

Issues besieging tolled highways

Consumers are unhappy with the steep hike in toll rates but concessionaires contend that it's overdue

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THE numbers that toll concessionaires generate are simply astounding that it would be hard to blame the man on the street for the recent steep hikes in rates.

For instance, Malaysia has a total of 28 highways and almost all except for one, showed an increase in traffic flows based on numbers between 2009 and 2013.

In 2013, the volume of traffic recorded on the toll highways of Malaysia was 1,641.37 million, showing an increase of close to 5% compared with 1,567.35 million recorded in 2012.

Overall, the 27 out of 28 highways experienced traffic increment for the year 2013 at a range of 0.27% to 46.66%, according to the Malaysian Highway Authority, a federal statutory agency under the Ministry of Works.

So the numbers show that clearly traffic has been increasing. But not all highways are profitable because the growth in traffic does not meet the forecast figures.

This is something that David Lee of Malaysian Rating Corp Bhd (MARC) can testify.

"Most of MARC-rated highways trailed the projected forecast" but it urban or intra-urban, with the exception of a few," says Lee who is the vice-president (ratings) of MARC.

Despite highways not meeting

traffic projections, it is worth noting that the country has yet to see the failure of an urban toll road.

So far only one toll concessionaire, Senai-Desaru Expressway has defaulted because its traffic numbers have been way below the projected figures. The highway concessionaire, nonetheless, has been able to restructure its debts.

Nevertheless, the steady traffic volume growth as well as concessionaires having a mix of profitable and non-profitable highways have cast doubt over the need to raise toll charges.

The contention is that traffic volume will keep increasing with population growth, collection will keep on adding to the coffers of concessionaires and more importantly strengthening their financial position.

Hence it is only a matter of time before they become profitable and allow some returns to shareholders.

RAM Ratings Sdn Bhd co-head of infrastructure and utilities ratings Davinder Kaur Gill says that toll concessionaires in RAM Ratings' portfolio last witnessed a toll rate hike in 2007.

"Some of the intra-urban highways under RAM's coverage have been operational for more than 10 years, they have yet to experience a toll rate hike in their operational life."

"Restructuring of concession agreements via preserving current toll rates at a lower rate while

extending concession tenures remains an alternative solution to this tolling impasse faced by the sector," Davinder says.

Lengthening concession period?

Since the 2008 general election, the Government has opted to maintain toll rates and increased the length of the concession because of it being a political hot potato.

However concessionaires have a different view on the matter. They have issued debt papers backed by scheduled toll hikes.

MARC's Lee says that non-monetary compensation such as extension of the concession tenure typically affect the cash flow of the concessionaire and introduce asset-liability mismatches to the project debt.

"Under such scenarios, concessionaires need to refinance the project debt. However, lengthening repayment obligations would potentially affect their ratings."

"Concessionaires also have to grapple with high financing costs with any increase in construction costs, and therefore lengthening of the concessions would also push the returns to shareholders into the far future," he says.

Lee explains that the credit risks associated with toll projects is mainly driven by traffic, concession and financing structure risks.

He says the debt amortisation profile of such projects is sculpted



to match revenue projections based on projected traffic growth rates and timely implementation of scheduled toll rate hikes.

"Concessionaires have not been allowed to increase toll rates according to their concession agreements in recent years, although cash compensations to make up for the lost toll revenues have usually been paid but on a deferred basis."

"This applies pressure on the concessionaires' ability to withstand the working capital gap which is critical to maintain project debt obligation. Some concessionaires underwent debt refinancing during that period pursuant to renegotiation of concession terms with the government," Lee says.

Also, whenever the concessionaires are not allowed a scheduled toll rate hike, the government has to compensate them based on the traffic flow. This is viewed as unfair to those residing outside the Klang Valley that do not use the highways.

"It is unfair that the government is using the public money to compensate the concessionaires. This goes against the user-pay concept, indirectly burdening taxpayers nationwide. Those living in Sabah and Sarawak will not be using the Damansara-Puchong Highway (LDP) or the Sprint highway," an industry observer notes.

The total compensation paid by the Government from 2008 to 2013 amounted to RM1.1bil, and RM402.9mil in 2014. The Government paid RM510mil in compensation for the January to October period this year following

the decision to postpone toll hike that should have been implemented in January.

