MAERSK LINE

Tariff Adjustment Submission

The Ports Regulator, 29 October 2013

Introduction

As a strategic business partner to TNPA and the entire Transnet Group, Maersk Line appreciates this invitation to comment on the proposed 8.5% tariff increase.

Maersk Line/Safmarine Tariff Process Submission

We have divided our feedback into the following three sections:

A. Key tariff adjustment factors
B. Benchmarking against global ports
C. Concluding comments

A) Key tariff adjustment factors

Based on Maersk Line's review of the TNPA application, our analysis shows that the current 2013/2014 tariff levels adequately cover TNPA's revenue requirement for 2014/2015.

Instead, we propose a downward adjustment in tariff for 2014/15 as opposed to TNPA's suggested 8.5% tariff increase. Maersk Line's findings are elaborated below to support this position. Table 1 illustrates TNPA's proposal versus Maersk Line's calculations which is further explained below.

Key factors	TNPA proposal	Maersk Line proposal
1. ER 2013/14	R 11,301 mil	R 11,301 mil
2. EVI 2013/14	3.5%	3.5%
3. ER 2013/2014 (incl. EVI)	R 11,773 mil	R 11,746 mil
4. RR 2014/15	R 10,947 mil	R 10,947 mil
5. ER at proposed tariff increase (incl. EVI)	R 12,744 mil	R 10,947 mil
Tariff adjustment	+8.5%	- 1%

Table 1: TNPA vs. Maersk Line calculations for 2014/2015 tariff adjustment

It should be noted that the figures represented above exclude any real estate considerations as we assume that the recovery ratio applied on the real estate revenue is fair. For this submission, we will be solely reviewing the revenue generated from TNPA's marine business.

Please find the breakdown of these factors listed below:

1. Estimated Revenue (ER) 2013/2014 of R 11,301 mil	
TNPA estimation of R 11,301 mil	**Maersk Line estimation of R 11,301 mil**
Additional comments: o The estimated revenue is derived from the summation of total revenue calculated by sector basis 2013/2014 budgeted volumes in Line with TNPA's estimation.[1] o Maersk Line agrees with TNPA on this amount on the principle that the budgeted volumes provided by TNPA are in line with industry expectations of volumes handled through all ports in South Africa.	

[1] Refer to TNPA's application page 39, table 19.

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2. Estimated Volume Increase (EVI) 2013/2014 of 3.5%	
TNPA estimation of 3.5%	**Maersk Line estimation of 3.5%**
Additional comments: ◦ Maersk Line agrees with TNPA's growth expectations of 3.5% while considering actual growth from the last FY 2012/2013, we anticipate a slight decrease from 2013/2014 estimation of 4.2%. ◦ The slight drop in volumes is mirrored in Maersk Line's volume development over the same period, which accounts for a considerable share of the market.	

3. Estimated Revenue (ER) 2014/2015 (adjusted for EVI) of R 11,746 mil	
TNPA estimation of R 11,773 mil	**Maersk Line estimation of R 11,746 mil**
TNPA estimated amount is derived basis volumes growth 14/15 of 13,642,986 units at 13/14 tariff book rates. This revenue contribution has been weighted accordingly by sector.	Maersk Line estimates revenue of R 11,746 mil based on 13/14 tariff book rates and volume growth of 3.5%. The marginal difference stems from taking an unweighted average of total port volumes.

4. Required Revenue (RR) of R 10,947 mil	
TNPA estimation of R 10,947 mil	**Maersk Line estimation of R 10,947 mil**
TNPA's proposed amount is derived using the RR formula as per the interim regulatory manual. Within the RR formula, it is noted that the ß coefficient used to capture TNPA's exposure to market risk has been reduced from 1.13 (2013/2014 tariff review) to 0.5 (2014/2015 tariff review) which displays a relatively low risk matched to TNPA's actual operating environment. It is noted that the weighted cost of capital (WACC) calculated for 2014 is markedly lower from 8.33% (2013/2014 tariff review) to 5.83% (2014/2015 tariff review).	Applying the RR formula, Maersk Line agrees with TNPA's required revenue. Two key factors that are significantly improved from last tariff review of 2013/2014 are the lower ß coefficient and improved WACC figures. Maersk Line agrees with these figures for 2014/2015 tariff review.

5. Forecasted Revenue (FR) 2014/2015, at Maersk Line proposed tariff reduction, to R 10,947 mil	
TNPA estimation of R 12,744 mil	**Maersk Line estimation of R 10,947 mil**
Taking the current tariff book rates in 2013/2014 and EVI of 3.5% results in revenue of R 11, 773 which is an over recovery of R 971 mil. Furthermore, applying the proposed increase of 8.5% to the ER 2014/2015 incl. EVI of 3.5% results in ER of R 12, 744 and an over-recovery of R 1,797 mil.	Based on the estimated revenue adjusted for the estimated volume increase as per point 3 above, it follows that TNPA receives a surplus of R 826 mil at current tariff book rates of 2013/2014. Maersk Line recommends a tariff reduction (-1% on 2013/2014 tariff book rates) to avoid surplus recovery, in line with TNPA's required revenue of R10, 947.

