

Competition and Markets Authority
Victoria House
37 Southampton Row
London
WC1B 4AD

Our ref CMA/15/001

Your ref

16 October 2015

Dear Sir / Madam

Competition in passenger rail services in Great Britain – A discussion document for consultation

Thank you for consulting Transport for Greater Manchester (TfGM) on the above discussion document. TfGM is responding in its role as the Executive of the Greater Manchester Combined Authority (GMCA). TfGM is the public body with responsibility for implementation of Greater Manchester's Local Transport Plan (LTP), which aims to strengthen Greater Manchester's economy through securing the delivery of a range of projects, service improvements and initiatives across the full range of Greater Manchester's transport modes. TfGM's remit includes responsibility for the Metrolink light rail system, investment in the bus network, strategic management of highways and the promotion of active travel such as cycling and walking.

TfGM has a statutory duty to keep under review the railway passenger services provided within Greater Manchester and its surrounding area. The LTP recognises that the rail system is particularly important for economic growth as it has the scope to both support more commuting and to provide crucial links between our economy and markets elsewhere in the UK. As a result the expansion of the rail network through projects including the Northern Hub is identified as a key priority for the GMCA. It should be noted that separate responses will be submitted by Rail North and by the Passenger Transport Executive Group (Pteg). GMCA is a member of Rail North and TfGM is a member of Pteg.

Rail Devolution

TfGM has worked with 28 Local Transport Authorities and Combined Authorities comprising Rail North with the aim of securing devolved control of rail services across the North. Rail North and DfT are working under a Partnership Agreement that will see the new Trans-Pennine Express and Northern Rail franchises

managed jointly by Rail North and DfT from April 2016. The specifications for both franchises were developed jointly by Rail North and DfT, drawing on expert local knowledge and experience. The transformational franchise specifications in the Invitations to Tender published in February 2015 were the result of considerable evidence gathering, option assessment and detailed analysis. TfGM is confident that the detailed understanding of service requirements linked to economic and social needs across the North of England will provide the services that are required, within Greater Manchester, across its boundaries and across the North of England.

The Franchising competition is using Contract Specifications that are less prescriptive than previous. The two franchises, Northern and Trans-Pennine are arranged similar to Option 2b in the consultation, but less evenly balanced than 60:40. The new Northern franchise has some more profitable, regional express services transferred-in from Trans-Pennine (and the bidders are encouraged to develop further services); and Trans-Pennine has an increased number of local flows.

The CMA Consultation

The basic premise of the consultation appears to be that there would be benefits from a greater degree of IN the market or on-track competition, in passenger rail services across the UK. The discussion document argues that these benefits would include; better quality of service, lower fares, more innovation, and more efficient use of available capacity all contributing to an increase in rail patronage. It also identifies issues in achieving greater on-track competition and a number of problems that would result from it. These include; current capacity constraints on the network, network planning and operational complexities, revenue abstraction from franchised operators and inflated bid costs, reduced ability to cross subsidise unprofitable services with profitable ones and reduced financial stability of rail operators.

The discussion document concludes that the above issues can be overcome and therefore more on-track competition is achievable and will have positive outcomes. Four options are proposed for how this could be achieved in practice intended as long-term proposals for inter-city routes (West Coast, East Coast and Great Western) and not intended to apply to commuting services.

TfGM does not consider it is either feasible or desirable to substantially increase the amount of on-track competition in the delivery of passenger rail services and to try and do so would make it more difficult to deliver an integrated public transport network that can underpin the economic growth of Greater Manchester.

The franchised passenger railway in the UK is based on the principle of competition FOR the market. As the consultation makes clear, there is and has been very limited competition IN the market, through entry to the market of Open Access (OA) operators. There are a limited number of examples of OA operators reducing fares in competition, creating new direct links from stations without them previously or introducing product innovations. However it is difficult to see how OA operations will actually drive down the overall operating costs. In fact, due to diseconomies of scale, the need for duplication of facilities (train fleets, crews, management, maintenance facilities, back-office infrastructures) it will often have the opposite effect. Where OA operators have entered the market this has led to abstraction from the incumbent franchised operator even where the overall market has been grown by the greater choice of service, for example Grand Central between York and London Kings Cross. Abstraction from the franchised operator in turn leads to higher costs within the franchise and a decrease in Premium (or increase in Subsidy) and by default investment. As the core regulated fares are set by Government the only pressure on fares is on the Advance Purchase (AP) tickets excluded from the Fares Basket. There are sometimes uplifts in quality evidenced as a result of on-track competition, but due to the difference in Track Access charging and the restriction on the dominant operators to manipulate the market place, the effects of competition between operators is relatively minimal.

