

EDITORIAL - February 2006

Can Governments Be Trusted?

ESTONIA's bold action to privatise Estonian Railways (EVR) in 2001 could come to a sorry end this year as a result of a change in the law in 2003 and a hostile economy minister which are undermining EVR's viability. EVR was the first part of the former Soviet State Railways to be privatised and is the only railway in Europe to have been privatised as an integrated unit.



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The government sold 66% of the shares in EVR to Baltic Rail Services (BRS), retaining the remaining 34% stake. BRS is owned by two US railway companies, Railroad Development Corporation (RDC) chaired by Mr. Henry Posner III and Rail World, whose president and CEO is Mr. Ed Burkhardt, plus Emerging Europe Infrastructure Fund, Netherlands, and Ganiger Invest, Estonia.

EVR is predominately a transit railway carrying freight between the Baltic ports and Russia. Estonia competes for this traffic with Baltic ports in Russia, Latvia, and Lithuania. The Estonia part of a typical haul is very short. "Our greatest challenge is to influence Russian cargo flows despite having little influence over Russian tariffs," Posner said.

Estonia passed a new Railways Act in 2003, which dramatically changed the rules of the game for EVR. "It was passed under the guise of adherence to the European Union norms, but represents a far more punitive and confiscatory regime than can be found anywhere else in Europe, and is especially difficult for a private company," Posner explained.

An open access regime of 20% was agreed at the time of privatisation. The new law changed this to 100%. The Railway Inspectorate was set up, which determines access charges. To EVR's consternation, these have been set at below cost. So far, there are two open-access operators competing with EVR. They have 30% of the market. Two more will start operating in May. "Most of them are directly linked to freight owners in Russia, putting EVR in an especially difficult competitive position," Posner told IRJ. As a result, EVR made a loss in 2004.

Posner says the new access regime had the effect of confiscating much of the value that BRS paid for. To make matters worse, Mr. Edgar Savisaar, was appointed economy minister in April 2005. He is pro-Russian and anti-privatisation. He has blocked attempts by EVR to revalue its assets to reflect the investment made to date.

EVR has been threatened with a fine for failing to invest sufficiently and criticised for importing heavy US locomotives which some claim have damaged the track. Both these assertions are strongly refuted by Posner. At privatisation, BRS agreed to invest Kroons

2.57 billion (\$US 199.5 million) in EVR by the end of this year. "As of November 2005, Kroons 2.64 billion have been invested in EVR," Posner told IRJ. "This has allowed EVR to rehabilitate more track than originally foreseen." Altogether, 293km of track has been rehabilitated and the amount of track passed for 120km/h operation has increased from 120 to 300km. BRS is contesting the fine through the Estonian courts. EVR has also been fighting against the new access regime, so far unsuccessfully.

EVR purchased 74 used 29-tonne-axleload General Electric (GE) locomotives for \$US 60 million to replace the fleet of Soviet-era 2TE116 locomotives which had an axleload of 23 tonnes. Modifications were made to bridges to accommodate the GE locomotives. Posner says he has ridden over the entire EVR network, bar a 2km branch line. "I have seen no evidence of deterioration of our infrastructure since the GE locomotives began operation. To the contrary, I ... can attest that our infrastructure has never been in a better condition."

BRS has been approached by the state-owned port of Tallinn to purchase some or all of its shares in EVR. As Posner explained, the sale will depend on whether the price reflects the investment made so far, and whether "the foreign shareholders are interested in staying in a country which has made it clear that they are no longer welcome." Burkhardt summed up the situation well: "My experience is that if a government makes a deal, the next government will comply with it. This is a norm around the world, but seems not to be in Estonia." **IRJ**

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