Rail
Partners

Track to Growth: Creating a dynamic railway for passengers and the economy

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Executive Summary

The track to growth is a reinvigorated public-private partnership for the railway

A thriving railway is a crucial tool for driving prosperity across Britain. As a lower-carbon form of transport, a successful railway can also act as an engine for green growth, helping to meet net-zero goals and air quality targets.

Nearly five years on from the announcement of the Williams Review, and after a pandemic that turned the industry on its head, delayed reform is undermining rail's ability to deliver to its full potential. Critical choices face the railway, including how we can bring more passengers back, make rail attractive against other modes, restore hundreds of millions of pounds in lost revenue, and ultimately set up the industry for long term success.

It is widely recognised that the railway is not performing as it should, but the scale of the challenges is often underestimated. Getting back on the track to growth involves correctly diagnosing the problems facing the railway, putting to one side ideological debates about public versus private, and prioritising what works. If competition between train companies is harnessed in a reinvigorated public-private partnership for the railway, it will drive better outcomes for passengers and taxpayers.

Section 1: We must correctly diagnose the railway's problems to find the right solutions

- Through a public-private partnership, train companies previously helped to arrest the decline of the railway post-British Rail, bringing passengers back in record numbers. Although franchising in its latter days needed reform, harnessing train companies to deliver passenger services was transformative for customers and the railway.
- However, even before the pandemic, the system was starting to show its weaknesses. The May 2018 timetable change brought into focus the lack of a single point of accountability to coordinate the railway, while franchising had become more prescriptive and constrained operators' ability to respond to changing customer needs.
- The growth of open access operators was often restricted in favour of franchised operators, with this market driven and less centrally controlled approach unable to prosper to its full potential. In addition, a complex and outdated fares system continued to erode customer confidence, with people put off train travel due to the complexity of the fares system.

The pandemic accelerated the need for change across industry

- Though the Williams Review sought to address these issues, the pandemic hit and accelerated the need for change while bringing new challenges. When people were asked to stay at home, Government suspended franchising and placed operators onto emergency contracts – with the DfT taking the lead on most commercial decisions.
- Emerging from the pandemic, revenue recovery has plateaued at around 85% to 90% of pre-pandemic levels – with taxpayer support sitting at around £1bn to £1.5bn per annum higher than pre-pandemic. However, post-Covid contracts are not designed for train companies to close the financial shortfall, and are now stifling their ability to adapt services to attract passengers.
- This is exacerbated by cost and revenue elements of the railway's bottom line sitting with different departments – DfT and Treasury respectively. Growing fiscal constraints leads the DfT to cut services to save money which makes the railway less attractive for passengers, meaning lower revenues and further cost pressures.

There are competing visions on how to tackle the railway's challenges

- Neither the challenges nor the solutions are a binary question of public vs private. The argument that ending the contracts of private sector train companies would solve blurred accountabilities, release significant funding to restore industry finances, entice passengers back to rail or overhaul the outdated fares system is misplaced.
- In fact, public control of the railway is arguably far greater in the aftermath of the pandemic than under British Rail, with the tightly controlled post-Covid contracts binding the commercial firepower of operators to Whitehall, requiring permission for even the smallest commercial decisions.
- Finding the right balance between the public and private sectors involves undertaking a fair assessment of the track record of train companies in Britain, and elsewhere, to determine how operators can be harnessed to accelerate recovery and growth of the railway post-Covid.

Section 2: A fair assessment of the last two decades shows train companies transformed a declining railway into a vibrant and growing sector

- A declining railway under British Rail led to an industry no longer meeting the needs of passengers and taxpayers. Looking for a way to avoid decline and stimulate growth, Government looked to train companies to run and manage passenger services.

- Rail Partners commissioned independent analysis by Oxera to examine the performance of the rail industry after privatisation in 1994. Oxera's research details how a public-private partnership and the commercial incentives placed on operators up until the pandemic led to a vibrant and growing railway – finding:

More passengers: Passenger journeys increased by 107%, outstripping normal economic growth, with 55% of this growth attributed to the role industry played in driving demand. Further, Great Britain had the highest passenger growth among major European railways, achieving passenger growth rates above real GDP growth.

Increased services and satisfaction: Passenger services increased by 32% and passenger satisfaction improved by 7 percentage points, with Great Britain outranking other major European railways in terms of passenger satisfaction.

Improved finances: Passenger revenue increased by 145% in real terms while operating costs remained low, only increasing by 16% in real terms, meaning industry was able to generate an operational surplus for the Treasury and taxpayer, while £14bn of private investment was put into improving rolling stock.

More jobs and a safer railway: A growing railway led to more jobs, increasing by around 22%, while also delivering one of the safest railways when compared to other major European railways.

- Although train companies did not get everything right and the franchising model needed reform, evidence shows that when harnessed in the right way, operators have a proven ability to deliver for passengers and taxpayers.

Section 3: Liberalisation of Europe's railways shows harnessing train companies in the right way has led to better outcomes – more services, newer trains, lower fares and reduced subsidy

- As Great Britain debates how to meet the challenges facing our rail industry, European countries have been moving forward to harness train companies to unlock the benefits of increased competition in rail. Seeking to tackle the inefficiency and poor fiscal position of public monopoly operators who have been slow to innovate.

- Drawing on a growing body of evidence, Rail Partners commissioned Arup and Frontier Economics to examine how the liberalisation of European railways is delivering better outcomes for passengers and taxpayers – finding:

More efficient operations: Evidence shows that where national and regional European governments have adopted a competitive tendering process, rather than direct awards, operational efficiency gains of 20-50% have been realised – allowing for more services on the network.

Reduced subsidy: Where passenger contracts have been competed, rather than directly awarded, data shows that subsidy has reduced by 15-50% - freeing up public funds. While open access operators have expanded services with no direct taxpayer support.

More services: In the countries examined where operators compete on the same routes, evidence shows that the number of departures increased, with some routes seeing up to a 60% increase in service levels – offering more choice to passengers.

More passengers: Evidence shows that operators competing on the same routes has led to up to 40% passengers increases, while demand on regional competitively tendered lines outperformed untendered long-distance lines in some countries – encouraging passengers to make greener choices.

Lower fares: Where operators compete on the same routes, evidence shows open access operators offered fare reductions of between 15-50% following entry, with fares being typically around 20-60% lower than that of the incumbent over time – providing a better deal for passengers.

- At a time when Europe is liberalising rail markets to harness the innovation and commercial acumen that train companies can deliver for passengers and taxpayers through competition, Britain risks losing these benefits through a stifling of the private sector.

Section 4: With the right reforms we can get back on the track to growth

- Getting the railway back on the track to growth involves industry working together to deliver a reinvigorated public-private partnership in order to create a dynamic railway in the interest of passengers, taxpayers, the economy and environment.
- This means public control through a new arms-length body, providing coherence across the system, and private sector train companies harnessed to drive better outcomes for passengers and taxpayers.

That is why reform should:

- **Establish a new arms-length body at the earliest opportunity to deliver public control and coherence across the railway –** addressing longstanding challenges around blurred accountabilities and a lack of strategic thinking across the system. The new body should be separate from Government and sit above industry, rightly providing the public control needed to ensure the railway is delivering for passengers, communities and environment. It should also harness the private sector, both contracted and open access operators, to deliver passenger and revenue growth, and firm cost control.
- **Harness the private sector to deliver for passengers and taxpayers today –** at a time when recovery has plateaued and taxpayer support remains higher than before the pandemic, a number of measures are needed to drive growth. So operators can respond quickly to passenger needs, commercial freedoms should be introduced immediately across all National Rail Contracts (NRC) to close the financial gap post-Covid.
- **Reunite cost and revenue within the DfT at first and then within the new arms-length body –** to ensure cost is not reduced to the detriment of revenue, it is essential to consider both sides of the ledger and the net impact of decisions. Considering cost and revenue holistically would help allow operators to begin closing the financial gap left by the pandemic and bring passengers back to rail in greater numbers.
- **Ensure the new contracting model allows train companies to deliver for passengers –** recognising that NRCs are bridging contracts, the new contracting model being developed must move away from overspecification and the culture of top-down decision making – harnessing operators to deliver as they did pre-Covid in Britain and are increasingly doing across Europe. Contracts should not take a one-size-fits-all approach, but should cover a spectrum of markets that are tailored to the passengers and geographies served.
- **The full potential of open access should be realised on long-distance routes –** at a time of tight fiscal constraints, open access operators can offer services at no direct cost to the taxpayer while helping to connect underserved communities. Whether it is quicker, more comfortable journeys or faster Wi-Fi, demand would shape the market meaning rail companies would have to adapt to the needs of passengers if they want to keep their business.
- **Reform the fares structure to ensure passengers get the best deal –** attracting and retaining customers post-Covid means government enacting the industry's longstanding fares reform proposals to deliver single-leg pricing and digital tickets. This would facilitate more pay-as-you-go and fares that can be dynamically priced by operators. A retail revolution is needed, with modern products helping to grow new markets, and transforming the perceived ease and fairness of the transaction.

- Getting back on the track to growth involves putting to one side ideological debates about private versus public ownership, recognising the challenges facing the railway, and putting in place the right solutions and structures based on what works for passengers and taxpayers.
- It is a shared responsibility to protect the railway's future and train companies, both domestically and abroad, have evidenced the skills and expertise required to grow patronage and protect taxpayers.
- If reform continues to stall, the railway faces a protracted hiatus, a stunted recovery from the pandemic and, in the worst case, a permanently smaller railway. However, with the right reforms, the railway can return to growth and help the country do the same – with rail acting as a catalyst for economic growth and decarbonisation.

In Great Britain, franchising led to:

Passenger journeys increasing by
107%
outgrowing other major European railways

Passenger services increasing by
32%

Passenger revenue increasing by
145%

Passenger satisfaction increasing by 7 percentage points
outranking other major European railways

Across Europe, more competition has led to:

Subsidy reductions of between
15-50%

Passenger increases of up to
40%

Service increases of up to
60%

Fare reductions of between
20-60%

> **It is a shared responsibility to protect the railway's future and train companies, both domestically and abroad, have evidenced the skills and expertise required to grow patronage and protect taxpayers.**

Section 1:
We must correctly diagnose the railway's problems to find the right solutions

If a reformed rail industry is to deliver what passengers expect, it is important to correctly identify the problems facing the railway. Reform has been needed for several years and the pandemic accelerated the need for change. The rail industry faces a mixture of challenges, including a continued blurring of accountabilities, an outdated fares system, plateauing passenger numbers, millions of pounds in reduced revenue, and prolonged industrial action. A response to these challenges is often to exclusively blame train companies and call for public control. However, this assessment ignores the realities of the post-Covid railway, whereby most railway decisions already sit with officials and politicians. It is widely recognised that the system is not working, but we must correctly diagnose the problems if reform is to be meaningful for passengers.

1.1 What rapidly emerged from the privatisation of the mid-90s was a public-private partnership

The decision was taken to harness the private sector, leading to a process whereby some ownership and operation of the railways was passed from government to the private sector. Started in 1994 and completed by 1997, the private sector became responsible for buying and leasing trains (rolling stock companies), running passenger and freight services through public contracts and open access arrangements (train operating companies and freight operating companies), and managing the infrastructure (Railtrack). It is a common misconception that government sold passenger services to the private sector, when in fact, it continued to 'own' services but 'franchised' these out to train companies for a set period of time. This approach required private train companies to take cost and revenue risk, managing a bottom line to drive better outcomes for passengers and taxpayers.

Privatisation was not straightforward, with much debate over the benefits of change and the subsequent industry model. Most significantly, the Hatfield crash in the early 2000s led to concerns over the effects of privatisation on infrastructure, and Railtrack was subsequently replaced by Network Rail, originally as a company limited by guarantee and then fully publicly owned from 2014. There was also a recognition of a need for more public control to coordinate and lead the network, with the Strategic Rail Authority (SRA) established in 2001 to franchise passenger services. However, the Government was concerned that the SRA was over-stepping its remit so this was abolished in 2006 in favour of direct control by the Department for Transport's Rail Group.

The system, except for a brief period, was never purely private and what rapidly evolved was a public-private partnership. This partnership consisted of the now public body Network Rail overseeing infrastructure, while passenger services were franchised by the DfT to private train companies, and freight services and train leasing were run entirely by the private sector. Franchising allowed both passengers and taxpayers to benefit from a formula that placed commercial incentives on train companies to drive better outcomes – through a profit motive. Train companies took on cost and revenue risk which incentivised operators to win new customers and drive profitable growth. This profit motive also encouraged the more efficient use of resources to reduce costs, and led to innovation in areas like timetabling, customer service and fares to generate more revenue to pay to Government or to reduce subsidy.

1.2 Train companies delivered a great deal within a public-private system

While franchising had run its course and needed reform by the time of the pandemic, it is important to recognise the successes of the previous two decades. The commercial incentives placed on train companies rejuvenated the sector post-British Rail and facilitated a growth in passengers and services. However, the role that train companies played under franchising still remains contested, with some arguing that the growth in passenger numbers and revenue would have occurred naturally. Rail Partners commissioned Oxera to independently examine the performance of the rail industry post-privatisation, looking at how a public-private partnership and the commercial incentives placed on train companies delivered tangible results.

Section 2 details Oxera's research which shows that of the 107% increase in passenger demand that occurred from 1997 to before the pandemic, 55% can be attributed to factors within the control of industry and train companies rather than economic factors such as GDP, population and employment growth. Further, the growth in passenger numbers, revenue and firm cost control overseen by industry and train companies led to the overturn of an operating deficit of around £820m in 1997/98, to generate an operating surplus for the taxpayer in many years prior to the pandemic. This meant the industry as a whole was able to fund its day-to-day operating costs from revenues without relying on government support – yielding dividends for government and taxpayers who shared in the success of the private sector.

While passenger operators did not get everything right, franchising objectively helped to revitalise Britain's railway. There is widespread agreement that the model needed reform, however there are many lessons to be learnt from the way in which the Government harnessed the innovation and commercial expertise of train companies. Given train companies have previously helped restore industry finances to good health, a fair assessment must be made of the challenges faced by the industry today, and how the private sector added value in the past, to identify how it can be harnessed to overcome those challenges again.

1.3 Before the pandemic the system was already creaking and needed reform

Before the pandemic, there were clear weaknesses in the system and the cracks were beginning to show. The blurring of roles and accountabilities were hampering the ability of industry to deliver for passengers – with the ORR, DfT, Network Rail and operators all having different levers and incentives, often pulling in different directions – with customers bearing the pain.

The May 2018 timetable disruption brought these challenges into focus, with Stephen Glaister's review outlining how operators, Network Rail, ORR, and DfT all made mistakes contributing to the problem (ORR 2018). Glaister noted how the DfT's decision to phase the introduction of services on Thameslink overstretched timetabling resources within Network Rail and the operator, while Network Rail wrongly believed it could make up lost time to deliver enhancements in the North West. At the same time, the DfT and ORR failed to sufficiently question assurances they received from both public and private parts of the industry about the risk of disruption. However, most importantly, the review highlighted that the lack of a guiding mind and single point of accountability risked a repeat of the same mistakes in the future.

In parallel, franchise agreements had become more prescriptive over time, and did not afford operators the ability to respond to changing customer need. The high level of prescriptive detail created barriers to implementing new products for customers, and barriers to driving better value for money or growing the industry. In 2010, the coalition Government paused re-franchising pending a review, with the goal of increasing the flexibility of operators and strengthening incentives to reduce costs, among other measures. However, subsequent high-profile franchise failures only led to a tightening of control by decision makers and officials rather than an examination of the root causes. This slowly stifled the advantages of private sector involvement in passenger services and the innovation that could benefit customers.

At the point of privatisation, it was envisaged that there would be greater numbers of open access operators on the network. In reality, on-rail competition was moderated in favour of franchised operators. In 2016, the Competition and Markets Authority (CMA) published a report highlighting the benefits that more open access could deliver for passengers, and that the system could be balanced by open access operators paying a public service obligation levy to contribute to the funding of important but unprofitable services (CMA 2016). It was envisaged that this would help cover any abstraction of revenues from franchised operators that might result from increased competition (although the evidence shows that revenues have grown overall). However, these measures were never adopted. This market driven, less specified and controlled approach to passenger services could have prospered where there was sufficient demand and capacity for different types of services, but these benefits were never fully realised beyond the East Coast Mainline.

