Rail Partners' *'Track to Growth'*: Reanimating the corpse of rail privatisation

RMT Briefing

Rail Partners 'Track to Growth' document is a slightly less confident, less heroic but no less partial and dishonest version of an established private sector 'Trade narrative'. Since privatisation, *Rail Partners* and their predecessor organisation, the Association of Train Operating Companoes (ATOC), have produced intermittent documents that attempt to claim credit the growth in passenger numbers and attribute this to the innovation and efficiency brought by the private sector.[1]

What distinguishes this latest document is a consistent attempt to paint the rail industry as an example of a 'public private partnership'. The political motivation for this is clear. It is designed to redescribe continued private sector train operation in terms that are appealing to people who are indifferent to the mode of delivery and purport to be interested only in 'results'.

In reality*, Track to Growth* is little more than an attempt to reanimate the corpse of privatisation using rehashes of old arguments that gloss the wretched record of the private sector on rail and its value-extractive nature.

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[1] The idea of the trade narrative is explored in Andrew Bowman, Peter Folkman, Julie Froud, Sukhdev Johal, John Law, Adam Leaver, Michael Moran and Karel Williams (2013), 'The Conceit of Enterprise: train operators and trade narrative', https://foundationaleconomycom.files.wordpress.com/2017/01/the-conceit-of-enterprise.pdf

‘Partnership’ and private sector failure

The examples that are used of ‘public private partnership’ are very revealing. For example, the massive role that the public plays in funding the railways and the role of Network Rail in running the infrastructure are not evidence of a successful public private partnership, they are evidence of massive and in the case of infrastructure, fatal, private sector failure.

Unlike in Europe, rail privatisation was a ‘big bang’ event that produced a series of private sector failures, most notably the collapse of Railtrack following a series of catastrophic rail accidents.

So bad has been the record of the private sector train operators that in spite of a legal prohibition on public sector operators bidding for contracts, 40% of the franchises are now being run directly by the DfT, something that is clearly making the private train operators queasy.

Rail Partners’ *Track to Growth* is littered with friendly-sounding references to partnership, but is little more than a repackaged attempt to gloss a history of failure and value-extraction by making wholly unjustifiable claims to having delivered historic success.

Taking the credit for growing passenger numbers

The empirical centrepiece of this document is Oxera research which analyses a series of metrics of rail industry ‘growth’ and ‘success’ and claims that 55% of this growth can be attributed to privatisation. This is an old claim that’s been dealt with many times in the past, but it’s worth looking at Oxera’s claim in more detail.

Oxera’s methodology amounts to looking at the rise in passenger journeys since 1997, subtracting everything that can be explained by ‘external factors’ and attributing the rest to the activities of the private sector. The ‘external factors’ are derived from those used in the Passenger Demand Forecasting Handbook such as gross value-added per capita, population and employment growth.

There are major problems with this approach. It has been recognised for years that the metrics in the Passenger Demand Forecasting Handbook have consistently failed to adequately explain movements in demand, persistently under-estimating it. For example, as a recent DfT report stated, ‘PDFH specifically under-forecasts non-London demand, particularly for commuting into core cities, a factor that has been recognised for some years.’[2] The Rail Delivery Group themselves have noted these weaknesses and the ‘absence of granularity’ in forecasting metrics in the PDFH in their *Long-Term Rolling Stock Supply Strategy* document.[3]

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[2] *Rail Demand Forecasting Estimation Final Report Final Draft*, Redacted, Prepared for Department for Transport November 2016 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/610059/phase2-rail-demand-forecasting-estimation-study.pdf

[3] Rail Delivery Group, Long-Term Rolling Stock Suply Strategy, (2018) p. 18; https://www.raildeliverygroup.com/files/Publications/2018-03_long_term_passenger_rolling_stock_strategy_6th_ed.pdf

It is highly problematic to calculate and weight the contribution of 'external factors' using forecasting data that are widely recognised to fail to adequately explain movements in passenger demand. The result is likely to be an under-calculation of the contribution of 'external factors' and a large unexplained quantity of demand. The magic trick that Oxera perform is then to announce that this gap, which they assess as being 55% of historic demand, can only be explained by the private train operating companies' entrepreneurial activities.

