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Local and Global **Transport and Logistics** Research

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Competition and Markets Authority
Victoria House
37 Southampton Row
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Dear Sirs

I am writing in response to your call for views on your document *Competition in passenger rail services in Great Britain*. I am not directly involved in the passenger rail industry itself. I am, however, chairman of a small transport consultancy (MDST) that works extensively in the rail industry, does have a number of clients (developers) interested in opening new stations but more particularly has been responsible for national rail freight forecasts (for Network Rail), for reviewing infrastructure charges and competition issues (for ORR) and assessing the competitive opportunities for rail freight, new rail freight terminals over 25 years and the capacity and utilization issues that need to be taken into account.

I have also a wide experience of the ports, shipping and distribution industries which have, I believe, lessons to contribute in the effective operation of transport entities in the private sector. I feel I may be able to make a number of helpful observations.

By your paragraphs:

10. one problem is that 'innovative solutions' are being judged by officials and not by consumers through market processes.
11. in my experience head-to-head competition was essential in promoting greater efficiency and reliability in the freight sector (almost entirely unsubsidised) and that the supermarkets would never have started to develop rail freight services and invest in rail linked distribution centres without it. True competition would allow the direct or indirect engagement of a much wider range of actors and allow the uplift in property values that can stem from passenger rail access to benefit the passenger rail industry to the benefit of the public purse. The railway industry fails to tap this huge resource because it concentrates on a 'internal' money go round model that means it cannot properly tap 'external' financial opportunities..

14. the present franchising system institutionalises fare increases; incremental efficiency gains may benefit either the operator or the State in so far as the operator gambles heavily on making such gains in tendering his bid. The passenger gains little from such efficiency benefits.
15. as you discuss in later paragraphs the franchise system involves a massive cross subsidy between different parts of the passenger rail industry. Such network benefits that this justifies could be captured through other mechanisms.

I would not recommend distinguishing between commuter and long-distance operators in deciding which routes or franchises to modify. 'Commuter' services compete with long distance operators (e.g. London Midland in competition with Virgin between Crewe and Milton Keynes or Chiltern between Solihull and Marylebone in competition with Birmingham International to Euston) using less efficient and smaller trains which by their slower speed soak up more network capacity and can only offer lower rates because they are subsidised. Perverse incentives creep in and there are no easy boundaries between the sectors.

17. one of the problems of the current arrangements is that Network Rail is not really incentivised to expand capacity and tends to be reluctant to change its timetabling standards (e.g. required time separation) and rules to expand capacity. It can also be inconsistent (see the various views it has taken re ECML capacity over the last few months and years) but the fact that it can only respond to conflicting requests tends to exacerbate the position. This quote from Network Rail's letter to the ORR on 2nd October with respect to East Coast Main Line capacity reflects the present position where no one appears to be able to grasp the nettle because capacity and calling patterns are inextricably interlinked:

"Since the capacity gain given by these enhancements [East Coast Main Line connectivity programme, now estimated at £331m], and their journey time and performance implications, is to some degree dependent on the pattern and routeing of services, it is not possible at this time to definitively confirm whether it is possible to run 8 LDHS [long distance high speed] services once the Connectivity outputs have been delivered".

This implies a most unsatisfactory way in which to manage investment in both infrastructure and the IEP new rolling stock programme (£1.2 billion for the 30 ECML train sets). It is worth noting that in the same document Network Rail confirms that one of the prospective open access operators on the ECML would be able to time their trains at 216 minutes London to Edinburgh (as compared with the franchised service offer of a 240 minute timing), reflecting the advantages that a competitive framework could offer. Why would a privatised railway industry resist such opportunities if customer interests are to be respected?

I believe the Dutch (ProRail) have a different approach. Its infrastructure manager's expectation with respect to freight train operators (and I believe passenger services) is that they set out their requirements annually and it assumes the responsibility of managing the

timetable to meet their requirements. I refer to this option for Network Rail later.

18. The DfT is indeed concerned about open access operators diverting revenue from franchised operators but you deal with this later (and I broadly agree) by pointing out more competition is likely to promote more traffic to 're-fill' the capacity available. The answer is to find an alternative to franchising, which had its origins in the view at privatization that traffic could continue to fall and operators would require the safety net of the public purse to sustain services protected by political pressures. Instead, passenger traffic has doubled.

Freight has had a similar experience; the year of privatization was effectively the lowest point in freight volumes since the middle of the 19th century; it started to grow again once private operators emerged post 1994.