Finally, a complex and outdated fares system continued to erode customer confidence, and passengers did not feel like they were getting value for money. Regulations that tie the fares system to the structures and buying requirements of the 1990s, coupled with further layers of requirements added

through individual franchise agreements, created a system riddled with anomalies. The result was a system with over 55 million fares, created in fixed bundles within a restrictive structure making it difficult for customers to untangle which ones might suit them best, making it impossible for the industry to guarantee the best value fare. When surveyed, up to 35% of people for whom rail travel was an option were put off by the complexity of fares pre-Covid (Rail Delivery Group 2019).

The rail industry identified many of these challenges and the solutions in its submission to the Williams Review and Easier Fares for All proposals in 2019, calling for a new arms-length body to act as a guiding mind for the railway, a new contracting model to overhaul the franchise system, and a reformed fares system to make rail more attractive. However, the pandemic hit and brought about a new set of challenges on top of those that already existed.

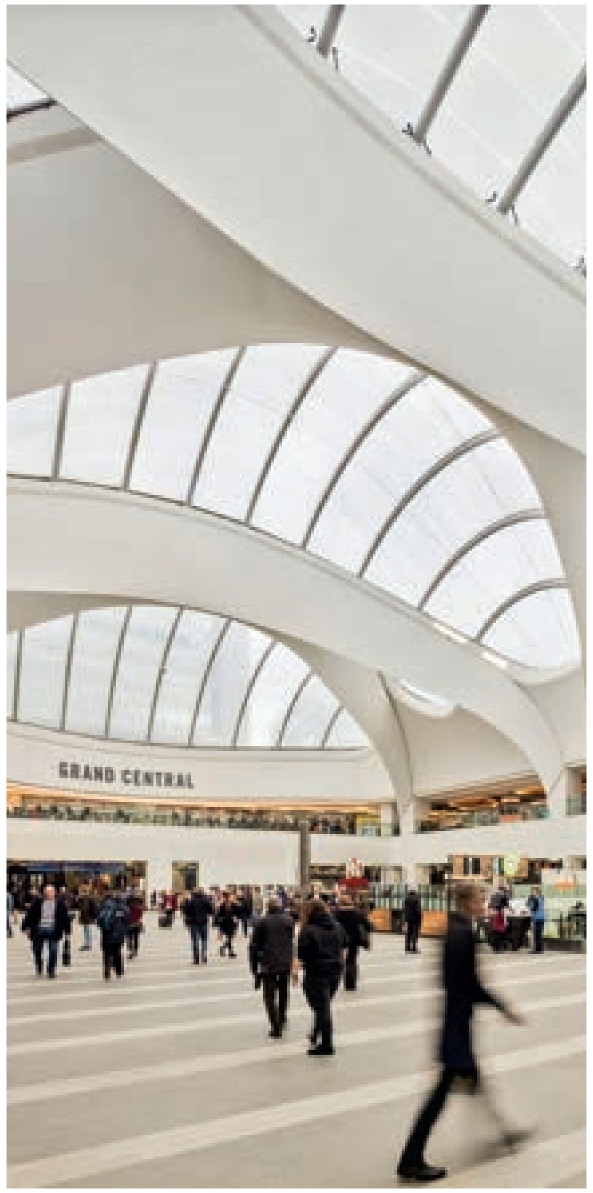
1.4 The pandemic accelerated the need for change across the industry

During the pandemic and concurrent collapse in passenger numbers, government suspended franchise agreements and stepped in to plug the financial gap to ensure services kept running for key workers. The Government put in place Emergency Measures Agreements (EMAs), covering all lost revenue and operational costs, paying operators a pre-determined fee to run services. These agreements rightly suspended the drive for operators to attract passengers and revenue, allowing them to focus on the critical task of getting people where they needed to be at a time of national crisis. This meant train companies were no longer managing revenue and cost risk, like under franchising.

When the EMAs expired after 6-months, the Government introduced Emergency Recovery Measures Agreements (ERMAs) which lasted between 6 and 18 months. The terms were similar to EMAs, although the total fee paid to operators reduced. The majority of operators have now moved from ERMAs to National Rail Contracts (NRCs) which formally terminated pre-existing franchise agreements. These are intended to be directly awarded 'bridging contracts' until new Public Service Contracts (PSCs) are designed and competed in full as envisaged in the Plan for Rail. These arrangements effectively make train companies contractors rather than franchise holders. While NRCs place more responsibility for managing cost onto operators, there is little commercial freedom or incentive to accelerate revenue growth – with operators having to seek permission from the DfT to introduce new services, deploy marketing campaigns, and respond to customer demands and needs.

In parallel, the aftermath of the pandemic continues to strain industry finances. The Government has provided tens of billions of pounds in additional taxpayer support to protect railway jobs and keep services running. A significant gap remains, with revenue plateauing between 85-90% when compared to 2019 – a shortfall of about £1-1.5bn per year (GBRTT 2023). The contractual arrangements that were rightly put in place during the pandemic, are now limiting the ability of operators to reduce the taxpayer burden post-Covid.

In order to shore up industry finances, the DfT has often been required to focus mainly on cost reduction without fully considering the impact on customers and revenue. This is a consequence of the post-Covid financial arrangements, whereby the cost budget for operators sits with DfT, but the revenue goes to Treasury. Under tight budget constraints, the DfT pushes operators to achieve savings through measures like service and marketing budget cuts. However, these cost saving measures often make the railway less attractive for passengers, meaning fewer people travelling, resulting in lower revenues and thus further cost pressures, which in turn leads to more cost cutting. This creates a scenario where no single government department or operator is looking across cost and revenue – no commercial business operates in this way. Proposals to spend money that will be net revenue generative, such as additional services, are often overlooked because DfT does not have the upfront funds and will not benefit from the revenue gains.



1.5 The financial impact of the pandemic is being exacerbated by industrial action

The immediate financial challenges both partly cause and are also exacerbated by ongoing issues around industrial disputes. Prolonged strike action has hindered rates of recovery and continues to make rail less attractive to the travelling public. Rail operating companies want to and have offered the unions fair pay increases. However, any deal must reflect the fact that government is currently paying for a significant proportion of the railway's costs, and the taxpayer will fund any pay increase. That is why any deal must be accompanied by reasonable reform to boost productivity and release the funds to pay for it.

Industrial action has also seen exaggerated claims that the profit made by industry could be used to fund a pay rise and cover reduced revenue. These claims are unfounded and continue to detract from the real challenges facing industry. NRCs have a fixed fee which equates to approximately 0.5% and an additional performance based fee only if demanding targets are met. The likely range of overall fees is £40m-£120m across all DfT contracted operators, with the top of the range only achievable through excellent performance (Rail Partners 2022). For context, the top end of this fee falls far short of providing a pay rise that would match anything close to inflation, and is less than 10% of the £1-1.5bn in reduced revenue compared to pre-Covid.

Even before the pandemic, train companies were making only modest profits of approximately 2%. As evidenced by Oxera's analysis (see Section 2), the involvement of train companies in railway operations generated benefits that outweighed this margin. Far from costing more through the opportunity to make a relatively modest profit, train companies generated a dividend for taxpayers through higher revenue growth and firm cost control.

1.6 Neither the challenges nor the solutions are a binary question of public vs private

Given the complex challenges facing the industry, the argument that simply ending the contracts of private sector train companies would solve issues around blurred accountabilities, restore industry finances, entice passengers back to rail, overhaul the outdated fares system, or even secure a deal with the unions is misplaced. Given that officials and politicians largely hold the levers of power over the railway post-Covid, a fair assessment of the challenges facing industry, and how train companies can be harnessed to overcome those challenges, is needed.

The European Union (EU) has been moving forward to inject more competition, innovation and commercial thinking into their railways. Through a series of 'railway packages', the EU has sought to challenge the dominance of state operators with the aim of creating a more efficient, customer-responsive industry – resulting in a growing rail market which is good for the economy and environment. This has involved the introduction of more open access services to compete on lines and tendering of passenger contracts to reduce cost. The move by the EU is not an indictment on the public

sector, but rather, recognises that over time state monopolies in rail become costly and undynamic. Rail Partners commissioned Arup and Frontier Economics to look at how Europe's major railways have introduced competition to drive customer and taxpayer benefits and provide a fresh perspective on how to make our railway fit for the future (see section 3).

The EU is not unique, with successful railways across the globe recognising the need to balance public control with private innovation. In the USA, infrastructure and freight operations are privately run with passenger services under state control. In Japan, passenger services and infrastructure are privately run whereas freight is public. Even closer to home, different degrees of public control exist while leveraging private sector innovation. Transport for London contracts out the Elizabeth Line and London Overground to MTR and Arriva respectively as part of a fully integrated system under public control. Similarly, Merseytravel contracts out passenger services to Transport UK Group and Serco under a joint venture. In all these instances, a profit motive has been introduced to drive better outcomes under the right public framework.

In short, industry finds itself in the same position it did in the early 90s under British Rail, with increased levels of subsidy to compensate for reduced revenue. Therefore, understanding how train companies both here and elsewhere have helped grow passenger numbers and revenue by delivering the services that customers want can inform the decisions we take today. Harnessing train companies in the right way can once again help meet the challenges the railway and the nation faces – incentivising operators to win new customers, reduce costs to the lowest possible base and drive profitable growth.

Section 2:
A fair assessment of the last two decades shows train companies transformed a declining railway into a vibrant and growing sector

Between 1997 and the start of the pandemic train companies helped to arrest the decline of Britain's railway and brought passengers back to rail in record numbers. While the franchising system in its latter days needed reform, harnessing train companies in the delivery of passenger services was transformative for customers and the railway. Rail Partners commissioned independent research which shows it allowed government to draw upon the commercial acumen and innovation that competition and the private sector enables. In turn, operators grew services and passenger journeys, surpassing that of European counterparts, while overturning an annual industry operating deficit to deliver a surplus. Understanding what worked well in the past while correctly diagnosing the challenges facing industry today is vital if reform is to succeed.

2.1 Rail Partners commissioned independent analysis to assess the performance of industry over the last 20 years

Under British Rail, the railway was in decline, it no longer met the needs of passengers and taxpayers, and was not contributing to the economic success of the country. Looking for a way to avoid decline and stimulate growth, the Government turned to train companies to run and manage passenger services. Under the model of franchising, commercial incentives were placed on operators to attract more passengers and revenue while containing costs. Operators used their operational expertise to innovate in areas like timetabling, customer service and fares – thus making more revenue to pay back to government or reduce subsidy.

It is clear that the role of train companies was a contributing factor in reversing the decline of the railway post-British Rail. However, the extent remains contested, with some arguing that its success was largely down to external factors, such as general economic growth. Rail Partners commissioned Oxera to undertake an objective examination of the extent to which train companies under a public-private partnerships influenced outcomes such as passenger and revenue growth.

The purpose of this analysis is not to call for a return to franchising. The aim is to undertake a fair assessment of the contribution of train companies to help inform the decisions taken today. It is not the case that private sector is good and the public sector is bad or vice versa. Rather, there are lessons that we can learn to inform a reinvigorated public-private partnership that will in turn support the goals of government to get back to growth.

2.2 Oxera undertook an objective examination of the role train companies played post-British Rail

Rail Partners commissioned Oxera to look at the role train companies played within a public-private partnership across a number of different metrics up until the pandemic. The first set of measures include an examination of rail usage, including passenger growth, passenger satisfaction and service levels. Secondly, from a financial perspective, Oxera examined the extent to which private sector involvement drove revenue and reduced costs, alongside investment in rolling stock. Lastly, Oxera measured the impact of private sector involvement across wider measures, such as safety and employment.

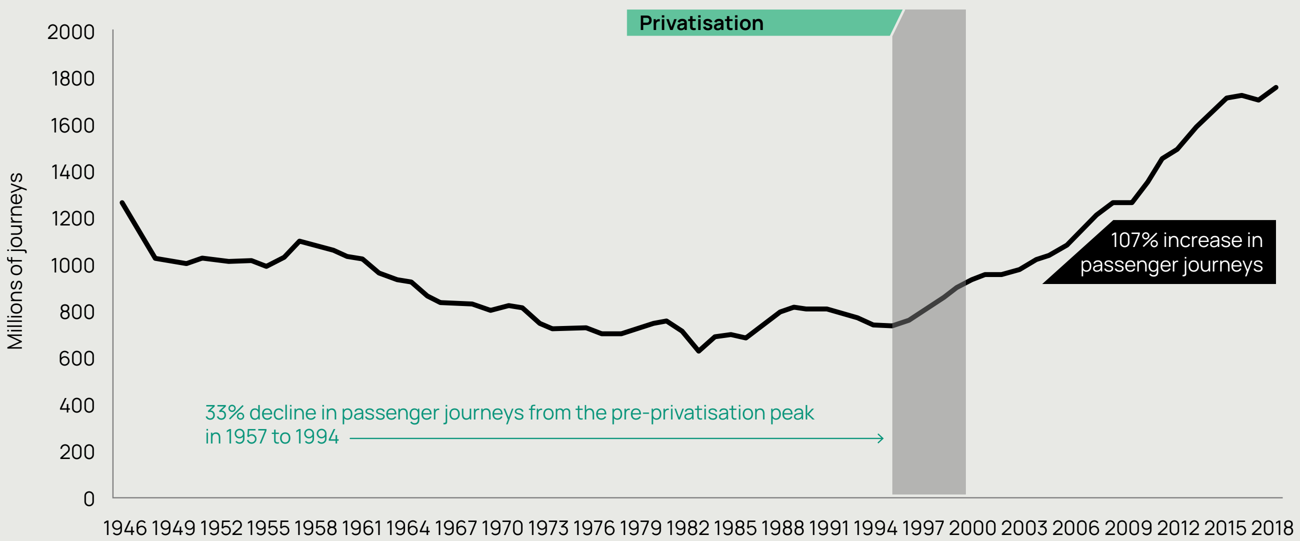
Oxera examined the performance of the industry as a whole and specifically the combination of public and private sectors whose respective roles have changed over time. This includes the role government has played in setting long-term funding arrangements and specifying franchises that helped the private sector to identify efficiencies and opportunities to improve services. As is the case with any study of this nature, some might argue the counterfactual of how the industry would have evolved if privatisation had not taken place. To address this, Oxera used multiple metrics to produce both weight of evidence and credible economic analysis including drawing upon European examples to examine trends over the same period.

The following section provides an overview of Oxera's findings.

2.3 Passenger journeys increased by 107%

Under British Rail, passenger journeys experienced a gradual decline during the post-war period. Figure 1 below shows that passenger journeys declined by 33% to 740 million per year by 1994 relative to the pre-privatisation peak of 1.1 billion in 1957. This decline occurred despite a robust economic growth rate over the period, where real GDP increased by 2.5% p.a. (or 150% over the whole period in total). While Richard Beeching's closures and periods of underinvestment undoubtedly contributed to this decline, there is a clear trend after privatisation with an increase in passenger volumes to 1.7 billion journeys per year in 2018 from 846 million in 1997, a 107% increase.

