
Armenia Looks To The Private Sector for Rail Network

Railway Gazette International, UK - 16/1/2007

IN SEPTEMBER, the government of Armenia invited bids for a concession to renovate and operate the country's rail network, following an initial prequalification announcement in June.

Armenia is currently implementing a wide range of economic reforms, supported by the US government, the World Bank, the European Union and the Asian Development Bank amongst others. Restructuring is already underway in the energy, water and communications sectors, and Armenian Railways has been established as a joint stock company wholly owned by the Ministry of Transport & Communications.

'Our desire is to make the railway more productive and less dependent on government', explained Transport Minister Andranik Manukyan, addressing a pre-bidding roadshow held at the headquarters of the European Bank for Reconstruction & Development in London on September 6.

'Armenia wants a successful railway', he emphasised. 'The government has taken action to strengthen the railway, improve the regulatory environment and reduce risks for the private sector. This concession will protect the economy of Armenia and enhance the contribution that will be made by rail transport.'

At the World Bank's suggestion, US-based consultancy HWTSK was brought in to assess the condition of the Armenian rail network and advise on the scope for involving the private sector. The World Bank and the Armenian government provided US\$15m in 2002-04 to fund the rehabilitation of 72 km of track, and the EU's tacis programme funded the installation of a new optic fibre communications network by Siemens which was completed in 2005. The government is currently negotiating funds for further infrastructure rehabilitation.

The concessionaire will also be expected to provide investment funding. According to the consultants, AR needs around US\$170m to modernise the network, of which half would go on infrastructure works and half on replacement of largely life-expired traction and rolling stock.

Traffic bounces back The AR network is predominantly single-track, with 736 route-km active and approximately 110 route-km out of service due to the border closures and a landslide. The entire network is electrified at 3 kV DC. AR has 41 main line electric locomotives, mostly ex-Soviet designs of classes VL8, VL10 and VL11. There are also 56 diesel locos, mostly used for shunting, together with 68 EMU cars. Hauled stock comprises 189 coaches and 3657 wagons, of which barely half are operational.

AR's traffic statistics clearly show the problems under which the railway has been labouring for the past 20 years. In 1988 the railway carried 30 million tonnes of freight and 5 million passengers.

Traffic was hit badly by the Spitak earthquake in December 1988 which severely damaged the line around Gyumri. Then came the breakup of the Soviet Union, and Armenian independence in 1991. Harsh economic conditions saw a 50% fall in traffic across all the railways in the region.

The war between Armenia and Azerbaijan in 1992 led to the border with Turkey being closed in 1993, cutting all transit traffic. However, there has been an upturn in recent years, due in part to a booming economy described by local

business leader Arsen Ghazaryan as 'a Caucasian Tiger'. Armenia is currently recording double-digit GDP growth year on year.

>From a low point of 1.4 million tonnes in 2000, AR's freight traffic has crept upwards to 2.7 million tonnes in 2006, and the target for 2007 was 2.8 million. According to AR's First Deputy General Manager Vahagn Karagiozyan, freight traffic in the first eight months was 400000 tonnes ahead of the previous year, and he was confident that traffic would top the 3 million mark by the year-end. 'We have the potential to double our traffic in the next few years', he predicted confidently.

Around 60% of AR's freight business is international, but with four of the five border crossings closed, all traffic has to be routed via Airum on the line to Tbilisi. Longer-distance traffic moves via Georgia's Black Sea ports of Poti and Batumi, which are linked by train ferry to ports in Russia and Ukraine.

Passenger traffic, however, has been declining steadily since a post-independence peak of 1.3 million passenger-journeys in 2002.

Rehabilitation of the local road network, coupled with the roundabout rail routes, makes the typical road trip between three and five times faster than rail. This has hit AR hard. Today the railway runs just one local and five inter-city trains a day, plus a daily international service to and from Tbilisi and a summer-only train to and from Batumi. In 2006 passenger traffic totalled just 675 000 journeys, or barely 27 000 passenger-km.