20. It maybe the ORR's policy objective but is not necessarily the DfT's.
23. One of the unfortunate aspects of open access operators to date is they operate with shorter trains (a consequence of being able to enter the market paying only incremental track charges). The objective should be to find ways of encouraging longer trains to achieve greater economies of scale, even in low density 'regional' markets where train splitting and joining (train sectioning) could be more encouraged.
25. Some capacity constraints maybe relieved by HS2 but the potential of cab signalling is probably over rated because present plans do not assume 'moving-blocks' except on newly built high speed lines. Other solutions (such as longer trains and train sectioning) should be encouraged.
28. If it was not for the UK not being party to the Schengen agreement the impact of international competition would already be with us. Why would a Eurostar not operate Paris – London – Leeds and not therefore compete for traffic between Leeds and London, After all, at one stage GNER was using regional Eurostar train sets itself on the route to Leeds?
31. You mention freight. Competition provided road hauliers, who had the confidence of the supermarkets, to buy rail capacity through competing freight train operators and so expand the rail freight market; that was a crucial step. The supermarkets had confidence in the hauliers if not the train operators and therefore began to engage. Furthermore, the arrival of competition forced Network Rail to review its own practices with respect to path allocation. My company reviewed the then rail freight grant system for the Strategic Rail Authority in 2002 with a view to extending grants to any company (not just Freightliner). At the time there were only 14 freight train paths per day ex Felixstowe and there was a view that if several train operators shared that capacity added complexity would actually reduce the paths available. The same infrastructure is now supporting 31 paths and the Port has now built new terminal capacity capable of handling 50 trains per day. Sharing capacity need not be a problem. Unfortunately funding for physical network capacity upgrade has stalled and further rail demand is frustrated because existing capacity is compromised by operating a

heavily subsidised one car passenger train along the same single line. Franchising based on political factors can be counter-productive to the wider public interest.

32. There have been considerable freight efficiency gains through operating longer and heavier trains. Incentives should drive a similar trend in the passenger sector.
34. Effectively the DfT is encouraging such high peak period charging by the train operators in order to generate the franchise payments that partly fund Network Rail's fixed costs. However, there are other ways of achieving this, such as simply charging train operators higher infrastructure charges in the peak period (capacity charging on train numbers as well as gross train weight for incremental wear and tear charges). There is perhaps a lesson here from the ports industry, whereby statutory ports (the larger ones mainly now in the private sector) under the Harbours Act can simply charge dues that are 'fit' (meaning fit to discharge their duty to maintain the harbours). Should Network Rail be split into several regions under the current review then the opportunity would be available for the different 'regions' of Network Rail to be compared by the Regulator to ensure that the charges levied in different areas or on different lines were fair and reasonable, leaving the different Network Rail areas to balance their books. It would not be necessary for the ORR to check their cost break down.

The public sector may, of course, choose to directly assist some areas and regions directly if otherwise charges were to drive trains entirely off the network. That would eliminate the need for franchise arrangements assuming that trains always covered their incremental operating costs. If they fail to achieve even that then it would be open to the same local political entities to provide subsidies through franchises; increasingly in line with the gradual devolution of powers under way in the UK (such as through the formation of Transport for the North)..

35. Such price competition, which I agree takes place, is highly distorted by the different franchise arrangements for the operators involved and cannot be expected to lead to an optimum outcome as it attracts passengers to shorter and slower trains!.
38. It might be more useful to actually review train operators' cost structures, as the DfT already does for freight in determining the case for grant assistance. If the object is to achieve efficiency through competition, reducing costs that can then be enjoyed by passengers because there is competition, then almost certainly an important target is to attract as many passengers as possible onto longer trains and to consider how that might be best achieved, making best use of limited network capacity. A simple cost model for train operation needs to be in the public domain so that such matters can be openly debated and understood by decision makers.
43. The supply of rolling stock should not be a problem in a rising market providing it is genuinely interoperable and capable of being joined to more or less any other stock. Rolling stock owners should be relaxed about making investments providing stock is interoperable.

New rolling stock that requires the network to be modified should generally be discouraged (with the exception of tilting train equipment as this improves asset productivity by raising speeds on some routes). This would allow short term chartering to be undertaken and lead to a position where, like shipping lines and airlines, equipment can be hired in and off-hired allowing innovative service offers to be developed by passenger service operators. Inflexible long franchises would then definitely not be required.

