KPMG
cutting through complexity

MAY/JUNE 2014

# Transport Perspectives

**This edition of Transport Perspectives focuses on two highly topical issues in the transport sector.**

In the first article, Helge Ramboel explores market entry strategies in an increasingly global public transport market.

In the second article, Samuel Boon discusses the challenges and opportunities for the future of the postal industry.

Contents

# Market Entry Strategies in a Globalising Public Transport Market

Helge Ramboel, Associate Director, Transport – KPMG in the UK

As the move towards public transport market liberalisation continues and governments across the world increasingly turn to the private sector for the provision of public transport services, international expansion has become a key strategic consideration of the operating groups.

This article considers the drivers of growth in the global public transport sector and the new market entry strategies adopted by industry players in order to capitalise on this opportunity.

## Global megatrends are driving opportunity

Several global megatrends are creating unprecedented new market opportunities for public transport operating groups.

First, deregulation and privatisation of existing public transport services and transport infrastructure assets is becoming increasingly common as many national governments, faced with budgetary constraints, look to the private sector to help in the delivery of cost savings and improved performance. In the May 2013 Transport Perspectives article 'Competition in the European Passenger Rail Market', we noted that efforts by the European Commission to create a Single European Railway Area have the potential to trigger radical changes in public transport provision. Whilst the degree of market liberalisation varies from country to country, and the move towards mandatory competitive tendering of Public Service Contracts in the EU suffered a setback in a European Parliament vote on 26 February 2014, steps towards market opening are evident across most EU countries. Outside of Europe, public transport liberalisation has reached an advanced stage in Australia[1] and other markets are starting to follow suit.

Second, mass urbanisation, particularly in emerging markets, creates an unprecedented requirement for investment in new urban public transport infrastructure. Research by the UN[2] suggests that Asia and Africa's combined urban populations will grow by approximately 2.2 billion by 2050, with India and China accounting for 497 million and 341 million, respectively. In response, with relatively few mass rapid transit systems currently in operation, both countries now have over thirty new metro systems either under proposal, planning or construction. Much of this investment in new urban public transport systems in emerging markets, will be tendered to the private sector, either via design, build, finance, operate and maintain (DBFOM) contracts or with the operations and maintenance element tendered separately.

## Operator strategies

To date, the market strategies adopted by industry players in response to these trends have varied.

The three large French players in the market, SNCF/Keolis, RATP and Transdev (formerly Veolia Transdev), have all adopted a global approach. To develop a global portfolio balanced between mature markets such as Europe and North America, and emerging markets with strong growth potential, such as India, China, Brazil and the Middle East, they have each established operations in a dozen or more countries. For example, Transdev has recently re-focused its strategy away from what it calls 'low growth activities' in Europe, to fund expansion in Asia, North America and Australia[3].

Deutsche Bahn, on the other hand, has focused its strategy on driving consolidation across the European public transport market. It has completed several strategic acquisitions in recent years, including that of Arriva in 2010 and Veolia Transdev's Central Europe assets in 2013. In Arriva, Deutsche Bahn acquired an established engine for international expansion. Since first entering the mainland European public transport market in 1997, Arriva has developed a significant market presence across 14 European countries.

A third group of players, the UK transport PLCs, including FirstGroup, Stagecoach and National Express, have focused their international strategies largely on North America.

---

1. Transport Perspectives, March/April 2014, Australia poised to become a major opportunity for global transport players: http://www.kpmg.com/Global/en/IssuesAndInsights/ArticlesPublications/Pages/transport-perspectives-march-april-2014.aspx.
2. http://www.un.org/apps/news/story.asp?NewsID=41722.
3. http://www.transdevplc.co.uk/media-centre/?newsID=28.

The only non-European players to make significant inroads into international public transport markets to date, MTR and ComfortDelGro, have adopted strategies focused on China, South East Asia, Australia and a handful of European countries.

As the market opportunities for experienced commercial operators in new international markets accelerate, whilst growth prospects in mature markets remain limited, we expect to see a trend towards more industry players adopting broader geographic diversification strategies.

## Trends in market entry

If market strategies have varied between industry players, so has the approach to market entry. For example, Deutsche Bahn/Arriva's European expansion has largely been driven by the acquisition of established local players. Keolis, conversely, has adopted a broad range of market entry modes ranging from organic entry (e.g. India), vertical bidding consortia (e.g. GoldLinQ Australia), minority stakes in market entry JVs (e.g. UK) and strategic JVs (e.g. Shanghai Shentong Metro Group) to acquisitions (e.g. Busslink Sweden).

