RECENT RAILWAY PRIVATISATION MEASURES IN BRITAIN.

Paul Truelove

Department of Civil Engineering, University of Aston,
Gosta Green,
Birmingham B4 7ET, England.

1. INTRODUCTION

The railway industry is possibly unique among modern transport modes in the extent of its linkages with developments that occurred long enough ago to be regarded as history. The traction equipment of the 1980's may be operating on structures built by hand a hundred and fifty years ago. This is one of the reasons why railways exercise a continuing fascination in the mind of the British public. Now that the privatisation of public utilities is a worldwide phenomenon, and the methods and possible benefits that might result are of great professional and political interest, it may be that evidence of experience during the growth of the British railway system in the nineteenth century, under conditions of very limited government intervention, and a multiplicity of separate companies, holds some lessons for those concerned with the formulation or implementation of privatisation in the 1990's. This paper traces the recent history of railway privatisation in Britain, but also draws examples from the much earlier history of the railway industry.

The movement towards the privatisation of state owned industries is a process that has been in operation in Britain for a decade. Some of the industries have manufactured consumer products, such as Jaguar cars, but most have been public utilities, or have some claim to form 'natural' monopolies. It is too simplistic to see the political motivation towards privatisation as a reaction against the policies of previous socialist administrations, for some of the companies now being privatised have their origins in nineteenth century municipal enterprises: for example the public water companies that built dams, reservoirs and aqueducts to serve Victorian cities such as Birmingham. Nor is it any recent thing for government to be involved in private companies: Disraeli, a Tory prime minister, bought shares for the British government in the Suez canal company.

Thus the accumulation of industries in government ownership is in part a result of the conscious efforts of government, particularly the Labour government of 1945 to 1951, but it is also the result of a variety of processes at work over a long period of time: ranging from by-products of Britain's colonial history, to a distrust of private monopolies that long pre-dates socialist governments. After the main 'conscious' phase of nationalisation in the late 1940's, subsequent conservative governments did de-nationalise the road haulage industry, previously owned by small-scale companies, but utilities with a national network, and no recent history of small-scale capitalist ownership, such as the G.P.O. telephones, and the national grid of the electricity board were left alone. The prevailing ethos within conservative governments was one of pragmatism: doctrines, and dogmas, were some kind of handicap suffered by socialists.

The place of railway nationalisation in this general picture is hard to categorise. Whilst the railways were nationalised during the main 1945 to 1951 phase, such was the condition of the railway system at the end of the second world war in 1945, that some form of state control - or at the very least - state funding, was inevitable. Moreover, the state ownership of railways was not uncommon elsewhere. Few countries might have state ownership of coal and steel industries, but many controlled their own rail companies, and more recently, their airlines.

The conservative government that was elected in 1979 differed from earlier conservative administrations in that its approach was determined more by doctrine than by pragmatism. State ownership was wrong, unnecessary, and a handicap to efficient operation. Only the stimulus of market forces could create producers responsive to the needs of consumers, lift the dead hand of bureaucracies that inhibited innovation, and foster a necessary change to more modern working practices. Throughout the past ten years, the government has resolutely pursued its policies of privatisation, and there is an ever growing catalogue of industries and utilities once publicly owned, but now in private hands. Extensive television advertising campaigns have persuaded many small investors of the merits of share ownership. At the end of this ten year period, a very long time in politics, British Rail remains in public ownership. Certain ancillary businesses have been sold off, but the fact that the railway remains in public ownership suggests that the selling off of a railway is a difficult task for even the most determined and vigorous of governments. Only now, in 1989, is the Secretary of State for Transport appointing a number of outside advisers to help draw up proposals. Samuel Montagu has been chosen as merchant bank adviser. Accountants Deloitte Haskins and Sells are asked to make recommendations on structure. National Economic Research Associates will advise on how to regulate the industry after privatisation.

