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# Brazil Railways Staff Retrenchment Program

PRL

Jan.15, 1998

# Brazil Railways

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- ◆ **Federal Railways (RFFSA)**

20,000 line-km, 35 billion ton-km, no passengers

- ◆ **Sao Paulo Railways (FEPASA)**

5,000 line-km, 6 billion ton-km, 1 billion passenger-km

- ◆ **CVRD Vitoria-Minas Railway (EFVM)**

900 line-km, 50 billion ton-km, mainly iron ore

- ◆ **CVRD Carajas Railway (EFC)**

1,200 km, 40 billion ton-km, iron ore

# RFFSA in 1995

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- ◆ Federally-owned Public Enterprise
- ◆ 40,000 employees  
down from 150,000 in 1957, when created
- ◆ Employee Productivity < 1 million TU/Emp
- ◆ Wage bill = 75% of expenditures
- ◆ Locomotive Availability: 53% decreasing
- ◆ Average Deficit: >US\$250m./year
- ◆ Debt: US\$3.0 billion, rapidly increasing

# Project Objectives

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- ◆ **Reduce Cost of Freight Transport**  
in Brazil's main corridors by 20% over 5 years
- ◆ **Improve Performance**  
through restructuring, and concessioning
- ◆ **Increase Productivity**  
through staff retrenchment and emergency repairs
- ◆ **Minimize Social Costs of Retrenchment**  
through severance pay, retraining, outplacement
- ◆ **Enhance Competition**, through regulatory reform

# Project Scope

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- ◆ **Restructure Operations & Assets**  
into 6 regional systems, separating rail/non rail assets
- ◆ **Reduce Staff by 22,000**  
to turn operations positive and attractive
- ◆ **Repair Locos & Tracks, in the Northeast region**
- ◆ **Reform Railway Regulation**
- ◆ **Settle Debt & Labor Liabilities**  
through revenues from sale of non-rail assets

# Implementation Progress

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- ◆ Project approved in June 1996 (\$350m.)
- ◆ Staff retrenchment completed  
retraining & outplacement still underway
- ◆ Repairs in Northeast 90% complete
- ◆ Concessioning completed  
all 6 concessions in operation from July 96-Jan 98
- ◆ Regulatory Reform still underway
- ◆ Financial Restructuring on track

# Staff Retrenchment Objectives

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- ◆ **Increase productivity**
  - remaining railway staff
  - laid off employees (retraining & outplacement)
- ◆ **Minimize social costs of layoffs**  
incentives, severance payments
- ◆ **Turn operations profitable** prior to sale  
to sell concessions for a positive price (no subsidy)
- ◆ **Reduce labor opposition to privatization**

# Staff Retrenchment Design

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- ◆ **analysis of regional labor markets**
  - modest qualifications of labor, jobs of poor quality
  - av. probability of being re-employed: .64 to .83
- ◆ **analysis of redundant staff profiles**
  - Avg age 40, limited education, limited skills,
  - paid 10-30% above corresponding market average
- ◆ **design of training, outplacement programs**
  - targeting job or business opportunities
- ◆ **design of incentives, severance packages**
  - avoid reduction of standard of living while unemployed

# Staff Retrenchment Components

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- ◆ **Incentives for early retirement**  
if at least 50 yrs old, 6 months salary
- ◆ **Incentives for voluntary separation**  
4-12 month salary (av. \$8,000) + legal entitl.(av. \$10,000)
- ◆ **Severance pay for other redundant staff**  
80% of incentive + legal entitlements
- ◆ **Retraining** (official training institutes , 150h. \$2,000)
- ◆ **Outplacement assistance**

# Economic Analysis

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## ◆ Costs:

- incentives and severance payments
- training and outplacement costs

## ◆ Benefits

- net increase in marginal productivity of redeployed staff
- marginal gain from avoided labor cost of RFFSA

◆ NPV(12%): US\$600m.

◆ Rate of Return: 40% (19% in NE, 50% in SE)

# Outcome so far

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- ◆ **20,000 redundant staff laid off by RFFSA**  
14,000 early retirement, 6000 voluntary sep. (\$320m.)
- ◆ **10,000 staff laid off by concessionaires**, using Government schedule of payments
- ◆ **600 in residual RFFSA**
- ◆ **1,000 retrained**, mainly for self-employment
- ◆ **Outplacement delayed, now operational**
- ◆ **Survey of laid-off staff** available in march 98

# Bank Financing of Severance Pay

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- ◆ **First Investment Project** with severance financing
- ◆ **LEG opposed**, productive investment issue, image
- ◆ **OPR used project as test case to OPC**
- ◆ **OPC decision:** minutes of Feb. 9, 1996 meeting
- ◆ **OPR memo to staff:** March 5, 96 “clarifies” policy
- ◆ **US abstention on Project:** June 20, 1996
- ◆ **Informal Board Meeting:** July 17, 1996

# Severance Pay Financing Policy

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- ◆ Adjustment Lending (SALs, SECALs, PERLs)
- ◆ Investment Lending: Productive Investment
  - ① in context of reforming public enterprise(s) only
  - ② design, justification based on increased productivity
  - ③ no restriction on share of severance pay in project cost
  - ④ macroeconomic, sector policies satisfactory, sustainability
  - ⑤ avoid over/underpayment, rehiring by public enterprise
  - ⑥ address social costs, avoid adverse publicity to Bank
  - ⑦ OC review of first several operations

# Lessons Learned

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- ◆ Severance package results from negotiation between management & staff, never optimal, acceptable
- ◆ Stimulate, guide mgt dialogue with unions
- ◆ Loan turned severance packages credible and reduced labor opposition to privatization
- ◆ Timing is tactical  
regulation, institutional reform can be fixed, refined later
- ◆ Training & Outplacement take time