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Dennis Hunter, Commission Chair
Humboldt Bay Harbor District
601 Startare Drive, Woodley Island
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June 22, 2008

Re: Draft Redwood Marine Terminal Business Plan

Dear Dennis,

I am providing my comments below on the *Draft Redwood Marine Terminal Business Plan (Business Plan)* and, as with the previous *Redwood Marine Terminal Feasibility Study* that preceded it, I still cannot find evidence that transshipping Asian goods through Humboldt Bay is a viable enterprise. I also do not see sufficient smaller scale shipping to warrant District investment in the multipurpose marine terminal. The *Business Plan* is fraught with unfounded assumptions and provides no solid basis for positive cash flow scenarios. Success of the larger-scale container ship option depends on the reconstruction of a railroad through the Eel River canyon, a prospect that I consider remote at best.

As result, I cannot support the adoption of the *Business Plan*, the District taking on the recommended \$35 million loan for the multipurpose terminal, nor having our Port assets auctioned off in the future to facilitate development of an international shipping terminal.

It just doesn't make business sense to me nor is it considered favorably by the majority of my constituents.

Competition for Asian Shipping Trade

A major assumption in the *Business Plan* is that the "US West Coast is projected to face capacity constraints at its existing container ports in the 2015 to 2020 time period and new capacity will be required, including investments at secondary ports and new port sites." This is speculative hype. Anyone following West Coast shipping news of late knows 1) the U.S. economic slowdown has decreased container shipping and auto shipping from Asia and 2) that expanding capacity is increasing competition among the existing ports. The *Business Plan* states that the Port of Humboldt would be competing with new second tier ports like Coos Bay, but in reality we would compete, if at all, against expanding major ports for diminishing business.

The San Francisco Chronicle (5/28/08) reported that Port of Oakland business this year was down 5.5%, Port of Los Angeles by 10% and Long Beach 7.5%. At the same time these ports are expanding their capacity with \$3 billion in California Prop 1B money.

After meteoric growth early in the decade, business at the Port of Seattle is expected to decline 5-7% this year (Seattle Post-Intelligencer, 6/15/08). The West Coast shipping boom related to the China trade is over and competition for future business will be intense.

The Los Angeles Times (6/15/08) described fierce competition developing in the West Coast shipping trade due to the expansion of the Panama Canal, Canadian investment in the Port of Prince Rupert, and expansion of Gulf and East Coast ports.

- "The Panama Canal expansion project is expected to increase cargo traffic there by as much as 73% over the record 4 million containers handled in 2007.
- In Canada, government officials are pouring \$3.3 billion into an effort to transform the newly opened Port of Prince Rupert, north of Vancouver, and the connecting CN railroad into the trade gateway of choice for container cargo destined for Midwestern U.S. states and other areas. 'This is a true national priority for us,' said John Higginbotham, principal advisor to Transport Canada's Asia Pacific Gateway and Corridor Initiative.
- Competitors along the East and Gulf coasts, once content to take on whatever Los Angeles and Long Beach couldn't handle, have embarked on major expansion projects.
- Edward DeNike, president of Seattle-based SSA Marine's SSA Containers division, said that West Coast harbors were in danger of falling into a situation where 'we're not going to control our own destiny' as customers find lower-cost options."

The Port of Humboldt is continually compared with Prince Rupert, British Columbia because the latter is a small seaport without a population base to consume goods. However, the \$3.3 billion government investment in infrastructure support for port development and its location -- two shipping days closer to Asia -- make it distinctly different.

Port of Seattle Seaport Managing Director Charlie Sheldon (Seattle P-I, 6/15/08) summed up market conditions on the West Coast: "If cargo keeps growing at 10 percent a year, then you can all live with the fantasy that a rising tide lifts all boats," Sheldon said. "But cargo is down ... so that means that a rising tide does not raise all boats." There is no reason to believe that the Port of Humboldt Bay can compete given diminishing trade volume and our inherent competitive disadvantages, which are noted in the PB Marine *Revitalization Plan*.

