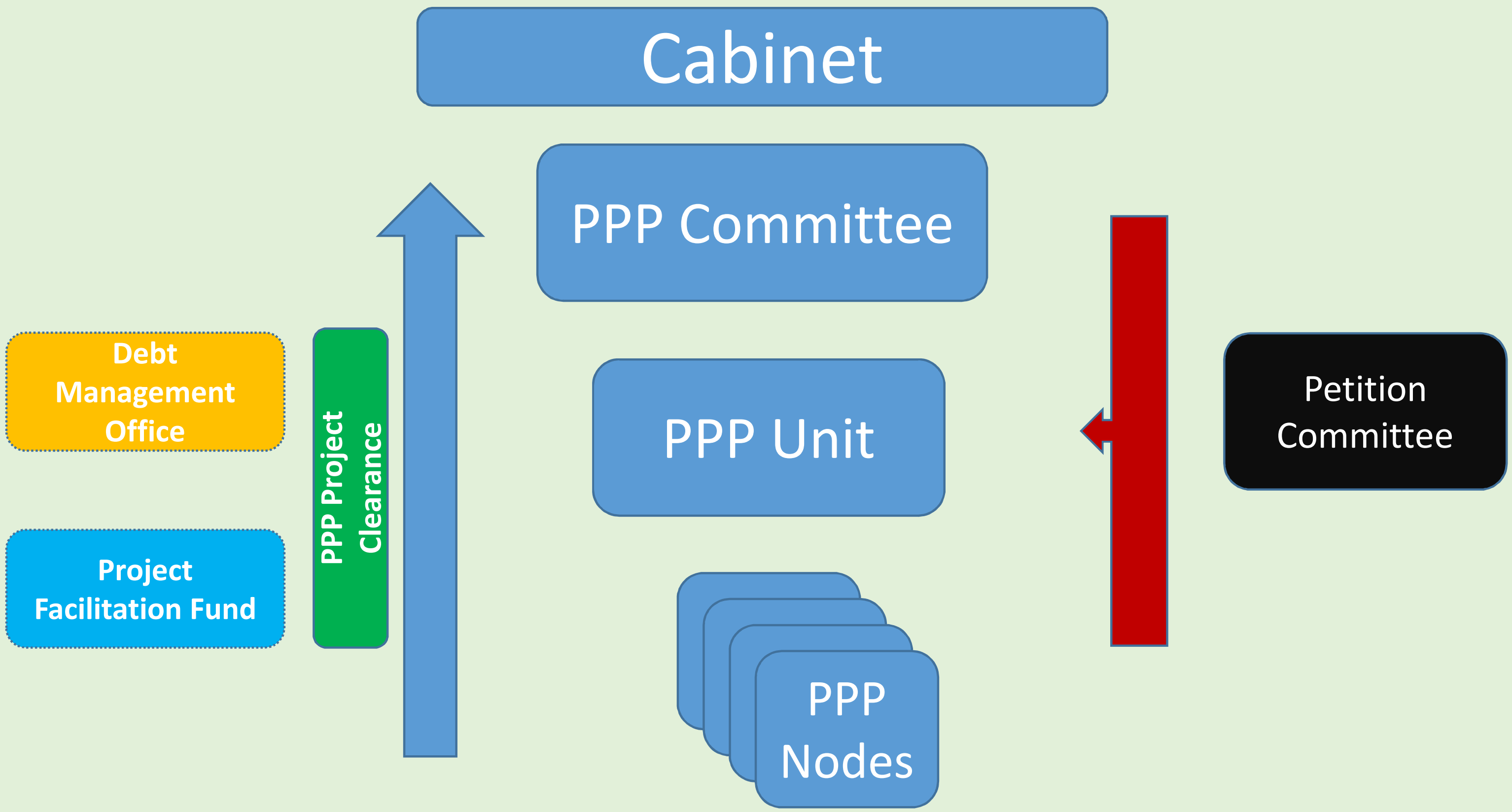
Governance Standards for PPPs

- **UN definition**—"...the processes in government actions and how things are to be done and not just what is done"
- **Efficiency**—using resources without waste delay or corruption and without burdening future generations
- **Transparency**—clarity and openness is decision-making
- **Decency**—development of rules without harming people or the environment
- **Participation** of all stakeholders
- **A PPP framework** to ensure that the governance standards are applied in the implementation of the project

Kenya Legal and Regulatory Framework

- Government of Kenya, Policy Statement on PPPs, November 2011.
- Public Private Partnership Act, 2013.
- Public Private Partnership Regulations, 2014.
- Public Private Partnership (Petition) Regulations (Draft), 2014.
- County Government Regulations (Draft), 2014.
- The Public Finance Management (Road Annuity Fund) Regulation (Draft), 2014.
- Public Private Partnership (Project Facilitation Fund) Regulations, 2015.
- Guidelines for the Assessment and Management of Fiscal Commitments and Contingent Liabilities (FCCL) in Public-Private Partnership (PPP) in Kenya and FCCL Technical Guidance Manual, August 2015
- Kenya Public Private Partnership Manual (still under preparation)