It is apparent from the history of open access operations in the UK that there are very limited, if any, flows that the market would consider sufficiently attractive that do not serve London. We note with interest the approval by ORR to the Blackpool – Queens Park Open Access application from Alliance Rail Holdings (owned by DB). This service will pass through the Manchester City Region without calling (the Warrington Bank Quay call having been refused by ORR).

Passenger Services in Greater Manchester and the North of England

Good links to London on the West Coast mainline are important to the economic development of the region and Government policy to rebalance the national economy. These links are about more than price or fares, as considerations such as journey times, access to trains at a number of stations (not just central Manchester), service frequency and length of operating day, punctuality and reliability, ease of use, and the availability and comfort of seats are all important passenger requirements.

Within Greater Manchester there are currently no OA operators, but there are six different franchised operators providing a wide range of passenger services, in some cases clearly competing with each other on speed, frequency, quality and in

a few cases price. These six franchises provide competition IN the market between Manchester and Liverpool, Preston, Leeds, Sheffield, Stoke-on-Trent, Crewe and Chester. Therefore all the main short / middle distance inter-urban markets are competitive with 3 franchised operators on all of these flows except Preston, Leeds and Chester which each have 2 franchised operators. However there is little evidence this competition has encouraged better quality services or any innovation. Old rolling stock of a low standard continue to be used, with overcrowding / standing for long periods of time a common occurrence.

The main problems faced by rail passengers in Greater Manchester do not arise from a lack of IN the market competition but are due to (unpredicted) high demand growth and an on-going under provision of capacity that has produced some of the highest levels of crowding¹ and some of the oldest and least reliable rolling stock in the country.

This is being partially addressed through rail devolution (discussed above) and the current refranchising process for the Northern and Trans-Pennine Express franchises. TfGM considers this is a much more efficient means of meeting service levels than for an OA Operator to provide, as the latter would seek to choose the most commercially advantageous flows at the cost of sub-optimal network utilisation. Indeed Franchising allows (at least in theory) for co-ordinated utilisation of available capacity, whereas an OA operator will be more interested in running services on the most commercially viable lines stopping where the flow is commercially advantageous and this may result in sub-optimum utilisation.

There are a number of franchised train operators, often competing on specific routes or flows in the Greater Manchester area, Table 3 in the CMA consultation document fails to recognise this. Taking the South Manchester corridor as an example, there are six TOCs operating in and out of Manchester Piccadilly, all of which serve the Manchester to Stockport market (being Virgin West Coast, Arriva Cross Country, Arriva Trains Wales, Trans-Pennine Express, East Midlands and Northern). This is on a par with the largest number of operators along a single stretch of route anywhere in the UK. South of Stockport the Macclesfield line carries three operators, the Crewe line carries four and the Hope valley line to Sheffield carries three.

Northern Rail, with an hourly service between Manchester Piccadilly and Stoke-on-Trent (operated by 3 car class 323 Emus), is the dominant operator and therefore sets the inter-available fare. There is a Virgin Trains fare that undercuts

¹ Further information on overcrowding on Greater Manchester rail services can be found at: <https://www.gov.uk/government/statistics/rail-passenger-numbers-and-crowding-on-weekdays-in-major-cities-in-england-and-wales-2014>

the Northern fare and Virgin operates two trains per hour on this corridor, one of which links Manchester Piccadilly, Stockport and Stoke-on-Trent with one calling additionally at Macclesfield. The Virgin trains are operated by 11 and 9 car Pendolino trains. In addition, there are two Arriva CrossCountry trains per hour on the Manchester Piccadilly to Stoke-on-Trent corridor, formed of either 4 or 5 car Voyager trains.

