Transnet National Ports Authority
Tariff Application FY 2014/15
Ports Regulator Road Shows

30 September 2013 – 04 October 2013

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- NPA Strategic Focus – aligned to Transnet MDS
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NPA Strategic Focus – aligned to Transnet MDS

NPA Strategic Focus – aligned to Transnet MDS

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Strategic Intent

"To enable the effective, efficient & economic functioning of an integrated port system to promote economic growth"

Driven by a 3-tier strategy and 6 goals

NPA 3-tier strategy	NPA Strategic Objectives	
Create & manage Infrastructure capacity ahead of demand	1. Effective port system 2. Economic port system	6. Organizational capacity / readiness
Improve Port efficiencies (oversight role)	3. Efficient port system 2. Economic port system	
Enhance the ports' position as integrated gateways for trade	4. Integrated port system. 5. Grow the market	

Aligned to Transnet MDS strategy

Capital Investment

Create & manage Infrastructure capacity ahead of demand

- Effective port system
- Economic port system

Volume growth

Enhance the ports' position as integrated gateways for trade

- Integrated port system
- Grow the market

Operational Efficiency &

Improve Port efficiencies

- Efficient port system
- Economic port system

Financial sustainability

Capital Delivery + Service Levels +Integration = Increased Volumes, Revenue and contain Costs

Strategy embodies the landlord functions set out in the Ports Act

Transnet MDS alignment with Government

Transnet R300bn capex program is essential to SA's economic growth and development strategy – ***Honorable President Jacob Zuma***

As a SOC, Transnet is required to align its strategic orientation and technical capacity with the requirements of the developmental state

Shareholder Statement of Strategic Intent

- *Reduce cost of logistics as a percentage of transportable GDP;*
- *Effect and accelerate modal shift by maximising the role of rail in the national transport task;*
- *Leverage the private sector in the provision of both infrastructure and operations where required;*
- *Integrate South Africa with the region and the rest of the continent; and*
- *Optimise the social and economic impact of all interventions undertaken by the Company in the achievement of the above objectives.*

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Functions of the Authority

Core Functions of Port Authority - Ports Act Section 11

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Landlord	Promote the use, improvement and development of ports, and control land use within the ports, having the power to lease port land under conditions it determines.
Master planner	Plan, improve, develop and maintain port infrastructure.
Controller of ports navigation	Make and apply rules to control navigation within port limits and approaches, ensure protection of the environment and ensure safety and security within port limits.
Controller of ports services & facilities	Ensure that port services and facilities are provided, and may enter into agreements or licence other parties to provide these.
Marketer & administrator	Ensure that adequate, affordable, equitable and efficient port services and facilities are provided for port users.
Change agent	Ensure non-discriminatory, fair, transparent access to port services and facilities; advancement of previously disadvantaged people; promotion of representivity and participation in terminal operations; enhanced transparency in port management.
Coordinator with other state agencies	Advise on all matters relating to the port sector, and liaise with all stakeholders.

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Services within the Ports

Services provided within the Ports

Other services to the cargo:
- Warehousing / cargo storage
- Cargo repairs
- Equipment rental
- Cartage (road / rail)
- Cargo inspection, storage and grouping

Other services in the port:
- Bus services
- Baggage handlers
- Fire fighting
- Fire protection
- Security
- Power and water supply
- Labour Provision
- Pollution control
- Clearing / forwarding

SECURITY

- **Aids to Navigation along the coast**
- **Vessel Traffic System, safety of Environment, port control**
- **Provision of basic port infrastructure and Aids to navigation within ports**
- **Dredging**
- **Pilotage**
- **Tug Services**
- **Berthing / Unberthing services**
- **Stevedoring (Cargo handling on board)**
- **Cargo Handling on quay**
- **Other cargo handling services**
- **Transport to / from storage**
- **Storage**
- **Delivery / Receiving via road / rail**

IMPORT CARGO

EXPORT CARGO

Other services to ships:
- Ship building and repairs
- Ship surveyors
- Bunkers
- Ship chandlers
- Hull cleaning
- Prop shining
- Pest control and fumigation
- Fire fighting
- Security
- Waste disposal
- Floating crane
- Radio / radar
- Vessel searchers
- Ships agents

THE AUTHORITY'S SERVICES

OTHER SERVICE PROVIDERS

CARGO FLOW

Adapted from the United Nations Conference on Trade and Development

Services provided within the Ports (continued)