Our findings are that TNPA is financially capable of delivering on their revenue requirement with a rate reduction of 1% on the 2013/2014 rates. Making use of the current tariff (2013/2014) and expected 3.5% volume increase, the Port Authority should anticipate an over recovery of their required revenue by R 971 mil. Taking an additional tariff increase of 8.5% into account, the Port Authority will further over recover by R 1,797 mil. While we support TNPA in earning a return commensurate with the risk of owning its assets, given its low risk operating environment (asset beta of 0.5) and decent return made at current tariff levels (R 971 mil), Maersk Line's proposal is to reduce current tariff levels by 1% for the above mentioned reasons.

B) Benchmarking against global ports

Part of TNPA's mission statement is to enhance its ports' geographical positioning as a leading gateway for trade emanating from the eastern and western seaboards. To deliver on this statement, we believe that it is crucial that TNPA delivers on two fundamental requirements; a superior service accompanied by a competitive cost structure.

To illustrate this, we have completed a benchmarking exercise making use of two representative vessels and eight ports located globally validating performance and cost against crucial port facilities operated by TNPA.

Actual port callers are used as a common basis for our benchmarking exercise, where the vessel specifications are as per table 2 below:

Vessel	Maersk Seletar
Maersk Service	SAFARI (Asia-South Africa)
Gross Registered Tons (GRT)	79,702 GRT
Length	318 metres
Container Volumes Carried	1574 TEU (Import Discharge cargo)
	1259 TEU (Export Loaded cargo)
	315 TEU (Empties Loaded)
Vessel	Safmarine Nokwanda
Maersk Service	SAECS (South Africa-Europe Continent)
Gross Registered Tons (GRT)	50,657 GRT
Length	265 metres
Container Volumes Carried	1000 TEU (Import Discharge cargo)
	800 TEU (Export Loaded cargo)
	200 TEU (Empties Loaded)

Table 2: Vessel specifications of vessels classed used for port benchmarking exercise.

Table 3 below illustrates total port costs per call based on the representative two vessel classes as represented in table 2 above:

Port Performance			Cost per call[2]			
Port	Average Waiting Time (hours)[3]	Average Berth Productivity (BMPH)[4]	Maersk Seletar (USD)	Safmarine Nokwanda (USD)	Cargo Dues[5] (USD)	Total Cost (USD)
Durban	36	28.6	34,699	25,189	337,321	372,020
Cape Town	21	26.4	38,084	25,794	337,321	375,405
Port Elizabeth	15	26.5	38,275	26,983	337,321	375,596
Bremerhaven	5	89.3	54,254	44,453		54,254
Rotterdam	2	83.0	53,747	50,077		53,747
Jebel Ali	4	94.7	27,238	19,847		27,238
Shanghai	10	102.9	26,822	18,422		26,822
Jawaharlal Nehru	4	100.4	25,982	19,044		25,982
Yantian	2	104.9	23,097	16,456		23,097
Tanjung Pelepas	3	92.2	15,834	12,042		15,834