Limits to the extent of power of the nationalised railway management are no new thing, and pre-date the 1979 conservative administration. Under the 1968 Transport Act, passed by a Labour administration, suburban services in provincial conurbations were provided not directly by British Rail. The required service would be specified by conurbation Public Transport Authorities, who would then enter into a contract with the railway for the provision of those services. In this way, the authority could ensure co-ordination among the various bus and rail services provided, and co-ordinate fares policies. As a method of service and fare co-ordination this worked well before the de-regulation of the bus industry under the 1985 Transport Act. It did create difficulties where the Passenger

Transport Authorities purchased rolling stock from the railway, that subsequently proved to be unreliable.

Since 1979, a number of businesses formerly a part of British Rail have been sold off. However, none of these - British Transport Hotels, Sealink Ferries, etc - are central to the running of the railways, so their sale has been a relatively straightforward matter. Next to go have been businesses that serve the industry or the passengers. but can be viewed as independent operations, such as station catering. The most complex task to date has been the sale of British Rail's coach building and repair subsidiary, British Rail Engineering Limited (BREL 1988) to a management buyout team backed by British and European business interests. Management and employees will take a 20% stake with Trafalgar House and Asea Brown Boveri taking 40% each. The inclusion of workforce participation in management buyouts, pioneered in this country's transport industries by the West Yorkshire Passenger Transport Authority's company Yorkshire Rider, now wholly owned by management and workforce, is a particularly interesting development. The reception given to the success of the buyout team by the railway trades unions has been one of cautious - even suspicious - welcome: but it has been interpreted by some labour politicians as one of the few positive consequences of the government's programme. The inclusion of European manufacturers in the successful bid follows the established method for international companies to overcome resistance to the offering of contracts to 'foreign' companies rather than home companies.

Thus it can be seen that whilst the central problems of privatising a national railway system have yet to be faced, considerable progress towards conservative government objectives has been made. Contracts for new rolling stock are all put out for competitive tender, rather than allocated automatically to BREL. Moreover, rail freight users may operate not only their own goods wagons, but also their own locomotives. This new freedom has resulted in the needs of freight users being met more closely. The aggregates firm of Fosters Yeomans chose to purchase locomotives that suit their specific requirement, and not available from British Rail. The aggregates firm, Redlands, has developed a wagon incorporating a conveyor unloading system that permits the delivery of aggregates to sites lacking expensive fixed handling equipment.

All these developments are steps towards privatisation, but the most significant development in railway management since 1979 has been the introduction of sector management. Traditional railway management was focussed upon the production and operation of services, rather than upon the needs of customers, and the costs and revenues resulting from meeting their needs. This shift in focus, with operating requirements determined by the needs of the business, has resulted in a more healthy financial position for the railways. Intercity services are now expected to operate without government support, from April 1988: likewise the freight and parcels sectors. Only the London suburban services (Network South east) and the provincial sector covering routes between provincial centres, and country branch lines, the chronic loss-makers, now receive central government support. In the year 1988/1989, Network Southeast was allocated £141 million, and the provincial sector £408 million. Even in these sectors, central government funding is applied in more limited ways. The provincial sector provides suburban services in provincial conurbations in accordance with contracts with the Passenger Transport Authorities of the conurbations. If the authorities decide no longer to sponsor services, central government would not fund their continued operation under the public service obligation grant made to the provincial sector.

The introduction of sector management has required the adoption of accountancy measures to reflect the usage of the same infrastructure by different business sectors. Broadly, the main user, or 'Prime user' of any track, must be accountable for that infrastructrure, and other business users pay only the marginal costs. This produces some anomalies, e.g. some suburban lines are much more expensive to run if there is no prime use by inter-city to bear the brunt of the fixed costs. These anomalies could cause great problems if British Rail were to be privatised on a sector basis.