In addition to the methodological issues involved in this logically and empirically questionable leap, Rail Partners and Oxera face another major problem, which is that there is a more academically respectable and well-established alternative explanation, which happens to be shared by the rail companies.

To add to the general impression of sleight-of-hand that emanates from this document, most of Oxera's graphs start at the point of privatisation, deliberately obscuring any evidence from beforehand. But one graph that does show evidence from before privatisation shows that passenger journeys were growing again under British Rail and only dipped ahead of privatisation alongside the recession of the 1990s (Figure 1).

This reflects the fact that there is a strong and established correlation between GDP and growth in passenger numbers that predates privatisation by decades. Privatisation of the railways coincided with the longest period of sustained economic growth in the post-war period. The correlation continues today. Even before the Covid pandemic, passenger number growth was slowing down and rates were flatlining coinciding exactly with the 'Great Recession' and the subsequent years of low GDP growth.[4]

In reality, the TOCs who paid Oxera have always understood this relationship. An ATOC report from 2009, for example, noted that 'passenger demand and GDP for most franchises are thought to be quite closely correlated'. This was echoed by Stagecoach around the same time.[5] In their 2018 annual report, FirstGroup noted the slowing growth in rail demand described above, saying "Industry studies suggest the main drivers for recent slowing in growth across the sector include UK macroeconomic uncertainty, modal shift due to sustained lower fuel prices and working practices, and the effect of rail infrastructure upgrade works taking place across the country."[6]

The rail companies' understanding of this relationship also explains the succession of measures devised to insulate the TOCs from 'exogenous' risks of passenger revenue

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[4] This is argued strongly in Karel Williams, Andrew Bowman, Peter Folkman, Julie Froud, Sukhdev Johal, John Law, Adam Leaver and Michael Moran (2013), 'The Great Train Robbery: the economic and political consequences of rail privatisation', pp. 115-118. https://www.firstgroupplc.com/~/media/Files/F/Firstgroup-Plc/AGM/2018/firstgroup-plc-annual-report-2018-final.pdf

[5] Bowman et al, *The Conceit of Enterprise,* pp. 10-11. None of these functioned to the satisfaction of the private companies because, as one consultancy has put it "the GDP/CLE mechanisms still left operators exposed to large amounts of risk outside of their control, *since mechanisms could not be calibrated to shield operators from all forms of external risk*". Who was this pointing to the limitation of passenger demand forecasting mechanisms? None other than Oxera! (Can the private sector help to get the rail industry back on track? - Oxera

[6] firstgroup-plc-annual-report-2018-final.pdf (firstgroupplc.com)

variations ‘beyond their control’ such as ‘cap and collar’ and the Central London Employment and GDP mechanisms.

In short, Oxera’s extravagant central claim that 55% of historically rising rail demand can be attributed to private sector intervention is simply not credible. Even the TOCs don’t really believe it. In fact, the movements in passenger demand can be far better explained without reference to the private companies at all and the industry knows it.

The facts are that growth in passenger numbers started before privatisation and would have happened whether or not British Rail had been privatised. The private train operating companies simply got lucky and have attempted to pass this off as a consequence of their own brilliance ever since.