RAM's Davinder believes the removal of subsidies and imposition of toll rate hikes is necessary, as it is part of the broader subsidy reform the Malaysian government has been undertaking since July 2010.

It is also a key criteria for Malaysia when it is rated by international rating agencies that want to see the Federal government budget deficit as a percentage of the economy drop to less than 3% next year.

Are highways cash cows?

An official familiar with highway concessions says that not all urban highways are profitable.

He says the perception is that highways are 'money-making'

machines because it provides steady cash flows. But the bulk of money goes towards paying off the banks.

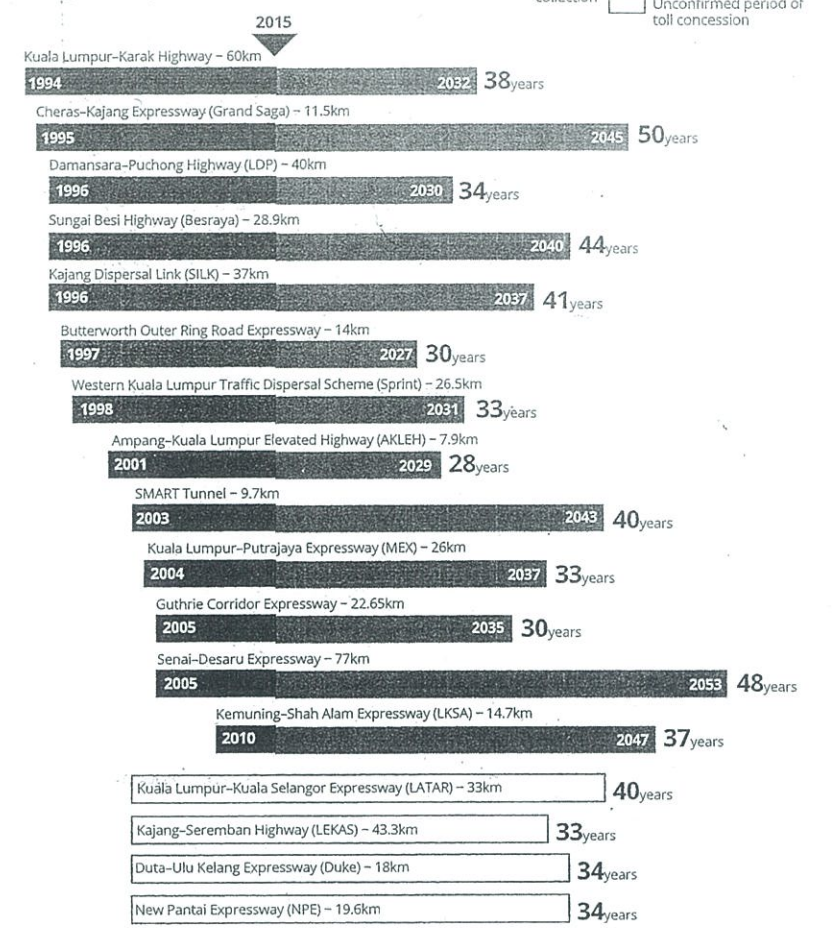
RAM's Davinder says that a large part of toll concessionaires' operational cashflows is channelled to its debt obligations due to the capital intensive nature of highway construction.

"In that respect, based on our observation of the RAM Ratings rated portfolio, the ratio of annual debt repayment to annual net operating cashflow for each toll concessionaire ranges from 30% to almost 100% in certain instances," says Davinder.

The industry official says that highways such as New Pantai Expressway and the Besraya Expressway have yet to declare any dividends for shareholders even

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Highway concession period



* Concession period includes supplemental concession agreements
Source: Various

HIGHWAYS IN NUMBER

According to the Malaysian Highway Authority, there are a total of 28 highways in Malaysia, with 19 of them being intra-urban highways.

The North-South Expressway is Peninsular Malaysia's main artery connecting all the states, stretching a total length of 772km. It recorded the highest traffic flow compared with other highways with 496.59 million in 2013.

In 2013, the volume of traffic recorded on the toll highways of Malaysia was 1,641.37 million, an increase of 4.72% compared with 2012's 1,567.35 million.