The financial performance of the loss-making sectors is improving. From a situation in which costs exceeded revenue by a factor of 4, the introduction of new rolling stock, and of cost saving measures - most notably on track and signalling - the factor is now down to about 3. In two ways this undoubted improvement ironically undermines the case for privatisation. Firstly, the notable improvement in management has been achieved without privatisation. Secondly, the greatest improvements to the provincial network have been in extending the range and variety of long distance cross-country routes between smaller towns and cities. Thus it is now possible to make a direct journey with out changing trains, from Blackpool in the northwest to Cambridge in the south east, whereas formerly several changes would have been required. These are the kind of routes it would be most difficult to operate were British Rail to be divided into small regional companies.

2. METHODS OF PRIVATISATION

Four different options for selling off the rail system are being considered by government ministers:

1. Privatisation as a single unit, the option favoured by the British Rail board.

2. Splitting British Rail into a number of independent regional companies (akin to the pre-nationalisation pattern), a proposal first put forward by the Centre for Policy Studies.

3. The creation of a national track authority, and the lease of the network components to competing rail companies, as proposed by the Adam Smith Institute.

4. (A variation of 3) The sale of British rail into the five recently created business sectors, i.e. Intercity, freight, parcels, network southeast and provincial.

Privatisation as a single unit is a simple concept, but more attention has been given to ideas that entail some new form of subdivision of the railway, either geographically or functionally. A report by Kenneth Irvine of the Adam Smith Institute argues for privatisation based upon the creation of a series of operating companies, for trains, train catering, train crew, freight terminals and operational land; and infrastructure companies for research and development, track, overhead power lines, signalling, train control stations and non-operational land. Irvine argues that the accepted wisdom that only one operator can safely use the network has been overtaken by the introduction of new signalling and train control procedures. The Department of Transport would set safety standards (much like the Board of Trade did in the nineteenth century) whilst the infrastructure companies would handle licensing arrangements with would-be train operators. New companies would have a legal right of access to rail infrastructure, alongside independent companies formed from British Rail's present business sectors. The infrastructure company would be the main recipient of grant from central government - subject to financial targets set by government. The lightening of the burden of infrastructure costs would - so the argument goes - permit the business sectors to flourish as profitable companies. Irvine accepts that the privatisation of the provincial sector would be a problem, but sees this as an opportunity for operating a franchising system, under which potential operators put in bids, positive or negative, to run services. Thus, the operator who required the least subsidy would be granted the right to a franchise.

The idea of supporting socially necessary but unremunerative transport by the granting of franchises has become established in the provision of bus services since the de-regulation of the bus industry in 1985, and most rural local bus services are now sustained in this way. Current schemes for the promotion of light rapid transit in cities such as Manchester will also rely upon franchising. Design and build contracts are becoming more common for many projects. The Docklands light railway provides an example. However, for Manchester, a design, build, operate and maintain contract is envisaged.

Independent regional companies: Analogies with Japan:

The break up of the Japanese National Railways that took place in April 1987 contains elements of all 4 of the methods of privatisation suggested for Britain. Six regional companies were created, but such is the shape of Japan that boundary problems between the regions should be minimised. Indeed, three of the regional companies are defined by the islands they serve. Ironically two of these islands have only recently been linked into the mainland network on Honshu by the Great Seto bridge, and the Seikan tunnel. Even the division of the Honshu mainland network into East, Central and West Japan railway companies is made simpler than would be possible in Britain by the long thin shape of Honshu.

In other respects, the Japanese railway privatisation resembles the idea of splitting British rail by business sector. The Japan Freight railway company provides nationwide freight transport using tracks owned by the passenger railway companies. The Shinkansen lines, which straddle the territory of 4 regional companies, are leased to the passenger railway companies by the Shinkansen property company. This procedure is simpler than would be possible in Britain, for with the exception of the proposed high speed link from the channel tunnel to London, the trains of the intercity business share the same tracks as are used by provincial and other trains.
Interestingly, the railways intend to retain a collective image as 'Japan Rail' for marketing purposes, and the Japan Rail pass remains available.

3. ANALYSIS OF BENEFITS AND PROBLEMS

3.1. Privatisation as a single unit.

This represents the least change option. There would be none of the problems associated with the production of acceptable methods for allocating costs and revenues to different independent companies. However, it must be stated that it is in the area of management information, concerning costs and patronage, that British Rail has made greatest progress in recent years.