Port Infrastructure		Revenue Stream
Port land and Terminals	Lease port land to terminal operators and other port service and port facility providers in the port(s).	Lease income (rentals)
Wet infrastructure	Lighthouse services infrastructure (lighthouses, buoys, beacons and electronic / radio navigation equipment) , port control and safety, entrance channels, breakwaters, turning basins, aids to navigation within port limits, vessel traffic services, maintenance dredging within ports.	Light dues, port dues, vessel traffic services fees
Dry infrastructure	Quay walls, roads, rail lines, buildings, fencing, port security, lighting (outside terminals), bulk services and in certain cases terminal infrastructure	Cargo dues, berth dues
Ship repair services	Provide and maintain ship repair facilities as well as the cranes utilised in such facilities.	Preparation fee, docking and undocking fees (vessels at repair facilities), Berth dues (vessels at repair quays)
Marine services	Pilotage, tug assistance, berthing, running of lines, floating cranes	Pilotage dues, tug assistance fees, berthing fees, running of line fees, floating crane hire fees

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Regulation of Port Services and Facilities

Regulation of Port Services and Facilities

- The Authority exercises such control in accordance with the provisions of the Act, by means of agreements, licences and permits.

Section 56(1) agreements

- Terminals (at end of current contracts & new)
- Future ship repair facilities
- Future off-shore cargo handling facilities

Section 65(5) and 65(3) licences

Existing operators of:

- Cargo terminals
- Waste disposal
- Private floating cranes

Section 57 licences

- Stevedoring
- Waste disposal
- Private floating cranes
- Existing off-shore cargo handling facilities (s66 – at end of current

Port Rule licences and registrations

Licences:

- Fire protection and maintenance services
- Diving
- Bunkering
- Pollution control
- Pest control
- Registrations:
- Agents (ships, clearing and forwarding)

Port Rule special longer-term access permits

- Road transport operators
- Rail transport operators
- Bus services and bus tour operators
- Labour brokers
- Vessel contractors
- Vendors