While setting the inter-available fare, Northern provides less frequency and less capacity on the corridor than the other operators combined. Virgin is able to charge a lower walk-on fare while providing greater capacity. The CMA dictate that the “dominant” operator cannot move to undercut, thus preventing any further competitive pressure (but protecting against coordinated use of pricing tactics to destroy competition). Due to these ticketing rules, Northern is prohibited from offering a lower priced non-advance own operator fare between Macclesfield and Manchester where it specifies the inter-available fare. This IN the market competition between franchised operators has already led to major demand movements from Northern to Virgin services, under-mining the former’s revenue but restricting over-crowding and therefore saving them the additional costs of providing additional rolling stock. Even if capacity constraints permitted OA services, it is difficult to see how an OA operator on this corridor would add any further value.

Table A below identifies rail routes in the Manchester City Region with more than one TOC providing services.

Table A – Manchester City Region competing TOC summary

Route	TOCs	Notes
Manchester-Stoke-on-Trent	VT, XC, NT	
Manchester-Crewe	VT, XC*, ATW, NT	* = peak times only
Manchester-Liverpool via Warrington Central	TP, EMT, NT	
Manchester-Liverpool via Earlestown	TP, NT, ATW	
Manchester-Preston	TP, NT	
Manchester-Leeds	TP, NT	
Manchester-Sheffield	TP, EMT, NT	
Manchester-Chester	NT, ATW	

Capacity Constraints

Current capacity constraints on the network limit the practical scope for new entry in the market by OA operators at present. However the CMA consultation relates to long term proposals for the development of the network and is based on the assumption that additional capability will be generated through infrastructure improvements. In reality, in the North of England, increases in capacity or capability have significantly lagged behind growth in demand, to the extent that the current network is highly congested and the industry regulators are forced to make difficult decisions about capacity allocation. Whilst network capability will be increased by the committed North of England Programmes (Northern Hub and North West Electrification) these enhancements are required because of existing overcrowding and forecast growth in demand and will be fully utilised from December 2019 by franchised operators.

Potentially ERTMS could further increase capability, however the main constraints in Greater Manchester are the number and length of platforms (which are not helped by ERTMS) and complex track / junction layouts (which ERTMS can only partially address). HS2 will not reduce the number of trains on the classic network because it does not have stations at every location currently linked to Manchester by the London / Birmingham trains. All the trains to / from Manchester (local and long-distance) planned to operate from December 2019 will continue to operate post HS2 as they are required for access to employment / journey to work trips (and business trips to other towns and cities) and are therefore essential to the local economy.

Public sector investment in additional capability needs to be supported by a business case incorporating a pattern of train services which are expected to operate and use the spare capacity created, hence the ORR's duty to have regard to the interests of funders in its allocation of network capacity. The public sector can not, invest speculatively in additional infrastructure capability and capacity to create more train paths that may or may not be utilised by an OA Operator.

Completion of the fourth platform at Manchester Airport has been followed by a track access application from Arriva Trains Wales (a DB company) to extend the Llandudno – Manchester Piccadilly service to Manchester Airport, effectively on an open access basis, now that a platform is available at Manchester Airport; capacity is presently available between Piccadilly and the Airport. If this is granted, it is not clear where that will leave the future Ordsall Chord services from Bradford to Manchester Airport, or other services for which the extra Northern Hub capacity was intended and thus funded.

Fares and Ticketing

The fully inter-available fare charged by a lead TOC for each station to station movement is set by DfT through franchise specification and any increase is also controlled by Government. Only other TOCs can offer walk-on single operator tickets which undercut the inter-available fare. Therefore the only effect on fares that more on-track competition will have will be on Advance Purchase (AP) tickets. All operators serving station to station flows can offer, at their commercial risk, AP tickets, but generally in Greater Manchester, Northern has declined to do so until very recently with the direct award.

