

A debate is raging on toll highways. Consumers are urging the government to ensure that there is no drastic hike in toll rates. The government has recently told concessionaires to value their assets in the event that the government decides to take back the highways.

Should the government take over the highways?

BY SIOW CHEN MING



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If the government cannot reverse the favourable terms granted to toll road concessionaires and is forced to compensate them if toll hikes have to be deferred, then it is better to take over the toll concessions.

That doesn't necessarily mean the government should immediately stop the collection of toll. Toll revenue is still necessary to repay the financing of the highways and to maintain and operate them.

But the government can, by taking over the toll concessions, put an end to further toll hikes, lower the rates or cut short the lengthy toll collection period. These can be achieved by eliminating the excessive profit of the concessionaires, and by refinancing or lowering the cost of debt through the issuance of cheaper debt papers based on the stronger credit rating of the government.

The lowering of toll rates can help mitigate the effect of further cuts in the petrol subsidies on the public and the logistic industries. This can be one of the many measures paving the way to gradually reduce the subsidy on retail petrol and diesel. The government cannot continue to pay such high subsidies in view of rising oil prices.

But having said that, the premise for the government to take over the toll roads is that it must ensure that the maintenance and operation of the toll roads must be made more efficient. It must also implement a more efficient capital structure in the toll road concessions. This will lower operating and financing costs hence lead to lower toll rates.

If the government can't improve overall efficiency, then it would be better if it did not take over the toll road concessions because the purpose of privatising toll roads, in the first place, was to promote efficiency but not at a huge expense to the people.

But having said that, how many of the existing highway operators can claim to be efficient?

Toll concessions are a complicated business. Returns are difficult to gauge or calculate because the details of the agreements are not made public by the government.

Most importantly, how the internal rate of return is arrived at when the concessions are

sealed is not known.

The IRR is based on the projected traffic flow and the toll that should be charged.

The profit of a toll road project does not just start from the collection of toll revenue, the annual financing costs of the highway as well as the associated maintenance and operating expenses — it begins with the construction of the highway itself.

The holder of a toll road concession often makes an immediate profit from the construction work by assigning jobs to associated and related companies at inflated margins.

Often, they prefer to worry about toll collection later. This is evident based on the varying cost per km incurred by each toll operator.

Due to the high construction costs, the concession holder reap big profits even before tolling starts.

And, if there is cost overruns, it become an excuse for the concessionaires to request higher rates, toll hikes, and longer concession periods.

PLUS Expressways Bhd, the biggest player in the toll road business, reported a pre-tax profit of RM773.3 million for the financial year ended Dec 31, 2004, on a turnover of RM1.65 billion. That is a whopping pre-tax profit margin of 46.9% after subtracting operating expenses as well as financing costs. There was no extraordinary profit during the financial year that drove up the profit.

Lingkar Trans Kota Holdings Bhd, the operator of the Damansara-Puchong Highway and the SPRINT Highway, reported a pre-tax profit of RM88.28 million against a turnover of RM226.71 million for the financial year ended March 31, 2005. Its pre-tax profit for FY2005 was affected by the opening of the new links in the SPRINT highway, on which traffic has yet to build up. In FY2004, its pre-tax profit was much higher at RM121.35 million, against turnover of RM212.05 million.

The government has made a mistake in allowing the concessionaires to incorporate such huge profit elements into the toll road projects. It is time to stop the mistakes from snowballing.

It may be cheaper to acquire these toll roads at their current valuation and forestall the long-term costs that the Malaysian public will eventually pay to "subsidise" the profits of the concessionaires. //

BY M SHANMUGAM



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The government would be taking a massive step backwards if it does take over toll concessions from highway operators.

In fact, there are at least five good reasons the government should not go back on its decision to privatise toll roads. First, it will involve the use of huge financial resources, which could be used to build alternative roads and other infrastructure.

Second, it will mean the government need not maintain highways in the country, which can also be an expensive affair in the long run. Third, the government would not then carry the risk of having to manage a bad highway or a stretch of road that does not meet traffic forecast.

Fourth, if the government nationalises all toll roads, it would be for the development of capital markets as there would be one less asset class to invest in. And lastly, why should the government bail out the unprofitable highway operators?

Yes, we are talking about highways that do not make money or provide adequate returns to its shareholders. Of the 26 highway concessionaires in the country, only those that operate older highways make decent returns because the traffic flow meets the forecast, given their maturity over time.

The bulk of new highways do not make money. The latest example of a highway in dire straits is Sunway Infrastructure's SILK Highway in Cheras/Kajang. It is possible that over time, SILK will meet its traffic forecasts. But in the immediate term it is in trouble.

Also, if the government decides to take back highways, it will only pave the way for the bankers, operators and others with interest to take the easy way out. The government will end up taking all the risk and other related costs involved in operating the highway, including the possibility of traffic shortfall.

For instance, what would happen if cracks appear on some of the highways a few years down the road? The government would certainly be able to absorb the cost, but is it worth the risk? For instance, when there was a landslide along the North-South Expressway (NSE) last year causing certain sections in Bukit Lanjan to be closed for several months, the

operator, PLUS, suffered losses from the drop in traffic flow. Why must the government be burdened with such a risk?

Highway maintenance is no easy task. At the moment, the prime responsibility for maintaining the highways lies with the concessionaires. And if they do not meet certain requirements, the government has the right to take the highways back, although they rarely do.

It also goes without saying that some of the best roads are the private roads. The NSE is easily one of the best-maintained roads in the country, arguably because it is in the hands of a private operator. And the cost is heavy. For instance, road surfacing and upgrades alone can go up to tens of billions of ringgit. A consultant estimated that the operating cost of PLUS, which includes resurfacing and repair works, could go up to RM60 billion over the next 20 years.

Taking about cost, taking over highways is no simple operation and will burn a big hole in the government's pocket. For instance, PLUS Expressways Bhd's market capitalisation stands at RM16.6 billion as at the close of the market last Friday. It has in its books debts of close to RM7 billion, which makes the total cost of its acquisition a whopping RM23.6 billion.

For RM23.6 billion, the government can not only improve and upgrade the existing alternative roads but also build another highway stretching from the northern tip to the southern end. At RM10 million per kilometre, the entire cost of a building a 900km freeway from Kangar to Johor Baru will only cost RM9 billion. This is much cheaper than taking over the toll concessionaires.

Perhaps the government could use the money to pay for the construction of new highways that are being planned. For instance, the RM3.2 billion West Coast Highway to be built by Kumpulan Europlus is a good alternative to the NSE and a project which can be borne by the government.

And what would be the impact of taking back the concession on the capital markets? Although the highway companies could continue to stay listed, it will only increase the holding of the government in strategic assets.

We already have naysayers critical of the stock exchange because the best and largest of the listed companies are tightly held by government entities. We certainly do not need to contribute further to the problem. Let the highways be run as they are. //

CROSSFIRE