High ← Degree of Regulation → Low

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Port Investment Planning

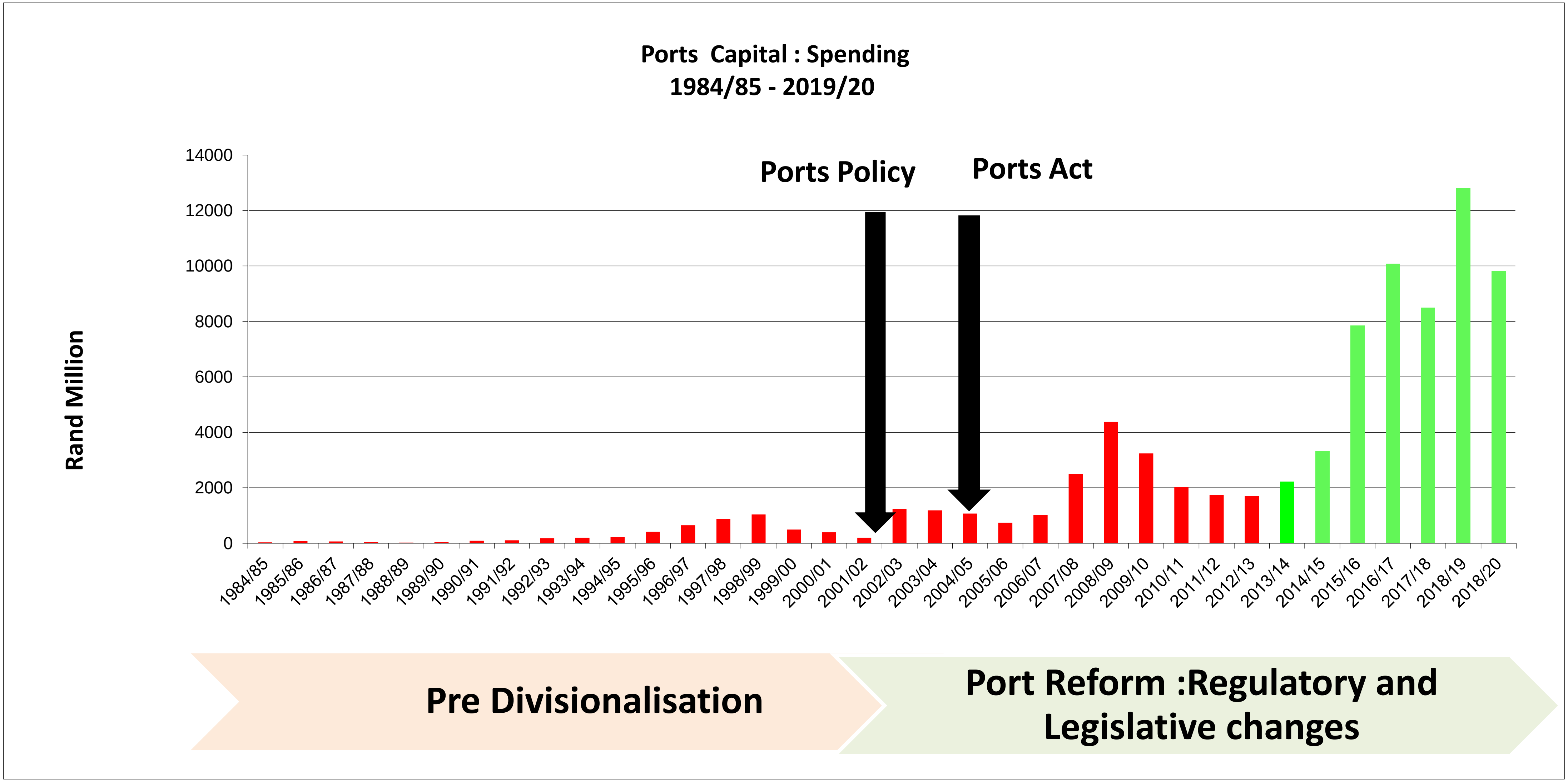
Port Investment Planning

The main function of the Authority is to ***own, manage, control*** *and* ***administer ports*** *to ensure their* ***efficient and economic*** *functioning, and in doing so the Authority must —*

a) plan, provide, maintain and improve port infrastructure;
b) prepare and periodically update a port development framework plan for each port, which must reflect the Authority's policy for port development and land use within such port;
c) control land use within ports, and has the power to lease land under such conditions as the Authority may determine;
d) provide or arrange for road and rail access within ports;
e) arrange for such services such as water, light, power and sewerage and telecommunications within ports;
f) maintain the sustainability of the ports and their surroundings;'