No Tangible Business Prospects

The *Business Plan* fails to name any firm or specific prospects for business, other than those in some exploratory phase. This lack of basis makes projections for positive cash flow implausible.

Cruise Ships: The *Business Plan* envisions positioning Humboldt Bay as one of several “niche” ports of call for cruise vessels operating along the U.S. West Coast. A surge in cruise ships coming to Humboldt Bay is speculative, with a partnership of West Coast niche ports (Cruise the West) only in an exploratory phase. While the cruise ship business has some potential, comparing Humboldt Bay’s opportunities with those of Puget Sound ports is gratuitous. We do not have an archipelago of islands to buffer swells off our coast.

I believe there is an opportunity for cruise ships to contribute to our economy, but they will only contribute significantly after we have invested in making our region more of a tourist destination (museum complex, aquarium, seafood institute/aquaculture attraction). Cruise ships usually are in port for only six hours; therefore, it is more logical to develop a cruise ship dock in Eureka for debarking directly to Old Town and the Marina Center area. If a museum complex were developed at the Redwood Dock, we would need to ferry cruise ship passengers via the Madiget (or a fleet of biodiesel Madiget replicas?).

Dry Bulk Cargo: The *Business Plan* describes the opportunity for this sector as follows:

“There are some company specific opportunities to handle dry bulk cargo over the Redwood Marine Terminal. One example is the movement of dry bulk fuel in barges for local power plants. The District will market and negotiate directly with individual shippers to assess unique requirements (storage, warehousing, etc.) and create customized port service solutions.”

If there are company specific opportunities, then the *Business Plan* should be able to identify them and provide projections of their volumes and revenues. The lack of details related to revenue indicate that there are, in fact, no tangible nor quantifiable prospects.

Project Cargo: “The Redwood Marine Terminal is a suitable location for handling heavy and oversized project cargo that may, **on occasion**, move in and out of the region.” I have highlighted “on occasion” because this indicates that economic benefits are not predictable and; therefore, cannot be used as a basis for economic projections. If wave energy is tapped by PG&E off Humboldt Bay, the need for some long term Humboldt Bay support facilities may emerge.

Non Cargo: “In the past, Humboldt Bay has received occasional calls by research vessels, including vessels operated by the National Oceanic and Atmospheric Administration (NOAA).” Occasional is again the key word here indicating it is not a significant contributor to revenue, particularly with the reservations noted elsewhere in the *Business Plan*: “based on practices at other ports, such vessels may be offered discounts or waivers on some or all port charges.”

Aquaculture: The aquaculture use of the Redwood Dock is tangible and desirable, but does not necessitate large scale pier development or associated dredging. In combination with a museum complex and the Samoa Cookhouse, an aquaculture facility could also be a stop of interest for tourists (oyster tastings and sales?).

Timber Heritage Society/Railroad Roundhouse Museum: I favor the development of the Samoa museum complex, with the THS using the historic roundhouse as one element and an historic train from Arcata to Samoa as an anchoring feature. This venture, however, will only be possible with a sound business plan in place developed in close cooperation with the City of Arcata and the Arcata Economic Development Corporation. While I think this venture is desirable, the potential for a significant rental factor and revenue for the District in the next five years from THS is minimal.

Does the Level of Business Justify Borrowing for Multipurpose Terminal Construction?

The *Business Plan* recommends that in order to build the multipurpose terminal the District “issue revenue bonds tied to project revenues. The District has the authority to issue revenue bonds to fund construction of facilities (California Harbors and Navigation Code, Appendix II, Chapter 4, Article 4).” Table 1 below is taken from the *Business Plan* and details expenses for construction, which total an estimated \$32-38 million, depending on the cost of environmental clean up. The plan estimates payback as follows: “Over the assumed 23-year project life (3 years of development and 20 years of operation), the project generates an internal rate of return (IRR) of 14.3%.”