Advance purchase fares limited to specific trains alone were developed by British Rail in the 1990's, but have taken off since the award of the 2005-8 round of franchises, in particular West Coast, Cross Country and Trans-Pennine. These advance products can offer significant discounts on the all operator walk on fares but at the cost of a major loss of flexibility. In essence a rail passenger has a choice of one train a day rather than the apparent 3 trains per hour. What advance purchase fares do provide is a demand management tool used to match demand and supply and relieve overcrowding at peak times offering much more affordable tickets to those willing to travel outside of the peak.

It is interesting to note that Arriva Cross Country has recently been permitted by DfT / ORR to introduce "on the day" AP tickets which have effectively circumvented the ban on the lead operator offering a single operator walk on fare. This initiative could potentially lead to the widespread use of this practice, effectively under-cutting other operators and reducing the value of a regular interval train service across all operators on a route, something TfGM would not support.

The current fares proposition is extremely complex with ticketing priced according to operators involved, time of day and varying by line of route for sometimes now irrelevant historical reasons. The current method for allocating revenue from inter-available tickets is a poor representation of travel patterns, hopefully smart ticketing will help address this.

The Department for Transport (DfT) issued Tender Documents for the Northern and Trans-Pennine Express rail franchises in February 2015, including requirements for smart ticketing. Franchise bidders were not permitted to propose their own smart ticketing schemes and were asked to demonstrate compliance with existing implementations. The new franchises are due to commence in April 2016 and TfGM has been in active discussions with prequalified bidders on a range of subjects including smart ticketing. TfGM is playing a lead role in the 'Transport for the North' discussions around smart

ticketing and in supporting the development of the business case for 'Smart in the North'.

Response to options identified by CMA

The consultation document identifies the following four options to increase competition in the passenger rail sector. TfGM response to each option is summarised below.

Option 1: Existing market structure, but significantly increased open access operations

While additional network capacity is due to be made available following completion of the Northern Hub infrastructure investment, the service development plans identified in the joint timetable development carried out by the Rail Industry, with the involvement of TfGM, identifies long term service plans that would utilise most of if not all of the additional capacity. As both of the current franchises to be renewed (Northern and Trans-Pennine Express) are subsidised, it appears highly unlikely that Open Access would be an attractive market proposition, even if paths became available. TfGM would be concerned at a loss of franchise value on the Northern and Trans-Pennine franchises, which we are working with DfT and Rail North partners to devolve. The potential for greater OA services can result in franchise bidders factoring in potential abstracted revenue and therefore increasing the subsidy.

In general, competition IN the market will only be possible with enhanced infrastructure capacity. The consultation accepts that expanding on rail competition is likely to have the greatest benefits on the three main commercial intercity routes (West Coast, East Coast and Great Western). Although HS2 will increase the capability of the network as a whole, the commuter services to / from London Euston are already overcrowded and therefore if that problem is to be resolved it is unlikely there will be much opportunity for longer distance Open Access services competing with HS2. Elsewhere in Greater Manchester, although enhanced signalling will increase capacity of the network at some locations, at the main terminal stations little more can be achieved to increase capacity due to their constrained city centre sites that limit the number and length of platforms and track layouts. Any spare paths could be used for increasing the freight market where there is a need, as these are OA services that would not abstract from incumbent franchise operators revenue.

Network Rail targets are currently based on punctuality / reliability and network availability. With more emphasis on more trains due to OA operations there would have to be greater emphasis on service frequency and journey times. To

achieve higher service frequencies / better journey times Network Rail may need to restrict the type of train that can operate at certain times / places. This could increase the cost of franchised operations (because new trains would be required) and reduce the number of freight trains that can be operated (with significant social / economic cost).

If unprofitable but socially valuable services are given priority on the network, at some times of day there will be little opportunity for OA services. If OA operators are given priority there will be social / economic costs (e.g. lack of access to employment) as a consequence of unprofitable but socially valuable services not being operated.

If the number of train operators / trains, and TAC paid, is continually changing this will make it extremely difficult for Network Rail to manage their business effectively. If OA operators are to be given higher priority the franchise specifiers will need to know their intentions before they can specify the franchise services, but if OA operators can change their service offer on a regular basis this could result in a need to revise franchises, at considerable public cost.

With enhanced dependency on OA operations it would cease to be possible to assess how any future infrastructure enhancement would be used, therefore the design standards / capability /cost could not be calculated and the value of benefits could not be ascertained, making it very difficult to develop a social / economic justification for future public investment in the network infrastructure.

