Opening Remarks by H.E. Siniša Hajdaš-Dončić, Minister of Maritime Affairs, Transport and Infrastructure

Opening Remarks by Mr. Hongjoo Hahm, Croatia Country Manager, World Bank

Presentation of the Croatia Railway Policy Note by Mr. Jean-François Marteau, Transport Specialist, World Bank

Questions and Answers
Railway Network
Croatia
Croatian Railway Sector Underwent Profound Transformation to Meet the EU Accession Criteria

- Railway sector came a long way over the past decade:
  - Legal and institutional framework harmonized with the EU Acquis Communautaire
  - Independent regulatory institutions in place
  - Croatian Railways restructured and reorganized towards customer-oriented and competitive business
  - State financial support to railway sector started to decrease

- As of July 1, 2013 Croatia became integral part of the European transport market, which requires the **sustainability** of implemented reforms in the railway transport sector and the **versatility** of railway companies to adapt to market changes
## Strong Challenges and Opportunities linked to EU Integration

### CHALLENGES
- Macro-economic instability and fiscal consolidation – Risk on Demand
- Infrastructure modernization
- Implementation of HŽ Restructuring Plan – Condition of the companies is fragile
- “Fourth Railway Package” and EU2020 strategy require additional sectoral adjustments

### OPPORTUNITIES
- Sector rationalization and structural reforms, business opportunities in a liberalized context
- EU Funds availability and EU priority for Rail
- Efficiency gains and improved competitiveness of rail sector
- Legal and institutional framework compliant with the acquis
Railways Policy Note Supports Rail Reform at Different Levels

- Policy Note findings based on the sector diagnostics undertaken by the World Bank team between 12/2011 and 09/2012 and HŽ Restructuring Plan approved in 06/2012

- Recommendations support different stakeholders in their efforts to improve Croatia’s rail system
  - Government → policy options & sector governance and financing proposals
  - Railway companies → solutions for financial and operational improvements for each ex-holding company

- Impact analysis of the government Restructuring Plan simulation of the impact of two scenarios with a focus on financial sustainability of ex HŽ Holding companies
The Note Proposes Solutions to Railway Sector Challenges in Three Main Areas

**SECTOR GOVERNANCE**

Government actions for effective formulation and implementation of public policies in the railway sector

**CORPORATE GOVERNANCE**

Corporate and management performance of service providers to ensure their long term sustainability

**BUSINESS CULTURE**

Change management practice based on setting up a business mindset in the railway sector in Croatia
State Subsidies to Railway Sector have been Considerably High and geared toward operations

<table>
<thead>
<tr>
<th>Source</th>
<th>Unit of HŽ Holding</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
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</thead>
<tbody>
<tr>
<td>State contribution in railway operations</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Passengers (PSC)</td>
<td></td>
<td>493.3</td>
<td>413.9</td>
<td>402.0</td>
<td>400.0</td>
<td>370.0</td>
<td>347.5</td>
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<tr>
<td>Passengers (other than PSC)</td>
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<td>154.2</td>
<td>168.3</td>
<td>11.7</td>
<td>6.4</td>
<td>8.2</td>
<td>6.2</td>
<td>1.8</td>
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<td>Freight transport (PSC)</td>
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<td>5</td>
<td>5</td>
<td>15</td>
<td>14</td>
<td>44</td>
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<tr>
<td>Freight transport (other than PSC)</td>
<td></td>
<td>139.4</td>
<td>153.1</td>
<td>21.7</td>
<td>4.6</td>
<td>11</td>
<td>21.4</td>
<td>1.4</td>
</tr>
<tr>
<td>Traction</td>
<td></td>
<td>19.4</td>
<td>2.3</td>
<td>5</td>
<td>7.3</td>
<td>2.9</td>
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<td></td>
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<tr>
<td>Infrastructure</td>
<td></td>
<td>1,538.9</td>
<td>1,381.9</td>
<td>1,346.7</td>
<td>1,405.8</td>
<td>1,198.9</td>
<td>1,165.3</td>
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<tr>
<td>Holding</td>
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<td>2</td>
<td>39.3</td>
<td>16</td>
<td>1.8</td>
<td>2.0</td>
<td></td>
<td></td>
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<tr>
<td>Total</td>
<td></td>
<td>2,330.8</td>
<td>2,122.2</td>
<td>1,818.5</td>
<td>1,872.4</td>
<td>1,653.1</td>
<td>1,579.5</td>
<td>1,484.6</td>
</tr>
</tbody>
</table>

| State contribution for investments |
| Passengers                     |                    | 87.0    | 152.0   | 141.1   | 109.0   | 33.3    | 92.8    | 54.0    |
| Freight                        |                    | 40.0    | 99.6    | 78.0    | 128.0   | 98.3    | 60.0    | 62.0    |
| Infrastructure                 |                    | 573.2   | 518.8   | 608.9   | 767.7   | 529.5   | 434.4   | 251.2   |
| Traction                       |                    | 164.4   | 130.0   | 96.9    | 64.9    | 79.0    |         |         |
| Total                          |                    | 700.2   | 770.4   | 992.4   | 1,134.7 | 758.0   | 652.1   |         |
| Total State Contribution (operations + investments) |     | 3,031.0 | 2,892.6 | 2,810.9 | 3,007.1 | 2,411.1 | 2,231.6 |         |