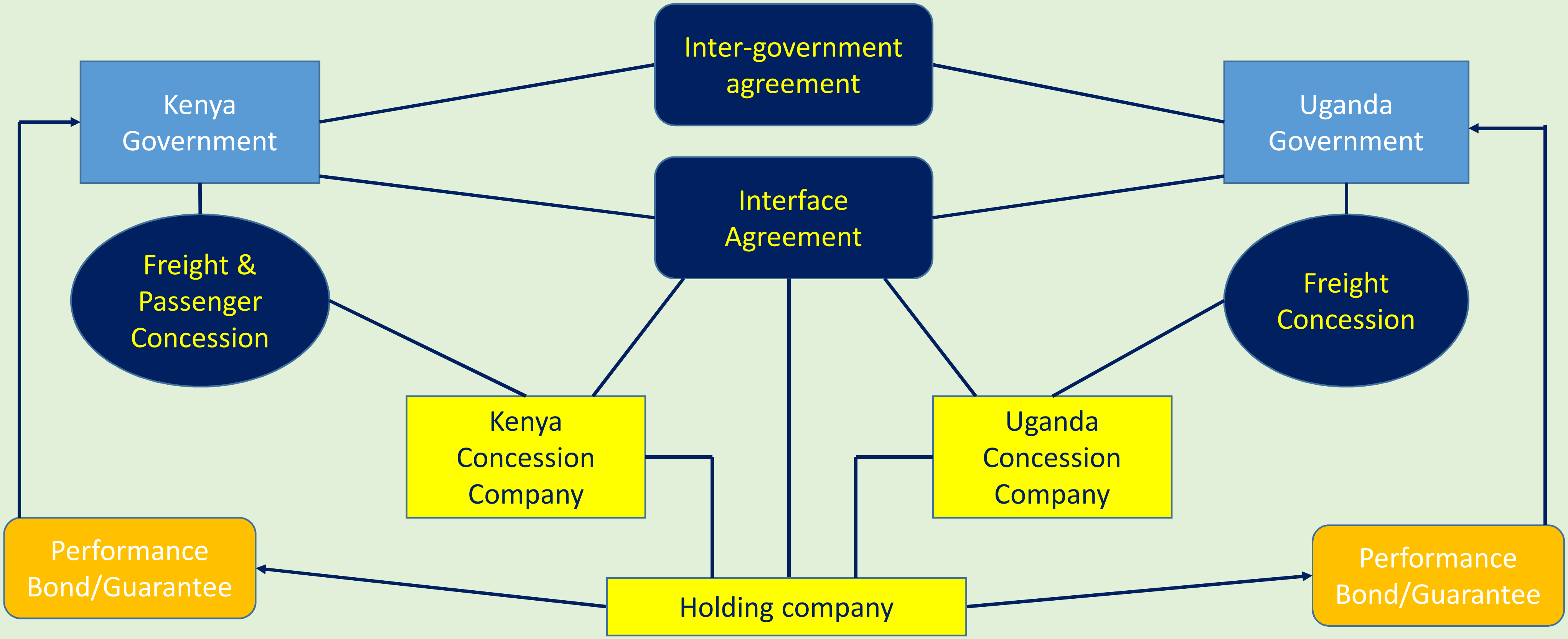
Kenya Institutional Framework



Legal, Regulatory and Institutional Framework - RVR

- Privatisation Law – Divestiture
- Concession – PPP Law
  - ✓ Limited "usufructory rights"
  - ✓ Limited guarantees
  - ✓ Credit enhancement mechanisms (minimum traffic/demand guarantee, VGF, etc.)
- Railways Act of Uganda amended in 2004 and the Kenya Railway Corporation Act in 2005.
- KRC and URC became Public Asset Holding Companies able to enter into concession agreements
- Interface Agreement signed on 7th April 2006.

Joint Concession Institutional Structure/Agreements



Transaction Implementation

- 25 years concession term
- Both concessions to be signed simultaneously
- All rehabilitation investments to be made by the private party
- All new investments to be owned by the Asset Holding Companies
- Passenger service in Kenya for 7 years
- Target performance: allow minimum speeds of 60km/hr. for freight and 80km/hr. for passengers within the first 5 years
- Possible termination if volume targets are not met in Year 10
- Lead investor to hold 35% ownership of each project company

Transaction Implementation (cont.)

- Requirement to achieve minimum local ownership levels of 20% in each country by Year 5
- Minimum Net worth of $35 million for the Lead Investor
- Lead Investor must be a railway operator with experience of carrying 100 million tonnes/yr. of freight and operate network of not less that 300km.

Transaction Implementation (cont.)