Table 1 provides an overview of the continuum of market entry modes and co-operation structures seen in the public transport market.

### Table 1: Modes of market entry and partnering structures

| Market entry mode | Characteristics | Examples | Benefits |
|---|---|---|---|
| **Organic entry** | • Direct entry in chosen market on a standalone basis, usually by establishing a local subsidiary/bidding entity. | • Keolis market entry in India (2012) | • Control retained |
| **International service alliances** | • The majority of cross-border services in continental Europe are operated as partnerships /Service alliances between national state operators. | • Eurostar (55:40:5 JV between SNCF, LCR and SNCB)<br>• Thalys (60:40 JV between SNCF and SNCB)*<br>• Alleo (50:50 JV between DB and SNCF) | • Access to otherwise closed markets |
| **Vertical bidding consortia** | • Commonly used for new build heavy/light rail infrastructure projects tendered on a DBFOM basis.<br>• Bidding consortia typically involves financing houses, ROSCOs and infrastructure providers as well as the operator. | • Renfe consortium winning Saudi Haramain high speed rail contract (2011)<br>• Keolis GoldLinQ consortium (Australia) (2011)<br>• RATP as operator in DBOM consortium for Rio de Janeiro tramway (2013)<br>• Serco and MTR currently bidding in separate consortia for North West Rail Link in Sydney | • Risk sharing<br>• Vertical alignment/ knowledge share |
| **Horizontal/ vertical market entry JVs** | • Common mode of market entry where the new entrant forms a JV with a local partner to overcome market entry barriers. | • Keolis, Abellio and MTR all entered the UK market via JVs with local partners<br>• National Express entered the German rail market in a JV with local freight and passenger rail operator IntEgro Verkehr (2013) | • Access to local market knowledge<br>• Speed of entry/ability to overcome other barriers to organic entry |
| **Strategic JVs** | • Longer-term, more strategic partnership between operators (e.g. in the targeting of new geographic or product market). | • Veolia Transdev and RATP strategic JV to target key Asian markets (notably India and China) (2009)<br>• Keolis strategic JV with the Shanghai Shentong Metro Group to bid for urban / regional networks in China, Asia and around the world (2013) | • Pooling of skills/financial resources and risk sharing |
| **Minority equity stakes** | • Direct investment may take the form of a minority equity stake in a target operator.<br>• May be seen as a transitional strategy or as a pure investment strategy with aims to achieve returns on capital. | • SNCF has 20% and 26% stakes in open access operators NTV (Italy) and WestBahn (Austria)<br>• Arriva has a 31.5% stake in Barraqueiro, the largest private public transport group in Portugal<br>• RATP has a 37% stake in Italian regional rail and bus operator La Ferrovia Italiana | • Less resource intensive than full take-over |
| **Mergers and acquisitions** | • Full takeover or merger.<br>• Can range from small bolt-on acquisition in existing or new markets to transformational strategic transactions to establish firm foothold in new geographies or drive industry consolidation. | • Deutsche Bahn's acquisitions of John Laing's rail business in the UK (2008), Arriva (2010) and Veolia's Central Europe assets (2013)<br>• Merger of Veolia Transport and Transdev (2011)<br>• FirstGroup's acquisition of Laidlaw in the US (2007)<br>• Keolis' acquisition of Busslink in Sweden (2003) | • Rapid establishment of foothold and platform for growth<br>• Control retained |

Source: KPMG analysis, April 2014

*This structure will be in place from 2015 as Deutsche Bahn has exited the existing 62:28:10 JV between SNCF, SNCB and Deutsche Bahn

An interesting development in partnering structures is the establishment, between some industry players, of long-term strategic JVs to target key emerging markets, notably:

- In 2009, Transdev and RATP entered into a 50:50 JV to target key Asian markets, notably China, South Korea and India with the aim to become an urban transport market leader in the region. To date, the JV has secured five operating contracts in China, the Seoul Metro Line 9 in South Korea and the Mumbai Metro Line 1 in India.
- In April 2013, Keolis entered into a strategic JV with the Shanghai Shentong Metro Group, the operator of the Shanghai metro system, to bid for urban and regional networks in China, Asia and around the world.

The tendency towards non-organic market entry can to a significant degree be explained by the characteristics of the transport sector and the pressures on national governments. Public transport is a highly visible and politically sensitive public service. Therefore, whilst value for money, innovation and service quality are important, many governments tend towards appointing a 'safe pair of hands' (preferably local) to try to minimise any potential risks.