3.2 Break up into independent companies

It is no accident that industrial relations are better in small closely-knit organisations. Management is in direct contact with the employees, and has a good knowledge of customers' requirements. Within the existing railway network, conditions on some short rural branch lines come nearest to meeting this ideal. Away from the remote fringes nothing like this is possible. British rail has 40,000 employees in the London area, and 458,000 passengers use its network every weekday. No component of the network is wholly self-contained. Advocates of the break up of the network into small components have suggested that the London to Southend route from Fenchurch street might be a suitable route to hive off from the British Rail system, to demonstrate the feasibility and benefits of this form of privatisation. This is one of two routes from London to Southend - a product of the evolution of the railway system under private ownership - and it is argued that this competition could again produce efficiency benefits. However, detailed examination of the route indicates that whilst it may he relatively self-contained from a passenger viewpoint, some of its track is used by freight. This freight, destined for Tilbury docks, will of course have its origins and destinations well outside the region, and the privatised company's jurisdiction. The allocation of priorities, between the requirements of the company's own passengers, and 'foreign' freight traffic, will be difficult to make on a rational basis. If the example of inter-company relations in Victorian times provide any guidance, the scope for disagreements and for delays will be enormous, even if a fair price for the use of the company's track can be agreed.

The more fundamental problem is that of contributory revenue. Since the 1840's, mechanisms have existed to permit railway users to purchase services from more than one railway company. The railway Clearing House established when Gladstone was president of the Board of Trade permitted the through ticketing of goods traffic. Such mechanisms are satisfactory when the railway system is potentially profitable throughout. However, when a railway contains regularly unprofitable components - and the present government appears to accept that it is politically necessary to retain the unremunerative branch lines of the provincial sector - the passenger who uses such a branch line as part of a journey including Intercity travel, may add to the costs of a loss-making company while contributing to the profits of another. Indeed, the profitability of an intercity route could depend upon the continued existence of unprofitable branches. Experience from the time of the Beeching closures bears this out. At the time of the grouping of Britain's 110+ railway companies into four large regional companies in 1923, the existence of unprofitable components to the railway system was recognised. The amalgamations were carried out largely on a geographical basis. However, no single company was formed for Scotland, as it was recognised that so many of the routes were through sparsely populated areas that even in 1923, a wholly Scottish railway could be unprofitable. The pre-existing companies having highland routes with expensive infrastructure and light traffic were therefore shared out among two companies, the London, Midland and Scottish; and the London and North Eastern Railways.
Then, tourism could not be the sole raison d'etre for a rural line. In 1988, one British Rail country branch line was offered for sale, and a purchaser has been found. That is the Aberwstwyth to Devil's Bridge steam railway. As a wholly tourist operation, reliant upon the public's enthusiasm for steam traction and Welsh mountain scenery, this must be regarded as a special case, and whilst there may be others such as the Settle and Carlisle line, they cannot be regarded as a useful model for loss-making railways generally. This line, heavily loss making, but with a combination of roles - for tourism, a small volume of local travel, and a main line diversionary route at times of major track maintenance - has now been judged by the government not to be a suitable candidate for separate privatisation.

3.3 The leasing or franchising of the right to operate services on the permanent way of a national track authority.

Under the terms of the 1985 transport Act, a local authority that wished to ensure the provision of a bus service that no commercial operator believed to be capable of profitable operation, could invite bus operators to submit tenders indicating the smallest payment they would require for them to operate the service that the local authority believed to be socially necessary. The company that submitted the lowest tender received the right to receive the fares passengers paid, and was obliged to provide the service specified by the local authority.