If OA operators were to become a more significant part of the national network, government will have to accept a role as operator of last resort to ensure continuity of service between key economic centres.

Option 2: Two franchisees for each franchise

As already reported the routes around Greater Manchester already feature much potential IN the market competition from a number of franchised operators. Passengers are already presented with a wide choice of ticketing options where they have to trade off flexibility against cost. Actively encouraging two franchises per area could increase the complexity further and cause confusion amongst passengers and it is not clear that this option would necessarily add any additional competition. Potentially it could also lead to a reduction in standard pattern timetables as is currently enjoyed and encouraged by TfGM.

Practically, the letting of two franchises for a single area would prove very problematic with each bidder having to make assumptions about the other operators' services and the reconciliation of the two bids could lead to many

challenges in the process. This has certainly proved to be the case for the new Northern and Trans-Pennine franchises.

There could also be issues relating to the ability of the franchise support industry in resourcing such duplication of bids, as well as the willingness of bidders to commit to such a number of potential bids. However DfT had no difficulty finding six bidders, three each for the new Northern and Trans-Pennine franchises.

Given the inter-dependence between two franchises covering a single area and the scope for one to under-mine the other, there would appear to be greater scope for an operator to fall into difficulties and hence the Government having to step in as Operator of Last Resort.

It is interesting to note that recent DfT policy has been to remove duplication, with Thames Trains and Great Western combined from 2006, Great Eastern and Anglia combined from 2004 and most recently Thames, Southern and Great Northern in 2015. This policy has been justified on the basis that a single operator per major London terminus will help to simplify operational planning. This proposed option to duplicate franchises would seem to contradict this policy and make operational planning more difficult. In addition, the provision of many more franchises with their associated franchise letting cost and headquarters function costs; would result in increased fares or higher subsidy and would seem to contradict the McNulty principles of driving down the costs of the railways.

Option 3: More overlapping franchises

As evidenced by Table A above, the Greater Manchester area already has much duplication or overlap of franchises but this has not necessarily resulted in greater competition, reduced fares or better quality services. On the Manchester – Leeds and the Manchester – Preston corridors neither franchised operator has attempted to reduce fares because demand is now very high and peak time services are already overcrowded. Nor has either operator attempted to address overcrowding, in part leaving it to the other to resolve, increasing capacity by introducing additional rolling stock would be costly for either operator and therefore the issue has not been resolved.

The new Northern and Trans-Pennine franchises have been simplified with the transfer of Barrow, Windermere and Blackpool services from Trans-Pennine Express to Northern and the transfer of the Manchester – Huddersfield and Huddersfield – Leeds local services from Northern to Trans-Pennine Express. These service transfers are a clear attempt to allocate primary responsibility for each corridor to a single operator to try to resolve the issues discussed above. In

the Greater Manchester experience, overlapping of franchises to encourage greater IN the market competition has not worked.

Services on the Liverpool – Manchester corridor are provided in three overlapping franchises, Trans-Pennine Express (TPE), East Midlands Trains (EMT) and Northern. Traditionally each TOC has operated 1tph, TPE’s Liverpool – Scarborough and EMT’s Liverpool – Norwich services via the CLC route through Warrington Central and Northern’s Liverpool – Manchester Airport service via the Chat Moss. Noting the success of growing the Leeds – Manchester market, which was smaller than the Liverpool – Manchester market, in 2007 the original North West RUS justified and recommended a fast service of 4tph between Liverpool and one station in central Manchester. Nothing happened. This recommendation was repeated, with fresh justification, in the following Northern RUS, but status quo prevailed until 2014, when TPE persuaded the DfT that introducing an hourly Liverpool – Newcastle express service via the Chat Moss and Manchester Victoria would be a better use for the 7 class 185s released by conversion of the Manchester – Scotland services to electric operation than the DfT’s original proposal for strengthening existing services between Manchester and Leeds or York.

