MAERSK LINE

Tariff Adjustment Submission
The Ports Regulator, 16 October 2014

Introduction
As a strategic business partner to TNPA and the entire Transnet Group, Maersk Line appreciates this invitation to comment on the proposed average 9.47% tariff increase. The document will cover the following areas:

A. TNPA tariff proposal
B. Container subsidisation of bulk cargo
C. Increasing revenue from real estate

A) TNPA tariff proposal

Maersk Line's analysis of TNPA's required revenue formula shows that the application is not justifiable but actually should show a downward adjustment in tariff for 2015/16 of -6.75% as opposed to TNPA's suggested 9.47% tariff increase. Maersk Line's findings are elaborated on below to support this position.

The key findings of the analysis are divided into three categories.

1. Financial data
2. Expected Volume Growth
3. Operational efficiencies.

Financial data

It is noted that TPNA has developed a solid foundation for their financial data and Maersk Line agrees to the majority of the available information.
However, Maersk Line notices that the formula and calculation behind the Hamada model are not explained and we find the result different from the 0.86 in the application.

Hamada equation is: $B_l = B_u[1 + (1 - T)(D/E)]$

In the application, the following information is shared:
Asset beta (B_u)=0.5, Tax rate=28% and D/E ratio is 50%.
Applying this to the model results in a leveraged beta of 0.68 which leads to a WACC of 5.08%, instead of TNPA's suggested WACC of 5.58%.

Maersk Line proposes to use the corrected WACC in the calculation accordingly.

Expected volume growth

TNPA expects container volumes to grow with 4.65% for the next tariff period, which is in line with Maersk Line's expectations.

Accumulated with the volume increase from the other sectors, the weighted average volume increase for FY2015/16 is 4.6% as per table 1[1].

[1] There are some discrepancies between expected growth in table 7, page 28 and table 18 page 42. Maersk Line has taken offset in table 7 figures.

Forecast FY 2015/16		
Weighted volume growth	% increase volumes	% of total volumes
Containers (TEU)	4.6%	2.2%
Vehicles (Units)	5.2%	0.3%
Break Bulk (Metric Tons)	9.4%	3.9%
Dry bulk (metric tons)	4.0%	77.0%
Liquid bulk (kl)	6.0%	16.7%
Weighted increase		**4.60%**

Table 1 - Volume growth

However, TPNA applies a decrease in volumes of -4.3% to the category "Marine and other revenue" and therefore concludes that the overall volume increase will be 2.80%.

The reason for the decline, as stated in section 6.3.7, is the sluggish economy and major shipping lines bringing less but larger vessels to the South African ports. This trend is not recognized by Maersk Line since the container shipping line vessels are already of the maximum size allowed in the South African ports. Furthermore, TNPA provides no background or data justifying the - 4.3% figure in the application which causes us to question the figure.

Therefore, Maersk Line proposes to use the 4.6% increase in the Required Revenue (RR) calculation instead of the 2.8%.

Operational Efficiencies

Maersk Line would like to highlight a concern in the methodology applied since the operating expenditures are simply added to the revenue requirement which implies TNPA does not expect to achieve any operational efficiencies.

This implication is given extra weight when reviewing the budgeted 25% increase of TNPA's operating expenditures submitted by TNPA in the application. This is cause for great concern.

The transportation industry has been under pressure during the financial turmoil over the past years which have put pressure on companies to review their cost picture and secure lowest cost. It is expected that all players in our industry follow this same behaviour and that TNPA should actively be pursuing operational efficiencies rather than simply continuing to assume a ballooning of operational expenses. It is recognised that inflation in South Africa is high and does impact some of the cost, but TNPA has set an obligation to reduce cost of logistics as a percentage of transportable GPD and create opportunities for growth in South Africa. This will not happen with the current spikes in tariffs and operational expenditures.

This leads to two recommendations from Maersk Line:

1) Required revenue methodology to be changed by the regulator to encourage TNPA to pursue operational efficiencies and mitigate cost increases

2) Change the expected operational expenditures to be in line with the expected volume growth, where TNPA gets compensated for the increase in volumes but their costs are not increasing uncontrollably.