Nevertheless, Manukyan insists that passenger operations should continue. 'A railway which does not have a passenger service is incomplete as a transport undertaking', he explains. 'Despite falling traffic in recent years, we still believe that passenger operations are an integral part of the railway. When the tender bids are assessed, advantage would be given to a bidder with a desire to keep the passenger operations, all other things being equal.'

Concessioning process Having looked at various models for privatisation, including the separation of infrastructure from operations, HWTSK recommended that a vertically-integrated concession would be the most appropriate model.

An initial concession period of 30 years is envisaged, with an option for further extensions. CPCS Transcom is acting as transaction adviser, preparing tender documentation and assisting the government in assessing the bids.

As well as appointing external advisers, the Ministry of Transport & Communications has established a Project Implementation Unit to develop the concession, together with a separate working group dealing with legal and regulatory issues. PIU Director Alexander Bakhtamyan insists that 'we intend to conduct an open, equitable and transparent international tender.'

Prequalification bids were due by September 21, and groups led by Russian Railways and Rites were shortlisted in October. However, Rites has subsequently withdrawn from the process, leaving RZD as the only party likely to have submitted a final bid on December 21.

Financial bids are to be opened on January 8, and the ministry hopes to announce the winner on January 15, with a view to handing over control of the network during 2008.

According to Gayan Torozyan, who heads the regulatory working group, the new railway law setting the framework for concessioning was 'almost ready to go to the national assembly for ratification' at the end of September. This will be followed in due course by secondary legislation to put the detailed concession terms in place.

With World Bank support, the government will take responsibility for funding the retirement or retraining of redundant staff, leaving the concessionaire free to recruit only as many employees as it feels necessary.

Manukyan insists that 'the government does not want to interfere in the business activities of the concessionaire', although it is planning to put in place some provision for open access, mainly so that Georgian Railways could run to Yerevan or through to Turkey if the border re-opens. The consultants believe that open access provision would provide the concessionaire with a degree of competitive pressure, although there is unlikely to be enough traffic to attract independent operators.

'The concessionaire will have exclusive rights to manage the infrastructure, but a clause will provide rights for others to use network at pre-determined access fees', explains Torozyan. The methodology for setting access charges 'will be agreed by the government and implemented by the concessionaire', probably requiring the production of some form of annual network statement.

The government also wants to retain the right to set maximum tariffs for 'commodities of strategic importance', although Torozyan says there will be a 'regulatory commission' to protect all parties.

According to Bakhtamyan, there will be no government subsidy for the operation of passenger services, which will continue to be cross-subsidised from the profitable freight business.

In parallel with the tendering process, PIU has started to draw up a draft concession agreement, which will form the basis of negotiations with the preferred bidder.

International connection Given the high proportion of international traffic, maintaining a continuing relationship with Georgian Railways will be critical to the success of the Armenian concession.

At the September roadshow, concerns were expressed about the Georgian government's announcement in August that it intended to award a 99-year concession to run the country's rail network to an international consortium (RG 9.07 p524) through a negotiated procedure, rather than by means of an open tender.

That proposal has since been withdrawn, and the Georgians are now looking at some form of international tender with the aim of privatising their railway by the end of 2008. The Armenian government remains confident that any new owners would continue to honour the current traffic arrangements.

'International freight and passenger tariffs have been set through a bilateral agreement between the governments, and will be protected for the next three years', insists Manukyan.

He believes that the winning bidder of the Armenian concession would be well placed to win a tender to operate the Georgian network as well. That would permit closer integration of the two railways to restore a truly international business, he suggests.

CAPTION: One of Armenian Railways' few main line passenger services links Yerevan with Yerashk. An EMU is seen here awaiting departure from the capital
CAPTION: Consultants have recommended withdrawal of all passenger services in Armenia because of dwindling ridership, but the government has pledged to retain them as part of an integrated network. This is the station in Yerevan
CAPTION: The key junction and marshalling yard at Massis is controlled from a Soviet-era signalbox. Despite four of Armenia's five border crossings being

closed, international freight is seen as a potential growth market for the railway in the future

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