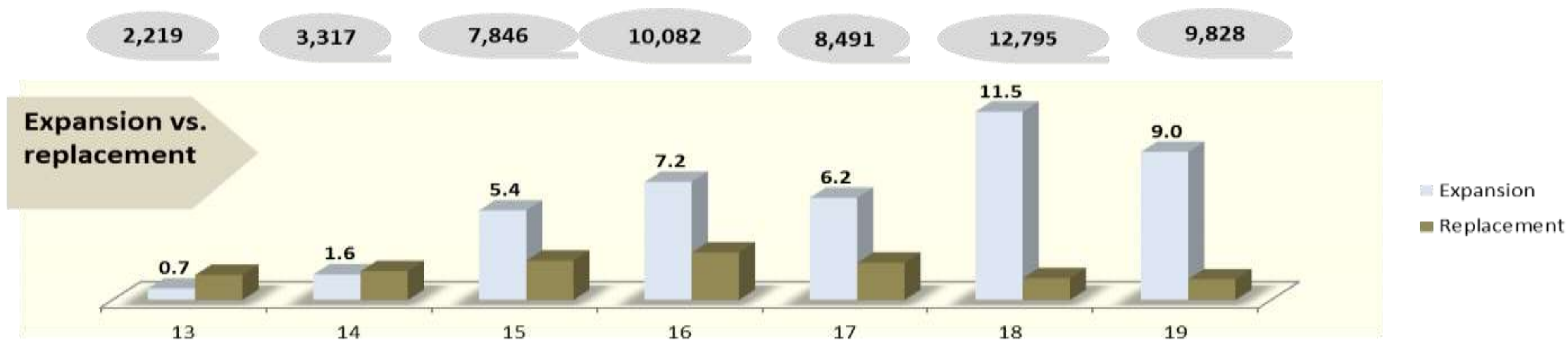
Ports Act section 11

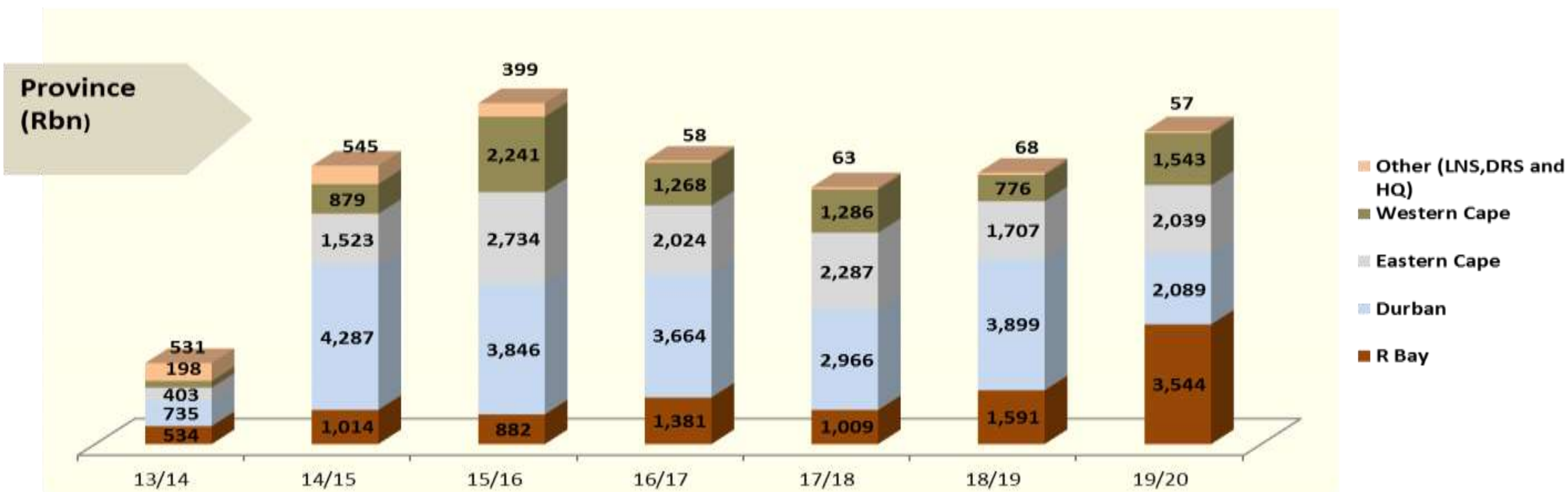
Port Investment Planning (Capital spending at Ports : Pre and Post Port Reform)



Port Investment Planning

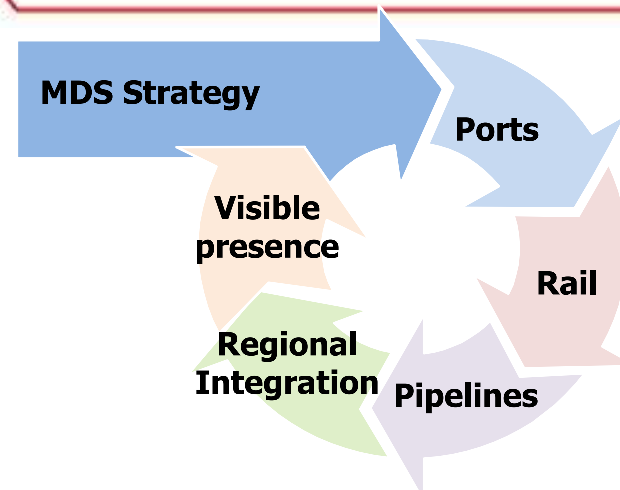
The Authority's Capital plan is R57.6bn of the Transnet MDS R307.5bn Capex Programme.





Port Investment Planning (continued)

		Estimate 2013/14 Rm	Draft 2014/15 Rm
Re-engineering, Integration, Productivity and Efficiency	To maximise return on investments by obtaining additional volumes	492	1267
	To maximise return on investments by improving operating efficiencies	351	683
	To preserve current revenue streams without obtaining additional volumes (i.e. revenue protection)	1037	895
Safety, Risk and Effective Governance	Ensure Safety Optimisation	202	383
	Optimise Business Enterprise Offerings	81	26
	Optimally Satisfy Social Investments(non economic value creating projects)	-	1
	Environmental	3	45
Human Capital	Optimise Human Resources	54	17
Total (excl.borrowing cost)		**2219**	**3317**



Asset Type	Estimate 2013/14 Rm	Draft 2014/15 Rm
Buildings & structures	653	729
Land	1	17
Machinery, equipment, Furniture	204	137
Permanent way and works	28	122
Vehicles, rolling stock & containers	-	3
Port facilities	1334	2310
Total (excl.borrowing cost)	2219	3317