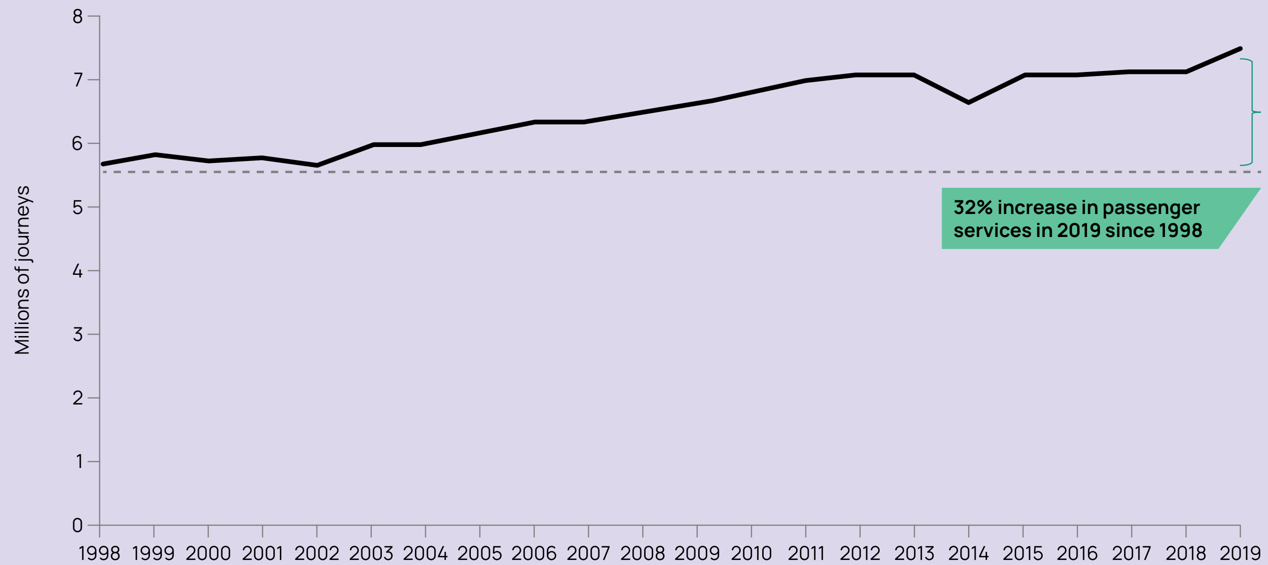
Figure 1: GB passenger journeys



2.4 Passenger services grew by 32%

The growth in rail use was also accompanied by an increase in passenger services. Figure 2 below shows that the number of passenger services, as measured by the number of planned stops less those that were cancelled or significantly late, increased by 32% from 1998 to 2019. Since privatisation, this demonstrates how train operators, working with the public sector, both identified and delivered new opportunities for services while ensuring that services are better utilised.

Figure 2: Number of passenger services



2.5 Passenger growth outstripped the level of general economic growth

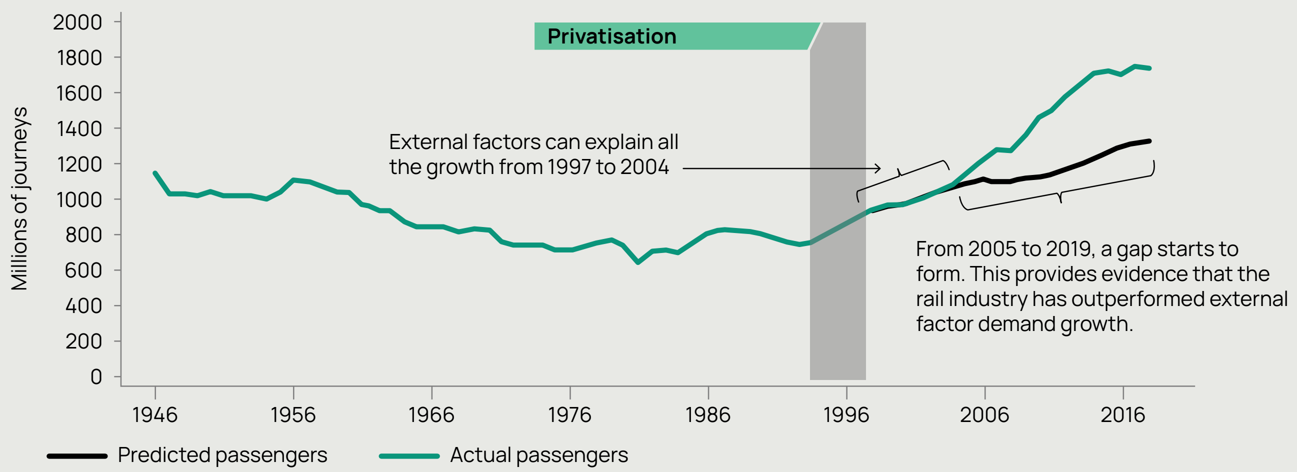
However, the previous graphs alone do not explain the extent to which privatisation was a contributing factor in passenger and service growth. Oxera further examined the reasons behind the rise in passenger demand, and specifically the extent to which the increase is due to external factors such as the growth in the economy as opposed to internal factors which, to some extent, would have been within the control of train companies such as improvements in the service offer. In order to estimate the role that operators might have played, Oxera calculated the growth in passenger travel since privatisation, and deducted the growth that can be explained by the main factors outside the control of operators and others. These are known as 'external factors' and include factors such as gross value added per capita, population and employment growth which can be quantified using the Passenger Demand Forecasting Handbook.

Figure 3 below shows total outturn passenger journeys across Great Britain (the light green line) and how much of this can be explained by external factors (the dark black line). Before 2004, passenger growth rates were fairly low when compared with the period after 2004. Almost all of the passenger growth since 1994 until 2004 can be explained by the growth in external factors. This was still a marked improvement on the pre-privatisation years. One potential reason that external factors explained all of the growth up until 2004 is the Hatfield rail crash in 2000. In response to the crash, Railtrack imposed widespread line speed restrictions in order to check for possible cracks in rails, which led to significant disruption and delays across the network. This led to several years of disruption—train punctuality returned to levels comparable to pre-Hatfield accident levels only after 2005.

Despite the disruption caused by Hatfield, the number of passenger journeys still grew in line with external factors such as GDP. This suggests that the rail industry was able to continue capitalising on external factors to grow passenger numbers, unlike in the pre-privatisation period when demand continued to decline even though there were extended periods of strong economic growth.

Since 2004, actual demand has increased significantly faster than at the rate that would have been predicted by external factors alone. Overall, Oxera found that, based on external factors, passenger journey numbers would have been expected to increase by 52% between 1997 and 2018, while actual growth over the same period was 107%. This means that around 55% of rail passenger growth since privatisation cannot be explained by external factors and provides an indication of the role the private sector played in driving demand, recognising that infrastructure capacity and reliability improvements would also have played a role.

Figure 3: Growth in rail passenger journeys that can be explained by external factors

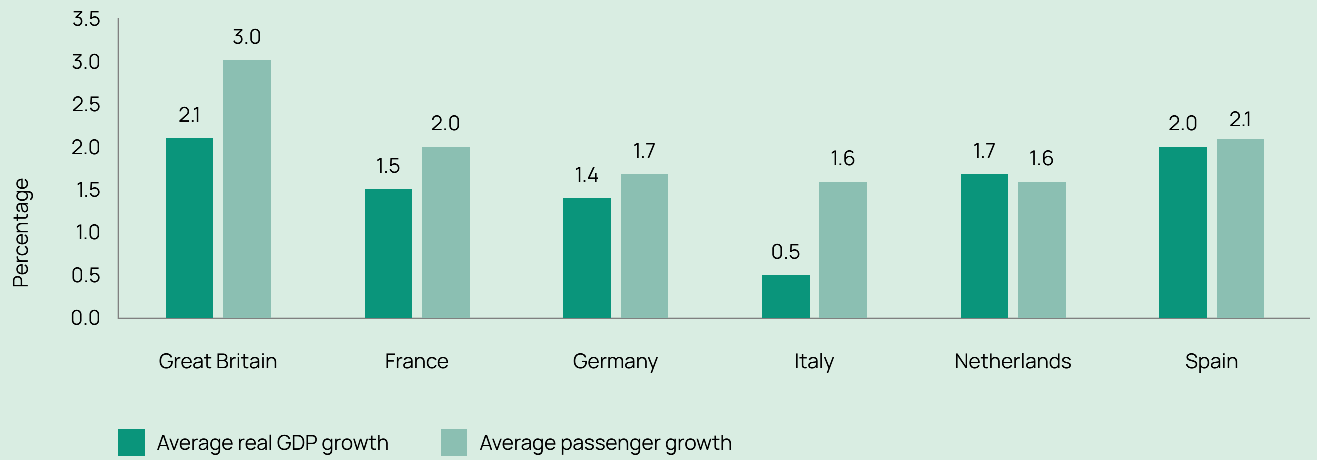


2.6 Passenger growth in Britain outstripped other major European railways

The role of train companies in driving growth of rail in Great Britain is further reinforced by examining passenger growth in other European countries – where state operators were typically dominant during the same period. Figure 4 below shows that since 1999, Great Britain has seen the highest average passenger growth rates at an average of 3.0% p.a. compared with France, Germany, Italy, the Netherlands and Spain, where passenger volumes have grown at a collective average of only 1.8% p.a.

The analysis considered whether this could be explained by differences in the growth rates of external factors across the different countries by comparing passenger growth rates against real GDP growth. While Great Britain had higher real GDP growth rates than other European countries, this factor alone cannot explain the differences in passenger growth rates. This is because Britain has achieved an annual passenger growth rate of 1.4% p.a. for each 1% of real GDP growth, which is surpassed only by Italy who have achieved 3.3% p.a. for each 1% of real GDP growth but in absolute terms Italy saw a much lower growth in passengers than Britain (1.6% p.a. on average compared to 3.0% p.a. on average). Although the evidence suggests that the strong passenger growth in Britain's rail industry cannot be solely explained by its stronger economic growth rates it is possible that differences in other external factors may have contributed to GB rail's relative success.

Figure 4: Real GDP growth and passenger growth in Great Britain compared with other EU countries, 1999–2019



2.7 Passenger satisfaction increased

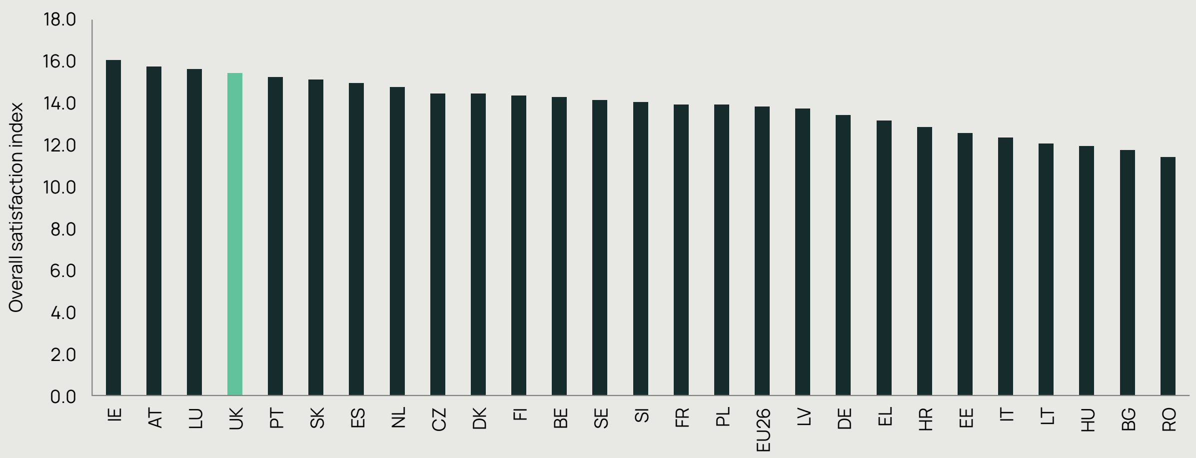
Another measure of rail industry performance is passenger satisfaction, which also improved after privatisation. Figure 5 below shows that overall passenger satisfaction, as measured by the National Rail Passenger Survey (NRPS), improved by seven percentage points from 76% in 1999 to 83% in 2019. Much of this improvement took place between 2002 and 2009. In the early 2000s, satisfaction dipped following Hatfield, while in the 2010s satisfaction remained broadly stable.

Figure 5: Passenger satisfaction

2.8 Passenger satisfaction in Britain was higher than other major European railways

To put domestic levels of rail passenger satisfaction into context, Oxera considered how passenger satisfaction in the UK compared with that in other countries. Figure 6 below presents passenger satisfaction across European countries where typically state operators are dominant. It shows that satisfaction in the UK is high relative to European counterparts, with only Ireland, Austria and Luxembourg having a higher level of passenger satisfaction – although these rail networks are considerably smaller. In comparison with other European countries with large rail networks such as Germany and France, the UK performs significantly better in this satisfaction index.

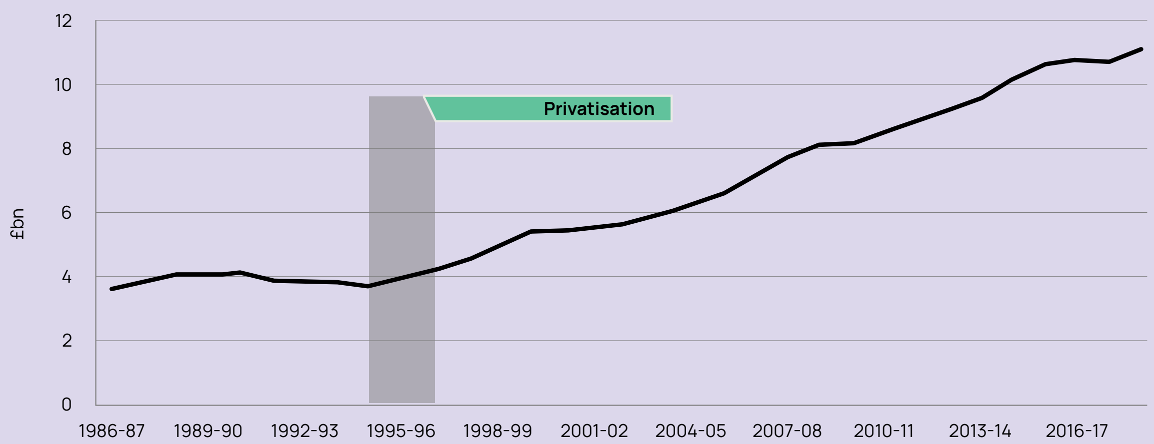
Figure 6: Passenger rail satisfaction in the UK and other European countries



2.9 Passenger revenue grew by 145%

Rail Partners further commissioned Oxera to assess the financial performance of GB rail, and in particular the extent to which poor financial performance under British Rail was overturned. The strong growth in passenger volumes led to a significant increase in passenger revenues, as shown in Figure 7 below. Passenger revenues were £4.5 billion in 1997–98 (in 2021–22 prices), and had increased to £11.1 billion by 2018–19, a real increase of 145%. Another driver of revenue growth is the rise in average revenue per passenger, albeit to a smaller extent than the volume growth. Average revenues in 1997–98 were 15p per passenger-km, compared with 21p in 2018–19, an increase of 38% in real terms.

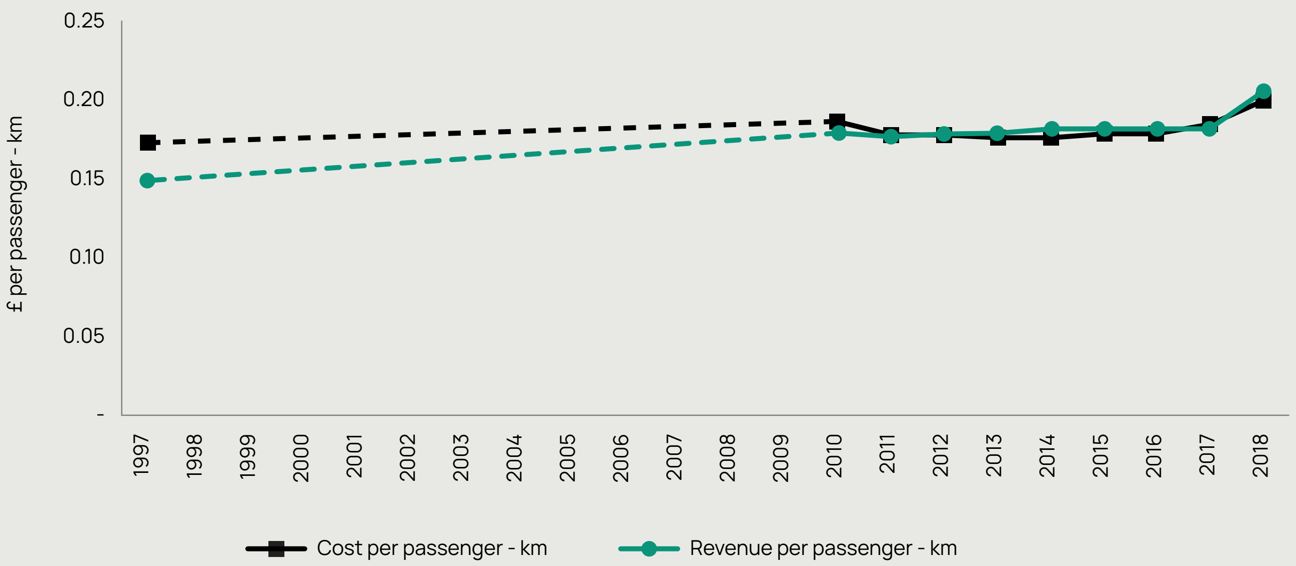
Figure 7: Passenger revenues since privatisation, 2021-22 prices



2.10 Operating costs remained low

Alongside revenue growth, average industry operating costs have increased, although at a much slower rate than revenues, from 17p per passenger-km in 1997–98 to 20p in 2018–19, an increase of around 16% in real terms. This is shown in Figure 8 below.

