Bus Fleet Renewal in Developing Countries: The experience of LAC
Presentation Structure

Paratransit service provision in LAC Cities

Business practice to support bus fleet renewal

Fleet renewal and bus financing challenges

New business models for fleet renewal and bus service provision

Conclusions
Paratransit service provision in LAC Cities
Significant progress has been achieved in areas of bus fleet renewal. Most of this achievement has involved an important level of formalization (using PPP-type schemes)

- ~ 200 cities with BRT systems worldwide
- Several cities with bus renewal programs for non-BRT interventions (CDMX, Guadalajara, Monterrey)

Bus interventions in several developing countries have typically followed a functionally disintegrated approach, disaggregation of a project into different contracts for different components

- Early success of TransMilenio in Bogotá, Colombia and Metrobus Line-1 in Mexico City have led to that model being replicated in other urban bus reforms
Business practice to support bus fleet renewal
Soft and hard measures needed to support bus fleet renewal

- Transport Authority
- Legal & Institutional Reforms
- Technical Studies
- Dedicated Infra & Technology
- Financial Vehicle (Trust Fund)
- Operator & Corporate Governance

Rolling stock
Soft and hard measures needed for creditworthiness evaluation

- **Transport Authority**
  - Ensures service is provided following service standards / limits informal competition

- **Legal & Institutional Reforms**
  - Enables conditions for service to be provided (concession/permit)

- **Technical Studies**
  - Provides technical basis for service (demand, OPEX, CAPEX requirements)

- **Dedicated Infra & Technology**
  - Improve services, help to optimize OPEX, service exclusivity, prevents revenue leakages

- **Financial Vehicle (Trust Fund)**
  - Ensures payment of obligations

- **Operator & Corporate Governance**
  - Ensure best-practices in corporate governance practices

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**Rolling stock**
Despite efforts of formalization, many bus projects have struggled to attract private sector participation, and often fail to achieve long-term sustainability

- Lower than expected demand with lack of subsidies and inability to generate alternative revenue sources
- Gains from economies of scale in formalization do not entirely offset increases in operating expenditures (OpEx) and capital expenditures (CapEx)
- Corporate governance is unknowledgeable regarding improvements needed to address inefficiencies post-implementation

The COVID-19 outbreak exposed many financial vulnerabilities, especially in permit-based conventional bus systems

- Majority of public transport experienced significant reduction in demand levels
- Debt service for formalized transport systems were renegotiated in most cases
Fleet renewal and bus financing challenges
Limited Appetite from Commercial Banks to Finance Fleet

International Banks do not consider these projects BANKABLE

- Small sized projects
- High level of risk and complexity
The Role of Bus Manufacturers Financial Arms

- Bus manufacturers provide financial options to bus operators.
- These manufacturers typically offer financial service to operators that manage large fleets.
- Cash flows are evaluated, and buses are used as collateral (there is a secondary market).
- In some cases, they require a partial guarantee.

**Credit Conditions**

- Interest rate: above what commercial banks can offer
- Maturity and grace period can be negotiated
- Equity is also financed or negotiated

**Suboptimal conditions**

- Rolling stock being selected based on which bus manufacturer can offer better financial conditions
- Cost of Capital for these bus manufacturers’ financial arms are very uncompetitive
### Local Commercial Banks

- Local commercial banks tend to understand local markets
- These banks evaluate cash flows and the corporate’s balance sheet (if any)
- Corporate assets and buses as utilized as collateral (although, buses as collateral do not have an impact on risk reduction; banks are not "bus dealers")
- Partial guarantee is required in some cases (where there is market)

### Credit Conditions:

| ✓ Interest rate: more expensive compared to larger/international banks |
| ✓ Include the cost of a partial guarantee |
| ✓ Limited maturity term: 6 years |
| ✓ 6 months grace period |
| ✓ 10-20% equity |

### Suboptimal conditions

- Expensive
- Only available when the operator can prove credit history and has other assets that can be used as collateral.
- These assets are locked and cannot be used for any other financial operation

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**THE WORLD BANK**

**Vehicle for Infrastructure Investment Support**

- Local Commercial Banks
In Paratransit service provision, private operators bear commercial risk that depend on the public authority.
### Strengths

- Is fundamental for the mobility of millions of urban residents
- Offers a wide variety of flexible transportation services with different types of vehicles.
- It is dynamic, agile and adaptable
- Not highly-subsidized
- Open to innovation
- Provides employment opportunities

### Weaknesses

- A business model highly dependent on income and low social protection of service providers
- Absence of benefits due to economies of scale
- Low operational efficiency, lack of coordination, lack of integration of services, low quality standards, which affects both users and the community.
- Have a sense of “owning” their territory of operation
- Lack of sectoral organizations or recognition of them (for example, workers' unions)
- Little knowledge of the sector and little data available
- Lack sense of governance in the sector
- Significant negative externalities

Creditworthiness evaluation influenced by these weaknesses
New business models for fleet renewal and bus service provision
Introduction to unbundling bus

• To address the issue of bus financing, some governments have introduced models where they award separate concessions for fleet provision and fleet operation.

• In this model, the public sector either provides the bus fleet itself or contracts a private sector partner to purchase the fleet for a concession. Then they provide private operators the fleet under lease and operating contracts.

• This new unbundled approach offers many potential advantages over the traditional model including opportunities to introduce:
  • New funding alternatives
  • Clean and cutting-edge technologies
  • Increased competition
  • Increased flexibility to reallocate fleets
Bundled Approach for Bus Service Provision (Option 1)

proposals mechanisms of Financing

2. Separation of Risks: model of separation of the acquisition of fleet of the operation

- Entity Manager
  - Contract of Concessio
  - Payments by availability (fee by vehicle)
- Supplier of fleet
  - Escrow Heritage Autonomous
- Creditors
  - Pay K+1
  - Disbursement of credit
- Fee to the user

- Entity Manager
  - Contract of Concessio
- operator
  - OPE
- Creditors
  - Pay K+1
  - Disbursement of credit
- Escrow Heritage Autonomous
- Fee to the user

* Components that depend on the demand and impact the income, are the that they can arrive affect the liquidity.
Bundled Approach for Bus Service Provision (Option 2)

1. State Government (GE) requests support from FONADIN for infrastructure investment projects.

2. FONADIN authorizes a loan for studies and authorizes support (conditional on GE investing in CKD).

3. GE invests in CKD.

4. CKD-Infras seeks investment in the market; they can be pension funds.

5. CKD invests in SITP and selects an operator.

FONADIN (recoverable resource) is a government entity that provides funding for infrastructure projects. GE invests in CKD to support the project, and the SITP operator is responsible for operating the service. The subsidy component is also highlighted to indicate additional support for the service.
Conclusions
• Bus renewal requires introducing some level formalization in the informal/semiformal service provision.

• Project structuring and risk allocation can help to access financing for bus renewal, but also depends on how advanced the financial sector (e.g. commercial banks) is at appraising and offering credit conditions that fit the needs of the sector.

• New structures (e.g. unbundling) can be implemented to overcome the high risk perception of the structures but requires a high level of sophistication at the government/agency level.
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