In addition, some emerging markets (e.g. China) impose restrictions on majority ownership of transport infrastructure assets and operations, requiring international entrants to be seen to be supporting the local economy by entering into minority stake JVs with a local player.

The experience of the UK passenger rail market shows that while these JVs may have a life of a decade or more, over time, they may become less relevant. Over the last 2-3 years, Keolis, Abellio and MTR, who initially entered the UK via JV vehicles, have come up the learning curve and become well-established players in their own right. They have all now bid on a standalone basis, sometimes in direct competition with their original JV partners.

## Key challenges for successful co-operation

Given these challenges, effective partnering is likely to be a key factor for successful market entry, particularly in emerging markets. For operating groups used to organic or acquisition driven growth, there are several challenges associated with a true co-operative model, particularly in emerging markets. These include:

- Moving from known, tried and trusted operating models and systems, with control as a given, to a shared organisation, where all decisions are jointly made;
- Cultural and linguistic differences;
- Unfamiliar ethical standards and business practices;
- Complex and ever-changing regulation, tax and compliance;
- The need to understand government involvement, both formal and informal; and
- The need to be aware of a partner's long term agenda and strategic direction.

## Choosing an international partnering approach

Where partnering is required, the following steps should be considered in order to extract maximum value from the relationship:

- Understand your own competencies and weaknesses, to enable you to look for a truly complementary partner;
- Confirm your long term aspirations and medium term goals (e.g. financial, geographic, reputational and technological) in order to understand what your JV(s) and partnership(s) are designed to deliver;
- Be clear in your thinking about your "red lines" – what are your own deal-breakers?
- Articulate your own "value proposition" to potential partners, as well as what you are looking for from them; and
- Acquire the right skills and experience, so that your deal can be built on a hard-nosed commercial reality and delivered in practice on the ground.

## Conclusions

More market opportunities for public transport operators are emerging across more geographies than ever before. From this period of industry transformation, there is an opportunity for a few global mega operators to emerge provided that they can effectively circumvent market entry barriers and balance the longer term growth agenda, be it organic or inorganic, against any short term objectives around shareholder return.

As globalisation of the public transport market continues, the operators that emerge as global leaders are likely to employ a variety of market entry strategies based on a flexible and adaptable approach tailored to the dynamics of each market.

# The Future of Postal Services

Samuel Boon, Associate Director, Advisory – KPMG Australia

"It is not the strongest of the species that survives, nor the most intelligent, but the one most responsive to change." Charles Darwin

Postal operators can often be considered the corporate face of a nation, capturing and distilling the spirit of the society into an organisation. Balancing this national interest with the progressive decline of their traditional revenue sources such as letters and packets is a reality for postal operators worldwide. Many postal organisations have long since taken sightings of the icebergs on the horizon, and are changing course in a variety of directions to exploit the future of what remains a promising industry in which revenues are still forecast to increase over the coming years. This article explores a number of innovative approaches being taken by these organisations in light of the challenges they face.

Considerations of structural changes in the market must be overlaid with prevailing trends in public finance affecting what has traditionally been a government-owned sector. Austerity measures, increasing privatisation, and voters' calls for a balanced budget are reducing tolerance for government subsidies in all sectors, even those traditionally regarded as essential services. Indeed, the rise of digital substitutes and ubiquity of instantaneous mobile telecommunications are challenging the very premise that mail is an essential service. Faced with a perfect storm of economic reality and public opinion, postal operators are being forced to stand on their own two feet, and are often doing so with commendable agility.

Australia Post, which is granted by its founding legislation a double-edged sword in the form of a monopoly and a corollary obligation specifying non-negotiable universal transit times regardless of delivery point remoteness, is currently entering its fourth year of implementing its Future Ready strategy. The mail


POST

business in Australia poses service challenges seen in only a few geographies worldwide, notably Canada – a small population, scattered about a vast land mass, which makes no concession for distance in its expectation of postal transit times. Canada Post, incidentally, recently announced that it would phase out door-to-door mail delivery in favour of community mailboxes, largely as a result of these very challenges. The Future Ready strategy, at Australia Post, brainchild of CEO Ahmed Fahour, is aimed at reorienting the organisation to a more customer-centric model, with financial performance underpinned by leveraging value-added services at Australia Post's almost 4,500 retail outlets, parcel volume growth, and most notably a n It is this e-Services division, which Australia Post describes as "a dedicated…business incubator focusing on opportunities such as secure, identity-verified, digital communications, e-commerce initiatives and other services"[1] which holds the key to the success of the strategy. Australia Post consistently ranks as one of the most trusted brands in the country[2] and is using this as a basis for exploring the provision of online identity verification services and a digital mailbox product offering bill presentment and payment, similar to Post Danmark's e-Boks solution, with the addition of an online storage 'vault'.