Consolidating the findings in the analysis leads to the following proposal to the 2015/16 change in tariff:

Description	TNPA application FY 15/16 Rm		ML Proposal FY 15/16 Rm	
RAB	ZAR	67,000	ZAR	67,000
Real Vanilla WACC		5.59%		5.08%
Return on capital	ZAR	3,745	ZAR	3,403
Plus: Depreciation	ZAR	1,807	ZAR	1,807
Plus: Operating expenses	ZAR	5,020	ZAR	4,194
Plus: Taxation expenses	ZAR	964	ZAR	964
Plus/Less: Clawback	ZAR	(328)	ZAR	(328)
Plus: ETIMC			ZAR	-
Revenue requierment	ZAR	11,208	ZAR	10,040
Less: Real estate	ZAR	(2,449)	ZAR	(2,449)
Total net revenue required	ZAR	8,759	ZAR	7,591

Marine revenue	FY 15/16 Rm		FY 15/16 Rm	
Prior year revenue	ZAR	7,783	ZAR	7,783
Estimated volume growth		2.80%		4.60%
Revenue after volume growth	ZAR	8,001	ZAR	8,141
Required revenue	ZAR	8,759	ZAR	7,591
Tariff increase		9.48%		**-6.75%**

Maersk Line sees TNPA as financially capable of delivering on their targets with a required revenue of R7,591m, leading to a -6.75% decrease from their current tariff level. This is vastly driven by the cost increase of 4.6% as per the expected volume growth instead of the unrealistic 25% cost increase which TNPA purports and Maersk Line finds unacceptable.

With the proposed 9.47% increase, TNPA will have an over-recovery of R1,168m with adverse impact on an already strugglingSouth African economy.

The same assumptions as above mentioned should be applied for the 2016/2017 & 2017/2018 financial years.

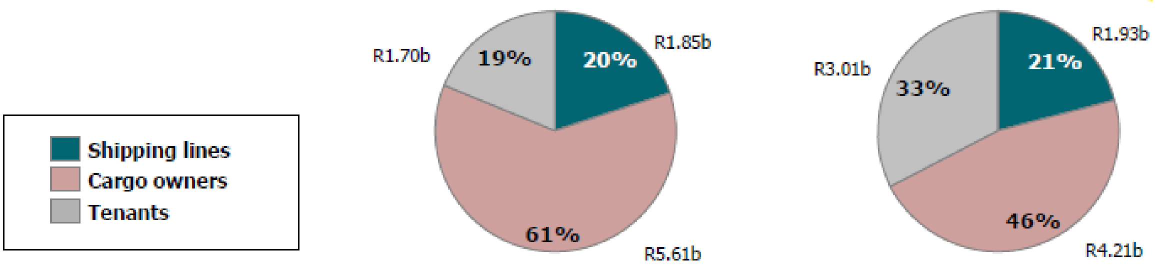
B) Container segment subsidisation of bulk

Following the proposed general level on the change in tariff compared to the required revenue, Maersk Line supports the findings of the regulator that the container industry is currently subsidising the bulk business in terms of tariffs compared to capital investments in the individual sectors. It is of the opinion of Maersk Line that each commodity group should be self-funding for investments and therefore it is recommended that the Port Regulator reviews and adjusts the tariff increase methodology for coming years so changes in tariffs are applied basis the investment for the given commodity.

This supports the proposed -6.75% decrease in tariffs for the container and marine tariffs.

C) Comment on increasing income from real estate

In the tariff application and the presentation provided in the roadshow by TNPA it becomes evident that TNPA is expecting an increasing share of their revenue to be derived from their real estate segment. I.e. collecting rent from their tenants of which TPT contributes the largest proportion. This will mean an increased cost for TPT, which might be inclined to recover this costs through increased terminal handling charges.



Maersk Line would like to raise this as a concern, since an increasing amount of our total port costs could fall outside the purview of the port regulators.

Therefore, Maersk Line would like to know from the port regulator if there is any intention to widen the scope of the Port Regulators control to include Transnet Port Terminals?

Concluding comments

The proposed 9.47% tariff application by TNPA will have a negative macroeconomic impact further reducing the ability of South Africa's business to complete in the global market place.

The analysis conducted by Maersk Line shows there is no financial basis for TNPA's suggested increase. The proposed tariff increase will allow TNPA to increase their cost with 25% and limit the incentive for actively pursuing operational efficiency improvements which Maersk Line believe should be the key focus for the port authorities for the coming years.

In conclusion, Maersk Line strongly suggests a tariff reduction of -6.75% for container and marine tariffs the 2015/2016 tariff review and we look forward to a favorable review from the Port Regulator.