Franchising of railway operations is an altogether more uncertain proposition than the tendering of bus service provision, where capital costs are far lower, and ready alternative uses for the vehicles may be available. There are no infrastructure problems. Alfred Goldstein, a leading advocate of franchising, whose ideas appear to have influenced the current processes of planning light rapid transit, does nevertheless recognise certain problems. A company holding a franchise to operate rail services must own - or have access to - expensive rolling stock, which has no readily available use if the operator loses the right to provide a service at the end of the franchise period. Customers will experience deteriorating conditions if rolling stock becomes life expired towards the end of the franchise period. One of the factors slowing the development of tramways in nineteenth century Britain was a condition imposed on private tramway companies that the local authority had the right to acquire the company after 21 years. Problems of this type might require a franchising operator to use rolling stock managed separately (by another company?) and to tender simply for the right to operate the line. It is not realistic to plan for the franchise period to coincide with the expected life of the operating company's equipment, for different equipment will have different levels of durability. Even with conventional equipment, lifespan may be uncertain. Few mini-bus operators even know the life expectancy of their vehicles.

There is little experience of franchising arrangements. The closest model is in the United States, where Amtrak's North Eastern corridor is shared by a dozen commuter and freight operators. Few, if any of the people involved in running those trains are enthusiastic about the principle of shared use.

Problems such as these may be soluble, but only at a price. That price is the introduction of extremely complex arrangements. In those circumstances, the most successful companies will be those that succeed first in understanding the inter-company contractual arrangements, or are best able to manipulate those contractual arrangements to their own company's ambitions. Moreover, if a major benefit of privatisation is seen as improving staff motivation, the introduction of greater complexity is unlikely to assist the workforce in identifying with the company.

The creation of separate regional operating companies would likewise necessitate complex financial arrangements. Different regional operating companies would require different levels of state aid in the form of public service obligation grants, and efficiency comparisons would be difficult, and dependent upon extraneous factors such as the health of the local economy. In the nineteenth century, where rival companies entered into contracts to share the same tracks, the consequences were sometimes bizarre, such as when signalmen could favour one company by deliberately holding back the train of another. Rivalries might not take that form in any new privatisation scheme, but the risk would be there. The potential for obstruction might be in the hands of the software writer rather than the signalman.

Whilst efficiency comparisons might be difficult, there is no doubt that the existence of separate companies might provide a fertile ground for innovations, and in marketing terms, comparisons could be made between companies, even if for all practical purposes direct competition over the same route is extremely unlikely.

4. CONCLUSION.

Progress towards privatisation is proceeding at a rapid pace, and the government's preferred method of privatisation may soon be known. Early in 1989, it appeared that the government favoured breaking up BR into the kind of independent regional companies that existed before 1923. The matter is still not resolved, but so well established has become the idea of sector management, it would appear unlikely that the chosen method will disregard the benefits that have been achieved under sector management.

It should be stressed that outside political circles there is little expectation of great benefits from further privatisation. Gallup polls give evidence as to public opinion on the government's privatisation programme. In October 1988, Gallup found that only 22% of electors thought that more state-owned industries should be privatised. Rather more - 30% - wanted the process reversed, with more industries owned by the government. The largest number, 38%, thought the balance was about right. A poll taken by B.R. in December 1988 showed that 40% of 1000 people questioned felt B.R. should definitely not be sold off to the private sector. Privatisation proposed for the water and electricity industries does not have majority support even among conservative voters. On the other hand, earlier poll findings showed that only minorities favoured the privatisation of gas and telephone industries at the time, yet they went ahead without electoral damage to the conservatives.

British Rail management has made great improvements in recent years. Most notably, the inter-city sector has transformed an operating loss of £86.2 million in 1987/1988 to an operating profit of £57.4 million in 1988/1989, thereby improving the chances of British Rail being privatised on a sector basis. That there is no necessary link between efficiency and ownership should be evident from the Swiss experience, where publicly owned and private railways co-exist and both have an image of awesome efficiency. If as much effort were put into the devising of effective staff efficiency incentives as has been put into the devising of privatisation schemes, and inter-company contractual arrangements, then perhaps the benefits would be the same or greater. Were this to happen, then the debate over the relative merits of nationalisation versus privatisation of railways would be seen as irrelevant to the management of the railway industry.