Figure 8: Average revenues and costs per passenger-km since privatisation, 2021-22 prices



2.11 Industry generated an operational surplus

These trends mean that, up until the pandemic, the rail industry was better able to cover the costs of its day-to-day operations than when the industry was first privatised. To measure this, Oxera calculated the industry operating deficit/surplus, defined as the difference between industry revenues and industry operating costs, generated by the rail industry in 1997–98 (the first full year following privatisation) and in the period from 2010–11 to 2018–19 when consistent data is available. The calculation uses both TOC and infrastructure manager operating costs (including maintenance costs) and revenues.

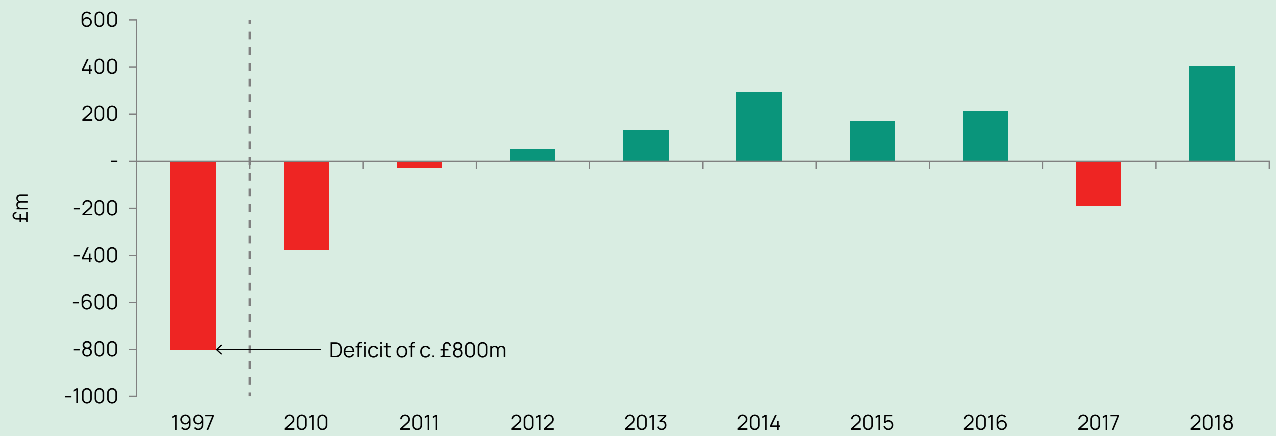
These calculations exclude capital costs (including renewals and enhancements) and also access charges, as the latter are an intra-industry transfer and so do not affect the overall revenues and operating costs faced by the industry. Also excluded are any payments from or made to the government because these also do not affect the internal operating costs.

The results are presented in Figure 9 below. This shows that, in 1997/98, the industry operating costs significantly exceeded revenues, leading to a deficit of around £800m in 2021/22 prices. However, the data shows that the industry was able to cover its operating costs to generate a surplus in most of the years following privatisation.

It should be noted that data from 2010–11 across the industry is available from the ORR using a consistent cost definition across all companies. However, the ORR did not collect data for the industry before 2010. Therefore, for 1997-98, the best available source of data is company statutory accounts. Figures in the statutory accounts will be different to those presented by the ORR due to differences in the way in which the data has been prepared.

Furthermore, there are inconsistencies in how different companies have presented the information, including adopting different turnover and cost definitions, different formats and detail, and different year-ends. As a result, calculating a measure of day-to-day operating costs from statutory accounts requires some judgement. For these reasons, the results for 1997-98 should be treated as a broad estimate that indicates the scale of the deficit when the industry was initially privatised, and how this deficit has evolved since. Nevertheless, the overall picture is very clear – a significant deficit between cost and revenue was turned into a surplus given the significant increase in revenues and keeping costs under control, delivering a significant benefit to the taxpayer.

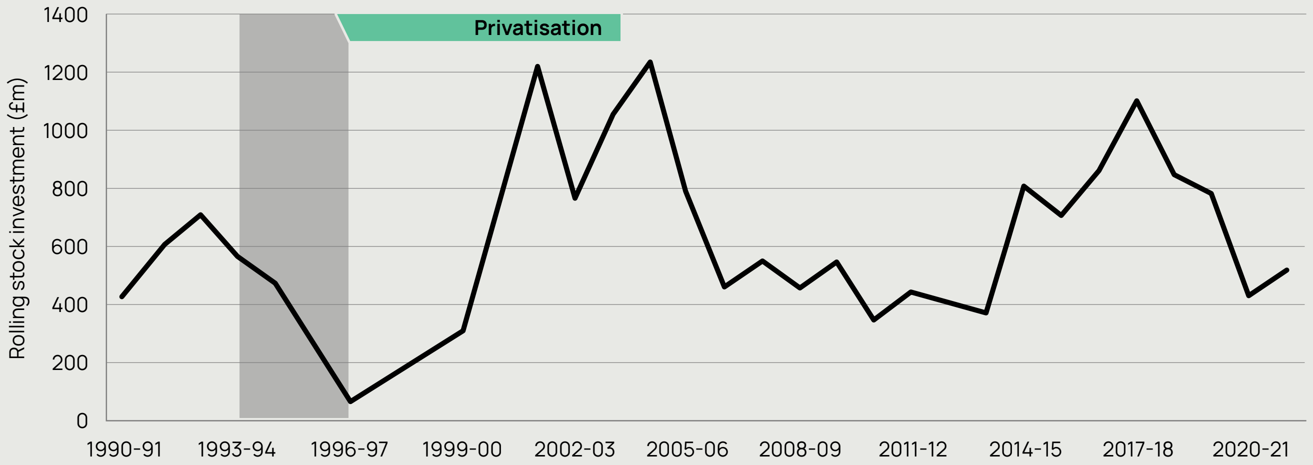
Figure 9: Rail industry operating surplus and deficit since privatisation, 2021-22 prices



2.12 Over £14bn was invested into rolling stock

Oxera examined the extent to which privatisation unlocked private sector investment into rolling stock. Figure 10 below shows that investment in rolling stock averaged £653m annually from 1997–98 (after privatisation was completed) to 2018–19. Across the whole period, a total of over £14bn was invested in rolling stock by the private sector.

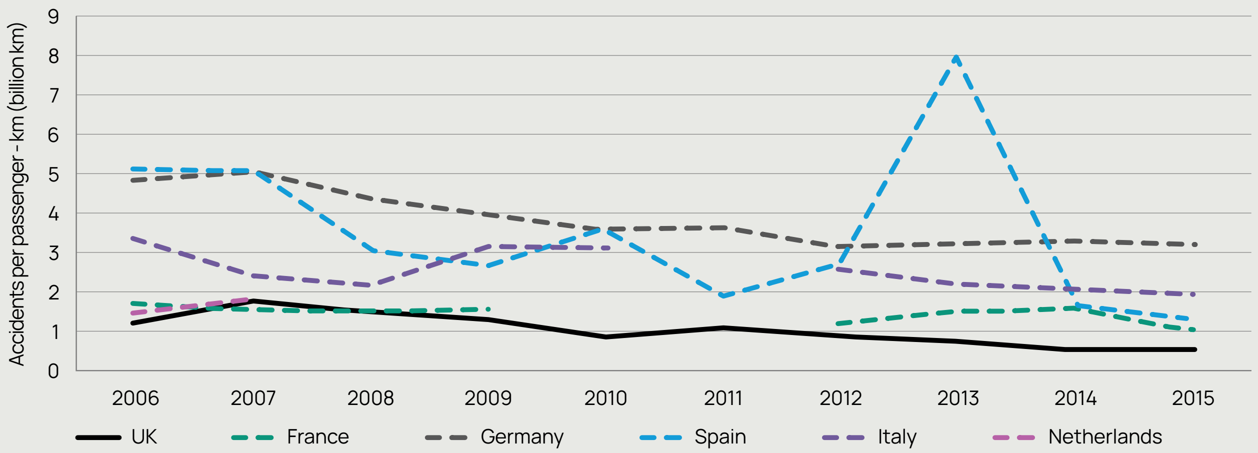
Figure 10: Private sector investment into rolling stock, 2021-22 prices



2.13 Record growth accompanied record safety

Oxera's analysis examined whether privatisation had an impact on safety. Figure 11 below shows that the UK rail industry performed well in comparison with other European countries in terms of safety. Of the countries considered (UK, France, Germany, Spain, Italy and the Netherlands), the UK has the lowest number of accidents per billion passenger-km. In particular, the UK significantly outperforms Germany and Spain, with fewer than two accidents per billion passenger-km, while both Germany and Spain have consistently had more than three accidents per billion passenger-km.

Figure 11: Safety of UK rail compared with other European countries, accidents per billion passenger-KM



2.14 More jobs were created

A growing and more prosperous railway led to more jobs. Oxera assessed how employment in the rail industry changed under privatisation using data from the Annual Population Survey (APS), which is available from 2005 onwards. This builds upon previous analysis by Rail Partners that focused solely on job growth within franchised operators, rather than across industry.

This dataset lists employment by standard occupational classification (SOC) code and identifying the most relevant to the rail industry does require a degree of judgement. This approach is unable to capture all the jobs related to the rail industry. For example, SOC codes are not granular enough to distinguish between rail and non-rail engineers, so we are unable to include rail engineers in these estimates.

Figure 12 below shows that rail jobs, as defined based on relevant SOC codes, increased by around 22% between the periods 2004–08 and 2015–19. This increase is significantly less than the doubling in rail passengers since privatisation, which suggests that the rail industry has also utilised its staff more effectively over time. Data from the Office or Rail and Road, collected from train operators, showed rail jobs in TOCs increased by 27% between 2011 to 2022.

Figure 12: Increase in rail jobs over time

2.15 Rail reform must build upon the achievements of the past and evolve to reflect the new operating realities

Oxera's analysis evidences the role that a public-private partnership played, whereby train companies played a key role in growing passenger numbers, recovering industry finances, generating higher customer satisfaction and delivering more jobs. The material changes that train companies contributed over the last 20 years should not be ignored as we look ahead to reform to address the current challenges facing rail. If the same behaviours are to be harnessed under a reformed railway, ideological debates about private vs public must be put to one side. Rather, the strengths and weaknesses of each should be objectively assessed and each harnessed appropriately.

Section 3: Liberalisation of Europe's railways shows harnessing train companies in the right way has led to better outcomes – more services, newer trains and reduced subsidy

The benefits that train companies can deliver for passengers and taxpayers are not just confined to Britain's rail market. The European Union (EU) has been legislating to liberalise its mostly state-run passenger services. Echoing the challenges seen under British Rail, the EU has sought to tackle the sluggishness of public monopoly operators who have become heavily indebted and slow to change and innovate, with the ultimate goal of making rail more competitive against others modes, more efficient, and more responsive to customer needs. Rail Partners commissioned independent research to examine what could be learnt from Europe's measures. At a time when the EU is opening up its rail markets to the benefits that train companies can bring for passengers, the UK risks sliding backwards, by closing itself to the commercial drive the private sector can deliver.

3.1 The EU is seeking to replicate the British success story and Britain can learn from the EU

Between 2001 and 2016, four legislative 'packages' were adopted by the European Union (EU) to gradually open up rail passenger services for competition and create the conditions for a single European railway area. A key aim of these packages was to foster innovation through competitive tendering for passenger contracts and more open access operations to "…revitalise the rail sector and make it more competitive vis-a-vis other modes of transport" (European Commission 2016). As Oxera's research highlights in Section 2, Europe's railways have failed to grow at the same pace as in Britain, with levels of satisfaction also lower than in Britain. Seeking to reverse these trends, governments of all colours have endorsed creating the conditions for train companies to compete in order to provide more efficient, customer-responsive services to foster growth and in turn reduce carbon emissions across the EU.

When the UK was an EU Member State, it played an influential role in shaping the outcome of the EU's rail packages. In fact, many aspects were based on the principles of the UK's 1993 Railways Act, which created the conditions for competitively bid passenger contracts and protected the rights of open access operators to run services on the network. Despite the introduction of these packages, the market share of state operators continues to remain high throughout Europe. Although some European countries have chosen different methods and timescales to liberalise their passenger rail markets, some have accelerated the pace. Where this is the case, a growing body of evidence shows that where train companies have been harnessed, through a competitive bidding process or on-rail competition, there are clear benefits for passengers and taxpayers.

3.2 Rail Partners commissioned one of the most comprehensive assessments to date of EU rail liberalisation

In order to learn lessons from how rail competition has been introduced in Europe, Rail Partners commissioned Arup and Frontier Economics to undertake one of the most wide-ranging studies exploring EU rail liberalisation – examining the extent to which train companies have delivered benefits for passengers and taxpayers across a number of measures. The research focused on eight major European railways: Austria, Czechia, France, Germany, Italy, Netherlands, Spain and Sweden. Across each country, two types of competition were explored: 'on-rail' competition and 'for-market' competition.

- **'On-rail' competition:** This sees two or more rail operators running services between the same origins and destinations, often providing services between large cities. Passengers are free to choose which operator they would like to travel with, in the same way airlines operate the same routes. On-rail competition can take different forms, such as open access operators competing with a state or contracted operator or open access operators

competing against each other. In the countries explored, on-rail competition is typically introduced by a new entrant open access operator providing services with no contract with the state and no financial support, taking significant amounts of both revenue and cost risk. In Great Britain, the East Coast Mainline has this type of competition, with the state operator LNER running alongside open access operators Lumo, Hull Trains and Grand Central.

- **'For-market' competition:** This sees businesses compete as part of a bidding process to run services on parts of the network, often for a mixture of commercially viable and unprofitable (or public service) routes. These services are let by a public body which is usually regional or national depending on the country, with bidders competing on metrics such as cost, revenue, efficiency and passenger outcomes. In Great Britain, this took the form of franchising, where the DfT or other authorities contracted out to train companies, allowing bidders to put forward proposals on how best to meet passenger needs while driving revenue and controlling costs, or concessions where the client retained more revenue and cost risk.

In each country and type of competition, the impact across a number of metrics was examined, including passenger outcomes such as service levels, customer satisfaction, and fares, and financial outcomes such as cost, revenue and subsidy. When undertaking research of this nature, it is important to recognise each country and rail system is unique, differing in institutional setup, context, and approach to collating and publishing data. Extracting data across multiple countries, languages and rail systems is also complex and the evidence base compiled by Arup and Frontier Economics draws on many existing data sources and literature.

Rail competition within many European countries is still relatively new and the markets are still evolving. In addition, there have been, and remain, barriers to entry to competitors: some are rail network specific such as access to rolling stock or service facilities and others are more general, such as legislative issues. This means that the observable benefits from competition are only just emerging but are likely to continue to grow across Europe as competition becomes more established. Nonetheless, this research should help to inform decision makers not only in Britain, but around the world.

3.3 Looking elsewhere can help to inform the decisions we take domestically

Across nearly all of the countries examined, on-rail competition through the introduction of open access operators is most clearly delivering benefits to passengers given this type of competition has been promoted under the third of the EU's railway packages since 2007 – with on-rail competition present in all countries explored. The commercial imperative to attract passengers, often against other modes or other train companies is reflected in increased passenger volumes, modal shift from road and air to rail, and innovative customer offerings to keep passengers returning. Further, evidence shows that competition from new open access operators often encourages state incumbents to adapt their offering, by investing in the refurbishment or purchasing of new rolling stock, launching new low-cost services, or adjusting fares to remain competitive.

Contracting and bidding to produce for-market competition is less widespread given the fourth of the EU's railway packages only requires countries to open domestic passenger services to competition from December 2023. However, some have moved faster and in the countries examined, competitive bidding is well established in Germany and Sweden, and is increasing in the Netherlands, Italy and Czechia. The impact of a competitive bidding process also varies depending on the type of contract and specification contained within. In

> **"Evidence shows that where national and regional European governments have adopted a competitive tendering process, rather than direct awards to a state incumbent, increased efficiencies, lower levels of subsidy and higher passenger numbers have been realised."**

Germany for example, tenders can be awarded on both gross and net cost-bases, where the tendering authority retains either all or very little of the revenue risk, respectively. Improvements in performance under these contracts can lead to demand increases and subsidy reductions, however this information is often not publicly available. Nonetheless, evidence shows that where national and regional European governments have adopted a competitive tendering process, rather than direct awards to a state incumbent, increased efficiencies, lower levels of subsidy and higher passenger numbers have been realised.