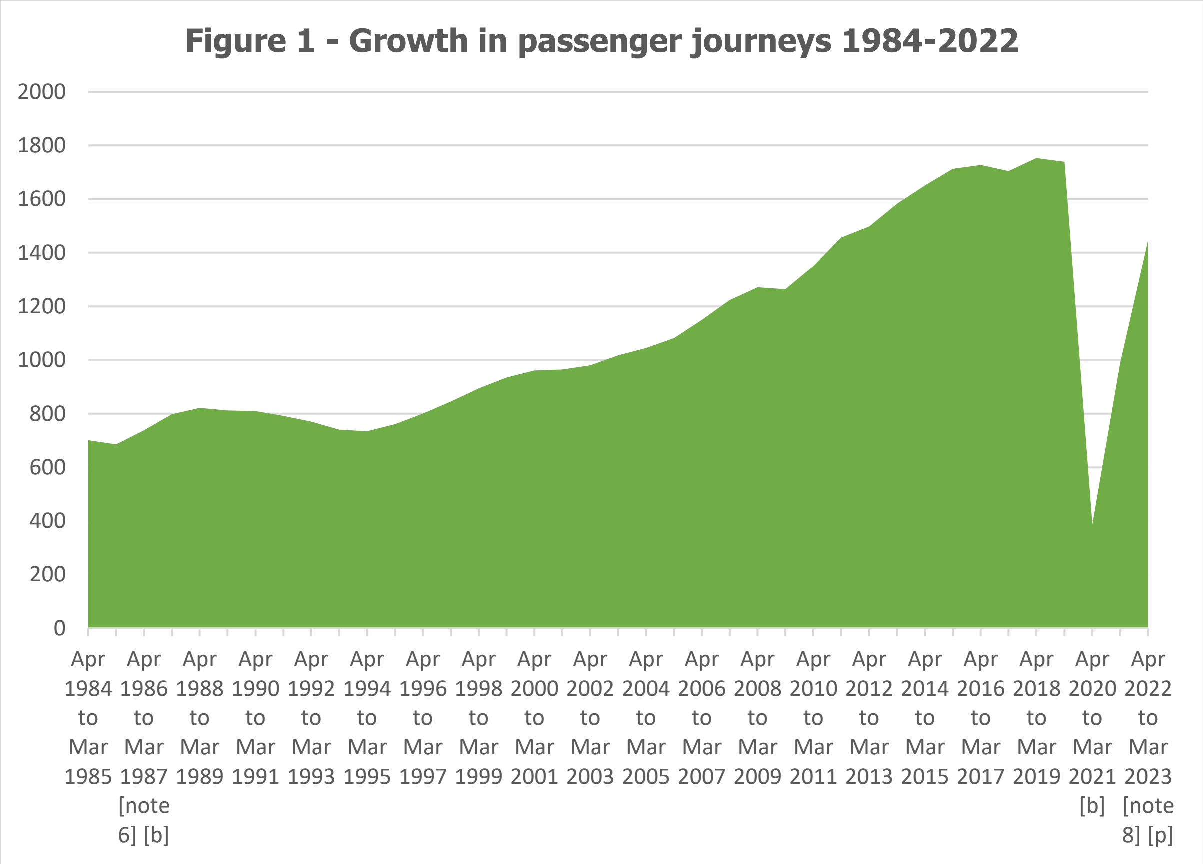
Passenger revenue growth and the hidden public subsidy

The only other Oxera graph that makes any reference to pre-privatisation data looks at increasing passenger revenue and makes the claim that privatisation was able to overturn the poor financial performance of British Rail.

