

How Las Vegas transport gamble turned into a one-track ride to ruin

It is billed as the easiest way to visit New York, Venice, Paris and the Sahara in a single day. But a slick USD 650m monorail linking Las Vegas's famous casinos is in trouble – and its problems are causing a headache on Wall Street.

Plastered with Vegas logos, the elevated train plies a route behind the vast hotels that line the Strip – the desert city's main thoroughfare, where tourists can peruse live lions, dancing fountains, a roaring volcano and a miniature Eiffel Tower, not to mention live shows by the likes of Bette Midler and Cher.

Conceived as a way to ease the Strip's traffic jams, it was opened with classic Vegas pizzazz in 2004 when Nevada's governor took an inaugural ride flanked by showgirls wearing 4ft headdresses. But since then, passengers have been hard to come by. Instead of the forecast 54,000 customers, the monorail is attracting barely 21,000 users a day.

On a sunny afternoon this week, passengers were few and far between. At the Flamingo stop, halfway down the strip behind a casino built by the mobster Bugsy Siegel, five people were waiting on the platform. „We're here because our feet are killing us,“ said Manuel Nieto, a tourist visiting from Albuquerque with his wife, Esther. „We walked for about 10 hours yesterday.“

The Nietos complained that the monorail is expensive at USD 5 a trip. That's partly because, unusually for a public transport project, it was funded entirely on borrowed money without a cent of subsidy from taxpayers.

Three tranches of debt were used to pay for the monorail. Lower tiers of USD 49m and USD 149m are plain vanilla risk-bearing notes held by public and private investors. But the biggest chunk, USD 450m of „senior“ debt, carries the name of Nevada’s department of business and industry and is insured by Ambac, a monoline insurer that is one of the US’s biggest financial guarantors.

At the end of January, the credit-rating agency Moody’s declared that barring an unexpected surge in passengers, the monorail will be unable to keep up repayments on its loans beyond 2010. Although the bonds’ insured status gives them a blue-chip AAA rating, Moody’s downgraded their underlying risk of default to a junk status, Caa2 – the third lowest level on its scale.

„Ridership levels haven’t been at the level expected really since the inception of the project,“ says Moody’s analyst Denise Person.

That verdict could hardly be worse for Ambac. Together with its monoline rivals MBIA and FGIC, it is facing huge liabilities after diversifying from its traditional strength of municipal bonds into backing mortgage-related securities. It lost USD 3.26bn in the fourth quarter.

Ambac has had its credit rating cut by Fitch and is on negative watch by Moody’s and Standard & Poor’s. A downgrade would mean a slump in the value of all the bonds it backs, prompting multibillion-dollar write-offs by Wall Street banks. The near certainty of a big payout on the Vegas monorail only compounds its problems – and it could even find itself operating the unloved railway. „As soon as Ambac makes a payment, they enjoy a range of step-in rights,“ says Moody’s analyst Bart Oosterveld. „They would basically take over the asset.“

Backers

The debacle is a deep disappointment for Nevada's monorail backers, who achieved a rare distinction in keeping a major transport infrastructure project off the public books. In Britain, light-rail schemes have generally required government aid. Between 1980 and 2004, seven systems were built, including trams in Birmingham, Manchester and Croydon. They cost GBP 2.2bn, of which GBP 1.2bn came from the government.

„The fact that it was all built with private money is amazing,“ says Larry Fabian, a Boston-based expert in light-rail projects. „Is there anything comparable in the US or in Asia?“

Bad luck has played a part. Bits starting falling off the trains within a few months of the opening, prompting a 14-week shutdown. And efforts to set up a system that would allow hotel guests to use their room key cards as tickets were frustrated. But critics say there are more fundamental problems. The line is hard to find, running through the back yards of hotels. It offers views of cooling towers, car parks and generators. And, crucially, it does not run to the airport. „If they don't connect to the airport, the whole thing is really stupid,“ says Fabian. „The real problem lies not with stupid investors but with dumb public officers who didn't cooperate with it properly.“

Wendell Cox, a transport consultant who advised opponents to the scheme, says many visitors to Vegas enjoy strolling along the strip on foot and have no desire to get on a train.

„The Vegas street scene is one of the most interesting street scenes in the US,“ he says. „I don't believe there is any way this kind of project could make money. I predicted it would go broke by 2007. I must admit I was wrong about that. It'll probably be 2010.“

Ambac has admitted that it is reserving cash for a default. A spokesman said: „It's been on our radar.“

Since the credit crunch began, the insurance firm's shares have dived by 90%. There is a chance, albeit still remote, that an evaporation of confidence among clients could drive it out of business. If so, the retail holders of monorail bonds will find themselves out of pocket – an extremely unusual event for triple-A-rated instruments.

The future is uncertain. The monorail company points out that its revenue is covering day-to-day operating costs, making liquidation foolish. Public subsidies would be controversial among taxpayers, since the train is largely to carry tourists rather than residents. In the worst-case scenario, a contingency fund exists to demolish the tracks – which would be an inglorious failure for a city proud of its prowess at judging the odds.