However, they hedge on their projection significantly:

“As stated in the Redwood Terminal Feasibility Study, proposed long term development will depend on trends in West Coast container trade, West Coast port capacity, rail connectivity to Humboldt Bay, and the competitiveness of the site versus expansion at existing ports and other secondary locations.”

Component	\$ Million
Terminal Improvements	\$18.11
Terminal Building Improvements	\$3.52
Terminal Utility Improvements	\$0.92
Development Fees	\$3.61
Construction Contingency	\$3.25
Total Cost (Excluding Items Below)	\$29.41
<i>Demolition and Environmental Mitigation Cost Estimates (10% to 30%)*</i>	<i>\$2.94 to \$8.82</i>
Total Estimated Cost	\$32.35 to \$38.23

Table 1. Taken from *Redwood Marine Terminal Business Plan* (p. 12).

In fact, different model scenarios show that, if cruise ship traffic levels or cargo amounts are not robust, the multipurpose terminal may not make money. Figure 9-5 from the *Business Plan* is captured here as Figure 1 and shows both positive and negative cash flow projections from 6 to 15 years out. The *Business Plan* accounts for potential losses as follows: “The poor performance under sensitivity # 2 reflect the lower revenues from cruise and cargo activity, and the fixed expenses, which do not decline with lower activity at the multipurpose berth.”

Given the lack of tangible prospects defined in the plan, I believe the likelihood of the multipurpose terminal losing money is very, very real.

The *Business Plan* also notes that costs of environmental review for construction of the multipurpose terminal will come out of District cash flow, which will likely add to budget deficits in the short term (next five years).

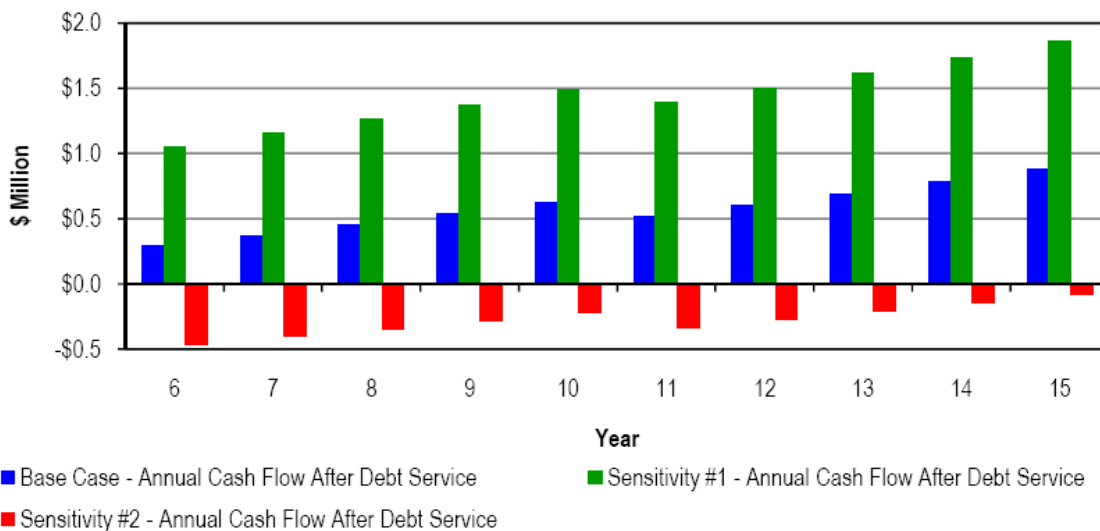


Figure 1. Projections of cash flow for the multipurpose marine terminal based on different model runs. Taken from the *Business Plan*, where it appears as Figure 9-5.