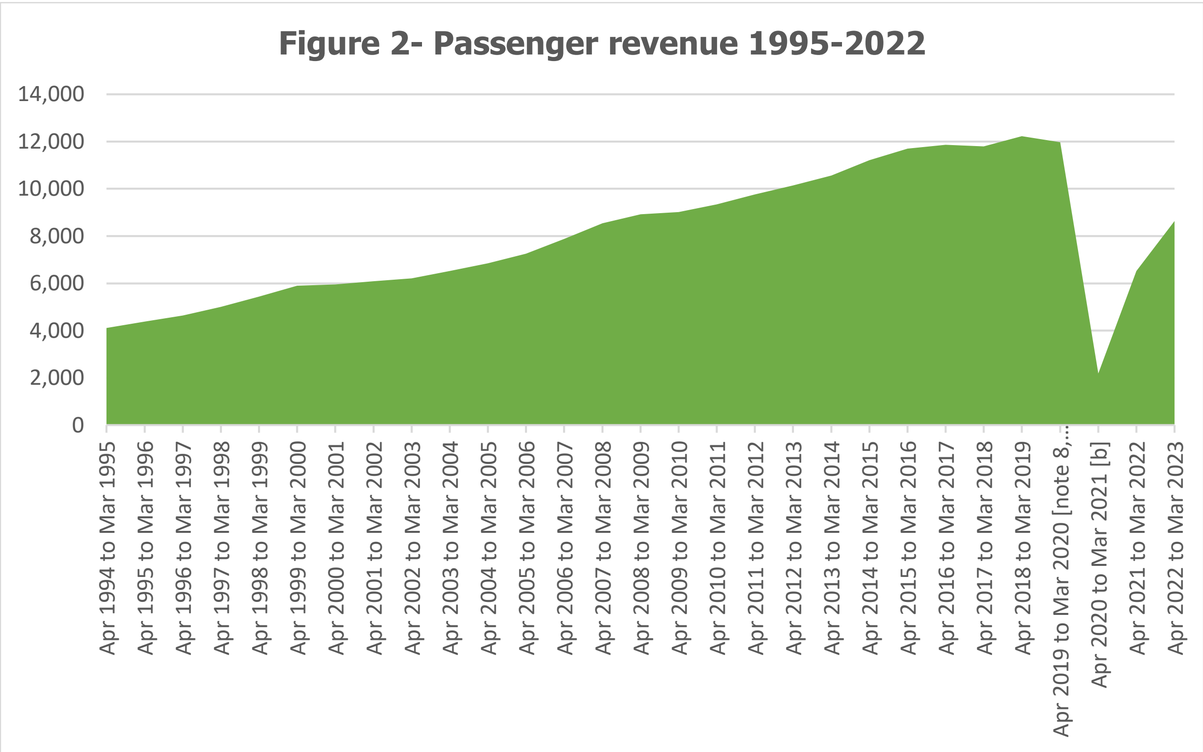
Firstly, this relies on a tired cliché endlessly recycled by opponents of nationalisation about the under-performance of British Rail. Yet as we’ve seen, passenger numbers had already begun to rise under British Rail, decades before privatisation. Equally, myths about its inefficiency are just that – myths recycled to favour the privateers’ trade narrative. By the 1980s, as passenger numbers picked up again, BR achieved an operating surplus and a superior level of efficiency to eight European benchmark rail systems, in spite of historic underfunding and under-investment.[7]

Secondly, Oxera’s analysis completely ignores the fact that growing passenger revenue has been accompanied by a massive expansion in public spending on rail. As Figures 1-3 show, total government spending on rail (including spending in the form of operational funding for passenger services infrastructure and freight, as well as enhancements funding for infrastructure) has risen consistently and significantly over the period of rising passenger numbers and the period of privatisation.

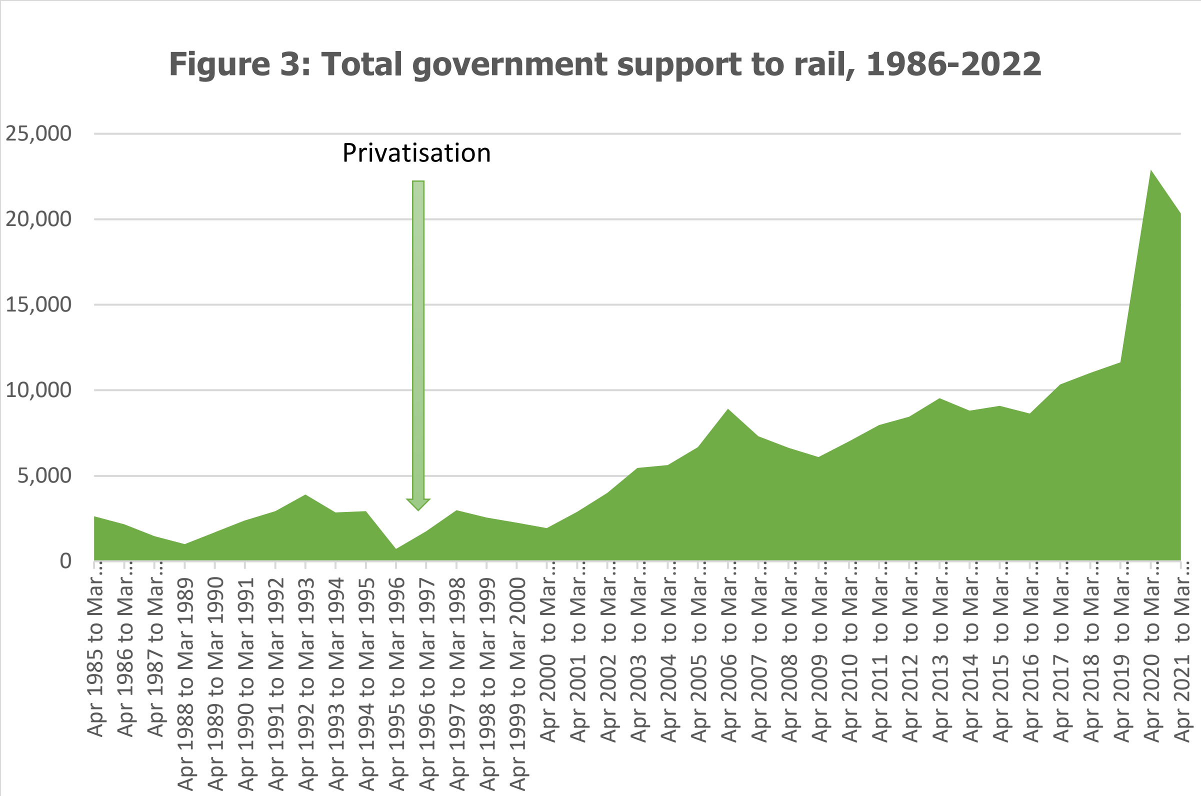
[7] See T. Gourvish, *British Rail, 1974-97: From integration to Privatisation* (Oxford, 2002), pp. 138-150.