In addition, the presence and success of a competitive bidding process demonstrates that for bidders in these markets to win tenders, they will have agreed to provide lower costs to the tendering authority and/or higher quality for the same cost. It therefore follows that where a new operator takes market share from an incumbent, competition has provided a benefit to the tendering authority. More widely, evidence shows that even the anticipation of having to compete for contracts stimulates innovation and improvements for passengers – with many state operators starting to alter service offerings or make efficiencies to stave off challengers. Overall, Arup and Frontier Economics' research shows that in European countries where train companies and competition are harnessed, either through for-market or on-rail competition, passengers and taxpayers begin to reap benefits.

The following sections present Arup and Frontier Economics' findings across all the countries and measures examined.

Austria: In Austria there is currently on-rail, but no for-market competition. Passenger rail is still largely dominated by state operator, ÖBB, who have an overall market share of around 90% based on all passenger kms*. On-rail competition started in 2011 with the introduction of WestBahn, an open access operator running trains between Vienna and Salzburg, which was extended to Innsbruck in December 2022.

Czechia: In Czechia, both for-market and on-rail competition is present. In 2011, and 2012, two open access operators, RegioJet and Leo Express began competing with the state-owned České Dráhy (ČD) on the Prague – Ostrava route. On-rail competitors have now achieved a 40% share of passenger kilometres in these markets*.

In 2014, the government approved a timetable for opening five long distance lines to for-market competition. In 2017, another six express long distance lines were opened up to for-market competition. At this stage, contracts have been awarded for seven express lines and 15 long distance lines. Express lines are still exclusively operated by state-owned ČD, whereas long-distance lines have been awarded to RegioJet, Arriva and GW train – alongside ČD. In these markets, privately-owned competitors have around 20% market share based on passenger kilometres*.

France: In France, on-rail competition is present and for-market competition is soon to be. On-rail competition began when Trenitalia started operating alongside the state operator SNCF on the Paris-Lyon-Milan high-speed line in 2021. This line remains the only service that is currently served by two different operators. In anticipation of competition, SNCF launched the low-cost high-speed service Ouigo in 2013. In addition to both the Ouigo and InOui brands, both operated by SNCF Voyageurs, some lines are also served by Eurostar-Thalys (of which SNCF is the majority shareholder) though this is limited to the Paris-Lille high-speed line as part of international services to London, Brussels and beyond.

The state-owned SNCF Voyageurs continues to be the sole operator across regional markets. The state and the regions have been able to launch calls for tenders since December 2019, but could also choose to extend existing SNCF contracts. Most regions where existing contracts with SNCF are coming to an end have chosen to run competitive tenders. The first private contracted regional operator, Transdev, will begin operations in 2025 in the Provence-Alpes-Côte d'Azur region. While rail competition in France exists, competitors operate fewer than 1% of all passenger kilometres*.

Germany: In Germany, both for-market and on-rail competition is present. Since 1996, individual regions have been responsible for both the procurement and financing of regional services. German regions and bidders are required to deliver a specified service offering, being able to compete on price and quality. Non-state operators include Go-Ahead, National Express, Netinera, and Transdev. Although for-market regional competition has been growing since 1996, around 66% of for-market regional service passenger kms are still operated by state operator DB.

On-rail competition started in 2018 with FlixTrain entering the market with the launch of their Hamburg – Düsseldorf – Cologne service. Until 2019, long-distance open access competitors FlixTrain, Nightjet and Thalys ran competing services, but the pandemic led to these operations being scaled back. For non-regional rail services, DB maintains a market share of around 96% of passenger kilometres*.

Italy: In Italy, for-market and on-rail competition are both present. High-speed lines gained on-rail competition in 2012 when open access operator NTV launched under its Italo brand, bringing direct competition to state owned Trenitalia between Salerno and Naples in the south, and Turin, Milan and Venice in the north. This has led to a gradual reduction in Trenitalia's market share of all passengers kms in Italy to around 85% at present*.

The first for-market operations began in 2005, and while regional contracts are competed, it has been difficult for any operator other than Trenitalia and its partners to win tenders. Despite this, the recent competition (which Trenitalia won) for the Turin Metropolitan Railway Service in the Piedmonte region appears to have improved revenue and reduced subsidy.

Netherlands: The Netherlands, has both on-rail and for-market competition. In 2022, Arriva launched the Netherland's first open access operations, operating night trains between Maastricht and Schiphol. Arriva's open access services to Schiphol was further expanded to Groningen.

The provisions for regional passenger rail tendering were developed by the government in 1998. There are 23 concessions for regional lines spread across 7 different private operators currently active. Regional authorities determine tendering criteria to align with their objectives and strategies, while also allowing the private sector freedom to innovate and improve services. Winners of regional tenders typically have the sole rights to provide public transport (including buses) in the given region for a number of years. Long-distance concessions for the 'main' rail network have been granted to state operator NS between 2005-2015 and currently 2015-2025. Competitors (non-NS operators) have a market share of around 7% of all passenger kilometres*.

Spain: In Spain on-rail competition is present on three high-speed routes, however for-market competition is currently not. The introduction of on-rail competition was meant to start in 2020 on three high-speed routes: Madrid-Barcelona, Frontera Francesa to French border, and Barcelona-Valencia; Madrid-Levante (Valencia/Alicante); and Madrid-Toledo-Seville/Malaga. However, this was delayed by the Covid-19 pandemic. The state infrastructure manager, Adif, designed three framework contracts of capacity to operate all three blocks of routes over a period of ten years. The first slot of 65% capacity was won by state operator Renfe, with open access operators Iryo winning 30% of capacity and Ouigo winning 5%. On-rail competition started in 2021 when Ouigo launched operations on the Madrid-Barcelona route. Renfe, in response to Ouigo's and Iryo's entry, launched a new low-cost service, AVLO, in 2021 designed to compete with the new operators.

For-market competition has not started in Spain, however operations may start from 2026, where around 3% of the value of public service contracts will need to be awarded through a tendering process. The process for this initial market opening will start in 2024 and is expected to be completed in 2033, when all non-high-speed routes will be subject to a competitive process.

Sweden: In Sweden, on-rail and for-market competition is present. Sweden is seen as one of the early adopters of for-market competition, however its passenger railway market has only been open to on-rail competition since 2010. Initial market opening focused on for-market competition, which is driven by regional authorities. The first for-market competitive tender started in 1990 and competitors (companies other than state operator SJ) operate more than 40% of passenger kilometres in these markets*.

In 2015, open access operator MTRX began operating in direct competition with SJ on the Stockholm-Gothenburg line, which is the busiest in Sweden. In 2021, another open access operator, FlixTrain, entered the market on this route, offering a low-cost alternative to SJ and MTR. Since the opening of the Swedish rail market to on-rail competition, competitors gained a market share of around 80% of passenger kilometres on competed routes*.

*Figures are approximates based on Arup and Frontier Economics analysis.

Operating efficiency

3.5 Train companies have delivered more efficient operations and made better use of assets

Where national and regional European governments have adopted for-market competition, rather than direct awards to a state incumbent, evidence shows significant efficiency gains of between 20-50%. While the leanness of open access operators has led to the efficient use of network capacity to provide services where they previously did not exist.

Arup and Frontier Economics examined whether for-market and on-rail competition delivered more efficient operations. As evidenced by Oxera, franchising in Britain led to greater efficiencies through better use of assets and strong cost control. While data is limited given that for-market competition is only just becoming more widespread across Europe, evidence shows that in the Netherlands, where it is more established, competitive bidding has led to significant efficiency gains. This highlights that going to the market, instead of guaranteeing an award to a state operator, drives leaner operations, such as through better use of rolling stock.

Regarding on-rail competition and open access operators, the lack of direct public funding means these operators are naturally incentivised to make the most efficient use of assets to make a profit. This leads to innovations to keep costs low, such as the adoption of digital channels for ticket sales. The case studies highlight key examples of where increased competition has led to more efficient rail operations.

Netherlands

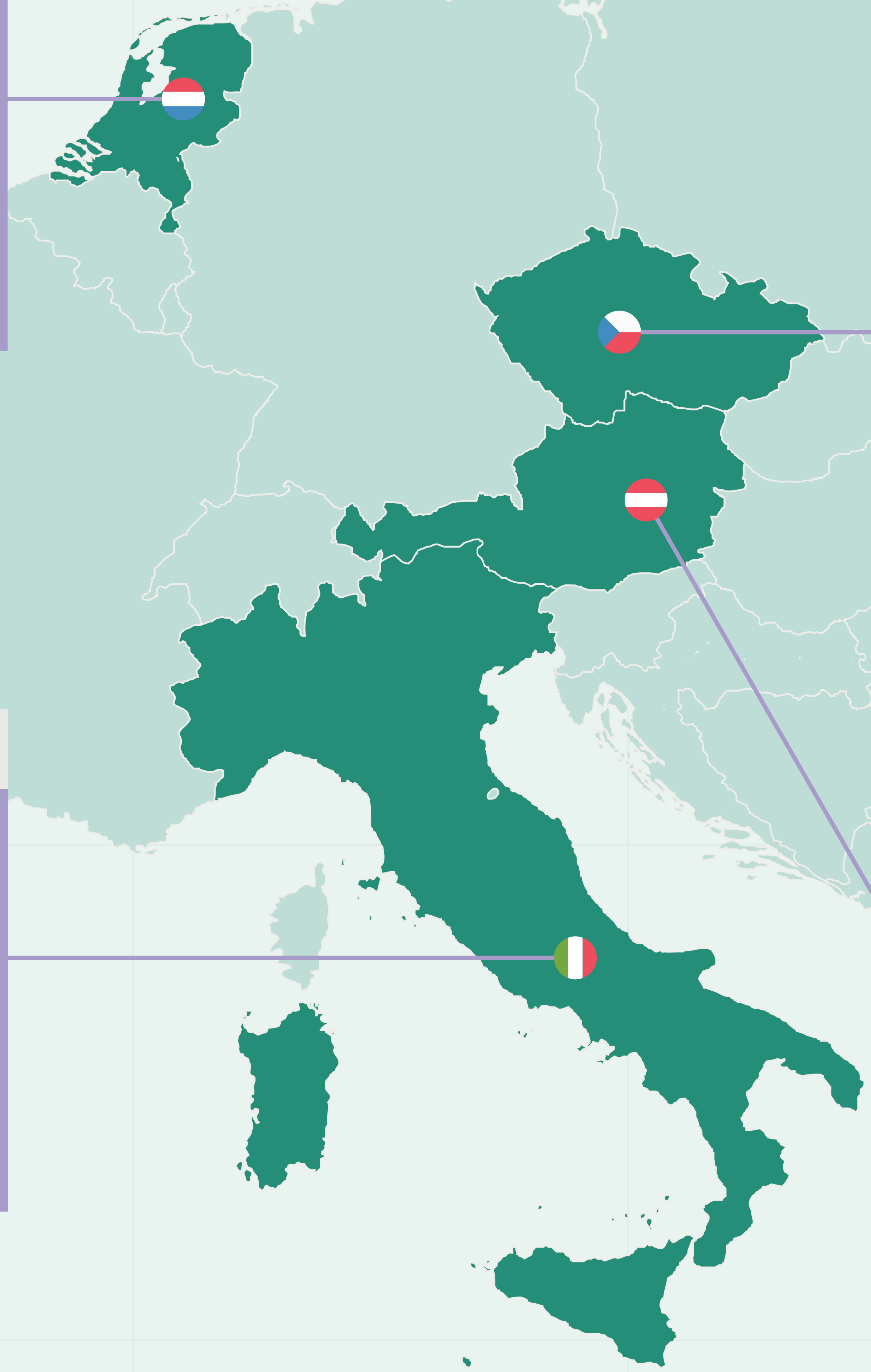
Tendering in the Netherlands led to efficiency gains of 20-50% whereas directly awarded contracts only achieved up to 10%

Gains in efficiency are being recognised as a benefit of for-market competition. A European Conference of Ministers of Transport report on tendering and decentralisation of Dutch regional passenger services noted that tendering has led to higher operational efficiency gains of 20-50% over directly awarded contracts which only achieved up to 10% efficiency gains. These gains have been harnessed to improve service levels by increasing service frequencies or through better connectivity, resulting in an increase in passenger journeys in more densely populated areas.

Italy

Italo has cut costs through the majority of tickets being sold online

Competition is driving the use of technology to manage costs effectively. Open access operator Italo's low-cost airline-inspired approach operates by minimising fixed costs through a number of methods. Most notably, Italo has adopted a digitisation approach to ticket sales, with around 80% of Italo's tickets sold online or through an app. Italo also keeps costs down through the outsourcing of train maintenance to the train manufacturer Alstom, which enabled a review of service that led to the provision of 8 additional daily services.



Czechia

The introduction of competition led to improved train performance

The entry of open access operators and tendered services has resulted in improved train performance. Between 2015 and 2018, the punctuality of trains in Czechia improved with regional and local passenger service punctuality increasing by 2%, and long-distance and high-speed service punctuality increasing by 5%. Similarly, the number of cancelled services also improved, with the number of cancelled regional and local services improving from 1.7 per thousand services cancelled to 1.3 per thousand, while long-distance and high-speed cancelled services improved from 1.8 per thousand services cancelled to 1.0 per thousand.

Austria

Despite WESTBahn reducing its fleet by 40%, service frequency only reduced by 20%

In Austria, open access operator WESTBahn has focused on fleet management and investment to drive better operational outcomes. Although WESTBahn reduced its fleet by around 40% in 2019 (prior to new fleet becoming available), service frequency only reduced by about 20% due to more intensive use of existing rolling stock.

Reduced subsidy

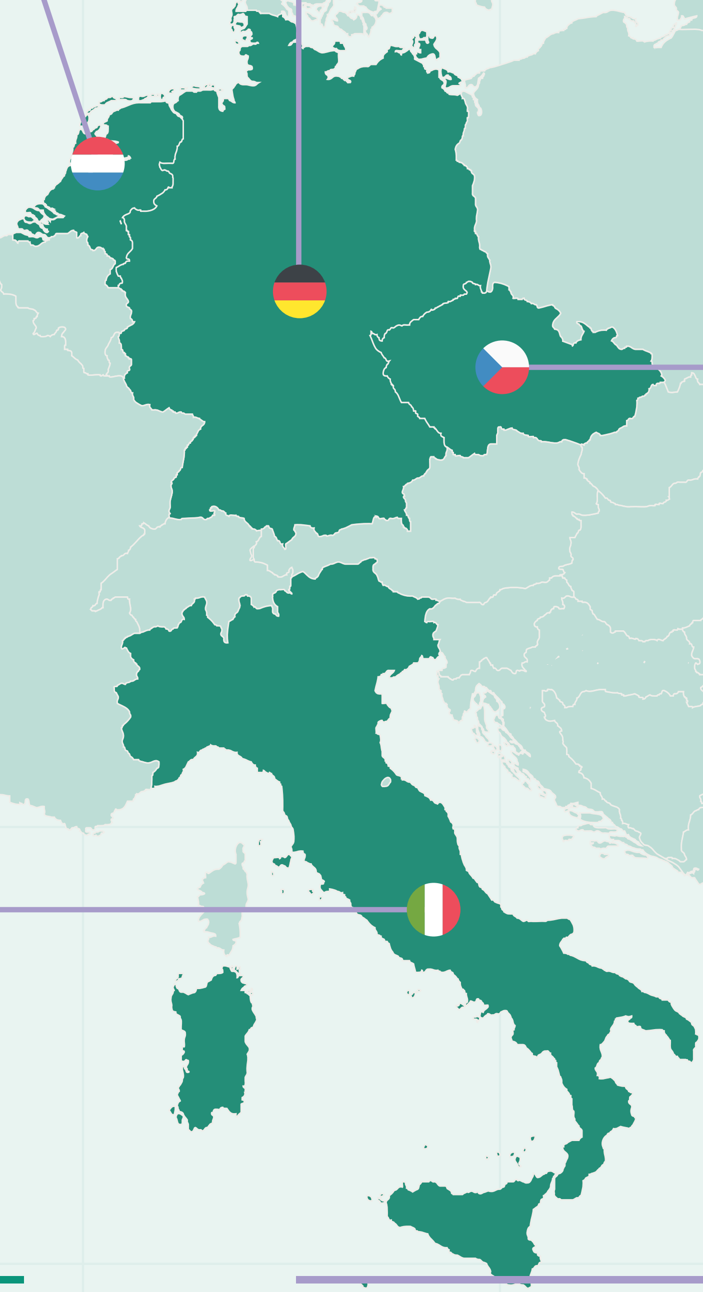
3.6 Train companies have reduced costs and driven revenue to ease public subsidy

Evidence shows that for-market competition can lead to a 15-50% reduction in public subsidy, while on-rail competition in many countries has led to an expansion of services at no direct cost to the taxpayer.

