

**TO:** Board of Directors  
**FROM:** Lloyd Major, GM Mechanical  
**APPROVED:** Jim Quinn, Chief Executive  
**DATE:** 19 August 2011  
**RE:** **Wagon Build Cost Comparison**

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**RECOMMENDATIONS:**

It is recommended that the Board of Directors:

1. **note** the contents of this report.

**Background**

This paper was requested at last month's board meeting to "set out the cost of wagon build at Hillside compared to prices quoted by other suppliers".

It sets out the most recent pricing comparisons undertaken and also summarises some of the other non-financial considerations that need to be taken into account.

**1. Summary**

The most recent comparison of the cost of building wagons at Hillside versus prices quoted by other suppliers was conducted as part of the evaluation of KiwiRail's CFT (Container Flat Top Wagon) RFP Process conducted in November of 2010.

The results of this evaluation (based on the four suppliers that made it through to the last stage of the process) showed that the price submitted by Hillside was approximately 25% more expensive than the winning bid from China Northern Railways (CNR).

A more detailed comparison of the winning bid from CNR versus the Hillside offering has been undertaken as part of the recent work to provide rationale behind restructuring the Mechanical business and the Hillside Workshop [REDACTED].

This work highlights that the price differential is at least 30% for the most optimistic scenario which would contain significant risk of cost and time overrun. It is considered that in reality the cost/price difference would be closer to 50% than to the 25% anticipated as part of the RFP Process [REDACTED].

The RFP price submitted by Hillside was based on a very optimistic view of the cost and productivity efficiencies that would arise from a large production run. However the RFP review team opinion was that Hillside would not be able to deliver the wagons to either the cost or delivery quoted. Based on the known costs of the recent build at Hillside of 35 CFT's the actual cost difference between building and buying would be closer to 50%.

There were also a number of non-financial considerations that had to be factored into the final decision including the ability of suppliers to deliver on the timelines demanded as part of the Turnaround Plan (TAP).

The 300 wagons in the RFP needed to be delivered quickly (by the end of Jul 2011) in order to allow the Freight business to meet increasing demand and to replace older (less reliable and more expensive to maintain) wagons. Nine months is the typical lead time before construction can begin in earnest for a New Zealand built wagon, and then delivery would ramp up to two per week.

Hillside simply could not meet the targets in the short timeframes demanded by the TAP (either for the initial or subsequent orders) and in addition, would require substantial capex to upgrade the plant and facilities to meet the faster delivery rates required. Unfortunately once the initial TAP demand was satisfied Hillside would have excess capacity that would be unable to be utilised.

## 2. RFP Final Price Results – Hillside Compared to Other Suppliers

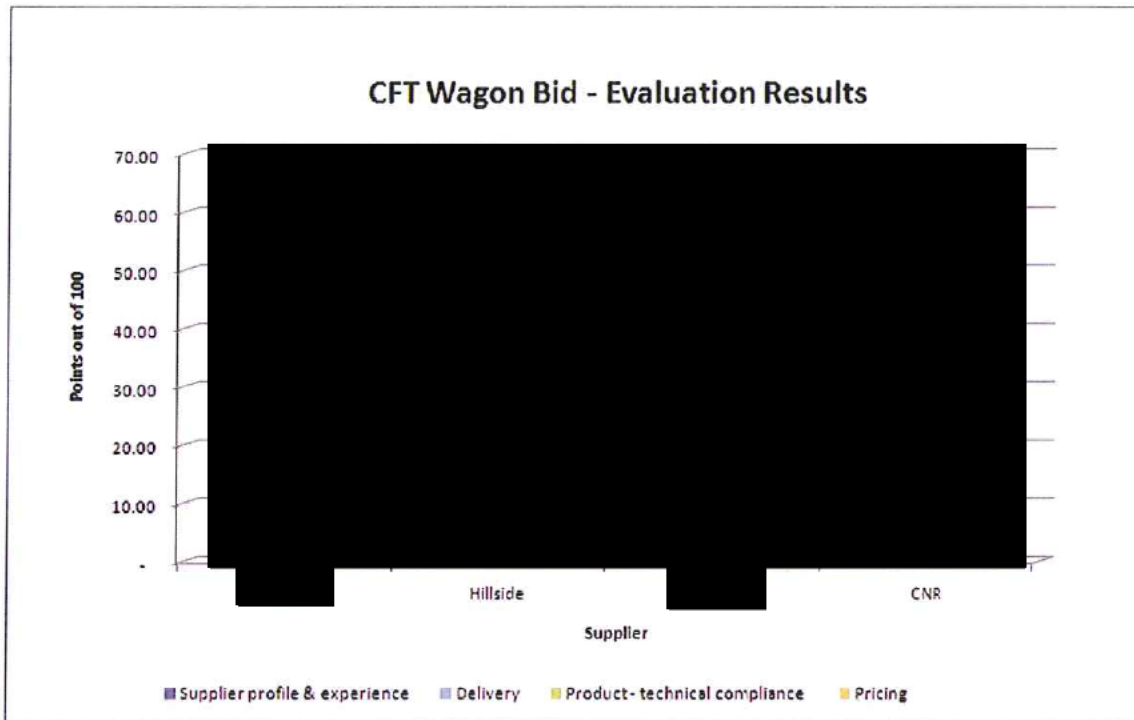
The following table shows how the Hillside bid lined up against the other suppliers that made it through to the last stage of the bid.

| Summary Information  | Bradken | Hillside          | CSR | CNR               |
|--|---------|-------------------|-----|-------------------|
| NZD Unit Price   |         |                   |     |                   |
| Units  |         |                   |     |                   |
| <b>Subtotal</b>  |         | <b>35,637,084</b> |     | <b>28,536,364</b> |
| Estimated Project Management Costs (negotiation, inspecting & testing) |         |                   |     |                   |
| Spares (assume 5%)   |         |                   |     |                   |
| <b>Total Cost</b>  |         | <b>37,793,128</b> |     | <b>31,390,000</b> |

## 3. Other Considerations

As well as price the RFP Process awarded points to other bidders based on Supplier Profile and Experience, Delivery Schedule, and Product Technical Compliance.

The results of the final points awarded are shown in the chart below.



#### 4. Conclusion

The cost of building wagons at Hillside is significantly more expensive than many overseas alternatives and other suppliers are superior on non-financial considerations as well.

One of the key assumptions of the TAP is that the wagon replacement program should be 'front loaded' in order to satisfy customer demand and give KiwiRail the opportunity to replace it's increasingly aged (poor reliability and expensive to maintain) wagon fleet.

Therefore, the ability to deliver large quantities of wagons in a short timeframe is paramount to achieving the stated goals of the TAP. Hillside, regardless of the price, cannot compete on this basis.