1,641.37 million cars (2013)

4.72%

Highways generally record an increase in traffic. Out of the 28 highways, 27 saw an increase in traffic in 2013 ranging from 0.27% to 46.66%.

Concessionaires get an average return of 10%, claims the association while 40% goes towards repaying bank loans, operations and maintenance, upgrading and repairing.

For every RM1 collected, 40sen goes towards maintenance, upgrades, repairs and operations. This is what the Association of Highway Concessionaires Malaysia claims.

Only a couple of toll booths have been dismantled in recent years. They are Taman Medan (NPE), East West Link, Cheras-Kajang Highway and Senai toll. One of the first toll gates to be dismantled was the Jalan Kuching toll in 2003.

Senai-Desaru Expressways Bhd experienced a severe cash flow problem as traffic volume of the expressway was not even 10% of the original projection. It restructured its RM1.46bil Islamic debt papers after RAM Ratings cited high likelihood of default.

The total compensation paid by the Government to concessionaires from 2008 to 2013 was RM1.1bil, and RM402.9mil in 2014. Throughout 2008 and 2011, the Government paid RM459mil in compensation, while in 2012 it paid RM329mil, and in 2013 it paid RM343mil.

Similarly, Silk Holdings Bhd restructured their bonds to avoid a full-blown default in 2007. After more than two years of negotiations, an agreement was struck with holders of the RM2.01bil BaiDS Islamic bonds secured on the SILK highway concession (SILK is a 100% subsidiary of Sunway Infrastructure Bhd, in which Sunway Holdings Inc Bhd had owned 36%). SunInc had to pay RM50mil to the bond holders to make up for shortfall in the bond redemption and surrender its 36% stake in SunInfra.

toll highway

Sprint Highway traffic way below forecast

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after 15 years of concession.

"The New Pantai Expressway (NPE) has a debt of RM280mil after 15 years of operations. And the company has not declared any dividend to shareholders. Would this be acceptable to shareholders of an ordinary listed company?" the official adds.

This is echoed by Lingkaran Trans Kota Holdings Bhd's (Litrak) chief executive officer Richard Lim.

He says that although traffic growth for Sprint Highway was between 4.3% to 4.4%, it was significantly below their forecast for average daily traffic.

"Note that the Government, in any concession agreement, does not guarantee traffic volume nor traffic revenue. Any shortfall in revenue as a result of lower traffic

"In the meantime, the toll concessionaire has to incur losses such as Sprint which incurred losses for over 14 years and only started making a profit this year of RM 1.5mil."

- Richard Lim

volume is a risk borne by Sprint," Lim tells StarBizWeek.

Lim says that it would not be feasible to lengthen the concession period to enable the company to recoup its investment.

Lim says the concession period cannot be lengthened without putting Sprint at a very high risk of insolvency or undertaking a very costly refinancing exercise since the company will be unable to repay its borrowings on time.

The extension, he says could also upset the public at large as the extension period will be long and could also severely affecting the shareholders who have to wait even longer for a return.

Lim explains that the business model used for the setting of toll rates for most highways was to start from a lower figure and to increase it over time, which is fairer since the value of money lessens over time.

The business model, Lim says used also took into account the increase in traffic volume over time and based on the increasing toll rate structure and increasing traffic volume, a revenue forecast was built which eventually formed part of the financial feasibility study on whether the tolled highway project was feasible or not.

As the construction of any highway is costly, a major portion of the financing has to be borrowed on a long-term basis with the bulk of repayment to be made only in later years when toll rates and traffic revenues are higher.

"In the meantime, the toll concessionaire has to incur losses such as Sprint which incurred losses for over 14 years and only started making a profit this year of RM 1.5mil," Lim says.

He also discloses that the shareholders of Sprint have not received

any returns/dividends from their investments since commencement of operations over 15 years ago with accumulated losses at RM440mil.

Since the 2008 general elections, there has not been any toll rate hikes. Concessionaires have been compensated for deferring their rate hikes. So when the rates went up on Wednesday, it was a steep increase, which was not to the amusement of city dwellers.

But from the way the implementation has taken off, it seems that there is no turning back on the decision by the government to allow the rate hike.

That is something highway users would have to bear with for a long time. Going forward however, regulators need to be smart to renegotiate the way highway projects are awarded to ensure that the toll rate hikes inflict less pain on the people.