

## The Mostyn–Dublin route

### P&O and Stena’s view of the Mostyn–Dublin route

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2. The building of the port facilities at Mostyn was initially financed by a [



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Under the terms of an operating agreement with the Port of Mostyn, P&O would make quarterly payments to Port of Mostyn [  ], an annual payment in respect of maintenance dredging, and port dues on a per unit basis subject to a minimum throughput. P&O planned to fund an additional £] million of port assets including terminal buildings.

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4. P&O's management accounts for the Mostyn-Dublin route reported an operating loss of [ ✂ ] in 2002, and a forecast operating loss of [ ✂ ]<sup>1</sup> in 2003. P&O told us that it had lowered freight rates on the route in an attempt to compensate for the unreliability of the service, and that this, compounded with the lower traffic volumes, meant that the economics of keeping the route open were [ ✂ ].

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<sup>1</sup>As at August 2003.

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6. During the discussions with Stena, P&O prepared a draft discussion paper<sup>2</sup> considering whether it was more profitable to keep the Mostyn-Dublin route open, or close it, and do the deal with Stena. This was based on a discounted cash flow (DCF) model which gave a net present value (NPV) of operating the route of £[✂] million (see Table 1). In the paper, P&O compared this NPV with the NPV of closing the route of [



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7. P&O told us that the DCF calculation was a best-case scenario that had been prepared to calculate the possible maximum value, and that the growth assumptions were aggressive, both for tourist and for freight traffic, and unrealistic given the continuing uncertainty over the ability of the Port of Mostyn to gain permanent or

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<sup>2</sup>Project Columba—Mostyn closure economics, 21 March 2003. P&O later told us that this was dated incorrectly and had actually been prepared in May.

long-term maintenance dredging consents. Without these growth assumptions the NPV would be negative.

8. We asked P&O to provide further information about its assumptions. In its response, P&O said that the projections in the DCF were unachievable for several reasons:

- Permanent dredging consents were not received in 2003 as expected.

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9. P&O provided two revised DCF calculations. The first of these was based on the original DCF but on the assumption that permanent dredging consents were not received, [ ✂ ]. This led to a negative NPV of –£[✂] million (see Table 2).

10. The second DCF was prepared to assess the prospects for the service at the present time. It was further revised to take account of the latest 2003 revenue and cost figures, and incorporated changes in operating costs as a result of a recently agreed transaction with [ ✂ ].<sup>3</sup> This showed a positive NPV of £[✂] million (see Table 3), which P&O compared with an NPV of £[✂] million based on closure of the route and charter/redeployment of the vessels.

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<sup>3</sup>Under a tripartite agreement between Port of Mostyn, [✂] and P&O, [ ✂ ] will [ ✂ ] P&O's berth at Mostyn to ship [✂].

[ ✂ ] will obtain the right to use

11. P&O said that if permanent dredging consents were obtained, the service would benefit from an estimated one-off increase in accompanied freight [ ✂ ] which would increase the net present value by £[✂] million. P&O said that for a number of reasons the grant of a permanent licence to dredge was highly uncertain and would remain so until late February 2004 at the earliest, after the date of our report. P&O's reasoning is set out in further detail in paragraphs 24 to 38.
12. During the course of the inquiry, we spoke to Defra to ascertain the current position with respect to the grant of dredging licences to the Port of Mostyn. Defra confirmed that it was currently conducting environmental studies and had not yet made a decision on the consents.
13. P&O said that, even if permanent dredging consents were obtained, the closure of the Mostyn-Dublin route would still be more profitable by around £[✂] million<sup>4</sup> and offered more certainty than continuing to operate the route. We noted that P&O had not included any uplift in its calculations for the benefit of extra traffic on its Liverpool–Dublin route. Stena estimated this benefit to be worth £[✂] million a year.
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<sup>4</sup>That is, the difference between NPV of closure at £[✂] million and that of continuing to operate, on the assumption permanent dredging consents are obtained, of about £[✂] million.

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16. P&O said that, post the Central transaction, there would be no economic or commercial rationale for continuing with just one underperforming central corridor route (ie Mostyn–Dublin) and the decision to close the route if the Central and Cairnryan transactions completed was not driven by disclosure or accounting issues.

17. We considered whether, in the event the Central transaction did not proceed, P&O might consider whether a similar arrangement might be arrived at with an alternative purchaser of the Liverpool–Dublin route, in order to avoid losing the financial benefits of expressing part of the consideration for the route sale as a contribution towards the closure costs of the Mostyn-Dublin route.

18. P&O said that it did not see this as a reason for keeping a loss-making route open, particularly given the high opportunity cost of using the *Ambassador* on the route, which was a valuable ship and could be chartered or sold or used somewhere else.

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### **Alternatives to closure**

21. P&O said that it had considered the option of replacing the *Ambassador* with the *Seafarer* when it proposed this idea to Stena during the negotiations leading up to the Central transaction. However, P&O told us that this would have publicly shown a lack of commitment to the service and further damaged its prospects.
  
22. We also considered whether P&O might be able to relaunch the route as a freight-only service, using a more economically viable ship than the *Ambassador*. P&O said that this type of operation would not fit with P&O's strategy of concentrating on passenger routes with a strong freight underlay but that it was a possibility that some time in the future another operator would start a service of this nature.

23. P&O also considered whether it could operate a primarily unaccompanied Mostyn–Dublin service on financial grounds. It estimated that the route would have incurred a loss, before central overheads, of [ ✂ ] in 2003 if it had replaced the existing vessels with two freighters. The forecast loss before central overheads on the Mostyn-Dublin route in 2003 was [ ✂ ]. However, P&O said that in this context it was necessary to consider the [ ✂ ] profits earned by the *Ambassador* at the weekend on the Dublin–Cherbourg route which it said would be lost if the Mostyn-Dublin route was retonnaged with freight-only vessels. Taking this into account, the forecast loss in 2003 would be [ ✂ ] whether or not it replaced the existing vessels with chartered freighters. P&O said that it would not choose to operate the service on this basis.

#### **Dredging issues at the port of Mostyn**

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