- Financials:
  - ✓ A fixed upfront concession fee of $3 million to GoK and $2 million to GoU – to be used to pay the costs of preparing and tendering the project.
  - ✓ A variable annual fee to be paid to each government:
    - Years 1 – 5 = 5% of annual gross revenues.
    - Years 6 – 25= 7% of annual gross revenues.
  - ✓ A fixed annual concession fee to be paid to each govt (to be proposed by bidders).
  - ✓ Fixed concession fee for Passenger Service in Kenya (to be proposed by bidders).

Financial Bids for KRC

	RITES/MAGADI	SHELTAM
FREIGHT REVENUE BANDS, USD MILLION	BID PERCENTAGE OF GROSS REVENUE	BID PERCENTAGE OF GROSS REVENUE
0-70	6.01%	11.1%
>70-100	6.02%	11.1%
>100-130	6.03%	11.1%
>130	6.04%	11.1%
UPFRONT FEES	USD 3.0 million	USD 3.0 million
PERSENGER SERVICES	USD Minus 6.0 million (**Subsidy**)	USD 1.0 million

Financial Bids for URC

	RITES/MAGADI	SHELTAM
FREIGHT REVENUE BANDS, USD MILLION	**BID PERCENTAGE OF GROSS REVENUE**	**BID PERCENTAGE OF GROSS REVENUE**
0-27	6.01%	11.1%
>27-38	6.02%	11.1%
>38-50	6.03%	11.1%
>50	6.04%	11.1%
UPFRONT FEES	USD 2.0 million	USD 2.0 million
PASSENGER SERVICES	Not Applicable	Not Applicable

Concession Performance

	Pre-Concession Performance			Post Concession Performance
-	Kenya Railways Corporation (KRC)	Uganda Railways Corporation (URC)	Total	Rift Valley Railways (RVR)
Total length of network (km)	2,210	1,241	3,451	1,333
Total freight volume (million tonnes/yr)	2.3	0.9	3.2	1.3
Main Commodities	Containers, soda ash & wheat	Containers,wheat & fuel		Containers, grain,cement, fuel & steel
Revenues (US $ million/yr)	53	19.5	73	76.3
Number of wagons	6,000	1,433	7,433	4,014
Number of locomotives	175	44	219	128
% wagon in operation	41	89	50	36
% of locomotive in operation	20	73	30	44

Concession Performance

2010 2011 2012 2013 2014 2015 2016

Prior to RVR acquisition by Citadel Capital (CC), the company was a loss making operation running ageing rolling stock and unable to meet its investment obligations. Travel delays were frequent and with very high transport costs. In 2008 WB & KfW threaten to withdraw $64 million commitment towards RVR's $350 million investment. Sheltam's MD, Roy Puffet steps down.

In February 2010 CC acquired 51% of RVR through its subsidiary Africa Railways

In November 2010, RVR entered into a management contact with America Latino Logistica

Upon acquisition, CC agreed with the governments a three point turnaround programme for RVR, requiring an investment of $287 million – by Sept 2011 $234 million had been raised

4 years after restructuring, RVR achieved all three KPIs agreed with the governments - clearing O/S concession fees, investing $40 million in infrastructure and rolling stock and achieving 1737 NTK in Kenya and 250 million NTK in Uganda.

CC was able to raise $234 million in senior debt and equity from a number of larger multilateral/International funding Institutions:

MDBs/IFIs	
African Development Bank	ICF Debt Pool
KfW (Germany)	Equity Bank (Kenya)
International Finance Corporation	DEG
FMO (Netherlands)	IFC (equity investment)
BIO Invest (Belgium	FISEA (PROPARCO)

Impact of SGR on RVR

- New parallel railway systems
- SGR Investment
  - Mombasa – Nairobi: US$3.6bn (or $7.6 million/km)
  - Nairobi – Naivasha: US$ 1.5 bn (or $12 million/km)
  - Total for Mombasa - Kampala: approx. $8 - 10bn.
- One way trip Mombasa – Kampala on RVR currently at 3.5 days
- Advantages of RVR:
  - Cost effectiveness
  - Familiarity with customers
- Likely to operate side by side – Japan, Australia, South America.

Lessons Learnt

- PPPs in railways should be structured and offered on a regional, system-wide basis;
- Governments should only pursue PPPs for the"right" reasons;
- Overly optimistic feasibility analyses must be questioned;
- A Concessionaire should be allowed to select the size and timing of the inputs, especially new investments;
- Appropriate legal, regulatory and institutional framework for PPP;
- Procurement process must ensure that a concession is not awarded to the "wrong guy";
- Clear risk-sharing by the Governments is essential:
  - ✓ Provision of some or all of the long-term financing needed for infrastructure renewal.
  - ✓ Credit enhancement mechanisms to lower cost of debt; e.g. demand/traffic guarantees.
- Unrealistic high concession fees requirements must be avoided.