Arup and Frontier Economics examined the extent to which for-market competition reduced the burden on taxpayers as it did in Britain for the day to day running of the railway. Data shows, across a number of countries, that public subsidy going into rail passenger services has reduced under a competitive bidding process – meaning public money can be spent on other public services. Evidence is most clear in Germany and the Netherlands, with the competitive tendering process encouraging the market to explore how services can be run in the most cost-effective manner – with a public client benefiting from the best bid.

While these examples and data primarily reflect where new entrants have won a tender, there are likely to be other tenders where the incumbent operator has won, but has reduced the cost to the tendering authority or added additional value. While data on these is typically not released into the public domain, particularly where national operators such as SJ in Sweden and DB in Germany have won or retained tenders, tendering and for-market competition will have served to deliver value to taxpayers and customers, even if the incumbent state operator retains the contract.

Although open access operators do not take direct funds from government, there is evidence that on-rail competition boosts the revenue base across an entire route, often to the benefit of all operators. While much data on revenue is commercially sensitive and not publicly available, it is likely that, in many cases, total revenue increases as the growth in patronage is larger than the reduction in fares. Similar trends can be seen in Great Britain on the East Coast Mainline, where the state operator LNER and open access operators Lumo, Hull Trains and Grand Central run. Open access operators on this line have largely recovered passenger numbers and revenue faster than all other operators when compared to pre-pandemic levels, as well as LNER. It is likely that the competitive dynamics of on-rail competition has brought passengers back in greater numbers across the entire line.



Netherlands

For-market competition led to an annual subsidy decrease of 50%

In the Netherlands, for-market competition for regional services led to cost savings through improved efficiency and thus reduced taxpayer support. A report on the tendering of regional rail services highlighted that a 15-year contract for 6 regional rail services in Groningen and Friesland in 2004/2005 resulted in an annual subsidy reduction of 50%. Further, the regional contract included the introduction of new rolling stock from 2006 and the implementation of the new national OV-Chipkaart smart card without additional cost to the regional authorities.

Italy

Competitive tendering led to reduced operating costs and increased revenue

The competitive tendering of the Piedmont regional Turin Metropolitan Railway Service resulted in increased revenue and lower operating costs, requiring less financial support from taxpayers. In the initial years of operation (2020-2022), revenue per km increased by 12%, and operating cost per train km has reduced by 9.4%, resulting in the subsidy coverage ratio (subsidy required after income to meet operating costs) reducing from 45.4% to 32.6%. This is expected to reduce further to around 18.66% in 2024.

As an open access operator, Italo took on the revenue risk associated with launching a new service. In 2014, Italo operated 11.8 million train-kilometres, earned €260m in ticket revenue, carried 6.6m passengers, and posted a €62m loss. Between 2014 and 2019, however, their operations increased 89.8% to 22.4 million train-kilometres, ticket revenue increased by 161.5% to €680.6m, passenger numbers increased by 206.9% to 20.1 million, and the company registered a profit of €151.4m. The competition also benefitted state operator Trenitalia by increasing their revenue despite increasing competition from Italo and reductions in fares.

Germany

Competitive tenders for regional rail services in Germany resulted in a 15-26% reduction in subsidy

Competition for the German regional rail market is reducing the cost to taxpayers. Although regional rail subsidies have nominally increased by around 1.2% per year from 2005 to 2019, with CPI over the same period around 1.4% per year (taking 2005 as a baseline), suggesting a slight real saving of around €0.2bn over the period. Examining subsidy per passenger km for the regional markets over the same period, there has been a reduction from around €0.14 per km in 2005 to €0.11 per km in 2019. Additional research also suggests a reduction in subsidy between 15-26% since for-market franchising began in 1996 through 2014.

The effects of competition on value can also be seen when comparing direct awards and competed contacts between 2015-2018. State incumbent Deutsche Bahn was awarded 68% of direct award contracts, whereas for competed contracts, DB's success rate reduced to 51%. The competition for contracts demonstrates that for 48 of the 98 contracts awarded between 2015-2018, the client accepted an improved offer.

For-market tendering is also driving increases in revenue. Revenue generated by tendered regional operators has increased between 2005 and 2019 at a rate of 4.4% per year, or a 90% increase.

Czechia

Competition in Czechia has led to lower costs and increased revenue

Czech taxpayers are benefitting from a competitive bidding process that reduces subsidies. The Czech private operator RegioJet was awarded the rail contract for the line R9 (Prague - Brno/Jihlava via Havlíčkův Brod), taking over operations from state operator ČD. In the tender, ČD's bidding price exceeded RegioJet's by over CZK 920m (approximately £33m), a 19% difference in price. According to RegioJet, the Czech Ministry of Transport saved 15-20% due to competitive tendering. In another example, Arriva was awarded the contract for line R14 (Ústí nad Labem – Liberec – Pardubice), saving the state CZK 302m (approximately £10m).

As a result of for-market competition, ČD has also had to lower its bids to win contracts. The Ministry of Transport also noted that the price bid by ČD for the tender of line R8 (Brno - Přerov - Bohumín) in 2018 decreased by around CZK 50m (approximately £ 1.7m in 2018) per year due to "competition pressures".

The total revenues across the railway, including competitors, also rose, reaching €1.69bn in 2018, a €1.36bn increase compared to 2015, a 500% increase. Despite ČD decreasing ticket prices following the opening of services to competition, it did not experience a financial loss as increased passenger numbers led to increased overall revenue. For example, revenue on the Prague and Ostrava routes increased by 14% between 2010 and 2016, despite the price of fares reducing by 42%.

More services

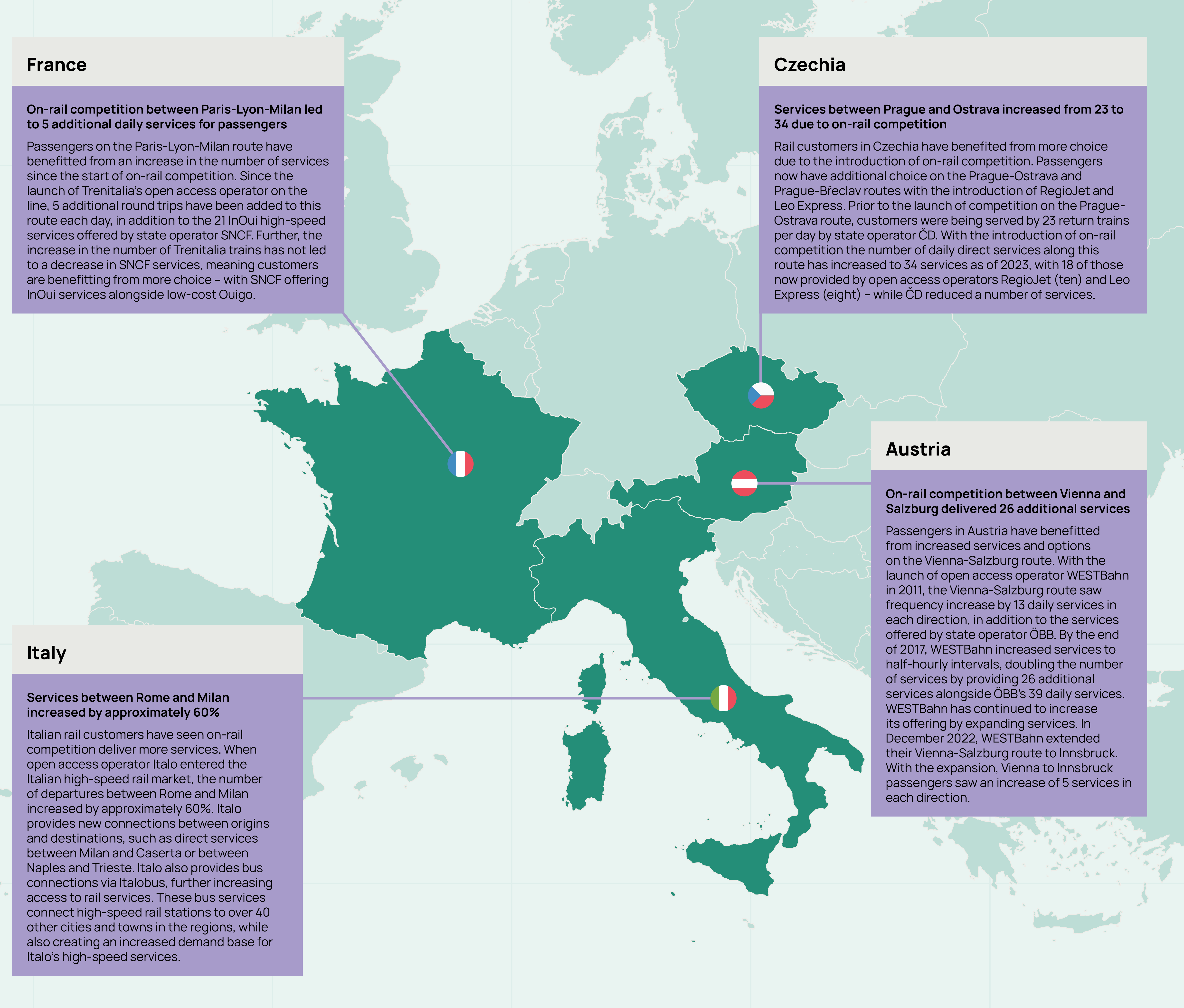
3.7 Train companies competing for passengers has led to more services

In the countries explored where on-rail competition is present, evidence shows that the number of departures increased, with some routes seeing up to a 60% increase in service levels.

Arup and Frontier Economics examined the extent to which on-rail and for-market competition led to increased service levels. In Britain, as set out in section 2, franchising led to a 32% increase in service levels, while on-rail competition on the East Coast Mainline has utilised spare capacity to provide additional services to passengers – similar trends can be seen across the continent.

In all the countries examined, the introduction of open access operators to deliver on-rail competition led to significant service increases that better reflect passenger demand and therefore attract new customers. Typically, open access operators run between major cities and compete with other modes such as air and road, meaning train companies seek to attract passengers through differentiated offerings. While frequency is largely dependent on demand and spare capacity on the network, Arup and Frontier Economics found anecdotal evidence of new entrants challenging infrastructure managers to identify additional capacity to enable new services. These additional services do not take state funding, meaning passengers benefit from additional services without extra money coming from the public purse. Moreover, evidence shows that the dynamics of competition across a route grows the market overall to the benefit of open access and state or contracted operators.

While there is clear evidence in Britain of franchising increasing service levels, there is more limited data in Europe regarding for-market competition. There is some evidence that shows improvements to service frequency following competitive tendering, however due to the often unknown nature of specifications, it is hard to demonstrate whether this is a product of competition or specification. The case studies highlight key examples of where increased competition has led to increased service levels.



France

On-rail competition between Paris-Lyon-Milan led to 5 additional daily services for passengers

Passengers on the Paris-Lyon-Milan route have benefitted from an increase in the number of services since the start of on-rail competition. Since the launch of Trenitalia's open access operator on the line, 5 additional round trips have been added to this route each day, in addition to the 21 InOui high-speed services offered by state operator SNCF. Further, the increase in the number of Trenitalia trains has not led to a decrease in SNCF services, meaning customers are benefitting from more choice – with SNCF offering InOui services alongside low-cost Ouigo.

Italy

Services between Rome and Milan increased by approximately 60%

Italian rail customers have seen on-rail competition deliver more services. When open access operator Italo entered the Italian high-speed rail market, the number of departures between Rome and Milan increased by approximately 60%. Italo provides new connections between origins and destinations, such as direct services between Milan and Caserta or between Naples and Trieste. Italo also provides bus connections via Italobus, further increasing access to rail services. These bus services connect high-speed rail stations to over 40 other cities and towns in the regions, while also creating an increased demand base for Italo's high-speed services.

Czechia

Services between Prague and Ostrava increased from 23 to 34 due to on-rail competition

Rail customers in Czechia have benefited from more choice due to the introduction of on-rail competition. Passengers now have additional choice on the Prague-Ostrava and Prague-Břeclav routes with the introduction of RegioJet and Leo Express. Prior to the launch of competition on the Prague-Ostrava route, customers were being served by 23 return trains per day by state operator ČD. With the introduction of on-rail competition the number of daily direct services along this route has increased to 34 services as of 2023, with 18 of those now provided by open access operators RegioJet (ten) and Leo Express (eight) – while ČD reduced a number of services.

Austria

On-rail competition between Vienna and Salzburg delivered 26 additional services

Passengers in Austria have benefitted from increased services and options on the Vienna-Salzburg route. With the launch of open access operator WESTBahn in 2011, the Vienna-Salzburg route saw frequency increase by 13 daily services in each direction, in addition to the services offered by state operator ÖBB. By the end of 2017, WESTBahn increased services to half-hourly intervals, doubling the number of services by providing 26 additional services alongside ÖBB's 39 daily services. WESTBahn has continued to increase its offering by expanding services. In December 2022, WESTBahn extended their Vienna-Salzburg route to Innsbruck. With the expansion, Vienna to Innsbruck passengers saw an increase of 5 services in each direction.

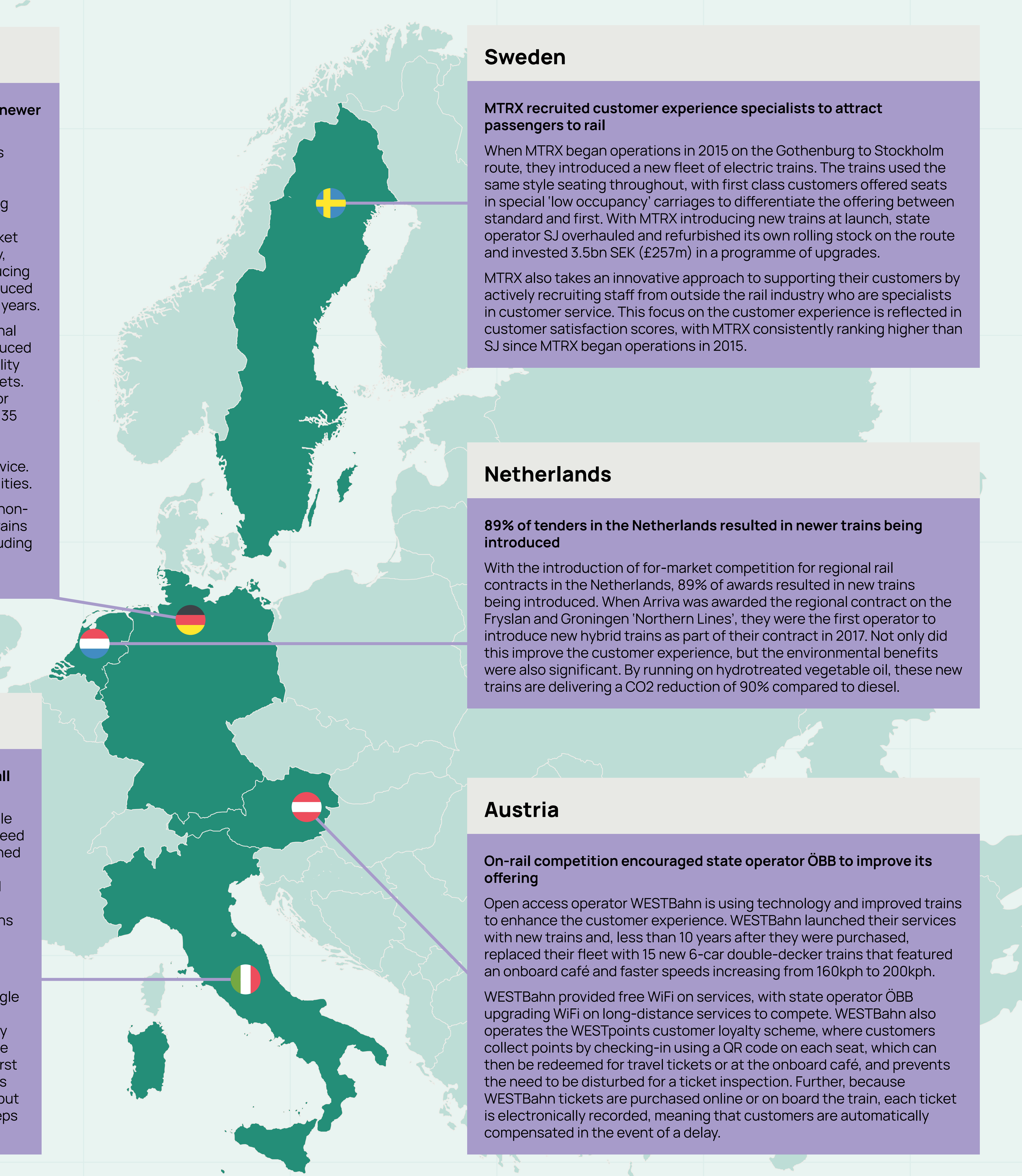
Newer trains

3.8 Train companies have innovated and introduced new trains to attract passengers

In almost all cases of on-rail competition examined, there are clear innovations to entice customers including the provision of free Wi-Fi, digital ticketing and loyalty programmes. Both on-rail and for-market competition led to the introduction of new or refurbished rolling stock.