Potential Profitability of Larger Scale Shipping Venture

The assumptions of the *Business Plan* with regard to expanding West Coast trade, and the ability of the Port of Humboldt to compete for the international shipping have been refuted above. Despite the claim of Goldman-Sachs’ representative at a recent District meeting that they can find a buyer at auction to set up an international shipping terminal in Humboldt Bay, the fundamentals of the business are unsound and, even if capital were acquired, the venture would not succeed.

The PB Marine *Revitalization Plan* (sponsored by the District in 2003) states categorically that the Port of Humboldt is in a non-competitive position with regard to auto and container shipping because of small population base, distance from a national

rail hub and time and cost necessary to get goods to market. Their characterization stated that this was the case **even if the railroad was back up and running**.

The competitiveness of the Port of Humboldt Bay has not changed in this regard, shipping volumes are diminishing and competition is increasing.

The larger scale shipping business relies on the reconstruction of the North Coast Railroad Authority's (NCRA) rail line and would make the District and NCRA virtual partners:

“Innovative development structures could be considered, such as a coordinated concession process with the North Coast Railroad Authority in which the terminal project and rail corridor are granted under a single long-term agreement to a private sector investor and operator.”

The Business Plan makes the following qualification with regard to railroad operation:

“The NCRA has not currently indicated when it expects to reopen the full rail corridor to Humboldt Bay. Full corridor restoration will be dependent on the feasibility of restoring service through the Eel River Canyon (environmental impacts, addressing weather and geological impacts on the rail line, etc.), the capture of freight volumes to support the significant capital investment, and identification of funding sources. There is interest in transportation infrastructure from the private sector (pension funds, investment funds, etc.) and a viable rail corridor may be attractive to private funding sources.”

The FEMA estimate in 1998 for reconstructing the NCRA through the Eel River Canyon was \$640 million; therefore, the cost of reopening the line will be in the high hundreds of millions. There is little likelihood that sufficient investment capital can be lured into such an investment.

Redwood Marine Terminal Business Plan is Now Goldman Sachs Plan

I note a substantial change in strategy within the *Business Plan* from the *Feasibility Study*, where the District was to be the owner and operator of the Port. The new draft envisions a large scale capitalist operating the Port on a long term lease:

“The District will act as a landlord port authority and enter into an agreement for the lease, design, construction and operation of the Redwood Marine Terminal for major cargo terminal activities. The private sector operator would take over management of the existing improvements and business of the terminal (the multipurpose berth, cruise shipping calls, etc.), and agree to expansion of terminal facilities.”

It would seem that the Goldman-Sachs offer to auction the Port assets to international investors is now embedded in the *Business Plan*. The District needs to retain an independent financial advisor to help negotiate its agreement with Goldman Sachs, which

has a conflict of interest in its sales position, and cannot be trusted to act in the District's nor in our community's interests.

The fiduciary responsibility of upon us as District Commissioners requires that we approach this very complex and long term business relationship with both circumspection and with an augmentation of our negotiating team immediately. Further, I strongly recommend that we not enter into an agreement with Goldman-Sachs until there an environmental review is complete and government agency approval obtained.

Timing of Environmental Review

The District has deferred environmental review of industrial development of the Redwood Dock and it is time that such a review be conducted before the *Business Plan* is adopted and certainly before a deal with Goldman Sachs is signed. I have not made arguments related to environmental effects of large scale harbor development because I considered the prospect unlikely due to its lack of financial basis. In fact there are a number of potentially significant adverse environmental effects that must be considered, including:

- Effects of deep dredging extending to the Redwood Dock
- Increased invasive species introduction
- Potential water pollution
- Noise and light pollution
- Increased railroad traffic through Eureka and Old Town
- Compatibility with Samoa Community Development plans
- Appropriateness of scale and location

District Cash Flow and Business Plan Scenarios

The District will risk its future fiscal solvency, if it adopts the *Business Plan*. In the short term, the District will have to cover costs for environmental review sufficient to meet California Environmental Quality Act requirements, which will likely further erode our current asset base. The acquisition of \$35 million in bond debt, may keep the District afloat during construction, but if business levels are not sufficient, negative cash flow problems will be exacerbated. As noted above, positive cash flow scenarios in the *Business Plan* are based on speculative prospects for business.