44. A properly constructed timetable following well developed timetabling rules should mean trains of quite different characteristics can share the network without in any way affecting reliability. However, the more similar are train operating characteristics the more trains can be timetabled along a line in the first place; another argument for interoperability.
49. A solution that increases the cash required from the public purse is unlikely to be politically acceptable so this approach is not likely to be attractive. Furthermore an arrangement whereby open access operators were forced to pay more than incremental costs (unless there is a capacity charge) would be illegal under EU directives for freight and place open access passenger and freight operators in different categories which may itself be legally challenging.
51. It seems reasonable to assume that SMART cards will soon be widely available and can therefore be the basis for charging and distributing revenue. This allows every train to be separately priced. Even advance fares could be accommodated (see my concluding comments).
54. The year 2023 does appear a good target date given how many franchises are currently organised to complete around that year.
57. This approach would mean franchised operators could face an uncertain future which would severely reduce what they would pay for the franchise.
65. This would be highly time-consuming to administer and therefore counter to the benefits of introducing market forces to drive efficiency gains.
67. Agreed
71. Network Rail could do this design.
72. the present system is much more reliable than before privatization but (scale) efficiency gains are much smaller than they could be. This is leading to an apparent need for more infrastructure investment in the future than should be the case.

Concluding comments.

Your consultation document is to be welcomed as the railway industry has become locked into a mode of administration that is failing to drive efficiency gains or integrate more widely into the economy. I would like to make a small number of additional points.

- Franchising was introduced to protect services because many were considered on privatization to be vulnerable. The doubling of passenger traffic over the last generation suggests this safeguard is no longer required, particularly on the longer routes where there are clearly several companies vying to offer services. Given that defining the working timetable is the responsibility of Network Rail (under regulation) the only possible reason for continuing with franchising is for the DfT to raise money to transfer elsewhere. There are other means of raising money.
- The implicit ambition to somehow balance financial surpluses on some routes with deficits elsewhere itself implies that railways are being considered as a separate 'business' which is totally counter to the spirit of privatization. In their heyday railway companies operated ports, ferries, distribution systems, hotels and even airlines because there was business logic in such integration and diversification. Artificial barriers between modes did not exist and would have been nonsensical. Yet in the passenger sector the industry continues to be treated as a balkanised British Rail not interested in stepping beyond its post 1962 Transport Act boundaries.
- By contrast in the freight sector we have road hauliers and shipping lines that contract for rail freight train capacity, quarry companies that own railway wagons and ports that operate inland rail terminals. That is, rail freight is well integrated into a wide range of other sectors through either ownership or long term contracts.
- There is a major opportunity for the property development sector to integrate into rail through rail adding value (directly or through planning conditions) to new developments. It would be curious to see how the ORR or the DfT would handle a proposition whereby a property company sought to be an open access commuter railway operator in competition with a rail passenger franchise holder; how would 'cross-subsidies' between property and the railways be handled. How would the financial driving force behind the development of what was the Metropolitan Railway be handled today?
- It is entirely within the legal framework defined by EU directives for network providers (and there may be several in the future if Network Rail is divided up for maintenance purposes) to levy 'capacity' charges and different charges on different routes in order to raise the revenue required to maintain and operate its network. This would correspond to the approach adopted by statutory trust ports which are not expected to make long term profits (i.e. should break even talking one year with the next). Charges could still be regulated by the ORR.
- Where such charges were affordable by train operators Network Rail would be able to define a working timetable that shared out paths between operators wishing to offer services (Dutch model).
- Where passenger train service operators could not afford such infrastructure charges and continue to be viable it would be open to the public sector (DfT or devolved authorities) to

then define franchised services that could be bid for in the same way as at present, with the possible caveat that for station pairs also covered by non-subsidised (non-franchised) services fares are set by the non-subsidised service to avoid under-cutting.

- There would seem no reason why under such arrangements and using a SMART card that passengers (including commuters) could not simply catch whichever train they chose leaving the train operator to set whatever charges he selected.
- That would provide both price and service level competition. Commuters could catch the 'first' train if they chose or wait for a cheaper one; it would be up to them. Advance fares could be offered just as at present.
- The present working timetable plus known open access aspirations could be the basis for establishing such an environment through Network Rail regions setting break even infrastructure charges based on a revised working timetable using 'capacity' charging principles (encouraging the use of long trains), employing wherever possible interoperable rolling stock leased on a relatively short term basis and auctioning rolling stock diagrams to train operators, rolling stock leasing companies being responsible for rolling stock maintenance depots.

I am sure that you will be presented with a wide range of views and I am pleased to add one more set!

Best regards

Mike Garratt