Considering placing a bid in a competitive tender to operate a 15-year rail concession. The contract would be operated by an SPV

A clean / flexible model for this tender project and a first analysis.

The objective is to determine the level of annual subsidy that would enable the company to reach its targeted project IRR.

- Concession period: from 01/01/2023 until 31/12/2037
- # of passengers in 2020: 10 million passengers

Revenue model

- The operator winning the tender will generate revenues from i) a subsidy, and ii) a passenger incentive fee based on the number of passengers transported in the tendered network. The annual subsidy and the incentive fee are paid annually every year within the concession period.
- Annual subsidy: level to be proposed by the transport operator The contract will be awarded to the operator offering the lowest level of annual subsidy
- Passenger incentive fee: set at €1.20 / passenger in 2023
- The subsidy and the passenger incentive fee (in €/passenger) are subject by contract to indexation formulas and assumed to grow at 1.5% per year
- Passenger volume: assumed to grow at 2% per year

Operational costs:

- Amount to 60 m€ in the first year of the concession
- Operational costs are expected to grow by 2% annually

Working Capital: 5% of yearly revenues

Capex/financing – train fleet:
- 25 trains for a total price of 100 m€ assumed to be depreciated linearly over 25 years
- Financed at 10% with equity and 90% with a 20-years bank debt (3month EURIBOR, margin of 200 BPs, constant principal repayment, Covenant: DSCR > 1.05x, Lock-up: DSCR > 1.3x)
- At the end of the contract, the fleet is sold at a discount of 20% to the net book value

Capex/financing – heavy maintenance: 4 m€ every 3 years from 2026 assumed to be depreciated linearly over 3 years and financed with bank debt over 3 years (interests of 3%, constant interest + principal repayment)

Corporate income tax: Assume an effective tax rate of 28.9%

• **Dividends:** equals to 80% of the net income of the previous year, minimum cash balance of 5 m€

Your analysis:
• Calculate the level of the annual subsidy to be paid in 2023 that would result in a project IRR of 9%.

What would be the corresponding equity IRR?

Present the outputs / ratios that would be of interest for your CEO including the three financial statements (P&L, Cash-Flow and Balance Sheet)

• For this level of annual subsidy, present in your model the two following sensitivities:

- The traffic is 40% lower than expected from years 2028 and 2031;

- The operational costs are 8% higher than expected.

Risk analysis: send back a document (Word or PowerPoint, maximum 1 page) **within 2 days**
On the basis of the case presented above, you are asked to draft a note to the attention of the executive committee of your company describing the main risks of the project