0.7% GDP
Despite Government’s Incentives Traffic Intensity Remained Low

Evolution of traffic intensity (traffic units/km)

Traffic intensity compared to EU (2011)
Croatian Railway Companies Lag Significantly Behind their EU Peers in Terms of Performance

Croatian railways – Labor productivity (2011)

- Slovakia: 96.9%
- Croatia: 100.0%
- EU-27: 193.6%
- Finland: 408.2%
- Latvia: 423.1%
- Lithuania: 432.3%

Infrastructure Managers in EU, Staff per km (2011)

- Croatia: 0.473
- EU-27: 1.638
- Lithuania: 2.843
- Latvia: 3.60
- Slovakia: 4.73

HZ Cargo – Wagon productivity (2011)

- Slovakia: 0.455
- Croatia: 0.473
- EU-27: 0.729
- Finland: 0.907
- Lithuania: 1.638
- Latvia: 2.843

HZ Passenger Transport – Coach productivity (2011)

- Lithuania: 1,215,625
- Slovakia: 1,428,656
- Finland: 3,042,320
- EU-27: 3,051,402
- Croatia: 4,374,684
HZ Restructuring Plan Assumes Further Increase in Public Funds to Railway Sector

Difference between the World Bank and HŽ level of public funds to railway sector needed in period 2012-2016

In HRK thousands

Source: HŽ Holding, WB Calculations
Government Needs to Create a Long-term Vision for the Railway Sector

- Government receiving **value-for-money**
- Making new **legal and institutional framework** work
- Ensure **financial independence** and long-term **sustainability** of public railway operators
- Opening the market and ensuring efficient logistics chains
Infrastructure Assets are Old and Suffering from a Serious Backlog
Large Investment in Rolling Stock Needed to Achieve EU Standards in Quality and Safety
Creating Conditions for Wise Investment Policy in Railway Sector

- Croatian Railways will require annually more than **EUR 130 million for maintaining the current system** → EUR 55 million for infrastructure, EUR 30 million for freight rolling stock, EUR 45 million for passenger rolling stock

- **EU Funds** to provide bulk of financing to railway sector but limited to core international network and passenger rolling stock

- Government to decide on affordable amount of **public investments** in the sector → limit investments to EU funds counterpart funding, most critical infrastructure and freight rolling stock

- **Railway network optimization** is necessary along with enhancement of Multi-Annual Infrastructure Contracts (MAICs) to improve rail infrastructure quality
Deciding on the Mode of Subsidies to Railway Sector – Track Access Charge and Public Service Contracts

- **Charging of infrastructure:**
  - Maintaining attractive level of TAC insufficient to attract traffic volumes
  - Low TAC & high operating subsidy to IM or high TAC & lower operating subsidy to IM with higher passenger subsidy
  - TAC optimization and harmonization

- **Strengthening PSCs and adjusting it to market demand**
  - Developing multi-annual and less fragmented PSCs to enable long-term planning and stimulate investments in railway passenger transport
  - Funding of rolling stock development → direct subsidy to control investment (currently done) or incorporation of depreciation in the PSC to empower the operator(s)
Making the EU Framework Work for Croatia

- Opening of the market an opportunity for Port of Rijeka+ HZ in its competition with Kopper and Trieste. But this works both ways.

- More than **EUR 2.4 billion** available to Croatian transport sector in EU Financial Perspective 2014-2020 → majority of funds will be earmarked for railways

- Bringing new operators to the market

- Meeting **ex-ante conditionalities** necessary precondition for effective and efficient usage of EU support:
  - Developed comprehensive transport plans and strategies
  - Ensured capacity of intermediate bodies and beneficiaries (HZ Infrastructure and HZ Passengers in railways)
  - Mature and realistic project pipeline
  - Developed environmental assessments for all projects
Ensuring Sustainability of the Railway Operators

- HZ restructuring plan and reforms undertaken: great first step
- Financial situation likely to be difficult for years: government has to spend better and companies to be more efficient
- Questions remain open:
  - Who is taking the lead in continuing sector modernization?
  - Financial means not secured
  - Cost-cutting measures not ambitious enough
  - Investment plans suppose large state transfers and loans and managing to use the EU funds quickly
- Government to assume a two pronged approach:
  - Overseeing companies to meet program & meeting targets on subsidies, staffing and network resizing
  - Create the environment which enables timely implementation of restructuring measures by companies and the opening of the market
Railway Operators to Continue Implementing Planned Measures

- Improving financial and operational sustainability of Croatian Railways Companies depends on:
  - Timely enforcement of existing restructuring cost-cutting targets
  - Assertiveness in attracting new business and improving quality of service
  - Reviewing and restructuring portfolio of subsidiaries
  - Improving corporate governance
  - Continuing privatization activities (almost done for HZ Cargo)
  - Modifying elements of restructuring plans as they go along with implementation to guarantee long-term viability
Redefining the Role of Government and Improve Sector Governance

- Sector Policy: Provide ambitious vision and intermodal strategy. Ensure good intermodal interfaces and investment and more efficient facilitation with neighboring countries outside the EU.
- Provide mid-term clarity on sector funding (investments, services).
- Sector Governance:
  - Clear and consistent ownership policy & transparent, accountable and professional management.
  - Railway related activities coordinated among ministries (MMATI, MOF, MRDEUF) & among government, railway agencies and railway operators.
  - Public Consultations.
- Strengthening human capacity in the railway sector at all levels.
Thank you for your attention!