Still in Asia, but servicing a market at the opposite end of the population density scale, Singapore Post is taking a different e-commerce tack. SingPost eCommerce is essentially an e-commerce outsourcing provider, which integrates Singapore Post's offering vertically up the value chain from delivery fulfilment to marketing, customer acquisition and care, and actual construction of digital infrastructure. Adidas was the launch customer in Singapore, and has now extended its e-commerce solution to provide full capability in six Southeast Asian countries. As evidence of just how serious Wolfgang Baier, Singapore Post's CEO, is about this vertical integration, the organisation acquired a majority stake in freight forwarder Famous Holdings, citing "efforts to grow…regional logistics and e-commerce business where customer demand for integrated solutions is strong."[3]

Singapore Post is also backing up its e-commerce strategy by borrowing some tactics from Australia Post's playbook, with the 2013 rollout of parcel lockers across selected sites in the island nation. An 11% CAGR in internet retailing is predicted for the five years to 2018 in a country with over 85% internet penetration[4], and Singapore Post has called on TZ Ltd, the company which provided parcel locker terminals for Australia Post, to provide it with the same solution.

Meanwhile in Europe, where La Poste of France is forecasting an average decrease in mail volumes of between five and six percent per year between 2013 and 2018[5], and Dutch PostNL is predicting 9-12% declines from 2014-17[6], still more innovative approaches are emerging. A number of postal organizations have recognised the advantage arising from owning a brand trusted by the community - drawing on this same theme and the government services rationalisation trend, the UK Post Office, now a separate entity from the recently privatised Royal Mail, has explored the possibility of providing basic police administration services and even converting sections of post offices into police bureaus.[7] This would deliver multiple benefits for the UK government: driving increased foot traffic to postal outlets, up-skilling the postal workforce, and allowing conflation of government service points of presence, presumably leading to eventual closure of selected points and driving related cost savings.

Similarly, Poland's Poczta Polska is harnessing postal authorities' unique position as 'of the government but not the government' to explore the provision of legal services, presumably company registrations, access to pension fund services and benefits, and provision of tax and other official certificates which require a government imprimatur.

While each of these ships of state is turning at its own pace and respectively adopting slightly varied headings, the direction of the tide is clear. Postal authorities worldwide are increasingly pursuing some combination of two broad strategies: using their trust and position in the community to integrate additional government-based services into their offering, or riding the e-commerce wave to deliver sustainable profitability.

It is a truism of our times that the pace of change is ever increasing; it took almost 2000 years for the standard delivery time of six days for the Roman postal service to take a letter from Rome to London to be bested; this did not occur until around 1900. Another hundred or so years, and we have instantaneous communication almost anywhere in the world; no wonder some of our greatest commercial edifices need to reinvent themselves. The question surely now becomes whether any source of advantage in the communications sector is indeed sustainable.

---

1. Australia Post Press Release "Future Ready - Australia Post's business renewal program", 21 April 2010.
2. RepTrak reputation ratings, November 2012.
3. "SingPost boosts e-commerce logistics arm with $60m acquisition", *Post & Parcel,* January 18 2013.
4. "Internet Retailing in Singapore", Euromonitor International, 10 April 2014"
5. http://legroupe.laposte.fr/en/Espace-Presse/Liste-des-communiques/La-Poste-is-setting-out-its-2013-2018-strategic-plan
6. http://www.postnl.com/nl/Images/20140224-postnl-2013-q4-presentation_tcm217-685888.pdf
7. "Police in joint venture talks with Post Office", *Financial Times,* January 11 2013.

## Contact us


**Dr Ashley Steel**
Global Chair – Transport and Logistics
**T:** +44 (0)20 7311 6633
**E:** ashley.steel@kpmg.co.uk

**Shazar Dhalla**
Global Executive – Transport and Logistics
**T:** +44 (0)20 7694 8242
**E:** shazar.dhalla@kpmg.co.uk

**Helge Ramboel**
Associate Director – Transport Advisory
KPMG in the UK
**T:** +44 (0)20 7311 5770
**E:** helge.ramboel@kpmg.co.uk

**Samuel Boon**
Associate Director – Advisory
KPMG Australia
**T:** +61 3 9288 5624
**E:** samboon@kpmg.com.au





Produced by Create Graphics | CRT015924 | April 2014 | Printed in the UK


**www.kpmg.com**