Source: ORR data: https://dataportal.orr.gov.uk/statistics/usage/passenger-rail-usage/table-1220-passenger-journeys/



Source: ORR data: https://dataportal.orr.gov.uk/statistics/usage/passenger-rail-usage/table-1211-passenger-revenue-by-sector/



Source ORR data: https://dataportal.orr.gov.uk/statistics/finance/rail-industry-finance/table-7270-government-support-to-the-rail-industry/

The fact is that public investment in rail has dwarfed private sector spending since privatisation.

On average over the last 15 years, the private sector has contributed around 9% of what government spends. 76% of that 9% is spent on rolling stock by the ROSCOs. Even spending on rolling stock has been mainly subsidised by government funding.

Spending that is actually attributable to the TOCs amounts to **1.9%** of what is spent by government each year on average.

Rail Partners are coy about that fact in this document, but when they're not trying to bamboozle the wider public, this is something the privateers actually boast about in front of their shareholders.

For example, in 2019, FirstGroup CEO Matthew Gregory reassured his investors that franchising involved little capital expenditure: "As we have said before, the capital expenditure in Rail is normally funded through the franchise payments or through third-party capital grants. The investment in Rail CapEx is usually using someone else's cash."

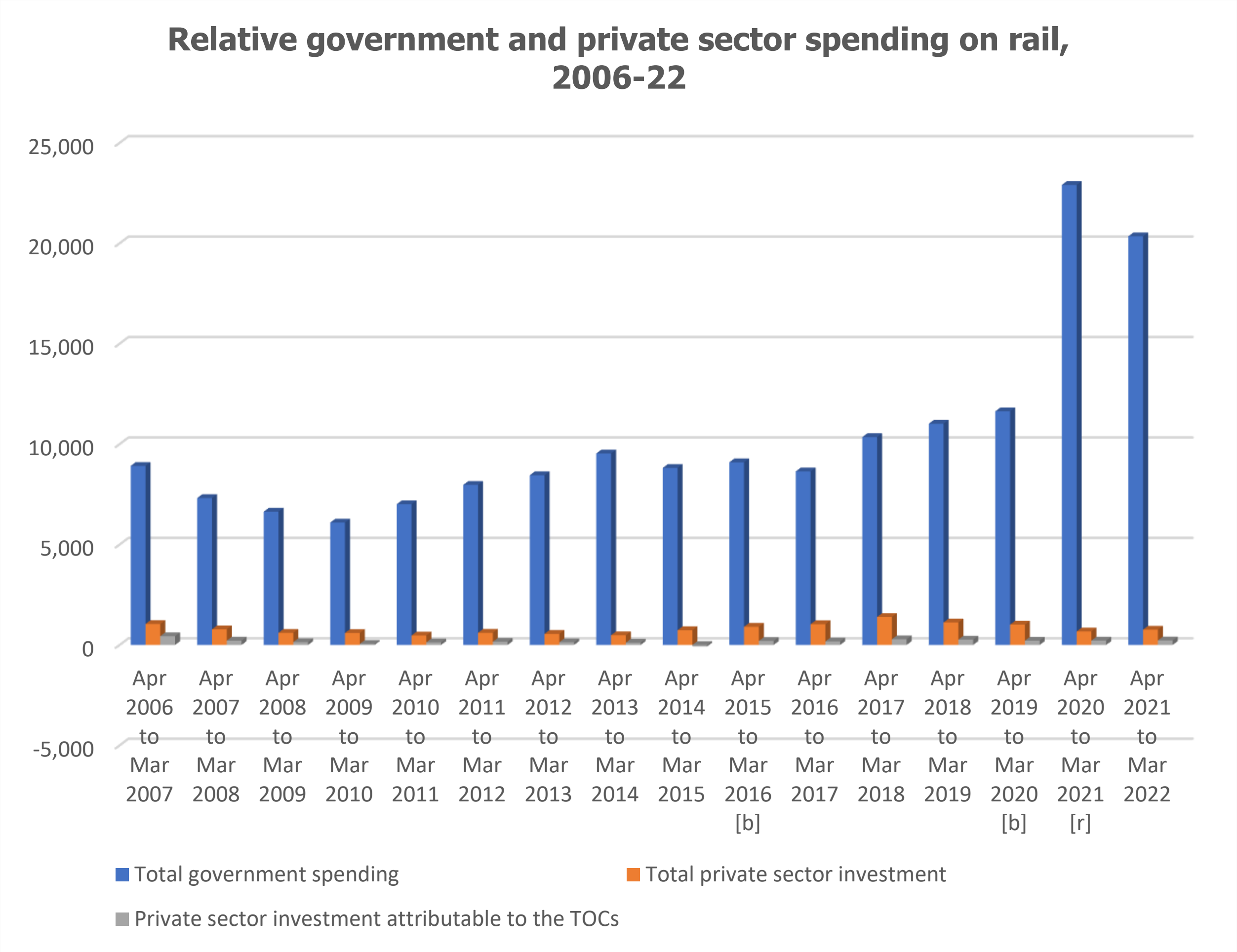
In their February 2022 trading update, Firstgroup said: "First Rail continues to be cash capital-light, with any capital expenditure required by the four management fee-based operations fully funded under the new contracts."[8]

[8] https://www.firstgroupplc.com/~/media/Files/F/Firstgroup-Plc/reports-and-presentations/presentation/fy-2021-22-results-presentation.pdf p. 13.