Major Capital Projects FY2013/14 to FY2019/20

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Durban Container Terminal	Deepening of Pier 2 berths -16 CD Reclamation of 17 ha between Pier 1 and Salisbury Island Construction of quay wall on eastern side of Pier 1 Container Terminal
Cape Town Container Terminal	Expansion of terminal to 1.4m TEUs and provide platform for further expansion
Port of Ngqura	Operationalisation of the port
Bulk	Increase SLD Iron Ore capacity from 60mtpa to 82mtpa 12mtpa Manganese Terminal at the port of NGQ RBAY Replacement and Refurbishment program- additional stack capacity Coal handling facility at ELON LNG Terminal at NGQ LPG Terminal at SLD
Break Bulk	Reconstruct sheetpile quay walls at DBN Maydonwharf MPT berthing capacity in RBAY Extension of Mossgas quay including dredging works
Fleet Replacement	Fleet Replacement ito Tug Boats, Pilot Boats, launches and Dredgers

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Tariff Application Approach

Tariff Application Approach

- The Port Directives were approved on 13 July 2009 (gazetted on 06 August 2009) and amended on 29 January 2010.
- Directives require the Regulator to ensure that the Authority's tariffs allows it to:
  - recover its **investment;**
  - recover its **costs;**
  - make a **profit** commensurate with the risk.

Regulatory Framework

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- The regulatory framework does not set a Tariff Methodology.
- The Authority's proposed Tariff Methodology has been consulted with stakeholders and is currently under review by the Ports Regulator.
- The Authority is of the view that its Tariff Methodology position paper is appropriate for tariff determination purposes.
- The proposed methodology addresses the financial sustainability of the Authority and Transnet especially during the critical years of the Transnet MDS.
- The Regulator, whilst considering the Authority's proposal issued an interim Regulatory Manual, applicable to the 2014/15 tariff year.
- The tariff application for FY 2014/15 has been prepared on the basis of the guidelines contained in the interim Regulatory Manual.

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Tariff Application

Tariff Application

The Interim Regulatory Manual prescribes the following Required Revenue (RR) formula:

Revenue Requirement

= Regulatory Asset Base (RAB) X Weighted Average Cost of Capital (WACC) + Operating Costs+ Depreciation + Taxation Expense – (+) Claw back +(-) Excessive Tariff Increase Margin Credit (ETIMC)

Key Principles of the Interim Regulatory Manual

- The key principles included in the Regulatory Manual are as follows:
  - ***Regulatory Asset Base (RAB)***: The value of total assets in the RAB is indexed to inflation each year - the Trended Original Cost ("TOC") approach.
  - ***Vanilla Weighted Average Cost of Capital (WACC):*** A real Weighted Average Cost of Capital will be applied, given that the RAB is indexed for inflation.
  - ***Operating Costs:*** Detailed and complete motivation for the expenses applied for is required.
  - ***Depreciation:*** The depreciation of the assets in the RAB will be calculated as straight line, 40 year depreciation on the opening balance of the RAB.
  - ***Taxation Expense:*** The Regulator will use the pass-through tax approach where the vanilla WACC will be applied to the average RAB.
  - ***Claw Back:*** The Regulator will spread the total impact of over/under recovery of revenue over a period of two tariff determinations.
  - ***Excessive Tariff Increase Margin Credit (ETIMC):*** The Regulator considers it prudent to avoid future tariff spikes by retaining and increasing the NPA's Excessive Tariff Increase Margin Credit (ETIMC).

Required Revenue calculation inputs

Regulatory Asset Base (RAB)

- Valuation of the RAB takes into consideration depreciation, inflation trending, capital work in progress (CWIP) and working capital:

RAB VALUATION	FY 2014/15 R'm
Opening Net Book Value	63,120
NBV Inflated	66,844
Less: Depreciation	-1,671
Add: Capex	3,317
Closing NBV	68,490
Average Opening and Closing	65,805
Less: Working Capital	-1,111
RAB Final	**64,694**

Required Revenue calculation inputs (continued)

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Weighted Average Cost of Capital (WACC)

- Vanilla WACC as prescribed by the Regulator translates to 5.83%.

WACC	FY 2014/15 R'm
Risk-free rate (nominal)	8.32%
Real risk free rate	2.29%
MRP	7.10%
Asset beta	0.5
Equity beta (using Hamada)	0.86
Gearing	50.00%
WACD (nominal)	9.34%
Inflation	5.90%
Tax rate	28.00%
Cost of equity (real)	8.40%
WACD (real, pre tax)	3.25%
	5.83%

Required Revenue calculation inputs (continued)

Taxation

- The Revenue Requirement formula considers tax expense to be a pass-through cost.

