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Mexican Government Awards Concession for Lucrative Northeast Rail Route

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In early December, the Communications and Transportation Secretariat (SCT) announced the concession of the northeast rail route to Transportacion Ferroviaria Mexicana (TFM), a consortium formed by shipping conglomerate Transportacion Maritima Mexicana SA (TMM) and US-based railroad company Kansas City Southern Industries (KCSI). The consortium paid almost 11.07 billion pesos (US$1.4 billion) for the 50-year concession, which was nearly three times higher than the next bid of 4.27 billion pesos (US$541 million) offered by Grupo Ferroviario Mexicano, a subsidiary of the mining company Grupo Mexico. A third partnership composed of Mexican engineering company Constructoras ICA, SBC International Railways, and Union Pacific Railroad offered the only other bid, at 4.16 billion pesos (US$527 million).

Two other potential bidders the US-based railroad Illinois Central Corporation and a consortium led by French company GEC-Alsthom had remained in the running until days before the concessions were awarded. But these two bidders failed to meet all the government's requirements, including at least 51% Mexican participation in their venture, and were thus disqualified from the final concessions. The Mexican government temporarily retained a 20% share of the northeast rail line. That stake will be converted to stocks for sale on Mexican and foreign stock exchanges.

In addition to the fee for obtaining the concession, TFM agreed to pay the federal government 0.5% of gross revenues for the first 15 years of the concession and 1.25% thereafter. TFM also pledged to spend 4.82 billion pesos (US$610 million) over the next 10 years to boost the efficiency of the railroad and promote a growth rate of 15.6% in traffic along this rail route between 1997 and the year 2006.

In an interview with United Press International, KCSI's Chief Executive Officer, Landon Rowland, projected that the volume of freight on the northeastern line could increase by 18% to 20% per annum during the next several years. At present, only about 12% of Mexico's total freight traffic moves by rail. The northeast rail line which runs from Nuevo Laredo, Tamaulipas state, to Mexico City is one of the most frequently used routes to transport products from the US- Mexico border to the Mexico City metropolitan area. The route, which spans almost 4,300 km, handles about 70% of the goods imported by rail. The railway ships 60% of Mexico's grain imports and 90% of imported autos and auto parts.

Arturo Garcia Torres, an executive with the state-run railroad company Ferrocarriles Nacionales (FERRONALES), said privatization of the route is essential for Mexico from a strategic standpoint. "Lowering shipping costs is necessary to be competitive on an international level, especially with our North American Free Trade Agreement (NAFTA) partners," said Garcia, who was the FERRONALES executive in charge of the northeast route. The northeast route is considered key to improving the movement of freight across the US-Mexico border.

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According to the plan presented by TFM, the northeastern rail line would connect at Laredo, Texas, with the Texas- Mexican Railway, which is also jointly owned by TMM and KCSI. The Texas-Mexican Railway would then connect with KCSI trains at interior points in Texas, shipping products through the midwestern US to Chicago and Canada. The potential to connect rail service from Canada to Mexico has led some officials to describe the new network established by TMM and KCSI as the "NAFTA Railway."

"The NAFTA railroad will be extremely powerful...more so in Mexico, where there is a lack of anything like an interstate highway network," KCSI's Rowland said in an interview with United Press International. Still, some transportation analysts are skeptical that rail traffic within the NAFTA countries will increase significantly, given the small size of KCSI's operations within the US. "Who would have thought that such an important transportation means for US-Mexico trade would end up in the hands of such a small participant?" said transportation specialist James Higgins of the financial services company Donaldson, Lufkin & Jenrette. Higgins and other transportation analysts had expected the SCT to award the bid for the northeast railroad route to the Union Pacific-ICA-SBC railways partnership. Union Pacific controls about 30,000 miles of track in the US, compared with only 2,900 miles of track for KCSI.

On the Mexican side, however, TMM is apparently a more suitable company for the privatization than Union Pacific's partner Grupo ICA. According to the daily newspaper El Economista, TMM has managed to obtain concessions for several lucrative transportation-related properties privatized by the government in the last two years. In addition to the northeast FERRONALES route, TMM has obtained concessions to manage the container-shipping facility at the Pacific Port of Manzanillo, as well as the port-management units at Acapulco and Puerto Vallarta. TMM director Juan Carlos Merodio said the acquisition of the northeast railroad will allow the company to expand its intermodal transportation service, connecting rail and truck transport with the seaports of Lazaro Cardenas in Michoacan state, Veracruz, and the ports of Tampico, Altamira, and Matamoros in Tamaulipas.

In addition, the rail line traverses the industrial cities of Monterrey and Queretaro. The privatization of the northeast rail line is expected to leave some current employees without a job, since TMM and KCSI have announced intentions to reduce the 8,000-person work force. In fact, TFM executives have already initiated a series of meetings with the railroad workers union (Sindicato de Trabajadores Ferrocarrileros de la Republica Mexicana, STFRM) to determine which jobs will be retained. The two sides are also discussing a new collective-bargaining agreement. According to FERRONALES director Luis de Pablo Serna, TFM anticipates rehiring current employees for the positions that are retained. He said some workers who are laid off will be offered new jobs with FERRONALES. The sale of the northeast line is the first successful privatization of a FERRONALES property.

In September of this year, the SCT suspended the privatization of the Chihuahua- Pacific rail line (CH-P) because two of the three qualifying bidders withdrew from the process (see SourceMex, 10/09/96). The remaining participant, Grupo Mexico, offered too little money for the concession, forcing the SCT to postpone this privatization. According to the SCT, bids will be reopened for the CH-P railroad sometime in January. [Note: Peso-dollar conversions in this article are based on

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the Interbank rate in effect on Dec. 11, reported at 7.89 pesos per US$1.00] (Sources: La Jornada, 11/26/96, 12/06/96; The News, 11/27/96, 12/06/96; Reuter, 11/21/96, 12/03/96, 12/05/96; United Press International, 12/06/96; El Financiero International, 12/02/96, 12/09/96; Associated Press-Dow Jones News Service, 12/09/96; Excelsior, 11/26/96, 12/10/96; El Universal, 12/02/96, 12/06/96, 12/10/96; El Economista, 12/03/96, 12/05/96, 12/09/96, 12/10/96)

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