Arup and Frontier Economics examined the extent to which on-rail and for-market competition led to increased levels of innovation. Regarding on-rail competition, the pursuit of greater patronage clearly incentivises open access operators to develop and create new offers to attract passengers. In order to differentiate the product, evidence highlights how open access operators have brought to market initiatives such as free Wi-Fi, automatic delay repay, digital ticketing and loyalty programmes. This dynamic, apparent in many other sectors, naturally encourages the market to explore new technology that customers demand or expect when travelling by rail.

Arup and Frontier Economics further examined the extent to which both on-rail and for-market competition led to the introduction of new trains. As evidenced by Oxera's research in section 2, franchising in Britain led to over £14bn of private investment going into new rolling stock, with bidders incentivised to deliver new trains to directly compete or win the contract. Train companies are often well placed to go out to the market and procure rolling stock that is both competitive on price and meets the requirements of passengers – in many cases taking this risk away from the taxpayer. In all the cases examined, open access operators provided new rolling stock, which was often followed by the state incumbent investing in the refurbishment or purchasing of new rolling stock. Following competitive tenders, evidence shows that new or refurbished rolling stock was introduced in each country examined. The case studies highlight key examples of where increased competition has led to innovations and improved rolling stock.



Germany

For-market competition in Germany has led to newer trains across the network

Tendering for regional rail contracts in Germany is delivering an improved experience for customers through the purchase of new trains. With the introduction of for-market competition new rolling stock has been introduced across many regional services. Data shows the introduction of for-market competition, alongside DB's rolling stock strategy, resulted in state operator Deutsche Bahn introducing new trains which, over the course of 10 years, reduced the average age of its trains from 17.3 years to 7.5 years.

When Go-Ahead won a contract to operate regional services in Bavaria beginning in 2022, they introduced a fleet of 56 new trains which improved accessibility through low floors and wheelchair accessible toilets. Similarly, when National Express won contracts for regional services, they launched operations with 35 new train sets in 2013 on the Rhein Münsterland-Express and Rhein-Wupper-Bahn services, and a further 82 in 2015 on the Rhein-Ruhr-Express service. These trains improved capacity and onboard facilities.

In another example, Transdev, one of the largest non-DB regional operators in Germany, ordered new trains through its various contracts over the years, including 137 new trains for its NordWESTBahn operations between 2000-2010.

Italy

Italo was the first operator in the world to install HEPA filters during Covid

Passengers have benefited from more comfortable travel after new trains entered the Italian high-speed network. When open access operator Italo launched its service in 2012, they introduced 25 new trains, followed by another 26. These new trains allowed Italo to offer a competitive service with Trenitalia which had ordered a new high-speed fleet of trains for its Frecciarossa brand in 2010.

In addition to rail services, Italo launched a complementary bus service which provided customers intermodal connections through a single system of integrated fares, providing seamless end-to-end journeys. Italo was also able to quickly respond to their customer's health concerns while traveling during the pandemic by becoming the first train operator in the world to install HEPA air filters on its trains. This not only protected customers, but also benefited the wider community by taking steps to help reduce transmission of the virus.

Sweden

MTRX recruited customer experience specialists to attract passengers to rail

When MTRX began operations in 2015 on the Gothenburg to Stockholm route, they introduced a new fleet of electric trains. The trains used the same style seating throughout, with first class customers offered seats in special 'low occupancy' carriages to differentiate the offering between standard and first. With MTRX introducing new trains at launch, state operator SJ overhauled and refurbished its own rolling stock on the route and invested 3.5bn SEK (£257m) in a programme of upgrades.

MTRX also takes an innovative approach to supporting their customers by actively recruiting staff from outside the rail industry who are specialists in customer service. This focus on the customer experience is reflected in customer satisfaction scores, with MTRX consistently ranking higher than SJ since MTRX began operations in 2015.

Netherlands

89% of tenders in the Netherlands resulted in newer trains being introduced

With the introduction of for-market competition for regional rail contracts in the Netherlands, 89% of awards resulted in new trains being introduced. When Arriva was awarded the regional contract on the Fryslan and Groningen 'Northern Lines', they were the first operator to introduce new hybrid trains as part of their contract in 2017. Not only did this improve the customer experience, but the environmental benefits were also significant. By running on hydrotreated vegetable oil, these new trains are delivering a CO_2 reduction of 90% compared to diesel.

Austria

On-rail competition encouraged state operator ÖBB to improve its offering

Open access operator WESTBahn is using technology and improved trains to enhance the customer experience. WESTBahn launched their services with new trains and, less than 10 years after they were purchased, replaced their fleet with 15 new 6-car double-decker trains that featured an onboard café and faster speeds increasing from 160kph to 200kph.

WESTBahn provided free WiFi on services, with state operator ÖBB upgrading WiFi on long-distance services to compete. WESTBahn also operates the WESTpoints customer loyalty scheme, where customers collect points by checking-in using a QR code on each seat, which can then be redeemed for travel tickets or at the onboard café, and prevents the need to be disturbed for a ticket inspection. Further, because WESTBahn tickets are purchased online or on board the train, each ticket is electronically recorded, meaning that customers are automatically compensated in the event of a delay.

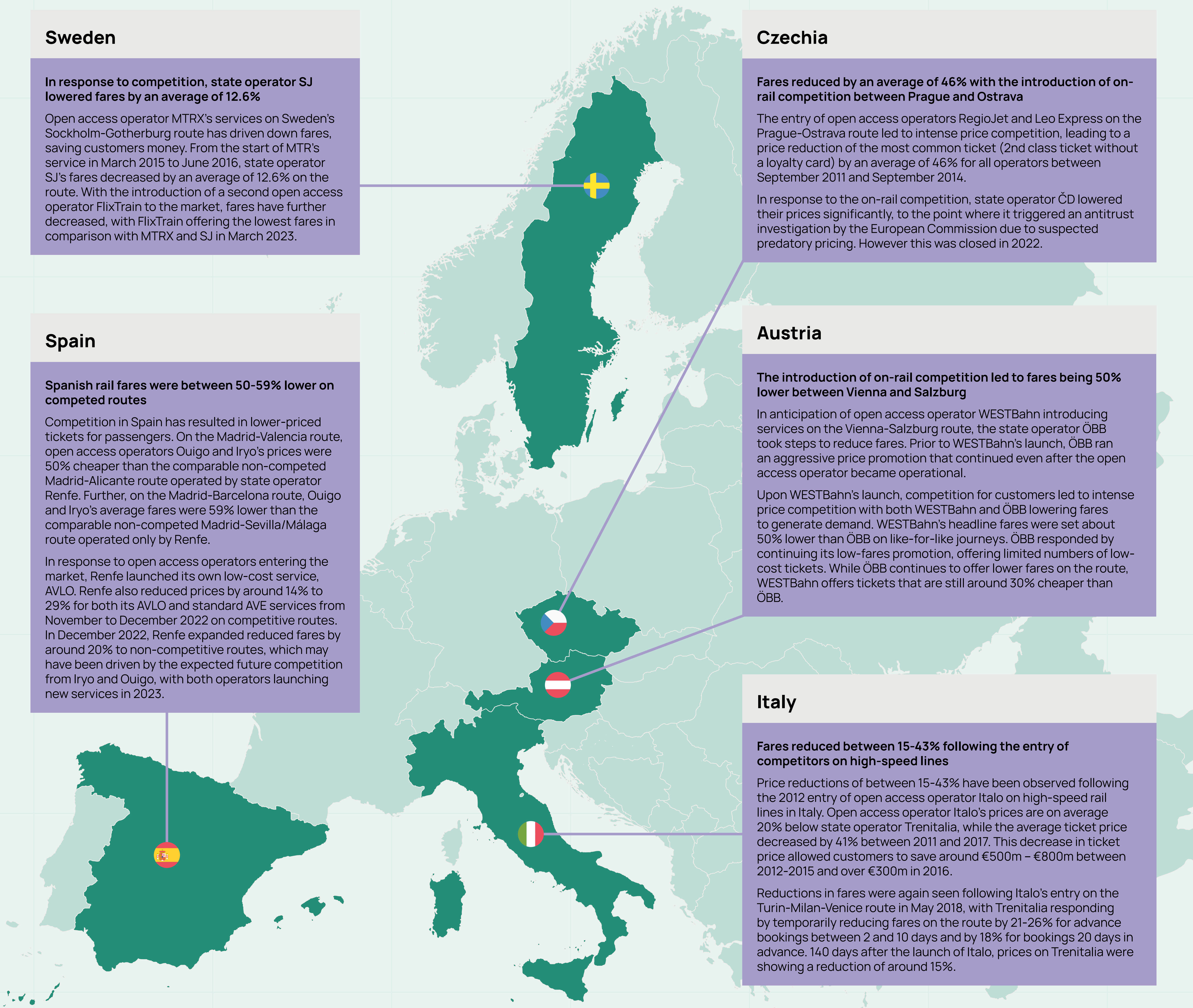
Lower fares

3.9 Train companies competing for passengers has led to lower fares

In all instances of on-rail competition examined, evidence shows fare reductions of between 15-50% following the entry of open access operators, with fares being typically 20-60% lower than that of the incumbent over time – based on Arup and Frontier Economics analysis.

Arup and Frontier Economics examined the extent to which fares changed following the introduction of on-rail and for-market competition. Clear evidence shows that the introduction of open access to deliver on-rail competition led to fare reductions in all countries examined, with new entrants offering lower price points to attract customers. Open access fares are typically dynamic and demand-led, meaning price points are better tailored to passenger need and market forces. This type of dynamic pricing is crucial between major cities where competition with air and road is fierce. If the price on offer is not right, passengers will vote with their feet and choose other modes. Arup and Frontier Economics further found data that the introduction of open access operators leads to incumbents lowering fares.

In the countries explored by Arup and Frontier Economics, there was not evidence from the limited examples of competitive tendering that it led to a reduction in fares, this is primarily because the client sets fares in the countries explored. The case studies highlight key examples of where increased competition has led to a reduction in fares.



Sweden

In response to competition, state operator SJ lowered fares by an average of 12.6%

Open access operator MTRX's services on Sweden's Sockholm-Gotherburg route has driven down fares, saving customers money. From the start of MTR's service in March 2015 to June 2016, state operator SJ's fares decreased by an average of 12.6% on the route. With the introduction of a second open access operator FlixTrain to the market, fares have further decreased, with FlixTrain offering the lowest fares in comparison with MTRX and SJ in March 2023.

Spain

Spanish rail fares were between 50-59% lower on competed routes

Competition in Spain has resulted in lower-priced tickets for passengers. On the Madrid-Valencia route, open access operators Ouigo and Iryo's prices were 50% cheaper than the comparable non-competed Madrid-Alicante route operated by state operator Renfe. Further, on the Madrid-Barcelona route, Ouigo and Iryo's average fares were 59% lower than the comparable non-competed Madrid-Sevilla/Málaga route operated only by Renfe.

In response to open access operators entering the market, Renfe launched its own low-cost service, AVLO. Renfe also reduced prices by around 14% to 29% for both its AVLO and standard AVE services from November to December 2022 on competitive routes. In December 2022, Renfe expanded reduced fares by around 20% to non-competitive routes, which may have been driven by the expected future competition from Iryo and Ouigo, with both operators launching new services in 2023.

Czechia

Fares reduced by an average of 46% with the introduction of on-rail competition between Prague and Ostrava

The entry of open access operators RegioJet and Leo Express on the Prague-Ostrava route led to intense price competition, leading to a price reduction of the most common ticket (2nd class ticket without a loyalty card) by an average of 46% for all operators between September 2011 and September 2014.

In response to the on-rail competition, state operator ČD lowered their prices significantly, to the point where it triggered an antitrust investigation by the European Commission due to suspected predatory pricing. However this was closed in 2022.

Austria

The introduction of on-rail competition led to fares being 50% lower between Vienna and Salzburg

In anticipation of open access operator WESTBahn introducing services on the Vienna-Salzburg route, the state operator ÖBB took steps to reduce fares. Prior to WESTBahn's launch, ÖBB ran an aggressive price promotion that continued even after the open access operator became operational.

Upon WESTBahn's launch, competition for customers led to intense price competition with both WESTBahn and ÖBB lowering fares to generate demand. WESTBahn's headline fares were set about 50% lower than ÖBB on like-for-like journeys. ÖBB responded by continuing its low-fares promotion, offering limited numbers of low-cost tickets. While ÖBB continues to offer lower fares on the route, WESTBahn offers tickets that are still around 30% cheaper than ÖBB.

Italy

Fares reduced between 15-43% following the entry of competitors on high-speed lines

Price reductions of between 15-43% have been observed following the 2012 entry of open access operator Italo on high-speed rail lines in Italy. Open access operator Italo's prices are on average 20% below state operator Trenitalia, while the average ticket price decreased by 41% between 2011 and 2017. This decrease in ticket price allowed customers to save around €500m – €800m between 2012-2015 and over €300m in 2016.

Reductions in fares were again seen following Italo's entry on the Turin-Milan-Venice route in May 2018, with Trenitalia responding by temporarily reducing fares on the route by 21-26% for advance bookings between 2 and 10 days and by 18% for bookings 20 days in advance. 140 days after the launch of Italo, prices on Trenitalia were showing a reduction of around 15%.

More passengers

3.10 Train companies have encouraged more people to choose rail

Data shows that on-rail competition in Italy and Spain led to passenger numbers increasing by up to 40% across certain routes, while demand on regional competitively tendered lines outperformed untendered long-distance lines in Germany.

Arup and Frontier Economics examined the extent to which on-rail and for-market competition led to increased passenger numbers. Regarding on-rail competition, while route-specific passenger numbers are often not publicly available, data suggests that factors such as increased service levels, lower fares, new rolling stock and wider innovations often result in patronage growth across an entire line. This is particularly clear in the case of open access operators in Spain, Italy, and Austria. This highlights how the dynamics of competition attracts more people to rail, encouraging passengers to make a greener choice of travel when compared to air and road.

In Britain, Oxera evidenced how for-market competition through franchising led to a 107% increase in passenger numbers up until the pandemic. Although evidence of for-market competition driving passenger growth is limited in Europe, Germany is showing strong passenger growth after contracting out passenger services. Notably, growth on regional competitively tendered routes has been stronger than non-competed routes, although this could be attributed to the transfer of responsibility for contracting of services to the regions and the improvements this has delivered. The case studies highlight key examples of where increased competition has led to more people choosing rail.

France

Data shows that on-rail competition led to 37% of passengers choosing Trenitalia over air

Customers are increasingly turning to rail along the competitive Paris-Lyon-Milan market. Following the launch of Trenitalia's services on this route, ticket retailer Trainline noted an increase in ticket sales on the Paris-Milan route of 216%. Trainline also noted an increase on the Paris-Lyon-Milan route of 106%, while the Paris-Lyon route increased by 14%.