Tax	FY 2014/15 R'm
Gross Income	**8,717**
Pre Tax debt return	*-*
Equity return on RAB	*2,717*
ETIMC	*-*
Depreciation	*1,671*
Opex	*4,329*
Deductions	**6,000**
Depreciation	*1,671*
Opex	*4,329*
Taxable Income	**2,717**
Gross up for tax	3,774
Tax at 28%	**1,057**

Required Revenue calculation inputs (continued)

Operating Expenditure

The total operating expenditure is highlighted below:

	Budget 2013/14 R Million	Forecast 2014/15 R Million	Deviation % 2013/14 VS 2014/15
Labour Costs	1 781	1 943	9.1%
Rates & taxes	250	264	5.6%
Maintenance	355	367	3.5%
Contract Payments	65	68	4.5%
Energy	445	485	9.1%
Professional services	37	39	4.7%
Material	97	94	-3.7%
Computer & Info systems	81	86	5.5%
Rental	60	68	13.5%
Security costs	68	73	6.9%
Research & development	82	72	-12.8%
Sundry operating costs	215	179	-16.9%
Total operating cost (excluding depreciation)	3 537	3 738	5.7%
Group Costs	653	591	-9.5%
Total operating cost (Including Group Costs)	4 190	4 329	3.3%

Required Revenue calculation inputs (continued)

Clawback

- The clawback relates to differences between allowed revenues and actual revenues

Recomputed Revenue requirement FY 2012/13	FY 2012/13 Recomputed	
Using ROD of FY 2012/13 (before Clawback of R1.4bn and ETIMC of R900m)	R'm *	R'm
RAB	57,779	
WACC	6.1%	
Return		3,542
Opex (AFS 2012/13)		3,109
Depreciation		1,472
Tax		950
		9,073

- The R9 073m is the recalculated revenue requirement for FY 2012/13.

Required Revenue calculation inputs (continued)

The value calculated for FY 2013/14 is as follows:

Actual Clawback FY 2012/13	R'm	R'm
Revenue Requirement (FY 2012/13)		9 073
Less: Clawback taken		**-1 440**
Act Mar'11 Clawback calculated	*874*	
Clawback Estimated Mar '12	*566*	
Add: ETIMC		**900**
RR before Clawback and ETIMC		8 533
2012/13 AFS Revenue		9 058
Final Clawback Mar '13		-525
Provisional taken in ROD 13/14		447
RESIDUAL CLAWBACK MAR '13		**-78**

Estimated Clawback 13/14	R'm
Allowed Revenue per ROD 13/14	9 838
Latest Estimate 13/14	9 437
Estimated Clawback 13/14	401
@ 50%	201
TOTAL CLAWBACK TO BE RECOVERED MAR 15	
Residual Clawback o/s Mar13	-83
Estimate Mar 14	201
Net Clawback	**118**

- As per the Regulatory Manual, the residual clawback of R78m is indexed by a finance cost equivalent to the WACC to give a total residual clawback of R83m.
- Estimate clawback for FY 2013/14 equates to R401m (revenue per ROD R9.8bn less latest estimate of revenue R9.4bn)

Required Revenue calculation FY 2014/15

Revenue Requirement	FY 2014/15 R'm
RAB	64,694
Real Post WACC	5.83%
Return on Capital	3,772
Plus: Depreciation	1,671
Plus: Operating Expense	4,329
Plus: Taxation Expense	1,057
Plus: Clawback	118
Revenue Requirement	10,947
Less: Real Estate	-2,113
Marine Revenue	**8,834**

The application of the Regulatory Manual Results in a Total Revenue Requirement of R10 947m, comprising of:

- Marine business: R8 834m
- Real Estate :R2 113m

Volume Growth FY 2014/15

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The Authority's estimated average volume growth for FY 2014/15:

REVENUE	2013/14 Revenue Budget (Nil % tariff increase) Rm	2014/15 Revenue:Before Tariff Increase Rm	2014/15 Revenue Volume Increase Rm	2014/15 Weighted Average Volume Increase %
Containers	3406	3535	129	3.8%
Break Bulk	291	285	-6	-2.1%
Dry Bulk	848	924	75	8.9%
Liquid Bulk	560	569	9	1.6%
Automotive	546	574	28	5.1%
TOTAL CARGO DUES AFTER REBATE	**5650**	**5886**	**236**	**4.2%**
Marine & other revenue	1812	1834	22	1.2%
TOTAL TARIFF BOOK REVENUE	**7462**	**7720**	**258**	**3.5%**
Real Estate Revenue	1975	2128	154	7.8%
TOTAL REVENUE	**9437**	**9848**	**412**	**4.4%**