The *Business Plan* gives the following time line for project development:

“As stated in the Redwood Terminal Feasibility Study, the projected timeline for development of the multipurpose berth is up to 5 years. The timeline for long term expansion will be driven by market conditions but is projected to be around 10 years, based on industry norms for terminal development from initial concept to completion. Both timelines are *flexible*.....”

It also states that timing of the Goldman Sachs offering of our assets for auction “will be determined by market demand for new terminal capacity on the U.S. West Coast.” While

the selling of port and railroad assets are supposed to “transfer risk to the private sector and minimize the risk exposure of the District,” in fact the greatest risk is if its investments in the multipurpose terminal are not profitable and large scale investment is not forthcoming. I consider this the most likely scenario.

I also noted recently in the press (Everett Herald, 6/11/08) that the Port of Everett, Washington is scaling back plans for development of an international container shipping terminal there due to very vigorous community opposition. I believe our District will encounter similar resistance here and should consider setting a different course of development than that laid out in the *Business Plan*. I think its adoption and moving forward with marketing the port/rail assets will not lead to a viable or sustainable business enterprise. Instead this course will not only risk the fiscal solvency of the District, but will also impede more viable courses of economic development as well as continuing to divide our community.

Sincerely,

A handwritten signature in black ink, appearing to read 'Patrick Higgins', with a large, sweeping flourish extending to the right.

Patrick Higgins

Table 1. Shipping categories and prospects according to Draft *Redwood Dock Feasibility Study*. Bold highlights indicate impediments.

Type of Shipping	Prospect
Bulk Cargo	“A likely requirement is to have a rail connection to transport recycled metals in from major population centers for processing and export.”
Container on Barge	“ Container shipping lines pointed out that very little international container cargo moves to and from the Humboldt County area due to the region’s small population and limited manufacturing base. Apart from the limited amount of container freight, container shipping lines stated that an important obstacle to COB service would be stevedoring charges at Oakland.”
Short Sea Shipping Market	“The commercial viability of a short sea shipping service for the Pacific Coast is under investigation with the focus on major freight corridors between Southern California, San Francisco Bay Area and the Pacific Northwest. If any of these corridors are deemed viable then consideration may be given to integration of secondary ports if they do not cause deterioration in the service quality between major ports. ”
Regional Freight Movements	“While the Port of Humboldt Bay is not being evaluated in current studies due to the small size of its market, it is reasonable that the same criteria would apply and that the majority of divertible cargo would be within a 50 to 100 mile distance of the port, essentially the Humboldt County hinterland. The hinterland may extend further inland if there is significant future congestion on the north-south I-5 truck corridor or new environmental regulations impose additional costs on trucking, which make short sea shipping more efficient than the I-5 corridor.”
Military Cargo	“On the West Coast, the majority of these shipments move through the Port of Oakland. Humboldt Bay does not currently meet the requirements to handle military cargo or to be a location for berthing of ready reserve ships. The development of new terminal infrastructure and the rail corridor may open up this opportunity for the port.”
Ready Reserve Force	“ The requirement for a full service port currently excludes Humboldt Bay as a candidate for berthing of RRF vessels. However, the District should periodically revisit this opportunity in case contracting conditions change in the future or if new terminal development takes place at Humboldt Bay that allows the District to meet contracting requirements.”
Autos	<i>Revitalization Plan</i> = NO. Redwood Dock Feasibility says some changes may occur, but very competitive.
Containers	<i>Revitalization Plan</i> = NO. The availability of a functional and efficient rail corridor between Humboldt Bay and the transcontinental rail system is a requirement to be considered for terminal investment and operation. The District must have a coordinated development strategy with the management of the rail corridor.