The increase in passenger numbers is also driving a modal shift to rail. According to an OpinionWay survey for Trenitalia, 37% of its passengers would not have taken the train or travelled by air without Trenitalia's services. Further, in an interview, the CEO of SNCF's long-distance passenger business noted that 50% of Ouigo's passengers were new to rail, suggesting they are choosing rail over other forms of transportation.

Spain

Passenger recovery post-Covid was higher on routes with on-rail competition compared to those without

The introduction of open access operators in Spain led to accelerated recovery in passenger journeys following the pandemic, with most of the routes with on-rail competition reaching pre-pandemic passenger volumes faster than non-competed comparators. In particular, the Madrid-Barcelona, Madrid-Málaga and Madrid-Valencia routes reached pre-pandemic passenger numbers in 2022. The faster recovery of passenger numbers where on-rail competition exists can be seen as these routes increased by more than 40% in comparison to 2019, while the comparative non-competed route of Madrid-Alicante only increased by 14%. Further, competition on the Madrid-Barcelona route is leading a modal shift from air with 76% of passengers choosing trains, 17% more than in 2019.

Germany

Passenger numbers increased faster on for-market routes when compared to non-tendered routes

German rail volumes have increased at a faster rate on regional routes where for-market competition exits when compared to non-tendered long-distance routes. Although many factors may have influenced this, after tendering, regional rail passenger kilometres increased by an average annual rate of 2.4%, a 52.6% total increase between 2002 and 2019, compared to 1.7%, a 36.3% total increase in the same period in the long-distance market.

Austria

State operator ÖBB recognised that on-rail competition had attracted more passengers to rail

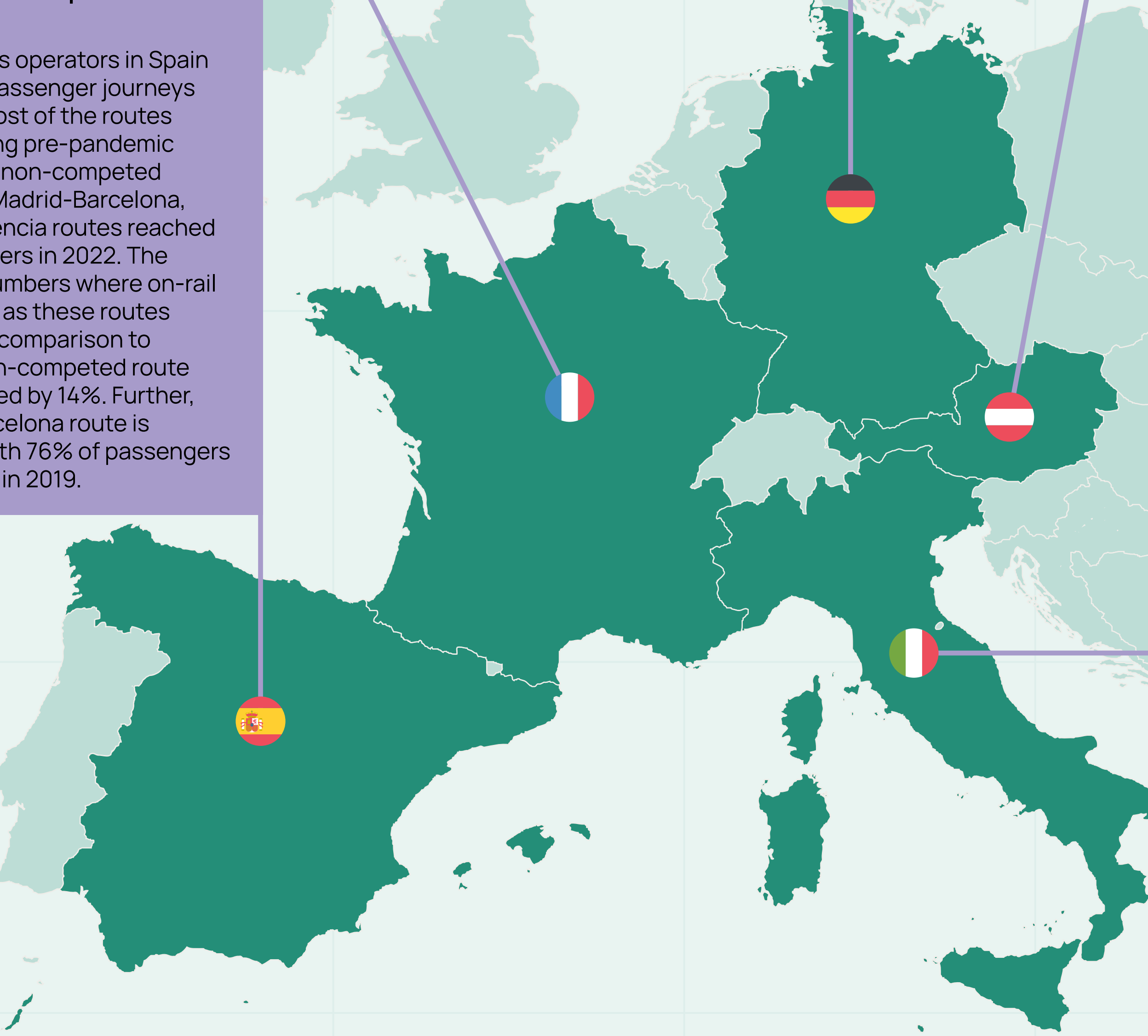
Customers are responding to more choice on the Vienna-Salzburg-Innsbruck line by choosing rail. The introduction of open access to the Austrian rail market has led to an increase in passenger growth according to the state operator ÖBB. They noted that passenger rail grew by 4.3% in 2018. This growth was a result of a 2.6% increase in ÖBB's performance and acknowledged 'the development on the private railway market' as a factor in the increase of rail passengers.

Italy

The introduction of on-rail competition between Rome and Milan led to a 90% increase in demand

Following the introduction of open access operator Italo to the high-speed rail market, the demand for rail has grown. Between 2011 and 2017, there was a 90% increase in demand (despite a reduction in GDP in Italy over the same time period) on the Rome-Milan corridor served by both Italo and Trenitalia. Trenitalia's services grew by between 1 to 3 million per year, reaching 31 million passengers in 2015. Italo also experienced increased demand, carrying 2 million passengers in 2012 and growing to 20 million in 2019.

The introduction of Italo to the high-speed market has also led to modal shift in favour of rail. Between 2008 and 2012, over 70% of the growth in high-speed rail demand was the result of demand being diverted from other rail services and transport modes. Further, the remaining 30% of growth in high-speed rail was newly generated demand. Italo's launch has contributed to a decrease in highway modal share from 57.3% to 45.2% and air from 10.5% to 7.3%. The modal shift from air is even more noticeable between Rome and Milan. Along this route, air's mode share reduced from 45% in 2009 to 26% in 2012 when competition was introduced in the high-speed rail market, but down to just 6% by 2018.



Section 4: With the right reforms we can get back on the track to growth

Getting back on the track to growth means reinvigorating the public-private partnership that was once successful in Great Britain and is delivering across Europe. Before the pandemic, it is clear the system was under significant strain, and that the pandemic only added to the challenges facing the railway. However, we must not only correctly diagnose the problems confronting industry, we must also make a fair assessment of train companies in Britain and elsewhere to determine how best they can be harnessed to meet those challenges. The independent research set out in this report shows how train companies in Great Britain played a signification role in reversing the decline under British Rail, achieving record passenger growth while rebalancing industry finances. Evidence from Europe also shows how train companies are delivering passenger growth and better customer outcomes through more competition. Domestic reform must once again harness train companies to not only deliver for passengers and taxpayers, but the nation as a whole – getting the railway back on the track to growth.

4.1 To rise to the challenges facing the railway we must correctly diagnose the problems

In order to find the right solutions, we must correctly identify the challenges facing the railway. Section 1 of this report set out those challenges, highlighting how longstanding issues around blurred accountabilities led to system wide failures such as the May 2018 timetable implementation. Repeated franchise failures and overprescription in contracts diminished the effectiveness of the private sector to deliver for passengers and taxpayers. The expansion of open access and the benefits it can deliver for passengers were suppressed. Finally, a complex and outdated fares system undermined the attractiveness of rail to passengers. Although the William's review sought to resolve these issues, the pandemic brought about a new set of challenges.

When most passengers were asked not to travel during Covid, Government stepped in to suspend franchising and the commercial drive of operators to chase patronage and revenue. Overnight, operators became contractors, with the Department for Transport (DfT) taking the lead on most decisions. However, as we emerge from the pandemic, revenue recovery has plateaued at around 85% to 90% of pre-pandemic levels – with taxpayer support sitting at around £1bn to £1.5bn higher than before the pandemic. The post-Covid contracts are now not designed for train companies to utilise their commercial expertise to close this financial shortfall.

This is further exacerbated by the fact that the cost and revenue elements of the railway's finances sits with different government departments. Currently, the budget for running services sits with the DfT, while the revenue generated by those services goes to Treasury. This leads to the DfT, under growing fiscal constraints, to cut services, marketing, and other budgets to save money. These cuts make the railway less attractive for passengers, meaning fewer people travelling, which in turn leads to lower revenues and further cost pressures, and thus more service cuts. The same financial challenges are also worsening industrial relations, with the need for any deal to reflect the financial pressures facing the industry.

As a result, the industry faces a complex and multi-layered set of challenges, including a lack of clear industry-wide leadership or accountability, a complex fares system, plateauing passenger numbers, prolonged industrial action, and increased levels of taxpayer subsidy, among others. To surmise that removing the private sector from rail and increased public control would solve these challenges is misjudged. Particularly when train companies already need to seek permission to make change happen within their operations and that public control is arguably greater than under publicly owned British Rail.

4.2 Independent analysis shows train companies not only delivered in Great Britain but are delivering across Europe

We must not only acknowledge the challenges facing industry, but undertake a fair assessment of the track record of train companies to determine how best they can meet those challenges. Section 2 presented independent analysis by Oxera highlighting the role train companies have previously played in Great Britain. Evidence shows that after the decline of British Rail, private train companies played a significant role in restoring the health of the railway – regrowing passenger numbers and overturning an operational deficit to deliver a surplus. Train companies did not get everything right, but the material change that operators contributed over the last 20 years should not be ignored as we look ahead to reform to address the current challenges facing rail.

The European Union (EU) has also recognised the role train companies can play in terms of growing passengers and reducing taxpayer subsidy. Section 3 charted how the EU and Member States have sought to tackle the inefficiency of public monopoly operators who have been slow to innovate and adapt. Arup and Frontier Economics' research highlights how liberalisation of European railways, through an expansion of on-rail and for-market competition, is leading to lower fares, more services, newer rolling stock, increased efficiencies and reduced taxpayer support. Once again highlighting that when done in the right way, commercial incentives and competition can be deployed in rail to deliver a better railway and value for taxpayers and customers.

4.3 The track to growth is a reinvigorated public-private partnership

At a time when Europe is liberalising rail markets to harness the innovation and commercial acumen that train companies can deliver for passengers, Britain risks stepping backwards and losing out on those benefits. Evidence from the continent and pre-Covid in Britain shows that competition can yield significant benefits for passengers and taxpayers. Looking forward, neither the private nor the public sector can do this alone – what is needed is a reinvigorated public-private partnership to meet the challenges the railway faces.

1. Establish a new arms-length body at the earliest opportunity to deliver public control and coherence across the railway.

To address longstanding challenges around blurred lines of accountability and a lack of coherence across the system, legislation should be brought forward to establish a new arms-length body – Great British Railways. This will rightly provide the public control needed to ensure the railway is delivering for passengers, communities and the environment. It should look across rail infrastructure and operations. As a client, the new body must be a guiding and not controlling mind, resisting the temptation to immerse itself in delivery and micromanagement of industry. Instead, it should harness train companies to do what they can do best: grow patronage and revenue while bearing down on cost.

A reformed system, under a new public arms-length body, should both create accountability and the right conditions for train companies to deliver as they did in the years following privatisation. In its role as market maker, the new body should oversee a reformed contractual landscape that sets outcomes for operators to deliver, rather than a top-down system of command and control. New contracts should give operators the right incentives to grow revenues back and control costs, and the right levers over timetabling and fare setting so they can respond to customers' needs quickly, using the in-depth knowledge of local needs and markets they have built up over a quarter of a century.

2. Harness the private sector to deliver for passengers and taxpayers today.

At a time when passenger numbers and revenue have plateaued and taxpayer support remains higher than before the pandemic, the system needs to innovate to restore financial sustainability by attracting customers in greater numbers. The most immediate step in this direction would be to facilitate greater commercial freedoms across all existing National Rail Contracts (NRC). By deploying and activating revenue and cost incentives in NRCs, the commercial expertise of the private sector would be once again harnessed to chase additional revenue and bear down on costs. To be successful, operators will need greater freedom to act rather than ask for permission.

3. Reunite cost and revenue within DfT at first and then within the new arms-length body.

To ensure cost is not reduced to the detriment of revenue, it is essential to consider both sides of the ledger and the net impact of decisions. At present, the DfT is often required to mainly focus on cost reduction without fully considering the impact on customers and revenue. This is a consequence of the post-Covid financial arrangements, whereby the cost budget for operators sits with DfT, but the revenue goes to Treasury. Considering cost and revenue holistically would allow operators to begin closing the financial gap left by the pandemic and bring passengers back to rail in greater numbers.

4. Ensure the new contracting model allows companies to deliver for passengers.

Recognising that NRCs are bridging contracts, the new longer term contracting model being developed should move away from overspecification and a culture of top-down decision making, instead harnessing operators to deliver for passengers and taxpayers. Contracts should not be a one-size-fits-all approach, rather they should be tailored to the markets and geographies served. This should take the form of a spectrum of contracts, with long-distance contracts allowing for significant commercial freedom and strong revenue incentives. At the other end of the spectrum would be Transport for London style commuter contracts that encourage bidders to bear down on cost while delivering a punctual and reliable service. In the middle, mixed market contracts, allowing for more commercial freedom where discretionary leisure and business markets exist. The Government should set out a clear timeline for developing the contracts and a pipeline for taking them to market to provide domestic and international transport businesses a framework against which to take investment decisions.

5. The full potential of open access should also be realised on long-distance routes.

The full potential of open access should also be realised where potential demand exists. At a time of tight fiscal constraints, open access operators can offer services at no direct cost to the taxpayer while helping to connect underserved communities. For some long-distance routes, more rail companies competing for passengers could offer a range of different services based on customer needs. Whether it is quicker, more comfortable journeys or faster Wi-Fi, demand would shape the market; meaning rail companies would have to adapt to the needs of passengers if they want to keep their business. For open access to prosper, it is vital that the access regime is fair, transparent, stable, and that the regulator is equipped to facilitate the expansion of this type of competition.

6. Reform the fares structure to ensure passengers get the best deal.

Attracting and retaining customers post-Covid means providing them with an experience that matches or betters the experience they receive from other transport modes, and other services and industries. A fares, ticketing and retail overhaul is needed, with a modernised customer experience that is adaptable to their changing needs. This means implementing single-leg pricing and more Pay-As-You-Go in urban areas and prices designed to fill empty seats on long distance journeys. A modern approach to ticketing is needed with new ways to pay through expanding the availability of digital tickets to cover more journey types and investing in more tap-in-tap-out systems across the railway. A transformed customer experience which attracts people back to rail, while creating efficiencies and additional revenue, is key to the long-term financial sustainability of the whole industry.

4.4 Getting back on the track to growth involves the public sector once again harnessing private train companies

Getting back on the track to growth involves putting to one side ideological debates about private vs public, recognising the challenges facing the railway, and putting in place the right solutions. It is a shared responsibility to protect the railway's future. Train companies, both domestically and abroad, have evidenced the skills and expertise required to grow patronage and protect taxpayers.

If reform continues to stall, the railway faces a protracted hiatus, a stunted recovery from the pandemic and, in the worst case, a permanently smaller railway. If we get it right, however, the railway can return to growth and help the country do the same – with rail acting as a catalyst for economic growth and decarbonisation.

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Rail
Partners

contactus@railpartners.co.uk
1 Northumberland Avenue,
London, WC2N 5BW
www.railpartners.co.uk