This is a clear illustration of the failure of three overlapping operators to develop a market, but also that each of them was acting perfectly rationally in accordance with economic theory; there is every incentive for a private company not to invest its own capital if it can instead achieve a return from investment made by other parties (in this case through the rail industry’s revenue allocation systems), so each operator waited for one of the others to make a move. Finally, with diesel units available, TPE calculated that it would make more profit from deploying them on a new Liverpool – Newcastle through service than from merely providing the additional capacity between Manchester and Leeds requested by DfT, and offered this alternative, which the DfT accepted.

The positive advantages of introducing yet more overlaps would therefore appear to be weak and would add little IN the market competition. In fact it would be likely to lead to greater operational inefficiency with existing operators having the extend dwell times or journey times to fit within the new operators. There is also the real risk that more operators interacting on and already congested network will give rise to more instances of compensatory events arising between operators, resulting in further inefficiencies. The overall results are likely to be increased passenger confusion, greater operational costs, revenue abstraction between operators and the need to draw higher public subsidy in total. As such TfGM cannot support this proposition.

Option 4: Licensing multiple operators, subject to conditions (including public service obligations)

This option as described seems to introduce a high level of complexity in the procurement process, with trading between bidders, selection of service groups and potentially one operator choosing the profitable set of services and leaving others with a collection of high subsidy services. Currently the franchising process in the main allows for cross-subsidy of services but this approach could undermine this policy. Public money is used where it is required to subsidise passenger rail, because revenues only capture a portion of the economic value of the rail network. There is a need to provide sustainable, efficient transport for the benefit of the economy, a need to which the rail network is able to contribute towards substantially. Allowing this approach would leave a large loss making part of the network which is then likely to lead to political pressure for service degradation in times of financial austerity.

It is also likely to lead to a major inefficiency of operation with the most profitable services likely to be quite disparate and requiring small pockets of operation. Issues such as allocating station calls to operators and depot access could become driven by the market alone. This could potentially replicate to some degree what has been observed in the deregulated bus market where the trunk profitable routes see enhancements whilst the less profitable parts of the network could see a major if not total loss of services. It is likely to lead to greater draw upon the public purse to maintain the uncompetitive routes, and would not seem to bring the CMA desired IN the market competition as most passengers would still only have a single operator for the majority of their journeys.

Where a train operator has a mix of profitable and unprofitable services (which would be the case if OA operators were required to operate some unprofitable but socially valuable services), management will tend to concentrate their efforts on the services that are profitable. This could result in the unprofitable not being developed to their full potential with the emphasis on cost reduction, not revenue growth and a failure to identify opportunities to develop revenue.

Summary

TfGM believe that this consultation process has started from the wrong position. The contention is that there is not enough competition within the service offer and hence that costs and subsidies are pushed up. This is despite very healthy competition being evident for recently let franchises with high levels of premiums (or low levels of subsidy) being offered.

If the focus is upon quality and the passenger, (as has been stated in the franchise process post the Brown review), then adding additional levels of government specified complexity, would seem to have the opposite effect. Perhaps the focus should be more on trying to improve on the current operation of the market, such as attempting to ensure that passengers are offered, and fully aware of, the most appropriate ticket for their travel requirements, allowing them to make an informed choice between price and flexibility. It is important to remember that the prime competitor to rail is the car, certainly in the Greater Manchester area, and the car mode does not provide the limitations which multiple operators and multiple ticket choices present.

Advance purchase, multi-operator services work best for longer distance routes where pre-planning of journeys is evident, presenting a market more akin to that of air travel. However providing a good value, unified public transport mode within an urban and inter-urban area which is priced competitively relative to the car for turn up and go journeys, for short to medium length journeys is a key facet of rail which should not be sacrificed for the perceived need for greater on-rail competition.

On the three routes suggested for increased on-track competition there is a strong London focus, which is met by the long-distance TOCs, with other TOCs catering for more local flows. However, especially away from London, there could be considerable benefit if the long-distance operators were required to accommodate local flows, especially at peak times. This could reduce the quantity of expensive operating resource needed for services such as Manchester-Stoke-on-Trent.

I hope you find these comments useful in the development of further work in this area. We are happy for CMA to publish this TfGM response to the consultation.

Yours faithfully

Amanda White
Head of Rail