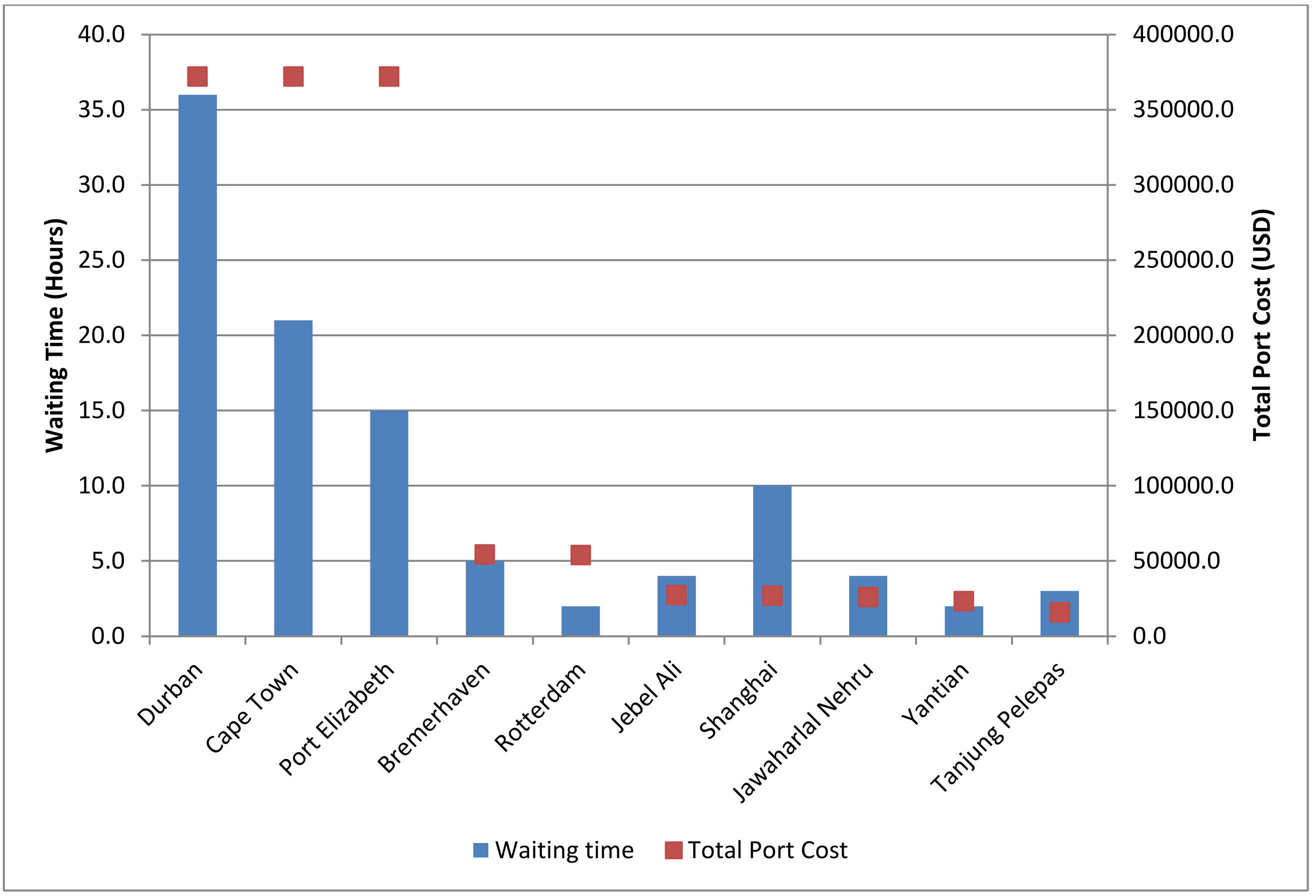
Table 3: Comparison of total port cost per call to port performance for selected ports.

The comparisons above illustrate the non-competitiveness of South African ports relative to key global ports. Asian ports are characterised by shorter waiting times, higher productivities and significantly cheaper port costs. The more expensive European ports deliver a superior port performance. Moreover, we have noted that the basic marine service charges billed to port users; port dues, pilotage and towage exceed the levels when compared to benchmark ports. These marine charges combined form the largest portion of port costs in South Africa. The global practice is for the National Port Authority in its capacity as landlord to hold the party responsible for delivering terminal operations equally accountable for optimal port performance.

As displayed in table 3, it should be noted that there is an additional element of cargo dues to consider which makes TNPA's port cost even more uncompetitive for its port users. This is because cargo dues remain a truly unique expense which renders South Africa largely incomparable to its global counterparts. When we factor in cargo dues against the other ports, TNPA's total cost is well above benchmark ports.

Graph 1 is a visual depiction of the factual evidence presented in table 3, contrasting port performance versus cost clearly illustrating the lack of competitiveness of TNPA ports when compared to global ports.

[2] Cost based on a 24-hour port stay. An exchange rate of 1 dollar = R9.8 is used here up from the R8.6 used during last year's analysis, this huge change still does not make the South African ports competitive.
[3] Waiting time is defined as the time spent between vessel arrival and arrival at pilot station. This parameter captures the marine operational delays which TNPA influence and is a good indicator for vessel turnaround time in a port.
[4] Berth Productivity is defined as the total number of moves handled per hour, from first lift to last lift.
[5] Cargo dues are weighted based on the two vessel classes used in our analysis.



Graph 1: Illustration of Total Port Cost versus Waiting Time for selected ports.

C) Concluding Comments

Marine operations have been identified as one of TNPA's focal areas for port efficiency, productivity and performance improvement. While there is a major requirement for the Authority to address marine operational delays and resource availability, these issues ought to be internalised by TNPA to find means to improve the port performance within South Africa by delivering on its own targets. In this way, the focus is shifted from altering price (proposed 8.5% tariff increase for 2014/2015) while delivering suboptimal performance to achieving performance targets which would translate to greater efficiencies and revenue generation as a result.

Furthermore, the proposed 8.5% tariff application by TNPA will have an undesired macroeconomic impact whereby South Africa's competitiveness as a trading partner in the global economy will be reduced. The proposed tariff increase will likely restrict TNPA's ability to play a leading role in positively influencing economic growth through efficient provision of infrastructure and optimal delivery of its marine operations services.

With the above in mind, Maersk Line suggests a tariff reduction of 1% for the 2014/2015 tariff review and we look forward to a favourable review from the Port Regulator.