Tariff adjustment FY 2014/15 (continued)

Marine Business revenue for FY 2014/15 of R8 834m is compared to estimated revenues for FY 2013/14 of R7 462m and increased for the average estimated growth in volumes of 3.5%

Marine Revenue	FY 2014/15 R'm
Latest Estimated Revenue for FY 2013/14	7,462
Estimated Volume Growth for FY 2014/15	3.50%
	7,723
FY 2014/15 Required Revenue	8,834
Tariff Increase	14.39%

NPA's Tariff Application

- The need for a tariff increase must be balanced together with the following objectives of Transnet:

  - Role of facilitating economic growth
  - Commitment to reducing the cost of doing business in South Africa.

- The Authority has therefore considered an approach to ensure a sustainable tariff increase which is in the interest of the economy.

- The Authority has assessed its financial needs in relation to MDS initiatives for FY 2014/15

- The Authority can be sustained with a revenue of R10 493m for FY 2014/15 comprising of Marine revenue of R8 380m and Real Estate revenue of R2 113m

- This would entail releasing R454m of the ETIMC provision previously created.

Marine Revenue	**R'm FY 2014/15**
Marine Revenue Required	8,834
Less ETIMC	454
Marine Revenue for FY 2014/15	8,380

NPA’s Tariff Application (continued)

- The Authority therefore applies to the Regulator for a revenue of R10 493m comprising of:

  - Marine business: R8 380m
  - Real Estate: R 2 113m.

- This translates to an average overall tariff adjustment of 8.5%.

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Pricing Strategy

NPA's proposed pricing strategy tries to accomplish several objectives

1 Sustainable

- Allows for ongoing investments to maintain and extend the SA port system appropriately

2 Comprehensive

- Provides sufficient detail for regulation
- Covers all Required Revenues
- Addresses all charges
- Clarifies all pricing modifiers

3 Defendable / compliant

- Based on clear principles
- Aligned with regulatory directives and expectations of the Ports Regulator
- Supported by a robust methodology

4 Simple

- Enhances ease of understanding and administration
- Rationalises charges
- Simplifies charges for port users

5 Competitive

- Comparable to other global ports
- Protects market share
- Supports SA economic development
- Fair on all port users
- Allows for competition within ports

6 Implementable

- Complies fully with legal and regulatory requirements
- Addresses impact on customers

Source: TNPA pricing strategy project

Objectives were translated into pricing principles

Design principles	Description	Application
Cost recovery	Each tariff should recover the cost of infrastructure and services provided	Cost recovery at port system level, not individual ports
User pays	Each port user should contribute for use of port facilities and services	Port users include shipping lines, terminal operators, cargo owners
Required Revenue	Revenue driven by tariff methodology on a disaggregated level	Individual tariffs set to meet Required Revenue at expected volumes
Competitiveness	Market implications of new tariff structure considered	Market expectations, best and common practices considered

Source: TNPA pricing strategy project

Proposed tariff structure results – long term – in balanced distribution of charges across port users

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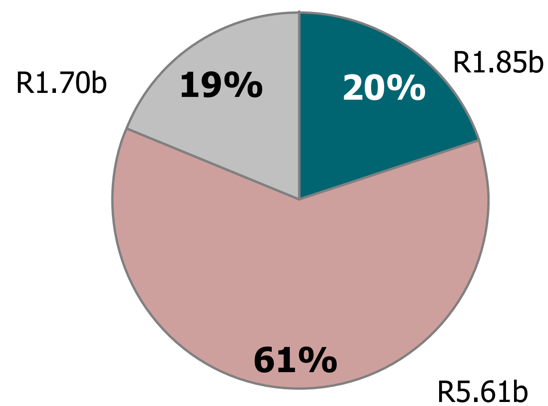
All numbers based on 2012/13 budget Required Revenue