If the private train operators want to make the case that passenger revenue growth can be attributed to an improved rail offer, they need to give credit where it's due and admit that this is more likely to be a consequence of the massive government investment in infrastructure and rolling stock since 1997 and not a result of their rather insignificant contribution.

Table 1: Government and private investment in rail

	Total government spending	Total private sector investment	Private sector as a % of government spending	Investment attributable to the TOCs	TOC investment as a % of government spending
2006-2007	8,915	1045	12%	438	4.9%
2007-2008	7,317	779	11%	216	3.0%
2008-2009	6,636	603	9%	142	2.1%
2009-2010	6,093	597	10%	53	0.9%
2010-2011	7,009	472	7%	129	1.8%
2011-2012	7,969	604	8%	159	2.0%
2012-2013	8,451	551	7%	135	1.6%
2013-2014	9,534	484	5%	115	1.2%
2014-2015	8,815	734	8%	-76	-0.9%
2015-2016	9,094	906	10%	200	2.2%
2016-2017	8,641	1035	12%	175	2.0%
2017-2018	10,350	1393	13%	283	2.7%
2018-2019	11,018	1120	10%	265	2.4%
2019-2020	11,632	1013	9%	214	1.8%
2020-2021	22,905	672	3%	217	0.9%
2021-2022	20,346	762	4%	225	1.1%
Average			**9%**		**1.9%**



Source ORR data: https://dataportal.orr.gov.uk/statistics/finance/rail-industry-finance/table-7270-government-support-to-the-rail-industry/

The privateers' 'operational surplus' accounting trick

The supposed 'operational surplus' made by private train operators is only achieved by discounting not only government spending on infrastructure but also the access charges paid to Network Rail. This is justified as these are an 'industry transfer', but these access charges are the only contribution the TOCs make to the main cost of the railways – infrastructure – and these have historically been held down by government to enable the TOCs to make any profit at all. To discount this cost is an accounting fiction being used to convey an impression of operational efficiency. The private sector's 'operational surplus' is effectively an accounting trick.