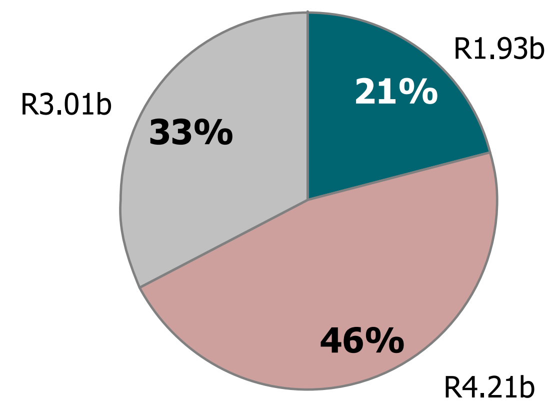
- Shipping lines
- Cargo owners
- Tenants

Current tariff structure



Proposed tariff structure

Indicative Tariffs to be updated



High level assessment	Current tariff structure	Proposed tariff structure
	Weak justification for tariff levels ✗	Based on defendable principles and approach ✓
	Rental too low for landlord port ✗	Charges to tenants aligned with international norms ✓

1. E.g. maintenance dredging
Note: Excludes Required Revenue, cost and assets allocated to the group "Other "
Source: TNPA cost model

Introduction of Beneficiation Promotion Programme (BPP) fully aligned with national priorities

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National priorities with key policies

	Key policy objective
Industrial Policy Action Plan 2012- 2015	1. Promotion of beneficiated products 2. Labour intensive growth 3. Economic diversification 4. Movement towards knowledge economy
New Growth Path	1. Create 5m jobs by 2020 via labour intensive economic growth 2. Focus on areas with potential to create large scale employment
Beneficiation Strategy for Minerals Industry	1. Optimise value chain linkages 2. Job creation 3. Industrialisation 4. Economic diversification
DTI Metals Sector Strategy	1. Improve global competitiveness 2. Enhancement of exports 3. Attract local and foreign investments 4. Maintain and create new employment 5. Encouragement of BBBEE

Proposal to adopt DTI beneficiation framework

	Stage 1	Stage 2	Stage 3	Stage 4
Metals sector description	Ore or concentrate	Processed or refined ore	Primary manufacture	Final manufacture
Industrial activity	• Mining • Production of ore & concentrate	• Smelters & refineries • Convert into bulk tonnage intermediate products	• Blast furnaces & foundries • Convert into refined semi-fabricated product	• Manufacturing factories • Finished product
Economic benefits	• Medium level of employment • No value add	• Low employment levels • Significant value add	• Higher employment levels • Substantial increase in value add	• Significant increase in employment levels • Significant value add
Generic description	Raw material	Processed/ refined raw material	Primary manufacture	Final manufacture
Examples				
Textile	Cotton fibre	Yarn	Woven fabric	Clothing item
Iron & Steel	Iron ore	Pig or cast iron	Wrought iron	Steel product
Food	Wheat	Basic wheat flour	Processed flour	Bread
Furniture	Timber logs	Cut timber pieces	Seasoned wood	End state furniture
Leather	Animal skin or hide	Tanned leather	Lubricated & dyed leather	Finished leather good

Cooperation with DTI required to apply beneficiation framework to other sectors than minerals and metals

Source: TNPA pricing strategy project

Update on Pricing Strategy

- Consultation of the NPA's proposed Pricing Strategy was held in March 2013
- Stakeholder comments/ questions and NPA's responses have been made available to the Regulator
- It is anticipated that the Regulator will make a final decision on NPA's proposed strategy shortly
- For FY 2014/15, individual tariffs (tariff book) will be informed by the Regulator guideline which will be issued post the current tariff determination process.

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Port Efficiency

Port Efficiency

The Authority has been repositioned through a comprehensive operations strategy defined by three broad spheres:

- Port performance monitoring based on pre-determined levels of productivity,
- Implementing the Authority's mandate at port level and
- Optimisation of existing port capacity.

Strategy will be executed by issuing Terminal Operator Performance Standards (TOPS) to all 90 licenced terminal operators.

TOPS is informed by factors such as terminal capacities, demand and commercial arrangements, amongst others.

Port Operations Centres has been established at all Ports to:

- track and monitor performance
- continuously improve port efficiency, productivity and performance.

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In accordance with the interim Regulatory Manual for the FY 2014/15 the Authority hereby applies to the Regulator for revenue of R10 493m comprising of:

- marine business revenue of R8 380m; and
- real estate business revenue of R2 113m

This translates to an average overall tariff adjustment of 8.5%

This revenue is necessary in order for the Authority to:

- recover its investment;
- recover its costs;
- make a return commensurate with the risk; and

Thereby sustainably fulfill its role and deliver on its objectives ito the Transnet MDS

The End