Behind the smokescreen – privatisation is parasitic value extraction

Rail Partners are correct to say that it's important to diagnose the problem correctly. However, their diagnosis is based on a self-serving trade narrative that relies on ignoring vast swathes of evidence of what has historically determined passenger numbers, magicking away the role of public investment, performing accounting tricks to conjure up a non-existent operational surplus and recycling tired cliches about nationalisation.

This self-serving narrative is aimed at neutralising the reality of privatisation which is that it rode a wave of economic growth while creating a fragmented, incoherent, expensive and barely functional rail network populated by rent-seeking companies who extract tax revenue and passenger fares and turn them into wholly unjustifiable profits.

The private train operating and rolling stock leasing companies have used their time in control of the railways to extract over £9 billion in dividends alone.

Table 2: The cost of dividends paid out by private train operating and rolling stock leasing companies since privatisation

	1996-2010*	2010-2021**	Total post-privatisation
TOCs	£1,000,000,000	£2,404,749,000	£3,404,749,000
ROSCOs	£2,520,000,000	£3,409,763,095	£5,929,763,095
Total	£3,520,000,000	£5,814,512,095	£9,334,512,095

*Source: *Rebuilding Rail* (Transport for Quality of Life, 2012)
**Source: RMT analysis of franchisee company accounts, 2010-2022

Even these profits aren't an index of success as they had to be politically constructed. As a series of academic studies have established since privatisation, the rail market had to be designed so that the Train Operating Companies' costs were as low as possible. That meant ensuring that the burden of paying for infrastructure was shunted onto Railtrack and then subsequently Network Rail. Access charges paid to Network Rail were held artificially low to create the possibility of profit, even though that created financial difficulties for the infrastructure provider, problems that have led to the ballooning of its debt and pressure to cut maintenance costs in a doom loop that points back toward the problems of the late 90s.[9]

The definition of insanity is doing the same thing over and over and expecting a different result

Rail Partners' suggested medicine is, of course, to leave passenger operations in the hands of the private sector but this time to try to sanitise continued value extraction by re-

[9] The literature on this feature of the privatised rail system is now extensive. See for example, Karel Williams, Andrew Bowman, Peter Folkman, Julie Froud, Sukhdev Johal, John Law, Adam Leaver and Michael Moran (2013), 'The Great Train Robbery: the economic and political consequences of rail privatisation', Andrew Bowman, 'An illusion of success: The consequences of British rail Privatisation', *Accounting Forum*, Volume 39, Issue 1, March 2015, Pages 51-63; McCartney, S., & Stittle, J. (2023). *The Privatisation of British Rail: How Not to Run a Railway* (1st ed.). Routledge.

branding it as 'public-private partnership'. This would be a disastrous mistake in which the only winners would be the shareholders of FirstGroup, Go-Ahead and Abellio.

The real solution is an integrated, publicly owned rail network

The spectre haunting Rail Partners' document is of a nationally integrated publicly owned rail network. This would ensure that every pound spent on vital public infrastructure actually goes into the rail network. It would:

- End the wasteful leakage of badly-needed funds out the railway into dividend and interest payments;
- create a single overarching body at arms length from government departments with representation at all levels for workers, passengers and devolved transport authorities.
- align the objectives and incentives of the people managing track and trains with each other and the wider public interest;
- remove incredibly wasteful interface costs;
- remove contractual barriers to innovation that come with private company passenger operations and rolling stock leasing;
- allow for integration of passenger services;
- create a single employer for the railway, laying the basis for improved industrial relations and allowing GB Rail to tap into the operational knowledge and skills of their workforce.

The blueprint for this already exists in the form of Labour's GB Rail document.[10]

[10] GB Rail: Labour Opposition White Paper https://labour.org.uk/wp-content/uploads/2020/03/GB_Rail_Labour_Opposition_White_Paper.pdf#:~:text=Labour%20proposes%20a%20structure%20for%20Britain%E2%80%99s%20railway%20that,of%20the%20GB%20Rail%20operations%20within%20their%20areas